Annexure - XIV

(Paragraph - 6.9)

Note of dissent recorded by Dr. M.L. Abhyankar, Member, HPC

On Compliance of Capital Adequacy Norms:

1. One of the terms of reference before the High Power Committee says that whether the UCBs should be subject to capital adequacy norms and if so, what norms should be prescribed to them. I am of the opinion that an UCB being a financial institution no compromise on capital adequacy norms vis-a-vis commercial banks can be prescribed for UCBs. This means the UCBs- at least stronger ones - should be subject to the same capital adequacy norms as applicable to commercial banks. Only a little more period should be given to them to achieve the first stage of 8%.

2. However, I am slightly in disagreement with the HPC regarding new avenues of collecting share capital by UCBs. That the strong UCBs be permitted to raise subordinate debts such as bonds, debentures (which may contribute to Tier II capital) has been unanimously accepted by the HPC. But the fact is that all UCBs - large or small - will not be able to go looking to respective UCBs financial strength for subordinate debt instruments. Hence I am of the view that as a uniform method all UCBs should be allowed (by making suitable changes in the Banking Regulation Act and also in Co-operative Societies Act) to issue non-voting shares - a new class of shareholders. At present, the shares of UCBs are to be returned to bank in case of resignation by a member. The bank is bound to buy back such shares at its face value only. Another feature of UCBs is that the share capital of the UCBs is always open-ended. This means that whenever a fresh loan is disbursed then corresponding linked shares are to be allotted to the borrower in keeping with the directives of the RBI. Thus the financial strength and stability of a particular UCB is never reflected at present in buying an selling of its shares.

3. Since last 5-6 years, the thinkers and workers in urban cooperative banking movement are suggesting the issue of such non-voting shares. These non-voting shares can be of a fixed total amount i.e. they will then not remain open-ended. These shares should be permitted to be traded easily in the stock exchange or any suitable common platform. The buying and selling price of such non-voting shares shall be automatically determined as per market forces i.e. financial strength such as earning per share, book value etc. in case of respective UCBs. if this is permitted, then and then only the investing public will be attracted for investment in shares of UCBs. These investors shall never be interested in exercising their rights in the management of the institution and, therefore, they can easily be attracted to such shares, although they carry no voting rights. Further, when this avenue is made open to all UCBs, the individual UCBs will naturally try to improve their management and financial performance in order to keep up the price of their non-voting shares in the investors' market.

Whether any ceiling on the value of Individual Share Holding in Urban Co-operative Banks be imposed ? (Para 6.8)

I am of the firm opinion that there should not be any ceiling on the value of individual share holding i.e. the total value of shares that can be held by a person in any Urban Co-operative Bank (UCB). The reasons for this argument are as below :

1. As per Reserve Bank's every old directive, there is a practice of share linking for all borrowers of UCBs. In cases of unsecured loans, the share linking is limited to 5% of the loan amount whereas in cases of secured loans, share linking is limited to 2.5% of the loan amount. The banks maximum loaning limit to a single party which is commonly known as 'exposure limit' depends on a fixed formula prescribed by RBI from time to time. In practice many UCBs are having the exposure limit ranging from Rs.1 crore to Rs.20 crores. If 2.5% share linking is to be applied to a loan of say Rs.20 crores, it will work out to Rs.50 lacs. But if any arbitrary and unrealistic limit is fixed for individual share holding (for example Rs.5 lacs) then the share linking shall not be applicable effectively to loans beyond Rs.2 crores. This means either the amount of the loan will have to be kept limited to Rs.2 crores or the loans can be given but the corresponding contribution to share capital of the UCB will not be available. This would not be only self-contradictory but also would lead to violation of RBI directives regarding share linking. Further, because the UCBs can neither go to the market for sale of their shares, nor the shares of UCBs can be purchased and sold in the stock exchanges, the only avenue left to the UCBs to achieve capital adequacy norms is linking of shares to borrowing. Hence any idea or effort of limiting the value of individual share holding will lead to definite destablising of many UCBs and also will depress the morale of workers in urban co-operative banking movement.

2. The history and evolution of co-operative legislations - both in the States as well as at the Centre - show that over a period of time, the restrictions on the value of individual share holding were being gradually removed (and in a State like Maharashtra, this limit has recently been increased to Rs.1 lakh per person). Again, in the Central Co-operative Societies Act, at present, there is no limit whatsoever on the value of individual share holding (excepting that of 20% of the total subscribed share capital). All the UCBs have struggled for last many years for removal of any artificial and arbitrary ceiling on the value of individual share holding they are at least successfully in case of Central Co-operative Societies Act, whereas in the respective State legislation these limits are being increased. This means that when the liberalisation is already on its way, it will be a 'about turn' to think of putting any limit on value of individual share holding and hence it will be opposed by all UCBs.

3. The Reserve Bank of India is also of very firm opinion till recently with this only avenue for UCBs to raise their share capital being such linkage of shares with the loan amounts. Hence the Urban Banks Department of RBI has in December, 1996 issued a circular letter requesting the Registrars of Co-operative Societies in all the State in India to either remove the ceiling and pending amendments in their State Co-operative Acts to that effect at least to increase it upto Rs.5 lakhs in order to enable UCBs to raise their share capital. The RBI should not therefore renege on its earlier stand of liberalisation of the ceiling on value of individual share holding in UCBs.

4. The advocates of putting certain ceiling on the value of individual share holding in UCBs maintain that the existing limit of 20% of the subscribed share capital appears to be too high and a single person holding upto 20% of the total subscribed share capital appears to be quite large and therefore unreasonable. But it is rather difficult to understand what is the exact fear or danger. In case of limited companies including commercial banks, the danger of take-over of the bank or the single person dominating the affairs of the company is certainly undesirable; but as per the co-operative principle of - 'one person - one vote' i.e. irrespective of the no. of shares held it will not allow at any time such take over or the danger of dominating the management of the society. Hence a comparison of an UCBs with a commercial bank or a company is not only untenable but also disastrous.