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MONETARY AND CREDIT INFORMATION REVIEW

Banking Regulation

Dishonour of cheques – Modification in procedure

The Reserve Bank on August 4, 2016 has decided to modify the procedure concerning the dishonour of cheques. It has been decided to leave it to the discretion of the banks to determine their response to dishonour of cheques of the account holders. Banks should put in place an appropriate policy approved by the Board or its Committee taking into consideration the need to prevent misuse of the cheque drawing facility and avoid penalising customers for unintended dishonour of cheques.

This has been done keeping in view the previous guidelines by the Reserve Bank wherein banks were advised to introduce a condition for operation of accounts with cheque facility that in the event of dishonour of a cheque valuing rupees one crore and above drawn on a particular account of the drawer on four occasions during the financial year for want of sufficient funds in the account, no fresh cheque book would be issued. Also, the bank may consider closing current account at its discretion. (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10541&Mode=0)

Implementation of Indian Accounting Standards (Ind AS)

The Reserve Bank on August 4, 2016 has advised that select All-India Term Lending and Refinancing Institutions(AIFIs) (Exim Bank, NABARD, NHB and SIDBI), shall follow the Indian Accounting Standards as notified under the Companies (Indian Accounting Standards) Rules, 2015, subject to any guideline or direction issued by the Reserve Bank in this regard, in the following manner:

(i) AIFIs shall comply with the Indian Accounting Standards (Ind AS) for financial statements for accounting periods beginning from April 1, 2018 onwards, with comparatives for the periods ending March 31, 2018 or thereafter. Ind AS shall be applicable to both standalone financial statements and consolidated financial statements. "Comparatives" shall mean comparative figures for the preceding accounting period.

(ii) AIFIs shall apply Ind AS only as per the above timelines and shall not be permitted to adopt Ind AS earlier.

2. Ind AS implementation is likely to significantly impact the financial reporting systems and processes and, as such, these changes need to be planned, managed, tested and executed in advance of the implementation date. Each AIFI is advised to set up a Steering Committee headed by an official of the rank of an Executive Director (or equivalent) comprising members from cross-functional areas of the AIFI to immediately initiate the implementation process. The name and details of the designated official and the team may be forwarded by email to us. The Audit Committee of the Board shall oversee the progress of the Ind AS implementation process and report to the Board at quarterly intervals. The critical issues which need to be addressed in the Ind AS implementation plan include the following:

a) Ind AS Technical Requirements: Diagnostic analysis of differences between the current accounting framework and Ind AS, significant accounting policy decisions impacting financials, drafting accounting policies, preparation of disclosures, documentation, preparation of proforma Ind AS financial statements, timing the changeover to Ind AS, and dry-run of accounting systems and end-to-end reporting process before the actual conversion.

b) Systems and processes: Evaluate system changes - assessment of processes requiring changes, issues having significant impact on information systems (including IT systems), and develop/strengthen data capture system, where required.

c) Business Impact: Profit planning and budgeting, taxation, capital planning, and impact on capital adequacy.

d) People - Evaluation of resources: Adequate and fully dedicated internal staff for implementation, comprehensive training strategy and program.

e) Project management: Managing the entire process-holistic approach to planning and execution by ensuring that all linkages are established between accounting, systems, people and business, besides effective communication strategies to stakeholders. (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10542&Mode=0)

Capacity Building in Banks and AIFIs

The Reserve Bank on August 11, 2016 has notified that the Committee on Capacity Building has made extensive recommendations pertaining to the overall HRM function per se, as also specific recommendations relating to particular areas/components of HRM function, viz., recruitment, performance assessment, promotion, placement, job rotation, etc. After examining the recommendations in detail, it is felt that recommendations pertaining to the banks may be implemented by the banks based on their organisational objectives and business strategies, after taking approval from their respective Boards.

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2. The Committee has also made a number of recommendations for certification of staff. In this regard, some of the recommendations of the Committee for implementation by banks are as under:

a. Banks should identify specialised areas for certification of the staff manning key responsibilities. To begin with, the banks should make acquiring of a certificate course mandatory for the following areas:

- Treasury operations – Dealers, mid-office operations.
- Risk management – credit risk, market risk, operational risk, enterprise-wide risk, information security, liquidity risk.
- Accounting – Preparation of financial results, audit function.
- Credit management – credit appraisal, rating, monitoring, credit administration.

Banks are free to require certification for other areas of work also. The employees working in the aforementioned areas should be asked to acquire certifications within a specified period, say, 6 months. This period can be extended depending on the time required for the certification. Banks should have a specific policy in place for this purpose.

b. To address the issues of mis-selling and to minimise customer complaints, the employees involved in marketing third party retail products and wealth management products must necessarily undergo an appropriate certification process. Where other financial sector regulators have prescribed any certifications, these must be complied with.

c. The issue of setting up of an accreditation agency for assuring and accrediting learning initiatives within the banking industry, etc., is being examined separately. In the interim, IBA has been requested to identify in consultation with the Reserve Bank and provide to its members, by end December 2016, a list of institutions and courses that will meet the certification requirements for different work areas mentioned above. For this exercise, IBA may, form an expert group comprising such agencies, institutions at it deems necessary

d. After the release of list, the banks should identify the courses/certifications that are suitable for their operations and put in place a Board approved policy, mandating obtainment of such certifications by its employees working in the respective areas. The banks should ensure that by end-March 2017, the employees in relevant areas have commenced the process of obtaining necessary certifications.

4. Keeping in view the fact that the Reserve Bank had constituted a 'Committee on Capacity Building' (July 2014) under the Chairmanship of former Executive Director, Shri G Gopalakrishna, with the objective of implementing non-legislative recommendations of the Financial Sector Legislative Reforms Commission (FSLRC), relating to capacity building in banks and non-banks, streamlining training intervention and suggesting changes thereto in view of ever increasing challenges in banking and non-banking sector. (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10548&Mode=0)

Partial Credit Enhancement (PCE) to Corporate Bonds

The Reserve Bank on August 25, 2016 has decided to increase the aggregate exposure limit from the banking system towards the Partial Credit Enhancement (PCE) to 50 per cent of the bond issue size, with a limit up to 20 per cent of the bond issue size for an individual bank.

2. As the purpose of PCE by banks is to enable wide investor participation in the corporate bond market, banks are expected not to invest in corporate bonds which are credit enhanced by other banks.(https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10571&Mode=0)

Prudential Norms for Off-balance Sheet Exposures of Banks

The Reserve Bank on August 25, 2016 has clarified that in cases where a derivative contract is restructured, the mark-to-market value of the contract on the date of restructuring should be cash settled. Cash settlement of only the change in mark-to-market value of the restructured derivative contract is required. It may, however, be ensured that the restructuring of the derivative contract is carried out at prevalent market rates, and not on the basis of off-market rates. (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10570&Mode=0)

Risk Weights for Exposures to Corporates, AFCs and NBFC-IFCs - Review

The Reserve Bank on August 25, 2016 has decided to make the following modifications to the risk weights applicable to unrated exposures to captioned entities:

- With effect from June 30, 2017, all unrated claims on corporates, AFCs, and NBFC-IFCs having aggregate exposure from banking system of more than INR 200 crore will attract a risk weight of 150%.
- However, claims on corporates, AFCs, and NBFC-IFCs having aggregate exposure from banking system of more than INR 100 crore which were rated earlier and subsequently have become unrated will attract a risk weight of 150% with immediate effect.

Keeping in mind the fact that at present unrated exposures to these entities attract a risk weight of 100 per cent (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10569&Mode=0)

Financial Markets Regulation Department

Market Repo Transactions in Government Securities Market

The Reserve Bank on August 25, 2016 has decided to relax the eligibility conditions and other terms of participation in repo transactions, particularly relating to the participation of gilt account holders in the repo market and has decided to permit the following transactions:

a. Gilt account holders (GAH) may enter into a repo transaction with its custodian or another GAH of the same custodian;

b. Co-operative banks may enter into repo transactions with all eligible market participants, including NBFCs;

c. Listed companies may borrow or lend under repos with all eligible market participants (including banks) without the minimum tenor restriction of seven days;

d. Eligible unlisted companies may borrow from any eligible market participant against special Government of India securities issued to them;

e. NBFCs registered with RBI, including Government companies which adhere to the prudential norms prescribed for NBFCs by the Department of Non-Banking Regulation, Reserve Bank of India, may borrow/lend under repos with all eligible market participants.(https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10573&Mode=0)

Repo / Reverse repo in Corporate Debt Securities

The Reserve Bank on August 25, 2016 has decided to permit brokers registered with the Securities and Exchange Board of India (SEBI) and authorised as market makers in corporate bond market to undertake repo / reverse repo contracts in corporate debt securities subject to the Directions ibid. (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10572&Mode=0)

Financial Inclusion and Development Department

Interest Subvention Scheme

The Reserve Bank on August 4, 2016 has notified that Government of India has approved the implementation of the Interest Subvention Scheme for the year 2016-17 for short term crop loans upto Rs 3 lakh with the following stipulations:

i) A subvention of 2% per annum will be made available to Public Sector Banks (PSBs) and in respect of loans given by the rural and semi–urban branches of Private Sector Scheduled Commercial Banks, for short term crop loan upto Rs.3,00,000/- per farmer provided the lending institutions make available short term credit at the ground level at 7% per annum to farmers. The 2% interest subvention will be calculated on the crop loan amount from the date of its disbursement/ drawal upto the date of actual repayment of the crop loan by the farmer or upto the due date of the loans fixed by the banks, whichever is earlier, subject to a maximum period of one year.

ii) An additional interest subvention of 3% per annum will be available to the prompt payee farmers from the date of disbursement of the crop loan upto the actual date of repayment by farmers or upto the due date fixed by the bank for repayment of crop loan, whichever is earlier, subject to a maximum period of one year from the date of disbursement. This also implies that the farmers paying promptly would get short term crop loans @ 4% per annum during the year 2016-17. This benefit would not accrue to those farmers who repay after one year of availing such loans.

iii) In order to discourage distress sale by farmers and to encourage them to store their produce in warehouses against warehouse receipts, the benefit of interest subvention will be available to small and marginal farmers having Kisan Credit Card for a further period of upto six months post-harvest on the same rate as available to crop loan against negotiable warehouse receipt for keeping their produce in warehouses.

iv) To provide relief to farmers affected by natural calamities, the interest subvention of two percent will continue to be available to banks for the first year on the restructured amount. Such restructured loans may attract normal rate of interest from the second year onwards as per the policy laid down by the RBI.

2. Banks may give adequate publicity to the above scheme so that the farmers can avail the benefits.

3. It was also advised as under:

i) Claims in respect of 2% interest subvention and 3% additional interest subvention may be submitted to the Chief General Manager, Financial Inclusion and Development Department, Reserve Bank of India, Central Office.

ii) In respect of 2% interest subvention, banks are required to submit their claims on a half-yearly basis as at September 30, 2016 and March 31, 2017, of which, the latter needs to be accompanied by a Statutory Auditor's certificate certifying the claims for subvention for the entire year ended March 31, 2017 as true and correct. Any remaining claim pertaining to the disbursements made during the year 2016-17 and not included in the claim for March 31, 2017, may be consolidated separately and marked as an 'Additional Claim' duly audited by Statutory Auditors certifying the correctness.

iii) In respect of the 3% additional subvention, banks may submit their one-time consolidated claims pertaining to the disbursements made during the entire year 2016-17 latest by April 30, 2018, duly audited by Statutory Auditors certifying the correctness. (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10540&Mode=0)

Priority Sector Lending status for Factoring Transactions

To increase liquidity support for the MSME sector, the Reserve Bank on August 11, 2016 has decided that factoring transactions on 'with recourse' basis shall be eligible for priority sector classification by banks, which are carrying out the business of factoring departmentally. The factoring transactions taking place through TReDS shall also be eligible for classification under priority sector upon operationalization of the platform.

2. Banks may classify their outstanding factoring portfolio on the reporting dates under MSME category, wherever the 'assignor' in the factoring transaction is a Micro, Small or Medium Enterprise, subject to the corresponding limits for investment in plant and machinery/ equipment and other extant applicable guidelines for priority sector classification.

3. In this regard, it is also reiterated that on Provision of Factoring Services by Banks - Review, inter-alia, the borrower's bank may also obtain from the borrower periodical certificates regarding factored receivables to avoid double financing/ counting. Further, the 'factors' must ensure to intimate the limits sanctioned to the borrower to the concerned banks and details of debts factored taking responsibility to avoid double financing. (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10549&Mode=0)

Pradhan Mantri Fasal Bima Yojna - Non-feeding of data by bank branches

The Reserve Bank in consultation with Ministry of Agriculture & Farmers Welfare (MoA & FW) on August 25, 2016 has advised all banks to enter farmer details in the unified portal for crop insurance. It has been brought to the Reserve Bank's notice that entries are not being made by the bank branches in the portal. Resultantly MoA & FW, State Governments etc. are not able to cull out any data leading to difficulties in assessment of coverage of crops insured, premiums deducted, etc. Banks are therefore advised to issue necessary instructions to their branches to feed the relevant data in the portal at the earliest.

As per the PMFBY operational guidelines of the Government of India, banks are also expected to capture all relevant data including land and crop details of all loanee farmers and non-loanee farmers availing crop insurance through the branches.

The banks have been advised to ensure strict compliance of the provisions of the Pradhan Mantri Fasal Bima Yojna and ensure coverage of 100% of defined loanee farmers along with good number of non - loanee farmers to achieve the defined objectives and targets fixed under the Scheme. (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10561&Mode=0)

Department of Banking Supervision

Risk- based Internal Audit

Keeping in view the change in demographic profile of the staff in banks on account of retirement leading to shortage of staff to conduct internal audit which is an important component of Risk Based Supervision (RBS), the Reserve Bank on August 25, 2016 has decided to permit banks to engage the services of its retired officials for assisting in internal audit subject to following conditions:

i. Each bank should formulate with the approval of their Board of Directors, a policy to engage the services of its retired personnel for a maximum tenure not exceeding three years in the areas where it does not have enough expertise. The policy should inter - alia include the terms of engagement, review of performance, termination of services, etc.

ii. Banks need to ensure that the retired personnel so engaged, work under the close supervision of the Management of the bank and the final sign off of the audit reports would be the responsibility of the serving bank officials.

Pay IT dues in advance at RBI or at authorised bank branches

The Reserve Bank on August 12, 2016 has appealed to income tax assessees to remit their income tax dues sufficiently in advance of the due date. It has also stated that assessees can use alternate channels like select branches of agency banks or the facility of online payment of taxes offered by these banks. These will obviate the inconvenience involved in standing in long queues at the Reserve Bank offices.

It is observed that the rush for remitting Income – Tax dues through the Reserve Bank of India has been far too heavy towards the end of September every year and it becomes difficult for the Reserve Bank to cope with the pressure of issuing receipts although additional counters to the maximum extent possible are provided for the purpose.

Twenty-nine agency banks are authorised to accept payments of Income Tax dues. (https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=37773)

In order to avoid conflict of interest, the retired personnel so engaged may not be assigned branches/ sections, where they had worked while in active service with the bank. (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10575&Mode=0)

RBI publishes Working Group Report on Corporate Bond Market in India

The Reserve Bank on August 18, 2016 placed on its website the report of the Working Group on Development of Corporate Bond Market in India.

The Group has made recommendations for market development based on detailed examination of the issues highlighted by earlier committees on the corporate bond market and suggestions received from the market participants. The recommendations relate to market structure, instrument design/valuation, regulation and legal aspects of the corporate bond market.

Background

The Sub-Committee of the Financial Stability Development Council at its meeting held on September 10, 2015 had decided to constitute a Working Group on Development of Corporate Bonds with representations from the Ministry of Finance, Government of India and all the regulators. Accordingly, a Working Group was constituted under chairmanship of Shri Harun R. Khan, the then Deputy Governor, Reserve Bank of India with senior officials from the Ministry of Finance, Securities and Exchange Board of India, Insurance Regulatory and Development Authority of India and Pension Fund Regulatory and Development Authority as members. (https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=37815)

Interesting, Profitable, and Challenging: Banking in India Today

"The current times are interesting, profitable, and challenging for the financial sector. Interesting because the level of competition is going to increase manifold, both for customers as well as for talent, transforming even the sleepiest areas in financial services; profitable because new technologies, information, and new techniques will open up vastly new business opportunities and customers; and challenging because competition and novelty constitute a particularly volatile mix in terms of risk," Dr. Raghuram G. Rajan, Governor, Reserve Bank of India said this in his speech to FICCI-IBA Annual Global Banking Conference, held in Mumbai on August 16, 2016.

Stating that India will have enormous project financing needs in the coming days, the Governor hoped that banks will not be irrationally exuberant in lending this time. According to him, first the focus should move more to improving the operational efficiency of stressed assets, and creating the right capital structure so that all stakeholders could benefit. Toward this, he suggested simultaneous action on two fronts - a creative search for new management teams, including the possible use of public sector firms or private sector agents, as also well-structured performance incentives such as bonuses for meeting cash flow/profit benchmarks and stock options.

To lower the risks further, he suggested bringing in more in-house expertise to project evaluation, including understanding demand projections for the project's output, likely competition, and the expertise and reliability of the promoter. He also suggested that real risks should be mitigated where possible, and where not, shared contractually between the promoter and financiers, or a transparent arbitration system agreed upon. He also said that the financiers should put in a robust system of project monitoring and appraisal, including where possible, careful real-time monitoring of costs by using information technology (IT). "It only required a stronger marriage between information technology and financial engineering with an important role for practical industry knowledge and incentive design," he said. An incentive structure for bankers so that they structure and monitor loans carefully, and get significant rewards, including promotions, if loans worked out was necessary according to him.

Further, authorities like the central bank and the Government should, over the medium term, reduce the differences in regulatory treatment between public sector banks and private sector banks, and more generally, between banks and other financial institutions to encourage effective competition among them. This can be achieved by paying for delivery of mandates and targeting them better towards the truly underserved as also withdrawing preferential treatment, to the extent feasible, at commensurate pace.

A parallel task for public sector banks was to improve the governance and management. He suggested that as the Bank Board Bureau (BBB) gains experience in appointment process, the final decision relating to appointments of executives and of non-official directors on bank boards should be left to it; executive appointments ultimately devolving on bank boards once they get professionalised. It was also important, in his view, to streamline and reduce the overlaps between the jurisdictions of the authorities, and specify clear triggers or situations where one authority's oversight is invoked and move much of the governance to the bank's board.

To fill out the ranks of middle management that have thinned out by retirements, banks should look for talent with expertise in project evaluation, risk management, and IT, including cyber security. Solutions like persuading courts to allow some campus hire, making bank entrance exams much less onerous to take, with applications, tests, and results, wherever possible, available quickly and online and to have more freedom to hire locally, and pay wages commensurate with the local labour market should be considered. Solutions like increased emphasis on performance evaluation, including identifying low performers with the intent of helping them improve, rewards like Employee Stock Ownership Plans (ESOPs) that give all employees a stake in the future of the bank might also be helpful. "None of these changes are easy, but they are also not impossible," he emphasised.(https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=37786)

Master Circulars/Directions

The Reserve Bank issued following master directions/circulars in the month of August 2016:-

Master Directions/Circulars	Date of issue
Master Direction - Residuary Non-Banking Companies (Reserve Bank) Directions, 2016	August 25, 2016
Master Direction - Standalone Primary Dealers (Reserve Bank) Directions, 2016	August 25, 2016
Master Direction - Miscellaneous Non-Banking Companies (Reserve Bank) Directions, 2016	August 25, 2016
Master Direction - Exemptions from the provisions of RBI Act, 1934	August 25, 2016
Master Direction - Core Investment Companies (Reserve Bank) Directions, 2016	August 25, 2016
Master Direction - Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 2016.	August 25, 2016
Master Circular – Collection of Direct Taxes - OLTAS	August 25, 2016

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