



RBI/2022-2023/118

Ref. No.DoS.CO.PPG/SEC.04/11.01.005/2022-23

September 19, 2022

The Chairman / Managing Director / Chief Executive Officer
All Primary (Urban) Co-operative Banks (UCBs)

Madam / Dear Sir,

**Compliance Function and Role of Chief Compliance Officer (CCO)-
Urban Co-operative Banks**

As part of the overall structure for Corporate Governance, the Compliance Function serves a critical role. Therefore, it has been decided to introduce certain principles, standards and procedures for Compliance Function in UCBs, keeping in view the principles of proportionality. Accordingly, this Circular shall be applicable to all UCBs under Tier 3 and Tier 4 categories¹ except UCBs under All Inclusive Directions (AID)². UCBs under Tier 1 and Tier 2 categories shall continue to be governed under the existing guidelines³.

2. The UCBs under Tier 4 category shall put in place a Board-approved policy and a Compliance Function, including the appointment of a Chief Compliance Officer (CCO), based on the Framework given in the [Annex](#), latest by April 1, 2023. The UCBs under Tier 3 category shall implement the same latest by October 1, 2023.

¹ Please refer to the Reserve Bank's Press Release dated July 19, 2022 on Revised Regulatory Framework for Urban Co-operative Banks (UCBs) in terms of which UCBs have been categorised into following four tiers for regulatory purposes: **Tier 1** - All unit UCBs and salary earner's UCBs (irrespective of deposit size), and all other UCBs having deposits up to ₹100 crore; **Tier 2** - UCBs with deposits more than ₹100 crore and up to ₹1000 crore; **Tier 3** - UCBs with deposits more than ₹1000 crore and up to ₹10,000 crore; **Tier 4** - UCBs with deposits more than ₹10,000 crore.

²A transition time of six months will be provided for ensuring compliance with these guidelines, as and when such UCBs come out of AID.

³ [Master Circular ref No. DCBR.BPD \(PCB/RCB\) Cir.No.2/14.01.062/2015-16](#) on Board of Directors-UCBs dated July 01, 2015 read with Circular ref No. UBD.No.BSD.I.PCB.11/12.05.01/2002-03 on Designating Compliance Officers in Urban Co-operative Banks dated August 16, 2002 issued by the Reserve Bank *inter alia* prescribe the role of Directors and the Audit Committee of Board with Compliance highlighted as one of the major responsibilities and for a senior official to be designated as 'Compliance Officer'.

3. This Circular shall be placed in the immediate next meeting of the Board of Directors for information and devising an implementation strategy, under the Board's supervision, in a time-bound manner.

Yours faithfully,

(Tarun Singh)
Chief General Manager
Encl.: Annex

Framework for Compliance Function and Role of Chief Compliance Officer in Primary (Urban) Co-operative Banks (UCBs) under Tier 3 and Tier 4 categories⁴

1. Introduction

The Compliance Function is an integral part of effective governance, along with the internal control and risk management processes. The UCBs under Tier 3 and Tier 4 categories shall treat the guidelines in the Circular as a set of minimum guidelines only and accordingly frame their own guidelines taking into account their corporate governance framework, the scale of operations, risk profile, organisational structure and code of conduct, etc.

2. Compliance Risk

Compliance risk is the risk of legal or regulatory sanctions, material financial loss or loss of reputation a UCB may suffer, as a result of its failure to comply with laws, regulations, rules, and codes of conduct, etc., applicable to its activities.

3. Scope and Coverage of Compliance Function

Compliance Function shall ensure strict observance of all statutory and regulatory requirements for the UCB, including standards of conduct, managing conflict of interest, treating customers fairly and ensuring the suitability of customer service.

4. Responsibility of the Board and Senior Management

4.1 The Board / Board Committee⁵ shall ensure that an appropriate Compliance Policy is put in place and implemented. Further, the Board / Board Committee shall prescribe the periodicity for review of Compliance risk.

4.2 The Senior Management shall:

- i) carry out an exercise, at least once a year, to identify and assess the major Compliance risk facing the UCB and formulate plans to manage it;
- ii) submit to the Board / Board Committee a review at the prescribed periodicity and a detailed annual review of Compliance; and
- iii) report promptly to the Board / Board Committee on any material Compliance failure while ensuring that appropriate remedial or disciplinary action is taken.

⁴ Except UCBs under All Inclusive Directions (AID). A transition time of six months will be provided for ensuring compliance with these guidelines, as and when such UCBs come out of AID.

⁵ 'Board Committee' means 'Audit Committee of the Board'

5. Responsibilities of Compliance Function

5.1 Compliance Function shall be responsible for undertaking the following activities at the minimum:

- i) *Assist the Board and the Senior Management in overseeing the implementation of Compliance Policy* including policies and procedures, prescriptions in Compliance Manuals, internal codes of conduct, etc.
- ii) *Play the central role in identifying the level of Compliance risk in the organisation.* The Compliance risks in existing / new products and processes shall be analysed and appropriate risk mitigants put in place. The Chief Compliance Officer (CCO) shall be a member of the 'new product' committee/s⁶. All new products shall be subjected to intensive monitoring at least for the first six months of introduction to ensure that the indicative parameters of Compliance risk are adequately monitored.
- iii) *Compliance Function shall monitor and test Compliance* by performing sufficient and representative Compliance testing, and the results of such Compliance testing shall be reported to the Senior Management. It shall periodically circulate the instances of Compliance failures among staff, along with the required preventive instructions. Staff accountability shall be examined for major Compliance failures.
- iv) *Ensure compliance of regulatory / supervisory directions given by RBI in both letter and spirit in a time-bound and sustainable manner.* RBI will continue to expect an effective Compliance Program where all Risk Mitigation Plan (RMP) / Monitorable Action Plan (MAP) points are complied with within the timelines prescribed. Unsatisfactory compliance with RMP/MAP may invite penal action from RBI.
- v) *Attend to compliance with directions from other regulators in cases where the activities of the entity are not limited to the regulation / supervision of RBI.* Further, discomfort conveyed to the UCB on any issue by other regulators, and action taken by any other authorities / law enforcement agencies, shall be brought to the notice of RBI.

⁶ If there is no such committee in existence, then the CCO shall evaluate all new products before these are launched.

- vi) *The Compliance Department may also serve as a reference point for the staff from operational departments for seeking clarifications / interpretations of various regulatory and statutory guidelines.*

5.2 The CCO shall be the nodal point of contact between the UCB and the regulators / supervisors and shall necessarily be a participant in the structured or other regular discussions held with RBI. Further, compliance to RBI inspection reports shall be communicated to RBI necessarily through the office of the Compliance Function.

5.3 In some UCBs, there may be separate departments / divisions looking after compliance with different statutory and other requirements. In such cases, the departments concerned shall hold the prime responsibility for their respective areas, which shall be clearly outlined. Adherence to applicable statutory provisions and regulations is the responsibility of each staff member. However, the Compliance Function would need to ensure overall oversight.

6. Broad Contours of Compliance Framework in UCBs

A. Compliance Policy

a. The UCB shall lay down a Board-approved Compliance Policy clearly spelling out its Compliance philosophy, expectations on Compliance culture, structure and role of the Compliance Function, the role of CCO, processes for identifying, assessing, monitoring, managing and reporting on Compliance risk. The Policy shall be reviewed at least once a year.

b. Broadly, the Policy shall ensure coverage of the following aspects:

- i) Measures to ensure the independence of the Compliance Function and its responsibility to freely disclose findings and views to Senior Management, Board / Board Committee;
- ii) Focus on various regulatory and statutory Compliance requirements;
- iii) Monitoring mechanism for the Compliance testing procedure;
- iv) Reporting requirements, including Compliance risk assessment and change in risk profile, etc., to the Senior Management and to the Board / Board Committee;
- v) The authority of the Compliance Function to have access to information as specified in Part D below;

- vi) A mechanism for dissemination of information on regulatory prescriptions and guidelines among staff and periodic updating of operational manuals; and
- vii) The approval process for all new processes and products by the Compliance Department, prior to their introduction.

B. Compliance Structure

The Compliance Department shall be headed by the Chief Compliance Officer, meeting the requirements prescribed in this Circular. UCBs are free to adopt their own organizational structure for the Compliance Function. However, the function shall be independent and sufficiently resourced, its responsibilities shall be clearly specified, and its activities shall be subject to periodic and independent review.

C. Compliance Programme

UCBs shall carry out an annual Compliance risk assessment in order to identify and assess major Compliance risks faced by them and prepare a plan to manage the risks. The annual review, to be carried out by the Senior Management, shall ensure coverage of at least the following aspects:

- i) Compliance failures, if any, during the preceding year and consequential losses and regulatory action, as also steps taken to avoid recurrence of the same;
- ii) Listing of all major regulatory guidelines issued during the preceding year and steps taken to ensure compliance;
- iii) Compliance with fair practices codes and adherence to standards set by self-regulatory bodies and accounting standards; and
- iv) Progress in the rectification of significant deficiencies and implementation of recommendations pointed out in various audits and RBI inspection reports.

D. Authority

The CCO and Compliance Function shall have the authority to communicate with any staff member and have access to all records or files that are necessary to enable her / him to carry out entrusted responsibilities in respect of Compliance issues. This authority shall flow from the Compliance Policy of the UCB.

E. Dual Hatting

- i. There shall not be any 'dual hatting,' i.e., the CCO shall not be given any responsibility which brings elements of conflict of interest, especially any role relating to business.

The CCO shall generally not be a member of any committee which conflicts her / his role as CCO with responsibility as a member of the committee, including any committee dealing with purchases / sanctions. In case the CCO is a member of any such committee, that would only be an advisory role.

ii. The staff in the Compliance Department shall primarily focus on Compliance Function. However, the Compliance staff could be assigned some other duties while ensuring that there is no conflict of interest.

F. Qualifications and Staffing of Compliance Function

Apart from having staff with basic qualifications and practical experience in business lines / audit & inspection functions, Compliance Function shall have adequate staff members with knowledge of statutory / regulatory prescriptions, law, accountancy, risk management, information technology, etc. Appropriate succession planning shall be ensured to avoid any future skill gap.

G. Internal Audit & Independent Review of Compliance Function

Compliance risk shall be included in the risk assessment framework of the Internal Audit Function, and Compliance Function shall be subject to regular internal audit. The CCO shall be kept informed of audit findings related to Compliance, which shall serve as a feedback mechanism for assessing the areas of Compliance failures.

H. Supervisory Focus

Examination of Compliance rigor prevalent in the UCB shall be a part of Reserve Bank's supervisory risk assessment process.

7. Appointment and Tenure of CCO

- i) Tenure: The CCO shall be appointed for a minimum fixed tenure of not less than 3 years. However, in exceptional cases, the Board/ Board Committee may relax the minimum tenure by one year, provided appropriate succession planning is put in place;
- ii) Removal: The CCO shall be transferred / removed before completion of the tenure only in exceptional circumstances, with the explicit prior approval of the Board / Board Committee, after following a well-defined and transparent internal administrative procedure;
- iii) Rank: The CCO shall be a senior executive of the UCB with a position not below two levels from the CEO. However, in the case of UCBs under Tier 3 category,

this requirement can be relaxed by one level further. If the UCB considers necessary, the CCO can also be recruited from the market;

- iv) Skills -The CCO shall have a good understanding of the industry and risk management practices, knowledge of regulations, legal requirements, and have sensitivity to Supervisory expectations;
- v) Stature - The CCO shall have the ability to exercise judgment independently. She / He shall have the freedom and authority to interact with regulators / supervisors directly and ensure compliance;
- vi) Conduct - CCO shall have a clean track record and unquestionable integrity;
- vii) Selection Process - Selection of the candidate for the post of the CCO shall be made based on a well-defined selection process and recommendations made by a committee constituted by the Board / Board Committee for the purpose. The Board / Board Committee shall take final decision in the appointment of CCO.
- viii) Reporting Requirements - A prior intimation to the Senior Supervisory Manager, Department of Supervision, Reserve Bank of India, shall be provided before appointment of the CCO, pre-mature transfer, resignation, early retirement, removal or any other change in terms and conditions regarding tenure of the CCO. In the case of appointment, such intimation shall be supported by a detailed profile of the candidate along with the '**Fit and Proper**' certification by the MD & CEO of the UCB, confirming that the person meets the prescribed supervisory requirements and rationale for changes, if any. '**Fit and Proper**' criteria may be examined based on the requirements spelt out in this Framework;
- ix) Reporting Line - The CCO shall have direct reporting lines to the MD & CEO and / or Board / Board Committee. In case the CCO reports to the MD & CEO, the Board / Board Committee shall meet the CCO at quarterly intervals on a one-to-one basis, without the presence of the Senior Management, including MD & CEO. The CCO shall not have any reporting relationship with the business verticals. Further, the performance appraisal of the CCO shall be reviewed by the Board / Board Committee.

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