

REGULATOR'S ROLE

Relevant for: Indian Economy | Topic: Issues relating to Growth & Development - Banking, NPAs and RBI

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It is a fraught time for India's central bank. After a much publicised conflict between the government and the RBI, which finally led to the exit of Governor Urjit Patel and a knock to its institutional reputation, it has been dealt another blow by the Supreme Court, which has told the regulator that it is duty bound to disclose the list of defaulters and also make public its annual inspection reports of banks and financial institutions. The SC, while stating that the RBI had committed contempt of court, has warned the regulator that non-compliance of its order would be taken seriously as the bank had been refusing to provide information on all these under the RTI Act, citing its disclosure policy. The other legal test the RBI faces is the unprecedented case of a regulated entity — the Kotak Bank — taking it to court over a regulatory ruling on lowering the shareholding of the original promoter of the bank.

For long, the RBI has resisted disclosure of defaulters on the ground that it would violate banking secrecy laws while justifying holding back information and inspection reports of its supervisory teams on individual banks on fears of a weakening of trust among depositors and the impact on the financial markets and stocks of listed banks. There is some truth to this argument in a country with low levels of financial literacy given that in the past, the country's finance minister and the RBI were forced to publicly assure depositors and investors of a private bank that their money was safe after a run on the bank, fuelled by rumours. Similarly, realising the potential damage which could arise because of the interpretation of a provision in the Financial Resolution and Deposit Insurance Bill on protection of deposits, the government had to step in last year to assuage concerns.

That does not, however, mean non-disclosure in perpetuity. One approach could be to provide this information after the RBI and the bank or an institution and its board have achieved closure and taken action based on regulatory findings, to limit any damage. This could be preferably to Parliament, which could help strengthen prudential supervision. As successive RBI governors and bankers have indicated, the pile up of bad loans in India is also because of judicial delays. India's two-year-old insolvency law has been a signature reform, but at the end of last year in over 30 per cent of the cases, the 270-day deadline had been breached. It is with good reason that after the 2008 financial crisis, governments worldwide are focussed on financial stability. Any hasty step which engenders that mandate may prove costly.

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