

NB.DOS.HO.POL.H-271/J.1-2003/04

Circular No. 101/DOS/14/2003

30 April 2003

**The Managing Director /Chief Executive Officer
All State Co-operative Banks**

Dear Sir,

**Guidelines on “Know Your Customer”
norms and “Cash transactions”.**

As you are aware, there is a felt need to establish a systematic procedure for ensuring identity of *a new customer* and to ensure that banks do not enter into business relationship until the identity of *a new customer* is satisfactorily established in the context of expanding business opportunities for banks. There is a need to have policies, practices and procedures that promote high ethical and professional standards to prevent banks from being used intentionally or unintentionally by criminal elements. The banks are thus required to put in place effective procedures to identify customers, refuse suspicious transactions and cooperate with law enforcement agencies. As part of this strategy a concept known as “Know Your Customer” (KYC) has been introduced for banks in India by RBI. As part of introduction of KYC principle, RBI/NABARD has issued number of guidelines relating *to identification of depositors* and advised the SCBs/DCCBs to put in place systems and procedures to help control financial frauds, identify money laundering and suspicious activities, and for scrutiny/monitoring of large value cash transactions. Instructions have also been issued by the RBI/NABARD from time to time advising banks to be vigilant while opening accounts for new customers to prevent misuse of the banking system for perpetration of frauds. Taking into account recent developments, both domestic and international, it has been decided by RBI to reiterate and consolidate the extant instructions on KYC norms and cash transactions. Accordingly, the following guidelines have been framed by RBI to reinforce the instructions on the subject with a view to safeguarding banks from being unwittingly used for the transfer or deposit of funds derived from criminal activity (both in respect of deposit and borrowal accounts), or for financing of terrorism. The guidelines are also applicable to foreign currency accounts/transactions.

2. “Know Your Customer” (KYC) Guidelines for New Accounts : The following KYC guidelines will be applicable to all new accounts with immediate effect.

2.1 KYC Policy

i. “Know Your Customer” (KYC) procedure should be the key principle for identification of an individual/corporate 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.

ii. The Board of Directors of the banks should have in place adequate policies that establish procedures to verify the bonafide identification of individual/corporates opening an account. 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.

2.2 Customer Identification :

i. The objectives of KYC framework should be two fold, (i) to ensure appropriate customer identification and (ii) to monitor transactions of a suspicious nature. Banks should obtain all information necessary to establish the identity/legal existence of each new customer, based preferably on disclosures by customers themselves. Typically easy means of establishing identity would be documents such as passport, driving license, etc. However, where such documents are not available, verification by existing account holders or introduction by a person known to the bank may suffice. It should be ensured that the procedure adopted does not lead to denial of access to the general public for banking services.

ii. In this connection, we also invite a reference to a Report on “Anti Money Laundering Guidelines for banks in India” prepared by a Working Group, set up by Indian Banks Association (IBA), for your guidance. It may be seen that the IBA Working Group has made several recommendations for strengthening KYC norms with anti money laundering focus and has also suggested formats for customer profile, account opening procedures, establishing relationship with specific categories of customers, as well as an illustrative list of suspicious activities.

3. “Know Your Customer” Procedures for Existing Customers

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 extant 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.

4. Ceiling and Monitoring of Cash Transactions

The extant RBI guidelines on the subject are as under :

- i. Bank are required to issue travellers cheques, demand drafts, mail transfer, and telegraphic transfers for Rs. 50,000 and above only by debit to customers' accounts or against cheques and not against cash. Further, the applicants, whether customers or not for the above transactions for amount exceeding Rs.10,000/- should affix permanent Income Tax Account No. on the applications. Since KYC is now expected to establish the identity of the customer and as the issue of demand draft etc. for Rs. 50,000 and above is by debit to account, the requirement for furnishing Permanent Account Number (PAN) stands increased uniformly to Rs. 50,000/-.
- ii. 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 scrutinise the same and if necessary, have them looked into by deputing officials.

5. Risk Management and Monitoring Procedures

In order to check possible abuse of banking channels for illegal and anti-national activities, the Board should clearly lay down a policy for adherence to the above requirements comprising the following :

5.1 Internal Control System

Duties and responsibilities should be explicitly allocated for ensuring that policies and procedures are managed effectively and that there is full commitment and compliance to an effective KYC programme in respect of both existing and prospective deposit accounts. Head Office of banks should periodically monitor strict adherence to the laid down policies and procedures by the officials at the branch level.

5.2 Terrorism Finance :

RBI has been circulating list of terrorist entities notified by the Government of India to banks so that banks may exercise caution if any transaction is detected with such entities. There should be a system at the branch level to ensure that such lists are consulted in order to determine whether a person/organisation involved in a prospective or existing business relationship appears on such a list. The authority to whom banks may report accounts suspected to belong to terrorist entities will be advised by RBI in consultation with Government.

5.3 Internal Audit/Inspection:

- i. An independent evaluation of the controls for identifying high value

transactions should be carried out on a regular basis by the internal audit department in the banks.

- ii. Concurrent/internal auditors must specifically scrutinise and comment on the effectiveness of the measures taken by the branches in adoption of KYC norms and steps towards prevention of money laundering. Such compliance report should be placed before the Audit committee of the Board of banks at quarterly intervals.

5.4 Identification and Reporting of Suspicious Transactions :

Banks should ensure that the branches and Head Offices report transactions of suspicious nature to the appropriate law enforcement authorities designated under the relevant laws governing such activities. There should be well laid down systems for freezing of accounts as directed by such authority and reporting thereof to the Head Office. Being matters of sensitive nature, there must be a quarterly reporting of such aspects and action taken thereon to the Audit committee of the Board or the Board of Directors.

5.5 Adherence to Foreign Contribution Regulation Act (FCRA), 1976

i. Banks should also adhere to the instructions on the provisions of the Foreign Contribution Regulation Act, 1976 cautioning them to open accounts or collect cheques only in favour of associations which are registered under the Act, *ibid* by Government of India. A certificate to the effect that the association is registered with the Government of India should be obtained from the concerned associations at the time of opening of the account or collection of cheques.

- ii. Branches of the banks should be advised to exercise due care to ensure compliance and desist from opening accounts in the name of banned organisations and those without requisite registration.

6. Record Keeping

Financial intermediaries should prepare and maintain documentation on their customer relationships and transactions to meet the requirement of relevant laws and regulations, to enable any transaction effected through them to be reconstructed. In the case of wire transfer transactions, the records of electronic payments and messages must be treated in the same way as other records in support of entries in the account. All financial transactions/records should be retained for at least five years after the transaction has taken place and should be available for perusal and scrutiny of audit functionaries as well as RBI/NABARD as and when required.

7. Training of Staff and Management

It is crucial that all the operating and management staff fully understand the need for strict adherence to KYC norms. All institutions must, therefore,

have an ongoing training programme so that staff are adequately trained for their roles and responsibilities as appropriate to their hierarchical level in complying with anti-money laundering guidelines and for implementing KYC policies consistently.

8. You are advised to put up this circular to the Board of Directors in the ensuing meeting and also bring the guidelines to the notice of your branches/ Controlling Offices and strictly adhere to the instructions on “KYC” norms. These guidelines are issued under Section 35 A of the Banking Regulation Act, 1949 (as applicable to Co-operative societies) and any contravention of the same will attract penalties under the relevant provisions of the Act.

9. Please acknowledge receipt, and advise the steps initiated in compliance with the various guidelines contained in the circular, to the concerned Regional Office of NABARD and RPCD, Reserve Bank of India, within a month from the date of receipt of this circular.

Yours faithfully,

Sd/-
(K. Anantharaman)
General manager
