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Regulatory Impact Assessment

Banking

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Contents

Preface

With most of the PSU and Private bank reporting significantly high numbers of NPAs, it highlights the current economic stress scenario impacting the financial sector in India as a whole. Banks have been plagued with high number of NPAs for quite sometime and with economy still growing at the sub 7% level, significant policy changes by the government could be a reasonable measure to tackle the menace. Further, there is also a need of capital infusion by the government in the PSU banks, given the BASEL III capital requirements to be met in near future.

The government has been trying to meet its fiscal deficit target resulting in the announcement of the Gold Bonds Scheme by the Government of India has and publishing of the guidelines pertaining to the same by the RBI.

With the credit environment not worsening in the economy and rising cases of fraud, the RBI come up with guidelines related to fraud monitoring and reporting to put a curb on the increasing fraud cases. Under this guideline RBI has revised the limits of frauds reporting and also modified the format of the return to be submitted to it by banks. Further RBI also came up with the guidelines related to Non-Fund Based Facility to Non-constituent Borrowers of Bank as per which Banks will be required to formulate a loan policy for grant of non-fund based facility to those customers, who do not avail any fund based facility from any bank in India.

With the budget session of parliament kicking in, government needs pass some critical bills such as Aadhaar bill, new insolvency code, Real estate regulator bill etc., which would pave the way for investment in the economy and also keep check on the rising levels of NPA in the economy.

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

Non-Fund Based Facility to Non-constituent Borrowers of Bank

RBI Circular Reference: RBI/2015-16/281
Date of Notification: January 07, 2016
Applicable Entities: All Scheduled Commercial Banks (excluding RRBs)

Background and Objective

Based on the recommendation of the Working Group on Discounting of Bills by Banks, hitherto Banks were allowed to provide non-fund based facilities like opening of LCs, providing guarantees and acceptances and purchase / discount / negotiate bills under LCs in respect of genuine commercial and trade transactions only to their borrower constituents who have been sanctioned regular credit facilities by the banks. This restriction was imposed to prevent frauds, diversion of funds etc. in case bank sanctions "one-off" transaction facilities without assessment of credit needs of the borrowers on well-established credit norms. RBI has relaxed the above restriction as some customers who do not avail of any Fund based facility from any bank operating in India but were finding it difficult to avail Non-Fund based facilities like Letter of Credits (LCs), Bank Guarantees.

Key directives issued by RBI

Please refer to paragraph 2(iii) of our circular DBOD.Dir.BC.62/13.07.09/2002-03 dated January 24, 2003 on 'Discounting/Rediscounting of Bills by banks' advising banks not to extend any non-fund based facilities to non-constituents borrowers of the banks. The restriction was imposed to prevent frauds, diversion of funds etc. in case bank sanctions "one-off" transaction facilities without assessment of credit needs of the borrowers on well established credit norms.

The above restriction has led to the problems faced by those customers, who require Non-Fund based facilities like Letter of Credits (LCs), Bank Guarantees, but do not avail of any Fund based facility from any bank. In view of recent developments in strengthening the system of collection and maintenance of credit information, the above restrictions have been reviewed.

Accordingly, it has been decided that Scheduled Commercial Banks can grant non-fund based facilities including Partial Credit Enhancement (PCE) to those customers, who do not avail any fund based facility from any bank in India, subject to the following conditions:

a) **Board Approved Policy :** Banks shall formulate a comprehensive Board approved loan policy for grant of non-fund based facility to such borrowers.

b) **Verification of Customer credentials :** The banks shall ensure that the borrower has not availed any fund based facility from any bank operating in India. However, at the time of granting non-fund based facilities, banks shall obtain declaration from the customer about the non- fund based credit facilities already enjoyed by them from other banks.

c) **Credit Appraisal and due-diligence:** Banks shall undertake the same level of credit appraisal as has been laid down for fund based facilities.

d) **Compliance with Know Your Customer (KYC) Norms / Anti-Money Laundering (AML) Standards / Combating of Financing of Terrorism (CFT) / Obligation of banks under PMLA, 2002 :** The instructions/ guidelines on KYC/AML/ CFT applicable to banks, issued by RBI from time to time, shall be adhered to in respect of all such credit facility.

e) **Submission of Credit Information to CICs:** Credit information relating to grant of such facility shall mandatorily be furnished to the Credit Information Companies (specifically authorized by RBI). Such reporting shall be subject to the guidelines under Credit Information Companies (Regulation) Act, 2005.

Non-Fund Based Facility to Non-constituent Borrowers of Bank

f) **Exposure Norms:** Banks shall adhere to the exposure norms as prescribed by RBI from time to time.

As hitherto, banks are, however, prohibited from negotiating unrestricted LCs of non-constituents in terms of para 2.3.9 of our Master Circular RBI/2015-16/95. DBR.No.Dir.BC.10/13.03.00/2015-16 dated July 1, 2015 on Loans and Advances- Statutory and Other Restrictions. In cases where negotiation of bills drawn under LC is restricted to a particular bank and the beneficiary of the LC is not a constituent of that bank, the bank shall have the option to negotiate such LCs, subject to the condition that the proceeds are remitted to the regular banker of the beneficiary.

Impact Assessment

- Banks will be required to formulate a loan policy for grant of non-fund based facility to those customers, who do not avail any fund based facility from any bank in India. Banks will have to alter their internal policies and procedures to accommodate such changes.
- The Banks will be required to obtain a declaration from the customer to the effect that the borrower has not availed any fund based facility from any bank operating in India. For this, Banks will have to adopt increased diligence by undertaking the same level of credit appraisal that has been laid down for fund based facilities.
- Banks will have to ensure that while granting non-fund based facilities to Non-constituent borrowers, KYC/AML/ CFT guidelines are adhered to.
- Banks must ensure inclusion of submission of credit information to CIC's in case of granting non-fund based facilities to Non-constituent borrowers. This may require Banks to develop or modify existing reporting mechanism to ensure such information is submitted to CIC's.
- Also Banks modify their discounting policy to the extent that negotiation of bills drawn under LC is restricted to a particular bank wherein the beneficiary of the LC is not a constituent of that bank, the bank may negotiate such LCs, subject to the condition that the proceeds are remitted to the regular banker of the beneficiary.

Setting up of IFSC Banking Units (IBUs) – Permissible activities

RBI Circular Reference: RBI/2015-16/282
Date of Notification: January 07, 2016
Applicable Entities: All Scheduled Commercial Banks (excluding RRBs)

Background and Objective

In April 2015, RBI had issued guidelines to financial institutions set up in the International Financial Services Centres (IFSC). Government of India has already announced setting up of an IFSC in Gujarat namely Gujarat International Finance Tec-City (GIFT) in Gandhinagar, Gujarat.

RBI has issued this circular with a view to relaxing some provisions of the April 2015 circular for setting up of bank branches in International Financial Services Centres (IFSC).

Key directives issued by RBI

Please refer to our circular DBR.IBD.BC.14570/23.13.004/2014-15 dated April 01, 2015 setting out RBI directions relating to financial institutions set up in the International Financial Services Centres (IFSC). Based on the feedback and requests received from various stakeholders, certain provisions of the directions have been reviewed and are modified as follows:

In terms of paragraph No.2.6 (v) of Annex I and II of the aforesaid directions, the IBUs are not allowed to open any current or savings accounts. It has now been decided that the IBUs can open foreign currency current accounts of units operating in IFSCs and of non-resident institutional investors to facilitate their investment transactions. It is again clarified that the IBUs cannot raise liabilities from retail customers including high net worth individuals (HNIs). Also, no cheque facility will be available for holders of current accounts in the IBUs. All transactions through these accounts must be undertaken via bank transfers.

In terms of paragraph No. 2.6 (iv) of Annex I and II of the above mentioned directions, the IBUs can raise short-term liabilities from banks subject to a limit prescribed by RBI. On a review, it has been decided that RBI will not prescribe any limit for raising short-term liabilities from banks. However, the IBUs must maintain LCR as applicable to Indian banks on a stand alone basis and strictly follow the liquidity risk management guidelines issued by RBI to banks. Further, NSFR will also be applicable to the IBUs as and when it is applied to Indian banks.

With a view to providing greater flexibility to the IBUs in their business transactions, it has been decided that exposure ceiling for IBUs shall be 5 percent of the parent bank's Tier-I capital in case of a single borrower and 10 percent of parent bank's Tier-1 capital in the case of a borrower group.

Impact Assessment

- Banking units operating in International Financial Service Centres (IFSCs) can now open foreign currency current accounts of units operating in IFSCs and of non-resident institutional investors to facilitate their investment transactions
- The exposure ceiling of IBUs has been pegged at 5 per cent of the parent bank's Tier-I capital in case of a single borrower and 10 per cent in the case of a borrower group.
- RBI will not prescribe any limit for raising short-term liabilities from banks.
- IBUs need to maintain LCR as applicable to Indian banks on a stand alone basis and strictly follow the liquidity risk management guidelines issued by RBI to banks.
- NSFR will also be applicable to the IBUs as and when it is applied to Indian banks.

Credit information reporting in respect of Self Help Group (SHG) members

RBI Circular Reference: RBI/2015-2016/291
Date of Notification: January 14, 2016
Applicable Entities: All Scheduled Commercial Banks (including RRBs), All Credit Information Companies

Background and Objective

A review of the implementation of the aforesaid directions by the Reserve Bank of India (RBI) revealed that banks had not made a significant progress in this regard. The banks also pointed out a number of challenges in implementation of these directions and requested for greater clarity on their scope. Consequently, the RBI constituted a working group with members from within RBI, NABARD, banks and credit information companies (CICs), to study the implementation challenges and suggest measures to address them.

Key directives issued by RBI

Underscoring the importance of credit information reporting in respect of the SHG members for financial inclusion, credit decision of banks and Micro Finance Institutions (MFIs) and credit quality of the SHG loan portfolios, the working group has emphasized the need for putting in place the credit information reporting for SHG members sooner than later. Nonetheless, the group has suggested following a phased approach to the implementation of the RBI direction so as to ensure that the data quality is not compromised. This circular sets out the implementation requirements in the first two phases.

Impact Assessment

The structure of the credit information in respect of SHG members to be collected and reported by banks to the CICs is set out below:

1) Information to be collected by banks from individual SHG members where the total amount of loan to be attributed to or to be availed by the SHG member exceeds Rs.30,000/- (Table 1 of annexure)

2) Information to be collected by banks from individual SHG members where the total amount of loan to be attributed to or to be availed by the SHG member is upto Rs.30,000/- (Table 2 of annexure)

3) Information on all individual SHG members to be reported by banks to CICs (Table 3 of annexure)

4) Information on individual SHG members to be collected by banks at the time of opening of new Savings Bank Accounts of the SHG (Table 4 of annexure)

The credit and non-credit information collected from the SHGs have been designed both from the perspective of identification of the individual borrowers and supplementing the information requirements of banks, regulatory and government development agencies for the purpose of evaluating the flow of credit to various sub-segments of the SHG members and designing suitable credit penetration strategies keeping in view the socio-economic profile of the sub-segments.

Banks shall have to put in place the necessary IT infrastructure to monitor the credit data from SHGs and the NPA levels in the segment on a regular basis.

Sovereign Gold Bond 2015-2016

RBI Circular Reference: RBI2015-2016/290
Date of Notification: January 14, 2016
Applicable Entities: The Chairman and Managing Director, All Scheduled Commercial Banks (Excluding RRBS) ,Stock Holding Corporation of India Ltd. (SHCIL)

Background and Objective

Sovereign Gold Bonds Scheme is an indirect way of investing in Gold. Instead of buying Physical Gold, investors can invest in gold in a paper form through Sovereign Gold Bonds. The under-lying asset for these bonds is Gold. These bonds will track the price of gold, plus an extra interest earning on top of that.

The first tranche (issue) of the Gold Bonds scheme was launched in November 2015. The first tranche was open for subscription from November 05 to November 20, 2015. The issue had got a subscription for 915.95 kg gold amounting to Rs 246 crore.

The Reserve Bank of India, in consultation with the Government of India, has decided to issue second tranche of Sovereign Gold Bonds.

Applications for Second tranche of 'Sovereign Gold Bonds Scheme' will be accepted from 18th January to 22nd January, 2016. The Gold bonds will be issued on 8th February, 2016. The Bonds will be sold through banks, Stock Holding Corporation of India Limited (SHCIL) and designated post offices.

Key directives issued by RBI

1.Second tranche Subscription dates: January 18th to January 22nd of 2016

2.Date of Issue: February 8, 2016

3.Public Issue Price: The Reserve Bank has fixed the public issue price at Rs 2,600 per gram for the sovereign gold bonds. (The issue price for first tranche was at Rs 2,684 per gram)

4.Eligibility: The Bonds will be restricted for sale to resident Indian entities including individuals, HUFs, trusts, Universities and charitable institutions.

5.Denomination: The Bonds shall be denominated in units of one gram of gold and multiples thereof. Minimum investment in the Bonds shall be two grams with a maximum limit of subscription of five hundred grams per person per fiscal year (April – March)

6.Redemption:
i.The Bonds shall be repayable on the expiration of eight years from February 8, 2016, the date of issue of Gold bonds. Pre-mature redemption of the Bond is permitted from fifth year of the date of issue on the interest payment dates

ii.The redemption price shall be fixed in Indian Rupees on the basis of the previous week's (Monday – Friday) simple average closing price for gold of 999 purity, published by IBJA

7.Minimum Size: Minimum permissible investment will be 2 units (i.e. 2 grams of gold).

8.Maximum Limit: The maximum amount subscribed by an entity will not be more than 500 grams per person per fiscal year (April-March). A self-declaration to this effect will be obtained.

9.Interest rate: The investors will be compensated at a fixed rate of 2.75 per cent per annum payable semi-annually on the initial value of investment

10.Receiving Offices: Scheduled commercial banks (excluding RRBs), designated Post Offices (as may be notified) and Stock Holding Corporation of India Ltd (SHCIL) are authorized to receive applications for the Bonds either directly or through agents

11.Eligibility for Statutory Liquidity Ratio (SLR): The investment in the Bonds shall be eligible for SLR

12.KYC Documentation: Know-your-customer (KYC) norms will be the same as that for purchase of physical gold. KYC documents such as Voter ID, Aadhaar card/PAN or TAN /Passport will be required

Export of Goods and Services – Project Exports

RBI Circular Reference: RBI/2015-16/287
Date of Notification: January 14, 2016
Applicable Entities: All Category – I Authorised Dealer Banks

Background and Objective

As per Regulation 18 of Notification No. FEMA 23/2000-RB dated 3rd May 2000 viz. Foreign Exchange Management (Export of Goods and Services) Regulations, 2000 , export of goods or services on deferred payment terms or in execution of a turnkey project or a civil construction contract requires prior approval of the approving authority, which considers the proposal in accordance with the guidelines issued by the Reserve Bank from time to time. Further as per A.P. (DIR Series) Circular No.11 dated July 22, 2014, in terms of which the structure of Working Group (consisting of representatives from Exim Bank, ECGC & RBI), which had been permitted to consider project exports and deferred service exports proposals for contracts exceeding USD 100 Million in value has been dispensed with and AD banks / Exim Bank were permitted to consider awarding post-award approvals without any monetary limit and permit subsequent changes in the terms of post award approval within the relevant FEMA guidelines / regulations. Project and service exporters used to accordingly approach AD banks / Exim Bank based on their commercial judgment. Since as per directives of Government of India i) the 'OCCI' has been renamed as 'Project Export Promotion Council' (PEPC) and ii) civil construction contracts may include turnkey engineering contracts, process and engineering consultancy services and Project construction items (excluding steel & Cement) along with civil construction contracts, via this circular, RBI has issued directives to make the necessary changes in Memorandum of Instructions on Project and Service Exports (PEM) .

Key directives issued by RBI

The revised Memorandum of Instructions on Project and Service Exports (PEM) is published by the RBI is available at : https://rbidocs.rbi.org.in/rdocs/content/pdfs/PEM140116_I.pdf

Authorized Dealers may bring the revision in the Memorandum to the notice of their constituents concerned.

The directions contained in this circular have been issued under section 10(4) and 11(1) of the Foreign Exchange Management Act (FEMA), 1999 (42 of 1999) and are without prejudice to permissions / approvals, if any, required under any other law.

Applicability

I. Exporters who have orders pertaining to:

1) Supply contracts on deferred payment terms

2) turnkey/civil construction contracts abroad

3) Export of services in the area of management, technical consultancy

II. They require fund based or non-fund based support from banks to execute their contracts

III. Such deferred payment terms require approval from AD banks or EXIM bank

Impact Assessment

While granting approval for deferred credit to the above mentioned exporters, the AD Category banks are required to examine terms related to Period of credit, nature of security obtained, nature of escalation and vis major clauses of the contract, extent and viability of such contracts and so on.

A Working Group (consisting of representatives from Exim Bank, ECGC & RBI) which was previously set up for such examination of credit upto 100 million has been done away with. Instead AD Category banks and EXIM banks have been empowered to consider 'post award' approvals without any monetary limit.

Export of Goods and Services – Project Exports (contd.)

1.Thus, such banks will have to relook their Project Export Management System procedures to include post award approvals.

2.Sufficient due diligence to ensure the creditworthiness of such exporters for the sake of post award approvals is required.

3.Thresholds with respect to past performance, default rates, industry-wise risk analysis, etc. will required since AD banks will be providing approvals after the initial agreement between the exporter and importers have been made.

4.Also, sufficient security against such credit with respect to the risk rating of the exporter is required to be undertaken by the banks.

5.Counterparties with whom such trade is set to take place must undergo suitable analysis to eliminate risk of default completely. Such exports being undertaken for more than one year, counterparty analysis must include a ‘going concern’ check till the maturity of the contract.

Other Key Guidelines issued by RBI in January 2016

S. No	Guidelines Reference	Date of Issue	Particulars	Impact
1	RBI/2015-2016/285	January 14, 2016	Master Circular – Basel III Capital Regulations - Clarification	Coupon payments on PDIs from the revenue reserves is subject to the issuing bank meeting minimum regulatory requirement for CET 1, Tier 1 and Total Capital Ratios at all times and subject to requirement of capital buffer framework. Banks must ensure and indicate in the offer document that they have full discretion at all times to cancel distributions / payments of coupons in order to meet eligibility criteria for perpetual debt instruments.
2	RBI/2015-2016/286	January 14, 2016	Financial Literacy Centres (FLCs) – Revised Guidelines	The revised guidelines for Financial Literacy Centers of Lead Banks and the operational guidelines for the conduct of camps by FLCs and rural branches of banks have been prepared and are as follows also refer Annex I herewith along with the reporting mechanism to be followed by SLBC Convener banks/lead banks. FLCs are the building blocks or the basic units that initiate financial literacy activities at the ground level and banks should provide the minimum basic infrastructure and strengthen the existing eco-system. The FLC being a part of the lead bank office or a rural branch should have a separate room or space with a seating capacity of minimum 10 members to address walk-in customers. Banks should immediately put in place board-approved policies on the modalities for engagement or recruitment of Financial Literacy Counsellors in FLCs. Further elaborating on qualification parameters of counsellor, it is required for counsellor to have prior experience in banking/related fields, working knowledge of computers and local language. Banks should also provide fixed remuneration at market rates with incentives for better performance and also provide vehicular support. Also, as per the revised norms, banks should conduct a minimum one outdoor camp per month by each FLC and rural branch of banks
3	RBI/2015-2016/288	January 14, 2016	Section 23 of Banking Regulation Act, 1949 - Relaxations in Branch Authorisation Policy - Off Site ATMs	RBI has permitted banks to offer all their products and services through the ATM channels provided the technology permits the same, and adequate checks are put in place to prevent the channel from being misused to perpetuate frauds on the banks/other genuine customers. Banks should put relevant measures in place to prevent the channel from being misused and frauds from occurring and should update their policies in the same regard

S. No	Guidelines Reference	Date of Issue	Particulars	Impact
4	RBI/2015-2016/289	January 14, 2016	Direct Benefit Transfer (DBT) Scheme – Seeding of Aadhaar in Bank Accounts – Clarification	In view of the Supreme Court's interim orders dated August 11, 2015 and October 15, 2015 on usage of Aadhaar, it is hereby clarified that use of Aadhaar card and seeding of bank accounts with Aadhaar numbers is purely voluntary and it is not mandatory.
5	RBI/2015-2016/293	January 21, 2016	Incentive for improving service to non-chest branches under Linkage Scheme	RBI has decided that for chest holding branches the service charges to be levied on cash deposited by non-chest bank branches to be raised to ₹5 per packet of 100 pieces from the existing rate of ₹2 per packet.
6	RBI/2015-2016/294	January 21, 2016	Payment of Agency Commission on pension accounts	The Reserve Bank had directed banks that a pensioner’s account should not exceed more than 14 credit transactions in a calendar year for retirement and arrear payments. Earlier the agency banks were compensated at Rs 65 per transaction for handling pension computation, payment and related services on behalf of central and state governments. However, RBI said that it has come to its notice that banks are apportioning payment of arrears on account of dearness relief (DR) or delay in start of pension month wise, which is resulting in inflated agency commission claims. RBI also directed the banks that cases involving payment of arrears on account of late start/restart of pension qualifies as a single transaction for claiming of agency commission. Besides, some of the central government departments and state governments prefer to compute the pension figures on their own and pass them on to banks for payment, such transactions may be included under non-pension payments, on which agency commission is payable on a turnover basis as per the existing norms, currently at 5.5 paise per Rs 100.

S. No	Guidelines Reference	Date of Issue	Particulars	Impact
7	RBI/2015-16/295	January 21, 2016	Fraud Reporting and Monitoring	A Central Fraud Registry (CFR) has been operationalized with effect from January 20, 2016. **Revision of limits in reporting of Fraud Cases** Frauds of ₹ 0.1 million and above but below ₹ 50 million will be monitored by the respective Regional Office of RBI under whose jurisdiction the Head Office of the bank falls / Senior Supervisory Manager (SSM) of the bank. Frauds of ₹ 50 million and above will be monitored by CFMC, Bengaluru, and Flash reports are to be sent in fraud cases of ₹ 50 million and above to the CGM-i-C, DBS, CO with a copy to CFMC at Bengaluru as against the present limit of ₹ 10 million and above. Henceforth banks/FIs need not send the hard copies of the FMR-1 returns. Instead a monthly certificate should be submitted to the effect that soft copy of all the frauds of ₹ 0.1 million and above, to be reported to the RBI in a month, has been sent to email. The certificate should contain serially the fraud number, name of the party, amount involved and the date of sending the soft copy to RBI. The certificate may be sent to CFMC, Bengaluru with a copy to the respective Regional Office of RBI under whose jurisdiction the Head Office of the bank falls /SSM of the bank, within seven days from the end of the month as per the format as given in the notification.

S. No	Guidelines Reference	Date of Issue	Particulars	Impact
8	RBI/2015-2016/296	January 21, 2016	National Rural Livelihoods Mission (NRLM) – Aajeevika - Interest Subvention Scheme	Public sector banks, Cooperative banks, Regional rural banks, Rural Cooperative banks will have to lend credit to women SHG as per the specific guidelines for term loans and cash credit limit and report the SHG loan account information to Nodal Bank's portal as per the required technical specification in order to avail interest subvention
9	RBI/2015-2016/298	January 21, 2016	Sale of India Gold Coin (IGC)	- The designated banks as defined in the Master Direction on Gold Monetization Scheme, dated October 22, 2015, have been permitted to sell the IGCs minted by MMTC. The terms and conditions shall be as per the contract between the designated bank and MMTC - The current restriction on selling of imported gold coin by the banks will continue.

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