Small Finance Bank

Why in News

Recently, the **Reserve Bank of India (RBI)** has received applications from two more entities under the **"on-tap" small finance bank licensing guidelines** of 2019.

> An "on-tap" facility would mean the RBI will **accept applications** and grant licences for banks **throughout the year.**

Key Points

- **About:**
    - These are the **financial institutions** which provide **financial services** to the **unserved** and **unbanked region** of the country.
    - Registered as **a public limited company** under the **Companies Act, 2013.**
    - Needs to open **at least 25% of its banking outlets** in **unbanked rural centres.**
    - Required to **extend 75% of its adjusted net bank credit** to the **Priority Sector Lending (PSL).**
        - The RBI mandates banks to lend a certain portion of their funds to specified sectors, like agriculture, Micro, Small and Medium Enterprises (MSMEs), export credit, education, housing, social infrastructure, renewable energy among others.
    - At least **50% of its loan portfolio** should constitute **loans and advances of up to Rs. 25 lakhs.**
    - The **maximum loan size and investment limit** exposure to a single and group debtor would be restricted to 10% and 15% of its capital funds, respectively. They **cannot extend large loans.**
    - If the **initial shareholding by promoters** in the bank is in excess of 40% of paid-up voting equity capital, it should be brought down to 40% within a period of 5 years.
    - Subject to **Cash Reserve Ratio (CRR)** and **Statutory Liquidity Ratio (SLR)** requirements.
        - Banks are required to hold a certain proportion of their deposits in the form of cash known as the CRR.
            - This **minimum ratio** (that is the part of the total deposits to be held as cash) is stipulated by the RBI.
        - The share of **Net Demand and Time Liabilities** that a bank is required to maintain safe and liquid assets, such as government securities, cash, and gold is termed as SLR.
- **Eligibility for Setting up SFBs:**
    - **Resident individuals/professionals** with 10 years of experience in banking and finance.
    - The companies and societies owned and controlled by residents.
    - **Existing Non-Banking Finance Companies (NBFCs), Micro Finance Institutions (MFIs), Local Area Banks (LABs)** and payment banks that are owned and controlled by residents.

- **Activities:**
  - Primarily undertake **basic banking activities** of acceptance of deposits and lending to unserved and underserved sections including small business units, small and marginal farmers, micro and small industries and unorganised sector entities.
  - Undertake other **non-risk sharing simple financial services** activities such as the distribution of mutual fund units, insurance products, pension products, etc. with the prior approval of the RBI.
- **Regulations:**
  - SFBs are governed by the provisions of the:
  - **Reserve Bank of India Act, 1934;**
  - Banking Regulation Act, 1949;
  - Foreign Exchange Management Act, 1999;
  - Payment and Settlement Systems Act, 2007;
  - Credit Information Companies (Regulation) Act, 2005;
  - Deposit Insurance and Credit Guarantee Corporation Act, 1961;
  - Other relevant Statutes and the Directives issued by the **Reserve Bank of India (RBI)** and other regulators from time to time.
- **Guidelines for 'on-tap' Licencing:**
  - **Capital Requirement:** The minimum paid-up voting equity capital / net worth requirement shall be Rs. 200 crores.
    - **For Primary (Urban) Co-operative Banks (UCBs),** desirous of voluntarily transiting into SFBs, initial requirement of net worth shall be at Rs. 100 crores, which will have to be increased to Rs. 200 crores within 5 years from the date of commencement of business.
  - **Scheduled Bank status to SFBs:** SFBs will be given scheduled bank status immediately upon commencement of operations.
  - **Payments Banks Conversion to SFBs:** The **payment banks** can apply for conversion into SFB after 5 years of operations if they are otherwise eligible as per these guidelines.

Scheduled Banks

- Scheduled banks are banks that are **listed in the 2nd schedule of the Reserve Bank of India Act, 1934.**
- The bank's paid-up capital and raised funds **must be at least Rs. 5 lakh** to qualify as a scheduled bank.
- Scheduled banks are **liable for low-interest loans from the Reserve Bank of India** and membership in clearinghouses.
- All commercial banks, including nationalized, international, cooperative, and regional rural banks, fall under scheduled banks.

Source: TH