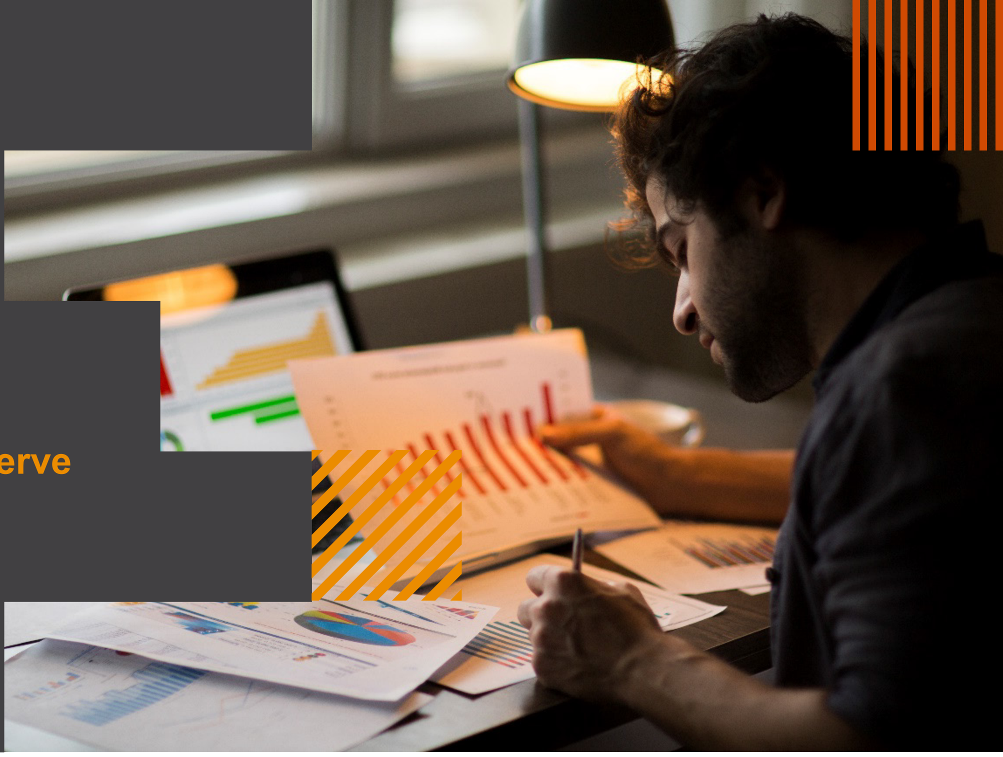
PwC India's Financial Services (FS) Risk Symposium

Key takeaways from the Reserve Bank of India (RBI)

Keynote session

February 2024



PwC India proudly conducted the second edition of its flagship FS Risk Symposium on 13 February 2024 at Hyatt Regency, Chennai. The symposium brought together experts from the banking, financial services and insurance (BFSI) and regulatory sectors to share their knowledge, experiences, insights and strategies to navigate the uncertain and emerging risk landscape.

Our second symposium was meticulously designed to focus more on the emerging challenges faced by non-banking financial banking corporation (NBFCs), small finance banks (SFBs) and smaller private sector banks.

Uma Shankar, Regional Director, RBI - Chennai, commenced the discussions by sharing her vast experience and insights on the emerging risk challenges faced by the Indian banking sector and the corresponding regulatory and supervisory expectations from RBI to tackle such risks.

She started her keynote address by emphasising that RBI's regulations are aimed at ensuring financial soundness and stability. Additionally, they focus on customer protection, especially when a new product or service is rolled out into the market.

She advised and encouraged the banking sector to continually innovate and adapt to advancing technologies to meet the ever-growing customer expectations. However, this needs to be done in a way so that along with regulatory compliance, banks are also able to take care of customers' interests. Necessary safeguards must therefore be built into new products or solutions to ensure protection of customers' interest.

While the risks associated with new products have to be examined thoroughly by the risk management function/team, continuous monitoring of the newly introduced product or service must be ensured by the compliance team to take corrective actions post launch, if necessary.

Banks should also equally consider the quality of outsourcing or third-party vendors in their contractual terms and ensure that these services align with the RBI-stipulated outsourcing frameworks. To mitigate third-party risks, banks should strengthen their internal change management systems such as password encryption, data security and assurance functions. Assurance functions have a crucial role to play in ensuring resilience of each financial institution and the system as a whole.

The following assurance functions were highlighted:

Compliance	Internal audit	Risk management

She mentioned that in order to empower the assurance functions, RBI has put introduced several initiatives over the last two and a half decades in line with the accelerated transformation of the banking structure.

In future, banks may have to embrace increased collaboration with other players in the financial system, including FinTechs, to meet customer expectations in a cost-effective manner. In this context, she referred to the regulatory sandbox initiative undertaken by the RBI for fostering responsible innovation.

Along with robust governance standards and compliance with the accounting standards applicable to the regulated entities (Ind AS for NBFCs is yet to be made applicable to banks), banks need to significantly focus on emerging climate risks and their impact on their business and customers, and factor in such new risks in their Internal Capital Adequacy Assessment Process (ICAAP).

Shankar also outlined two major expectations of the RBI as a supervisory for banks:

Building resilience:

She emphasised that the supervised entities should constantly endeavour to build resilience by enhancing their abilities to anticipate and absorb shocks, and adapt to the constantly evolving environment.

Strengthening lines of defence against risks:

She also focused on strengthening the following three lines of defence in banks:

1. business units/ verticals
2. risk management (risk management committee of the board, Chief Risk Officer and other functionaries) and compliance (Chief Compliance Officer)
3. internal audit (Head of internal audit and related functionaries)

She also chalked out the minimum expectations RBI has from banks for ensuring effective oversight and assurance functions:

- **Policy:** Banks' board of directors must frame relevant policies, consistent with the bank dynamics (size, nature, complexity), in line with the extant regulations, which must have a documented proof of the purpose, authority and responsibility of the oversight and assurance functions while conducting periodic reviews.
- **Independence:** Oversight and assurance functions should be independent of the risk-taking functions and of one another as well, but must have a co-operative functional relationship with business functions and among themselves.
- **Stature and authority:** Oversight and assurance functions should have the same stature as business verticals and must have the ability to influence and change business operations, if required.
- **Resources, competence and training:** Oversight and assurance functions must have skilled employees who are trained in their respective updated markets and product-learning competencies.
- **Risk and compliance culture:** The top management in banks should take the responsibility to encourage and promote a healthy risk and compliance culture.

Way forward

Smt. Shankar concluded the session with a few insightful notes for banks to embrace disruptive innovations through increased collaborations with FinTechs – referring to the regulatory sandbox framework issued by the RBI in 2021, delineated to foster innovations. She also emphasised how banks must place high importance on their cybersecurity and IT governance structures and frameworks, and that their outlined policies should be distinct from each another. Along with robust governance and compliance of Ind AS standards in NBFCs and future banks, the RBI expects banks to focus on climate risks by developing novel models and understanding global policy response by governments to mitigate the same.

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