Welcome Clarity

Why in news?

RBI has decided to amend the ownership and control norms for private banks.

How RBI streamline licensing, ownership and control norms for private banks so far?

- **Ownership -** The minimum capital has been pegged at INR 500 crore.
- Promoters must have sound credentials and integrity and with a successful track record of 10 years.
- **Control Norms -** RBI present regulations on ownership structure and shareholding appear quite conflicted.
- **Anomaly -** It is not known whether it prefers promoter to invest more in private banks to ensure good governance or favours widely dispersed shareholding to check promoter influence.
- Present regulations try to do a bit of both.
- It mandates that private bank promoters hold at least a 40 % equity stake in the first 5 years
- Overtime RBI dilute their voting rights to below 20 % and 15 % within 10 and 15 years, respectively.
- Private banks promoted at different times are subject to different rules, leading to some promoters using non-equity routes to infuse capital and others legally challenging the regulator on the inconsistency of its rules.
- The RBI's decision to selectively adopt the recommendations of its Internal Working Group (IWG) is a welcome reform move.

Why the reforms suggested by IWG of RBI seem welcoming?

- **Ownership** - The RBI insisted a 10-year track record and initial capital requirement of Rs 1,000 crore (instead of Rs 500 crore) for aspirants to universal bank licences.
- This will help **weed out non-serious players** and allow only entities with sufficient fund-raising ability into the fray.
- **Control Norms -** It requires all private bank promoters to hold a minimum 40 % equity stake in the first 5 years
- It will be reduced to 26 per cent within 15 years.

- It makes promoters invest more thereby **facilitating timely equity infusions for stressed banks.**
- But to ensure that individuals don't exercise undue influence over lending decisions, high promoter stakes may need to be counter-balanced by stronger bank boards and compliance functions.

Does RBI allow large corporate, industrial houses and NBFCs to setup banks?

- RBI hasn't taken a call on this. The regulator may not be wrong.
- Most banking frauds in India have had their origins in connected lending and diversion of funds to group entities.
- Reason being internal checks such as statutory audits and external checks such as RBI's supervisory mechanism, have so far proved unequal to detecting such cases early.
- Having recently taken on the oversight of co-operative banks, small finance banks and proliferating digital lenders in addition to legacy universal banks, the RBI today has its hands full in terms of regulatory capacity.
- It shows that RBI pragmatically wants to set its own house in order, before inviting unknown entities into it.

Reference

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