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MONETARY AND CREDIT INFORMATION REVIEW

Banking Regulation

Guidelines for Concurrent Audit System revised

The Reserve Bank has revised the guidelines for concurrent audit system in commercial banks, in view of the changes in banks' organisational structure, business models, use of technology (implementation of Core Banking Solution), etc.

(I) Scope of Concurrent Audit

Concurrent audit is essentially a management process integral to the establishment of sound internal accounting functions and effective controls and setting the tone for a vigilant internal audit to preclude the incidence of serious errors and fraudulent manipulations. The audit will necessarily have to see whether the transactions or decisions are within the policy parameters laid down by the Head Office, they do not violate the instructions or policy prescriptions of the Reserve Bank, and that they are within the delegated authority.

(II) Coverage of Business/Branches

New areas posing risk may be brought under the purview of concurrent audit. Non-branch units may be brought under the purview of concurrent audit. The branches with high risk are to be subjected to concurrent audit irrespective of their business size. Further, all specialised branches viz., agriculture, small and medium enterprises(SME), corporate, retail assets, portfolio management, treasury, forex, back office, etc., may be covered under concurrent audit. Certain areas where risk has reduced on account of computerisation, implementation of core banking system may be excluded from the purview of concurrent audit. Concurrent audit at branches should cover at least 50 per cent of the advances and 50 per cent of deposits of a bank. Concurrent audit should be conducted in:

(a) Branches rated as high risk or above in the last Risk Based Internal Audit (RBIA) or serious deficiencies found in Internal Audit;

(b) All specialised branches like large corporate, mid corporate, exceptionally large/very large branches (ELBs/VLBs), SME;

(c) All centralised processing units like Loan Processing Units (LPUs), service branches, centralised account opening divisions, etc.,

(d) Any specialised activities, such as, wealth management, portfolio management services, card products division, etc., data centres, treasury/branches handling foreign exchange business, investment banking, etc. and bigger overseas branches, critical head office departments, and

(e) Any other branches or departments where, in the opinion of the bank, concurrent audit is desirable.

(III) Types of activities to be covered

(i) The main role of concurrent audit is to supplement the efforts of the bank in carrying out simultaneous internal check of the transactions and other verifications and compliance with the procedures laid down.

(ii) The scope of concurrent audit should be wide enough/ focused to cover certain fraud - prone areas, such as, handling of cash, deposits, advances, foreign exchange business, off-balance sheet items, credit-card business, internet banking, etc.

(iii) The detailed scope of the concurrent audit should be clearly and uniformly determined for the bank as a whole by the bank's Inspection and Audit Department in consultation with the bank's Audit Committee of the Board of Directors (ACB).

(iv) In determining the scope, importance should be given to checking high-risk transactions having large financial implications as opposed to transactions involving small amounts.

(v) While the detailed scope of concurrent audit may be determined and approved by ACB, certain minimum items of coverage are given. In addition to the above, the items where the Reserve Bank has specifically advised the banks to be covered under concurrent audit, may also be part of the checklist of the concurrent auditor.

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Use Info on CRILC: Banks advised

The Reserve Bank advised scheduled commercial banks (excluding regional rural banks) to make use of the information available in Central Repository of Information on Large Credits (CRILC) and not limit their due diligence to seeking no-objection certificate (NOC) from the bank with whom the customer is supposed to be enjoying the credit facilities as per the declaration. Further banks may also seek 'No Objection Certificate' from the drawee bank where the initial deposit to current account is made by way of a cheque. The Reserve Bank has set up CRILC to collect, store, and disseminate data on all borrowers' credit exposures. Banks / Financial Institutions are required to report their credit information to CRILC. (DBR.Leg.BC.25./09.07.005/2015-16 dated July 2, 2015)

RBI to pay Agency Commission to Banks for KVP and Sukanya Samriddhi Account Scheme

The Reserve Bank has decided to pay agency commission to authorised banks for handling the work relating to the Kisan Vikas Patra(KVP), 2014 and Sukanya Samriddhi Account schemes as per the extant rates. Further, the Government of India has desired to have a bank-wise and region-wise weekly progress report on implementation of Sukanya Samriddhi Account. Accordingly, all agency banks implementing the scheme are advised to furnish region-wise weekly progress report indicating the number of Sukanya Samriddhi Accounts opened to Budget Division, Department of Economic Affairs with a copy to Joint Director, National Saving Institute, CGO Complex, 'A' Wing, 4th Floor, Seminary Hills, Nagpur – 440006. (DGBA.GAD.No. 14/15.02.003/2015-16 dated July 2, 2015)

Guidelines for Concurrent Audit System revised

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(IV) Appointment of Auditors and Accountability

(i) The option to consider whether concurrent audit should be done by bank's own staff or external auditors (which may include retired staff of its own bank) is left to the discretion of individual banks.

(ii) In case the bank has engaged its own officials, they should be experienced, well trained and sufficiently senior. The staff engaged in concurrent audit must be independent of the branch where concurrent audit is conducted.

(iii) Appointment of an external audit firm may be initially for one year and extended upto three years, after which an auditor could be shifted to another branch subject to satisfactory performance.

(iv) If external firms are appointed and any serious acts of omission or commission are noticed in their working, their appointments may be cancelled and the fact may be reported to RBI & ICAI.

Apart from these, the guidelines also include instructions regarding (V) Facilities for effective Concurrent Audit; (VI) Remuneration and (VII) Reporting Systems.

Since the concurrent audit system is regarded as part of a bank's early warning system to ensure timely detection of irregularities and lapses, which also helps in preventing fraudulent transactions at branches, the bank's management may continue to bestow serious attention to the implementation of various aspects of the system, such as, selection of branches/coverage of business operations, appointment of auditors, appropriate reporting procedures, follow-up/ rectification processes and utilisation of the feedback from the system for appropriate and quick management decisions.

The Reserve Bank has further advised banks to review the present system of concurrent audit immediately and incorporate necessary changes therein. The modified concurrent audit system of the bank should then be placed before the Audit Committee of Board of Directors (ACB).DBS.CO.ARS.No. BC. 2/08.91.021/2015-16 dated July 16, 2015)

RBI introduces STP of Fixed Rate LAF and MSF

As part of the endeavour to smoothen the liquidity management operations, the Reserve Bank, on July 27, 2015 introduced Straight Through Processing (STP) in fixed rate Liquidity Adjustment Facility (LAF) Repo, fixed rate LAF Reverse Repo and Marginal Standing Facility (MSF) operations. This will enable eligible participants to receive the credit or debit immediately on placement of the bids or offers, subject to the availability of the collateral or funds, within the prescribed time window. There will be no change in the process of placing bids/offers by the eligible participants. The STP will be introduced with effect from August 3, 2015 .

Eligible participants can, as hitherto, place multiple bids/offers in the respective liquidity facilities. Settlement of the transaction will be automatic and immediate after the placement of the bid/offer. The transactions undertaken by a participant will be final and request for cancellation of bids or offers will not be entertained.

The time window for availability of the respective facility of fixed rate LAF Repo, fixed rate LAF Reverse Repo and MSF, after the introduction of STP, will be same as hitherto. The timings for the LAF and MSF windows will be extended for a longer duration in near future to give eligible participants more flexibility to operate these windows.

The automation of these facilities will, in no way, affect the discretionary character of these facilities and the Reserve Bank will continue to determine the extent of liquidity injection/absorption depending upon the prevailing liquidity conditions in the system. The other terms and conditions for LAF and MSF will remain unchanged.

Banks can slot SLR / MSF Securities in Day 1 Bucket

The Reserve Bank has now allowed commercial banks (excluding regional rural banks and local area banks) to slot their excess statutory liquidity ratio (SLR) securities and marginal standing facility (MSF) eligible securities under the Day-1 bucket. As per the extant instructions, approved securities are required to be slotted under respective maturity buckets, excluding the amount required to be reinvested to maintain SLR corresponding to the Demand and Time Liability (DTL) profile in various time buckets. Securities in excess of mandatory SLR as well as securities eligible for MSF were also required to be slotted as per the above instructions while these securities, in fact, exhibit the liquidity characteristics required for slotting in day-1 bucket in view of their ready access to liquidity by way of repo and MSF presently upto two percent of NDTL. (DBR. No.BP.BC.26/21.04.098/2015-16 July 2, 2015)

Discounting Future Cash Flows for Restructuring Loans

On a review, the Reserve Bank advised all scheduled commercial banks (excluding regional rural banks) that a rate equal to the actual interest rate charged to the borrower before restructuring may be used to discount the future cash flows for the purpose of determining the diminution in fair value of loans on restructuring. In cases where the existing credit facilities to a borrower carry different rates of interest, the weighted average interest rate (with share of each credit facility in the total outstanding of the borrower as on the date of restructuring being used as weights) may be used as the discounting rate. This discount rate may be used to discount both the pre-restructuring cash flows as well as post-restructuring cash flows. This methodology may be consistently used wherever banks are required to compute fair/present value of loans under the guidelines issued by the Reserve Bank, including for the purpose of computing net present value of project loans. This instruction will be applicable to all projects where changes in amortisation schedule have been carried out. Under the extant instructions, a rate equal to the bank's Benchmark Prime Lending Rate or base rate (whichever is applicable to the borrower) as on the date of restructuring plus the appropriate term premium and credit risk premium for the borrower category on the date of restructuring were used to discount future cash flows for the purpose of determining the diminution in fair value of loans on restructuring. (DBR.No.BP.BC.27/21.04.048/2015-16 dated July 2, 2015)

Currency

Numerals in Ascending Size on ₹ 100 Notes

The Reserve Bank on June 25, 2015, issued ₹ 100 denomination banknotes in Mahatma Gandhi Series – 2005 with a new numbering pattern. In these notes, the numerals in both the number panels of these banknotes are in ascending size from left to right, while the first three alphanumeric characters (prefix) remain constant in size.

Printing the numerals in ascending size is a visible security feature in the banknotes so that the general public can easily distinguish a counterfeit note from a genuine one. The Reserve Bank, in consultation with Government of India, has been improving security features of Indian banknotes so as to make their counterfeiting difficult and make it easy for members of public to identify genuine banknotes.

The design of banknotes with numerals in ascending size is similar in all other respects to the current design of ₹100 banknotes in Mahatma Gandhi Series – 2005 except for the new numbering pattern. The banknotes will continue to have "₹" symbol on the obverse and the reverse, an inset letter 'R' in both the numbering panels, bear the signature of Dr. Raghuram G. Rajan, Governor, Reserve Bank of India, and the year of printing '2015' printed on the reverse of the banknotes.

All the banknotes in the denomination of ₹ 100 issued by the Reserve Bank in the past will continue to be legal tender. The new numbering pattern will be introduced in a phased manner in all other denominations.

Co-operative Banking

Guidelines on issue of ATM-cum-Debit Cards

The Reserve Bank has permitted co-operative banks (Primary (Urban) Co-operative Banks/ State Co-operative Banks (StCBs)/ District Central Co-operative Banks) which are Core Banking Solution (CBS) enabled, to issue ATM cards/ ATM-cum-debit cards in tie-up with a sponsor bank. Such banks, being sub-members of National Financial Switch (NFS), are required to fulfil the risk management requirements prescribed by the sponsor bank and meet expenses devolving on them under the agreement with the sponsor bank. Banks should set up their own arrangement for issuing cards, authorisation of cards and customer support/ redressal mechanism and ensure to provide uninterrupted services to their customers. (DCBR.BPD. (PCB/RCB).Cir. No. 1/16.20.000/2015-16 dated July 16, 2015)

Foreign Exchange Management

Investment in Companies engaged in Tobacco Related Activities

In terms of the extant regulations, foreign direct investment is prohibited in manufacturing of cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes. The Reserve Bank has clarified that the prohibition applies only to manufacturing of the products mentioned therein and foreign direct investment in other activities relating to these products including wholesale cash and carry, retail trading etc. shall be governed by the sectoral restrictions laid down in the Foreign Direct Investment (FDI) policy framed by the Department Of Industrial Policy and Promotion, Ministry of Commerce and Industry, Government of India and in the Schedule 1 of Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2000. (A.P. (DIR Series) Circular No.2 dated July 3, 2015)

Re-export of Unsold Rough Diamonds without EDF

In order to facilitate re-export of unsold rough diamonds imported on free of cost basis at Special Notified Zone (SNZ), the Reserve Bank has clarified to authorised dealers that the unsold rough diamonds, when re-exported from the SNZ (being an area within the Customs) without entering the Domestic Tariff Area (DTA), do not require any Export Declaration Form (EDF) formality.

Entry of consignment containing different lots of rough diamonds into the SNZ should be accompanied by a declaration of notional value by way of an invoice and a packing list indicating the free cost nature of the consignment. Under no circumstance, entry of such rough diamonds is permitted into DTA. For the lot/ lots cleared at the Precious Cargo Customs Clearance Centre, Mumbai, Bill of Entry shall be filed by the buyer. AD bank may permit such import payments after being satisfied with the bona-fides of the transaction. Further, AD bank shall also maintain a record of such transactions. (A.P. (DIR Series) Circular No.1 dated July 2, 2015)

Financial Markets

MIBID/MIBOR replaced by New Independent Benchmark from July 22

The existing overnight benchmark interbank rate in India is replaced from July 22, 2015 by a new benchmark called the FBIL Overnight Mumbai Interbank Outright Rate (Financial Benchmarks India Private Ltd-Overnight MIBOR). The FBIL-Overnight MIBOR will be based on actual traded rates and will be administered by a new company called the Financial Benchmarks India Private Ltd (FBIL). The existing rate called the Overnight MIBID/MIBOR based on polled rates is set by FIMMDA-NSE.

Financial Benchmarks India Private Ltd (FBIL) has been jointly formed as an independent company for administration of benchmarks in financial markets by the Fixed Income Money Market and Derivative Association of India (FIMMDA), Foreign Exchange Dealers' Association of India (FEDAI) and Indian Banks' Association (IBA). This follows the recommendations of the Committee on Financial Benchmarks set up by the Reserve Bank in February 2014 (Chairman: Shri P. Vijaya Bhaskar, Executive Director).

Over a period of time, FBIL will also take over the administration of foreign exchange benchmarks and other Indian Rupee interest rate benchmarks in consultation with the stakeholders. FIMMDA and FEDAI who are the current benchmark administrators for the Indian rupee interest rate and foreign exchange benchmarks, respectively, will continue to act as administrators for the Rupee interest rate and foreign exchange benchmarks till they are shifted to FBIL. The Reserve Bank will set up an appropriate oversight mechanism for ensuring that the benchmark determination process and its governance framework remain robust and credible.

Taking note of the concerns arising from reports of manipulation of key benchmark rates in certain financial markets, the Reserve Bank had sought to strengthen the existing framework for benchmark setting process with various measures. Considering that financial benchmarks need to be robust and reliable, the Reserve Bank had advised the benchmark submitters to implement various measures for strengthening the governance framework for benchmark submission. Moreover, FIMMDA and FEDAI had also notified a code of conduct for the submitters.

Non-Banking Regulation

RBI's Prior Approval for Acquisition of NBFCs

On a review, the Reserve Bank issued directions to non-banking financial companies (excluding primary dealers) on prior approval of the Reserve Bank for:

a) any takeover or acquisition of control of an NBFC, which may or may not result in change of management;

b) any change in the shareholding of an NBFC, including progressive increases over time, which would result in acquisition/ transfer of shareholding of 26 per cent or more of the paid up equity capital of the NBFC except in certain specified cases.

c) any change in the management of the NBFC which would result in change in more than 30 per cent of the directors, excluding independent directors. Prior approval would not be required for those directors who get re-elected on retirement by rotation.

However, NBFCs shall continue to inform the Reserve Bank regarding any change in their directors/ management as required in Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 1998, Non-Systemically Important Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2015 and Systemically Important Non-Banking Financial (Non-Deposit Accepting Holding) Companies Prudential Norms (Reserve Bank) Directions, 2015.

NBFCs shall submit an application for obtaining prior approval of the Reserve Bank, with the prescribed documents, to the regional office of the Department of Non-Banking Supervision in whose jurisdiction the registered office of the NBFC is located. A public notice of at least 30 days shall be given before effecting the sale of, or transfer of the ownership by sale of shares, or transfer of control, whether with or without sale of shares. Such public notice shall be given by the NBFCs and also by the other party or jointly by the parties concerned, after obtaining the prior permission of the Reserve Bank. The public notice shall indicate the intention to sell or transfer ownership/ control, the particulars of transferee and the reasons for such sale or transfer of ownership/ control. The notice shall be published in at least one leading national and in one leading local (covering the place of registered office) vernacular newspaper. (DNBR (PD) CC.No. 065/03.10.001/2015-16 dated July 9, 2015 and DNBS. (PD) 029/CGM (CDS)-2015 dated July 9, 2015)

Applicability of Credit Concentration Norms

On a review, the Reserve Bank has advised all non-banking financial companies (excluding primary dealers) that in determining concentration of credit/investment, the following shall be excluded:

(i) investments of NBFC in shares of (i) its subsidiaries; (ii) companies in the same group, to the extent they have been reduced from owned funds for the calculation of net owned fund (NOF) and

(ii) the book value of debentures, bonds, outstanding loans and advances (including hire-purchase and lease finance) made to, and deposits with (i) subsidiaries of the NBFC; and (ii) companies in the same group, to the extent they have been reduced from owned funds for the calculation of NOF. (DNBR (PD) CC.No. 064/03.10.001/2015-16 dated July 2, 2015)

Payment and Settlement Systems

Final Guidelines on PPIs for Mass Transit System

The Reserve Bank on July 9, 2015, issued the final guidelines on Prepaid Payment Instruments for Mass Transit System (PPI-MTS) enabling the issuance of a separate category of semi-closed prepaid payment instruments for mass transit systems. The PPI-MTS can be used within the mass transit systems and will have a minimum validity of six months from date of issue. Such PPIs will be reloadable instruments subject to an outstanding limit of ₹ 2,000/- at any point of time. Apart from the mass transit system, such PPI-MTS can be used at other merchants whose activities are allied to or are carried on within the premises of the transit system.

This new category of semi-closed PPIs has been introduced taking into account the requests received from various segments, including providers of mass transit services, such as, metro train and road transport services. The PPI-MTS will enhance commuter convenience and will also facilitate the migration to electronic payments in line with the country's vision of moving to a less-cash society.

Earlier, the Reserve Bank had placed on its website the draft circular on "Prepaid Payment Instruments (PPI) for Mass Transit System (PPI-MTS)" on May 28, 2015 for public comments.

Financial Inclusion

Committee on Medium-term Path on Financial Inclusion

The Reserve Bank, on July 15, 2015, announced the constitution of a Committee with the objective of working out a medium-term (five year) measurable action plan for financial inclusion with Shri Deepak Mohanty, Executive Director, Reserve Bank as the Chairman. The terms of reference of the Committee are as under:

(i) To review the existing policy of financial inclusion including supportive payment system and customer protection framework taking into account the recommendations made by various committees set up earlier;

(ii) To study cross country experiences in financial inclusion to identify key learnings, particularly in the area of technology-based delivery models, that could inform the Reserve Bank's policies and practices;

(iii) To articulate the underlying policy and institutional framework, also covering consumer protection and financial literacy, as well as delivery mechanism of financial inclusion encompassing both households and small businesses, with particular emphasis on rural inclusion including group-based credit delivery mechanisms;

(iv) To suggest a monitorable medium-term action plan for financial inclusion in terms of its various components like payments, deposit, credit, social security transfers, pension and insurance; and

(v) To examine any other related issues.

It may be recalled that on the occasion of the Reserve Bank's 80th anniversary, Hon'ble Prime Minister in his address urged the Reserve Bank to take the lead in encouraging financial institutions and to set a medium-to-long term target for sustainable financial inclusion.

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