



THE KASARAGOD CO-OPERATIVE
TOWNBANK
LTD, No.970

COMPLIANCE POLICY

(B Res No. _____ Date _____)

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1. Introduction

As part of its ongoing efforts to address bank supervisory issues and enhance sound practices in banking organizations, Reserve Bank of India in tandem with the recommendations of Basel Committee on Banking Supervision, has issued guidelines on the 'compliance function' in banking organizations. With the advent of the Risk Based Supervision approach, some additional aspects have also been overseen more incisively to cater to the need for tighter compliance in a stricter regime as envisaged by the RBI.

The Compliance Function envisages strict observance of all statutory provisions contained in various legislations such as Banking Regulation Act, Reserve Bank of India Act, Foreign Exchange Management Act, Prevention of Money Laundering Act etc. as well as to ensure observance of other regulatory guidelines issued from time to time; standards and codes prescribed by IBA, FEDAI, FIMMDA, BCSBI etc; and also, bank's internal policies and fair practices code.

Compliance laws, rules and standards generally cover matters such as observing proper standards of market conduct, managing conflicts of interest, treating customers fairly, and ensuring the suitability of customer advice. They also include specific areas such as the prevention of money laundering and terrorist financing and may extend to tax laws that are relevant to the structuring of banking products or customer advice.

Compliance laws, rules and standards have various sources, including primary legislation, rules and standards issued by legislators and supervisors, market conventions, codes of practice promoted by industry associations, and internal codes of conduct applicable to the staff members of the bank will be the important sources for compliance laws, rules and standards. These rules and standards may go beyond what is legally binding.

2. Objective of Compliance Function

The purpose of the compliance function is to assist the bank in managing its compliance risk which can be defined as *"the risk of legal or regulatory sanctions, material financial loss, or loss to reputation a bank may suffer as a result of its failure to comply with laws, regulations, rules, related self-regulatory organization standards, and codes of conduct applicable to its banking activities"*.

Compliance risk is sometimes also referred to as integrity risk, because a bank's reputation is closely connected with its adherence to principles of integrity and fair dealing and embrace broader standards of integrity and ethical conduct.

3. Compliance Function and its relevance in the Bank

The compliance area is critically important in identifying, evaluating and addressing legal and reputational risks. An enterprise-wide compliance program will help the bank to look at and across business lines and activities of the organization as a whole and to consider how activities in one area of the bank may affect the legal and reputational risks of other business lines and the entire enterprise.

An enterprise-wide compliance program will also help the management and the board in understanding where the legal and reputational risks in the organization are concentrated, provide comparisons of the level and changing nature of risks and identify those control processes that most need enhancement.

The compliance function thus aims at ensuring that controls and procedures capture the appropriate information to allow senior management and the board to better perform their risk management functions.

4. Organizational Structure



4.1 Board of Directors

In recognition of the various aspects of the Bank's compliance risk, the Board will approve and annually review this policy. It will ensure that an appropriate compliance policy is always in place to manage compliance risk and also oversee its implementation. Compliance failures if deemed necessary will be placed through the ACB and appropriate remedial measures will be taken. A detailed annual review will be placed to the Board through the ACB in the ensuing quarter. It will also ensure that compliance issues are resolved effectively and expeditiously by senior management with the assistance of compliance staff.

Corporate culture emphasizes standards of honesty and integrity and the board of directors will lead by example. In order to ensure that the activities of the compliance function are subject to independent review, the compliance function and the audit function of the bank will be kept separate.

4.2 Audit Committee of the Board (ACB)

The ACB is given the task of overseeing the implementation of the compliance policy and reviewing the compliance function on a quarterly basis. It will also review compliance failures if any and take appropriate remedial measures.

4.3 Senior Management (MD & CEO)

The bank's Senior Management will be responsible for identifying and managing the compliance risk through all levels of the organization. Whenever breaches are identified Senior Management will take appropriate remedial or disciplinary action. With the assistance of the Compliance Cell the Senior Management will

- at the close of each financial year, assess the main compliance risk issues facing the bank and formulate plans to manage them.
- report to the Board of Directors through ACB on the bank's management of its compliance risk, in such a

manner as to assist Board members to make an informed judgment on whether the bank is managing its compliance risk effectively; and

- report promptly to the Board through ACB any material compliance failure (e.g. failure that may attract a significant risk of legal or regulatory sanctions, material financial loss or loss to reputation).

4.4 Chief Risk Officer

Chief Risk Officer will be responsible for advising the Board and Senior Management on the bank's compliance with applicable laws, rules and standards and keep them informed of developments in the area. He will also help educate staff about compliance issues, act as a contact point within the bank for compliance queries from employees, and provide guidance to staff on the appropriate implementation of applicable laws, rules and standards in the form of policies and procedures and other documents such as compliance manuals, internal codes of conduct and practice guidelines. Co-ordination with departments for ensuring compliance of all regulatory & statutory requirements.

4.5 Chief Compliance Officer

The Chief Compliance Officer (should not be less than the rank of DGM or equivalent) will be the Head of the Compliance Cell. He will be the nodal point of contact between the bank and the regulator and will be a participant in the quarterly informal discussions held with RBI. He will assist the top management in effectively managing the compliance risks faced by the bank. He will have the freedom to call for any report/data from any department or from any senior executive. He will have the overall responsibility for coordinating the identification and management of the bank's compliance risk and supervising the activities of other compliance function staff. He will be a signatory to the 'Product Evaluation Committee' and the policy / procedure formulation for outsourcing contracts in the bank. He will ensure that all new products are subjected to intensive monitoring for the first six months of introduction by the concerned departments and that the indicative parameters of compliance risk are adequately monitored. His functions will be subject to review by ACB/Board at least on yearly basis.

The Chief Compliance Officer will be appointed for a minimum period of three years and during this tenor he may be removed/transferred only with the approval of the Board through the ACB and through an internal administrative procedure in which his negligence in discharging compliance function or his serious acts of omission or commission in financial or administrative matters is established, recorded in a transparent manner. The Reserve Bank of India will also similarly be kept informed of the name, address and contact number of the Chief Compliance Officer as also any change thereof, as and when it takes place.

4.6 Compliance Cell

The Compliance Cell will consist of Chief Risk Officer, Chief Compliance Officer, Assistant General Manager, Compliance Cell and officers of the Cell.

Asst. General Manager, Compliance Cell will coordinate the compliance functions related to identifying, analyzing and reporting compliance risk. For matters related to compliance function, the Asst. General Manager Compliance Cell will report to the Chief Compliance Officer.

5. Functional Requirements of Compliance Cell

The bank's compliance function will be independent. The staff in the Compliance Cell at the Head Office, will primarily focus on compliance functions. The compliance staff may be assigned some other duties without giving room for conflict of interest. Under no circumstances, the compliance staff will be assigned audit/inspection duty as it gives rise to serious conflict of interest.

Apart from the basic qualifications, the Compliance staff will preferably have a fair knowledge of law, accountancy and information technology and also adequate practical experience in various business lines and audit/inspection functions to enable them to carry out their duties effectively.

In order to keep the compliance staff up-to-date with developments in the areas of banking laws, rules and standards, regular and systematic education and training will be given to them. They will be adequately trained in new products and services introduced in the banking industry as well as in the areas of corporate governance, risk management, supervisory practices etc.

Compliance Officers will have access to all information they require and have the right to conduct investigation and report the findings to the Chief Compliance Officer.

The Compliance Cell will be adequately staffed so as to ensure that the department discharges its functions without any resource constraint.

6. Functions and responsibilities of Compliance Cell

The Compliance Cell will

- 6.1 Act as the focal point for receipt and dissemination of all regulatory and internal guidelines/instructions. It will ensure that appropriate instructions get promptly issued within the organization and are actually received at each office and the instructions are implemented. It will also monitor compliance with the regulatory guidelines/instructions.
- 6.2 Play the central role in the area of identifying the level of compliance risk in each business line, products and processes and issue instructions to operational functionaries. Ensure identification of the level of compliance risk in the products and processes of the various business lines. On introduction of new products and processes the compliance risk is assessed and noted under the respective business line.
- 6.3 Advise and assist the senior management on compliance laws, rules and standards. It will provide guidance to staff on the appropriate implementation of compliance laws, rules and standards through policies and procedures and other documents such as compliance manuals, internal codes of conduct and practice guidelines. Provide continuous and mandatory training to all staff of the Bank on compliance aspects and the need to comply with the instructions meticulously along with the disciplinary measures through staff accountability framework / policies for non-compliance, will be imparted so as to promote a compliance culture in the Bank.
- 6.4 To devise a time bound strategy that will ensure RBI AFI RAR/ RMP points are complied within the prescribed periods. To identify compliance failures in the bank using the internal audit and concurrent audit as a feedback mechanism.
- 6.5 Bring to the notice of RBI any discomfort conveyed to the bank on any issue by other regulators.
- 6.6 Monitor/ensure timely submission of regulatory returns by the controlling offices through appropriate mechanism like maintenance of manual calendar and centralized generation of regulatory reports.
- 6.7 Monitor and test compliance by performing sufficient and representative compliance testing and report the results to the senior management. Compliance Risk testing of branches is being conducted based on

the analysis of compliance risk as reflected in the Risk Based Internal Audit (RBIA) report of each branch conducted during the quarter.

- 6.8 Consider ways to measure compliance risk (e.g. by using performance indicators) and use such measures to enhance compliance risk assessment. The process is described under Annexure-II where the methodology in selection of samples and quantity required for compliance testing under the Tranche-III is detailed.
- 6.9 Conduct compliance reviews/investigations, whenever required. The authority to use external experts for the purpose of investigation if required, is left to the discretion of the Chief Compliance Officer.
- 6.10 Place before the Board and circulate to all the functional heads an Annual Report on compliance failures/breaches. Although normal reporting line of Compliance Cell will be to senior management, the Cell will also have the right of direct access to the Board of Directors or to ACB, bypassing normal reporting lines. The reports submitted to the Senior Management, Audit Committee of the Board and Board of Directors is detailed in Annexure-I
- 6.11 Disclose in annual report of the bank non-compliance of any regulatory guidelines and administrative actions taken against the bank along with corrective steps taken to avoid recurrence of the lapses.

7. The Compliance Programme

The responsibilities of the compliance function i.e reporting/review and compliance assessment will be carried out under a compliance programme as mentioned in Annexure-I & II. The compliance programme will be risk-based and subject to oversight by the Chief Compliance Officer to ensure appropriate coverage across businesses and co-ordination among risk management functions. More emphasis for compliance risk will be given in the risk assessment methodology of the Internal Inspection of the branches and audit programme will cover the adequacy and effectiveness of the bank's compliance function including testing of controls commensurate with the perceived level of risk. The activities of compliance function will also be subject to annual review by the Internal Audit conducted by the Bank and under AFI.

In future the bank may choose to carry on business in various jurisdictions for a variety of legitimate reasons. In such cases, it will be ensured that applicable laws and regulations in all such jurisdictions and that the organization and structure of the compliance function and its responsibilities are consistent with local legal and regulatory requirements. It will also be ensured that compliance responsibilities specific to each jurisdiction are carried out by individuals with the appropriate local knowledge and expertise, with oversight from the Chief Compliance Officer in cooperation with the bank's other risk management functions.

The code of conduct for employees envisages working towards earning the trust of the society by dealing with customers in a fair manner and conducting business operations consistent with rules and regulations. Instances of major compliance failures on the part of employees will be reported by the Compliance Cell to the Staff Department for taking appropriate action.

1. Reports from Compliance Cell to MD & CEO

Based on the reports/certificates received from various heads of Departments/Cells/Offices Compliance Cell will identify compliance failures and major failures if any will be reported to MD & CEO.

Name of Report	Contents@	Periodicity**
Monthly Compliance Report to MD & CEO	i) Compliance to statutory provisions, regulatory guidelines, Banks internal policies, systems and procedures ii) Compliance failures, if any during the month and steps taken to avoid recurrence of the failures iii) Consequential losses and regulatory action v) Compliance Risk identified if any	Monthly

**** Will be submitted within 20 days from the close of the month.**

@ Report should include details of compliance failures reported by various Departments and Zonal Offices

2. Reports from Compliance Cell to ACB

Within 30 days from the close of every quarter (June, September, December) a brief report on the compliance position will be placed before the ACB. This report will show a consolidated position of all major items appearing in the monthly reports submitted to MD & CEO.

Name of Report	Contents	Periodicity \$
Quarterly Compliance Report to ACB	i) Compliance of all statutory provisions, regulatory guidelines, including Banks internal policies ii) Compliance failures, if any during the quarter and Steps taken to avoid recurrence of the failures, iii) Consequential losses and regulatory action iv) Compliance Risk identified if any	(June, September, and December)

\$ As there is a yearly return in the month of March from the Compliance Cell to the Board through ACB, the Cell need not submit a separate quarterly return for the quarter ending March.

3. Reports from Compliance Cell to Board through ACB

Name of the Report	Contents	Periodicity ^
Annual Compliance Report to Board	<p>i) Compliance failures, if any during the preceding year and consequential losses and regulatory actions as also steps taken to avoid recurrence of the same.</p> <p>ii) Compliance with fair practices codes and adherence to standards set by self- regulatory bodies and accounting standards.</p> <p>iii) System of internal control to minimize compliance risk.</p> <p>iv) Compliance Risk identified if any</p> <p>v) Penalties imposed and Penal action taken against the Bank under various Laws & Statutes</p> <p>vi) List of all major regulatory guidelines issued during the preceding year and steps taken by the bank to ensure compliance</p> <p>vii) Independence of compliance function</p> <p>viii) Progress in rectification of significant deficiencies pointed out in the internal audit, statutory audit and RBI inspection reports and position of implementation of recommendations made therein.</p> <p>ix) Strategy for the next year including restructuring of Compliance Cell,, if necessary, posting/transfer/training of staff</p>	Yearly (As on 31st March every year.)

[^] Will be submitted within 40 days from close of the year.

CHIEF EXECUTIVE OFFICER

DIRECTOR

DIRECTOR

CHAIRMAN