JPNN|Mumbai | July 17, 2014|A week after Budget announcement, the Reserve Bank Thursday issued draft guidelines for setting up of 'local feel' small banks, which will disburse small-ticket loans to farmers and

businesses. The central bank also issued draft guidelines for setting up of payment banks, which will cater to marginalised sections of society, including migrant labourers, for collecting deposits and remitting funds. Such banks can be set up with a minimum capital of Rs 100 crore as against Rs 500 crore required for normal commercial banks, according to the guidelines. "Both payments banks and small banks are 'niche' or 'differentiated' banks, with the common objective of furthering financial inclusion," the RBI said while issuing draft guidelines for licensing of payments banks and small banks. The proposed small banks will provide a whole suite of basic banking products such as deposits and supply of credit, but in a limited area of operation, it said. On the other hand, payments banks will offer a limited range of products such as acceptance of demand deposits and remittances of funds. They will have a widespread network of access points particularly in remote areas, either through their own branch network or through Business Correspondents (BCs) or through networks provided by others. Foreign investments in these new category banks would be as per the FDI policy.The existing non-bank pre-payment instrument issuers, non-banking finance companies (NBFCs), corporate BCs, mobile telephone companies, super-market chains, companies, real sector cooperatives and public sector entities may apply to set up a payments bank.In case of small banks, resident individuals with 10 years of experience in banking and finance, companies and Societies will be eligible as promoters to set up small banks.

NBFCs, micro finance institutions (MFIs), and Local Area Banks (LABs) can also opt for conversion into small banks. "Preference will be given to professionals from banking or financial sector, NBFCs and MFIs to set up small banks, if they meet the 'fit and proper' criteria," the draft said.Local focus and the ability to serve smaller customers will be a key criterion in licensing such banks, it said. "The area of operations of the small bank will normally be restricted to contiguous districts in a homogeneous cluster of States/Union Territories so that the bank has the 'local feel' and culture," it said, adding, the bank may be allowed to expand in one or more states with geographical proximity. In his Budget speech on July 10, Finance Minister Arun Jaitley had said: "RBI will create a framework for licensing small banks and other differentiated banks. Differentiated banks serving niche interests, local area banks, payment banks etc. Are contemplated to meet credit and remittance needs of small businesses, unorganized sector, low income households, farmers and migrant work force."

Earlier in April, the RBI had given in-principle approval to IDFC and Bandhan Financial Services to set up full-fledged banking operations. The RBI is working on the guidelines for continuous authorisation of universal banks and will come out with these separately. At present, there are 27 public sector banks and 22 private sector lenders in the country. Recently, RBI Governor Raghuram Rajan had said that the proposed Post Bank could start as a payment bank, making use of post office outlets to raise deposits and make payments. For setting up of payment bank, preference will be given to those applicants who has access points primarily in the under-banked states or districts in the North-East, East and Central regions of the country.

However, to be effective, the payments bank should ensure widespread network of access points particularly to remote areas, either through their own branch network or BCs or through networks provided by others. The bank is expected to adapt technological solutions to lower costs and extend its network, it said. Of the minimum capital, the guidelines said, the promoters' initial minimum contribution will be at least 40 per cent, to be locked in for a period of five years. Shareholding of the promoters should be brought down to 40 per cent within three years, 30 per cent within a period of 10 years, and to 26 per cent within 12 years from the date of commencement of business of the bank, it said. As far as small banks are concerned, it will be subject to all prudential norms and regulations of RBI as applicable to existing commercial banks including requirement of maintenance of Cash Reserve Ratio and Statutory Liquidity Ratio. However, in view of concentration of its area of operations, the small bank will be required to have a well diversified portfolio of loans and advances spread over its area of operations, it said. "The maximum loan size and investment limit exposure to single or group borrowers or issuers would be restricted to 15 per cent of its capital funds," it said.

At least 50 per cent of its loan portfolio should constitute loans and advances of size upto Rs 25 lakh in order to extend loans primarily to micro enterprises, it said. In case of small banks shareholding by promoters in the bank in excess of 40 per cent should be brought down to 40 per cent within three years from the date of commencement of business of the bank. "Further, the promoter’s stake should be brought down to 30 per cent of the paid-up voting equity capital of the bank within a period of 10 years, and to 26 per cent within 12 years from the date of commencement of business of the bank," it said. Entities other than promoters will not be permitted to have shareholding in excess of 10 per cent of the voting equity capital of the bank. Suggestions and comments on these draft guidelines should be sent to RBI by August 28. Agency