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# RBI Revives On-Tap Urban Cooperative Bank Licensing to Strengthen Cooperative Banking Governance and Financial Stability

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## Recent Developments:

- **The Reserve Bank of India (RBI)** has proposed resuming **'on-tap' licensing** for **Urban Cooperative Banks (UCBs)** after a gap of more than **two decades**, and released **draft guidelines** for stakeholder consultation during the **August 2026 Monetary Policy Committee (MPC)** meeting.
- Fresh UCB licensing had remained suspended since **2004** after the **1993–2001 liberalised licensing regime** resulted in rapid expansion, governance deficiencies and financial stress in several cooperative banks.
- The RBI has simultaneously proposed reforms in the **Marginal Cost of Funds Based Lending Rate (MCLR)** and **External Benchmark Lending Rate (EBLR)** frameworks to improve transparency, standardise lending practices and strengthen monetary policy transmission.

## Urban Cooperative Banks (UCBs):

### *Meaning:*

- **Urban Cooperative Banks (UCBs)** are cooperative banking institutions operating primarily in **urban and semi-urban areas**, providing banking and credit services to **small borrowers, Micro, Small and Medium Enterprises (MSMEs), self-employed persons and retail customers**.
- UCBs function on **cooperative principles**, where members are both **owners and customers** of the institution.

### *Legal Status, Regulation:*

- UCBs are regulated by the **Reserve Bank of India (RBI)** under the **Banking Regulation Act, 1949** (as applicable to cooperative societies).
- **Managerial, administrative and incorporation-related matters** are governed by the respective **Registrar of Cooperative Societies (RCS)** or the **Central Registrar of Cooperative Societies (CRCS)** under the cooperative laws.
- The **Banking Regulation (Amendment) Act, 2020** significantly strengthened the **RBI's regulatory, supervisory and resolution powers** over cooperative banks while preserving their cooperative character.
- UCBs are regulated under a **dual regulatory framework**, where banking functions are supervised by the RBI and cooperative management is supervised by the respective cooperative registrars.

### *Capital Raising:*

- UCBs are permitted to issue **equity shares** and **preference shares** for capital augmentation, subject to prior approval and regulatory guidelines issued by the RBI.

***Current Status:***

- India has **1,457 Urban Cooperative Banks**, according to the **Reserve Bank of India (RBI)** and the **National Bank for Agriculture and Rural Development (NABARD)**.

**Need for Resuming UCB Licensing:**

***Background:***

- Between **1993 and 2001**, the RBI followed a **liberalised licensing policy**, resulting in rapid growth in the number of UCBs.
- Weak governance standards, inadequate capital, poor risk management and rising non-performing assets led to financial instability in several cooperative banks.
- Consequently, the RBI suspended fresh licensing in **2004** and focused on consolidation, stronger regulation and supervisory reforms.
- The proposed framework reflects greater regulatory confidence following governance reforms and improved supervisory mechanisms.

**Key Highlights of RBI Draft Guidelines:**

***Operational Eligibility:***

- Only **Credit Cooperative Societies** with a minimum operational history of **10 years** are eligible to apply for conversion into an Urban Cooperative Bank.

***Capital Requirements:***

- Applicants must maintain a **minimum deposit base of ?10,000 crore**.
- Applicants must possess a **minimum net worth of ?300 crore**, based on audited financial statements as on **31 March** of the preceding financial year.

***Financial Soundness:***

- Applicants must maintain a **Capital to Risk-Weighted Assets Ratio (CRAR)** of at least **12%** at the time of licensing.
- The **Net Non-Performing Assets (Net NPA)** ratio must not exceed **3%**.

***Geographical Presence:***

- The RBI proposes to prioritise societies registered under the **Multi-State Cooperative Societies Act, 2002**.
- Preference will be given to institutions operating across **multiple States** to improve business diversification, governance standards and financial resilience.

***Licensing Approach:***

- The proposed **'on-tap' licensing system** will permit eligible entities to apply throughout the year instead of waiting for specific licensing windows.
- Draft guidelines have been released for **public consultation** before finalisation.

**Interest Rate Framework Reforms:**

***Rationalisation of Lending Rates:***

- The RBI has proposed a comprehensive review of the **Marginal Cost of Funds Based Lending Rate (MCLR)** and **External Benchmark Lending Rate (EBLR)** frameworks.

***Objectives:***

- Standardise **interest computation methodologies** across regulated entities.
- Harmonise **benchmark reset frequencies** for floating-rate loans.
- Improve **transparency**, **consumer protection** and **comparability** of lending rates.
- Strengthen **monetary policy transmission**, ensuring policy rate changes are reflected more efficiently in lending rates.

***Expected Benefits:***

- Greater uniformity in loan pricing across banks.
- Faster transmission of changes in the **Repo Rate** to borrowers.
- Improved transparency and reduction in hidden pricing variations.
- Enhanced protection for retail borrowers through predictable benchmark revisions.

**Tier-Based Regulatory Framework for UCBs:**

***Background:***

- Since **2022**, the RBI has adopted a **four-tier regulatory framework** for UCBs based on deposit size to enable **proportionate regulation**, strengthen financial resilience and improve supervisory effectiveness.

***Tier-I:***

- Includes **Unit UCBs**, **Salary Earners' UCBs** irrespective of deposit size and all other UCBs with deposits up to **?100 crore**.

***Tier-II:***

- Includes UCBs having deposits above **?100 crore** and up to **?1,000 crore**.

***Tier-III:***

- Includes UCBs having deposits above **?1,000 crore** and up to **?10,000 crore**.

***Tier-IV:***

- Includes UCBs with deposits exceeding **?10,000 crore**.

**Significance of the Reforms:**

***Financial Inclusion:***

- Expansion of well-governed UCBs can improve access to formal banking services for **small businesses, MSMEs, traders and middle-income households**.

***Strengthened Cooperative Banking:***

- Higher eligibility standards are expected to improve governance, financial discipline and depositor confidence.

**Kamaraj IAS Academy**
Plot A P.127, AF block, 6 th street, 11th Main Rd, Shanthi Colony, Anna Nagar, Chennai, Tamil Nadu 600040
Phone: **044 4353 9988 / 98403 94477** / Whatsapp : **09710729833**

***Improved Risk Management:***

- Strict capital adequacy and asset quality norms reduce the probability of future cooperative bank failures.

***Better Monetary Policy Transmission:***

- Rationalised lending benchmarks improve the effectiveness of the RBI's monetary policy decisions across the banking system.

***Enhanced Consumer Protection:***

- Uniform interest rate practices reduce information asymmetry and improve borrower awareness.

**Challenges Associated with UCBs:**

***Governance Issues:***

- Political interference, weak board oversight and limited professional management continue to affect some cooperative banks.

***Dual Regulation:***

- Shared regulatory responsibilities between the **RBI** and **Registrar of Cooperative Societies (RCS)** may create coordination challenges.

***Technology Adoption:***

- Smaller UCBs often face constraints in adopting advanced digital banking infrastructure and cybersecurity systems.

***Capital Constraints:***

- Cooperative ownership structures restrict capital mobilisation compared with commercial banks.

**UPSC Value Addition:**

***Important Committees:***

- **Madhava Das Committee (1978):** Recommended strengthening the cooperative banking structure.
- **High Powered Committee on Urban Cooperative Banks (2001):** Recommended consolidation, improved governance and stronger prudential regulation.
- **Expert Committee on UCBs (2021):** Recommended the **four-tier regulatory framework**, differentiated regulation and enhanced capital standards.

***Related Legislations:***

- **Banking Regulation Act, 1949**
- **Banking Regulation (Amendment) Act, 2020**
- **Multi-State Cooperative Societies Act, 2002**