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Banking Regulation Global Guide – India

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Legislation and Regulatory Authorities

Legislation

1. What is the legal framework for banking regulation?

The legal framework for banking regulation in India is as follows:

- Banking is primarily governed by the Banking Regulation Act, 1949 (Banking Regulation Act). The Banking Regulation Act provides the legal framework for the regulation and supervision of banks in India. It also (among others) provides for licensing and management of banks, and regulates banks' operations.
- The Reserve Bank of India (RBI), the country's central bank and the main regulatory body for banking, was established by the Reserve Bank of India Act, 1934 (RBI Act). The RBI Act empowers RBI to issue directives, rules, regulations, instructions and guidelines to banks and financial institutions on various banking and financial sector related topics.
- The RBI also regulates foreign exchange and current and capital account transactions by the authority granted to it by the Foreign Exchange Management Act, 1999 (FEMA).

Other supplemental legislation which apply to banking are the:

- Recovery of Debts Due to Banks and Financial Institutions Act, 1993.
- Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.
- Payment and Settlement Systems Act, 2007.
- Credit Information Companies (Regulation) Act, 2005.
- Deposit Insurance and Credit Guarantee Corporation Act, 1961.

2. What are the regulatory authorities for banking regulation in your jurisdiction? What is the role of the central bank in banking regulation?

Lead Bank Regulators

The RBI is the country's central bank and banking regulator. The RBI has extensive authority to oversee the financial industry including:

- Establishing standards for setting up and licensing banks (including international bank branches or subsidiaries in India).
- Corporate governance.
- Prudential standards.
- Requirements for product and service structuring.

The RBI issues circulars and guidelines from time to time for regulating the banking sector in India. The RBI's main goal is to provide comprehensive supervision of the financial sector, which includes commercial banks, financial institutions and non-banking financing companies (NBFCs).

Other Authorities

Apart from the RBI, banks are also governed by the Ministry of Finance, part of the central government. The central government has the authority to make laws relating to the banking sector and to direct the RBI on public policy and other matters relating to regulating banks and financial institutions.

Central Bank

See above, Lead Bank Regulators

Others

The Directorate of Enforcement has responsibility for:

- Enforcing the provisions of the Prevention of Money Laundering Act, 2002 by conducting investigations to trace the assets derived from the proceeds of crime.
- Conducting investigations into suspected contraventions of foreign exchange laws and regulations.
- Adjudicating and imposing penalties on individuals and institutions that have contravened the above laws and regulations.

Bank Licences

3. What licence(s) must conduct banking services and what activities do they cover?

To conduct banking business in India, entities must obtain a licence from the RBI under the provisions of the Banking Regulation Act.

The two primary categories of licence are the:

- Universal bank licence.
- Differentiated bank licence. This includes licences for payment banks and small finance banks, each with its own eligibility criteria and guidelines.

In addition to providing core banking services such as accepting deposits and providing loans, banks in India engage in a range of ancillary business including:

- Securitisation.
- Trade finance.
- Execution of trusts.
- Guarantee and indemnity business.

Entities proposing to deal in foreign exchange must obtain a separate authorised dealer licence granted under the FEMA. Authorised dealers are responsible for overseeing and facilitating foreign exchange and cross-border transactions.

4. What is the application process for bank licences?

Application

Any banking company wishing to commence banking business in India must obtain a licence from the RBI (section 22, Banking Regulation Act). The application is prepared and submitted by the applicant to the RBI under one of the following categories:

- **Private bank**. The application must be made in the format specified by the RBI (see *rbidocs.rbi.org.in/rdocs/Forms/PDFs/TBRCRE010115_FIII7723074542564D7C8A847B2966E38B07.PDF*) and submitted to the Chief General Manger, Department of Banking Operations and Development, Reserve Bank of India, Central Office, 12th Floor, Central Office Building, Mumbai 400 001. An up-to-date copy of the memorandum and articles of association must be submitted with the application.
- **Foreign bank (branch)**. The application must be made in the specified format (see *rbidocs.rbi.org.in/rdocs/Forms/PDFs/RBIGRANTLICENCE20022018.PDF*) and submitted to the Principal Chief General Manager, Reserve Bank of India, Department of Banking Operations and Development, International Banking Division, 13th floor, Central Office Building, Shahid Bhagat Singh Marg, Mumbai 400 001.

  The following documents must be submitted with the application:

  - copies of memorandum and articles of association or similar documents;
  - last three years' financial statements;
  - certificate from supervisory authority that the applicant bank is duly authorised as a bank, is of good standing and it is under their consolidated supervision;
  - copy of the approval/authorisation given by the home country supervisor/regulator permitting to open a branch office in India; and
  - approval letter from the bank's board.
- **Foreign bank (wholly owned subsidiary) (WOS)**. The application must be made in the specified format (see *rbidocs.rbi.org.in/rdocs/Forms/PDFs/TBRCRE010115_FIII7723074542564D7C8A847B2966E38B07.PDF*) and submitted to the Principal Chief General Manager, Reserve Bank of India, Department of Banking Operations and Development, International Banking Division, 13th floor, Central Office Building, Shahid Bhagat Singh Marg, Mumbai 400 001. An up-to-date copy of the memorandum and articles of association must be submitted with the application.

  RBI has not prescribed any fees for submitting applications.

Requirements

The main requirements for obtaining a private bank licence are the following (among others):

- **Eligible promoters**. The following are eligible to establish a bank in India:
  - professional individuals or entities/groups in the private sector; and
  - NBFCs which are resident in India and/or owned and controlled by residents.

- **Fit and proper criteria**. The promoter should have a sound financial record of at least ten years, proper business credentials and integrity. The RBI can seek feedback on the applicant from other regulators and enforcement and investigative agencies.
- **Corporate structure**. Where an individual promoter or entity is part of a larger group of companies, the bank must be set up only through a non-operative financial holding company (NOFHC). The NOFHC must be the holding company for the bank as well as for all the other financial services entities of the group.

  Other conditions will apply to the corporate structure of NOFHC under various company laws and regulations.
- **Minimum voting/equity capital requirements for banks and shareholdings by the NOFHC**. The initial minimum paid-up voting equity capital for a bank is INR5 billion. The NOFHC must initially hold at least 40% of the bank's paid up voting equity capital which will be locked in for five years and which will gradually be decreased to 15% within 15 years.

  The bank must list its shares on the stock exchanges within three years of the start of business by the bank.
- **Foreign shareholding in the bank**. The aggregate non-resident shareholding in the new bank must not exceed 49% for the first five years after which it will be in accordance the extant policy.
- **Board composition**. The board must have a majority of independent directors.

  (Banking Regulations Act; RBI Guidelines for "on tap" Licensing of Universal Banks in the Private Sector.)

The decision to issue a banking licence to any applicant is at the sole discretion of the RBI.

Foreign Applicants

Foreign banks are currently allowed to set up business in India through either a branch or a WOS.

All foreign banks that meet one or more of the below criteria must apply for a WOS licence only:

- Banks incorporated in a jurisdiction having legislation giving a preferential claim to deposits of the home country in winding up proceedings.
- Banks that do not have adequate disclosure requirements in their home jurisdiction.
- Banks with complex structures.
- Banks which are not widely held.
- Banks which do not satisfy the RBI on the adequacy of their supervisory arrangements (including disclosure arrangements) and market discipline in the country of their incorporation.
- Banks which for any other reason the RBI considers need a subsidiary form of presence in India.

- A foreign bank which has set up as a branch in India since August 2010 and is considered by the RBI as being systemically important. "Systematically important" means its assets in Indian books (on balance sheet and credit equivalent of off-balance sheet items) are 0.25% or more of the total assets (inclusive of credit equivalent of off-balance sheet items) of all scheduled commercial banks in India on 31 March of the preceding financial year.

  A foreign bank that does not meet the above criteria can apply to set up either as a branch or as a WOS.

The main requirements for foreign applicants to obtain a banking licence as a branch are:

- Assigned capital of USD25 million must in place at the time of opening the first branch in India.
- An annual branch expansion plan must be submitted as the branch expansion of foreign banks will be considered in view of India's commitments with the WTO.
- The track record of the foreign bank's and its groups' compliance and functioning in the global markets must be assessed. Reports from home country supervisors can be sought, where necessary.
- Due consideration is given to the bilateral and diplomatic relations between India and the home country.

The main requirements for by foreign applicants to obtain a banking licence as a WOS are:

- Setting up of WOS in India must have the approval of the home country regulator/supervisor.
- The bank will be subject to adequate prudential supervision under internationally accepted standards, which includes consolidated supervision in its home country.
- The initial minimum paid-up voting equity capital for a WOS is INR5 billion.
- The newly set up WOS of the foreign bank is required to have the entire amount of initial capital in place, which must be funded by free foreign exchange remittance from its parent company.

Timing and Basis of Decision

There is no specified timing for the grant of a licence in the relevant regulations. On the basis of past licences provided by the RBI, it usually takes between about 12 and 18 months. The in-principle approval granted by RBI is generally valid for between about 12 and 18 months.

The RBI has clarified that it may not be possible for them to issue licences to all the applicants meeting the eligibility criteria. The final decision to grant a licence is taken by the RBI. Licences are issued on a very selective basis to those who:

- Comply with the stated requirements.
- Have an impeccable track record.
- Are likely to comply with the best international and domestic standards of customer service and efficiency.

For granting licences to foreign banks setting up a WOS in India, the following additional factors (among others) are also taken into consideration:

- Economic and political relations with the country of incorporation of the parent bank.
- Reciprocity with home country of the parent bank.
- Financial soundness.
- Ownership pattern.
- International and home country ranking of the parent bank by a reputable agency.
- Home country/parent bank rating by an internationally respected rating agency.
- International presence of the bank.
- Adequate risk management and internal control systems.

Cost and Duration

Licences issued by the RBI may be subject to any terms and conditions it determines at its sole discretion.

There is no specified duration of the licence which is issued until cancelled voluntarily or by the RBI.

No cost for obtaining a licence has been specified by the RBI.

The bank must comply with the applicable prudential norms of maintaining capital and liquidity reserves under the applicable guidelines.

5. **Can banks headquartered in other jurisdictions operate in your jurisdiction on the basis of their home state banking licence?**

   A foreign bank must obtain a banking licence for conducing banking business in India (see Question 4).

Forms of Banks

6. **What forms of bank operate in your jurisdiction, and how are they generally regulated? Does the regulatory regime distinguish between different forms of banks? Are there any specific requirements for banks or banking groups in your jurisdiction in relation to the scope of business or organisation?**

State-Owned Banks

In India, state-owned banks (known as public sector banks) are those banks in which the major or full stake in the bank is held by the central or state government. The ownership and control of these banks is assumed by the Government of India.

Apart from common laws that apply to most banks, state-owned banks are regulated under certain specific acts, such as the:

- State Bank of India Act, 1955.

- Export-Import Bank of India Act, 1981.
- Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970.

Universal Banks, Commercial and Retail Banks

Universal banks or scheduled commercial banks are full service banks and provide all eligible financial products. There is no separate regulatory regime for universal banks, commercial and retail banks in India. These banks are primarily governed by the Banking Regulation Act and the RBI Act.

Investment Banks

Investment banks are regulated by the Securities and Exchange Board of India (SEBI) under the Securities and Exchange Board of India Act, 1992. The SEBI is the regulator for the securities markets in India and is responsible for regulating and supervising all participants in the securities market, including investment banks.

Investment banks in India are primarily involved in providing advisory services related to mergers and acquisitions, underwriting securities and other capital market transactions. These activities are regulated by the SEBI through various regulations, guidelines and circulars.

Private Banks

Private banks in India are regulated by the RBI. The RBI is responsible for licensing, regulating and supervising private banks.

There is no separate regulatory regime for private banks in India. These banks are primarily governed by the Banking Regulation Act and the RBI Act.

Other Banks

There are other special financial institutions set up in India for financing agriculture and rural development and other small scale businesses, such as the Small Industries Development Bank of India and the National Bank for Agricultural and Rural Development. These institutions are governed under their own specific acts notified by the Government of India.

Apart from the above, two specialised banking entities are:

- Payment banks. Payment banks are institutions with specific licensing conditions restricting their activities mainly to accepting demand deposits and providing payments and remittance services.
- Small finance banks. These are banks which primarily undertake basic banking activities of acceptance of deposits and lending to unserved and underserved sections including small business units, small and marginal farmers, micro and small industries and unorganised sector entities.

Both the above types of banks are primarily governed by the Banking Regulation Act and the RBI Act. However, separate guidelines are issued by the RBI for these banks.

Regulation of Systemically Important Financial Institutions (SIFIs)

The RBI provides licences to NBFCs under the RBI Act. A non-banking financial company having total assets of INR500 crores (about USD60 million) is classified as a systemically important non-banking financial company (SIFI). These entities are regulated under the RBI Act and rules and regulations issued under that Act.

Organisation of Banks

Legal Entities

7. What legal entities can operate as banks? What legal forms are generally used to operate as banks?

Under the Banking Regulation Act, banking business must be conducted by a company. A foreign banking company can set up a branch in India without establishing or incorporating a company in India (see Question 4).

8. What requirements apply to the structure of banking groups?

Entities and groups in the private sector and NBFCs engaged in other multiple businesses are eligible to set up a bank through a wholly owned NOFHC (see Question 4). The principles that apply to the NOFHC are:

- The NOFHC must be the holding company of the bank and of the other financial services entities of the group.
- The NOFHC must be registered as a NBFC with the RBI and is governed by a separate set of directions issued by the RBI.
- At least 50% of the directors of the NOFHC must be independent directors.
- The corporate structure should not impede the effective consolidated supervision of the bank and the NOFHC by the RBI.
- The prudential norms prescribed by the RBI apply to the NOFHC both on a stand-alone and on a consolidated basis.
- Neither the NOFHC nor the bank is allowed to have any exposure to the promoter group. The bank is not allowed to invest in the equity/debt capital instruments of any financial entities held by the NOFHC.

Separately, Indian banking groups are subject to restrictions on cross-holdings, which limit the extent to which one entity within the group can hold shares or other interests in another entity within the group. This is intended to prevent excessive interdependence between entities within the group and to promote greater transparency and accountability.

9. What are the legislative and non-legislative corporate governance rules for banks?

The Companies Act, 2013 (Companies Act) and the Banking Regulation Act are among the laws that govern corporate governance for banks in India.

The Companies Act deals with the board of directors' composition, the functioning, appointment and removal of directors, and audit and reporting requirements.

The Banking Regulation Act regulates and supervises banking companies and sets out provisions for the appointment and removal of directors, maintenance of books and accounts and audit and reporting requirements.

Additionally for listed companies, the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 apply, which focus on investor protection through disclosures.

To ensure a robust banking system and financial soundness, the RBI issues guidelines from time to time to comply with best international practices and norms and banks in India must comply with all the RBI guidelines that apply to them.

The guidelines cover, among others:

- Fit and proper criteria for directors of banks.
- Separation of the post of chairperson and managing director (MD)/chief executive officer (CEO).
- Directors' remuneration.
- Diversified ownership of private sector banks.
- Risk-based internal audit framework.
- Standards for outsourcing IT services. Regulated entities must:
  - conduct proper due diligence on service providers;
  - monitor and control outsourced activities; and
  - establish a robust risk management framework to comprehensively deal with the identification, measurement, mitigation, management and reporting of all risks associated with the outsourcing of IT services (see also Question 13).

RBI specifically aims to ensure corporate governance and bank soundness through transparency and disclosure standards aligned with international best practices, systems of off-line surveillance and prompt corrective action.

The Indian Banks' Association (IBA) was formed on 26 September 1946, and all banks are members of this non-statutory body. The IBA also advises banks on corporate governance.

The corporate governance of SIFIs is regulated under the provisions of the RBI Act and specific corporate governance guidelines issued by the RBI.

10. What are the organizational requirements for banks?

Private Banks in India must be incorporated as companies under the Companies Act. Foreign banks can operate in India as a WOS (incorporated as company in India) or through a branch (where no company is incorporated in India).

State-owned banks are either incorporated as companies under the Companies Act or statutory bodies incorporated under specific legislation.

11. What is the supervisory regime for management of banks?

The management of banks is governed by the Banking Regulation Act. The RBI has supervisory power over the management of the banks. The RBI's supervisory functions relating to management of banks cover a wide range of activities including:

- **Fit and proper criteria**. The RBI ensures that the individuals who manage banks meet certain fit and proper criteria, such as their integrity, reputation and experience.
- **Board of directors**. The RBI sets guidelines for the composition and functioning of the board of directors of banks, including the appointment of independent directors, the separation of the roles of chairperson and CEO and the establishment of board committees.
- **Risk management**. The RBI requires banks to have robust risk management frameworks, including policies and procedures for credit risk, market risk, operational risk and liquidity risk management.
- **Internal controls**. The RBI requires banks to have effective internal controls, including internal audit and compliance functions to ensure that their operations are conducted in a safe and sound manner.
- **Capital adequacy**. The RBI sets capital adequacy requirements for banks to ensure that they have sufficient capital to absorb losses and maintain their financial stability.
- **Asset quality**. The RBI monitors the asset quality of banks and requires them to maintain adequate provisions for bad loans.

The Banking Regulations Act also governs the appointment, reappointment, termination and remuneration of a chairperson, managing or full-time directors of banks. The RBI has the power to remove any chairperson, director, CEO or other officer or employee of a bank on various grounds such as to:

- Maintain public interest.
- Ensure proper management of the bank.
- Prevent the bank’s affairs being conducted in a manner detrimental to the interests of the depositors.

Certain requirements must be met by the directors of banks, as follows:

- Directors of the board must have relevant professional experience. At least 51% of the board must have expertise in accountancy, agriculture and rural economy, banking, co-operation, economics, finance, law, small-scale industry or any other matter which is useful to the bank.

Of these directors, at least two must have special knowledge in agriculture and the rural economy, or small-scale industry.

- Directors of the bank must not own or be connected to any other company other than a small-scale industrial concern.
- Unless they are chairperson or a full-time director, a director's term must not exceed eight years.

(Section 10A, Banking Regulation Act.)

The RBI has issued separate guidelines on the management of SIFIs.

12. Do any remuneration requirements apply?

Under the Banking Regulation Act, the remuneration for the chairperson, MD, any other director, manager, CEO and any amendments to their remuneration require prior approval of the RBI.

Further, no banking company is allowed to employ any person whose remuneration takes the form of commission or of a share in the profits of the company, or whose remuneration is excessive in the RBI's opinion.

The RBI has issued guidelines for compensation of full-time directors, CEOs, material risk takers and control function staff. These guidelines are aligned with the Financial Stability Board (FSB) principles for Sound Compensation Practices and the Implementation Standards for Sound Compensation Practices and the Supplementary Guidance. The FSB principles have been endorsed by the G-20 countries and the Basel Committee on Banking Supervision (BCBS).

The RBI guidelines apply to private banks and foreign banks operating in India.

13. What are the risk management rules for banks?

The RBI has set out comprehensive risk management guidelines for banks operating in India. Some of the key recommendations include that banks should:

- Have a risk management committee (RMC) formed by the board comprising non-executive directors only, one of which must have risk management expertise. The RMC reports directly to the board and is responsible for:
  - developing procedures and policies to identify, monitor and measure the risk profile of the bank;
  - verifying models used for pricing complex products;
  - identifying new risks; and
  - reviewing existing risk models in the light of developing best practices in the market.
- Have a loan policy, approved by the board, covering methodologies for measuring, monitoring and controlling credit risk. Further, banks must have a comprehensive risk rating and categorisation system and undertake ongoing loan portfolio reviews.
- Have a comprehensive asset liability management process based on:

  - an efficient management information system;
  - an asset liability committee comprising of bank's senior management; and
  - effective processes to manage liquidity, market and trading risks coupled with funding and capital planning and profit planning and growth projection.

- Appoint a chief risk officer (CRO), a senior official in the bank's hierarchy with necessary and adequate qualification and experience in risk management, having a board approved policy defining their roles and responsibilities. The CRO:
  - is appointed for a fixed term and can be transferred or removed before completion of the term only with the board's approval and on a report to the RBI and, for listed banks, to the SEBI;
  - must not have any reporting relationship with the business verticals of the bank and must not be given any business targets;
  - has direct reporting lines to the MD or the RMC and cannot be appointed as CEO, chief operating officer, chief financial officer or any other similar function.

- Comply with the RBI directions to regulate the outsourcing of IT and IT enabled services by banks and other regulated entities to address various risks involved in outsourcing such services to third party providers. All regulated entities, must (among others):
  - evaluate the need for outsourcing the IT services based on a comprehensive assessment of attendant benefits, risks and availability of commensurate processes to manage those risks;
  - have a board approved IT outsourcing policy which captures criteria for selection of service providers, roles and responsibilities of the board and senior management, disaster recovery and continuity plans, exit strategies and systems to monitor and review such activities;
  - ensure that the outsourcing agreement with each service provider allows the regulated entity to retain adequate control over the outsourced activity and the right to intervene to meet legal and regulatory obligations and to continue its business operations.

- Have a board approved policy for undertaking a risk-based internal audit which includes, in addition to selective transaction testing, an evaluation of the risk management systems and control procedures prevailing in various areas of a bank's operations.

- Follow the RBI guidelines on overall objectives, governance, design and implementation of stress testing programmes to be followed by banks to periodically carry out stress tests involving shocks such as increase in non-performing assets (NPA), depletion in collateral, concentration risk, foreign exchange risk and so on.

Liquidity and Capital Adequacy

Role of International Standards

14. What is the capital adequacy framework that applies to banks?

The capital adequacy framework for banks in India is based on the Basel III accord, which is a global regulatory framework for banks established by the BCBS. A bank must comply with the capital adequacy ratio (CAR) requirements at the consolidated group level and at standalone level.

The CAR is calculated as the ratio of a bank's capital to its risk-weighted assets (RWA), which are assigned different risk weights based on their credit, operational and market risk. Commercial banks must maintain a CAR of 9%.

In addition to the minimum CAR requirement, banks are also subject to additional capital buffers, such as the capital conservation buffer (CCB), which requires banks to hold additional Tier 1 capital to absorb losses during times of financial stress.

The RBI is the regulatory authority responsible for supervising and enforcing the capital adequacy framework for banks in India. The RBI conducts regular stress tests to assess the resilience of banks' capital buffers and their ability to withstand adverse shocks to the financial system.

Separately, an SIFI must maintain a minimum capital ratio consisting of Tier I and Tier II capital which must be at least 15% of its aggregate on-balance sheet RWA and of risk adjusted value of off-balance sheet items.

15. What liquidity requirements apply?

The following liquidity requirements issued by the RBI apply to banks:

- Cash reserve ratio (CRR): a prescribed percentage of a bank's net demand and liabilities deposits (NDTL) as reserves in cash form with the RBI. Currently, the CRR is 4.50%.
- Statutory liquidity ratio (SLR): a prescribed percentage of a bank's NDTL in the form of liquid assets such as cash, gold and government securities. Currently, the SLR is 18%.
- Net stable funding ratio (NSFR): a measure of the available stable funding relative to the required stable funding. It is intended to promote funding stability in a bank over long-term and limits overreliance on short-term wholesale funding. Currently, a bank must maintain NSFR at a minimum of 100%.
- Liquidity coverage ratio (LCR): banks must maintain a minimum level of high-quality liquid assets ensuring sufficient liquidity for meeting the bank's short-term obligations under stressed conditions. Currently, a bank must maintain LCR of 100%.

SIFI must adhere to liquidity risk management guidelines specified by the RBI. An SIFI with assets of approx. USD 1.22 billion and above must maintain a specified liquidity coverage ratio.

16. What leverage requirements apply?

Banks must comply with leverage ratio guidelines issued by the RBI. Under these guidelines, banks must maintain a minimum leverage ratio of 4% for domestic systemically important banks (D-SIBs) and 3.5% for other banks.

In addition to the minimum leverage ratio requirement, the RBI guidelines also require banks to monitor and manage their leverage risks on an ongoing basis. The leverage ratio guidelines in India are intended to complement the existing capital adequacy framework and to provide an additional measure of the risk level of a bank's balance sheet.

Only specific SIFIs must maintain a leverage ratio. For example, NBFCs registered to issue co-branded credit cards with banks must maintain a leverage ratio of seven.

Consolidated Supervision

Role and Requirements

17. What is the role of consolidated supervision of a bank in your jurisdiction and what are the requirements?

Role

The RBI is responsible for the consolidated supervision of banks in India. Consolidated supervision is primarily aimed at the identification and management of risks at the group level, rather than banks at an individual level. This evaluates the strength of the group with the objective of monitoring the impact of other group companies on the bank part of the group.

Requirements

The supervisory framework for consolidated supervision of the banks is comprised of the following three components:

- **Consolidated financial statements**. These are prepared in addition to standalone financial statements in accordance with the format prescribed under the Banking Regulation Act. These include a consolidated balance sheet, consolidated statement of profit and loss, principal accounting policies and notes to the accounts.
- **Consolidated prudential returns**. These are aids in examining the consolidated prudential information at group level.
- **Consolidated capital requirement**. All banking and other financial subsidiaries except subsidiaries engaged in insurance and any non-financial activities (both regulated and unregulated) must be fully consolidated for the purpose of capital adequacy. Exposures of the banks to group companies are also separately regulated by the RBI.

Shareholdings/Acquisition of Control

18. What reporting requirements apply to the acquisition of shareholdings in banks?

The acquisition of shareholdings in banks is governed by the Reserve Bank of India (Acquisition and Holding of Shares or Voting Rights in Banking Companies) Directions (Bank Shareholdings Directions), 2023 and the Banking Regulation Act.

Under the Bank Shareholdings Directions, any prospective shareholder seeking to acquire more than 5% of the share capital or voting rights in a banking company qualifies as a major shareholder and cannot complete the acquisition without the prior consent of the RBI.

Subsequent to the acquisition, if at any time the aggregate holding falls below 5%, the person must seek fresh approval from the RBI if the person intends to again raise the aggregate holding to 5% or more of the paid-up share capital or total voting rights of the banking company.

This restriction does not apply to foreign banks operating in India as a branch and not as a WOS.

19. What requirements or restrictions apply to the acquisition of shareholdings and of control of banks?

The RBI has prescribed conditions on acquisitions and holdings of shares or voting rights in banks (see Question 18). The RBI's permission for such acquisitions is subject to certain maximum percentages of the paid-up share capital or voting rights of the bank, depending on the acquiring person/entity:

- Non-promoters that are natural persons, non-financial institutions, financial institutions directly or indirectly connected with large industrial houses and financial institutions that are at least 50% owned or controlled by individuals (including their relatives and persons acting in concert): 10%.
- Non-promoters that are financial institutions (excluding the above), supranational institutions, public sector undertakings and central or state government: 15%.
- Promoters:
  - 26% after 15 years has elapsed from start of business of the bank; or
  - a higher percentage as part of the licensing conditions or as part of a shareholding dilution plan approved by the RBI during the first 15 years of business.

For permitted shareholdings of between 10% and 40%, the shares acquired must remain locked in for the first five years from the date the acquisition is completed. Where a person is permitted to hold 40% or more of the shares, only 40% of the paid-up equity share capital will remain locked in for the first five years from the date the acquisition is completed.

Under the RBI directions, no bank must (among others):

- Have an equity investment in a subsidiary company or non-subsidiary financial services company individually exceeding 10% of the bank's paid up share capital and reserves as per the last audited or a subsequent balance sheet, whichever is lower.
- Hold more than 10% equity in a deposit taking NBFC (except for a housing finance company).
- Hold more than 10% in a company which is not its subsidiary engaged in non-financial services or 10% of the bank's paid-up capital and reserve, whichever is lower.

  Where the investee company is engaged in non-financial activities permitted for banks or the additional acquisition is for protecting the bank's interest on loans/investments made to a company or restructuring of debt, the investment can exceed the 10% limit but must not exceed 30% of the paid-up share capital of the investee company.

While there are no specific directions for acquisitions of shareholdings or control in branches of foreign banks, it is advisable for any change in shareholding or acquisition, especially one resulting in change of control, to be notified to the RBI.

20. Are there specific restrictions on foreign shareholdings in banks?

The foreign shareholding limits are regulated by the Foreign Direct Investment (FDI) Policies of India. The following limits currently apply:

- **Public sector banks**. The foreign shareholding limit is set at 20% of the paid-up capital.
- **Private sector banks**. The foreign shareholding limit is set at 74% of the paid-up capital. The entry route is automatic (without RBI approval) for shareholdings of up to 49% and must be done by the government route (with the RBI's approval) for those of between 49% and 74%.
- **Foreign Banks**. Foreign direct investment of up to 100% is allowed for the WOS of a foreign bank.

(FDI policy of 2020.)

Liquidation, Resolution and Transfer

21. What is the legal framework for liquidation of banks?

The High Court has the authority to order the liquidation or winding up of a bank (Banking Regulation Act). The jurisdiction of the High Court is determined by the location of the registered office of the bank (for a bank incorporated in India) or the principal place of business (for a bank incorporated outside India).

The process for winding up can be initiated by the central government, the RBI or the bank itself (if its inability to pay its debts is certified by the RBI). The central government can direct the RBI to inspect or report on a bank and will direct the RBI to apply for winding up if it believes that the bank's affairs are detrimental to the interests of its depositors.

The RBI can also initiate the winding up process if:

- The bank's licence is cancelled.
- The bank fails to comply with the minimum capital and reserve requirements or other provisions of the Banking Regulation Act.
- The RBI believes that the bank is unable to pay its debts or is continuing operations to the detriment of its depositors.

Once the High Court passes a winding up order, a liquidator attached to the High Court is appointed to conduct the liquidation. The RBI can also apply to act as the liquidator. The liquidator is responsible for taking charge of the bank's assets, determining the claims of all creditors, realising the bank's assets and distributing the proceeds to its creditors based on the priority of payment.

The SIFI service providers and banks are not specifically included within the ambit of Insolvency and Bankruptcy Code, 2016 (IBC). However, the central government, in consultation with the appropriate financial sector regulator(s), is empowered under section 227 of the IBC to notify specific SIFI service providers other than banks for the purpose of their insolvency and liquidation proceedings under the IBC. In the past, under the aforementioned section, RBI has applied to initiate insolvency resolution of few SIFI service providers like Dewan Housing Finance Corporation Ltd (DHFL) and Srei Infrastructure Finance Limited.

22. What is the recovery and resolution regime for banks? Does your jurisdiction have any specific mechanisms for the transfer of banking business in a resolution scenario, for example to a bridge bank or a regulatory agency?

Obligations to Prepare Recovery Plans

Banks are expected to have a consolidated business continuity plan covering critical aspects of process and technology. In addition to this, the RBI can ask the bank to prepare a corrective action plan under the PCA Framework (see below).

Powers of the Regulator

The RBI has issued a Prompt Corrective Action (PCA) Framework for Scheduled Commercial Banks (PCA Framework) for the recovery and resolution of banks. This provides the criteria for determining steps which can be taken by the RBI for restoring the financial health of a bank and an indicative list of such steps.

Under the PCA Framework, the RBI:

- Has the authority to intervene and initiate corrective actions for a distressed bank.
- Assesses the financial health of a bank based on certain parameters and, if necessary, initiates prompt corrective action plan for its resolution.

In a resolution scenario, where the financial viability of a bank is in question, the RBI has several options available to it under the PCA Framework, which include resolution of the bank by amalgamation or reconstruction. The specific mechanisms vary based on the specific circumstances and the RBI has the discretion to determine the most suitable course of action.

Broadly the discretionary actions include special supervisory actions and actions related to:

- Strategy.
- Governance.
- Capital.
- Credit risk.
- Market risk.
- HR.
- Profitability.
- Business operations.

Further, the PCA Framework applies to all banks operating in India including foreign banks operating through branches or subsidiaries. However, there is no specific mechanism for the transfer of banking business in a resolution scenario and any corrective action to be taken is at the discretion of the RBI.

23. Are there any mechanisms for the transfer of banks' business?

The central government has the power, on an application by the RBI, to:

- Order a moratorium for up to six months
- Sanction the scheme prepared by the RBI of reconstruction or amalgamation of the bank with any other bank.

(Section 45, Banking Regulation Act.)

Section 45(5) of the Banking Regulation Act lists the types of measures that can be contained in such a scheme. A scheme can include the transfer of banks' business partially or wholly.

Other than the above, the bank can transfer its loan exposure to another bank or financial institution under the guidelines issued by the RBI in relation to transfers of loan exposure.

24. Are there any requirements governing the continuity of banks' business?

Banks should put in place appropriate business continuity plans (BCP) and test them periodically to secure their information systems, ensure their continuity and check their robustness (notification issued by the RBI on Business Continuity Planning (BCP), Vulnerability Assessment and Penetration Tests (VAPT) and Information Security dated 26 June 2013).

Banks must formulate a consolidated BCP document covering critical aspects of people, process and technology in view of the increased use of electronic banking channels.

The BCP should cover policies, standards and procedures to:

- Ensure continuity, resumption and recovery of critical business processes at an agreed level.
- Limit the impact of any bank crisis on people, processes and infrastructure (including IT).
- Minimise the operational, financial, legal, reputational and other material consequences arising from a banking crisis.

Further, banks are also required to conduct disaster recovery (DR) drills on a regular basis.

Conduct of Business

25. What conduct of business standards apply to banks' deposit-taking and lending activities?

The IBA Code for Banking Practice was issued with a view to its uniform adoption by the member banks. The code is intended to promote good banking practices by setting out minimum standards for banking services such as current accounts, savings and other deposit accounts and lending activities.

The RBI has also issued guidelines which apply to banks' deposit-taking activities and directions to scheduled commercial banks to regulate interest on deposits which include the following:

- There must be a comprehensive policy on interest rates on deposits duly approved by the board of directors or any relevant committee.
- The rates must be uniform across all branches and for all customers and there must be no discrimination among customers on the amount of interest paid on deposits of similar amounts, accepted on the same date at any of the bank's offices.
- Interest rates payable on deposits must be strictly in accordance with the schedule of interest rates disclosed in advance.

The RBI's Master Circular - Loans and Advances – Statutory and Other Restrictions dated 1 July 2015 provides a framework (applicable to all scheduled commercial banks but excluding regional rural banks) to regulate lending activities. The circular:

- Stipulates various restrictions on loans and advances
- Sets out fair practice guidelines on for lenders to protect borrowers from unfair lending practices and to hold banks/financial institutions to higher levels of ethical practices.

Further, the RBI has issued directions to regulate interest rates on advances including in relation to penal interest.

Complaints Handling

26. Do any requirements apply to the handling of complaints to banks concerning their deposit-taking or lending activities?

The RBI's Master Circular on Customer Service in Banks (dated 1 July 2015) contains detailed guidelines on customer service, including the requirement for banks to ensure that a suitable mechanism exists for receiving and addressing complaints from its customers with specific emphasis on resolving complaints fairly and expeditiously.

The circular requires banks to:

- Ensure that complaint registers are kept at prominent place in their branches to make it easy for customers to enter their complaints.
- Have a system of acknowledging the complaints, where the complaints are received through letters or forms.
- Fix a time-frame for resolving the various types of complaints received.
- Prominently display at the branches the names of the officials who can be contacted for redress of complaints, together with their direct telephone number, fax number, physical and e-mail address for the proper and timely contact by customers and for enhancing the effectiveness of the complaints process.
- Include in the information displayed at their branches the name and other details of the relevant officer appointed under the Banking Ombudsman Scheme, 2006.

- Display on their website the names and other details of head office/regional office officials who can be contacted for redress of complaints including the relevant Ombusdman contact details (see below).
- Display on their website the names and other details of their MD/CEO and other operational managers.

Banks are also required to publicise their grievance process through advertisements and website exposure.

To reinforce the complaints process, banks must appoint an internal ombudsman to function as an independent and objective authority at the apex of their complaints resolution system. Where a customer is dissatisfied by a bank's handling of a complaint, it can file a complaint with the banking ombudsmen of the RBI under the Banking Ombudsman Scheme.

Under the RBI's circular on Strengthening of Grievance Redress Mechanism in Banks dated 27 January 2021, banks are now required to have a comprehensive framework including:

- Enhanced disclosures on customer complaints.
- A mechanism for recovering the costs incurred by the RBI from banks for maintainable complaints received against them in excess of the peer group average.

The circular also promised to review the complaints procedure and the supervisory action the RBI can take against banks that fail to improve their complaints in a timely manner.

Regulatory Developments and Recent Trends

27. What are the regulatory developments and recent trends in bank regulation?

Some of the key regulatory developments and trends in banking regulation in India are:

- **Development of a "green finance" ecosystem**. The RBI and the Indian Government are working on measures to boost sustainable financing and to meet climate change commitments, including:
  - the Ministry of Finance issued the Framework for Sovereign Green Bonds, aimed at reducing the carbon impacts of the Indian economy.
  - the RBI issued a framework for acceptance of green deposits by scheduled commercial banks, including small finance banks and all deposit-taking NBFCs.
- **Enhancing efficient regulatory processes**. Regulated financial businesses generally require licences, authorisations and approvals from the RBI under various statutes and regulations. The application and approval processes for these can now be done in on-line and off-line modes. The central government has announced the need to simplify, ease and reduce cost of compliance by financial sector regulators within set time limits to decide the applications under various regulations. The RBI is developing a secure web-based centralised portal for all types of applications made to the RBI across all functions.
- **Pre-sanctioned credit lines at banks through the Unified Payment Interface (UPI)**. The UPI is currently linked to customers' deposit or pre-paid accounts. It is proposed that the scope of UPI will be extended to facilitate payments financed by credits from banks.

- **IT governance**. The RBI released draft Master Directions on Information Technology Governance, Risk, Controls and Assurance Practices dated 20 October 2022 following its Statement on Developmental and Regulatory Policies released on 10 February 2022.

- **Review of penal charges in loan accounts**. The RBI has issued draft guidelines which include instructions relating to charging penal interest or charges tend to be used for "credit discipline" among borrowers rather than as a revenue enhancement tool over and above the contracted rate of interest.

- **Digital lending.** The RBI has issued guidelines to regulate digital lending activities in India and to enhance protection of the customers or borrowers. The new guidelines introduce various changes including:

  - prohibiting grants of credit on e-wallets;
  - regulating the collection of fees by lending apps;
  - mandating the compulsory reporting of all digital loans to the credit bureaux;
  - regulating the collection and usage of customer data by Fintech companies; and
  - curbing first loss default guarantee arrangements.

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