RBI releases Guidelines for on tap Licensing of Small Finance Banks in the Private Sector

The Reserve Bank had issued the Guidelines for Licensing of “Small Finance Banks” in the Private Sector on November 27, 2014. Recently, RBI released the revised guidelines on the same. Major changes from the earlier Guidelines on Small Finance Banks dated November 27, 2014, are (i) The licensing window will be open on-tap; (ii) minimum paid-up voting equity capital / net worth requirement shall be ₹ 200 crore; (iii) for Primary (Urban) Co-operative Banks (UCBs), desirous of voluntarily transiting into Small Finance Banks (SFBs) initial requirement of net worth shall be at ₹ 100 crore, which will have to be increased to ₹ 200 crore within five years from the date of commencement of business. Incidentally, the net-worth of all SFBs currently in operation is in excess of ₹ 200 crore; (iv) SFBs will be given scheduled bank status immediately upon commencement of operations; (v) SFBs will have general permission to open banking outlets from the date of commencement of operations; (vi) Payments Banks can apply for conversion into SFB after five years of operations, if they are otherwise eligible as per these guidelines.

Snapshot of the guidelines are as follows:

Objectives :The objectives of setting up of small finance banks will be for furthering financial inclusion by (i) provision of savings vehicles primarily to unserved and underserved sections of the population, and (ii) supply of credit to small business units; small and marginal farmers; micro and small industries; and other unorganised sector entities, through high technology-low cost operations.

Eligibility Criteria: Resident individuals/professionals (Indian citizens), singly or jointly, each having at least 10 years of experience in banking and finance at a senior level; and Companies and Societies in the private sector, that are owned and controlled by residents (as defined in FEMA Regulations, as amended from time to time), and having successful track record of running their businesses for at least a period of five years, will be eligible as promoters to set up small finance banks.

Existing Non-Banking Finance Companies (NBFCs), Micro Finance Institutions (MFIs), and Local Area Banks (LABs) in the private sector, that are controlled by residents (as defined in FEMA Regulations, as amended from time to time), and having successful track record of running their businesses for at least a period of five years, can also opt for conversion into small finance banks after complying with all legal and regulatory requirements of various authorities and if they conform to these guidelines. Further, existing Payments Banks (PBs) which are controlled by residents and have completed five years of operations are also eligible for conversion into small finance banks after complying with all legal and regulatory requirements of various authorities and if they conform to these guidelines.

Corporate Structure: The promoters / promoter group may choose to set up the small finance bank either as a standalone entity or under a holding company, which shall act as the promoting entity of the bank. However, if there is an intermediate company between the small finance bank and its promoting entity, it should be a Non-Operative Financial Holding Company (NOFHC). If the promoters desire to set up the small finance bank under a holding company structure, without an NOFHC, the holding company / the promoting entity shall be registered as an NBFC – CIC with the Reserve Bank.

Scope of activities: The small finance bank, in furtherance of the objectives for which it is set up, shall primarily undertake basic banking activities of acceptance of deposits and lending to unserved and underserved sections including small business units, small and marginal farmers, micro and small industries and unorganised sector entities. It can also undertake other non-risk sharing simple financial services activities, not requiring any commitment of own fund, such as distribution of mutual fund units, insurance products, pension products, etc. with the prior approval of the RBI and after complying with the requirements of the sectoral regulator for such products.

Capital requirement: The minimum paid-up voting equity capital for small finance banks shall be ₹ 200 crore, except for such small finance banks which are: a. transited from UCBs for which the capital requirement will be as prescribed in eligibility criteria and b. converted from NBFC/MFI/LAB/PB for which the capital requirement will be as prescribed in conditions for NBFCs/MFIs/LABs/PBs converting into a bank. In view of the inherent risk of a small finance bank, it shall be required to maintain a minimum capital adequacy ratio of 15 per cent of its risk weighted assets (RWA) on a continuous basis, subject to any higher percentage as may be prescribed by RBI from time to time. Tier I capital should be at least 7.5 per cent of RWAs. Tier II capital should be limited to a maximum of 100 per cent of total Tier I capital. Basel II norms will be generally applicable to the small finance banks, unless stipulated otherwise.

The detailed Guidelines for 'on tap' Licensing of Small Finance Banks in the Private Sector released by RBI are enclosed for your kind reference.

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