



Governance in Urban Cooperative Banks

For Prelims: [Reserve Bank of India \(RBI\)](#), [Urban Cooperative Banks](#), [Non-Performing Assets](#)

For Mains: Features of Cooperative Banks and Challenges

Source: [TH](#)

Why in News?

Recently, the Governor of the [Reserve Bank of India \(RBI\)](#) addressed concerns regarding [Urban Cooperative Banks \(UCBs\)](#) and emphasized the need to **bolster their governance**.

- While the UCB sector has shown overall financial improvement, **individual entities face vulnerabilities** that must be addressed to ensure the sector's stability.

What are the Concerns Regarding Urban Cooperative Banks (UCBs)?

- **Financial Vulnerabilities:**
 - Some urban cooperative banks (UCBs) face financial vulnerabilities, such as **low capitalization, high levels of [non-performing assets \(NPAs\)](#), or insufficient reserves**, which indicate potential instability.
- **Governance Issues:**
 - Inadequate robust governance practices can hinder a **UCB's overall performance and integrity**.
 - Poor governance may lead to **mismanagement, non-compliance, or ethical concerns within the bank**.
- **Compliance Challenges:**
 - Compliance issues suggest that certain UCBs may **struggle to meet regulatory and legal requirements**.
 - Non-compliance can result in penalties, legal issues, and reputational damage.
- **Risk Management:**
 - Concerns exist about the ability of some UCBs to effectively **identify, assess, and manage various risks**.
 - Risk management deficiencies can lead to unexpected financial losses or operational disruptions.
 - **Credit Risk:**
 - UCBs may need to improve credit risk management practices. This includes issues related to **loan underwriting standards, monitoring of borrower performance, and handling non-performing loans**.
 - **Liquidity Risk:**
 - Inadequate liquidity management can lead to difficulties in meeting financial obligations.
- **IT Infrastructure and Cybersecurity:**
 - UCBs must establish **robust IT infrastructure and [cybersecurity](#)** measures to protect

sensitive data and systems.

What are the RBI's Recommendations for UCBs?

- The RBI directed the directors of UCBs to strengthen their governance practices, especially the three supporting pillars of **compliance, risk management, and internal audit**.
- The RBI urged the boards to be more proactive in **Asset Liability Management** and the necessity of managing liquidity risk in a more systematic manner.
- On the functioning of the boards, the RBI emphasised five aspects - **adequate skills and expertise of directors, the constitution of a professional board of management, diversity, and tenure of board members, transparent and participatory nature of board discussions, and effective functioning of board-level Committees**.
- The RBI cautioned them **against using innovative accounting practices** to camouflage their actual financial position.
 - The RBI encouraged them to adopt appropriate business strategies and explore **suitable technology solutions to sustain and grow their business and serve their customers**.

What are Urban Cooperative Banks (UCBs)?

- Co-operative Banks, which are distinct from commercial banks, were born out of the concept of **co-operative credit societies where members from a community group together to extend loans to each other, at favorable terms**.
- Co-operative Banks are broadly classified into **Urban and Rural co-operative banks based on their region of operation**.
- UCBs 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.
 - But in 2020, **all UCBs and multi-state cooperatives were brought under the supervision of RBI**.
- In 2021 RBI appointed a committee that suggested a 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.
- As of **March 2021, there are about 1,539 UCBs in India**. The deposit base of UCBs stood at Rs 5 lakh crore as of March 2020 and advances over Rs 3 Lakh crore.
 - Despite their large numbers, **UCBs' market share in the banking sector was low and declining at around 3%**. They accounted for **3.24% of deposits and 2.69% of advances**.

UPSC Civil Services Examination, Previous Year Question (PYQ)

Prelims:

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 banking related functions such as issue of license to start new banks/branches, matters relating to interest rates, loan policies, investments and prudential exposure norms are regulated and supervised by the Reserve Bank under the provisions of the Banking Regulation Act, 1949 after an amendment in 1966. **Hence, statement 3 is 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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