SWIFT [UPSC Notes for GS III]

SWIFT (Society for Worldwide Interbank Financial Telecommunication)

Context: RBI had been warning lenders on possible misuse of Society for Worldwide Interbank Financial Telecommunication (SWIFT); it has finally fined 36 banks for negligence.

What is SWIFT?

- SWIFT is the global messaging software and is headquartered in Brussels, Belgium. It is a global member-owned cooperative that.
- It allows financial entities to send and receive messages about financial transactions in a secure, standardised and reliable environment.
- It was founded in 1973 to develop a secure electronic messaging service and common standards to facilitate cross-border payments.
- The messages are encrypted to protect confidentiality.

Details:

- It was much before the Punjab National Bank Scam in 2018 that the RBI cautioned the banks about the possible misuse of the SWIFT infrastructure and directed them to implement safeguards.
- Despite repeated warnings by the RBI, the PNB fraud happened. Even after the PNB scam banks failed to wake up and as a result, the RBI had to impose monetary penalty on 36 banks for failing to implement the safeguard which was mainly to integrate the SWIFT infrastructure with Core Banking Solution (CBS) within a time frame.
- The Banking Regulation Act gives power to the RBI to impose a maximum penalty of Rs. 1 crore for a single breach.
- In 2017 under former RBI Governor Urjit Patel, the RBI had set up an enforcement department to centrally speed up regulatory compliance.
- The goal was to split up those who oversaw possible breaches of rule and those who decided on penalising actions so that the enforcement process functioned in a fair manner and was based on evidence.

SWIFT and Its importance in India

The SWIFT is a secure financial message carrier which can avoid fraudulent transactions. In other words, it transports messages from one bank to another bank. Its core role is to provide a secure transmission channel so that the message from Bank A reaches the Bank B only. Bank B, in turn, knows that Bank A, and no one other than Bank A, sent, read or altered the message en route. Banks, needless to say, should have checks in place before actually sending messages. One of its biggest failures in the PNB case was the missing link between SWIFT and the bank's backend software. This allowed fraudulent to use letters of understanding or a loan request to another bank through the SWIFT network to transfer funds.

RBI Circular:

- It was an outcome of PNB scam. It was believed that the scam is mainly due to people and process failure not so much a technology failure.
- Though there was some technology tweaking that the banks had to do, the guidelines were mainly about people and process.

Conclusion:

- There are speculations that the RBI action may not go down well with the global intergovernmental agency Financial Action Task Force (FATF) during the country assessment.
- Currently, the 4th round of assessment is going on and India would mostly be assessed soon.
- The FATF reviews anti-money laundering, combating the financing of terrorism policies of countries, the compliance of financial institutions of these countries and the supervisory effectiveness in enforcing them.
- Questions could be raised as to why banks are so reluctant to comply with regulatory directions on an important issue such as international wire transfer mechanism.
- Queries may also be raised as to why the regulator was unable to make lenders comply with its directions in a time-bound manner and as to what steps the regulator is taking so that such incidents do not recur.