

INTERNATIONAL FINANCIAL SERVICES CENTRES AUTHORITY

Seventh Authority Meeting on 30th June, 2021

Gist of Agenda item: Draft amendment to the International financial Services Centres Authority (Banking) Regulation, 2020

Draft amendment to IFSCA (Banking) Regulation, 2020 (hereinafter referred to as the Regulation), which have been already circulated, are based on the following broad principles and rationale:

- i. IFSCA is in the process of preparing a consolidated IFSCA Rule book/ Compendium of instructions for banking business in IFSCs. The compendium of instructions shall, *inter-alia*, encompass modules on General matters¹, Representative Office, Regional Administrative Office and Prudential Norms². Amendment/ replacement of provisions under the Regulation is considered necessary for operationalizing some of the core proposals envisaged in the proposed Rule book/ compendium of instructions

- ii. **Nomenclature of IFSC Banking units / Banking Units to be used irrespective of Parent Bank being Indian or Foreign³**

The Regulation prescribes uniform operational guidelines/ directions, permissible activities, prudential norms for all the BUs, irrespective of the country of incorporation of the Parent Bank (i.e Indian Banking Unit or Foreign Banking Unit). Further, in all our communications/ instructions/ circulars, Indian Banking Units or Foreign Banking Units are commonly referred to as Banking Units (BUs) or IFSC Banking Units (IBUs), which is also the term conventionally used by Banking Units.

- iii. **Withdrawing definition of ‘Qualified Individuals’ and ‘Qualified Resident Individuals’ from the Regulation and amending the Regulation that reference thereto⁴**

¹ licensing, control, controlled and designated functions, core principles, supervision, conduct of business, client classification, and communication, conduct of investment business, conflict of interest, accepting deposits, OTC Derivatives, AML/CFT, complaint handling & dispute resolution

² capital adequacy, Risks (credit, market, operational and liquidity)

³ Amendments provision under Reg. 2(1) (c) and omitting provision under Reg. 2 (1) (e) and Reg. 2 (1) (g) of the Regulation

⁴ Omitting provision under Reg. 2 (1) (k), Reg. 2 (1) (l) of the Regulation and amending provisions under Reg. 8 and Reg. 11 of the Regulation

In the absence of deposit insurance and lender of last resort in IFSC, the prescribed net worth criteria for individuals (i.e Qualified Individual, Qualified Resident Individual) serves as a proxy for the maturity of the depositor. However, the net worth criteria for individuals may be subject to changes (as already done in case of qualified resident individuals⁵ for certain transactions⁶) and hard coding them in the Regulation may require due amendments from time to time. IFSC Banking Rule Book/ compendium of instructions shall have a dedicated module covering the client classification, covering the retail clients and the suitability criteria (financial capacity, knowledge about risks) to be laid out by the FIs (including the Banking Units (BUs)) while offering certain types of financial products and services.

iv. Allowing minimum capital for the Banking Units to be maintained by the respective Parent Bank⁷

The application of minimum capital requirement (USD 20 million) to Banking Units operating as a branch of the parent banks, as stipulated in the Regulation needs reconsideration. Presently, under the Regulation, CRAR, Leverage Ratio are allowed to be maintained at the parent level. Liquidity coverage ratio (LCR) may also be maintained at Parent Bank level, subject to prior approval from the Authority. Given that branches are not legal entities, they cannot hold capital of their own. Such requirements are artificial and amount to only the maintenance of assets or liquidity (or both). The requirements also result in a high level of regulatory and supervisory burden for the regulators to ensure compliance and enforcement. This burden is not justified by any benefit in managing risks to regulatory objectives. In line with the practice in other International financial centres (IFCs), the requirement for capital for the exposures of the BU may be allowed to be fulfilled at the Parent level and compliance would be sought through certification by the Parent to that effect. The Authority would also have the capacity to require BUs to maintain a minimum level of capital.

v. Permitting Banking Units to comply with directions/ instructions issued by their Home Regulator, unless otherwise specified by the Authority⁸

Reg. 4 (2) of the Regulation intends to allow a cushion of continuing operation to the BUs during the interim period of IFSCA coming out with fresh operational guidelines. Under the IFSCA Act, 2019, two foreign banks⁹ have been granted licence by IFSCA to set up BUs at IFSC for whom RBI is not the regulator. It would therefore not be correct to require such BUs to follow the directions of RBI in areas where IFSCA is silent. Therefore, with a view to promote ease of doing business, the proposed

⁵ IFSCA circular- F.No.110/IFSCA/Banking Regulation/2020 -21/13, dated 19.2.2021

⁶ RBI circular- RBI/2020-21/99 A.P. (DIR Series) Circular No. 11, dated 16.2.2021

⁷ Amending provisions under Reg. 3 (3) (a) of the Regulations

⁸ Amending provision under Reg. 4 (2) of the Regulation

⁹ HSBC plc. and Barclays plc.

amendment permits BUs to comply with the directions/ instructions issued by their Home regulator, unless otherwise specified by IFSCA.

vi. **Withdrawing provisions on exposure ceiling in the Regulation¹⁰**

The prescribed ceilings for branch level exposures are effectively fixed at a very high level, as they are tied to the parent bank's capital. The exposure ceilings are amenable to prudential prescriptions by the Authority from time to time and will be appropriately covered, along with other related aspects, under the prudential rules of the Rule Book/ Compendium of instructions

vii. **Widening the scope of permitted activities¹¹ for the Banking Units**

In order to align with activities permitted to be undertaken by Banks in some benchmark jurisdictions, the permitted activities' for BUs prescribed under Reg. 13 of Regulation require widening while remaining within the scope of "financial service" as defined u/s 3(1)(e) of the IFSCA Act, 2019. Moreover, since the licence to BUs is issued under the Banking Regulation Act, 1949 (BR Act), the activities permitted u/s 6 of the BR Act are also applicable to BUs, unless specifically prohibited by the Authority. The proposed amendment, when approved, would allow BUs to undertake activities permitted to be undertaken by any financial institution under IFSCA Act, 2019 (unless expressly prohibited by the Authority). BUs, being banks, would also be eligible to conduct the lines of business enumerated under section 6 of the Banking Regulation Act, 1949 (as amended from time to time).

2. Approval of the Authority is sought for notifying draft International Financial Services Centres Authority (Banking) (Second Amendment) Regulation, 2021 in the Official Gazette, after carrying out changes, if any, of drafting and consequential nature. The Authority is further requested to authorise the Chairperson to make such necessary, consequential and incidental steps to operationalise the said Regulation.

¹⁰ Omitting provisions under Reg. 7 of Regulations

¹¹ Amending provision under Reg. 13 of the Regulations