PwC's Banking Insights
June 2018

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Earlier this month, the Indian currency hit an all-time low of 69.10 against the dollar. The continued strengthening of the US dollar coupled with poor foreign investment inflows and concerns over rising oil prices has been instrumental in keeping the rupee under tremendous pressure. While a major basket of currencies of economies like the Philippines, Indonesia, South Korea, Taiwan and Singapore has witnessed a fall, the Indian rupee has emerged as the worst performer. Year-to-date outflow from the Indian bond market has also seen a steep rise, while other countries such as China, South Korea, Thailand and the Philippines have received net inflows to their debt market thus far.

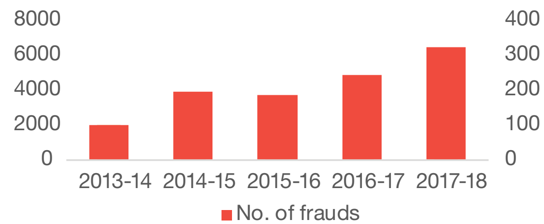
A reason for the same may be the RBI's fixation with inflation that has made it rather slow in reacting to changing global events, resulting in the underperformance of the currency and outflows from the debt market.

The hike in the repo rate early last month also caused the rupee to depreciate further. Further, the current scenario of foreign portfolio investor (FPI) outflows is also responsible for the weakening of the rupee. Overseas investors have already pulled out nearly 48,000 crore INR in the first half of 2018, following high crude oil prices and trade war worries. The FPI expectation is that the rupee may depreciate even further if the US Federal Reserve continues to hike rates. The increasing interest rates in the US do not augur well for the Indian economy and thus leads foreign investors to shift their focus to developed economies like the US. Further, with the challenges the Indian economy is facing, FPIs have chosen to shift focus outside India.

While economists may have predicted a further fall in rupee to 70 against the dollar, this is, however, unlikely as the Reserve Bank of India (RBI) will certainly not be comfortable with that expensive a rupee. The RBI has stated time and again that while it does not target any level of the domestic currency, it does intervene in the forex market to check the volatility of the currency.

Further, the recent instances of frauds hitting the banking sector have also forced the RBI to assess the operational risk framework for banks. Operational risks in banks have implications across the entire spectrum of risks and hence, materialisation of operational risk may be symptomatic of the weakness in the underlying risk management framework, internal controls, internal audits and governance mechanism. The data released by the RBI as part of the FSR indicates a substantial increase in the frauds being reported, as seen below.

Frauds reported (amount involved >= 1 lakh INR



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Further, the banking stability indicator also showed that deteriorating profitability as well as asset quality pose elevated risks to the banking sector stability. Weak profitability of scheduled commercial banks (SCBs) is also a concern as low profits can prevent banks from building cushions against unexpected losses and make them vulnerable to adverse shocks. There are several structural issues resulting in low profitability of SCBs, including high loan loss provisions, debt overhang, increasing costs and declining revenues. Profitability of weak banks on an average has been worsening since the last two fiscal years and more efforts will be needed to improve their resilience.

This issue covers an impact analysis of key regulations issued in the month of June 2018, including the regulations around encouraging formalisation of micro, small and medium enterprises (MSME) sector, review of margin requirements under liquidity adjustment facility (LAF) and marginal standing facility (MSF), monthly reporting through external commercial borrowing (ECB) 2 Return, interest rate options in India, spreading of market-to-market (MTM) losses, and creation of investment fluctuation reserve, a liberalised remittance scheme and control measures for ATMs in India. This issue also covers a special article on RBI's draft guidelines on the loan system for delivery of bank credit.

Impact assessment of regulatory changes in June 2018

Encouraging formalisation of MSME sector[1]

Circular reference:

RBI/2017-18/186 DBR.No.BP.
BC.108/21.04.048/2017-18
Dated 6 June 2018

Applicability:

All banks and NBFCs regulated by the Reserve Bank of India

Background:

The implementation of the Good and Services Tax (GST), created ripples in the micro, small and medium enterprises (MSME) sector, affecting liquidity of the entities. The quality of the loans extended by banks and non-banking financial companies (NBFCs) to these MSME borrowers also deteriorated, thereby creating pressure to qualify assets as non-performing due to overdues in payments. However, in line with the government's intention to support MSMEs, the RBI has rolled out some relief in the non-performing asset (NPA) classification for MSME borrowers. For the purpose of smooth transition and ease of formalisation, the MSMEs registered under GST will be aligned with the current asset classification norms in a phased manner.

Extract from the regulation:

Having regard to the input credit linkages and ancillary affiliations, it has now been decided to temporarily allow banks and NBFCs to classify their exposure, as per the 180 days past due criterion, to all MSMEs, including those not registered under GST, as a 'standard' asset, subject to the following conditions:

1. The aggregate exposure, including non-fund based facilities, of banks and NBFCs to the borrower does not exceed 250 million as on May 31, 2018.
2. The borrower's account was standard as on August 31, 2017.
3. The payments due from the borrower as on September 1, 2017 and falling due thereafter up to December 31, 2018 were/are paid not later than 180 days from their original due date.
4. In respect of dues payable by GST-registered MSMEs from January 1, 2019 onwards, the 180 days past due criterion shall be aligned to the extant income recognition and asset classification (IRAC) norms in a phased manner, as given in the Annex. However, for MSMEs that are not registered under GST as on December 31, 2018, the asset classification in respect of dues payable from January 1, 2019 onwards shall immediately revert to the extant IRAC norms.
5. The other terms and conditions of the circular dated February 07, 2018 remain unchanged.

1. https://www.rbi.org.in/Scripts/BS_CircularIndexDisplay.aspx?Id=11289

Annex

Period during which any payment falls due	Time permitted
1 September 2017 to 31 December 2018	180 days
1 January 2019 to 28 February 2019	150 days
1 March 2019 to 30 April 2019	120 days
1 May 2019 onwards	90 days

Impact assessment:

- Consequent to the regulation, banks and NBFCs are not allowed to classify their exposure, as per the 180-day criterion, to all MSMEs with credit facilities within the limit and including those that are not registered under GST. The alignment to the Income Recognition and Asset classification shall happen in a phased manner:
- For MSME accounts classified as standard as on 31 August 2017 and having payments due between 1 September 2017 and 31 December 2018, the asset would be classified as an NPA after 180 days.
- All the MSMEs registered under GST will be aligned to the IRAC norms in a phased manner from 1 January 2019. This allows the MSMEs to reap the benefits of the formalisation and ease in transition under GST.
- This has a positive impact on the banks as they are not overburdened with NPAs and can gradually classify and strengthen their monitoring process for NPAs of the MSME sector as per the RBI guidelines.
- For MSMEs not registered under GST by 31 December 2018, the asset classification for dues payable will align immediately with the 90-day norm and not in a phased manner.

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Review of margin requirements under the Liquidity Adjustment Facility and Marginal Standing Facility[2]

Circular reference:

RBI/2017-18/188 FMOD.MAOG
No.125/01.01.001/2017-18
Dated 6 June 2018

Applicability:

All Scheduled Commercial Banks (Excluding Regional Rural Banks),
Scheduled Urban Co-operative Banks and
Standalone Primary Dealers

Extract from the regulation:

Currently, the margin requirements under the Liquidity Adjustment Facility (Repo) and Marginal Standing Facility (MSF) in respect of Treasury Bills/Central Government dated securities (including Oil Bonds) and State Development Loans (SDLs) stand at 4 per cent and 6 per cent, respectively.

As announced in the **Second Bi-monthly Monetary Policy Statement for 2018-19**, it has now been decided to assign margin requirement on the basis of residual maturity of the collateral, i.e., the Treasury Bills, Central Government dated securities (including Oil Bonds) and State Development Loans (SDLs). Further, it has also been decided that the margin requirement for rated SDLs shall be 1 per cent lower than that of unrated SDLs for the same maturity bucket. The revised margin requirements for Central Government Securities and SDLs being offered as collateral would be as given in the table below:

Category of Collateral	Residual Maturity of Collateral				
	0-1 year	1-5 years	5-10 years	10-15 years	> 15 years
Treasury Bills and Central Government Dated Securities (including Oil Bonds)	0.5%	1%	2%	3%	4%
SDLs (unrated)	2.5%	3%	4%	5%	6%
SDLs (rated)	1.5%	2%	3%	4%	5%

2. https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11291&Mode=0

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The revised margin requirements would come into force with effect from August 1, 2018. All other terms and conditions of the current LAF (Repo) and MSF schemes will remain unchanged.

Impact assessment:

- The revised margin requirements based on residual maturity will lead to reduction in the amount of securities to be offered by banks for obtaining overnight funds from the RBI (e.g. for borrowing 100 crore INR from the RBI under MSF, banks used to provide government securities of 104 crore INR; under the revised requirement, banks will have to provide government securities of only 101 crore INR if the residual maturity is between 1–5 years and so on).
- The requirement will lead to an increase in available securities with banks and eventually, an increase in the borrowing capacity of banks.

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Continuation of Interest Subvention Scheme for short-term crop loans on interim basis during the year 2018-19[3]

Circular reference:

RBI/2017-18/190 FIDD.CO.FSD.BC.No.21/05.04.001/2017-18
Dated 7 June 2018

Applicability:

The Chairman/ Managing Director & CEOs
All Public & Private Sector Scheduled Commercial Banks

Background and objective:

- The Interest Subvention Scheme (ISS) was launched to ensure that farmers have easy access to agricultural credit. Credit is a critical input in achieving higher farm output. Institutional credit will help in delinking farmers from non-institutional sources of credit where they are compelled to borrow at usurious rates of interest.
- Normally, a farm loan attracts an interest rate of 9%. But the government has been providing interest subvention to make available short-term farm credit at an affordable rate and help boost farm output. Under the scheme, the government will continue to provide 2% interest subsidy to ensure farmers get a short-term farm loan of up to 3 lakh INR at an effective rate of 7%. An additional 3% interest subsidy will be given to those who repay on time. Thus, only 4% interest will be charged from prompt repayers.

3. https://www.rbi.org.in/Scripts/BS_CircularIndexDisplay.aspx?Id=11293

Extract from the regulation:

- As advised by the Government of India (GoI), as an interim measure, the Interest Subvention Scheme will be implemented in 2018-19 till further instructions are received, on the terms and conditions approved for the Scheme for 2017-18. All banks are, therefore, advised to take note and implement the Interest Subvention Scheme for 2018-19 accordingly.
- Further, as advised by GoI, from 2018-19 the ISS is being put on DBT mode on 'In kind/services' basis and not on 'In cash' basis and all loans processed in 2018-19 are required to be brought on ISS portal/DBT platform, once it is launched.
- In terms of Govt. of India letter F.No. 1-4/2017-Credit –I dated August 16, 2017, the Interest Subvention Scheme as Plan-Non plan categorization of schemes will be dispensed with. Accordingly, the Interest Subvention Scheme 2018-19 will be required to be settled as applicable in Plan Scheme viz. Scheduled Caste (SC), Scheduled Tribe (ST) and North East Region (NER) etc.
- Therefore, banks are required to capture category-wise data (General, Scheduled Caste (SC), Scheduled Tribes (ST), North Eastern Region (NER)-General, North Eastern Region (NER)-SC, North Eastern Region (NER)-ST) of beneficiaries under the Scheme for reporting of the same on ISS portal individual farmer wise to settle the claims arising from 2018-19 onwards. Till such time the DBT portal becomes functional banks are requested to submit their claims, category-wise as indicated above.
- The Bank in consultation with Govt. is working on the detailed modalities regarding categorisation of loans. Till such time the modalities are finalised, banks may obtain the category-wise data on self-declaration basis. There should however be no cap on the loans given under each category.

Impact assessment:

- The ISS provides short-term loans at reasonable rates and encourages farmers to repay on time and avoid default. These loans will give a boost to the agricultural produce of the country and contribute towards the growth of the economy.
- In recent times, banks have faced issues with a rise in NPAs while providing huge loans to corporates. With the latest amendments, the banks can gradually accommodate greater lending towards the agricultural sector and can reorient their operations while doing so to reduce NPAs.
- The RBI has advised banks to make Aadhaar linkage mandatory for availing short-term crop loans and also conducting strong due diligence of the borrower. By doing so, the existing system is enhanced and a gateway is built to attract only genuine farmers who wish to avail concessional crop loans.

Gold Monetization Scheme, 2015[4]

Circular reference:

RBI/2017-18/192 DBR.IBD.BC.109/23.67.001/2017-18
Dated 7 June 2018

Applicability:

All Scheduled Commercial Banks (Excluding Regional Rural Banks)

Background and objective:

In a country like India, where gold is considered to be a safe investment, Indians keep a significant portion of their wealth in the form of gold. Gold as such is an unproductive asset which yields very less returns as it typically sits idle in lockers or households. The Gold Monetization Scheme was introduced in 2015 which modified the then existing Gold Deposit Scheme and the Gold Metal Loan Scheme. This scheme was introduced to mobilise the gold held by households and economic institutions and to facilitate its use for other productive purposes.

Further, in June 2018, certain characteristics of this scheme, such as maturity, rate of interest and minimum lock-in period were improvised. The scheme allows a bank's customers to deposit their idle gold holdings for a fixed period in return for interest in the range of 2.25% to 2.50%. The main aim was to utilise the idle gold by putting it to productive use and generating returns for investors and further reducing the country's reliance on gold import.

4. https://www.rbi.org.in/Scripts/BS_CircularIndexDisplay.aspx?Id=11295

Extract from the regulation:

- The existing sub-paragraph 2.2.1 (ii) shall be amended to read as follows:

  "The short term deposits shall be treated as bank's on-balance sheet liability. These deposits will be made with the designated banks for a short period of 1-3 years (with a facility of roll over). Deposits can also be allowed for broken periods (e.g. 1 year 3 months; 2 years 4 months 5 days; etc.). The rate of interest payable in the case of deposits for maturities with broken periods shall be calculated as the sum of interest for the completed year plus interest for the number of remaining days at the rate of D/360*ARI"

  Where, ARI= Annual Rate of Interest
  D= Number of days

- The existing sub-paragraph 2.2.2 (iv) shall be amended to read as follows:

  "(iv) Other features of the Medium and Long Term Government Deposit (MLTGD) shall be as under:

(a) Maturity

The Medium Term Government Deposit (MTGD) can be made for 5-7 years and Long Term Government Deposit (LTGD) for 12-15 years or for such period as may be decided by the Central Government from time to time. Deposits can also be allowed for broken periods (e.g. 5 years 7 months; 13 years 4 months 15 days; etc.).

(b) Rate of interest:

The rate of interest on such deposits will be decided by Central Government and will be notified by Reserve Bank of India from time to time. The current rate of interest as notified by the Central Government are as under:

i) On medium term deposit – 2.25% p.a.

ii) On long term deposit – 2.50% p.a.

The rate of interest payable in the case of deposits for maturities with broken periods shall be calculated as the sum of interest for the complete year plus interest for the number of remaining days at the rate of D/360*ARI

Where, ARI= Annual Rate of Interest

D= Number of days

(c) The periodicity of interest payment

The periodicity of interest payment on these deposits is annual and shall be paid on 31st March every year. A depositor will have an option to receive payment of simple interest annually or cumulative interest at the time of maturity, in which case it will be compounded annually. This option shall be exercised at the time of deposit.

(d) Minimum lock-in period

A Medium Term Government Deposit (MTGD) is allowed to be withdrawn any time after 3 years and a Long Term Government Deposit (LTGD) after 5 years.

2 https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11186&Mode=0

(e) Interest on premature withdrawal

The amount payable to the depositor on premature withdrawal after lock-in period shall be calculated as a sum of (A) and (B), as indicated below:

(A) Actual market value of the gold deposit on the day of withdrawal

(B) Interest payable on the value of the gold at the time of deposit as under."

Type of deposit	Lock-in period (years)	Actual period for which the deposit has run (years)	
		>3 and < 5	≥5 and < 7
MTGD	3	Applicable rate for MTGD at the time of deposit - 0.375%	Applicable rate for MTGD at the time of deposit - 0.25%

Type of deposit	Lock-in period (years)	Actual period for which the deposit has run (years)		
		>3 and < 5	≥ 7 and < 12	≥12 and < 15
LTGD	5	Applicable rate for MTGD at the time of deposit - 0.25%	Applicable rate for LTGD at the time of deposit - 0.375%	Applicable rate for LTGD at the time of deposit - 0.25%

3 https://www.rbi.org.in/Scripts/BS_CircularIndexDisplay.aspx?Id=11185

- The existing sub-paragraph 2.2.2 (v) shall be amended as under:

  "In the case of MLTGD, the redemption of principal at maturity shall, at the option of the depositor, be either in Indian Rupee equivalent of the value of deposited gold at the time of redemption, or in gold. However, any pre-mature redemption of MLTGD shall be only in INR. Where the redemption of the deposit is in gold, an administrative charge at a rate of 0.2% of the notional redemption amount in terms of INR shall be collected from the depositor. However, the interest accrued on MLTGD shall be calculated with reference to the value of gold in terms of Indian Rupees at the time of deposit and will be paid only in cash."

- The existing sub-paragraph 2.2.2 (ix) shall be amended as under:

  "Central Government has decided that with effect from November 5, 2016, designated banks will be paid handling charges (including gold purity testing, refining, transportation, storage and any other relevant costs) for MLTGD at a flat rate of 1.5% and commission at the rate of 1% of the rupee equivalent of the amount of gold mobilized under the scheme until further notice."

- The Reserve Bank of India Master Direction No.DBR.IBD. No.45/23.67.003/ 2015-16 dated October 22, 2015 on Gold Monetization Scheme, 2015 has been updated incorporating the above changes.

Impact assessment:

- This is an opportunity provided to the customers of the banks to deposit their physical gold with a minimum lock-in period of 3 years and to avail interest on it instead of the yellow metal lying idle in their households or lockers and yielding no interest.
- After a small success derived from the Gold Monetization Scheme of 2015, the government has made certain changes to the scheme to reduce the demand for physical gold and shift a part of the gold imported every year for investment purposes into financial savings through gold bonds. This revamp will enable more individuals to open a hassle-free gold deposit account and contribute towards the shift.
- The government will be formulating a comprehensive gold policy to develop gold as an asset class. They will also soon establish a consumer-friendly and trade-efficient system of regulated gold exchanges in the country. With these initiatives, the dependency on physical gold should come down considerably and there should be a significant growth in the wealth of investors, providing a boost to the country's economy.

4 https://www.rbi.org.in/scripts/NotificationUser.aspx?Id=11183&Mode=0

External Commercial Borrowings (ECBs) – Monthly reporting through ECB 2 Return[5]

Circular reference:

RBI/2017-18/193
A. P. (DIR Series) Circular No. 29
Dated 7 June 2018

Applicability:

All Category I Authorised Dealer Banks

Extract from the regulation:

Attention of Authorized Dealer Category I (AD Category I) banks is invited to Annex III of Part V of Master Direction No.18/2015-16 dated January 01, 2016 on Reporting under Foreign Exchange Management Act, 1999, as amended from time to time.

- It has been decided to capture the details of the hedges for ECBs through a simplified format of ECB 2 Return. Part E of the Return, accordingly, is modified so as to include only standard information on hedged/unhedged ECB exposure. Details of hedging in Part E.1 of the Return and foreign exchange earnings and expenditure in Part E.2 of the Return should be furnished in additive format. Further, for reporting in respect of natural hedge, provisions contained in paragraph 2 (iii) of A.P. (DIR Series) Circular No. 15 dated November 07, 2016 should be followed.
- Revised monthly reporting format of ECB 2 Return would be applicable from month-end June 2018

Impact assessment:

- Banks will have to bring the contents of this circular to the notice of their constituents and customers.
- Banks will have to ensure timely submission of ECB 2 Return as any lapse at the time of reporting through this return and/or failure to adhere to the timeline of its submission and/ or any lapse at the time of reporting through Form 83 is a contravention of the provisions of the Foreign Exchange Management Act, 1999 (42 of 1999).

5 https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11296&Mode=0

Foreign Investment in India - Reporting in Single Master Form[6]

Circular reference:

RBI/2017-18/194 A.P (DIR Series) Circular No.30
Dated 7 June 2018

Applicability:

All Category – I Authorised Dealer Banks

Background and objective:

In alliance with the Indian government's efforts to strengthen foreign investment and ease of doing business in India, the RBI issued a circular on 7 June 2018 with the aim of simplifying reporting under the Foreign Exchange and Management Act (FEMA), 1999.

Extract from the regulation:

Reserve Bank, with the objective of integrating the present reporting structures of various types of foreign investment in India, will introduce a Single Master Form (SMF). The SMF would be filed online.

1. SMF would provide a facility for reporting total foreign investment in an Indian entity {as defined in Foreign Exchange Management (Transfer or issue of security by a person resident outside India) Regulations 2017, dated November 7, 2017}, as also investment by persons resident outside India in an Investment Vehicle.
2. Prior to the implementation of the SMF, Reserve Bank would provide an interface to the Indian entities, to input the data on total foreign investment in a specified format. The interface will be available on RBI website https://firms.rbi.org.in from June 28, 2018 to July 12, 2018. Indian entities not complying with this pre-requisite will not be able to receive foreign investment (including indirect foreign investment) and will be non-compliant with Foreign Exchange Management Act, 1999 and regulations made thereunder.
3. The entities may be in readiness with the requirements to be provided in the Entity Master. The final form, when hosted, will be available in the Master Direction-Reporting under FEMA, 1999.
4. AD Category-I banks may bring the contents of this circular to the notice of their customers / constituents concerned.
5. The directions contained in this circular have been issued under sections 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.

6 https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11297&Mode=0

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Impact assessment:

The SMF for reporting of various investments under FEMA (transfer or issue of security by a person resident outside India) Regulations is a welcome move by the RBI as it would ensure much-needed uniformity in terms of various kinds of reporting that Indian entities are obligated to do every time they receive foreign capital.

However, considering the current practices of e-Biz filing through the AD Bank and the varying timelines provided in the regulations for relevant reporting, the said transition and process of incorporation might bring in a few practical challenges.

Along with Indian entities, foreign investors who have invested in such entities should also be familiar with such reporting and the associated timeline to ensure that they are allowed to invest further capital into their subsidiaries or other investment companies in India.

Interest rate options in India[7]

Circular reference:

RBI/2017-18/198 FMRD.DIRD.9 /14.01.020/2017-18
Dated 14 June 2018

Applicability:

All Eligible market participants

Background and objective:

The RBI has permitted the use of interest rate swaptions in rupees to hedge interest rate risk. Swaptions are basically options that give the holder the right but not the obligation to enter into an underlying swap. A swap is nothing but a derivative contract through which two parties can exchange financial instruments.

Extract from the regulation:

As announced in the first bi-monthly Monetary Policy Statement 2018-19 dated April 05, 2018, it has now been decided to permit Interest Rate Swaptions in Rupees so as to enable better timing flexibility for the market participants seeking to hedge their interest rate risk.

- The Reserve Bank of India has accordingly issued a Notification No.FMRD.DIRD.8/2018 dated June 14, 2018 enabling the introduction of swaptions.
- These directions have been issued under Section 45 W of Chapter III D of the Reserve Bank of India Act, 1934.
- The Interest Rate Options (Reserve Bank) Directions, 2018 will supersede the Interest Rate Options (Reserve Bank) Directions, 2016 dated December 28, 2016.
- These directions shall come into force with effect from June 15, 2018.

7 https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11302&Mode=0

Impact assessment:

- This move, which will deepen the domestic derivative market, is a big positive for participants looking to hedge their interest rate risk.
- Banks will have to ensure all over-the-counter (OTC) transactions executed among market makers shall be reported within 30 minutes of the trade to the Trade Repository of the Clearing Corporation of India Limited (CCIL) since interest rate options are permitted on exchanges authorised by SEBI as well as in the OTC market.
- As regards the settlement of these transactions, OTC transactions executed among market makers shall be settled bilaterally or through any clearing arrangement approved by the RBI for the purpose. Settlement basis and other market conventions for OTC transactions in interest rate options will be specified by Fixed Income Money Market and Derivatives Association (FIMMDA) in consultation with market participants.

Investment by Foreign Portfolio Investors (FPI) in Debt - Review[8]

Circular reference:

RBI/2017-18/199 A.P. (DIR Series) Circular No. 31
Dated 15 June 2018

Applicability:

All Authorised Persons

Background and objective:

The RBI in consultation with the Securities Exchange Board of India (SEBI) revised the limits of debt investments by FPIs at the end of April 2018 by issuing 2 notifications—one on 27 April 2018 and the other on 1 May 2018—with the objective of simplifying the process of investments into debt instruments by FPIs in India. Based on the feedback received from custodians, FPIs and other stakeholders, it has been decided to provide some operational flexibility as well as a transition path for FPIs and custodians to adapt to these regulations.

Extract from the regulation:

- In supercession of the directions contained in **AP (DIR Series) Circular No. 24 dated April 27, 2018 and AP (DIR Series) Circular No. 26 dated May 1, 2018**, the following directions are issued:

  (a) Definitions

  – Short-term investments" are defined as investments with residual maturity up to one year;
  – The term "related FPIs" shall mean 'investor group' as defined in Regulation 23(3) of SEBI (Foreign Portfolio Investors) Regulations, 2014;
  – The term "entities related to the corporate" shall have the meaning assigned to 'related party' in section 2(76) (viii) of the Companies Act, 2013. Issuers that are owned or controlled by the Government of India or State Governments shall be exempted from the definition of "entities related to the corporate";
  – "SRs" mean Security Receipts issued by Asset Reconstruction Companies;
  – "Multilateral Financial Institutions" mean FPIs which are Multilateral Financial Institutions in which Government of India is a member.

  (b) Revision of minimum residual maturity requirement

  – In terms of A.P. (DIR Series) Circular No. 13 dated July 23, 2014, FPIs were required to invest in Government bonds with a minimum residual maturity of three years. Henceforth, FPIs are permitted to invest in Central Government securities (G-secs), including in Treasury Bills, and State Development Loans (SDLs) without any minimum residual maturity requirement, subject to the condition that short-term investments by an FPI under either category shall not exceed 20% of the total investment of that FPI in that category.
  – In terms of A.P. (DIR Series) Circular No. 71 dated February 03, 2015, FPIs were required to invest in corporate bonds with a minimum residual

8 https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11303&Mode=0

maturity of three years. Henceforth, FPIs are permitted to invest in corporate bonds with minimum residual maturity of above one year, subject to the condition that short-term investments in corporate bonds by an FPI shall not exceed 20% of the total investment of that FPI in corporate bonds. These stipulations would not apply to investments in SRs by FPIs.

– The requirement that short-term investments shall not exceed 20% of total investment by an FPI in any category applies on an end-of-day basis. At the end of any day, all investments with residual maturity of up to one year will be reckoned for the 20% limit.
– Short-term investments by an FPI may exceed 20% of total investments, only if the short-term investments consist entirely of investments made on or before April 27, 2018; that is, short-term investments do not include any investment made after April 27, 2018.

(c) Revision of security-wise limit

– The cap on aggregate FPI investments in any Central Government security, currently at 20% of the outstanding stock of that security stands revised to 30% of the outstanding stock of that security.

(d) Online monitoring of investments in G-sec and SDL Categories

– FPIs were permitted to invest in G-secs till the limit utilization reaches 90%, after which the auction mechanism was triggered for allocation of the remaining limit. With Clearing Corporation of India Ltd. (CCIL) commencing online monitoring of utilization of G-sec limits, the auction mechanism has been discontinued with effect from June 1, 2018.
– Utilization of FPI investment limits in G-secs and SDLs is being monitored online by the Clearing Corporation of India Ltd. (CCIL). Any transactions in breach of the investment limit in each category will not be accepted. Custodians and FPIs may note that any transaction that leads to a breach of the investment limit for the category will need to be reversed.
– Upon sale/redemption of securities (in G-secs and SDLs), the concerned FPIs may reinvest within a period of two working days from the date of sale/redemption (including date of sale/redemption). If the reinvestment is not made within that time period, reinvestment shall be subject to availability of limits for that category.
– The primary responsibility of complying with all limits for investment in G-secs and SDLs viz., investment utilization limit, security wise limit in G-secs, concentration limit and minimum residual maturity requirement shall lie with the FPIs and custodians.
– CCIL will also monitor the various other limits and caps for FPI investment in G-secs and SDLs. The operationalization of the same will be notified by CCIL.

(e) Concentration limit

Investment by any FPI (including investments by related FPIs), in each of the three categories of debt, viz., G-secs, SDLs and corporate debt securities, shall be subject to the following concentration limits:

- Long-term FPIs: 15% of prevailing investment limit for that category.
- Other FPIs: 10% of prevailing investment limit for that category.
- In case an FPI has investments (INV0) in excess of the concentration limit on the effective date (date on which these concentration limits come into existence), it will be allowed the following relaxations, subject to availability of overall category limits, as a one-time measure:
  - In case an FPI has investments (INV0) in excess of the concentration limit on the effective date, it will be allowed to undertake additional investments such that its portfolio size at the end of any day (INVt) does not exceed INV0 plus 2.5% of investment limit for the category on the effective date. Once (INVt) falls below the prevailing concentration limit for the category, the FPI shall be free to make investments up to the applicable concentration limit.
  - In case an FPI has investments (INV0) within the concentration limit, but in excess of 7.5% (12.5% in case of FPIs in the 'Long-term' sub-category) of the investment limit for the category on the effective date, that FPI shall be allowed to undertake additional investments such that its portfolio size at the end of any day (INVt) does not exceed INV0 plus 2.5% of the investment limit for the category on the effective date. Once INVt falls below the prevailing concentration limit for the category, the FPI shall be free to make investments up to the applicable concentration limit.
  - All other FPIs will be allowed to invest up to the applicable concentration limit.

(f) Single/Group investor-wise limits in corporate bonds
FPI investment in corporate bonds shall be subject to the following requirements:

- Investment by any FPI, including investments by related FPIs, shall not exceed 50% of any issue of a corporate bond. In case an FPI, including related FPIs, has invested in more than 50% of any single issue, it shall not make further investments in that issue until this stipulation is met.
- No FPI shall have an exposure of more than 20% of its corporate bond portfolio to a single corporate (including exposure to entities related to the corporate).
  - In case an FPI has, as on April 27, 2018, exposure in excess of 20% to any corporate (including exposure to entities related to the corporate), it shall not make further investments in that corporate until this requirement is met.
  - 'New' investments (i.e., investments made after April 27, 2018) by FPIs would be exempted from this requirement till March 31, 2019. These 'new' investments will, however, have to comply with this requirement thereafter.
  - To facilitate newly registered FPIs to build up a diversified portfolio, FPIs registering after April 27, 2018 are permitted to comply with this requirement by March 31, 2019, or six months from the date of registration, whichever is later.
  - The requirements of single/group investor-wise limits in corporate bonds would not be applicable to investments by Multilateral Financial Institutions and investments by FPIs in SRs.

(g) Pipeline investments in corporate bonds

- Investment transactions by FPIs in corporate bonds that were under process but had not materialized as on April 27, 2018 (pipeline investments), shall be exempt from the requirements specified in paragraphs 4(f)(i) and 4(f)(ii) of this circular, subject to the custodian of the FPI reasonably satisfying itself that:
  - The major parameters such as price/rate, tenor and amount of the investment have been agreed upon between the FPI and the issuer on or before April 27, 2018;
  - The actual investment will commence by December 31, 2018; and
  - The investment is in conformity with the extant regulations governing FPI investments in corporate bonds prior to April 27, 2018.

(ii) Custodians may, based on their assessment of adherence to the above conditions, permit, or not permit, as the case may be, pipeline investments by FPIs without reference to the Reserve Bank.

(h) Other changes

No FPI shall invest in partly paid debt instruments.

These directions would be applicable with immediate effect. The directions contained in AP (DIR Series) Circular No. 24 dated April 27, 2018 and AP (DIR Series) Circular No. 26 dated May 1, 2018 stand withdrawn.

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

Impact assessment:

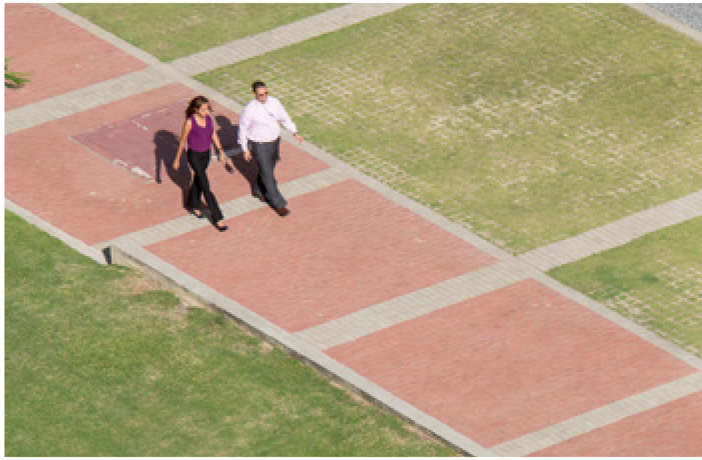
The primary responsibility of complying with monitoring the corporate debt investment limits is with the FPIs on whose behalf depositories will monitor the investment limits. As the depositories are maintaining the data on investor group level, depositories shall monitor the investments at the investor group level. Custodians shall be responsible for monitoring their own clients.

At the time of monitoring the corporate debt investment limits, depositories shall identify the FPIs in breach and inform their respective custodians, who, in turn, shall advise their FPI clients on doing the needful. For the monitoring of G-secs/SDLs utilisation limits by the CCIL, depositories shall share the investor group data with the RBI and CCIL on a monthly basis.

The stock exchanges and depositories shall put in place the necessary systems for the online monitoring of the investment limits.

Appropriate action may be initiated against FPIs who are not in compliance with the requirements specified here.

The increase in limits on FPI investments along with the easing of minimum residual maturity from 3 years to 1 year should encourage FPI investment into India's corporate debt markets. Additionally, introducing exposure limits could impact the entry of new FPI entrants into the market.



Prudential Norms for Classification, Valuation and Operation of Investment Portfolio by Banks – Spreading of MTM losses and creation of Investment Fluctuation Reserve (IFR)[9]

Circular reference:

RBI/2017-18/200 DBR.No.BP.BC.113/21.04.048/2017-18
Dated 15 June 2018

Applicability:

All Scheduled Commercial Banks & Small Finance Banks (SFBs)

Extract from the regulation:

1. In view of the continuing rise in the yields on Government Securities, as also the inadequacy of time to build investment fluctuation reserve (IFR) for many banks, it has been decided to grant banks the option to spread provisioning for their mark to market (MTM) losses on all investments held in available for sale (AFS) and held for trading (HFT) for the quarter ending June 30, 2018 as well. The provisioning required may be spread equally over up to four quarters, commencing with the quarter ending June 30, 2018.
2. Banks that utilise the above option shall make suitable disclosures in their notes to accounts/ quarterly results providing details of -
   - the provisions made for depreciation of the investment portfolio for the quarter ending June 2018 and
   - the balance required to be made in the remaining quarters.
3. It may be noted that the other requirements prescribed in the above circular, including creation of IFR, remain in force.

Impact assessment:

1. In the wake of the continuing rise in government securities' yields, the RBI has eased the provisioning norms for banks yet again. In April 2018, the RBI had allowed banks to spread provisioning for mark-to-market losses on investments held in AFS and HFT for third and fourth quarters of 2017–18.
2. As per this guideline, banks have been given an option to spread provisioning for their MTM losses on all investments held in AFS and HFT for the quarter ending 30 June 2018 as well. If the banks avail this option, they will have to spread the provision over up to four quarters, commencing with the quarter ending 30 June 2018.
3. Further, they will have to make suitable disclosures in their notes to accounts/quarterly results and provide details of –

9 https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11304&Mode=0

- the provisions made for depreciation of the investment portfolio for the quarter ending June 2018
- the balance required to be made in the remaining quarters

4. Banks will continue to transfer an amount not less than the lower of the following to the IFR –
   - net profit on sale of investments during the year
   - net profit for the year less mandatory appropriations until the amount of IFR is at least 2% percent of the HFT and AFS portfolio on a continuing basis. Where feasible, this should be achieved within a period of 3 years.
5. Banks may, at their discretion, draw down the balance available in IFR in excess of 2% of their HFT and AFS portfolio for credit to the balance of profit/loss as disclosed in the profit and loss account at the end of any accounting year.
6. In its erstwhile guidelines on the same subject, the RBI had advised banks to create an IFR with effect from the year 2018–19. The IFR shall continue to be eligible for inclusion in tier 2 capital.

Basel III Framework on Liquidity Standards - Liquidity Coverage Ratio (LCR), Liquidity Risk Monitoring Tools and LCR Disclosure Standards[10]

Circular reference:

RBI/2017-18/201
DBR.BP.BC.No.114/21.04.098/2017-18
Dated 15 June 2018

Applicability:

All Scheduled Commercial Banks (excluding RRBs) & Small Finance Banks (SFBs)

Background:

The liquidity coverage ratio (LCR) aims at ensuring the availability of a set level of high-quality liquid assets (HQLAs), which can be readily converted into cash to meet the liquidity needs for 30 days under a significantly severe liquidity stress scenario. The LCR was introduced by the RBI, starting with a minimum requirement of 60% from 1 January 2015 and reaching minimum 100% on 1 January 2019. The LCR is a ratio of stock of HQLAs to the total net cash outflows over the next 30 calendar days. Liquid assets comprise high-quality assets that can be readily sold or used as collateral to obtain funds in a range of stress scenarios. There are two categories of assets which can be included in the stock of HQLAs, viz. Level 1 and Level 2 assets.

Extract from the regulation:

1. The regulation reads as below:
2. Presently, the assets allowed as the Level 1 High Quality Liquid Assets (HQLAs) for the purpose of computing the LCR of banks, inter alia, include (a) Government securities in excess of the minimum SLR requirement and, (b) within the mandatory SLR requirement, (i) Government securities to the extent allowed by RBI under Marginal Standing Facility (MSF) [presently 2 per cent of the bank's NDTL] and (ii) under Facility to Avail Liquidity for Liquidity Coverage Ratio (FALLCR) [presently 9 per cent of the bank's NDTL].
3. It has been decided to permit banks, with effect from the date of this circular, to reckon Government securities held by them up to another 2 per cent of their NDTL, under FALLCR within the mandatory SLR requirement, as Level 1 HQLA for the purpose of computing their LCR. Hence, the carve-out from SLR, under FALLCR will now be 11 per cent, taking the total carve out from SLR available to banks to 13 per cent of their NDTL.
4. For the purpose of LCR, banks shall continue to value such government securities reckoned as HQLA at an amount not greater than their current market value (irrespective of the category under which the security is held, i.e., HTM, AFS or HFT).

10 https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11305&Mode=0

Impact assessment:

1. This is a move in order to support banks' compliance with the 100% LCR requirement by January 2019.
2. For computation of HQLA, banks can now consider G-secs held by them under the FALLCR up to 13% of their net demand and time liabilities (NDTL).
3. The valuation of such securities should not be more than the current market value.
4. This action would help the banks in measuring their ability to absorb economic shocks through maintenance of the LCR.

Priority Sector Lending – Targets and Classification[11]

Circular reference:

RBI/2017-18/203 FIDD.CO.Plan.BC.22/04.09.01/2017-18
Dated 19 June 2018

Applicability:

All Scheduled Commercial Banks (Excluding Regional Rural Banks and Small Finance Banks)

Background:

Several changes have been made to priority sector lending (PSL) norms by the RBI in recent times. The changes included new categories of PSL and separate targets for weaker sections. Priority sector non-achievement is assessed on a quarterly average basis at the end of the respective year instead of an annual basis, as done at present. Banks which face a shortfall in lending to priority sectors/ subsectors at the necessary targets are required to contribute to the funds of the Rural Infrastructure Development Fund (RIDF) and similar funds set up with the National Bank of Agriculture and Rural Development (NABARD)/Small Industries Development Bank of India (SIDBI)/National Housing Bank (NHB). In a boost to affordable housing under the Pradhan Mantri Awas Yojana (PMAY), the RBI raised the housing loan limits under PSL for economically weaker sections and lower income groups.

Extract from the regulation:

1. In terms of the above Master Direction, loans to individuals up to ₹ 28 lakh in metropolitan centres (with population of ten lakh and above) and ₹ 20 lakh in other centres, are eligible to be classified under priority sector, provided that the cost of dwelling unit does not exceed ₹ 35 lakh and ₹ 25 lakh, respectively.
2. With a view to bringing convergence of the Priority Sector Lending guidelines for housing loans with the Affordable Housing Scheme, and to give a fillip to low-cost housing for the Economically Weaker Sections and Low Income Groups, the housing loan limits for eligibility under priority sector lending will be revised to ₹ 35 lakh in metropolitan centres (with population of ten lakh and above), and ₹ 25 lakh in other centres, provided the overall cost of the dwelling unit in the metropolitan centre and at other centres does not exceed ₹ 45 lakh and ₹ 30 lakh, respectively.
3. Furthermore, the existing family income limit of ₹ 2 lakh per annum, prescribed under Para 10.4 of the above Master Direction, for loans to housing projects exclusively for the purpose of construction of houses for Economically Weaker Sections (EWS) and Low Income Groups (LIG), is revised to ₹ 3 lakh per annum for EWS and ₹ 6 lakh per annum for LIG, in alignment with the income criteria specified under the Pradhan Mantri Awas Yojana.

11 https://www.rbi.org.in/Scripts/BS_CircularIndexDisplay.aspx?Id=11308

4. All other terms and conditions specified under the Master Direction shall remain unchanged. Master Direction ibid, is being updated simultaneously to reflect the above changes.
5. The revised guidelines shall come into effect from the date of the Circular.

Impact assessment:

1. Even as the PSL requirements are eased in the housing segment, banks need to take measures to minimise their credit risk and also monitor NPAs arising from low-ticket buckets of the housing loan market. Banks must strengthen their screening and monitoring process and follow up in respect of lending to this segment in particular.
2. The RBI is closely monitoring the housing segment and may even consider tightening of the loan-to-value (LTV) ratios or an increase in the risk weights in such categories when necessary.
3. Banks should try to orient their operations and expand their lending to support the growth of affordable housing across India.

Liberalised Remittance Scheme – Harmonisation of Data and Definitions[12]

Circular reference:

RBI/2017-18/204
A.P. (DIR Series) Circular No. 32
Dated 19 June 2018

Applicability:

All Category - I Authorised Dealer Banks

Background and objective:

The Reserve Bank of India (RBI) has tightened the norms for remitting funds abroad under the Liberalised Remittance Scheme (LRS), making PAN mandatory for anyone using this scheme. Through the LRS, it was noticed that many Indian citizens and traders were remitting funds to bet on stocks and properties, breaching specified limits under the scheme. Going forward, banks will be using the PAN of the remitter as a unique identifier to aggregate the remitter-wise data.

Impact assessment:

- All Category-I Authorised Dealer Banks will have to ensure that PAN is furnished for making all remittances under the LRS.
- This will have a positive impact as it will ensure that money being transferred abroad is tax-paid money and will also serve as a monitoring mechanism for these remittances to ensure that individuals adhere to the limits prescribed.

Extract from the regulation:

- It has been decided that furnishing of Permanent Account Number (PAN), which hitherto was not to be insisted upon while putting through permissible current account transactions of up to USD 25,000, shall now be mandatory for making all remittances under Liberalised Remittance Scheme (LRS).
- Further, in the context of remittances allowed under LRS for maintenance of close relatives, it has been decided, in consultation with Government, to align the definition of 'relative' with the definition given in Companies Act, 2013 instead of Companies Act, 1956.

12 https://www.rbi.org.in/Scripts/BS_CircularIndexDisplay.aspx?Id=11309

Control measures for ATMs – Timeline for compliance[13]

Circular reference:

DBS(CO).CSITE/BC.5/31.01.015/2017-18
Dated 21 June 2018

Applicability:

All Scheduled Commercial Banks (excluding Regional Rural Banks)

All Small Finance Banks and Payment Banks

White-Label ATM Operators

Background and objective:

- A circular DBS.CO/CSITE/BC.8074/31.01.015/2016-17 dated 17 April 2017 was issued to banks highlighting concerns about ATMs running on Windows XP and/or other unsupported operating systems.
- Banks were advised to put in place, with immediate effect, suitable controls enumerated in the illustrative list of controls as part of the advisory issued.
- The slow progress on the part of banks in addressing these issues, the vulnerability arising from banks' ATMs operating on an unsupported version of the operating system and non-implementation of other security measures have affected the interests of banks' customers adversely as well as affected their image. There has been a spate of ATM frauds in recent times which underlines the RBI's concern in the area of ATM security.

Synopsis of the regulation:

- In order to address the issues around ATM security in a time-bound manner, banks and white-label ATM operators are advised to initiate immediate action in this regard and implement the following control measures as per the prescribed timelines:

13 https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11311&Mode=0

Sr. No.	Control measures for ATMs	To be completed by
a.	Implement security measures such as BIOS password, disabling USB ports, disabling auto-run facility, applying the latest patches of operating system and other software, terminal security solution, time-based admin access, etc.	August 2018
b.	Implement anti-skimming and whitelisting solution	March 2019
c.	Upgrade all the ATMs with supported versions of operating system. Such upgrades shall be carried out in a phased manner to ensure that in respect of the existing ATMs running on unsupported versions of operating system. i. Not less than 25% of them shall be upgraded by ii. Not less than 50% of them shall be upgraded by iii. Not less than 75% of them shall be upgraded by iv. All of them shall be upgraded by	 September 2018 December 2018 March 20W19 June 2019

- A copy of this circular may be placed before the board of directors at its ensuing meeting, along with the proposed action plan for implementation of these measures. A copy of the board-approved compliance/action plan in respect of the aforesaid control measures may be sent to the RBI latest by 31 July 2018. The progress made in implementation of these measure should be closely monitored to ensure meeting the prescribed timelines. As the implementation of the foregoing control measures would also require field visit(s) to the ATMs, banks should plan and implement these measures in an optimal manner.
- It may be noted that any deficiency in timely and effective compliance with the instructions contained in this circular may invite appropriate supervisory enforcement action under the applicable provisions of the Banking Regulation Act, 1949, and/or the Payment and Settlement Systems Act, 2007

Impact assessment:

- This new mandate will ensure banks invest in ATM upgrades to clean up the banking sector's ATMs and safeguard banks' reputation.
- Upgrading ATMs will also help blunt jackpotting or cash-out attacks, in which attackers infect machines with malware and instruct them to dispense all of their cash. Such attacks are much more difficult to block if machines are running outdated operating systems with well-known vulnerabilities.
- Banks will need to place before their board of directors a copy of this circular along with the proposed action plan for implementation of these measures. A copy of the board-approved compliance/action plan in respect of the aforesaid control measures would need to be sent to the RBI by 31 July 2018.
- Further, banks would need to closely monitor the progress made in the implementation of these measures to ensure meeting the prescribed timelines. As the implementation of the foregoing control measures would also require field visit(s) to the ATMs, banks would need to plan and implement these measures in an optimal manner.
- Any deficiency in timely and effective compliance with the instructions contained in the said circular may invite appropriate supervisory enforcement action under the applicable provisions of the Banking Regulation Act, 1949, and/or the Payment and Settlement Systems Act, 2007.

Other notifications in June 2018

Circular ref. no.	Name of the circular	Brief instructions
RBI/2017-2018/185 dated 6 June 2018[14]	Change in bank rate	• As announced in the Second Bi-Monthly Monetary Policy Statement 2018-19 dated 6 June 2018, the bank rate stands adjusted by 25 basis points from 6.25% to 6.50% with effect from the said date. • Further, penal interest rates on the shortfall in reserve requirements, which are specifically linked to the bank rate, also stand revised as follows: – Bank rate plus 3.0 percentage points (9.50%) or – Bank rate plus 5.0 percentage points (11.50%)
RBI/2017-2018/184 dated 6 June 2018[15]	Marginal Standing Facility	• As announced in the Second Bi-monthly Monetary Policy Statement 2018-19 dated 6 June 2018, the policy repo rate under the liquidity adjustment facility (LAF) stands adjusted by 25 basis points from 6.0% to 6.25% with effect from the said date. • Consequent to the change in the repo rate, the marginal standing facility (MSF) rate stands adjusted to 6.50% with effect from the said date. • All other terms and conditions of the extant MSF scheme will remain unchanged.

14 https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11288&Mode=0
15 https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11287&Mode=0

Circular ref. no.	Name of the circular	Brief instructions
RBI/2017-2018/183 dated 6 June 2018[16]	Liquidity Adjustment Facility – Repo and Reverse Repo Rates	• As announced in the Second Bi-monthly Monetary Policy Statement 2018-19 dated 6 June 2018, the policy repo rate under the LAF stands adjusted by 25 basis points from 6.0% to 6.25% with effect from the said date. • Consequent to the change in the repo rate, the reverse repo rate under the LAF stands adjusted to 6.00% with effect from the said date. • All other terms and conditions of the extant LAF scheme will remain unchanged.
RBI/2017-2018/205 dated 21 June 2018[17]	Customer Service provided by agency banks	• The RBI has been receiving complaints from various quarters that pensioners are not being treated with due consideration by bank officials, specifically old pensioners, when they come to the branches for pension-related transactions. • Thus, the RBI has directed all agency banks disbursing pension to provide considerate and sympathetic customer service to pensioners, especially those pensioners who are of old age.
RBI/2017-2018/191 dated 7 June 2018[18]	Banking Regulation Act, 1949 – Section 26A Depositor Education and Awareness Fund Scheme, 2014 – Operational Guidelines - Payment of Interest	• The RBI vide the circular DBOD.No.DEA Fund Cell. BC.126/30.01.002/2013-14 dated 26 June 2014 on the captioned subject had specified that the rate of interest payable by banks to the depositors/ claimants on the unclaimed interest bearing deposit amount transferred to the DEA Fund shall be 4% simple interest per annum until further notice. • The rate of interest has since been reviewed and it has been decided that the rate of interest payable by banks to the depositors/claimants on the unclaimed interest bearing deposit amount transferred to the fund shall be 3.5% simple interest per annum with effect from 1 July 2018. The settlement of all claims received by the banks on or after 1 July 2018 will be at this rate, until further notice. • The other contents of the circular dated 26 June 2014 remain unchanged.

16 https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11286&Mode=0
17 https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11310&Mode=0
18 https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11294&Mode=0

Special article: Draft guidelines on Loan System for Delivery of Bank Credit[19]

Circular reference:

RBI/2017-18/ DBR.No.BP.BC....../21.04.048/2017-18
Dated 11 June 2018

Applicability:

All Scheduled Commercial Banks (Excluding Local Area Banks and Regional Rural Banks), Small Finance Banks

Background and objective:

- The financial sector of India has been evolving exponentially through various reforms and different regimes over the past two decades. However, with current financial vulnerabilities and frauds, the RBI has decided to tighten the guidelines for delivery of fund-based working capital to large borrowers in order to promote better credit discipline amongst the working capital borrowers. As per the RBI's FSR in December 2017, more than four-fifths of the NPAs arise on account of default of large borrowers. The recent draft guidelines introduce a minimum level of 'loan component' on fund-based working capital loans and also a compulsory credit conversion factor (CCF) of 20% for the undrawn cash credit availed by borrowers. These guidelines are applicable to larger borrowers having an aggregate fund-based working capital limit of 150 crore INR and above from the banking system.
- Currently, once a borrower avails a working capital loan, the funds may be utilised and drawn down anytime during the year, which provides greater flexibility to the borrower with respect to withdrawing funds. The lending institutions are not required to charge any commitment fee and also have the flexibility and the right to cancel any undrawn limits unconditionally without accommodating a certain portion of capital for the same. Working capital finance is provided by way of various fund and non-fund based methods such as cash credit, working capital demand loans, bank guarantees and letter of credit. The most popular method of working capital financing is through cash credit as it is a revolving facility. The RBI recognises the regulatory challenges that come along with cash credit in terms of perpetual rollovers, ineffective transmission of liquidity management and hampering of financial growth and smooth transmission of monetary policy. The asset liability mismatches arising out of the burden of cash credit have affected the operations of banks.

19 https://rbi.org.in/scripts/bs_viewcontent.aspx?Id=3495

- With the proposed changes, the RBI aims to enhance the delivery of credit in the banking system and also improve the quality of the loans. According to the draft guidelines, for a working capital loan availed by any large borrower, a minimum level of 'loan component' of 40% will be applicable from 1 October 2018, which will further be revised to 60% with effect from 1 April 2019. This 40% is calculated on the sanctioned working capital loan and ad-hoc credit facilities. Beyond this, drawings from the sanctioned loan may be in the form of cash credit facility. In the case of a consortium, it is necessary for all the lenders to ensure that the loan component meets the necessary requirements. The guidelines propose to allow the fixation of tenor of the working capital demand loans by banks in consultation with the borrowers with a threshold of seven days. Being subject to the extant IRAC norms, the repayment and rollover of the loan component may be up to the discretion of banks or consortia to allow instalments or bullet repayment. The draft also states the introduction of CCF that converts an off balance sheet exposure to its credit exposure equivalent. Risk weights with a CCF of 20% for the unutilised portion of working capital loan availed by large borrowers will be applicable effect from 1 April 2019.

Extract from the regulation:

With a view to enhance credit discipline among the larger borrowers enjoying working capital facility from the banking system, it is proposed to modify the system for delivery of bank credit for such borrowers as follows:

1. Minimum level of 'loan component' and Effective date

   In respect of borrowers having aggregate fund based working capital limit of Rs. 150 crore and above from the banking system, a minimum level of 'loan component' of 40 percent shall be effective from October 1, 2018. Accordingly, for such borrowers, the outstanding 'loan component' must be equal to at least 40 percent of the sanctioned fund based working capital limit, including ad hoc credit facilities. Hence, for such borrowers, drawings up to 40 percent of the total fund based working capital limits shall only be allowed from the 'loan component'. Drawings in excess of the minimum 'loan component' threshold may be allowed in the form of cash credit facility.

2. Sharing of Working Capital Finance

   The ground rules for sharing of cash credit and loan components may be laid down by the consortium, wherever formed, subject to guidelines on bifurcation as stated in paragraph 1 above. All lenders in the consortium shall be individually and severally responsible to make sure that at the aggregate level, the 'loan component' meets the above mentioned requirements. Under Multiple Banking Arrangements (MBAs), each bank shall ensure adherence to these guidelines at individual bank level.

3. Amount and tenor of the loan

   The amount and tenor of the Working Capital Demand Loan (WCDL) may be fixed by banks in consultation with the borrowers, subject to the tenor being not less than seven days. Banks may decide to split the loan component with different maturity periods as per the need of the borrowers.

4. Repayment/Renewal/Rollover of Loan Component

   Banks/consortia/syndicates will have the discretion to stipulate repayment of the 'loan component' in instalments or by way of a "bullet" repayment, subject to IRAC norms.

5. Risk weights for undrawn portion of cash credit limits

   Effective from April 1, 2019, the undrawn portion of cash credit/ overdraft limits sanctioned to the aforesaid large borrowers, irrespective of whether unconditionally cancellable or not, shall attract a credit conversion factor of 20 percent.

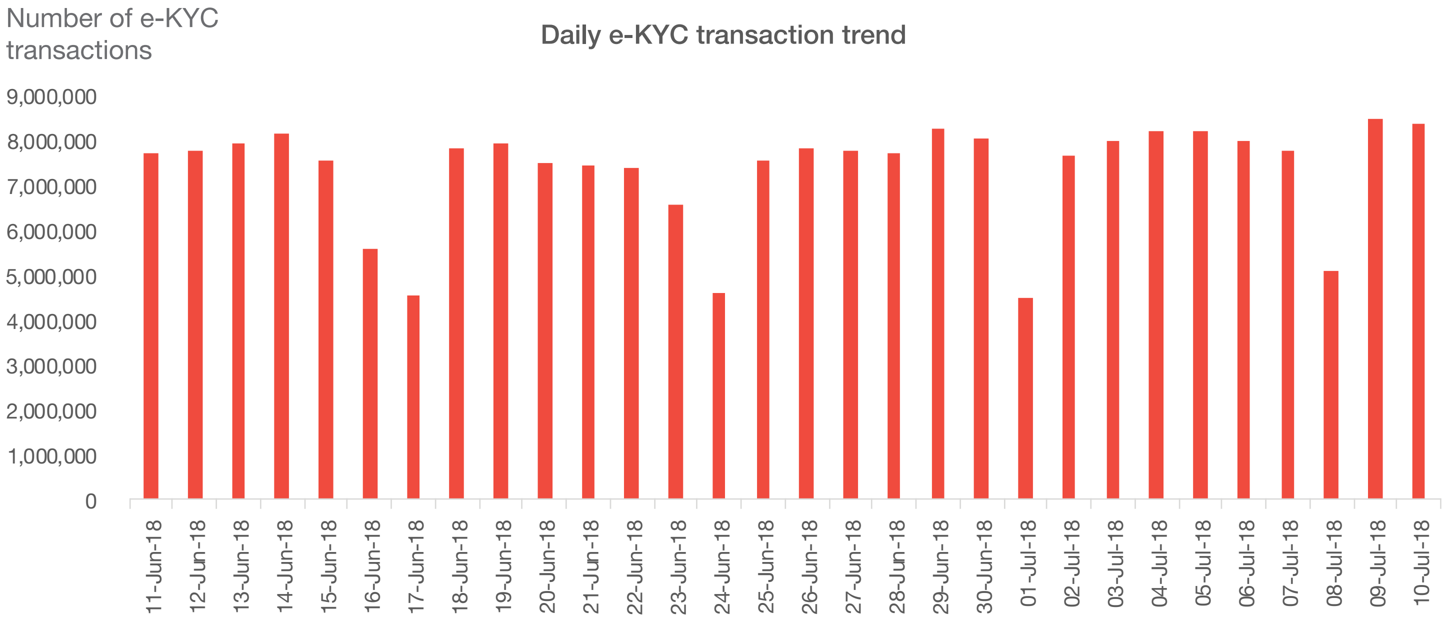
6. The 40 percent loan component will be revised to 60 percent, with effect from April 1, 2019.

Impact assessment:

- There is an overall positive impact from the implementation of the stated guidelines. The challenges faced by banks in terms of asset liability mismatches and poor liquidity management have led to higher operational risks. Some of the impacts are:
  - It will lead to better intra-day fund management and short-term liquidity in the banking system which will help in achieving better asset liability management (ALM).
  - Adherence to the RBI regulatory requirements and also improve banks' regulatory reporting.
  - This also urges the borrowers towards better liquidity planning and imparts greater credit discipline.
  - With the new guidelines, lenders will be required to assess the working capital requirements of a borrower more accurately and this improves the internal monitoring processes of banks.
  - The development of term money will take place due to the utilisation of working capital demand loans for specified durations.

Aadhaar-based e-KYC

Considering the increasing importance and dependence on Aadhaar-based e-KYC, we bring to you a dashboard depicting volumes of daily e-KYC transactions.



Source: UIDAI

Preface
Impact assessment of regulatory changes in June 2018
Other notifications in June 2018
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