

A WELCOME RETREAT: WITHDRAWING THE FRDI BILL

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

In just under 12 months since its introduction in Parliament, the [Centre has quietly withdrawn the Financial Resolution and Deposit Insurance Bill, 2017](#). The decision to seek the Lok Sabha's approval to withdraw the legislation this week is a clear acknowledgement by the government that it had underestimated the extent and intensity of public opposition to the proposed law. One provision in the Bill had, in particular, generated the greatest debate and attracted the fiercest criticism and ultimately proved to be its very undoing: the "bail-in" clause. That banks, by the very nature of their business, are essentially dependent on the funds lent to them by depositors to serve as the pool of lendable resources from which they provide credit to borrowers is well known and requires no elaboration. So when a depositor apprehends that her hard-earned savings placed in a bank may be at risk from a law that forces her to partake in the pain of financial losses in case her bank is forced into resolution on account of distress, she will naturally fear such a legislation. The government did make strenuous efforts to reassure the public, explaining the rationale for the Bill as well as the built-in "safeguards" relating to the bail-in provision. However, its exertions made little headway. Union Minister Piyush Goyal finally informed the joint parliamentary committee that was reviewing the Bill that a "resolution of these issues would require a comprehensive examination and reconsideration", and that therefore the government deemed it "appropriate" that the Bill be withdrawn.

However, the need for a specialised dispensation to cope with large financial corporations on the verge of going bust cannot be overstated, especially given the contagion risk that a bank failure can pose to overall financial stability. The withdrawal of the FRDI Bill should therefore be used as an opportunity by policymakers to reappraise the existing framework for resolving bankruptcy scenarios among financial entities. While such a review ought to include an evaluation of the progress made by the Insolvency and Bankruptcy Code in addressing the crucial issue of debt resolution in the banking sector, it must also look at ways to strengthen the Deposit Insurance and Credit Guarantee Corporation. Set up in the early 1960s in the aftermath of the collapse of two banks, the DICGC, which guarantees repayment of bank deposits up to 1 lakh in case a bank is liquidated, has not reviewed the amount under guarantee since 1993. This anomaly must be addressed, especially at a time when several state-run public sector banks have been roiled by a series of frauds and high levels of bad loans. Any measure that helps prevent further erosion of public faith in the beleaguered banking system would undoubtedly be very welcome.

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