

Are Our Regulators Imaginative?

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The recent deposit ponzi scam in West Bengal and the proliferation of such dodgy small-depositor financial schemes in other parts of the country point to the inadequate role of financial regulators. Despite ample examples of the misery they cause, the regulators have not yet responded to the challenges, leaving poor investors at the mercy of the scamsters.

In several caricatures drawn by Max Beerbohm, the eyes of the politicians featured are usually closed; they stand out as blank statues in their own lifetime. If Max were alive today, our regulators would have caught his fancy. He might well have depicted them “sans teeth, sans eyes, sans taste, sans everything”.

Indeed it is season time for caricatures. A storm has come and gone, and thousands have lost everything because they did not know how to protect themselves. It is all their fault. They should have learnt to behave as rational human beings. If they were greedy, god has served them right. They must have skipped their daily prayer: “Lead us not into temptation but deliver us from evil”.

But they deserve some thanks as well, for, unwittingly, they have sparked off great scenes of entertainment. It helped politicians chisel their vocabulary of abuse against their opponents; news channels ran thrilling episodes of verbal fisticuffs, upstaging their mainstream entertainment rivals; newspaper readers have been buried under salacious verbiage even as the truth remains as largely elusive as ever. The enforcement agencies are clueless, going from nowhere to nowhere while lawyers are busy searching for loopholes in the existing laws. Great opportunities have opened up for them. They now have to defend several culprits, sorry, celebrities!

Absent Regulators

In this great drama, the regulatory agencies are missing. But they have to answer questions; they cannot be allowed to remain cosy in their isolation. Storms never come without warning. There are agencies to spot and track them, to issue warnings by the hour, to alert disaster management groups and protect the probable victims.

Questions do arise about the behaviour of the regulatory agencies: some laden with emotional overtones, some accusatory, but all underlined by a feeling of wrenching sadness. We have always known politicians have a habit of letting us down, but regulators? Never. So the question arises, was the trust in them misplaced?

Regulators must have been aware that several mushroom companies were raising huge sums by way of deposits or similar instruments from poor people in rural and semi-urban areas. Masterminded by a few politically connected unscrupulous persons, these companies were duping poor people of their lifelong savings, luring them with false promises. This is not a new phenomenon in the financial world. If the regulators were not aware of what was happening, they owe an explanation to the citizens of the country. It is their duty to keep their antenna up and tuned.

Even if they knew little, they must have known — if we are to go by several notorious precedents — that these money-raising schemes could blow up any time. Was it not then their duty to use as many forums as they could to give out warnings? They could have taken advantage of our extensive television network to reach the remotest corners of the country. Of course, being regulators, they should have avoided making direct references to any particular company, but a message in general terms sent out continually would have served the purpose.

They could have also promoted television and radio discussions on the subject involving well known persons from various areas, such as commercial bankers, cooperative bankers, members of state legislatures, district councils, and panchayat samitis. These discussions would have also served the purpose of promoting financial literacy, while alerting rural people against dubious money-raising schemes.

Implicit Approval

Why did the regulatory agencies not do all this? What is it that held them back? Is it lack of imagination? Is it a sort of philosophical concern about “archaic” regulatory ethics? Or is it — many would like to put this disturbing thought away — that those who were being duped have no voice, while the ones duping them are celebrities?

These celebrities are daring. Their suave dealings with the political masters are engineered to create regulatory diffidence, and in the course of time the inevitable happens, the silence of the regulator is interpreted by many as implicit approval. Witness what is happening in a case that is now before the Supreme Court. Would things have come to such a pass if the regulators, both the Reserve Bank and SEBI, had about two and a half decades back shown determination in finding out how a few companies were raising deposits from the public through shady instruments? Such cases have now become examples for other unscrupulous persons to follow.

If the regulators had intended to stay a step behind, they could have harnessed the

resources of the organised banking and financial system and persuaded these institutions to undertake joint publicity campaigns. That would have been the most fruitful utilisation of the funds earmarked by them for corporate social responsibility projects.

Banking the Poor

Of late, it is being increasingly reported that ordinary poor people are finding it difficult to open accounts in banks and deposit their small savings in safe institutions. The know-your-customer (KYC) requirements keep them out. It must be understood that the identification requirements for high net worth individuals and poor daily wage earners cannot be the same. We have to be imaginative. A different set of KYC requirements must be prescribed for the poor. The rules may well be relaxed for small-depositor accounts with a limit of, say, Rs one lakh.

It may be recalled that during the 1960s, many southern banks had agents to collect pigmy deposits from daily wage earners. This practice was later given up because of some misuse. The banks should be asked to reintroduce such schemes in rural areas now that there are ways to prevent such abuse through technology.

What is important and urgent today is that the points of deposit collection must be multiplied rapidly in rural areas. A number of new banks are needed in these areas to increase the existing coverage. While sanctioning new licences will take time, it makes eminent sense to immediately initiate moves to convert post offices into banks, as has been done in many countries. That would enhance the range of services available in scattered villages all over the country and help in keeping away deceitful and dodgy operators.

Let me, at the end, reproduce what I had written about a decade ago ("Behind the Celebrity Mask", 24 February, 2004) in the pages of this weekly:

Our style of regulatory tactics suited to the old style gentlemanly capitalism will not do. Our market intelligence system has to be extensive, but more important, it has to be unorthodox. Listen to the whisperings in the market place, create listening points all over—as many as possible; be attentive to signals that emit from there, have the courage to put uncomfortable questions to those who pose as financial celebrities, demonstrate independence and prove the credibility of the regulator. The rest will automatically follow.