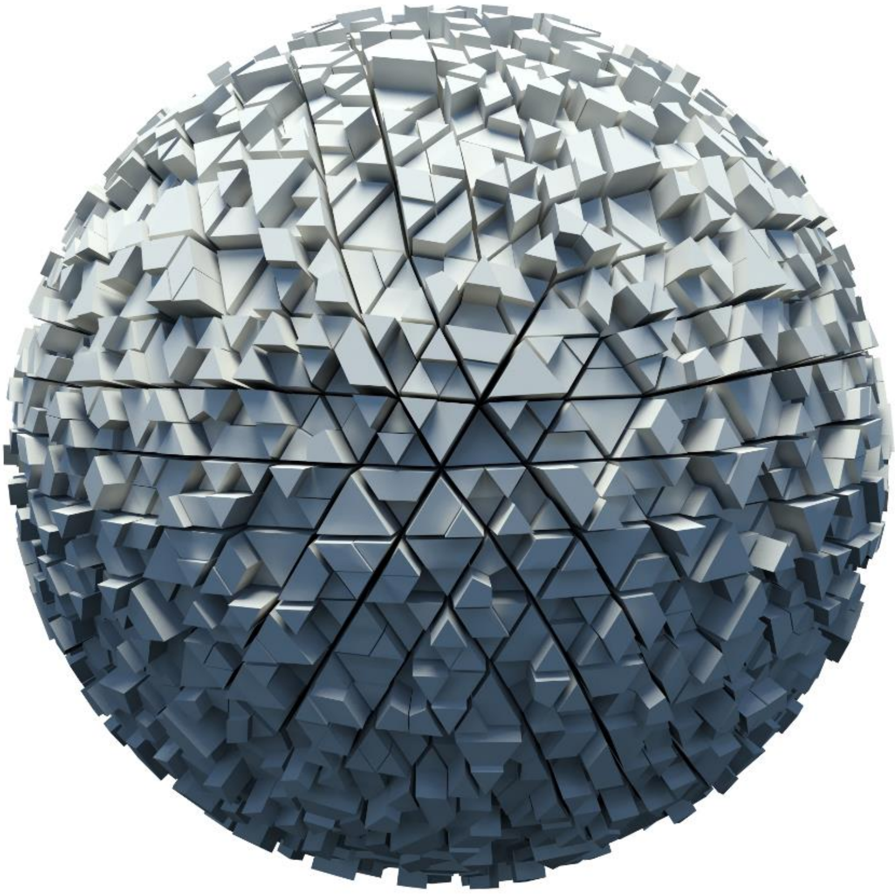

Regulatory Impact Assessment

Banking

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Contents

Preface

Last week, it came as a great surprise to many people worldwide that a majority of British voters – 52 per cent – supported Britain exiting the European Union. This unexpected decision impacted the global financial markets to a severe extent with the Pound dropping to its lowest level against all currencies, notably against US Dollar, against whom such a depreciation as last seen in 1985-86. The Brexit has wide political as well as economic repercussions that would be more clear as and when UK formally exits the EU.

Last month the RBI Governor Raghuram Rajan announced that he won't be renewing his second term, as his first term comes to end on September 3rd. His tenure as RBI governor has largely been successful, with India able to build a mammoth war-chest of forex reserves, rupees value being largely stable against USD and inflation at a comfortable level. Though many expected him to continue his tenor, he will be moving back to his teaching career in USA.

On the domestic front, the recently released provisional estimate of gross value added (GVA) for the year 2015-16 marginally scaled down the annual growth rate to 7.2 per cent, on a deceleration of services sector activity in relation to the advance estimates. There was, however, a sequential pickup in activity in Q4 in line with expectations. As regards in the current financial year, the India Meteorological Department (IMD) has forecast an above-normal and well-distributed south west monsoon as El Nino wanes – albeit with a slightly delayed onset. Realization of this prediction is critical for the outlook for agriculture sector since reservoir levels have been depleted to 17 per cent of capacity – 40 per cent lower than the level a year ago. Even though rabi procurement was lower in April-May 2016 than a year ago, mid-May food stocks at 58 million tones were almost three times the norm for Q1.

With FCNR-B deposit scheme nearing to an end, and to stabilize the Rupee as an impact of outflow of USD $ from the economy, RBI formulated the Foreign Exchange Management (Deposit) Regulations, 2016. Also with large scale violation and abuse of FIRCs, RBI has made it mandatory for reporting of transactions on Export Data Processing and Monitoring System (EDPMS) platform and e-FIRCs will be issued to check on the abuse of FIRCs.

In the coming months, with monsoon expected to be above normal and the 7th Pay commission coming into force, we expect the consumption in the economy may increase and there may be inflationary pressure in the economy. As an outcome of the same, Raghuram Rajan's successor will have his hands full with these unique situations and hope he/she will be able to lead Indian economy and banking industry to a path of growth.

Our point of view on key RBI guidelines issued in May 2016

Foreign Exchange Management (Deposit) Regulations, 2016

RBI Circular Reference: RBI/2015-16/390
Date of Notification: May 05, 2016
Applicable Entities: All Category - I Authorised Dealers and Authorised Banks

Background and Objective

RBI has observed that AD Banks are frequently coming across cases related to opening of accounts for multilateral organizations in foreign currency.

In line of the same, the aforementioned guideline lays down modalities as to how the foreign exchange business has to be conducted by the Authorised Persons with their customers/constituents.

The regulation seek to regulate deposits between a person resident in India and a person resident outside India and also make available finance to such residents through their foreign currency assets.

Key directives issued by RBI

The regulations prescribed in the guideline seeks to regulate deposits between a person resident in India and a person resident outside India:

The circular highlights some key definitions such as Deposit, Non-resident Indian (NRI), Person of Indian Origin (PIO) and Permissible currency.

In terms of Regulation 4 of the Deposit Regulations, no restriction under these regulations shall be applicable for opening of rupee/ foreign currency deposit accounts by certain persons as prescribed in the guideline.

In terms of Regulations 5 and 6 of the Deposit Regulations, a person resident outside India may open deposit accounts with Authorized Dealer/ authorized bank/Indian company under various schemes. Details of the schemes have been specified in the respective schedules. The major features are detailed in the guideline

Impact Assessment

The impact of the insertions done through the aforementioned circular against the Foreign Exchange Management (Deposit) Regulations, 2000 and other circulars as prescribed in the guideline is listed below:

- FEM (Deposit) Regulations, 2000 have been repealed and replaced by FEM (Deposit) Regulations, 2016, hence AD-Banks must align their internal policies with current regulations.
- RBI vide this new notification has now separately defined PIO (Person of Indian origin) which was earlier referred under NRI (Non-Resident Indian) category. Banks should update their policy to incorporate the same.
- AD Banks can now grant loans to PIOs/NRIs against the security of the funds held in NRE accounts without any limits, subject to any usual margin requirements.
- AD Banks should ensure that there is no premature withdrawal of deposits from NRE accounts in case a loan availed against such deposits.
- RBI has permitted AD Banks to open Special Non-Resident Rupee Account (SNRR account) to facilitate business interest in India to any person resident outside India. However, opening of account by individual/ entities of Pakistan/ Bangladesh nationality/ ownership will require prior approval of the RBI.
- Some of the salient features of the SNRR account which should be updated in the banks relevant policy is as below:
- The account should carry the nomenclature of the specific business against which the account is opened
  - The account would not earn any interest
  - All debits / credits must commensurate with the business operations only
  - The balances shall be eligible for repatriation
  - Transfers from NRO account to SNRR account are prohibited

Foreign Exchange Management (Deposit) Regulations, 2016

AD Banks can open, hold and maintain FCY account for any shipping or airline company to meet its local expenses. The credits in such accounts should be for the purpose of freight or passage fare collections in India or inward remittances through banking channels from its office outside India. Banks should update their policy to incorporate the change

RBI has permitted AD Banks to open and maintain non-interest bearing foreign currency account and an SNRR account for unincorporated joint ventures (UJV) of foreign companies/ entities, with Indian entities, executing a contract in India. Banks should ensure that the tenure for the account must be concurrent with the tenure of the contract

Establishment of Branch Office (BO)/ Liaison Office (LO)/ Project Office (PO) in India by foreign entities - procedural guidelines

RBI Circular Reference: RBI/2015-16/397
Date of Notification: May 12, 2016
Applicable Entities: All AD Category - I Banks

Background and Objective

With the aim to control/monitor the establishment of branch offices, liaison offices and project offices in India, the Regulator has, in exercise of it powers conferred upon by FEMA guidelines in this regard, outlined the precise eligibility, permissible activities, required forms and formalities, registration, approval, and other related procedures to be carried out.

This more specifically applies to non-residents as defined therein, and is aimed at reducing illegal and unauthorized foreign establishments. By permitting mainly Authorised Dealer I Banks, Insurance Companies, etc. to be the principle users of this regulation, the RBI has streamlined such activities to renowned entities over which it seemingly has control and can demand required information and correspondence as and when required

Key directives issued by RBI

The regulations prescribed in the guideline seeks to highlight provisions in relation to the procedure for a person resident outside India to open a branch office or a liaison office or a project office including the eligibility criteria, document submission requirements and the validity period for the same.

In terms of Section 7 and 8, the regulation highlights the permissible transactions that can be made from such accounts by the person resident outside India.

The circular also highlights the procedure around extension of validity of such accounts, closure of accounts and additionally provides a guidance note in relation to key aspects for the usage of such accounts.

Impact Assessment

AD Category-I banks have been entrusted the responsibility to conduct due diligence with respect to the following:

- AD Banks will be required to build system database/functionality to segregate sectors under 100% FDI. If the application does not fall under these sectors AD bank will be required to send the application for RBI approval
- AD Banks will be required to set parameters w.r.t net worth, profit etc.to establish the fact that the BO/LO in India has a financially sound track record. In case an applicant is a subsidiary of the AD Banks, a process may be put in place to accept a Letter of Comfort (LOC) from the parent company stating that parent / group company will fund the operations, if necessary
- AD Banks may be required to have an appropriate policy in place for dealing with these applications in conformity with the FEMA Regulations and Directions.
- AD Banks may be required to put a process in place to issue an approval letter to the non-resident entity for establishing BO/LO in India after performing such due diligence procedures as required by the RBI
- AD Banks may have to put a process in place to monitor the set-up of BO/PO/LOs to ensure that they are set-up in line with the request/ within six months from the date of the approval letter. The approval letter should have a clause to that extent.
- In case a request for extension is received before the expiry of the validity of the approval, AD Bank should bear in mind that the extension can be granted only for a period of 3 years from the date of expiry of the original approval / extension granted, and that the entire extension process has to be completed within one month from the date of from the receipt of the request. The AD Bank should also seek to obtain the necessary documentation from the account holders.
- AD bank needs to ensure that the transactions pertaining to the account are done in accordance with the stipulated guidelines

Establishment of Branch Office (BO)/ Liaison Office (LO)/ Project Office (PO) in India by foreign entities - procedural guidelines

- AD Category-I banks may ensure that a process is in place to prohibit extension in case of entities relating to the construction sector and NBFCs, beyond the permitted two years. Ideally, automatic disallowance for such extensions with the help of system-driven processes could be put in place.
- AD Banks may put a process in place to adhere to all the conditions for opening non-interest bearing foreign currency accounts.
- AD Banks are required to ensure appropriate police verification for applicants from designated countries (as specified in the regulation) and are required to submit the approval letter for these applicants to the RBI
- AD bank may allow transfer of assets from BOs/LOs/POs in line with the RBI regulations
- AD Bank to take cognizance of the guidance note prescribed by the RBI in Section 16 of the regulation

Repo / Reverse Repo Transactions with RBI

RBI Circular Reference: RBI/2015-16/403
Date of Notification: May 19, 2016
Applicable Entities: All RBI regulated eligible entities

Background and Objective

The Liquidity Adjustment Facility (LAF) is a monetary tool that allows banks to borrow / lend money to RBI. It is used by banks to manage day to day mismatches in liquidity. LAF involves repurchase (Repo) / reverse repurchase (Reverse Repo) agreements. A repo transaction allows banks to borrow funds from RBI to meet their short term needs by selling securities with a promise to buy back the securities at a predetermined rate. A reverse repo transaction allows banks to lend money to RBI by buying securities with the agreement to sell them back to the central bank in the future. The interest paid / earned for borrowing / lending funds is known as the repo interest.

Key directives issued by RBI

Please refer to our circular It has been decided i.e. October 3, 2016 to align accounting norms to be followed by market participants for repo / reverse repo transactions under LAF and Marginal Standing Facility (MSF) of RBI with the accounting guidelines prescribed for market repo transactions. Banks are further required to recognize the market value of collateral securities for calculating the haircut instead of face value while initiating LAF / MSF transactions. The securities acquired by banks from RBI under reverse repo transactions will be bestowed with SLR status. Banks may also carry out re-repo of securities acquired by banks under LAF reverse repo transactions.

Impact Assessment

- Change in the accounting guidelines will now require banks to recognize the essence of transactions under LAF as an obligation for a future date instead of outright sale / purchase of securities thereby making income recognition from LAF / MSF transactions more transparent. As a result, the securities that were being marked to market under HFT / AFS will now have to be accrued for to recognize interest income or expenditure.
- This will directly impact the banks' income statement thereby reducing volatility in P&L. Re-repo of securities acquired under LAF will further strengthen the G-Sec market and increase trading activity.
- Banks will be required to update their requisite policy to incorporate the changes suggested in the guideline.

Export Data Processing and Monitoring System (EDPMS) – Additional modules for caution listing of exporters, reporting of advance remittance for exports and migration of old XOS data

RBI Circular Reference: RBI/2015-16/414
Date of Notification: May 26, 2016
Applicable Entities: All Category – I Authorised Dealer Banks

Background and Objective

The Reserve Bank of India had launched a comprehensive IT- based system called Export Data Processing and Monitoring System (EDPMS) for better monitoring of export of goods and software and facilitating AD banks to report various returns through a single platform. The EDPMS had been operationalized with effect from February 28, 2014 and the same was be available to AD banks with effect from March 01, 2014. Through this circular, RBI intends to simplify the procedure for filing returns on a single platform and for better monitoring; to integrate the returns related to (a) handling of shipping bills for caution listed exporters; (b) delayed utilization of advances received for exports; and (c) exports outstanding with Export Data Processing and Monitoring System (EDPMS) which has been in operation since March 1, 2014.

Key directives issued by RBI

Attention of AD Category - I banks is invited to paragraph number C.2, C.15, C.20, C.24 and C.28 of Master Direction No.16 dated January 1, 2016 on Export of Goods and Services.

2. To simplify the procedure for filing returns on a single platform and for better monitoring, it has been decided to integrate the returns related to (a) handling of shipping bills for caution listed exporters; (b) delayed utilisation of advances received for exports; and (c) exports outstanding with Export Data Processing and Monitoring System (EDPMS) which has been in operation since March 1, 2014.

Impact Assessment

- AD category – I banks can access the updated list of caution listed exporters through EDPMS on daily basis. Hence, banks will now have to ensure that they refer to the updated caution list of exporters on a regular basis.
- RBI will caution / de-caution the exporters based on the recommendation of AD Category – I banks. AD may forward its findings to the concerned regional office of RBI recommending inclusion of the name of the exporter in the caution list. This will require the banks to report cases where the exporter is not traceable or not making any serious efforts for realization of export proceeds. Banks will have to develop a reporting mechanism in order to ensure adherence to the said directive of the RBI.
- This guideline requires banks to record advance remittances received for exports in EDPMS. Besides, banks will also be required to record old outstanding advances received. This would require banks to develop a recording mechanism to ensure that all advances have been captured in the EDPMS. Besides the reporting requirements, the first time implementation of the directive may have a significant impact as old outstanding advances are also to be captured in EDPMS along with the FIRC numbers in case of electronic FIRCs. This process of recording may involve banks updating their current SOPs to incorporate such changes.
- The quarterly return for reporting of unutilized advances will be discontinued and the reporting of overdue export advances will be required to be done on EDPMS. This change in the method of reporting will have to be provided for by the AD category banks in their SOPs..

Export Data Processing and Monitoring System (EDPMS) – Additional modules for caution listing of exporters, reporting of advance remittance for exports and migration of old XOS data

- Banks are now required to discontinue separate XOS reporting and report the same on EDPMS. The change in the reporting requirements will involve shift from manual reporting to automated reporting. Banks will have to bring in place a mechanism to ensure all the outstanding bills reported through XOS are updated on EDPMS and the same is closed as and when the amount is realized
- Banks will be required to adapt the new reporting system from June 15, 2016. The shift towards reporting on EDPMS will require banks to significantly alter their IT system / operating procedure. Besides, banks will have to ensure that every transaction is reported on EDPMS and processed only if they are appearing in EDPMS. The first time transition from to EDPMS reporting may involve a significant amount of data entry in order to ensure all previous transactions required to be reported have been updated on EDPMS correctly.

Other Key Guidelines issued by RBI in May 2016

S.No	Guidelines Reference	Date of Issue	Particulars	Impact
1	RBI/2015 - 2016/391	May 5, 2016	Discontinuation of Statements on Special Agriculture Credit Plan (SACP)	From April 2016, RBI has decided to discontinue the process where by Banks were required to submit half yearly statements on Statements on Special Agriculture Credit Plan (SACP) to FIDD. However, for the half year ended March 2016, banks may forward the statement to RBI.
2	RBI/2015 - 2016/392	May 5, 2016	Transactions in derivatives by regulated institutional entities on electronic platforms	RBI vide this guideline has permitted institutional entities, with effect from June 1, 2016, subject to the approval of their respective sectoral regulators to apply for membership of electronic trading platforms in IRS which have CCIL as the central counterparty for settlement Access to an electronic trading platform for IRS transactions for regulated institutional entities will increase participation in the OTC derivative market enabling CCIL as the central counterparty for settlement will reduce counterparty risk as well.
3	RBI/2015 - 2016/393	May 5, 2016	Currency Distribution & Exchange Scheme (CDES) for bank branches based on performance in rendering customer service to the members of public	On review of the scheme of Incentives & Penalties, RBI has decided to decided to segregate the scheme of incentives from penalties as also to revise certain incentives. Accordingly RBI has formulated a new “Currency Distribution & Exchange Scheme (CDES)” containing revised incentives. Details of the same are mentioned in the guidelines. performance based incentives will be paid as per the old guideline. Incentives for installation of machines have been restricted to Cash Recyclers & ATMs dispensing lower denomination notes, subject to certain caps on reimbursement of cost per machine and will be effective from May 5, 2016 Banks may take note of the same and update their incentives and penalties policies to incorporate the changes prescribed by RBI

S.No	Guidelines Reference	Date of Issue	Particulars	Impact
4	RBI/2015 - 2016/395	May 12, 2016	Foreign Exchange Management (Exports of Goods and Services) Regulations, 2015	Based on the revision to the Foreign Exchange Management (Exports of Goods and Services) Regulations, 2000 , following are the impact to Banks: • AD – Banks can now open an FCY account for a unit located in a Special Economic Zone (SEZ). • EDF form would be completely replacing the GR form used for declaration of export of Goods at Non-EDI ports. Hence AD-Banks must update their internal policies to include the changes prescribed by the RBI. • In case export of services to which none of the Forms specified in these Regulations apply, AD Banks are not required to source any declaration forms for services exported by Indian corporates. • AD Banks are now required to vet the contract for receipt of advance against exports • In case of change of buyer/consignee, AD – Banks must amend their internal policy to change the repatriation period from 12 months to 9 months. • AD-Banks are required to report any extension of time in realizing the export proceeds beyond stipulated period in the EDPMS system. • In case of set-off of export receivables against import payables, both the transactions of sale and purchase may be reported separately in R-Returns and in FETERS which was earlier only reported in R-Returns.
5	RBI/2015 - 2016/402	May 19, 2016	Rupee Drawing Arrangement - Submission of statement/returns under XBRL	RBI has now advised all the AD category - I banks to the submit statement E on total remittances received every quarter in the eXtensible Business Reporting Language (XBRL) system from the quarter ending June 2016. The reporting platform may be accessed at https://secweb.rbi.org.in/orfsxbrl/. To obtain user name and password to the system, banks are required to submit the duly filled in form, in Annex I of the guideline, through email on or before May 30, 2016.

S.No	Guidelines Reference	Date of Issue	Particulars	Impact
6	RBI/2015-2016/410	May 26, 2016	Merchant Acquisition for Card transactions	In order to encourage banks to expand card acceptance infrastructure to a wider segment of merchants across all geographical locations and considering the experience gained by the banks in merchant acquiring business, banks have been advised by the RBI to put in place their own Board approved policy on merchant acquisition
7	RBI/2015-2016/411	May 26, 2016	Memorandum of Procedure for channeling transactions through Asian Clearing Union (ACU)	Banks can now receive and pay for the purpose of funding or for repatriating the excess liquidity in the ACU Dollar and ACU Euro accounts as per revised minimum amount and the multiples, i.e., \$ 500 / € 500
8	RBI/2015-2016/412	May 26, 2016	Foreign Exchange Management Act, 1999 (FEMA) Foreign Exchange (Compounding Proceedings) Rules, 2000 (the Rules) - Compounding of Contraventions under FEMA, 1999	With a view to providing comfort to individuals and corporate community by minimizing transaction costs and the at same time taking a serious view of wilful, malafide and fraudulent transactions, the Reserve Bank was has empowered to compound all the contraventions of Foreign Exchange Management Act, 1999 (FEMA) except section 3(a) of FEMA. To ensure more transparency and greater disclosure, RBI has permitted public disclosure of compounding orders passed on or after June 1, 2016 on a monthly basis on the Bank's website in the format prescribed in the circular. Banks are required to publish on their website guidelines (annexed in the circular) pertaining to computation method on the amount imposed during compounding
9	RBI/2015-2016/413	May 26, 2016	ATMs - Security and Risk Mitigation Measures for Card Present (CP) Transactions	In order to ensure and enhance the safety and security of transactions at ATMs, banks are required to ensure that all their existing ATMs which are installed/operated by them are suitably configured so as to support processing of EMV Chip and PIN cards by September 30, 2017 In case of new ATMs being installed by the Banks, the same are required to be necessarily enabled for EMV and PIN processing


80
80

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