

CHAPTER - I

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INTRODUCTION AND METHODOLOGY

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In this Chapter is given (A) Introduction to the subject of this study, and (B) Methodology followed for the study.

**A) Introduction.**

Urban Co-operative Banks operate mainly in urban and semi-urban areas in the country. They mobilise savings from the people in their areas of operation and provide credit facilities to their members who belong to economically lower strata.

There is no difference so far as banking functions are concerned between urban co-operative Banks and commercial Banks. However, urban co-operative Banks being users-organizations are compact organizations so far the area of operation is concerned. Urban co-operative Banks are wedded to the social objectives with a strong sense of social purpose. These Banks have democratic management and a predominantly democratic character which are the essence of co-operation.

A Study Group on Credit Co-operatives in the Non-Agricultural Sector (1963) under the Chairmanship of Shri.V.P.Varde, appointed by the Government of India, suggested certain norms and recommended that the urban co-operative Banks should have a minimum paid-up share capital of Rs.50,000.00 and those undertaking the provision of banking facilities should be termed as 'Urban Co-operative Banks'.

The Committee pointed out the need for establishing new urban co-operative Banks and extending their membership, making the Banks economically viable, diversifying their loan portfolio and for ensuring enhanced financial assistance from them to the small industrialists and artisans.

Extension of Banking Regulation Act, 1949.

With effect from 1st March 1966, certain provisions of the Banking Regulation Act, 1949, were extended to co-operative Banks.

An urban co-operative Bank is called a primary co-operative Bank and is defined as a co-operative society with,

1. the primary object of transacting Banking business,
2. having the paid-up share capital and reserves of not less than Rs.1.0 Lakh, and
3. the bye-laws of which do not permit admission of any other co-operative society as its member.

The category of primary co-operative Banks also includes salary earners' societies having paid-up share capital and reserves of Rs.1.0 Lakh or more and if the bye-laws provide for, acceptance of deposits from non-members.

With substantial increase in the operations of co-operative Banks, it was considered anomalous to leave out co-operative banking institutions from the purview of the statutory control of the Reserve Bank of India. After the introduction of Deposit Insurance Scheme to commercial Banks in 1962, there was a demand from certain quarters that co-operative Banks should also get the benefit of this scheme and for

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this, the co-operative Banks had to be subjected to some degree of control of the Reserve Bank of India.

Functioning of the urban co-operative Banks with the paid-up share capital and reserves of Rs.1.0 Lakh and over, termed as primary co-operative Banks, came under the control of the Reserve Bank of India, as per the Banking Regulation Act, 1949, in the matters such as maintenance of cash-reserves, liquid assets, regulation of loans and advances, opening of new places of business and publication of audited balance sheet and profit and loss account.

Further, every urban co-operative Bank existing on 1st March 1966 or a new urban co-operative Bank registered thereafter was required to apply to the Reserve Bank of India for a licence to carry on or commence banking business. The statutory power of inspection of urban co-operative Banks was also vested in the Reserve Bank of India, which it could exercise directly or through the concerned State Co-operative Bank. However, powers regarding organization, registration, management and winding up of urban co-operative Banks continued to be governed by the Co-operative Societies Act of the State concerned.

Working Group on Industrial Financing  
through Co-operative Banks:

Damry Committee (1967).

In pursuance of the recommendations of Varde Committee the Reserve Bank of India set up a Working Group on Industrial Financing through Co-operative Banks under the chairmanship of Shri.P.N.Damry, Dy.Governor, Reserve Bank of India. The Working Group suggested that an urban co-operative Bank was the only suitable co-operative

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financing agency which could successfully undertake the function of providing adequate finance to small scale industrial units. Its recommendations provided a new dimension to the role and functions of the urban co-operative Banks in the country and these have generally formed basis of the policy about urban co-operative Banks in the country over the past decade. It recommended that these Banks should be encouraged through Government contribution to their share capital, concessional refinance from Reserve Bank of India against their loans to specified categories for cottage and small scale industries and the benefit of credit guarantee scheme. It recommended speedy organization of operations of some of the existing urban co-operative Banks and permission to them to open branches anywhere in the district or State where there were good prospects of business with industrial units which were not served by local urban co-operative Banks. It also recommended the removal of restrictive provisions in the bye-laws of the urban co-operative Banks which come in the way of advancing block capital loans, provisions of adequate loans to a single borrower or discrimination between small scale industrial units organised by individuals or partnership firm or joint stock companies.

The recommendations of the working group were of special importance to the urban co-operative Banks which came under the purview of the Reserve Bank of India earlier than 1966 when certain provisions of the Banking Regulation Act, 1949, were made applicable to them.

The Committee recognised urban Banks as the most suitable agency to provide finance to units other than co-operatives but run by individuals, firms and Companies. With a view to encourage

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them to undertake financing of cottage and small scale industries, the Committee made many valuable recommendations as follows:

a) Refinance under Section 17(2)(bb) read with Section 4(c) of Reserve Bank of India Act, 1934, should be made available to urban Banks, undertaking finance to cottage and small industries;

b) The Reserve Bank of India should provide loans from its National Agricultural Credit (Long Term Operations) Fund to the State Government for enabling them to contribute to share capital of the urban Banks undertaking finance to cottage and small scale industries;

c) High priority should be given to the organization of urban co-operative Banks in areas where there is sufficient concentration of cottage and small scale industries carried on by individual units. The share capital of these Banks should be strengthened by government contribution;

d) The Reserve Bank should frame suitable criteria for including urban Banks in the approved list of institutions which could directly avail themselves of the credit guarantee scheme for small scale industries even though they might not be issued licence by the Reserve Bank of India;

e) Existing urban co-operative Banks may be allowed to extend their area of operations so as to make it possible for them to have dealings with the individual units which are not too far away from an office of the Bank to render supervision both costly and difficult;

f) The banks should be permitted to open a branch office anywhere in the district or the State, where there are good prospects for business with industrial units and these are not being served by a local urban co-operative Bank;

g) Whenever necessary, the bye-laws of urban co-operative Banks should be amended to enable these Banks to provide loans to a single borrower upto a limit which will be adequate for the purpose of financing small scale industries. Care will have to be taken, however, to ensure that the facilities are not monopolised by a few affluent individual members. The State Government should ensure wherever necessary that the Co-operative Societies Act and bye-laws of urban Banks are suitably amended to remove such of those provisions, if any, which restrict the financing of small scale industrial units regardless of whether they are individuals or partnership firms or joint stock Companies;

h) The bye-laws of urban co-operative Banks should contain a clear provision enabling them to provide block capital loans to small scale industrial units. Existing restrictions, if any, which inhibit them from advancing block capital loans should also be removed.

The urban co-operative Banks were mainly catering to the credit needs of middle class people such as salary earners, small traders, etc. in urban and semi-urban areas. With the growing needs of the people, there was diversification of activities of these Banks. Mainly providing consumption loans earlier, they re-oriented their loaning

policies with emphasis more on loans for production-oriented purposes, consequent upon the implementation of the recommendations of Damry Committee.

Banking Commission Report (1972):

Banking Commission (1972) appointed by the Government of India also suggested a definite role for the urban Banks in the total banking structure of the country in mobilising deposits and the financing the sector of small borrowers and in financing for house-construction and its repairs to the members of the Banks. This type of banking provided useful avenue for those who have the necessary ability to set up a Bank. The Commission had even recommended the grant of Scheduled Status to well organized urban co-operative Banks and the provision of remittance facilities and loan assistance on reasonable terms through the nationalised Banks to the non-scheduled urban Banks.

The important benefits which will accrue to the urban co-operative Banks by giving status of a scheduled Bank are as under:-

- i] Free remittance facility from the Reserve Bank of India;
- ii] As refinance under Section 17(2)(bb) of the Reserve Bank of India Act is being provided by the Reserve Bank of India through the State Co-operative Banks which are scheduled Banks and because urban co-operative Banks are not scheduled Banks, they are not getting direct refinance facility from the Reserve Bank of India. By scheduling the urban co-operative Banks, they can get refinance directly from the Reserve Bank of India and thus reduce the cost of operations and avoid procedural delays;



iii] The present scheme of refinance by the Industrial Development Bank of India to the urban co-operative Banks for giving long-term loans to the small scale industrial units also lays down that the refinance will be provided through the Scheduled Banks, i.e. either through commercial Banks or State Co-operative Banks. Scheduling the urban co-operative Banks would enable them to avail of the Industrial Development Bank of India refinance directly from the Industrial Development Bank of India and thus, reduce the cost of borrowing as also procedural delays.

iv] At present, the Government Corporations or semi-Government bodies insist on guarantees to be provided by the customers from the scheduled Banks only. Urban co-operative Banks have, therefore, either to lose their clientele or to obtain guarantee for their clients from a scheduled Bank and to offer their own counter-guarantees to such scheduled Banks as their guarantees are not accepted. The latter procedure increases the cost to the clients. By scheduling the urban banks, they will be enabled to issue guarantees directly.

v] The Central/State government bodies or Corporations are not keeping their surplus funds with the urban co-operative Banks as they are required to keep funds with scheduled Banks. If urban co-operative Banks are given the scheduled Bank's status, they will also be able to accept deposits from the Government bodies or Corporations;

vi] It may be argued that by giving scheduled bank's status to the urban co-operative Banks, they may be asked by the Reserve Bank of India to maintain higher liquidity. In

this connection, it may be pointed out that though the State Co-operative Banks are also the scheduled Banks, they are not required to maintain higher liquidity than the prescribed minimum, even though an enabling clause is provided in the Banking Regulation Act. Urban co-operative Banks are alive to these responsibilities and since only the licensed, sound and good working urban co-operative Banks would be given the scheduled bank's status, they would be willing to shoulder additional burden of maintaining higher liquidity on the basis of norms laid down for the State Co-operative Banks;

vii] Giving the status of a scheduled Bank to the urban co-operative Banks would enhance the image of these Banks in the eyes of the public and the society at large and would effectively strengthen the business of these Banks and increase the confidence of the public.

Recommendations of Banking Commission:

Some of the important recommendations of the Banking Commission are:

Urban co-operative Banks do useful work in mobilising deposits and financing the sector of small borrowers such as small scale industries, professionals, retailers and so on.

Another useful activity is the financing for house-construction and its repairs to the members of the Banks. Also, this type of banking provides a useful avenue for those who have the necessary ability to set up a Bank.

The Commission recommended that establishment of urban co-operative Banks should be encouraged by the authorities by such means as:-

- i] according the status of a scheduled Bank to the well managed urban co-operative Banks, if they so desire;
- ii] counting towards liquid assets the deposits which these Banks place with the nationalised banks; and
- iii] asking the nationalised Banks to give such of the urban co-operative Banks which remain non-scheduled, free remittance facilities and borrowing facilities on reasonable terms.

The Commission further recommended that in order to ensure that the productive and distributive activities are adequately financed by such Banks,

- i] there should be a system of ceilings on borrowings by individual, linking it only to the amount of shares held;
- ii] lending for long term purposes, such as house construction, should be allowed subject to a ceiling that may be specified by the Reserve Bank of India regarding the proportion of such lending to the total loans given by the Bank;
- iii] similarly, there should be a ceiling on the proportion of total loans for consumption purposes, this ceiling need not apply in the case of employees co-operative credit societies.

The Commission recommended that steps should be taken to enable the urban co-operative Banks to make better use of the financial assistance available from the Reserve Bank of India.

## **B) Methodology.**

As urban co-operative Banks can play an important role in improving economic conditions of the middle- and lower-middle class people and in financing the small scale industries; and as Kolhapur is known for its small scale industrial units, the researcher felt that a study of industrial finance by the Urban Co-operative Banks in Kolhapur may prove to be a fruitful exercise in understanding the role played by these Banks in financing such units. As on 31st March, 1988, there were as may as 8,416 small scale industrial units in and around Kolhapur, registered with the District Industries Centre, Kolhapur.<sup>1</sup> There are, on the other hand, 16 urban co-operative Banks in Kolhapur as on that date.

## **C) Scope and Objectives of the Study.**

The scope of this study extends to studying the industrial finance provided by urban co-operative Banks in Kolhapur and the difficulties encountered by the lending Banks. The following objectives have been borne in mind while conducting this study:

- 1) To study the industrial finance advanced by the urban co-operative Banks in Kolhapur; and
- 2) To study the legal, operational and other practical difficulties encountered by these Banks.

### Selection of Banks:

For the purpose of studying the industrial finance advanced by the urban co-operative Banks in Kolhapur, the researcher thought of

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1. Government of Maharashtra, District Industries Centre, Kolhapur (Ed.)  
'Action Plan - 1988-89 to 1989-90'.

selecting 3 to 4 urban co-operative Banks with adequate financial resources so that they can meet the demands for finance for small scale industrial units. The researcher listed all the 16 Banks and ranked them on the basis of deposits as on 30th June, 1987. The first five of these Banks and their deposits as on 30th June, 1987, were as follows:

	<u>Name of the Bank</u>	<u>Deposits</u> Rs.in Lakhs	<u>Ranking</u>
1.	Shree Veershaiv Co-operative Bank Limited	1,601.37	I
2.	The Kolhapur Maratha Co-operative Bank Ltd.	1,294.28	II
3.	Shree Mahaveer Co-operative Bank Limited	1,039.42	III
4.	The Kolhapur Urban Co-operative Bank Limited	969.83	IV
5.	Kolhapur Janata Sahakari Bank Limited	877.98	V

Out of the above 5 banks, Shree Mahaveer Co-operative Bank Limited had to be dropped as the data available with this Bank were found to be inadequate for the purpose of study. The remaining four Banks were, thus, selected for the purpose of the study by using purposive sampling method.

#### Collection of Data.

Collection of data is done in the following manner:-

- 1) Data relating to the 16 urban co-operative Banks were collected from the office of the Kolhapur District Urban Co-operative Banks' Association;
- 2) Data relating to the four urban co-operative Banks selected were collected from the various sources as follows:
  - a) Annual Reports of these Banks. Most recent data, i.e. for the years 1985-86, 1986-87 and 1987-88, were given importance. To understand the previous trend, data for

the years 1973, 1978 and 1983 were also collected. Apart from Annual Reports, records of the concerned Banks were used for this purpose.

- b) For the purpose of understanding the organization structure, certain operational aspects and the difficulties encountered at the time of financing industrial units, the researcher had to have discussions with various officers of each of these Banks;
  - c) Books and periodicals were also used for the purpose of understanding the urban co-operative Banks' role in financing the industry in general.
- 3) Legal, operational and other practical difficulties were understood by observation and also by discussing them with various Bank officials.

#### D. Presentation of the Report.

The report of this study has been divided into six Chapters. **First Chapter** includes an introduction to the subject and the methodology followed for the purpose of this study. **Second Chapter** explains the purposes for which the urban co-operative Banks grant loans and advances, the procedure for their sanction, disbursement and recovery, recommendations of various committees in this regard and the RBI directives in connection with such loans and advances. Particular stress is given on loans and advances for industry and priority sector. **Third Chapter** gives the organizational structure and the progress made by each of the following four Banks selected for the study:

1. Shree Veershaiv Co-operative Bank Limited, Kolhapur;
2. The Kolhapur Maratha Co-operative Bank Limited, Kolhapur;
3. The Kolhapur Urban Co-operative Bank Limited, Kolhapur;
4. Kolhapur Janata Sahakari Bank Limited, Kolhapur.

**Fourth Chapter** is sub-divided into two parts; Part-I includes data presentation, and Part-II, the difficulties encountered by the urban co-operative Banks in financing the industry. The data presented in this Chapter relate to each of the four Banks mentioned above and for a period of four years, i.e. from 1984-85 to 1987-88. Particular importance is given to data on Loans and Advances in general and on Loans and Advances to small scale and cottage industries in particular. Industrial advances made under Priority Sector Scheme is also studied. The difficulties encountered are classified as legal, operational and others. **Fifth Chapter** gives the evaluation of the industrial finance provided by the selected urban co-operative Banks in Kolhapur City. **Sixth Chapter** contains the summary and conclusions.

#### E) Limitations of the Study.

As the environmental aspect concerning the urban co-operative Banks at other places are different from those obtained in Kolhapur, some of the conclusions drawn and suggestions made in this dissertation may not be applicable to the Banks in other cities like, say, Pune, Bombay, etc.