UNIT 8 CENTRAL BANK: ITS ROLE AS REGULATOR OF THE BANKING SYSTEM

Structure

8.0 OBJECTIVES

After going through this unit, you will be able to:

- To identify the role and powers of the Reserve Bank of India to regulate the Indian banking sector under the Reserve Bank of India Act, 1934 and the Banking Regulation Act, 1949;
- To understand the RBI's Integrated Ombudsman Scheme, 2021;
- To identify the role of the RBI in combating financial terrorism; and
- To examine the RBI's prudential norms.

8.1 INTRODUCTION

Have you ever wondered how a country's Central Bank can influence the economy and impact your everyday life? Have you ever thought how the Indian Banking System Regulated by the Reserve Bank of India? How can a single institution wield such power over the entire economy? This unit tries to explain this power. The Reserve Bank of India, as per the Banking Regulation Act, 1949, is authorized to inspect and regulate banks in the interest of the banking system, and the welfare of depositors and the public. The Reserve Bank of India is responsible for regulating commercial banks and LABs under the Banking Regulation Act, 1949, the Reserve Bank of

India Act, 1934, and related laws. RBI's Department of Co-operative Bank Regulation (DCBR) regulates State Co-operative Banks (StCBs), District Central Co-operative Banks (DCCBs) and Urban Cooperative Banks (UCBs). RBI's main tasks include setting regulations for compliance with banking laws, such as licensing, branch expansion, reserve maintenance, and bank management. It also approves the establishment of bank subsidiaries and new banking activities. The Bank aims to foster a strong, diverse, and competitive banking system by establishing prudent regulations and staying updated on domestic and global developments to adapt policies accordingly. It strives to align regulatory standards of commercial banks with international best practices. To achieve its goal of establishing a world-class banking system in India, it maintains a flexible organizational structure with professionally skilled staff and adapts its activities to meet current needs.

8.2 THE RESERVE BANK OF INDIA ACT, 1934

The Reserve Bank of India Act, 1934 is very important law which gives various powers to the Reserve Bank along with its obligations. The Act is applicable to whole of India. The following sections are noteworthy:

Section 22: Exclusive power to issue currency notes

The text of section 22(1) goes as follows:

> *"The Bank shall have the sole right to issue bank notes in [India], and may, for a period which shall be fixed by the [Central Government] on the recommendation of the Central Board, issue currency notes of the Government of India supplied to it by the [Central Government], and the provisions of this Act applicable to bank notes shall, unless a contrary intention appears, apply to all currency notes of the Government of India issued either by the [Central Government] or by the Bank in like manner as if such currency notes were bank notes, and references in this Act to bank notes shall be construed accordingly".*

Interpretation: As per section 22(1), the RBI has exclusive power to issue bank notes for a time period fixed by the Central Government on the recommendation of the Central Board. Apart, it will issue the currency notes of the Government of India (e.g., ₹ 1 note). In this regard, the students are advised to read the press release[1] (dated 19th March 2016) made by the RBI. The link of the press release is given in the footnote.

Section 24: Demonetisation of currency notes

The two sub-sections of section 24 go as follows:

1) *Subject to the provisions of sub-section (2), bank notes shall be of the denominational values of two rupees, five rupees, ten rupees, twenty rupees, fifty rupees, one hundred rupees, five hundred rupees, one*

[1] https://www.rbi.org.in/commonperson/english/scripts/Press Releases.aspx?Id=1714

thousand rupees, five thousand rupees and ten thousand rupees or of such other denominational values, not exceeding ten thousand rupees, as the Central Government may, on the recommendation of the Central Board, specify in this behalf.

2) *The Central Government may, on the recommendation of the Central Board, direct the non-issue or the discontinuance of issue of bank notes of such denominational values as it may specify in this behalf.*

Interpretation: As per section 24(1), the RBI can issue the bank notes of ₹ 2, ₹ 5, ₹ 10, ₹ 20, ₹ 50, ₹ 100, ₹ 500, ₹ 1000, ₹5000, and ₹10,000 or such other note as specified by the Central Government on the recommendation of the Central Board[2]. However, as per section 24(2), the RBI is required to stop the issue of the specified bank notes on being directed by the Central Government. The 2016 demonisation is a recent example in this regard in when the bank notes of ₹ 500, ₹ 1000 were discontinued.

Section 42: Cash reserves of scheduled banks to be kept with the RBI

Cash Reserves Ratio: According to section 42(1), every bank (whose name appears in the Second Schedule of the Act) is required to maintain with the RBI an average daily balance[3]. The amount of such balance cannot be less than the specified percentage (known as Cash Reserve ratio – CRR[4]) of the total of the demand and time liabilities in India as per the returns filed by the bank concerned under section 42(2). In this regard, according to Direction 4 of Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR), Directions – 2021[5]

> *"Every bank shall maintain in India by way of cash reserve, a sum equivalent to such percent of the total of its Net Demand and Time Liabilities (NDTL) in India, in such manner and for such dates, as the Reserve Bank in terms of Section 42(1) of the RBI Act, 1934 and Section 18(1) of BR Act, 1949 [including provisions of Section 18 (1) of the BR Act as applicable to cooperative banks], may specify, by notification in the Official Gazette, from time to time having regard to the needs of securing the monetary stability in the country".*

There is no upper or lower limit on CRR. Till 2006, the lower and upper CRR limits were 3% and 20% respectively.

Note: BR Act means the Banking Regulation Act, 1949.

Statutory Liquidity Ratio (SLR) : According to Section 42(2) of the RBI Act, notwithstanding anything contained in sub-section (1), the Reserve Bank

---

[2] Central Board means the Central Board of Directors of the Reserve Bank of India – Section 2 of the RBI Act, 1949.
[3] Average daily balance means the average of the balances held at the close of business on each day of a fortnight. Further, fortnight means the period from Saturday to the second following Friday, both days inclusive.
[4] As of 7th May 2024, the CRR is 4.5% (https://rbi.org.in/Home.aspx)
[5] https://m.rbi.org.in/scripts/BS_ViewMasDirections.aspx?id=12131#

directs scheduled commercial banks to maintain with the Bank, in addition to the balance prescribed by or under sub-section (1) of the RBI Act , an additional average daily balance the amount of which shall not be less than the [rate specified in the notification, such additional balance being calculated with reference to the excess of the total of the demand and time liabilities of the bank as shown in the return referred to in sub-section (2) over the total of its demand and time liabilities] at the close of business on the date specified in the notification as shown by such return so however, that the additional balance shall, in no case, be more than such excess.

Consequent upon amendment to the Section 24 of the Banking Regulation Act,1949, effective January 23, 2007, the Reserve Bank can prescribe the SLR for SCBs in specified assets. The value of such assets of a SCB shall not be less than such percentage not exceeding 40 per cent of its total DTL in India as on the last Friday of the second preceding fortnight as the Reserve Bank may, by notification in the Official Gazette, specify from time to time.

Thus, there is no lower limit of SLR requirement, however, the upper limit is 40 per cent.

8.3 THE BANKING REGULATION ACT, 1949

The Banking Regulation Act of 1949 is a significant legislation in India governing the operations of all banking entities within the country. Originally enacted as the Banking Companies Act of 1949, it became effective on March 16, 1949, and was later renamed as the Banking Regulation Act of 1949 on March 1, 1966. Initially, the law was limited to regulating banking companies. However, in 1965, amendments were made to include cooperative banks and introduce other modifications. The Banking Regulation Act provides a comprehensive framework for the supervision and regulation of commercial banking in India, complementing the Companies Act of 1956. Notably, primary agricultural credit societies and cooperative land mortgage banks are exempted from its provisions. Under this Act, the Reserve Bank of India (RBI) is empowered to license banks, oversee shareholding and voting rights, regulate board appointments and management, govern bank operations, prescribe audit instructions, manage moratoriums, mergers, and liquidations, issue directives for public welfare and banking policy, and levy penalties. In 1965, the Act was amended to extend its coverage to cooperative banks through Section 56. These banks, typically operating within a single state, are established and managed by the respective state governments. However, RBI retains authority over licensing and regulation of their business activities. The Banking Act serves as a complementary legislation to previous banking-related acts.

Revised Banking Regulation (Amendment) Act, 2020 is effective from 29th September 2020[6]. The amended Act encompassed 1,482 urban and 58 multi-state cooperative banks, subjecting them to RBI oversight. Notably, the Act

[6] https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=52595

empowered the RBI to undertake bank reconstructions or mergers without necessitating moratoriums. The following sections are noteworthy:

Section 22(1): Licensing of Banking Companies

As per section 22(1), no banking company can carry on its business without taking license from the RBI. The RBI is given the power to fix such conditions of license as it thinks to fit.

Section 22 (4): Cancelling license

According to section 22(4), the RBI reserves the power to cancel the license given to banking company under section 22(1). In the following circumstances, the RBI may cancel the license:

a) if the company ceases to carry on banking business in India

b) if the company at any time fails to comply with any of the conditions of license fixed by the RBI.

c) if at any time, any of the conditions referred to in section 24(3), and section 24(3A) are not fulfilled.

Note: If the decision of the RBI to cancel the license is not appealed to the Central Government, then the decision of the RBI is final.

Section 23(1): Restrictions on opening of new, and transfer of existing, places of business

According to section 23(1), without the approval of the RBI, no banking company can open a new place of business in India or change (except within the same city, town or village) the location of its business in India.

Moreover, without the approval of the RBI, no banking company incorporated in India can establish a new branch outside India or relocate an existing one to a different location in any foreign country or area, except within the same city, town, or village. However, this restriction does not apply to the temporary opening of a branch for up to one month within the same locality where the banking company already operates, for events like exhibitions, conferences, fairs, or similar occasions, to provide banking services to the public.

Section 24: Maintenance of a percentage of assets

> *"A scheduled bank, in addition to the average daily balance which it is, or may be, required to maintain under Section 42 of the Reserve Bank of India Act, 1934 and every other banking company, in addition to the cash reserve which it is required to maintain under section 18, shall maintain in India, assets, the value of which shall not be less than such percentage not exceeding forty per cent, of the total of its demand and time liabilities in India is on the last Friday of the second preceding fortnight as the Reserve Bank may, by notification in the Official Gazette, specify from*

time to time and such assets shall to maintained, in such form and manner, as may be specified in such notification".

Interpretation: According to section 24(1), a scheduled bank and every other banking company is required to maintain a certain percentage (known as Statutory Liquidity Ratio – SLR[7]) of its assets in specified form like cash, gold, etc. This requirement is in addition to CRR as given section 42 of the RBI Act and however, these deposits are maintained by the banks themselves and not with the RBI. SLR cannot exceed 40 per cent. In case of inflationary pressure, the RBI might opt to raise SLR to diminish the credit creation ability of banks.

Section 26A: Establishment of Depositor Education and Awareness Fund Pursuant to the amendment of the Banking Regulation Act, 1949, section 26A has been added in 2013, granting the Reserve Bank the authority to establish The Depositor Education and Awareness Fund (the Fund). This section mandates that any account in India with any bank that has not been operated for ten years or any unclaimed deposit for over ten years be credited to the Fund within three months of the ten-year period expiring. The Fund is intended to promote depositors' interests and for other purposes specified by the RBI. Depositors can still claim their deposits or operate their accounts even after the ten years have passed and the funds have been transferred. The bank is responsible for paying the depositor and then claiming a refund from the Fund.

Section 35: Inspection

The RBI can inspect any banking company and its books and accounts at any time, on being directed by the Central Government. After the inspection, the Reserve Bank has to give the banking company a copy of its report.

Check Your Progress 1

1) Describe some important sections of The Reserve Bank of India Act, 1934.

   …………………………………………………………………………………

   …………………………………………………………………………………

   …………………………………………………………………………………

2) What are the main provisions of the Banking Regulations Act, 1949?

   …………………………………………………………………………………

   …………………………………………………………………………………

   …………………………………………………………………………………

[7] As of 7th May 2024, SLR is 18 percent.

3) Do you think that the BR Act, 1949 gives immense powers to the Reserve Bank of India?

…………………………………………………………………………………

…………………………………………………………………………………

…………………………………………………………………………………

8.4 COMBATING FINANCIAL TERRORISM

Combating financial terrorism (CFT) refers to the efforts made by the Reserve Bank, along with other regulatory bodies and law enforcement agencies, to prevent and disrupt the flow of funds used to support terrorist activities. The Reserve Bank implements various measures to detect and deter financial transactions that may be linked to terrorism. In this regard, the RBI has issued **Master Circular**[8] — Know Your Customer norms / Anti-Money Laundering Standards/ Combating of Financing of Terrorism /Obligation of banks under PMLA, 2002. Students are advised to read this master circular to enhance their knowledge. The circular starts with its purpose paragraph which goes as follows:

> *"Banks and financial institutions (FIs) have been advised to follow certain customer identification procedure for opening of accounts and monitor transactions of suspicious nature for the purpose of reporting the same to appropriate authority. These 'Know Your Customer' (KYC) guidelines have been revisited in the context of the recommendations made by the Financial Action Task Force (FATF) on Anti Money Laundering (AML) standards and on Combating Financing of Terrorism (CFT). Detailed guidelines based on the recommendations of FATF and the paper issued on Customer Due Diligence (CDD) for banks by the Basel Committee on Banking Supervision (BCBS), with suggestions wherever considered necessary, have been issued. Banks/FIs have been advised to ensure that a proper policy framework on 'Know Your Customer' and Anti-Money Laundering measures is formulated and put in place with the approval of their Boards".*

8.5 THE BANKING OMBUDSMAN SCHEME, 2006

An ombudsman is an independent official appointed to investigate complaints against organizations on behalf of individuals who believe they have been treated unfairly or improperly. Ombudsmen are typically impartial and objective, tasked with resolving disputes and ensuring that the rights of individuals are upheld according to the law or relevant regulations. They often have the authority to investigate complaints, mediate between parties, make recommendations for resolving issues, and sometimes enforce corrective actions or remedies. Ombudsmen serve as a recourse for

[8] https://www.rbi.org.in/Scripts/BS_ViewMasCirculardetails.aspx?id=9848

individuals who have exhausted other avenues for resolving their grievances and seek an impartial resolution.

To resolve the complaints of the customers of various banks, the RBI has launched **the Banking Ombudsman Scheme, 2006**[9] (amended scheme is effective from July 1, 2017). The Banking Ombudsman Scheme is an expeditious and inexpensive forum for bank customers for resolution of complaints relating to certain services rendered by banks. The Banking Ombudsman is a senior official appointed by the Reserve Bank of India to redress customer complaints against deficiency in certain banking services covered under the grounds of complaint specified under Clause 8 of the Banking Ombudsman Scheme 2006 (As amended upto July 1, 2017). Currently, twenty Banking Ombudsmen have been designated, and their offices are primarily situated in state capitals. The addresses and contact information for these Banking Ombudsman offices are available in Annex I of the Scheme. The scheme covers all scheduled commercial banks, regional rural banks and scheduled primary co-operative banks. If a bank fails to respond within one month of receiving a complaint, rejects the complaint, or if the complainant is unsatisfied with the bank's response, they can lodge a complaint with the Banking Ombudsman. According to point 8 of the schemes, the grounds of the complaints are as follows:

1) Non-payment or inordinate delay in the payment or collection of cheques, drafts, bills etc.;

2) Non-acceptance, without sufficient cause, of small denomination notes tendered for any purpose, and for charging of commission in respect thereof;

3) Non-acceptance, without sufficient cause, of coins tendered and for charging of commission in respect thereof;

4) Non-payment or delay in payment of inward remittances;

5) Failure to issue or delay in issue of drafts, pay orders or bankers cheques;

6) Non-adherence to prescribed working hours;

7) Failure to provide or delay in providing a banking facility (other than loans and advances) promised in writing by a bank or its direct selling agents;

8) Delays, non-credit of proceeds to parties' accounts, non-payment of deposit or non-observance of the Reserve Bank directives, if any, applicable to rate of interest on deposits in any savings, current or other account maintained with a bank;

[9] https://rbikehtahai.rbi.org.in/resolve-complaints-faq.html

9) Complaints from Non-Resident Indians having accounts in India in relation to their remittances from abroad, deposits and other bank related matters;

10) Refusal to open deposit accounts without any valid reason for refusal;

11) Levying of charges without adequate prior notice to the customer;

12) Non-adherence to the instructions of Reserve Bank on ATM / Debit Card and Prepaid Card operations in India by the bank or its subsidiaries;

13) Non-adherence by the bank or its subsidiaries to the instructions of Reserve Bank on credit card operations;

14) Non-adherence to the instructions of Reserve Bank with regard to Mobile Banking / Electronic Banking service in India by the bank;

15) Non-disbursement or delay in disbursement of pension (to the extent the grievance can be attributed to the action on the part of the bank concerned, but not with regard to its employees);

16) Refusal to accept or delay in accepting payment towards taxes, as required by Reserve Bank/Government;

17) Refusal to issue or delay in issuing, or failure to service or delay in servicing or redemption of Government securities;

18) Forced closure of deposit accounts without due notice or without sufficient reason;

19) Refusal to close or delay in closing the accounts;

20) Non-adherence to the fair practices codes as adopted by the bank;

21) Non-adherence to the provisions of the Code of Bank's Commitments to Customers issued by Banking Codes and Standards Board of India and as adopted by the bank;

22) Non-observance of Reserve Bank guidelines on engagement of recovery agents by banks;

23) Non-adherence to Reserve Bank guidelines on para-banking activities like sale of insurance / mutual fund /other third-party investment products by banks;

24) Non-adherence to Reserve Bank guidelines on para-banking activities like sale of insurance / mutual fund /other third-party investment products by banks;

25) Any other matter relating to the violation of the directives issued by the Reserve Bank in relation to banking or other services.

26) Any other matter relating to the violation of the directives issued by the Reserve Bank in relation to banking or other services.

Customers can also file complaints regarding inadequacies in service concerning loans and advances:

1. Non-observance of Reserve Bank Directives on interest rates;
2. Delays in sanction, disbursement or non-observance of prescribed time schedule for disposal of loan applications;
3. Non-acceptance of application for loans without furnishing valid reasons to the applicant; and
4. Non-adherence to the provisions of the fair practices code for lenders as adopted by the bank or Code of Bank's Commitment to Customers, as the case may be;
5. Non-observance of any other direction or instruction of the Reserve Bank as may be specified by the Reserve Bank for this purpose from time to time.
6. The Banking Ombudsman may also deal with such other matter as may be specified by the Reserve Bank from time to time.

Source: https://rbidocs.rbi.org.in/rdocs/Content/PDFs/BOS2006_2302017.pdf

The Reserve Bank - Integrated Ombudsman Scheme, 2021

The Reserve Bank - Integrated Ombudsman Scheme, 2021 (the Scheme) was launched on November 12, 2021. The Scheme integrates the existing three Ombudsman schemes of RBI namely,

1) The Banking Ombudsman Scheme, 2006;
2) The Ombudsman Scheme for Non-Banking Financial Companies, 2018; and
3) The ombudsman scheme for digital transactions, 2019.

The Scheme, framed by the Reserve Bank in exercise of the powers conferred on it under Section 35A of the Banking Regulation Act, 1949 (10 of 1949), Section 45L of the Reserve Bank of India Act, 1934 (2 of 1934), and Section 18 of the Payment and Settlement Systems Act, 2007 (51 of 2007), will provide cost-free redress of customer complaints involving deficiency in services rendered by entities regulated by RBI, if not resolved to the satisfaction of the customers or not replied within a period of 30 days by the regulated entity.

In addition to integrating the three existing schemes, the Scheme also includes under its ambit, Non-Scheduled Primary Co-operative Banks with a deposit size of ₹50 crore and above. The Scheme adopts 'One Nation One Ombudsman' approach by making the RBI Ombudsman mechanism jurisdiction neutral.

Some of the salient features of the Scheme are:

1) It will no longer be necessary for a complainant to identify under which scheme he/she should file complaint with the Ombudsman.

2) The Scheme defines **'deficiency in service'** as the ground for filing a complaint, with a specified list of exclusions. Therefore, the complaints would no longer be rejected simply on account of "not covered under the grounds listed in the scheme".

3) The Scheme has done away with the jurisdiction of each ombudsman office.

4) A Centralised Receipt and Processing Centre has been set up at RBI, Chandigarh for receipt and initial processing of physical and email complaints in any language.

5) The responsibility of representing the Regulated Entity and furnishing information in respect of complaints filed by customers against the Regulated Entity would be that of the Principal Nodal Officer in the rank of a General Manager in a Public Sector Bank or equivalent.

6) The Regulated Entity will not have the right to appeal in cases where an Award is issued by the ombudsman against it for not furnishing satisfactory and timely information/documents.

The Executive Director-in charge of Consumer Education and Protection Department of RBI is the **Appellate Authority** under the Integrated Ombudsman Scheme.

8.6 RBI'S PRUDENTIAL NORMS

The RBI, following recommendations from the Committee on Financial System led by Chairman Shri M. Narasimham has implemented gradual changes to ensure that banks accurately depict their financial status in their balance sheets. These changes involve introducing prudential norms for income recognition, asset classification, and provisioning for advances across banks. In this regard, the RBI issued a revised **master circular**[10] - **Income Recognition, Asset Classification, Provisioning and Other Related Matters – UCBs (dated 2nd April 2024)**. The students are advised to go through the circular available on the official website of the RBI, however, some of the most prominent points are discussed here briefly.

1) Asset Classification

Banks should classify their assets into the following broad groups:

a) **Standard assets:** A standard asset refers to a loan or financial asset that doesn't exhibit any signs of problems and doesn't pose more than the normal level of risk associated with the business. In other

[10]https://www.rbi.org.in/scripts/BS_ViewMasCirculardetails.aspx?id=12658#1

words, it is an asset that is considered healthy and is not classified as a Non-Performing Asset (NPA), indicating that it is being serviced as per the agreed terms and doesn't raise concerns about repayment.

b) **Sub-standard assets**: An asset falls into this category if it has been classified as a Non-Performing Asset (NPA) for a period up to 12 months. In such cases, the current financial standing of the borrowers/guarantors or the current market value of the collateral pledged is insufficient to ensure full recovery of the owed amount by the banks. Essentially, assets classified as sub-standard exhibit clear credit weaknesses that hinder the repayment of the debt. There is a notable risk that banks may incur losses if these deficiencies are not rectified.

c) **Doubtful assets:** An asset is categorized as doubtful if it has been classified as a Non-Performing Asset (NPA) for over 12 months. A loan classified as doubtful shares all the weaknesses found in sub-standard assets. However, it also carries the additional characteristic that these weaknesses render the full collection or liquidation highly questionable and improbable based on current known facts, conditions, and values. In essence, doubtful assets pose significant challenges for recovery or liquidation, making their future outcomes uncertain.

d) **Loss assets**: A loss asset is one where loss has been identified by the bank or internal or external auditors or by the Co-operation Department or by the RBI's inspection, but the amount has not been written off, whether completely or partly. In other words, such an asset is considered un-collectible and of such little value that its continuance as a bankable asset is not warranted although there may be some salvage or recovery value.

2) Non-performing assets (NPAs)

Assets are classified as non-performing assets if:

a) In case of a term loan, the interest or principal instalment is overdue for more than 90 days.

b) The account remains 'out of order', in respect of an Overdraft / Cash Credit (OD/CC) and all other loan products being offered as an overdraft facility, including those not meant for business purposes and/or which entail interest repayments as the only credits.

c) The bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted.

d) In the case of direct agricultural advances as listed in Annex 1 (of the circular), the overdue norm specified at para 2.1.3 (of the circular) would be applicable. In respect of agricultural loans other than those specified in Annex 1, identification of NPAs would be done on the same basis as non-agricultural advances.

e) Any amount to be received remains overdue for a period of more than 90 days in respect of other accounts.

f) In addition, an account may also be classified as NPA in terms of certain specific provisions of this Master Circular, including inter alia paragraphs 2.2.7 and clarifications provided under the frequently asked questions (FAQs) in Annex-4 of the document: (https://www.rbi.org.in/scripts/BS_ViewMasCirculardetails.aspx?id=12658#1.

3) Income Recognition

a) The policy of income recognition has to be objective and based on the record of recovery. Income from non-performing assets (NPA) is not recognised on accrual basis but is booked as income only when it is actually received. Therefore, banks should not take interest on non-performing assets to their income account on accrual basis.

b) However, interest on advances against term deposits, NSCs, KVPs and life insurance policies may be taken to income account on the due date, provided adequate margin is available in the accounts.

c) Fees and commissions earned by the banks as a result of re-negotiations or rescheduling of outstanding debts should be recognised on an accrual basis over the period of time covered by the re-negotiated or rescheduled extension of credit.

d) If Government guaranteed advances remain 'overdue' for more than 90 days, the interest on such advances should not be taken to income account unless the interest has been realised. This shall be applicable in cases of both Central and State Government guaranteed accounts.

e) In cases of loans where moratorium has been granted for repayment of interest, banks may recognize interest income on accrual basis for accounts which continue to be classified as 'standard'.

f) As a prudent practice and in order to bring about uniform accounting practice among banks for booking of income on units of UTI and equity of All India Financial Institutions, such income should be booked on cash basis and not on accrual basis.

g) In respect of income from Government securities or bonds of public sector undertakings and All India Financial Institutions, where interest rates on the instruments are predetermined, income may be booked on accrual basis, provided interest is serviced regularly and is not in arrears.

h) Interest realised on NPAs may be taken to income account, provided the credits in the accounts towards interest are not out of fresh / additional credit facilities sanctioned to the borrower concerned.

4) Provisioning norms

Provisioning depends upon the type of the asset i.e.,

i) Loss Assets

The entire assets should be written off after obtaining necessary approval from the competent authority and as per the provisions of the Co-operative Societies Act / Rules. If the assets are permitted to remain in the books for any reason, 100 per cent of the outstanding should be provided for.

ii) Doubtful Assets

a) Provision should be 100 per cent of the extent to which the advance is not covered by the realisable value of the security to which the bank has a valid recourse. The realisable value should be estimated on a realistic basis.

b) In regard to the secured portion, provision may be made on the following basis, at the rates ranging from 20 per cent to 100 per cent of the secured portion depending upon the period for which the asset has remained doubtful:

Period for which the advance has remained in 'doubtful' category	**Provision requirement**
Upto 1 year	20%
1 to 3 years	30%
Advances classified as doubtful for more than 3 years on or after April 1, 2010	100%

iii) Sub-standard assets

A general provision of 10 per cent on total outstanding should be made without making any allowance for ECGC guarantee cover and securities available.

Check Your Progress 2

1) What do you understand by combating financial terrorism (CFT)?

……………………………………………………………………………

……………………………………………………………………………

……………………………………………………………………………

2) Define the non-performing assets (NPAs) as defined by the RBI.

………………………………………………………………………………

………………………………………………………………………………

………………………………………………………………………………

3) Briefly describe the Banking Ombudsman Scheme, 2006

………………………………………………………………………………

………………………………………………………………………………

………………………………………………………………………………

8.7 LET US SUM UP

The unit elucidates the pivotal role of the Reserve Bank of India (RBI) as outlined in the Reserve Bank of India Act, 1934 and the Banking Regulations Act, 1949. The RBI Act delineates the various powers conferred upon the RBI, such as the authority to issue banknotes/currency and determine the Cash Reserve Ratio (CRR) to regulate the financial system effectively. Additionally, the unit underscores the significance of the Banking Regulations Act of 1949, which empowers the RBI to enforce regulations governing aspects like determination of the Statutory Liquidity Ratio (SLR), inspection procedures, licensing, license cancellation, etc. Furthermore, the text delves into the critical role of the RBI in combating financial terrorism, highlighting its efforts in safeguarding the stability and integrity of the financial system. It elaborates on the Banking Ombudsman Scheme of 2006, designed to address grievances and ensure fair practices within the banking industry. Lastly, the unit discusses the RBI's norms for asset classification, income categorization, and other relevant financial parameters, emphasizing its role in maintaining transparency and accountability within the banking sector.

8.8 KEY WORDS

Combating Financial Terrorism : Combating financial terrorism involves efforts by regulatory authorities and financial institutions to prevent, detect, and mitigate activities that fund or facilitate terrorist organizations or activities.

CRR (Cash Reserve Ratio) : The Cash Reserve Ratio (CRR) is the percentage of a bank's total deposits that it is required to maintain as reserves with the Central Bank (in India, the Reserve Bank of India).

Money Laundering : It involves a series of complex financial transactions aimed at concealing the illicit source

		of money, typically through layers of transactions and financial instruments, to integrate the "dirty" money into the legal financial system.
Non-Performing Assets (NPAs)	:	NPAs refer to loans or advances extended by banks and financial institutions that have ceased to generate income for the lender. An asset becomes non-performing when the borrower fails to make interest or principal payments for a specified period, typically 90 days or more.
RBI's Ombudsman Scheme 2006	:	The Reserve Bank of India's Ombudsman Scheme, 2006, is a mechanism established by the RBI to address and resolve grievances and complaints of customers against banks and other financial institutions regulated by the RBI.
SLR (Statutory Liquidity Ratio)	:	SLR is the percentage of a bank's Net Demand and Time Liabilities (NDTL) that it is mandated to maintain in the form of liquid assets such as cash, gold, or government-approved securities.
The Banking Regulation Act, 1949	:	The Banking Regulation Act, 1949, is an Indian legislation that governs the functioning and operations of banks in India. It empowers the Reserve Bank of India (RBI) to regulate the banking sector.
The Reserve Bank of India Act, 1934	:	The Reserve Bank of India Act, 1934, is an important legislation that provides the legal framework for the establishment, powers, and functioning of the Reserve Bank of India (RBI).

8.9 SOME USEFUL REFERENCES

1) https://www.rbi.org.in/commonman/english/Scripts/speeches.aspx?Id=3161

2) https://rbidocs.rbi.org.in/rdocs/Publications/PDFs/RBIA1934170510.PDF

3) https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=52595

4) https://www.rbi.org.in/scripts/BS_ViewMasCirculardetails.aspx?id=12658#1

5) https://rbidocs.rbi.org.in/rdocs/Content/PDFs/BOS2006_2302017.pdf

6) https://www.rbi.org.in/Scripts/BS_ViewMasCirculardetails.aspx?id=9848

8.10 ANSWERS/HINTS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

1) Section 22: Exclusive power to issue currency notes, Section 24: Demonetisation of currency notes, Section 42: Cash reserves of scheduled banks to be kept with the RBI.

2) Section 22(1): Licensing of Banking Companies, Section 22 (4): Cancelling license, Section 23(1): Restrictions on opening of new, and transfer of existing, places of business, Section 24: Maintenance of a percentage of assets, Section 26A.

3) Banking Regulation (Amendment) Act, 2020 empowered the RBI to undertake bank reconstructions or mergers without necessitating moratoriums. Sections like Section 22(1), Section 22(4), Section 23(1), Section 24, Section 35 have given a lot of power to RBI.

Check Your Progress 2

1) CFT refers to the efforts made by the Reserve Bank, along with other regulatory bodies and law enforcement agencies, to prevent and disrupt the flow of funds used to support terrorist activities. The Reserve Bank implements various measures to detect and deter financial transactions that may be linked to terrorism.

2) Assets are classified as non-performing assets if: the interest or principal instalment, bill is overdue for more than 90 days, the account remains 'out of order', in respect of an Overdraft / Cash Credit (OD/CC).

3) The Banking Ombudsman Scheme is an expeditious and inexpensive forum for bank customers for resolution of complaints relating to certain services rendered by banks. The Banking Ombudsman is a senior official appointed by the Reserve Bank of India to redress customer complaints against deficiency in certain banking services.