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Know your Customer Compliance of Regional Rural Banks of South India

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ABSTRACT *Money laundering is a serious issue in India because they may be used for anti national activities or terrorism. Know Your Customer (KYC) compliance is a precaution taken by the Reserve Bank of India (RBI) for controlling the money laundering as per Prevention of Money laundering Act, 2002. The investigators conducted this as a qualitative study and the method used was Documentary analysis. The study was guided by the research questions related to the guidelines provided by RBI, the documents used by the Regional Rural Banks (RRBs) for KYC and how RBI penalizes the RRBs if they failed to comply with the guidelines. The collected data are analyzed and arranged in the systematic order here. RBI had been penalizing the banks which are failed to satisfy the norms.*

On the Recommendations of the United Nations the Government of India has passed the Money Laundering Act 2002. Money laundering means to create money by doing illegal activities like drug trafficking and smuggling and it is not easy to understand the origin of funds. Hence the Bank officials are more vigilant in knowing their customers. For protecting the customers the Bank adopts the 'Know Your Customer' (KYC) policy.

According to Iyengar (2007), the needs of the KYC study to reduce the Reputation Risk, compliance Risk, and legal Risk. Risk of loss is the loss due to severe impact on the banks reputation. This may be of particular concern given the nature of the bank's business which requires the confidence of depositors, creditors and the general Market place. Compliance risk is risk of loss due to failure of compliance with key Regulations governing the bank's operations. Legal Risk is the possibility of law suits adverse judgments or contract resulting from failure to observe mandatory KYC Standards or from the failure to Practice due diligence. Consequently the banks can suffer fines, criminal liabilities and special penalties imposed by supervisor.

Objectives of know your customer is to ensure appropriate customer identification and to monitor transactions of a suspicious nature It also helps to control and Regulate the criminal offences like smuggling, drug trafficking and reduce the risk of identity theft, theft of currency , fraud and to understand the main origin of funds.

NEED AND SIGNIFICANCE OF THE STUDY

The investigators intended to study the KYC compliance of Regional Rural Banks as the guidelines provided by Reserve Bank of India (RBI) for controlling money laundering. The Regional Rural Banks (RRBs) are the subsidiaries of leading scheduled banks in that area. In South India there are Ten RRBs in the four states like Andhra Pradesh, Karnataka, Kerala and Tamil Nadu after amalgamation of the related RRBs and before that there are fifteen RRBs. The investors collected secondary data from the websites of these RRBs and RBI and thus wanted to explore this area as a documentary analysis.

RESEARCH QUESTIONS

What are the guidelines provided by RBI to the RRBs for KYC compliance?

What are the documents used by the RRBs for KYC compliance?

How RBI penalizes the RRBs who fail to comply with the guidelines?

METHODOLOGY

The methodology used was documentary analysis. The study was used secondary data like RBI guidelines and the official websites of the RRBs in South India. The information so collected has been analyzed as per the objectives of the study.

DISCUSSION AND FINDINGS

The guidelines provided by RBI to the RRBs for KYC compliance

KYC Procedures for New Customers

According to RBI guidelines for chairmen of All RRBs (2003) KYC procedure should be the key principle for identification of an individual incorporate opening an account. The customer identification should entail verification through an introductory reference from an existing account holder/a person known to the bank or on the basis of documents provided by the customer. The Board should also have in place policies that establish processes and procedures to monitor transaction of suspicious nature in accounts and have systems of conducting due diligence and reporting of such transactions.

KYC Procedures for Existing Customers

According to RBI guidelines for chairmen of All RRBs (2003) Banks are expected to adopt due diligence and appropriate KYC norms at the time of opening of accounts in respect of existing customers in terms of RBI's exact instructions communicated by NABARD/RBI from time to time. However in case of any omission, the requisite KYC procedures for customer identification should be got completed at the earliest.

Ceiling and Monitoring of Cash Transactions

Since 2003 KYC was established to identify the customers

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who transact the amount above 50,000 by furnishing Permanent Account Number (PAN). The banks are required to keep a close watch on cash withdrawals and deposits for Rs. 5 Lakh and above in deposit, cash credit or overdraft accounts and keep record of details of these large cash transactions in a separate register and report such transactions as well as transaction of suspicious nature with full details in fortnightly statements to their Head Office. The Head Office should immediately scrutinize the same and if necessary, have they looked into by deputing officials.

Risk Management and Monitoring Procedures
There are several incidence of abuse of banking channels for illegal and antinational activities. To prevent the Board should clearly lay down the following policies.

Internal control system
Duties and Responsibilities should be clearly allocated to ensure the effectiveness of KYC programme and also periodical checking should be done by Head Office of banks.

Control Terrorism finance
The RBI gives a list of terrorist entities. So the banks may exercise some care if any transaction are found in such entities. Branch level systems ensure to determine whether a person/organization involved in such activities. The authority is responsible to submit the report to the RBI.

Internal Audit/Inspection
An internal audit helps to identify the high value transactions. It should be ensured whether it is done or not in regular basis.

Concurrent auditors must scrutinize and comment on the effectiveness of measures taken by the branches. The reports should be submitted before the audit committee of the Board of banks Identification and Reporting of suspicious Transactions.

The branches and Head Offices report the suspicious transactions to the concerned authorities. If any suspicious accounts are noticed such accounts should be frozen. Quarterly reporting should be sent to the Board of Directors.

Adherence to Foreign Contribution Regulation Act (FCRA) 1976
The bank should pursue the instructions on the provisions of the foreign contribution Regulation Act, 1976. At the time of opening an account or collecting cheques the banks should ensure whether the organization had registered with the government. A certificate of registration must be obtained from the concerned organization at the time of opening an account.

Record Keeping
Financial intermediaries should maintain documentation on their customer relationship and Transactions when electronic transactions are made, the relevant records in support of entries should be shown in the account. It should be available for perusal and scrutiny of audit functionaries.

Training of Staff and Management
All the operating and Management staff must fully understand the need for strict adherence to KYC norms. For the staff should be given adequate training and anti money laundering guidelines.

According to RBI Guidelines for The Chairmen of All RRBs (2003) RRBS are advised to put up The guidelines to the Board of Directors n the ensuring meeting and also bring the guidelines to the notice of your branches/controlling offices and strictly adhere to the instruction on "KYC" norms. These guidelines are issued under section 35 A of the Banking Regulation Act, 1949 and any contravention of the same will attract penalties under the relevant provisions of the Act.

II. The documents used by the RRBs for KYC compliance
The documents to be used for proving the identity of the customer includes Passport, PAN Card, Voters' ID card, Driving License, Job card issued by MNREGA and so on. The customer should submit any of the documents like Ration card, Electricity bill, Telephone bill, Letter from employer, Income tax/Wealth tax assessment order and so on.

In order to address these issues create public awareness and give wide publicity to these KYC simplification measures, RBI has issued a press release together with a poster and a booklet comprising a few common questions relating to KYC norms for opening bank accounts.

RBI have been simplified the KYC norms for helping the common man for opening new account.

MEASURES TAKEN FOR SIMPLIFICATION
1. Single document for proof of identity and proof of address.

Valid documents for KYC purpose include passport, driving license, voters ID card, PAN card, Aadhaar letter issued by UIDAI and Job Card issued by NREGA signed by a state government official.

2. No Separate Proof of Address is required for Current Address.

Since migrant workers, transferred employees often face difficulties while submitting a proof of current address for opening a bank account such customers can submit only me proof of address while opening a bank account.

3. No Separate KYC Documentation is Required While Transferring Accounts from One Branch to Another of the Same Bank.

Once KYC is done by done branch of the bank it is valid for transfer of the account to any other branch of the same bank. The customer would be allowed to transfer his/her account from one branch to another branch without restrictions and on the basis of declaration of his coal address for communication.

Relaxation regarding officially valid documents for low risk customers
If a person does not have any of the officially valid documents but f it is categorized as 'low risk' by the banks, then she can open a bank account by submitting any one of the following documents.

Identity card with applicants photograph.
Letter issued by a gazette officer, with a duly attested photograph of the person.

Time intervals for periodic updating of KYC for existing low/medium and high risk customers have been increased from 5/2 years to 10/8/2 years.

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Actions taken by RBI against who fail to comply with the guidelines

In 2011 March, RBI has penalized Saptairi Gramin Bank Chittoor, Andhrapradesh for violating the KYC norms. RBI has imposed a monetary penalty of Rupees Five Lakhs as per section 46 and 47 A of Banking Regulation Act, 1949. In 2013, RBI penalized twenty two nationalized banks for the violation of KYC norms including Canarabank (sponsor of Kerala Gramin Bank), State Bank of India (sponsor of Andhra Pradesh Grameena Vikas Bank) and Indian Overseas Bank (sponsor of Pandyan Grama Bank) on 2013 July. RBI imposes partial freezing of the accounts of the customers who were failed to produce documents as per KYC compliance.

CONCLUSION

KYC is the most important tool for preventing Money Laundering in India. Money laundering may cause high inflation and thereby RBI has imported many rules and restrictions on banks and financial institutions to prevent Money Laundering. RBI has provided guidelines for RRBs on KYC time to time and as Central bank of India, RBI had been taken action against the RRBs and their sponsoring banks that violate the guidelines.

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