CHAPTER FOURTH:

ECONOMIC DEVELOPMENT AND CO-OPERATIVE BANKING IN GLOBLISATION.

4.1- DUAL CONTROL ON CO-OPERATIVE BANKS.
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4.5- ECONOMIC DEVELOPMENT BY CO-OPERATIVE BANKS.
4.1 DUAL CONTROL ON CO-OPERATIVE BANKS:

Origin of dual control

"Regulating the activities of India's Co-operative Banks first came into focus as an adjunct of the extension of deposit insurance to this sector of banking" Reserve Bank of India and various State Governments had extensive deliberations over the issue of bringing in Co-operative credit institutions carrying on banking activities under the ambit of Banking Regulation Act. Unless, the Reserve Bank, as the Central Bank of the country, was able to exercise control over Co-operative banks, it was not found feasible to introduce deposit insurance cover for these institutions. Initially many a State Government expressed its reservation in sharing the control over Co-operative societies carrying on banking business with Reserve Bank of India. A conference convened by RBI in November 1963 to deliberate on the issue, "witnessed intense debate over the virtues of vesting in the Bank powers to liquidate a Co-operative bank or supersede its management, with the Madras Government, in particular, marshalling ideological, constitutional and practical arguments against the idea. Mysore joined Madras in suggesting that the regulation by Reserve Bank was too high a price to pay for extending insurance cover to depositors of Co-operative banks". The RBI, made strenuous efforts to dispel these apprehensions and clarified that it would advise State Governments and RCS whenever it contemplated taking any serious action against a Co-operative bank. The then Governor of RBI, Shri P.C.Bhattacharya assured the
State Governments that the Bank would entrust its powers to regulate Co-operative banks only to the Agricultural Credit Department which was familiar with these institutions and was sensitive to their special needs. It was explained that it would not be feasible to extend deposit insurance cover to UCBs if the RBI was not vested with these powers through suitable legislative measures.

Co-operative banks not only received substantial funds by way of created money from RBI but also accepted deposits from public and financed agriculture, industry, commerce and trade. With the State Governments committed to a policy of positive support to Co-operative banks, it was felt that the impact of Co-operative credit institutions on the monetary and credit policy was going to become more and more significant. In late fifties and early sixties, a number of banks had failed, thus, adversely affecting the interests of the depositors. This had led to certain amendments in the Banking Regulation Act. It was considered desirable to extend some of these provisions also to banks in the Co-operative sector so as to safeguard the interest of depositors.

Hence, the RBI felt that it was a regulatory necessity to bring the banking institutions operating in the Co-operative sector within the statutory control of RBI. Thus, the application of banking laws to Co-operative banks basically emanated because of the following reasons;

i) Interests of depositors required extension of Banking Regulation Act to banks in the Co-operative sector,

ii) RBI's supervision was considered necessary for extending deposit insurance.
iii) Substantial funds were granted to Co-operative credit structure by way of created money from RBI and, hence, it had a monetary policy connotation.

iv) Public interest required that institutions having substantial public deposits and functioning as banks should operate under the supervision of Reserve Bank of India.

After prolonged deliberations on the need for RBI to have control over Co-operative societies carrying on banking business, the Banking Laws (Application to Co-operative Societies) Bill was passed by the Parliament. It received the assent of the President in September 1965 and the Act came in to force from 1 March, 1966. With this amendment in the Banking Regulation Act, certain provisions of the Banking Regulation Act became applicable to Co-operative banks carrying on banking business. This brought in an era of dual control over Co-operative banks. In terms of the Co-operative Societies Act of the State, the Registrar of Co-operative Societies was to have jurisdiction over the incorporation, registration, management, amalgamation, merger, liquidation etc. and the Reserve Bank was to have jurisdiction over the banking activities of the Co-operative society.

In terms of Article 246 of the Constitution, the field of exercise of legislative powers is divided into three areas;

(i) Exclusively reserved for the Union of India and referred to as the "Union List"

(ii) Exclusively reserved for the States and referred to as the "State List"

(iii) Those left for both and referred to as the "Concurrent List".
These areas of Legislation are indicated by Entries in List I, II and III respectively, of the VII Schedule to the Constitution. The Co-operative Credit Societies doing banking business fall, to a certain extent in the area exclusively reserved for the Union and to a certain extent, in the area exclusively reserved for the States. These results in the duality of jurisdiction over Co-operative banks both by the Reserve Bank of India, in terms of the Banking Regulation Act, 1949 and the Registrar of Co-operative Societies, in terms of the Co-operative Societies Act, of the State concerned. Entries 43 and 45 in the Union List and the Entry 32 of the State List are the relevant Entries for and they read as under:

**Union List**

Entry 43, "Incorporation, regulation and winding up of trading corporations, including banking insurance or any financial corporation's but not including Co-operative societies." Entry 45, "Banking"

**State List**

Entry 32, "Incorporation, regulation and winding up of Corporations, other than those specified in list I, and universities; unincorporated trading, literary, scientific, religious and other societies and associations; Co-operative societies".

8.6 In a case involving corresponding entry (banking) under the Government of India Act, 1935, (Bank of Commerce India Vs Nripendranatha Datta, AIR 1945 FC 7) the Supreme Court observed that the Entry must be held to cover only such laws which affect the conduct of business of a bank. The Hon'ble Supreme Court in R. C. Cooper Vs Union of India, 1970 (3) SCR 530, again observed that Entry 45 in List I of the VII Schedule is 'banking' and not banker or bank. The Court
also observed that a Legislative Entry indicates the contour of plenary power and must receive a meaning conducive to the widest amplitude, subject, however, to limitations inherent in the federal scheme which distributes legislative power between the Union and the Constituent units. These are then the broad constitutional limitations within which the Committee has to make its recommendations.

**Approach of the Committee**

The Committee had detailed discussions with individual cooperators, Co-operative banks and their federations. All of them unanimously expressed their dissatisfaction over the "dual control regime". They felt that the dual control regime over UCBs should end and RBI should act as the regulatory authority for the banking activities of UCBs. Perhaps, on no other issue, was there such unanimity of views. After having heard the views of the cooperators, federations and Co-operative banks as also the State Governments officials, and after examining the existing statutory framework under the State Co-operative Societies Acts, the Committee feels that the dual control regime, per se, need not cause any hindrance to the growth of the urban banking movement. It is the absence of a clear cut demarcation between functions of RBI and that of the State Governments that adversely affects the smooth functioning of Urban Co-operative Banks.

Interestingly, the Committee did not find similar difficulties in the supervision and regulation of banking companies. Although they are registered as companies under the Companies Act 1956, by the Registrar of Companies, they
carry on the banking business under the sole Supervision of RBI. This is because
the Registrar of Companies does not interfere in the field covered by the Banking
Regulation Act. Once a company registered under the Companies Act, gets
license from Reserve Bank, its *activities* are regulated by its Memorandum and
Articles of Association and the provisions of the B R Act. Since the provisions of
Banking Regulation Act have an overriding effect on the Memorandum and
Articles of Association, the RBI becomes the sole regulatory authority in relation
to business activities of banking companies.

The Committee believes that the role of the Reserve Bank in matters of
supervision of a bank vis a vis a company or a Co-operative society, should be
looked at from the functional angle rather than the institutional angle. No doubt
urban Co-operative banks are Co-operative entities, but their primary objective is
to carry on banking business. Regulation of banking business is the concern of the
Reserve Bank. Hence, it is absolutely necessary that Reserve Bank should be the
sole regulator of the banking business carried on by Urban Co-operative Banks.
The issue needs to be examined, in the context of experience of Co-operative
banks operating under the dual control regime, as also, the interest of the banks
and their depositors.

The Committee has been informed that at times, there has been interference
by State Governments, even in the banking related functions of urban Co-
operative banks. A few instances brought to the attention of the Committee of
overlapping jurisdiction resulting in avoidable difficulties for UCBs are
chronicled below:
i) In terms of Section 23 of Banking Regulation Act, 1949 (AACS) the RBI has the authority to issue a branch license to an urban Co-operative bank and under the existing policy, RBI issues branch license after convincing itself about the financial strength of the UCB. Strangely, in some states, the UCBs are required to obtain "No Object Certificate" (NOC) from RCS of the concerned State even after the licence has been granted by the RBI.

The Committee fails to understand the necessity of a NOC from the Registrar of Co-operative Societies. The Committee feels that grant of licence is purely banking related function and should be left to the Reserve Bank.

ii) Another area of concern arising out of dual control is investment of surplus funds by UCBs. The "investment" is also a banking function within the meaning of Section 5 of Banking Regulation Act, 1949. Hence UCBs should, subject to the guidelines issued by the Reserve Bank, have the freedom to choose the products in which they may invest. Yet, some Registrars of Co-operative Societies insist on their permission being taken for every investment decision. Due to limited avenues of profitable investments in the Co-operative sector, the RBI has allowed UCBs to invest up to 10% of their surplus funds in the equity of All India Financial Institutions, units of UTI, and PSU bonds. However, in some of the States, this freedom is frustrated by the Registrars of Co-operative Societies. The Committee is unable to understand why; the RCS or any other Government Official should sit in judgments over the commercial decision of the board or a professional treasury manager of a bank.
iii) There are instances when the Registrars of Co-operative Societies have issued instructions in clear conflict with those issued by Reserve Bank. For example, in terms of Section 21 of the Banking Regulation Act 1949, the Reserve Bank is empowered to give direction to a Co-operative bank regarding "the rate of interest and other terms and conditions on which advances or other financial accommodations may be made or guarantees may be issued". Section 21 (3) further lays down that every bank shall be "bound to comply with any direction given by Reserve Bank". Notwithstanding these provisions, there are instances where a RCS issued a direction that UCBs should charge interest on deposits in accordance with his instructions. After having learnt about it, the RBI took up the matter with the RCS and with the Cooperation Department of the State but has not succeeded in getting the directive withdrawn.

iv) Area of operation is again a matter closely related to the banking business and should, therefore, remain in the domain of the RBI. The Reserve Bank found that barriers on expansion of UCBs were adversely affecting their growth. Hence, it allowed UCBs to expand their area of operation to the entire district of their registration and in some cases to the whole of the State. Notwithstanding RBI's clearance, in many States, specific approval of RCS is insisted upon. When a company desires to expand its activities to all over the State, the Registrar of Companies does not prescribe any restrictions on its expansion. If General Body approves the expansion and RBI gives clearance, the Committee does not find any rationale for a further approval to be granted by the RCS. One member (Shri Subhash S. Lalla) feels area expansion by way of opening new branches involves
banking as well as Co-operative function. RCS should also have a say in branch expansion matters to see if Co-operative character will be diluted and whether the branch expansion really benefits the members of the UCB.

v) Similarly, acquisition of movable and immovable properties, incidental to carrying-on the banking related functions, needs approval of RCS. Some UCBs expressed difficulty in getting permission even for buying computers. Registrars of Co-operative Societies insist on their prior permission before recruiting any staff even for banking related functions.

vi) Democratic spirit is the quintessential trait of Co-operative societies. But a State, which happens to be a cradle ground for Co-operative movement in India, superseded the Boards of Management of all Co-operative societies, including UCBs, with a stroke of pen on the pretext of reorganizing and strengthening the Co-operative sector. It is needless to add that the said decision was a fall out of change in political dispensation rather than a desire to bring any substantial improvement in the development of Co-operative institutions. As a result, banks were placed under the charge of the nominees of Registrar of Co-operative Societies for over a period of 6 years. Even after the democratic process was restored, the State Govt. appoints Co-op. Department's officials as MDs of UCBs.

vii) In many a State, the General Body or the Managing Committee cannot write off Unrecoverable / bad debts from the books without the concurrence of the Registrar of Co-operative Societies even though the act of writing-off an asset is purely a management decision and guidelines are issued by RBI and Central RCS in this regard.
The above instances pertaining to the role played by the State Government functionaries in the working of UCBs, which were brought to the attention of the Committee, caused concern to it. It, therefore, wanted to personally interact with the functionaries of State Governments to ascertain their viewpoint. The Committee interacted with the representatives of various State Governments. Some States were represented by the Secretary Cooperation, some by RCS and some by both. Most of them found fault with the Managing Committees and senior functionaries of UCBs who in some cases, were alleged to have vested interests, lack motivation and financial integrity. They are convinced that if the role of the RCS is curtailed, it would result in sharp increase in the sickness rate of UCBs. They feel that RBI is far removed from the field realities and, hence, it is in no position to diagnose and take necessary curative measures in time to remove the deficiencies inherent in the working of the UCBs. Most of them feel that Chartered Accountants (CAs) are just not good for the audit of UCBs. When it was put to them that the country is trusting CAs to audit companies with a turnover of several thousands crores of rupees, they replied that UCBs are a class by themselves and CAs are not equipped to audit these delicate entities. They are not even prepared to give an option to UCBs to choose between Co-operative audit and CA's audit, keeping in view the cost, speed and quality of these two classes of auditors.

They asserted that even if the RBI has exclusive jurisdiction on the banking functions of UCBs, the RCS and the State Government will be pilloried by the public and press, if anything goes wrong with an UCB. They said that, they are
not prepared to bear the cross in the event of failure of RBI's supervision. When it was put to them that Registrar of Companies or the concerned State Government are not being blamed for the sickness of the commercial banks, they argued that public always associate regulation of UCBs with RCS. When it was brought to their notice that State Governments appointed their employees, who were at the verge of retirement, for a period of two to three years in UCBs without reference to their work experience, their reply was that the quality of staff selected by the Managing Committee is any day much inferior.

The Committee is of the opinion that right and timely investment decisions will maximize bank's profits. Some of the State Governments do not give freedom to UCBs to invest their surplus funds but dictate where the investment should be made. When this problem was raised with the representatives of State Governments, they emphatically argued (except in Madhya Pradesh) that funds from Co-operative sector cannot be allowed to be invested outside the Co-operative sector.

The instances mentioned above are only illustrative. One of the suggestions, repeatedly put forth by the cooperators is that excesses of dual control regime can be contained by transferring the item "cooperation" to Union List or to Concurrent List so as to enable the Union Parliament to legislate on the subject of Co-operative banks. Given the federal policy of our country, it is unlikely that the State Governments would agree to such a transfer. Earlier Committees like Madhava Das Committee, Marathe Committee and quite recently Narsimham Committee have all suggested that there is need to address the issue
of 'duality of control', by carrying out necessary statutory amendments. However, nothing substantial has been done till date. The Committee is of the opinion that the only effective way to address the problem of dual control is to carry out amendments in the State Co-operative Societies Act, the Multi State Co-operative Societies Act, 1984, as also the Banking Regulation Act, 1949 to clearly demarcate the banking related functions which are to be regulated slowly by RBI and those related to establishment of Co-operative societies and their Co-operative character which shall remain within the domain of the RCS of concerned state. The Committee feels that for banking related functions, the RBI should be the sole regulator.

4.2 SOCIAL STATUS OF CO-OPERATIVE BANKS:

The Reserve Bank of India (RBI) has dismissed the board of Maharashtra State Co-operative Bank Ltd (MSC) and appointed two state government officials as administrators to run the bank, which is celebrating its centenary year.

The central bank got into act after the co-operative bank had its net worth or equity and reserves eroded by piling bad assets. A National Bank for Agriculture and Rural Development (Nabard) audit of the bank’s 2009-10 balance sheet revealed that its net worth turned negative by Rs. 140 crore as it had to set aside money or provide for bad loans. According to the Nabard report, the bank’s net loss in fiscal 2010 was Rs. 775.98 crore and bad loans Rs. 500 crore, nearly 30% of total’s advances. Nabard executive director Prakash Bakshi confirmed that his organisation had suggested corrective action on MSC by RBI.
"This bank was already under various RBI directions for the last 13 to 14 years, but at the end of March 2010, its net worth became negative by Rs. 140 crore because of the huge provisions the bank had to make on loans given to co-operative sugar factories and co-operative spinning mills," he said.

Late evening on Friday, RBI dismantled the board and appointed state government’s agriculture secretary Sudhir Goel and planning Secretary Sudhir Shrivastav as administrators.

No small depositors will lose money as the bank is protected under the deposit insurance scheme of the regulator, a RBI official said on condition of anonymity. Under this scheme deposits up to Rs. 100,000 is insured.

"It will take few days for us to streamline bank’s affairs and chalk out the plan for recovery, but our priority will be to maintain utmost transparency in bank’s affairs," Goel said.

Bakshi of Nabard said the administrators will now review both the loans and recovery processes of the bank. There is no restriction on the bank accepting fresh deposits or giving back money to depositors, as it has enough investments to pay creditors. "Liquidity is not an issue with the bank. It has Rs. 14,000 crore of investments in government bonds," Bakshi said.

The bank had a deposit base of Rs. 18,998 crore in September 2010, according to its website. In March 2010, its net non-performing assets were 7.6% of advances. Bakshi said bulk of the deposits is from institutions such as other co-operative banks and credit co-operative societies. The development has come as a huge embarrassment for the ruling Nationalist Congress Party (NCP) and state’s
deputy chief minister Ajit Pawar, who is controlling bank’s affairs for last decade or so.

Out of 44 directors on the bank board, 25 belong to NCP including Pawar, 14 to Congress and two each from the Bharatiya Janata Party and Peasants and Workers Party and one from Shiv Sena. Pawar did not respond to a text message sent on Saturday.

“The bank has attached some 86 properties including some sugar Cooperatives and Co-operative spinning mills but as most of them belonged to MLAs and ministers of ruling NCP-Congress combine, none of them was sold,” said BJP member of state legislative assembly Devendra Fadanvis, who raised the issue of mismanagement of bank’s affairs in the recently concluded budget session of the state assembly.

Had they been auctioned, it could have fetched the bank Rs. 3,000 crore. Fadanvis also demanded that an expert committee should be appointed to oversee the affairs of bank. NCP spokesman Jitendra Avad dubbed RBI’s action as “unilateral and unjustified” and said no explanation was sought from bank before the board was superseded. “It is up to members of board whether to challenge RBI’s action in court of law or not,” he said. Noted political analyst Pratab Asbe, who keeps a close watch on state’s political, social and economic issues, said NCP should share the blame for this as it has most members on the board, but Congress, BJP and Sena also can’t deny their role as they have representatives on board.
Sugar Co-operatives and sugarcane farming will suffer following RBI's decision as due to bumper sugarcane crop and ban on exports, sugar Co-operatives are already facing liquidity crunch. To remain afloat in the sugar crushing season (September to March), they will require working capital.

4.3 ACCEPTANCE OF DEPOSITS AND LOANS AND ADVANCES BY CO-OPERATIVE BANKS:

No Co-operative bank shall make loans and advances on the security of its own shares or grant unsecured loans or advances to any of its directors or to any firm or private company in which the director has interest.

This above clause shall not apply to grant of unsecured loans or advances made by a Co-operative bank against bills for supplies or services made or rendered or bill of exchange arising out of bonafide commercial or trade transactions or trust receipts furnished to the Co-operative bank or Loans made by primary Co-operative banks on terms approved by RBI. Urban Co-operative Banks Provides loan to Small Scale industries, Businessman, Salary Holder and small shopkeepers.

LAON SCHEME ADOPTED BY CO-OPERATIVE BANKS:

Agriculture:

In the field of agriculture, diversification can be thought of in encouraging farmers to take up cultivation of hybrid varieties of crops rather than the traditional ones. For example, Hybrid paddy which needs approximately Rs. 8000 per acre as cost of cultivation would yield around 10 tones which is almost four times the normal yield of the paddy crop. Farmer therefore, will be able to make
good money out of this activity and at the same time bank may be able to deploy more loan to the same activity. In this way, many other crops like cotton, oilseeds, tomato and others have got hybrid seeds evolved for the purpose and farmers are ready to take up the cultivation but credit being the constraint is taking up their cultivation in a big way. Hence, one may need to look into the areas specifically by taking into account local agro-economic factors and diversify their portfolio.

**Horticulture**

In case of Horticulture, Co-operative banks' stake in its development is very low and many of the CCBs had never given a thought to finance horticulture in a big way despite the encouragement being given by GOI under the mission mode of National Horticulture Mission (NHM). Under the NHM, GOI envisages to double the production of fruits and vegetables to 300 million tons from the existing 140 million tons by the year 2012. If the mission objective has to be achieved, investments need to be made in a big way in the horticulture development and the role of Co-operative Banks so far in promoting these activities is abysmal. There are many horticulture areas where banks can lend and at the same time increase the prosperity of the farmers like lending to fruit orchards such as mango, banana, grapes, citrus fruits, strawberry, etc. Of late, many scientific revolutions have taken place in the cultivation of horticulture crops and a new technique for high density plantation has come. In this High Density Plantation (HDP), the same variety of the fruit crop will be cultivated but the density of crop will go up by two / three times than the traditional ones which
simultaneously hikes the unit cost for the activity. In the normal traditional plantation, if the unit cost for mango is around Rs. 10,000 per acre, the unit cost for HDP works out to Rs. 90,000 per acre. By promoting such activities, the banks are not only increasing the credit portfolio but are also helping to generate substantial quantities of horticulture produce which may in turn give scope for promotion of processed industries and also other ancillary activities like cold storage, transportation, etc in the area. All these new activities that will come around this principal activity of horticulture would again give a great scope for the banks to increase their lending. Under NHM and also in AMI Programme, subsidies are available to take up activities and the banks should be able to promote these activities so that farmers and the area will get substantial investments which may lead to overall prosperity.

Of late, there is a surge in demand for vegetables and the cultivation of vegetables is being taken up mostly by borrowing money from moneylenders. Going by the quantum of vegetables being cultivated in the country i.e. 90 million tons every year, the estimated credit requirement for producing such a volume would be stupendous since banks and specifically Co-operative banks are not great players in extending credit. Vegetable cultivation may have to be looked into as business potential awaiting and also as a great profit churner by Co-operatives which otherwise is being financed by moneylenders at very high cost. Further, the demand for exotic vegetables and vegetables produced under controlled conditions is rising which again needs a sizeable investment from the
banking sector. It is, therefore, necessary for the Co-operative banks to look into this portfolio with clear insight so as to make a profitable diversification.

In case of floriculture, the country produces substantial quantities of flowers for domestic consumption, extraction of essential oils and also manufacture of pesticides (Pyrethrums) but going through the portfolio of Co-operative Banks, one will wonder whether any time some attention has been paid to this most lucrative business. In view of this, the Co-operative banks may look into this portfolio for diversification.

Agro and Farm Forestry:

Demand for forest based raw materials for industrial purposes is growing at fast pace and that availability of the same from the traditional forest are dwindling day by day forcing the industry to look into avenues of getting the forest species cultivated on farm land to ensure continuous raw material supply. In this direction, good work has been done by various Government agencies as well as private forestry companies to promote various forestry species and the most important among them are Eucalyptus, Poplar, Bamboo, Acacia, etc,. With the availability of clonal multiplication as well as tissue culture technologies, the cultivation of forestry species have become very remunerative and the gestation period of the crops had also come down. Many farmers in some of the states are making good profit by cultivating clonally Eucalyptus, Tissue cultured bamboo, etc. Moreover, these crops can be cultivated on degraded farm lands which are needed to be put under green cover immediately, to ensure arresting of further degradation, ensuring income to the land owners and continuous supply of raw
materials to the industry. Co-operative Banks may look into the option of extending finance to the forestry crops in a big way. Forestry crops can be cultivated either as block plantations or they can even be cultivated on bunds and in both the systems bankers are going to make brisk business which again will lead to successful diversification of their portfolio.

Bio-Fuels

Bio-fuels have become the talk of the town and prominent crops among them are Jatropha and Pongamia. Oil extracted from both the crops is used for production of bio-diesel after subjecting it to etherification. Due to the produce price already fixed by Government of India, growing of these crops proved to be profitable to the farmers possessing marginal and sub-marginal lands which are otherwise not fit for cultivation of regular crops. Keeping in view the vast stretches of degraded/marginal and sub-marginal lands available in the service area of the Co-operatives, an effort should be made to make a roster of such lands and try to promote these crops in a mission mode. CCBs and PACS should take active interest in bringing such lands under green cover and this effort would lead to deepening of credit flow in those areas.

Medicinal and Aromatic Plants:

The demand for medicinal and aromatic plants is in the range of Rs. 3, 00,000 crores and is growing @ 15% every year. Fortunately India is one such country which can produce almost all the medicinal and aromatic plants. However, lending done in this area is still meager due to unfamiliarity of the bankers with the concept. There are more than 30 varieties of medicinal crops
and another 8-10 aromatic plants which can be successfully cultivated in the
country and demands for their products is on the rise. Another special feature of
these medicinal and aromatic plants is the ability to absorb substantial amount of
credit which in turn may give considerable scope for increasing credit volume to
the banks. Returns from the crops are also good and marketing channels have
opened up at many places and therefore, the Co-operative Banks may look into
this area with all seriousness and find out avenues to forge links with consuming
industry and finance on a tri-partite agreement mode. Cultivation of these crops
also entails the farmers for capital investment subsidy and banks can be sure of
getting definite repayments because of back-ended nature of subsidy being given
by National Medicinal Plants Board. Further, extraction of the alkaloids both from
Medicinal and aromatic plants needs investments in processing plants / extraction
units at the local level which again opens up scope for the bank to increase their
lending in the agro-processing / non-farm sector activities.

Animal Husbandry:

Though India is ranked number one in milk production in the world, the
scope for the activity is still very high because of the growing population. Dairy
activity is being promoted by Co-operatives for quite some time, but their lending
is mostly confined to one or two animal units only. Of late, dairying has become
very profitable and is emerging as a standalone activity without linking it to any
agricultural activity. In many places, farmers with 5 to 10 acres of land are taking
up dairy as a main activity and are cultivating grass and legumes for the dairy
activity exclusively without going for cultivation of other crops. Return on the
investment from the dairy activity is substantial and promoting Mini dairy units of 10 to 20 animals is most profitable for a Co-operative bank to diversify into.

**Poultry:**

Poultry is another major activity which absorbs substantial amount of credit from the banking system. Giving loans to big units is well known but the recent initiative of the Veterinary Department of UP proved that backyard rearing of poultry birds (100 to 200 birds) by small and marginal farmers and people belonging to SC / ST categories can give substantial returns to those people. In view of the quick as well as definite returns the poor and marginal segments of the population are getting from this activity, Co-operative Banks may consider to diversify into this activity in a big way by giving small loans for backyard poultry to a large number of customers.

**Quantum of Loan:**

a. Quantum of loan: Quantum of loan shall be decided based on the crops to be cultivated and scale of finance for such crops and a small component for meeting the contingencies related to cultivation of crops. Some additional loan component towards alternate income generating activity, as per need.

b. Maximum ceiling: Rs. 25000/- per member including a limit of Rs. 2500/- towards consumption expenses.

**Rate of interest:**

- For short term crop production loans: @ 7.0% per annum till the interest subvention scheme of GOI is in force and as per normal rate applicable to such type of advances afterwards.
• For income generating activities under allied activities / non-farm sector: As per extant guidelines.

**Other Conditions:**

• The applicant should be a permanent resident of the operational area of the branch. Branches shall establish the identity and permanent address of the tenant farmer / oral lessee.

• The tenant farmer / oral lessee shall open SB A/c under SyndSamanya Scheme.

• The applicant is not indebted to any other financial institutions.

• Eligible crops are to be covered under crop insurance scheme.

• The borrower shall be covered under Personal Accident Insurance Scheme.

• In the case of subsidiary activity like dairy / sheep rearing etc. insurance of animals is compulsory.

**4.4 MANAGEMENT AND ADMINISTRATATION OF CO-OPERATIVE BANKS:**

**Final authority in a Co-operative society:-**

Final authority of a Co-operative society shall vest in the General Body of the members. An Annual General Body meeting of a Co-operative society shall be held once in a year within a period of 3 months after the date fixed for making up its accounts for the year for the purpose of approval of the programme of activities, election, if any and consideration of annual report audit report and disposal of net profit.
Committee of Management:-

Management of a Co-operative society vests in a Committee shall consist of not less than 9 members one reservation for women, one for SC/ST. Term of office of the Committee three years. Elections to be held for the entire committee other than the nominated members.

Nominee of the Government on the Committee of a Co-operative society:-

How the Govt. gets such right of nomination? Government has subscribed to the share capital assisted in formation or augmentation of the share capital guaranteed repayment of principal and payment of interest on debentures guaranteed debt repayments.

How many nominees?

State Government has the right to nominate as its representatives not more than 3 persons or 1/3 rd of the total number of members of the Committee of the Co-operative society, whichever is less.

Conditions for Suppression of the Committee

• In the opinion of the Registrar, If the committee is negligent, makes default, commits any act prejudicial to the interest of the society or society is not functioning in accordance with the provisions of the Acts, Rules and bye-laws; then RCS may remove the said committee and appoint an Administrator for such period not exceeding one year.

• More than 70 % of total dues of any primary society, which is a credit society, against its members during any Co-operative year remain unpaid at the end of such year;

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• The number of defaulting members exceeds 70% of the total number of indebted members of such society at the end of such year; then the chairman and all the members of the committee shall vacate their offices.

Appointment of Special Officer:-

• Upon the report of the RCS or otherwise, the State Govt. may appoint a special officer.

• Maximum period of 2 years.

• Can be extended by another year.

• Special officer subject to control of RCS/State Government.

• Shall perform all functions of the Committee.

• Special officer shall before expiry of the term, arrange for constitution of a new committee.

Powers with State Govt. to give direction -

• In public interest.

• Affairs of the society being conducted detrimental to the interest of the members.

• That will be binding on the society.

• The above powers of the Govt. can be delegated to the RCS, by a specific notification.

Privileges of Co-operative Societies:

First charge of Co-operative society on certain assets

Charge on land owned by members or held as tenants by members borrowing loans from certain Co-operative societies.
Deduction from salary, to meet society's claim in certain cases-the employer shall be competent to deduct from the salary, or wages and pay, to the society in satisfaction of any debts.

Charge and set off in respect of shares or interest of members in the capital of a Co-operative society: - a Co-operative society shall have charge upon the share or interest in the capital etc. payable to a member and may set off any sum credited or payable to a member.

It shall not be necessary for any member of a committee, secretary or any other officer to appear in person or by agent at any registration office in any proceedings connected with registration of any instrument.

Management of funds and operation of bank account:

The group is to manage its own funds as also the fund it receives from outside. Normally the sources of funds for the group are membership fees, savings, fines, and donations, interest on loans, bank loan, bank interest, and contribution from outside. The fund is used for normal loaning as decided in the meetings as also for meeting emergencies faced by the group members. The cash is handled at three stages.

1. Secretary / treasurer holding cash meet emergencies.
2. Secretary / treasurer holding the savings before depositing in the bank.
3. The office bearers who are authorised to withdraw cash/loan from bank for disbursement among members.

All the members of the group must be gradually exposed to operating the bank account.
Group Discipline:

The group must function democratically and in disciplined manner. The repayment ethics, effectiveness of peer pressure, implementation of norms and sanctions reflect the discipline and dynamics of the group.

Participation of various agencies

It may not be untrue if it is said that not even a single Banking & Non-Banking Financial Institution has been left out which is not participating in the microfinance activities. Major players in the microfinance sectors can be categorised as under:

1. Formal Financial Institutions - Public sector Commercial Banks, Pvt. Sector Commercial Banks, Regional Rural Banks and Co-operative Banks
2. Micro Finance Institutions (MFIs) - NGO promoted, Section 25 companies, registered under Societies Act etc
3. Government - GoI in association with all the State Governments in implementing the one of the largest microfinance programme i.e., SGSY

Funds and Investment Management:

In the banking parlance, the term “Funds Management” encompasses raising of resources and application of resources in different forms of assets. The profit of a bank depends primarily on the utilization of its funds in loans and advances, investments. Effective and efficient management of the funds and investment will bring prosperity to the banks.
Management of CRR

As per section 18 of the BR Act, every non-scheduled Co-operative bank shall maintain in India by way of cash reserves with self or by way of balance in current account with the RBI or the State Co-operative Bank of the State concerned or by way of net balance in current account, a sum equivalent to at least 3.0% of the total of its demand and time liabilities (DTL) in India, as on the last Friday of the 2nd preceding fortnight, and shall submit to RBI, before the 20th day of every month, a return showing the amount so held on alternative Friday during a month. Since no income accrues out of the amount maintained under CRR, banks should endeavor to maintain exactly 3.0% so that the statutory obligations are fulfilled while not losing any interest income.

Management of Statutory Liquidity Ratio (SLR):

In terms of Section 24 of BR Act, 1949 (AACS), a CCB/SCB or RRB. In addition to the CRR banks shall also maintain in India in cash, or in gold or in unencumbered approved securities, or in account with SCB, an amount which shall not, at the close of business on any day, be less than 25% of the total of its demand and time liabilities in India, as on the last Friday of the 2nd preceding fortnight. ‘Unencumbered approved securities’ are securities in which a trustee may invest money under clause (a) to (c) of Section 24(2).

The SLR portfolio includes non-earning assets like cash and balances in C/A and earning assets like investments in Government and other approved securities. In order to optimize the returns, the banks have to:-

I. Minimize the cash / balance in C/A portion to the extent possible
II. Restrict the SLR investments up to 25% or slightly more than that

III. Divert the non-SLR funds for investing in more lucrative avenues

**NON-SLR INVESTMENTS:**

1. Holding of Shares & Debentures in Private Sector Companies or Institutions other than Cop Sector. The Co-operative banks should not subscribe to the initial or subsequent issue of shares / debentures of private sector companies or bodies or organizations other than in Co-operative sector unless specifically permitted by the Reserve Bank.

2. Deposits with other institutions and other Co-operative banks:
   
   2.1 Scheduled Co-operative banks should not place deposits with any other Co-operative banks.
   
   2.2 Non-scheduled Co-operative banks may place deposits with strong scheduled Co-operative banks, fulfilling the following norms:-
   
   2.3 The Co-operative banks should not park their funds as deposits with other institutions / companies / corporations etc.
   
   2.4 Co-operative banks may, however, maintain balances in current accounts with other banks for meeting their clearing and remittance requirements.

3. **Investment in Certificate of Deposits (CDs):**

   All Co-operative Banks are permitted to make investments in CDs issued by scheduled commercial banks and other financial institutions approved by the Reserve Bank of India, subject to the fulfillment of certain conditions.
4. Fixing of prudential limits

4.1 The Board of Directors of banks should fix a prudential limit for their total investment in non SLR securities and sub limits for the following debt securities.

i) Bonds of public sector undertakings,

ii) Bonds / equity of All India Financial Institutions

iii) Infrastructure bonds floated by All India Financial Institutions

iv) Unsecured redeemable bonds floated by nationalized banks

v) Units of UTI and

vi) Certificate of deposits issued by scheduled commercial banks and other financial institutions approved by RBI

4.2 The total investment in (i) to (vi) above should not exceed 10 per cent of the banks' total deposits as on 31 March of the previous year, with a sub-ceiling of 5 per cent of incremental deposits of the previous year for investment covered.

4.3 Banks should ensure that exposure, to a single issuer of debt securities is within the individual exposure ceiling prescribed by RBI for grant of advances, based on the capital funds of the bank.

4.4 Banks which have exposures to investments in non-SLR securities in excess of the prudential limit prescribed above as on 31 March 2003 should not make any fresh investment in such securities till they ensure compliance with the above prudential limit.

4.5 As a matter of prudence, banks should stipulate entry-level minimum ratings/quality standards and industry-wise, maturity-wise, duration-wise etc, limits to mitigate the adverse impacts of concentration and risk of liquidity.
5. Role of Board of Directors:

5.1 Banks should ensure that their investment policies duly approved by the Board of Directors are formulated after taking into account all the relevant issues specified in these guidelines on non-SLR investment. Banks should put in place proper risk management systems for capturing and analyzing the risk in respect of non-SLR investment and taking remedial measures in time.

5.2 The board should devise a system to ensure that the limits prescribed in paragraph above are scrupulously complied. The Boards should appropriately address the issue of ensuring compliance with the prudential limits on an ongoing basis, including breaches, if any, due to rating migration.

5.3 Boards of banks should review the following aspects of non-SLR investments twice a year:

   I. Total business (investment and divestment) during the reporting period
   II. Compliance with the prudential limits prescribed by the Board for non-SLR investment
   III. Rating migration of the issuers/issues held in the bank’s books and consequent diminution in the portfolio quality.
   IV. Extent of non-performing investments in the non-SLR category and sufficient provision thereof.

Manner of Holding Mandatory Investments

   The Securities may be held in any of the three forms, viz, (a) Physical scrip form, (b) Subsidiary General Ledger (SGL) Account and (c) in a dematerialized account with the depositories (NSDL/CSDSL, NSCCL). In respect of securities
with SGL facility, the SGL account can be maintained in the bank’s own name directly with the Reserve Bank of India, or in a Constituent SGL Account (CSGL) opened with any scheduled commercial bank/State Co-operative Bank/Primary Dealer (PD) or Stock Holding Corporation of India Ltd (SHCIL). The Co-operative Banks are not permitted to open and maintain CSGL Account of other Co-operative Banks / other entities like charitable institutions trusts etc.

**General Guidelines regarding Investments**

1. The Co-operative Banks should not undertake any purchase/sale transactions with broking firms or other intermediaries on principal to principal basis.

2. No sale transaction should be put through by the Co-operative banks without actually holding the securities in their investment accounts, i.e., under no circumstances should banks hold an oversold position in any security.

3. For purchase of securities from the Reserve Bank through Open Market Operations (OMO), no sale transactions should be contracted prior to receiving the confirmation of the deal / advice of allotment from the Reserve Bank.

4. Only scheduled banks are at present permitted to become members of NDS and participation of DVP III mode for settlement of Government securities transactions.

5. Scheduled Co-operatives Banks may undertake retailing of Government securities with non-bank clients, such as provident funds, non-banking financial companies, high net worth individuals, etc, subject to the following conditions.
• Banks may freely buy and sell Government securities on an outright basis at the prevailing market prices without any restriction on the period between sale and purchase.

• Retailing of Government securities should be on the basis of ongoing market rates/yield curves emerging out of secondary market transactions.

• No sale of Government securities should be affected by banks unless they hold securities in their portfolio either in the form of physical scrip or in the SGL account maintained with the RBI.

• Immediately on sale the corresponding amount should be deducted by the bank from its investment accounts and also from its SLR assets.

• These transactions should be looked into by the concurrent / statutory auditors of the bank.

6. Scheduled Co-operative banks should put in place adequate internal control checks / mechanisms as advised by the RBI from time to time.

7. Banks may take advantage of the non-competitive bidding facility in the auction of the Government of India dated securities provided by the RBI. Under this scheme, banks may bid up to Rs two crore (face value) in any auction of Government of India dated securities, either directly, through a bank or through a primary dealer. For availing this facility, no bidding skill is required as allotment up to Rs two crore (face value) is made at the weighted average cut-off rate which emerges in the auction. Co-operative Banks may also participate directly or through a bank or a primary dealer in the auctions of State Development Loans, where coupon is mostly fixed in advance and notified by the RBI. An
advertisement in leading newspapers is issued 4 – 5 days in advance of the date of auction. Half-yearly auction calendar of GOI securities is also issued by the RBI.

8. CSGL Accounts should be used for holding the securities and such accounts should be maintained in the same bank with which the cash account is maintained. For all transactions delivery versus payment must be insisted upon by the banks.

9. In case CSGL account is opened with any of the non-banking institutions indicated above, the particulars of the designated funds account (with a bank) should be intimated to that institution.

10. All transactions must be monitored to see that delivery takes place on settlement day. The particulars of the designated funds account (with a bank) should be intimated to that institution.

11. Officials deciding about purchase and sale transactions should be separate from those responsible for settlement and accounting.

12. All investment transaction should be pursued by the Board at least once a month.

13. The banks should keep a proper record of the SGL forms received/issued to facilitate counter-checking by their internal control systems / NABARD inspectors / other auditors.

14. All purchase/sale transactions in Government securities by the banks should necessarily be through SGL Account (with RBI) or constituent SGL Account (with scheduled commercial banks/SCB/PD/SHCI or in a dematerialized account with depositories (NSWDL/CDSL/NSCCL).
15. No transactions in Government securities by a Co-operative bank should be undertaken in physical form with any broker.

16. The entities maintaining the CSGL/designated funds accounts are required to ensure availability of clear funds in the designated funds accounts for purchases and of sufficient securities in the CSGL Account for sales before putting through the transactions.

17. The security dealings of banks generally being for large value, it may be necessary to ensure, before concluding the deal, the ability of the counter-party to fulfill the contract, particularly where the counter-party is not a bank.

18. While buying securities for SLR purposes, the bank should ensure from the counter parties that the bonds it intends to purchase have and would continue to have SLR status. The bank should also verify this from independent sources in case of doubt.

19. In order to avoid concentration of risk, the banks should have fairly diversified investment portfolio. Smaller investment portfolios should preferably be restricted to securities with high safety and liquidity such as Government securities.

20. The Co-operative banks may seek the guidance of Primary Dealers’ Association of India / Fixed Income and Money Market Dealers’ Association (FIMMDA) on investment in Government securities.

**Management of Investment Risks:**

Investments are not risk free. It is important that the banks as well as IOs understand the various risks that are natural to investment banking. Some of the important risks are:
• Default risk
• Interest rate risk
• Reinvestment risk
• Purchasing power risk
• Liquidity / marketability risk
• Option risk

Default Risk

Default risk refers to the probability of default in repayment of principal or the payment of interest. Presently, Government Securities alone are considered default risk free. Though the inter bank deposits are treated similarly, still they have an element of default risk. In respect of other investments, credit rating of higher grade has to be selected so as to lower the default risk.

Interest Rate Risk

The possibility that a charge in the market rate of interest in a security will affect the price of the security adversely is known as the Interest Rate Risk.

Reinvestment Risk

Reinvestment risk arises in the event of a decline or fall in the interest rate. In such case, investments/interest on investments which mature will have to be reinvested at a lower rate of interest, resulting in reduction in the income.

Purchase Power Risk

Interest rate has two components, 'Real Interest Rate' and 'inflation'. In respect of fixed income security the coupon or interest rate remains fixed during the tenure of the instrument. However, if the inflation is on rise during this period,
the real rate of interest may gradually decline, reducing the purchasing power of the bank.

**Liquidity / Marketability Risk**

A security's liquidity is defined at the easy with which an investor can exit the instrument. Liquidity is ensured by availability of secondary market. Liquidity is also dependent on the issue size.

**Option Risks**

Call and Put options are sometimes regular features of some of the instruments. Under Call option, the issuer may redeem the instrument much before its maturity period, particularly in a falling interest rate scenario.

**BOARD MEETINGS:**

Board of Directors represents the general body. Though general body is the supreme body in the Co-operative democracy, it is the Board, which plans, takes important policy decisions and ensures the implementation of the policies framed. It draws its power from the members and acts on behalf of the members. As all the members cannot participate in the decision-making and management, the Board of Directors as the representative body of the members discharge the responsibilities entrusted to them. The Board meets more often than the general body. Usually it meets once in a month and more times when required. The decisions are taken jointly by the Board and all directors are expected to abide by the joint decision.
FUNCTIONS OF THE BOARD:

1. The main functions of the Board with reference to meetings are to frame policies, review the results and ensure maintenance of good-relations between the management and the members.

Framing Policies:

As the Co-operative banks are expanding their activities, they are required to improve the quality of their working and must be competent. The directors must be competent enough to frame pragmatic policies to satisfy the needs of the organization and its members.

Reviewing Results:

After the policies are framed, the directors are expected to entrust the responsibility of implementing them to the management appropriately and delegate powers accordingly to achieve the results. In the meanwhile, the progress must be reviewed by the Board at important stages. If the policy is apparently not a success, the Board must decide, after weighing all the evidence, whether to extend the trial period even at some cost or modify the policy, if necessary.

Maintaining Cordial Relations:

1. It is the responsibility of the Board to see that cordial relations exist between the management and the members and it should act as a bridge between the two groups. The Boards of Directors of Co-operative banks have the responsibility of overseeing the performance of the respective bank's operations and ensure that they function in accordance with the guidelines issued by the RBI/NABARD/GoI/State Government, and achieve the objectives set before
them. To enable the Boards of Directors to discharge this responsibility, the CEO/Secretary to the Board are expected to submit periodical reviews to their respective Boards on various operational aspects of the banks, particularly in respect of developmental objectives set before them. Periodical reviews are also placed before the Boards which throw light on the internal health of the institutions such as those relating to inter-branch reconciliation, vigilance, recovery of dues, etc.

2. The Board of Supervision (for SCBs, DCCBs and RRBs) constituted by NABARD reviewed the agenda items being placed before the Board of Directors of SCBs and DCCBs and observed that no uniform periodicity is observed by the banks in the submission of such reviews and that these notes do not encompass all the major aspects of banking operations. Such reviews, therefore, did not enable the Boards to take an overall view of the performance of the banks and identify the problems that the banks may face in specific areas to facilitate adoption of timely rectification measures. In short, a view emerged that the scope and content of some of the prescribed reviews did not meet the intended objectives and required suitable changes in the light of recent developments in the banking sector. The Board of Supervision also noted the need for division of the reviews into three parts, viz., reviews to be put up to (i) Board, (ii) Managing Committee and (iii) Audit Committee, so as to ensure that the deliberations get focused.

3. Accordingly the revised calendar of reviews to be put up to the Board, Managing Committee and Audit Committee are indicated below. SCBs/DCCBs should initiate necessary steps to submit specific reviews to the Board/Managing...
Committee/Audit Committee in accordance with the calendar. The calendar outlines the critical minimum requirements for review and the bank Boards will have discretion to prescribe additional reviews to suit their requirements.

4. The revised schedule may please be brought into force with immediate effect. If for any particular reason it is not possible to place a memorandum as per the calendar before the Board in the month it is due, a note should be put up to the Board giving reasons for the delay, indicating when the review is proposed to be placed before the Board.

A. Calendar of Reviews to be put up to the Board of Directors of SCBs and DCCBs

I. Every Board Meeting:

1. Funds Management

   I. Information about funds position of the bank

   II. Compliance with CRR/SLR requirements

   III. Details of investments in call deposits, non-SLR investments made, Securities traded and income earned / loss incurred, if any.

   IV. Compliance with RBI instructions in regard to maintenance of investments in Government Securities.

   V. Details of borrowings availed of from higher financing agencies (SCB/NABARD/State Govt., etc.) under various lines of credit limits vis-a-vis the Maximum Borrowing Power.

   VI. Position of deposits mobilised, amount invested in various avenues and advances made.
The report should not be a fact sheet but should capture qualitative data on the important market trends, market developments, regulatory initiatives, etc. between the review periods and should stimulate constructive suggestions and discussions on critical appraisal of the strategies followed presently and the need for changes.

VII. Concurrent audit report by internal auditors and compliance report thereon (to be placed before the CEO and Chairman every month).

2. Loans and advances:

I. Review of various credit limits sanctioned by Managing Director/Chairman/Executive Committee.

II. Sanction of term loans (for setting up/modernisation of sugar factory/spinning mill/ginning press, etc.) and follow up.

III. Participation in Consortium Finance.

IV. Adherence to exposure norms prescribed by RBI/NABARD.

3. General

I. Compliance in respect of outstanding observations of the Board.


III.Circulars received from RBI, NABARD, DICGC, RCS and Apex Bank.

IV. Implementation of the instructions/directives/guidelines issued by RBI/NABARD/Govt.

V. Submission of Statutory returns including OSS returns.
II. Quarterly

1. Business Plan: Targets and Achievements

I. Performance reviews vis-a-vis business goals such as deposit mobilisation, credit disbursal, recovery of loans, etc. The reviews should be comprehensive and cover specifically the bank's structural / organisational requirement. It should lead to initiation of business strategies of growth and profitability. The review should also contain bank's performance under special programmes of credit assistance like SHG, SGSY, etc.

II. Review of high yielding advances sanctioned by the bank.

III. Review of progress in implementation of Government sponsored programmes.

IV. Recoveries affected under NPA accounts. The report should be comprehensive and cover requisite details on the deficiencies observed, systemic controls required for avoidance of incidence of NPAs, etc. The review should also look at loan policy caveats on exposure thresholds, borrower-wise/industry-wise, etc. and other credit risk management initiatives on ongoing basis.

V. Details of OTS / waiver of irrecoverable loans / interest.

VI. Recovery under legal action (cases of ABN filed, decree/awards obtained and EPs filed/ executed).
2. Branch performance:

I. Branch-wise targets and achievements under various business parameters.

II. Review of branch profitability with suggestions measures to improve the position of loss making branches. Need for branch expansion and branch rationalisation.

III. Progress in inspection of branches and important observations of branch inspections.

IV. Review of discussions held during Branch Manager's review meetings.

3. Working Results:

An analysis of the working results of the bank on a quarterly basis along with an analytical note and proposals for future course of action. The bank's comparative position should also be highlighted.

4. Others:

I. A comprehensive review of the Vigilance Cell including position of vigilance cases and disciplinary cases initiated against the bank's staff and secretaries of affiliated societies.

II. Review of cases of frauds, misappropriations, embezzlements, defalcations, etc. together with action for recovery thereof. Review of cases of acuities and security arrangements in the bank.

III. A review of customer services rendered by the bank with analysis of complaints received and action taken.

Progress in implementation of the Action Plan prepared for recompliance with Section 11 of the B.R. Act, 1949 (AACS) - (For Sec.11 non-compliant banks).

V. Observations of the Audit Committee.

**Administrative controls**

Rotation of staff, keeping vigil on the style and expenditure of bank officers, periodical transfer of staff between branches/bank, are some of the common methods needed for administrative control. Also, staff members and officials whose integrity is in doubt should not be posted at sensitive desks. Suspect staff members must be kept under vigilance. Feedback from anonymous sources, complaints should also be followed up to the extent possible.

**Staff Accountability**

In view of the social responsibility cast on banks and to keep the incidence of corruption and malpractice under check, there is a need for fixing staff accountability for irregularities and malpractices at all levels, at the appropriate time. Inspector's/auditor's failure detects or report serious irregularities should also be viewed seriously. Clear guidelines for delegation of financial powers to different staff levels, sanction of advances, post-sanction monitoring etc. should indicate what constitutes abuse of authority, negligence in compliance to terms of sanction, monitoring etc. should be drawn up so that officer taking genuine business decisions are not victimized. In the process of fixing staff responsibility, the possibility of loss of employee morale should be carefully considered and
balanced. The aim of internal controls is basically to strengthen the banks and its operations on sound lines.

**Concurrent audit**

While the volume of operations in most Co-operative banks and RRBs do not warrant concurrent audit, the main branch/HO branch and other major branches may need to have concurrent audit so also provide checks and controls on key areas of branch functioning on a day to day basis. During concurrent audit of bigger branches having huge volume of transactions test-check of 10-25 % of income expenditure items, inter -branch and inter-bank accounts, interest paid, interest received on deposit accounts and clearing transactions should preferably be done by the bank's own staff.

The smaller branches will not be able to have concurrent audit system. Hence the audit function may have to be merged with the internal inspection system. The findings of concurrent audit need to be put up to the Board of Directors and compliance followed up by the Inspection Department.

**Internal Inspection /audit**

Banks often tend to use audit and inspection as interchangeable terms. To understand the scope of these terms, it is necessary to define these terms. Audit is a quantitative analysis of the operations of an organization with correct and honest record keeping in accordance with sound accounting principles and statutory requirements. The basic purpose is to assess the integrity of books of accounts and other records, to ensure that they reflect the assets and liabilities, income and expenditure, correctly. The scope of inspection is broader than that of audit and
also includes elements of audit as it is fundamentally a qualitative review of the affairs of an organization. Its objective is not only to verify observance of prescribed procedures and guidelines but also to promote and maintain safe and sound operating practices and conditions. Some banks have in internal inspection department often only on paper and some do not carry out any effective inspection of the bank's branches. The basic duties of inspection /audit are prevention and detection. The inspection schedule is to be finalized by the HO and periodicity, duly maintained. The follow-up of compliance is to be done by the Inspection Department at HO and depending upon irregularities, special audit of problem branches should be taken up by the inspection Department from HO. Disciplinary action is to be taken against officers deputed for internal inspection, for perfunctory inspection reports and for not having reported on problem accounts and areas in specific branches inspected by them. All internal inspection reports as also compliance reports are to be put up to the Audit Committee /Board of Directors.

Vigilance Cell and Monitoring of frauds

Frauds in banks are acts of criminal deception resorted to by persons singly or in collusion with other to derive gains to which they are not entitled. Bank frauds are generally cases of misappropriation or criminal breach of trust, encashment of forged instruments, manipulation of books of accounts, operation of fictitious accounts and conversion of properly, unauthorized credit facilities extended for renewal or for illegal gratification, cheating and forgery and irregularities in forex transactions. Frauds in Co-operative banks and RRBs are
generally perpetrated by bank staff by flouting established systems and procedures. The primary responsibility for preventing frauds is that of the bank management. All frauds need to be followed up and monitored. Police action, as also internal inquiries need to be initiated so that the bank recovers its funds along with interest and is not put to pecuniary loss. Speedy action to plug operational loopholes has to be initiated and fraud cases have to be put up to the Board of Directors for information. Weak follow-up action on frauds by the bank will send wrong signals to other staff members of similar inclination and invite further desertion. While some banks have set up Vigilance Cells, these have not developed into effective instruments for curbing the growing trend of vigilance cases in banks. The Vigilance function in banks concentrates on the punitive role rather than on preventive or detective vigilance. Vigilance tends to concentrate only on action after complaints are received or after detection of frauds, malpractice and irregularities at a very late stage. The role of vigilance needs no emphasis especially in rural areas where non-repayment of bank dues is often linked by borrowers to rent-seeking officials. These vigilance cases should be vigorously followed up by the top management.

**Review by Board of Directors**

Follow-up of all audit/inspection reports and monitoring follow up action, need to be initiated by the Board of Directors as under:

I. To review follow-up action on audit/inspection reports whether internal or statutory

II. To ensure compliance on statutory inspection/audit reports
III. To ensure accountability for unsatisfactory compliance of inspection report, delay in compliance and non-rectification of deficiencies

IV. To take periodical review of accounting policies/system to ensure greater transparency in bank accounts and adequacy of accounting controls

V. To give directions in respect of lacunae observed in performance reports wherever necessary

VI. To review all frauds and vigilance cases with a view to reducing their occurrence

VII. To review progress in inter-branch and inter-bank reconciliation

VIII. To monitor process in balancing of books, clearing adjustment amounts, sundry/suspense items, balance sheet items and other house-keeping items

IX. To review funds management with specific reference to maintenance of CRR/SLR

X. To review investment policy particularly investments in non-SLR securities like shares and debentures

XI. To review the compliance with various sections of BR Act/RBI Act/Co-operative Societies Act/Rules / bye-laws as applicable to the concerned banks

Unless steps are taken immediately to review the internal controls systems in the bank and initiate measures to promote better housekeeping, accounting systems and maintain control over the banks operations, the Co-operative banks cannot expand their business levels and compete with other banks. Computerization also needs to be reviewed as a measure to have competitive edge, maintain customer services and have control over operations.
4.5 ECONOMIC DEVELOPMENT BY CO-OPERATIVE BANKS:

Long-held traditions of self-help gave impetus to small community-based co-operative societies that have evolved, with the help of the Aga Khan Fund for Economic Development (AKFED), into small co-operative banks, which then merged to form the Development Co-operative Bank, and eventually metamorphosed during the 1990s into the Development Credit Bank (DCB).

From its origins in small institutions addressing the needs of underserved communities, especially in the co-operative sector, DCB has emerged as a fully fledged commercial bank providing advanced corporate finance services at one end of the spectrum while continuing to service the needs of co-operative society borrowers.

The Aga Khan Fund for Economic Development (AKFED) is the single largest stakeholder in the Bank. The Fund holds a stake of 49% in the Bank. The AKFED promotes private sector initiatives and entrepreneurship through equity investment, in partnership with multilateral agencies, international investors, local development institutions and individuals.

AKFED also had a vital role in facilitating finance for home ownership by playing an instrumental role in the launch of the Housing Development Finance Corporation Limited (HDFC) in the mid 1970s.

Microfinance

As part of the Aga Khan Foundation's rural development activities, community organisations work to set up independent means of sustaining themselves, which is usually achieved through micro-credit schemes. For
example, a women's federation in Bharuch district in Gujarat state recently accessed a loan-based scheme for animal husbandry. Likewise, federations of farmers groups have considerably reduced agriculture input costs (seeds, fertilisers and pesticides) through bulk purchases based on demand from member institutions, simultaneously ensuring the quality of inputs supplied.

India and Economic Development: Speech from the President Smt. Pratibha Devisingh Patil in 9th All India Conference of Urban Co-operative Banks and Credit Societies:

The urban Co-operative credit movement in India is a century old. There are over 20 million members of urban Co-operative banks in India making it, in terms of membership, the largest Co-operative system in the world. It is a vast sector comprising over 1,850 urban banks and around 40,000 credit societies. The reserves of urban Co-operative banks aggregate to over Rs.1.1 lakh crore. Though the share of the Co-operative banking sector in the entire banking system in India is about 5 percent, it is an important segment considering the number of consumers availing of its services.

Visualizing the importance of Co-operatives in the development process, the first Prime Minister of India, Pandit Nehruji, said that he wanted to "convulse" the nation with Co-operatives. He had an abiding faith in the Co-operative system, the objective of which was to give small traders, artisans, factory workers and others access to institutional credit, instead of them going to the private moneylender and then often meeting with disastrous consequences. By catering to the credit requirements of people with limited means in the urban and semi-urban
centers, the urban Co-operatives seek the financial inclusion of people who are economically disadvantaged and this is extremely important for the equitable growth in the country.

In a fast globalizing world order and growing competition, the challenge is to have a strategy for the urban Co-operative banks who have the resilience to adapt to new requirements. A small number of Co-operatives have grown to be big entities and are in a position to meet competition, but a number of others need support for their survival.

The strength of the Co-operative movement is in its collectivity. Co-operative institutions, particularly small urban Co-operative banks and credit societies find it difficult to face competition from bigger players in the field, as the latter have at their command resources, technology and managerial competence, far greater than what Co-operative banks have. For the individual banks and societies to be competitive, the sector as a whole must be strong and each unit should be backed by collective strength. The urban banks ought to seriously consider ways of networking amongst themselves and aggregating their resources as well as their requirements so that they have the advantage of size while approaching the financial markets and dealing with larger entities. Such systems and structures exist in many countries, where a single strong apex body is providing the expertise and resources for the grassroots level banks to operate. The possibility of this could be examined in the Indian context. It is equally important to make use of new management systems and technological
advancements to modernize the urban Co-operative sector. They may also consider mobile banking to reach out to their clientele.

The unprecedented growth of our economy, year on year for the last few years, is also bringing about huge demographical changes. Rapid urbanization through migration is now resulting in a significantly large section of the population in urban areas being financially excluded. To bring them under the institutional fold for their financial and banking requirements is a challenge but it is also a tremendous opportunity for the urban Co-operative banks and credit societies. Organizational strengths such as committed leadership, efficient use of resources, transparency in operations and involvement of members are, however, pre-requisites for the Co-operatives to be able to take advantage of the opportunities. Improvement in overall governance should strengthen Co-operatives and equip them to become premier vehicles of financial inclusion.

The rate of growth of credit by Co-operative banks is not keeping pace with the rate of growth of credit by the rest of the banking sector. The share of Co-operative banks, both in the agricultural and in the urban sectors, appears to be progressively shrinking. This could, in the long run, have an adverse effect on credit to marginal farmers, artisans and weaker sections of society. It is, therefore, imperative that Co-operative banks are strengthened to be in a position to take up financing for the less privileged sections of society. It will be equally important for the co-operative banking sector to set targets and work out innovative strategies to achieve them. The innovative strategies should essentially aim at
improving the income levels of the beneficiaries, so that they do not fall into a debt trap.

The banking and the financial sector are essentially based on trust of the depositors and the public. The urban Co-operative credit sector must look at all avenues of increasing this trust. Aberrations that may have crept up over a period of time need to be addressed at the earliest. The country has a stake in self-help economic entities like Co-operatives.

Economic empowerment of women and involvement of youth is very essential for any meaningful growth. The financial sector in the post-reforms period in the country has been laying great emphasis on young financial professionals managing key posts in the sector. In fact, some of the highest paid professionals in the banking sector are young women. On the other hand, there is no such initiative in this direction by the Co-operative banking movement. Youth, as experience has shown, is attracted to and motivated to work in those areas where there is challenge, dynamism, an enabling environment and returns which are commensurate with their efforts. Co-operative leaders will have to do some self-analysis as to whether they are sincerely making efforts to provide all this to the youth so as to attract them. Otherwise, there is a distinct possibility of young professionals ignoring the sector altogether in the days to come. Urban credit societies, along with agricultural societies, can become a significant base for providing a range of activities with the involvement of youth for the creation and equitable distribution of wealth.
Insofar as supporting efforts to improve the economic position and empowerment of women are concerned, there is no route that is better than that of Co-operatives and Self Help Groups. Women Co-operative Banks are better acquainted with the situation and requirements of women. They can help channelize the capacities and talents of women and can become important instruments of economic betterment. Women Co-operative Banks, therefore, must be encouraged. Urban Co-operative banks should also have special programmes for women. I would be very happy if the management of the movement considers increasing the representation of women on the Boards of Co-operative banks and credit societies, to certain minimum levels through changes in their bye-laws, so that economic empowerment of women gets support at the grass-roots level.

Co-op Banking & Financial Inclusion:

For the financial inclusion of this group to be successful there is very little innovation that can be done in the office of the bank. But if the Bankers move in the field, they will be able to innovate products and services on the basis of observing clients, households, markets and workplaces to tailor the financial services to suit the needs of this segment. Thus to perform this challenging task of offering integrated financial services to the poor women, the Co-operative Banks are definitely more suited. The sense of co-operation is highly essential to harness the vast economic energy that is waiting to be unleashed in the poor women. Experiences world over in the developing nations have only reconfirmed the need for co-operative banking to bring about inclusion of this segment in the
mainstream economy. Again world over poor women have proved to be reliable borrowers and borrowers who have the family interest in mind.

Co-operative Banking and Agriculture sector:

To ensure that in the agricultural part of our Plan the village as a whole should be actively associated in framing targets, in suggesting suitable methods for achieving them, in evolving and directing a suitable organisation for day to day working and in checking periodically the progress made. A willing and constructive participation of the people can alone ensure the success of the Plan. While a general stirring of the aspirations of the people is to be noticed all over the country, the establishment and successful working of village organisations remain to be achieved in many parts. Latterly there has been a welcome earnestness on the part of State Governments for the establishment of Panchayats as civic and developmental bodies charged with the general responsibility of attending to the collective welfare of the village community. Panchayats have an indispensable role to play in the rural areas. As representing the best interests of all sections of the community their status is unique. Many activities such as, framing programmes of production for the village, obtaining and utilising governmental assistance for the betterment of the village, such as, the construction of roads, tanks, etc., encouraging villagers to improve the standards of cultivation, organising voluntary labour for community works and generally assisting in the implementation of economic and social reform legislation passed by the States, will naturally fall within the purview of the panchayat.

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On the other hand, for the working of individual programmes of economic development, where not only the general interest but also the specific responsibility and liability of a member have to be ensured, a more integrated and binding form of association is needed. Specific and practical tasks of reclaiming land, of providing resources for better cultivation, of marketing the product of the villagers, both agriculturists and artisans, can be best performed through co-operatives. The co-operative agencies will naturally have to conform to the principles of business management, namely, of satisfactory service and economical working. That they are not profiteering associations and that they function for mutual service makes them desirable agents of democratic planning. It is therefore very necessary that Co-operative agencies in the village should have the closest possible relationship with the principal democratic body namely, the panchayat. Though in the discharge of their functions the two bodies have specific fields to operate, in a number of common functions by having mutual representation and by having common ad-hoc committees, it will be possible to build up a structure of democratic management of developmental plans through the organisations, the panchayats and the co-operative societies. We therefore suggest that in so far as institutional reform is an essential part of the implementation of the Five Year Plan, emphasis in due proportion and in appropriate melds should be placed both on panchayats and on co-operative societies.

State Plan Schemes:-

Continuing Schemes:-
Integrated Co-Operative Development Project (ICDP):

The scheme aims at strengthening existing primary Co-operative societies and developing PACS/LAMPS for multipurpose activities to improve existing Co-operative structure and modernization and upgradation of management of Co-operatives. The financial assistance is provided to Co-operative societies through state government in the form of loan, share capital as well as subsidy under refinance scheme of National Co-operative Development Corporation (NCDC). In the year 2008-09, the project was implemented in Hazaribagh, Deoghar & Dumka. The projects in Deoghar, Dumka and Hazaribagh are completed on 31.12.08. This scheme is being implemented in the districts of Garhwa, Giridih and Latehar which was started during the year 2007-08 and five more districts namely Lohardaga, Dhanbad, Godda, Sahebganj and East Singhbhum during the current fiscal i.e. 2008-09 are to be covered under NCDC aided Integrated Co-operative Development Project. A sum of Rupees 995.00 Lakh is proposed as subsidy, share capital and loan for the year 2009-10.

Managerial Subsidy to PACS/LAMPS:

As per the recommendation of Reserve Bank of India PACS and LAMPS were formed. There are 474 LAMPS AND 857 PACS in the state. There is a provision of one Paid Manager in each PACS & LAMPS and one Co-operative Extension Officer as member Secretary in each LAMPS. The salaries of these personnel are given as Managerial subsidy by the government and disbursed through District Cadre co-operative societies. For the fiscal year 2009-10, a sum
of Rupees 100.00 Lakhs for PACS and Rupees 100.00 Lakhs for LAMPS are being proposed.

**Infrastructure for Primary Co-operative Societies and Regional Offices:**

There is an urgent need not only to create new/additional infrastructure already created become functional, but to achieve this goal Construction and repairing of Godowns in selected LAMPS/PACS/VMSS is required. At the same time, construction of combined office buildings for regional offices and strengthening of infrastructure of the same are also necessary. A sum of Rupees 550.00 Lakhs for Construction/Repairing of Godowns and other infrastructures including establishment of Hawler/Mini Rice Mills in LAMPS/PACS/VMSS and Rupees 25.00 Lakhs for Strengthening of infrastructure of Regional Offices are being proposed for the year 2009-10.

**Grant to Co-operative Training Centers at Ranchi and Deoghar:**

There are two Co-operative Training Centers at Ranchi and Deoghar each in the state, which imparts training to Junior Co-operative Officers, Office Bearers and Employees of different Co-operative Societies in the state. A sum of Rupees 12.00 Lakh is being proposed for imparting training and allied activities for the year 2009-10.

**Share Capital and Subsidy/Grant to special type of Co-operative Societies for the welfare of ST/SC/OBC and women:**

In the State, there are so many type of co-operative societies registered for welfare of SC/ST/OBC/Women. These Societies are not in a position to progress their own due to paucity of fund. Therefore the State Government assists them by
way of granting share capital and Subsidy. A sum of Rupees 75.00 Lakhs as share
capital and a sum of Rupees 300.00 Lakhs as Subsidy are proposed for the year
2009-10.

Share Capital Contribution of JASCOLAMPF, VEGFED and
JHAMCOFED:-

The Jharkhand State Co-operative Lac Marketing & Procurement
Federation Ltd. (JASCOLAMPF) and The Jharkhand State Vegetable Co-
operative Marketing Federation (VEGFED) are the apex Co-operative institution
of the state and they are doing procurement, processing, value addition and
marketing of lack and vegetables respectively. Jharkhand State Minor Forest
Produce Co-operative Development and Marketing Federation Ltd.
(JHAMCOFED) is also an apex Co-operative institution and will undertake
procurement, processing, value addition, marketing and development of minor
forest produce. A sum of Rupees 50.00 Lakhs, 50.00 Lakhs and 50.00 Lakhs
respectively as share capital for JASCOLAMPF, VEGFED and JHAMCOFED is
being proposed for the year 2009-10.

Computerization of DCCBs:-

This scheme aims at providing financial assistance to DCCB for
computerization, the total requirement of fund for computerization was Rupees
823.00 Lakhs and of which amount of Rupees 500.00 Lakhs allocated in the year
2008-09 rest amount of Rupees 323.00 Lakhs is proposed for the year 2009-10.
Loan and Subsidy to NCDC Aided Self Supporting Co-operative Societies:-

This scheme aims at providing financial support for the livelihood promotion and self employment generation in Poultry, Agri-horticulture and other Sectors to the under Privileged class through Self Supporting Co-operative Societies under N.C.D.C. Schemes. For this, a sum of Rupees 200.00 Lakhs is proposed for the year 2009-10 under N.C.D.C. Scheme to Self Supporting Co-operative Societies as Loan and Subsidy.

New Schemes:-

Transport Subsidy for Lifting of Fertilizer from IFFCO for LAMPS/ PACS/VMSS:-

The Primary Agriculture Credit Co-operative Society/ LAMPS & VMSS are purchasing fertilizer from IFFCO, to supply their farmer members, IFFCO is providing transport subsidy to these societies. The transport subsidy being provided by the IFFCO is so limited that most of the societies do not lift fertilizer because payment of extra transport cost shall either be a loss item for them or they shall have to sale the fertilizer at a higher price which will resultanty increase the cost of cultivation. Keeping in view the fertilizer availability even in remote villages of the state and to facilitate the poor farmers of the state to obtain fertilizer in uniform price it is proposed that transport subsidy be given to PACS/LAMPS & VMSS on fertilizer business equal to the transport subsidy being provided by the IFFCO to these societies. A sum of Rupees 50.00 Lakhs as subsidy for transport of fertilizer is proposed for this year 2009-10.
Interest Subvention to DCCBs Agricultural Loan:

The DCCBs are providing short term agriculture loans to the poor farmers of the state at 9% rate of interest. The DCCBs are allowed 2% interest subvention on Short Term Agriculture Credit from Govt. of India through NABARD. In view of backward agricultural condition and to boost up the agriculture in the state farmers need agriculture loan at a cheaper rate, which is available in other states like Chhatishgarh, Karnataka, etc. It is therefore proposed to provide 4% interest subvention for the small and marginal farmers of this state to enable the District Central Co-operative Bank to provide Short Term Agriculture Credit at 3% rate of interest. For this a sum of Rupees 300.00 Lakhs is proposed for the year 2009-10.

Subsidy for Construction of Cold Storages and other infrastructure for Co-operative Societies:

This Scheme aims at providing financial assistance to Co-operative Societies for setting up Cold Storage and other infrastructures for preservation and value addition of the fruits and vegetables etc. produced by the farmers. A total sum of Rupees 725.00 Lakhs is being proposed as Subsidy for the year 2009-10. Under this Scheme 90% of the total cost of construction will be provided by the State Government and rest 10% will be met by the beneficiary Co-operative Societies.