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MONETARY AND CREDIT INFORMATION REVIEW

Banking Supervision

Revised Prompt Corrective Action Framework for Banks

The Reserve Bank on April 13, 2017 revised the framework for Prompt Corrective Action (PCA) for banks. The provisions of the revised PCA framework will be effective from April 1, 2017 based on the financials of the banks for the year ended March 31, 2017. The framework would be reviewed after three years. The PCA framework does not preclude the Reserve Bank of India from taking any other action as it deems fit in addition to the corrective actions prescribed in the framework. The salient features of the revised PCA framework are:

- Capital, asset quality and profitability continue to be the key areas for monitoring in the revised framework;
- Indicators to be tracked for capital, asset quality and profitability would be Capital to Risk (Weighted) Assets Ratio (CRAR)/ Common Equity Tier- I ratio, Net NPA ratio and Return on Assets, respectively;
- Leverage would be monitored additionally as part of the PCA framework;
- Breach of any risk threshold would result in invocation of PCA;
- The PCA framework would apply without exception to all banks operating in India including small banks and foreign banks operating through branches or subsidiaries based on breach of risk thresholds of identified indicators; and
- A bank will be placed under PCA framework based on the audited Annual Financial Results and the Supervisory Assessment made by the Reserve Bank. However, the Reserve Bank may impose PCA on any bank during the course of a year (including migration from one threshold to another) in case the circumstances so warrant.

Mandatory and Discretionary Actions		
Specifications	**Mandatory actions**	**Discretionary actions**
Risk Threshold 1	• Restriction on dividend distribution/remittance of profits. • Promoters/owners/parent in the case of foreign banks to bring in capital	**Common menu** • Special Supervisory Interactions • Strategy related • Governance related • Capital related • Credit risk related • Market risk related • HR related • Profitability related • Operations related • Any other
Risk Threshold 2	• In addition to mandatory actions of Threshold 1, • Restriction on branch expansion; domestic and/or overseas • Higher provisions as part of the coverage regime	
Risk Threshold 3	• In addition to mandatory actions of Threshold 1, • Restriction on branch expansion; domestic and/or overseas • Restriction on management compensation and directors' fees, as applicable	

(https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10921&Mode=0)

Compliance with Ghosh Committee Recommendations

On a review of the implementation status of Ghosh Committee recommendations in various banks, the Reserve Bank on April 20, 2017 advised all scheduled commercial banks that they need not report the compliance to the Ghosh Committee recommendations, to the Audit Committee of the Board (ACB). However, banks are advised to ensure that:

i) Compliance to these recommendations are complete and sustained; and

ii) These recommendations are appropriately factored in the internal inspection/audit processes of banks and duly documented in their manual/ instructions, etc.

(https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10934&Mode=0)

Banking Regulation

Role of the Chief Risk Officer

As part of effective risk management, the Reserve Bank on April 27, 2017 has advised all scheduled commercial banks that they are required, inter-alia, to have a system of separation of credit risk management function from the credit sanction process. However, it is observed that the banks follow diverse practices in this regard. In order to bring uniformity in approach followed by banks, as also, to align the risk management system with the best practices, banks are advised as under:

- They shall lay down a Board-approved policy clearly defining the role and responsibilities of the Chief Risk Officer (CRO).

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- Appointment of the CRO shall be for a fixed tenure with the approval of the Board of Directors of the banks. The CRO may be transferred/removed from his post before completion of the tenure only with the approval of the Board and such premature transfer/removal shall be reported to the Department of Banking Supervision, Reserve Bank of India, Mumbai. In case of listed banks, any change in incumbency of CRO shall be reported to the stock exchanges also.
- CRO shall be a senior official in the banks' hierarchy and shall have the necessary and adequate professional qualification/experience in the areas of risk management.
- The CRO shall have direct reporting lines to the MD & CEO / Risk Management Committee (RMC) of the Board. In case the CRO reports to the MD & CEO, the RMC shall meet the CRO on one-to-one basis, without the presence of the MD & CEO, at least on a quarterly basis.
- The CRO shall not have any reporting relationship with the business verticals of the bank and shall not be given any business targets.
- In case the CRO is associated with the credit sanction process, it shall be clearly enunciated whether the CRO's role would be that of an adviser or a decision maker. The policy shall include the necessary safeguards to ensure the independence of the CRO.
- In banks that follow committee approach in credit sanction process for high value proposals, if the CRO is one of the decision makers in the credit sanction process, he shall have voting power and all members who are part of the credit sanction process, shall individually and severally be liable for all the aspects, including risk perspective related to the credit proposal. If the CRO is not a part of the credit sanction process, his role will be limited to that of an adviser.
- In banks which do not follow committee approach for sanction of high value credits, the CRO can only be an adviser in the sanction process and shall not have any sanctioning power.
- The CRO in his role as an adviser shall be an invitee to the credit sanction/approval committee without any voting rights in the proceedings of the committee.
- There shall not be any 'dual hatting' i.e. the CRO shall not be given the responsibility of Chief Executive Officer, Chief Operating Officer, Chief Financial Officer, Chief of the internal audit function or any other function.

(https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10948&Mode=0)

IFSC Banking Units – Permissible Activities

The Reserve Bank on April 10, 2017 modified its directions relating to operations of the Indian Financial System Code (IFSCs) Banking Units (IBUs) and financial institutions in IFSC as follows:

- IBUs, with the prior approval of their board of directors, can undertake derivative transactions including structured products that the banks operating in India have been allowed to undertake as per the extant Reserve Bank directions. However, IBUs need to obtain the Reserve Bank's prior approval for offering any other derivative products. Before seeking the Reserve Bank's approval, banks shall ensure that their IBUs have necessary expertise to price, value and compute the

First Bi-monthly Monetary Policy Statement, 2017-18

Resolution of the Monetary Policy Committee (MPC)

The fourth meeting of the Monetary Policy Committee (MPC), constituted under section 45ZB of the amended Reserve Bank of India Act, 1934, was held on April 5 and 6, 2017 at the Reserve Bank of India, Mumbai. The meeting was attended by all the members - Dr. Chetan Ghate, Professor, Indian Statistical Institute; Dr. Pami Dua, Director, Delhi School of Economics; and Dr. Ravindra H. Dholakia, Professor, Indian Institute of Management, Ahmedabad; Dr. Michael Debabrata Patra, Executive Director; Dr. Viral V. Acharya, Deputy Governor in-charge of monetary policy - and was chaired by Dr. Urjit R. Patel, Governor.

On the basis of an assessment of the current and evolving macroeconomic situation at its meeting on April 6, 2017, the Monetary Policy Committee (MPC) decided to:

- keep the policy repo rate under the liquidity adjustment facility (LAF) unchanged at 6.25 per cent.

Consequent upon the narrowing of the LAF corridor as elaborated in the accompanying Statement on Developmental and Regulatory Policies, the reverse repo rate under the LAF is at 6.0 per cent, and the marginal standing facility (MSF) rate and the Bank Rate are at 6.50 per cent.

The decision of the MPC is consistent with a neutral stance of monetary policy in consonance with the objective of achieving the medium-term target for consumer price index (CPI) inflation of 4 per cent within a band of +/- 2 per cent, while supporting growth. The main considerations underlying the decision are set out in the statement below.

Other Highlights of the Monetary Policy Committee meeting

- GVA growth is projected to strengthen to 7.4 per cent in 2017-18 from 6.7 per cent in 2016-17, with risks evenly balanced
- With progressive remonetisation, the surplus liquidity in the banking system declined from a peak of Rs. 7,956 billion on January 4, 2017 to an average of Rs. 6,014 billion in February and further down to Rs. 4,806 billion in March 2017
- The level of foreign exchange reserves was USD 369.9 billion on March 31, 2017

Developmental and Regulatory Policies

Liquidity Management Framework for Monetary Policy Operations

- Reserve Bank to employ a mix of instruments like variable reverse repo auctions, operations under the Market Stabilisation Scheme (MSS) using T-bills and dated securities, issuances of Cash Management Bills (CMBs), Open Market Operations (OMO sales and purchases); to manage surplus liquidity and to keep it in a position closer to neutrality;
- Proposal for Standing Deposit Facility (SDF) by suitable amendment to RBI Act is under Government's consideration;
- Monetary Policy rate corridor narrowed, making the Reverse Repo under LAF to be 25 bps lower than the policy repo rate and tbe MSF rate to be 25 bps higher than the policy rate.

Banking Regulation and Supervision

- Revised Prompt Corrective Action (PCA) framework for banks based on recommendations of FSDC sub-committee to be issued by mid-April 2017;
- Minimum level of Net Owned Funds (NOF) requirement for Asset Reconstruction Companies (ARCs) to be increased from Rs 2 crores to Rs 100 crores;
- Instructions on capital requirement for Partial Credit Enhancement (PCE) enhanced bonds to be issued by end of April 2017;
- Final guidelines to clarify what is a 'banking outlet' and harmonising the treatment of different forms of bank presence in underserved areas to be issued by end-April 2017;

Financial Markets

- A draft policy framework for introduction of tri-party repo to be placed in public domain by mid-April 2017;
- Draft guidelines on simplified hedging facility for forex exposure for entities exposed to exchange rate risk to be placed in public domain by mid-April 2017

Payment and Settlement

- To improve the efficiency of NEFT system and customer convenience, 11 additional settlement batches to be introduced at 8:30am onwards, taking the total number of half hourly settlement batches under NEFT to 23 batches during a day, with opening and closing batch remaining at 8:00am and 7:00pm respectively;
- Final guidelines for issuance and operation of Pre-paid Instruments (PPIs) in India would be issued by end-May 2017.

Financial Inclusion

- A pilot project on financial literacy to be commissioned in nine states across 80 blocks by NGOs in collaboration with sponsor banks. Such centres for financial literacy would be set up under a common name and logo "Money-wise Centre for Financial Literacy".

capital charge and manage the risks associated with the products / transactions intended to be offered and should also obtain their Board's approval for undertaking such transactions.

- The fixed deposits accepted from non-banks by the IBUs cannot be repaid pre-maturely within the first year. However, fixed deposits accepted as collateral from non-banks for availing credit facilities from IBUs or deposited as margin in favour of an exchange, can be adjusted prematurely in the event of default in repayment of the loan or meeting a margin call.
- An IBU can be a Trading Member of an exchange in the IFSC for trading in interest rate and currency derivatives segments that the banks operating in India have been allowed to undertake as per the extant Reserve Bank directions.
- An IBU can become a Professional Clearing Member (PCM) of the exchange in the IFSC for clearing and settlements in any derivatives segments subject to certain conditions.
- IBUs are allowed to extend facility of bank guarantees and short term loans to IFSC stock broking/commodity broking entities."
- A financial institution or a branch of a financial institution set up in the IFSC and permitted/recognised as such by the Government of India or a Regulatory Authority shall be treated as a person resident outside India. Any person resident outside India, having business interest in India, may maintain Special Non-Resident Rupee Account(s) (SNRRA) with an Authorised Dealer in the domestic sector for meeting their administrative expenses in INR. Accordingly, any financial institution or a branch of a financial institution including an IBU operating in an IFSC and permitted/recognised as such by the Government of India or a Regulatory Authority, can maintain SNRRA with a bank (Authorised Dealer) in the domestic sector for meeting its administrative expenses in INR. These accounts must be funded only by foreign currency remittances through a channel appropriate for international remittances which would be subject to the extant FEMA regulations. The financial institution can make payments, permissible under FEMA regulations, from its SNRRA, in its capacity as a customer, by suitably instructing the domestic bank with whom the SNRRA is maintained.

Background

The Reserve Bank modified the directions after examining the issues, suggestions and queries from the stakeholders regarding operations of the IBUs and financial institutions in IFSCs.

(https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10918&Mode=0)

Banks' Investment in Units of REITs and InvITs

The Reserve Bank on April 18, 2017 allowed banks to participate in Real Estate Investment Trusts (REITs) and Infrastructure Investment Trusts (InvITs) within the overall ceiling of 20 per cent of their net worth permitted for direct investments in shares, convertible bonds/ debentures, units of equity-oriented mutual funds and exposures to Venture Capital Funds (VCFs) [both registered and unregistered], subject to the following conditions:

- Banks should put in place a Board approved policy on exposures to REITs/ InvITs which lays down an internal limit on such investments within the overall exposure limits in respect of the real estate sector and infrastructure sector;
- Banks shall not invest more than 10 per cent of the unit capital of an REIT/ InvIT; and
- Banks should ensure adherence to the prudential guidelines issued by the Reserve Bank from time to time on Equity investments by Banks, Classification and Valuation of Investment Portfolio, Basel III Capital requirements for Commercial Real Estate Exposures and Large Exposure Framework, as applicable.

(https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10929&Mode=0)

Compliance with Accounting Standard by Banks

The Reserve Bank on April 18, 2017 has clarified that the repatriation of accumulated profits shall not be considered as disposal or partial disposal of interest in non-integral foreign operations. Accordingly, banks shall not recognise in the profit and loss account, the proportionate exchange gains or losses held in the foreign currency translation reserve on repatriation of profits from overseas operations.

Background

It has been observed that banks have been recognising gains in profit and loss account from Foreign Currency Translation Reserve (FCTR) on repatriation of accumulated profits / retained earnings from overseas branch(es) by treating the same as partial disposal. The matter has been examined taking into consideration, among others, the views of the Institute of Chartered Accountants of India.

(https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10930&Mode=0)

Additional Provisions for Standard Advances

With a view to ensure that banks have adequate provisions for loans and advances at all times, the Reserve Bank on April 18. 2017 advised all scheduled commercial banks (excluding RRBs) as under:

i) Banks shall put in place a Board–approved policy for making provisions for standard assets at rates higher than the regulatory minimum, based on evaluation of risk and stress in various sectors;

ii) The policy shall require a review, at least on a quarterly basis, of the performance of various sectors of the economy to which the bank has an exposure to evaluate the present and emerging risks and stress therein. The review may include quantitative and qualitative aspects like debt-equity ratio, interest coverage ratio, profit margins, ratings upgrade to downgrade ratio, sectoral non-performing assets/stressed assets, industry performance and outlook, legal/ regulatory issues faced by the sector, etc. The reviews may also include sector specific parameters;

iii) More immediately, as the telecom sector is reporting stressed financial conditions, and presently interest coverage ratio for the sector is less than one, Board of Directors of the banks may review the telecom sector latest by June 30, 2017, and consider making provisions for standard assets in this sector at higher rates so that necessary resilience is built in the balance sheets should the stress reflect on the quality of exposure to the sector at a future date. Besides, banks should also subject the exposure to the sector to closer monitoring.

It is advised that the provisioning rates prescribed are the regulatory minimum and banks are encouraged to make provisions at higher rates in respect of advances to stressed sectors of the economy.

(https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10931&Mode=0)

Disclosure in the Notes to Accounts

In order to ensure greater transparency and promote better discipline with respect to compliance with Income Recognition, Asset Classification and Provisioning (IRACP) norms, the Reserve Bank on April 18, 2017 advised banks to make suitable disclosures, wherever either (a) the additional provisioning requirements assessed by the Reserve bank exceed 15 percent of the published net profits after tax for the reference period or (b) the additional Gross NPAs identified by the Reserve Bank exceed 15 percent of the published incremental Gross NPAs for the reference period, or both.

Background

The Reserve Bank assesses compliance by banks with extant prudential norms on income recognition, asset classification and provisioning IRACP as part of its supervisory processes. There have been instances of material divergences in banks' asset classification and provisioning from the Reserve Bank norms, thereby leading to the published financial statements not depicting a true and fair view of the financial position of the bank.

(https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10932&Mode=0)

Interest Rate Data on Monthly Basis from April 2017

With a view to improving the frequency and timeliness of release of interest rate data, the Reserve Bank on April 3, 2017 has decided that the following four tables will now be released on a monthly basis beginning April 2017:

- Bank group-wise WALR on outstanding rupee loans;
- Bank group-wise WALR on fresh rupee loans sanctioned;
- Individual bank-wise 1- year MCLR; and
- Bank group-wise 1- year median MCLR
- The tables are at present being released on a quarterly basis.

The Reserve Bank has been publishing data on lending rates of banks on its website every quarter since the quarter ended June 2002.

A new table on bank-group-wise weighted average domestic term deposit rates has also been introduced.

(https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=40045)

Financial Inclusion and Development

Financial Literacy Week

To emphasise the importance of financial literacy, the Reserve Bank on April 13, 2017 has decided to observe the week from June 5 to June 9, 2017 as Financial Literacy Week across the country.

The literacy week will focus on four broad themes, namely, KYC, Exercising Credit Discipline, Grievance Redressal and Going Digital (UPI and *99#). The five messages that will be communicated to the common man based on the above broad themes are available under "Financial Literacy Week" in the downloads section of the financial education webpage of the Reserve Bank.

Local language versions of the posters (A3 size) for display in bank branches, flyers (A5 size) for distribution to camp participants and charts (A2 size) for use by trainers during camps, would be printed and provided by the regional offices of the Reserve Bank.

Banks are advised to make logistical arrangements to collect the posters/flyers/charts from the Regional offices of the Reserve Bank during the first two weeks of May and distribute the same to their branches and Financial Literacy Centres (FLCs) well in advance before the Financial Literacy Week.

During the week, the following activities have been planned:

- Banks to advise their Financial Literacy Centres to conduct special camps on each of the five days in backward/unbanked areas. FLC Counsellors may utilise the charts of A2 size for training purposes. FLCs may distribute the promotional material of A5 sizes to the participants.
- All bank branches in the country may display A3 size posters on the five messages in the local language in a prominent place inside the branch premises. These posters will continue to be displayed for at least six months in the branch premises even after the Financial Literacy week is over.
- Banks may display one message each day on the home page of their websites in English and Hindi and also display one message each day on the ATM screens across the country in English and the local languages
- All Rural branches may conduct one camp on any of the five days of the week after branch hours.
- An online quiz will be hosted for the general public on the four broad themes to generate interest/awareness about financial literacy. Details of the quiz will be intimated shortly through the Reserve Bank's website www.rbi.org.in.

It is the endeavour of the Reserve Bank to reach out to the common man during the Financial Literacy week and seek the whole hearted co-operation from the banking fraternity at large in making this event a grand success.

(https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10920&Mode=0)

Non Banking Regulation

Requirement of NOF for ARCs

The Reserve Bank on April 28, 2017 advised that no Asset Reconstruction Company (ARC) shall commence or carry on the business of securitisation or asset reconstruction without having Net Owned Fund (NOF) of not less than Rupees two crore or such other higher amount as the Reserve Bank may, by notification, specify.

Accordingly, and keeping in view the greater role envisaged for ARCs in resolving stressed assets as also the recent regulatory changes governing sale of stressed assets by banks to ARCs, it has been decided to fix the minimum NOF requirement for ARCs at ₹ 100 crore on an ongoing basis

All the ARCs which are already registered with Reserve Bank of India as on the date of the Notification and not having the revised minimum NOF as on date shall achieve a minimum NOF of ₹ 100 crore latest by March 31, 2019. ARCs shall submit a certificate from their Statutory Auditors periodically as evidence of compliance thereof.

(https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10949&Mode=0)

Government and Bank Accounts

Systems and Controls for Government Banking

The Reserve Bank on April 7, 2017 advised all agency banks to ensure that internal/concurrent audit at bank branches verifies whether government business is being conducted as per rules and regulations prescribed by the Government/Reserve Bank of India. Accordingly, the internal/concurrent audit at bank branches may also examine, among other things, various aspects of government banking, such as, agency commission claims and pension payments.

(https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10912&Mode=0)

Financial Markets Operations

Security Substitution Facility

The Reserve Bank on April 12, 2017 allowed substitution of collateral (security) by the market participants during the tenor of the term repos conducted by Reserve Bank of India under the Liquidity Adjustment Facility, from April 17, 2017.

The securities offered for substitution by the market participants shall be of similar market value based on the latest prices published by the Fixed Income Money Market and Derivatives Association of India (FIMMDA).

The facility will be available in the e-kuber portal from Monday to Friday between 9:00 a.m. and 5:00 p.m. on all working days in Mumbai.

(https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10919&Mode=0)

Debt Management

Draft Framework on introduction of Tri-Party Repo

The Reserve Bank of India on April 11, 2017 released the draft framework on the introduction of Tri-Party Repo. Tri-party repo will enable market participants to use underlying collateral more efficiently and facilitate development of the term repo market in India. Draft directions allow introduction of tri-party repo on both Government securities and corporate bonds.

Comments on the draft framework are invited from market participants by May 5, 2017. Comments may be emailed or sent by post to the Chief General Manager, Reserve Bank of India, Financial Markets Regulation Department, Central Office, Main Building, Mumbai – 400001.

(https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=40121)

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