



Cooperative Banks

For Prelims: Urban Cooperative Banks, recent Developments, National Federation of Urban Cooperative Banks and Credit Societies, Multi-State Cooperative Societies Act, 2002

For Mains: Features of Cooperative Banks and Challenges

Why in News?

Recently, the Minister of Home Affairs and Cooperation has addressed a conclave, organised by the National Federation of Urban Cooperative Banks and Credit Societies (NAFCUB), emphasising the needed Reforms for [Urban Cooperative Banks \(UCB\)](#).

- The NAFCUB is an **Apex Level Promotional body of Urban Cooperative Banks** and Credit Societies Ltd. in the Country. Its objective is **to promote the urban cooperative credit movement and protect the interest of the Sector.**

What are the Cooperative Banks?

- **About:**
 - It is an institution **established on a cooperative basis to deal with the ordinary banking business**. Cooperative banks are **founded by collecting funds through shares, accepting deposits, and granting loans**.
 - They are **Cooperative credit societies** where members from a community group together to extend loans to each other, at favorable terms.
 - They are registered under the **Cooperative Societies Act of the State** concerned or the [Multi-State Cooperative Societies Act, 2002](#).
 - The Co-operative banks **are governed by the,**
 - [Banking Regulations Act, 1949](#).
 - **Banking Laws (Co-operative Societies) Act, 1955.**
 - They are broadly divided into **Urban and Rural cooperative banks**.
- **Features:**
 - **Customer Owned Entities:** Co-operative bank **members are both customer and owner of the bank**.
 - **Democratic Member Control:** These banks are **owned and controlled by the members, who democratically elect a board of directors**. Members usually have equal voting rights, according to the cooperative principle of “one person, one vote”.
 - **Profit Allocation:** A significant part of the yearly profit, benefits or surplus is usually allocated to constitute reserves and a part of this profit can also be distributed to the co-operative members, with legal and statutory limitations.
 - **Financial Inclusion:** They have played a significant role in the financial inclusion of unbanked rural masses. They provide cheap credit to masses in rural areas.
- **Urban Cooperative banks (UCB):**
 - The term Urban Cooperative Banks (UCBs) is not formally defined but refers to primary cooperative banks **located in urban and semi-urban areas**.

- The Urban Cooperative Banks (UCBs), the Primary Agricultural Credit Societies (PACS), the Regional Rural Banks (RRBs), and Local Area Banks (LABs) could be **considered as differentiated banks as they operate in localized areas.**
- Till 1996, these banks were allowed to lend money only for non-agricultural purposes. This distinction does not hold today.
- These banks were **traditionally centred on communities and local workgroups as they essentially lent to small borrowers and businesses.** Today, their scope of operations has widened considerably.

What are the Challenges Faced by the Cooperative Banks?

- **Changing Trends in Financial Sector:**
 - Changes in the financial sector and evolving microfinance, FinTech companies, payment gateways, social platforms, [e-commerce companies](#), and [Non-Banking Financial Companies \(NBFCs\)](#) challenge the continued presence of the UCBs, which are **mostly small in size, lack professional management**, and have geographically less diversified operations.
- **Dual Control:**
 - The UCBs were **under dual regulation by the state registrar of societies and the RBI.**
 - But in 2020, all UCBs and multi-state cooperatives were brought under the supervision of RBI.
- **Money Laundering and Corruption:**
 - Cooperatives have also become avenues for **regulatory arbitrage, circumventing lending and anti-money laundering regulations.**
 - Investigations into the case of [Punjab and Maharashtra Cooperative \(PMC\) Bank](#) scam have **shown gross financial mismanagement** and a complete breakdown of internal control mechanisms.
- **Declining of Agricultural Lending:**
 - The RBI report noted that despite **a crucial role played by the sector, its share in total agricultural lending diminished** considerably over the years, from as high as 64 % in 1992-93 to just 11.3 % in 2019-20.
- **Unfair Audit:**
 - It is well known that **audits are done entirely by department officials & are neither regular nor comprehensive.** Delays in the conduct of audits and submission of reports are widespread.
- **Government Interference:**
 - Right from the beginning the government has adopted an attitude of patronizing the movement. Cooperative **institutions were treated as if these were part & parcel of the administrative set up of the government.**
- **Limited Coverage:**
 - The size of these societies has been very small. Most of these societies are confined to a few members and their operations extended to only one or two villages. as a result their resources remain limited, which make it impossible for them to expand their means and extend their area of operations.

What are the Recent Developments?

- In January 2020, the RBI revised the [Supervisory action Framework \(SAF\)](#) for UCBs.
- In June 2020, the Central government approved an Ordinance to bring all urban and multi-state cooperative banks **under the direct supervision of RBI.**
- In 2021 RBI appointed a committee that suggested [4 tier structure for the UCBs.](#)
 - **Tier 1** with all unit UCBs and salary earner's UCBs (irrespective of deposit size) and all other UCBs having deposits up to Rs 100 crore.
 - **Tier 2** with UCBs of deposits between Rs 100 crore and Rs 1,000 crore,
 - **Tier 3** with UCBs of deposits between Rs 1,000 crore and Rs 10,000 crore and
 - **Tier 4** with UCBs of deposits more than Rs 10,000 crore.

Way Forward

- The establishment of the **country's dedicated Ministry of Cooperation would be a crucial moment** for the history of the cooperative movement.
- The RBI should interpret the Act's provisions so that they do not disrupt UCBs and people's faith is restored in the cooperative banking system.
- There is a need to undertake institutional reforms like **transparency in recruitment and implementation of a robust accounting system**, which are necessary for their growth.
- There is a need to bring in new people, young people and professionals in managerial roles, who will take cooperative forward.
- NAFCUB needs to focus more on the Urban Credit Cooperative Societies particularly on their accounting software and their common bylaws.
- Having a good Urban Cooperative Bank in every town is the need of the hour and country. NAFCUB should not only take up the problems of cooperative banks and solve them **but at the same time should also work better for Symmetrical Development**.

UPSC Civil Services Examination, Previous Year Question (PYQ)

Q. With reference to 'Urban Cooperative Banks' in India, consider the following statements:

1. They are supervised and regulated by local boards set up by the State Governments.
2. They can issue equity shares and preference shares.
3. They were brought under the purview of the Banking Regulation Act, 1949 through an Amendment in 1966.

Which of the statements given above is/are correct?

- (a) 1 only
- (b) 2 and 3 only
- (c) 1 and 3 only
- (d) 1, 2 and 3

Ans: (b)

Exp:

- Co-operative banks are financial entities which belong to its members, who are at the same time the owners and the customers of their bank. They are established by State laws.
- Co-operative banks in India are registered under the Cooperative Societies Act. They are also regulated by the RBI and governed by Banking Regulations Act, 1949 and Banking Laws (Co-operative Societies) Act, 1955.
- Cooperative banks lend as well as accept deposits. They are established with the aim of funding agriculture and allied activities and financing village and cottage industries. National Bank for Agriculture and Rural Development (NABARD) is the apex body of cooperative banks in India.
- Urban Co-operative Banks (UCB) are **regulated and supervised by State Registrars of Co-operative Societies (RCS)** in case of single-state co-operative banks and Central Registrar of Co-operative Societies (CRCS) in case of multi-state co-operative banks and by the RBI. Hence, statement 1 is not correct.
- The **Reserve Bank of India came out with draft guidelines allowing primary UCBs** to augment capital through issuance of equity shares, preference shares and debt instruments.
- The UCBs could raise share capital by issue of equity to persons within their area of operation enrolled as members and also through additional equity shares to the existing members. **Hence, statement 2 is correct.** Therefore, option (b) is the correct answer.
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 - The UCBs **could raise share capital by issue of equity to persons** within their area of operation enrolled as members and also through additional equity shares to the existing members. Hence, statement 2 is correct. Therefore, option (b) is the correct answer.

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