History of Urban Co-operative Banks in India
CHAPTER 3

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3.1 Introduction
3.2 Urban Co-operative Banks Defined
3.3 Need for Urban Banking
3.4 Origin and Development of Urban Co-operative Banks in India
3.5 Duality Control on Urban Co-operative Banks in India.
3.6 Progress of Urban Co-operative Banks
3.7 Recent Developments
3.8 Urban Co-operative Banks as Scheduled Banks
3.9 Federation of Urban Co-operative Banks
3.10 Objectives and Functions of Urban Co-operative Banks
3.11 Area of Operation
3.12 Membership
3.13 Management
3.14 Resources
   3.14.1 Deposits
   3.14.2 Borrowings
   3.14.3 Loan Operations
   3.14.4 Banking & other facilities
   3.14.5 Investments
3.15 Statewise progress of Urban Co-operative Banks

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CHAPTER 3

HISTORY OF URBAN CO-OPERATIVE BANKS IN INDIA

3.1 Introduction

One of the objectives of the research is to study development of co-operative Banking in India and Maharashtra State. This chapter explains the same. The term urban Co-operative Banks (UCBs) though not formally defined, refers to primary co-operative banks located in urban and semi-urban areas. These banks, till 1996, were allowed to lend money only for non-agricultural purposes. This distinction does not hold today. These banks were traditionally centered on communities, localities work place groups. They essentially lent to small borrowers and businesses. Today, their scope of operations has widened considerably.

The origin of the urban co-operative banking movement in India can be traced back to the close of nineteenth century when, inspired by the success of the experiments related to the co-operative movement in Britain and the co-operative credit movement in Germany such societies were set up in India, co-operative societies are based on the principles of co-operation-mutual help, democratic decision making and open membership. Co-operatives represented a new and alternative approach to organisation as against proprietary firms, partnership firms and joint stock companies which represent the dominant form of commercial organisation.
3.2 **Urban Co-operative Banks defined**

An urban co-operative Bank is defined as one which is organised for accepting deposits from the public, which is usually repayable by cheques which carry on normal banking business. Urban Banks are those credit societies which undertake all kinds of banking business including the acceptance of all types of deposits and the provisions of banking facilities for their clientele, such as making advances on personal surety, issue of drafts, discounting Hundis, collection of Bills etc.

3.3 **Need for Urban Co-operative Banking**

The need for Urban Co-operative Banking arises from the fact that Joint stock Banks are not interested in providing credit to the urban middle class. This is because it is not advantageous for joint stock banks in developing the business of small loans on account of high cost of advancing and receiving them. Further joint stock banks are not likely to have under ordinary circumstances, full and intimate knowledge of the standing and resources of persons of moderate means; they will not advance loans on personal securities. In such circumstances, the man with limited means in urban area may approach money lender. The establishment of Urban co-operative Bank is the most suitable alternative to these customers.

3.4 **Origin and Development of Urban co-operative Banks in India**

The first known mutual aid society in India was probably the 'Anyonya Sahakari Mandal'i organised in the erstwhile princely State of Baroda in 1889 under the guidance of Vithal Laxman Kavthekar. Urban co-operative credit societies, organised on a community basis to meet the consumption oriented credit needs of their members. From its origins then to today, the thrust of UCBs, historically, has been to mobilise savings from the middle and low income urban groups and purvey credit to their members - many of which belonged to weaker sections.

The enactment of Cooperative Credit Societies Act, 1904, however, gave the real impetus to the movement. The first urban cooperative credit society was registered in Canjeevaram (Kanjivaram) in the erstwhile Madras province in October, 1904. Amongst the prominent credit societies were the Pioneer Urban in Bombay (November 11, 1905), the No.1 Military Accounts Mutual Help Co-operative Credit Society in Poona (January 9, 1906). Cosmos in Poona (January 18,
in the Belgaum district, the Kanakavii-Math Co-operative Credit Society and the Varavade Weavers' Urban Credit Society (March 13, 1906) in the South Ratnagiri (now Sindhudurg) district. The most prominent amongst the early credit societies was the Bombay Urban Co-operative Credit Society, sponsored by Vithaldas Thackersey and Lallubhai Samaldas established on January 23, 1906.

The Cooperative Credit Societies Act, 1904 was amended in 1912, with a view to broad basing it to enable organisation of non-credit societies. The Maclagan Committee of 1915 was appointed to review their performance and suggest measures for strengthening them. The committee observed that such institutions were eminently suited to cater to the needs of the lower and middle income strata of society and would inculcate the principles of banking amongst the middle classes. The committee also felt that the urban cooperative credit movement was more viable than agricultural credit societies. The recommendations of the Committee went a long way in establishing the urban cooperative credit movement in its own right.

In the present day context, it is of interest to recall that during the banking crisis of 1913-14 when no fewer than 57 joint stock banks collapsed, there was a flight of deposits from joint stock banks to co-operative urban banks. Maclagan committee chronicled this event thus:

“As a matter of fact, the crisis had a contrary effect, and in most provinces, there was a movement to withdraw deposits from non-co-operatives and place them in co-operative institutions, the distinction between two classes of security being well appreciated and a preference being given to the latter owing party to the local character and publicity of co-operative institutions but mainly, we think, to the connection of Government with co-operative movement.”

The Government of India Act in 1919 transferred the subject of "Cooperation" from Government of India to the Provincial Governments. The Government of Bombay passed the first State Cooperative Societies Act in 1925 "which not only gave the movement its size and shape but was a pace setter of cooperative activities and stressed the basic concept of thrift, self help and mutual aid." Other States followed. This marked the beginning of the second phase in the history of Cooperative Credit Institutions.
There was the general realization that urban banks have an important role to play in economic construction. This was asserted by a host of committees. The Indian Central Banking Enquiry Committee (1931) felt that urban banks have a duty to help the small business and middle class people. The Mehta-Bhansali Committee (1939), recommended that those societies which had fulfilled the criteria of banking should be allowed to work as banks and recommended an Association for these banks. The Co-operative Planning Committee (1946) went on record to say that urban banks have been the best agencies for small people in whom Joint stock banks are not generally interested. The Rural Banking Enquiry Committee (1950), impressed by the low cost of establishment and operations recommended the establishment of such banks even in places smaller than taluka towns.

The first study of Urban co-operative banks was taken up by RBI in the year 1958-59. The Report published in 1961 acknowledged the widespread and financially sound framework of urban co-operative banks; emphasized the need to establish primary urban cooperative banks in new centers and suggested that State Governments lend active support to their development. In 1963, Varde Committee recommended that such banks should be organised at all urban centers with a population of 1 lakh or more and not by any single community or caste. The committee introduced the concept of minimum capital requirement and the criteria of population for defining the urban centre where UCBs were incorporated.

### 3.5 Duality of Control on Urban co-operative Banks in India

However, concerns regarding the professionalism of urban cooperative banks gave rise to the view that they should be better regulated. Large cooperative banks with paid-up share capital and reserves of Rs. 1 lakh were brought under the preview of the Banking Regulation Act 1949 with effect from 1st March, 1966 and within the ambit of the Reserve Bank's supervision. This marked the beginning of an era of duality of control over these banks. Banking related functions (viz. licensing, area of operations, interest rates etc.) were to be governed by RBI and registration, management, audit and liquidation, etc. governed by State Governments as per the provisions of respective State Acts. In 1968, UCBS were extended the benefits of Deposit Insurance.
Towards the late 1960s there was much debate regarding the promotion of the small scale industries. UCBs came to be seen as important players in this context. The Working Group on Industrial Financing through Co-operative Banks, (1968 known as Damry Group) attempted to broaden the scope of activities of urban co-operative banks by recommending that these banks should finance the small and cottage industries. This was reiterated by the Banking Commission (1969).

The Madhavdas Committee (1979) evaluated the role played by urban co-operative banks in greater details and drew a roadmap for their future role recommending support from RBI and Government in the establishment of such banks in backward areas and prescribing viability standards.

The Hate Working Group (1981) desired better utilisation of banks’ surplus funds and that the percentage of the Cash Reserve Ratio (CRR) & the Statutory Liquidity Ratio (SLR) of these banks should be brought at par with commercial banks, in a phased manner. While the Marathe Committee (1992) redefined the viability norms and ushered in the era of liberalization, the Madhava Rao Committee (1999) focused on consolidation, control of sickness, better professional standards in urban co-operative banks and sought to align the urban banking movement with commercial banks.

A feature of the urban banking movement has been its heterogeneous character and its uneven geographical spread with most banks concentrated in the states of Gujarat, Karnataka, Maharashtra, and Tamil Nadu. While most banks are unit banks without any branch network, some of the large banks have established their presence in many states when at their behest multi-state banking was allowed in 1985. Some of these banks are also Authorised Dealers in Foreign Exchange.

**3.6 Progress of Urban Co-operative Banks**

The Progress of Urban Co-operative Banks is shown in Table 3.1.
Table 3.1

Progress of Urban Banks and Primary Co-operative Banks

(‘ Crores)

<table>
<thead>
<tr>
<th>Sr. No.</th>
<th>Particulars</th>
<th>Urban Banks</th>
<th>Primary Co-operative Banks</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Number of Banks</td>
<td>815</td>
<td>1585</td>
</tr>
<tr>
<td>2</td>
<td>Membership (in lakh)</td>
<td>5</td>
<td>12</td>
</tr>
<tr>
<td>3</td>
<td>Own Funds</td>
<td>4</td>
<td>9</td>
</tr>
<tr>
<td>4</td>
<td>Deposits</td>
<td>17</td>
<td>32</td>
</tr>
<tr>
<td>5</td>
<td>Working Capital</td>
<td>22</td>
<td>44</td>
</tr>
<tr>
<td>6</td>
<td>Advances During the Year</td>
<td>19</td>
<td>32</td>
</tr>
<tr>
<td>7</td>
<td>Advances Outstanding</td>
<td>12</td>
<td>23</td>
</tr>
<tr>
<td>8</td>
<td>Overdues</td>
<td>1</td>
<td>3</td>
</tr>
</tbody>
</table>

Source: V. V. Ghanekar – Co-operative Movement In India P. 154, 155

It is observed from Table 3.1 that there is expansion of urban banks from 815 in 1948-49 to 1239 in 1988-89. It should be noted that with the introduction of Banking Regulation Act 1949 with effect from March 1966 urban banks with paid up share capital and reserves of Rs 1 lakh and above have been classified as primary co-operative banks. The Reserve Bank of India introduced scheme of rehabilitation of weak primary co-operative banks. Accordingly, 68 primary co-operative banks were rehabilitated in 1977-78.
3.7 Recent Development

Over the years, primary (urban) cooperative banks have registered a significant growth in number, size and volume of business handled. As on 31st March, 2003 there were 2,104 UCBs of which 56 were scheduled banks. About 79 percent of these are located in five states, - Andhra Pradesh, Gujarat, Karnataka, Maharashtra and Tamil Nadu. Recently the problems faced by a few large UCBs have highlighted some of the difficulties these banks face and policy endeavors are geared to consolidating and strengthening this sector and improving governance.

3.8 Urban co-operative Banks as Scheduled Bank

During the year 1988-89 11 primary co-operative banks each with demand and time liabilities of over ₹ 50 crores were included in the second schedule to the Reserve Bank of India Act, 1934. This is first time when primary co-operative banks have been scheduled. During the year 1988-89. The R. B. I cleared another 15 proposals for registration by the Registrar of co-operative societies.

3.9 Federation of Urban/Banks

With the growth of urban co-operative banks, their federation or associations have been formal in some of states including Gujrat, Karnata, Maharashtra, west Bengal, Madhya Pradesh, and the Union Territory of Delhi. Some of them published useful data on urban banks in their states. They held regional or state level seminars or conferences to discuss the problem faced by these banks and to suggest appropriate remedial measures.

The National Federation of Urban Co-operative Banks and credit societies have also been formed since February 1977 with its head quarter in New Delhi. It has composite membership of State Federations as well as individual urban banks. Its object is to activism, stimulate and regulate the urban banking movement in India. It holds seminars and conferences to discuss the difficulties faced by urban banks and its measures for their redress.

3.10 Objectives and Functions of Urban Co-operative Banks

The main objects and functions of the urban co-operatives are:
1) To attract deposits from members as well as non-members.
2) To advance loans to members.
3) To act as agent for the joint purchase of domestic and other requirements of the members.
4) To undertake collection of bills, accepted or endorsed by members.
5) To arrange for safe custody of valuable documents of members.
6) To provide other facilities as provided by commercial banks.

3.11 Area of Operation

The area of operation of an urban co-operative bank is usually restricted by its bye-laws to a municipal area or a town. In some cases it exceeds this area.

3.12 Membership

The membership of urban co-operative bank is composed of persons living in urban areas, such as traders, merchants, salaried and professional classes etc. The conditions relating to the membership are laid down in their bye-laws.

The membership of these urban co-operative banks varies considerably. In Tamilnadu, the average membership exceeded 7000, while in Maharashtra it was over 3000, in Kerala, it was 2500, in Orissa 2000, in Madhya Pradesh 1800, in West Bengal it was about 900.

3.13 Management

The management of urban co-operative Bank rests in the board of Directors, who are elected by General Body, consisting of all the members. The final authority in all matters rests with the general body but actual conduct of the affairs of the bank rests with the board of directors and the secretary of the bank.

The tenure of office of the Board of Directors varies in the states. The usual practices are to hold elections (a) each year (b) once in three years, and (c) each year by rotation for one third of the board. Holding the elections every year is not favoured by the study group. The advantages of holding elections once in three years are that expenses are kept at a minimum and the board of directors has time to learn the working of the bank. It is also observed that in a large number of institutions the same persons were elected to the board of directors from term to
term. It can be checked by incorporating the clause in the bye-laws that prevents a person from contesting election more than one or two consecutive terms.

3.14 **Resources**

Owned funds and borrowed funds are main sources of finance of Urban Co-operative Bank. Own funds include paid up capital, accumulated reserves created out of appropriate from profits. Borrowed funds cover deposits of members and non members and loan from central co-operative banks.

3.14.1 **Deposits**:
The percentage of deposits to working capital varied from state to state. It was 76% total capital in 1967-68. These banks have succeeded in attracting deposits from non members also because of growing public confidence in their working. These banks generally accept current deposits, saving deposits and fixed deposits. But with increasing competition by the commercial banks, more intensive efforts will be required by urban co-operative banks to attract more deposits.

3.14.2 **Borrowing**:
Such borrowings of urban co-operative banks from other financing agencies are negligible. These banks generally borrow from central co-operative bank, while a few borrowed from the appex banks. The study group on credit co-operatives in the Non Agricultural Sector (1963) that the urban banks should be affiliated with central co-operative banks and appex banks should not finance them directly.

3.14.3 **Loan Operation**:
The loan operations of UCB (Urban Co-operative Banks) consists of granting fixed loans or cash credit loans to their members against mortgage of unencumbered immovable property, or on surety of one or more persons who are also members. The member is eligible for loan against personal security upto 5 to 10 times the share capital paid by him.
3.14.4 Banking and other facilities:
UCBs provide facility of withdrawal of deposits by cheque and arrange for remittance of funds to other centre. Some banks collect pensions, pay regularly insurance premiums of its members, discount hundis and bills.

3.14.5 Investments:
The UCBs invest their surplus money in government and other trustee securities.

3.15 Statewise Progress of Urban Co-operative Banks:
During the period 1919-38, many urban credit co-operatives came to be organised in Bombay and Madras provinces’. The Urban Credit Societies which came into being in Bombay confined their activities to the members of particular communities and their lending operations were also primarily with a view to meeting the consumption needs of their members. Later, the economic boom created by the Second World War (1939-45) provided a stimulus to the growth of urban banks in India.

The usefulness of urban banks in financing artisans, small traders, factory workers and urban middle classes was recognised by various committees and working groups such as Central Banking Enquiry Committee (1931), the Co-operative Planning Committee (1946) The Study Group on credit co-operatives in Non Agricultural Sector (1963), the Working Group on industrial Financing through Co-operative Banks (1968). Certain provisions of Banking Regulation Act 1949 were extended to Urban Co-operative Banks having paid up share capital and reserves of ` 1 Lakh. The Reserve Bank acquired control over the functioning of Urban Co-operatives Banks especially in respect of maintenance of reserves and liquid assets, regulation of loans and advances, opening new branches etc.

The Urban Co-operatives Bank having paid up share capital and reserves of ` 1 lakh was classified as Primary Co-operative Bank, by Reserve Bank of India in 1968. Total number of these Primary Co-operative Banks was 1408 in June 1978. The State wise distribution indicates that Maharashtra is top with 348 banks, followed by Gujarat (265), Karnataka (225), Andhra Pradesh (132) Tamil nadu (131) and West Bengal (111), Kerala had (67) such banks while all other states had less than 25 each.
Over the years, Primary (Urban) Co-operative Banks have registered a significant progress in growth, in number and size and volume of business handled. As on 31st March 2003, there were 2104 UCBs of which 56 were scheduled banks. About 79 percent of these banks are located in five states – Andhra Pradesh, Gujrat, Karnataka, Maharashtra and Tamilnadu.
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