SYLLABUS

Class – B.Com (Plain) IV Sem
Subject – Banking Law & Practice in India

Unit-I	Principles of Banking: Definition of Bank, Creation of Money: Present Structure of Commercial Banks India. Principles of Management in Banks: Managerial Functions in Bank, Recruitment, Selection, Training, Promotion and Control Staff.
Unit – II	Indian Banking System – Features, Money Lenders, Nationalization of Commercial Banks and its Effects, Classification of Banking Institutions. Reserve Bank of India – Functions, Control of Credit by RBI, Power of RBI.
Unit – III	Management of Deposits and Advances Deposit Mobilization, Classification and Nature of Deposit Accounts, Advances, Lending Practice, Types of Advances. Investment Management: Nature of Bank Investment, Liquidity and Profitability. Cheques, Bills and their Endorsement, Government Securities. Procedure of E – Banking
Unit – IV	Banking Regulation Act 1949 – Important provisions: Restrictions on Advances. Privatization of Banks, Narasimhan Committee Report, Banking Sector Reforms in India.
Unit – V	Management of Finance: Bank Accounts, Records, Reports, Statement of Advances, Appraisal of Loan Application. Development Banking In India – IFCI, IDBI, ICICI, Export Credit and Guarantee Corporation of India.

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Unit – 1

DEFINITION OF BANK:

A bank is an institution which deals with money and credit. It accepts deposits from the public, makes the funds available to those who need them, and helps in the remittance of money from one place to another. In fact, a modem bank performs such a variety of functions that it is difficult to give a precise and general definition of it. It is because of this reason that different economists give different definitions of the bank.

According to Crowther, a bank "collects money from those who have it to spare or who are saving it out of their incomes, and it lends this money to those who require it."

In the words of Kinley, "A bank is an establishment which makes to individuals such advances of money as may be required and safely made, and to which individuals entrust money when not required by them for use."

According to John Paget, "Nobody can be a banker who does not (i) take deposit accounts, (h) take current accounts, (iii) issue and pay cheques, and (iv) collects cheques-crossed and uncrossed-for its customers,"

Prof. Sayers defines the terms bank and banking distinctly. He defines a bank as "an institution whose debts (bank deposits) are widely accepted in settlement of other people's debts to each other."

Again, according to Sayers, "Ordinary banking business consists cash for bank deposits and bank deposits for cash; transferring bank deposits from one person or corporation to another; giving bank deposits in exchange for bills of exchange, government bonds, the secured promises of businessmen to repay and so forth".

According to the Indian Companies Act, 1949, banking means "the accepting for the purpose of Indian Companies lending or investment, of deposits of money from the public, repayable on demand or otherwise, and withdraw able by cheque, draft or otherwise."

In short, the term bank in the modern times refers to an institution having the following features:

i. It deals with money; it accepts deposits and advances loans.
ii. It also deals with credit; it has the ability to create credit, i.e., the ability to expand its liabilities as a multiple of its reserves.
iii. It is commercial institution; it aims at earning profit.
iv. It is a unique financial institution that creates demand deposits which serve as a medium of exchange and, as a result, the banks manage the payment system of the country.

HISTORY OF BANKING IN INDIA

Banking in India in the modern sense originated in the last decades of the 18th century. The first banks were **Bank of Hindustan (1770-1829)** and **The General Bank of India**, established 1786 and since defunct.

Colonial era

During the period of British rule merchants established **the Union Bank of Calcutta in 1829**, first as a private joint stock association, then partnership. Its proprietors were the owners of the earlier **Commercial Bank and the Calcutta Bank,** who by mutual consent created **Union Bank** to replace these two banks. In 1840 it established an agency at Singapore, and closed the one at Mirzapore that it had opened in the previous year. Also in 1840 the Bank revealed that it had been the subject of a fraud by the bank's accountant. Union Bank was incorporated in **1845 but failed in 1848**, having been insolvent for some time and having used new money from depositors to pay its dividends.

The **Allahabad Bank,** established in 1865 and still functioning today, is the oldest Joint Stock bank in India, it was not the first though. That honour belongs to the **Bank of Upper India**, which was established in **1863**, and which survived until 1913, when it failed, with some of its assets and liabilities being transferred to the **Alliance Bank of Simla**.

Foreign banks too started to appear, particularly in Calcutta, in the 1860s. The **Comptoir d'Escompte de Paris** opened a branch in Calcutta in 1860, and another in Bombay in 1862; branches in Madras and Pondicherry, then a French possession, followed. **HSBC** established itself in Bengal in 1869. Calcutta was the most active trading port in India, mainly due to the trade of the British Empire, and so became a banking centre.

The first entirely Indian joint stock bank was the **Oudh Commercial Bank**, established in 1881 in Faizabad. It failed in 1958. The next was the **Punjab National Bank**, established in Lahore in 1895, which has survived to the present and is now one of the largest banks in India.
Around the turn of the 20th Century, the Indian economy was passing through a relative period of stability. Around five decades had elapsed since the Indian Mutiny, and the social, industrial and other infrastructure had improved. Indians had established small banks, most of which served particular ethnic and religious communities.

The presidency banks dominated banking in India but there were also some exchange banks and a number of Indian joint stock banks. All these banks operated in different segments of the economy. The exchange banks, mostly owned by Europeans, concentrated on financing foreign trade. Indian joint stock banks were generally undercapitalized and lacked the experience and maturity to compete with the presidency and exchange banks. This segmentation let Lord Curzon to observe, *"In respect of banking it seems we are behind the times. We are like some old fashioned sailing ship, divided by solid wooden bulkheads into separate and cumbersome compartments."*

The period between 1906 and 1911, saw the establishment of banks inspired by the Swadeshi movement. The Swadeshi movement inspired local businessmen and political figures to found banks of and for the Indian community. A number of banks established then have survived to the present such as **Bank of India, Corporation Bank, Indian Bank, Bank of Baroda, Canara Bank** and **Central Bank of India.**

The fervour of Swadeshi movement lead to establishing of many private banks in Dakshina Kannada and Udupi district which were unified earlier and known by the name **South Canara** (South Kanara) district. Four nationalised banks started in this district and also a leading private sector bank. Hence undivided Dakshina Kannada district is known as "Cradle of Indian Banking".

During the First World War (1914–1918) through the end of the Second World War (1939–1945), and two years thereafter until the independence of India were challenging for Indian banking. The years of the First World War were turbulent, and it took its toll with banks simply collapsing despite the Indian economy gaining indirect boost due to war-related economic activities. At least 94 banks in India failed between 1913 and 1918.

Post-Independence
The partition of India in 1947 adversely impacted the economies of Punjab and West Bengal, paralysing banking activities for months. India's independence marked the end of a regime of the Laissez-faire for the Indian banking. The Government of India initiated measures to play an active role in the economic life of the nation, and the Industrial Policy Resolution adopted by the government in 1948 envisaged a mixed economy. This resulted into greater involvement of the state in different segments of the economy including banking and finance. The major steps to regulate banking included:

- The **Reserve Bank of India**, India's central banking authority, was established in April 1935, but was nationalised on 1 January 1949 under the terms of the Reserve Bank of India (Transfer to Public Ownership) Act, 1948 (RBI, 2005b).
- In 1949, **the Banking Regulation Ac**t was enacted which empowered the Reserve Bank of India (RBI) "to regulate, control, and inspect the banks in India".
- The Banking Regulation Act also provided that no new bank or branch of an existing bank could be opened without a license from the RBI, and no two banks could have common directors.

Nationalization in the 1960s

Despite the provisions, control and regulations of the Reserve Bank of India, banks in India except the **State Bank of India or SBI**, continued to be owned and operated by private persons. The first major step was Nationalization of the **Imperial Bank of India** in 1955 **via State Bank of India Act**. State Bank of India was made to act as the principal agent of RBI and handle banking transactions of the Union and State Governments.

By the 1960s, the Indian banking industry had become an important tool to facilitate the development of the Indian economy. At the same time, it had emerged as a large employer, and a debate had ensued about the nationalization of the banking industry. Indira Gandhi, the then Prime Minister of India, expressed the intention of the Government of India in the annual conference of the All India Congress Meeting in a paper entitled *"Stray thoughts on Bank Nationalization."* The meeting received the paper with enthusiasm.

Thereafter, her move was swift and sudden. The Government of India issued an ordinance ('Banking Companies (Acquisition and Transfer of Undertakings) Ordinance, 1969') and nationalized the 14 largest commercial banks with effect from the midnight of 19 July 1969. These banks contained 85 percent of bank deposits in the country. Jayaprakash Narayan, a national leader of India, described the step as a *"masterstroke of political sagacity."* Within two weeks of the issue of the ordinance, the Parliament passed the Banking Companies (Acquisition and Transfer of Undertaking) Bill, and it received the presidential approval on 9 August 1969.

A second dose of nationalization of 6 more commercial banks followed in 1980. The stated reason for the nationalization was to give the government more control of credit delivery. With the second dose of nationalization, the Government of India controlled around 91% of the banking business of India. Later on, in the year 1993, the government merged **New Bank of India** with **Punjab National Bank**. It was the only merger between nationalized banks and resulted in the reduction of the number of nationalized banks from 20 to 19. After this, until the 1990s, the nationalized banks grew at a pace of around 4%, closer to the average growth rate of the Indian economy.

Liberalization in the 1990s

In the early 1990s, the then government embarked on a policy of liberalization, licensing a small number of private banks. These came to be known as *New Generation tech-savvy banks*, and included Global Trust Bank (the first of such new generation banks to be set up), which later amalgamated with Oriental Bank of Commerce, **UTI Bank** (since renamed **Axis Bank**), **ICICI Bank** and **HDFC Bank**. This move, along with the rapid growth in the economy of India, revitalised the banking sector in India, which has seen rapid growth with strong contribution from all the three sectors of banks, namely, government banks, private banks and foreign banks.
The next stage for the Indian banking has been set up with the proposed relaxation in the norms for Foreign Direct Investment, where all Foreign Investors in banks may be given voting rights which could exceed the present cap of 10%,at present it has gone up to 74% with some restrictions.

The new policy shook the Banking sector in India completely. Bankers, till this time, were used to the 4–6–4 method (Borrow at 4%;Lend at 6%;Go home at 4) of functioning. The new wave ushered in a

modern outlook and tech-savvy methods of working for traditional banks.All this led to the retail boom in India. People not just demanded more from their banks but also received more.

Current period

By 2010, banking in India was generally fairly mature in terms of supply, product range and reach-even though reach in rural India still remains a challenge for the private sector and foreign banks. In terms of quality of assets and capital adequacy, Indian banks are considered to have clean, strong and transparent balance sheets relative to other banks in comparable economies in its region. The Reserve Bank of India is an autonomous body, with minimal pressure from the government.

With the growth in the Indian economy expected to be strong for quite some time-especially in its services sector-the demand for banking services, especially retail banking, mortgages and investment services are expected to be strong. One may also expect M&As, takeovers, and asset sales.

In March 2006, the Reserve Bank of India allowed Warburg Pincus to increase its stake in **Kotak Mahindra Bank** (a private sector bank) to 10%. This is the first time an investor has been allowed to hold more than 5% in a private sector bank since the RBI announced norms in 2005 that any stake exceeding 5% in the private sector banks would need to be vetted by them.

In recent years critics have charged that the non-government owned banks are too aggressive in their loan recovery with housing, vehicle and personal loans. There are press reports that the banks' loan recovery efforts have driven defaulting borrowers to suicide.

CREATION OF MONEY

In economics, money creation is the process by which the money supply of a country or a monetary region (such as the Eurozone) is increased. A central bank may introduce new money into the economy (termed 'expansionary monetary policy') by purchasing financial assets or lending money to financial institutions. Commercial bank lending then multiplies this base money through fractional reserve banking, which expands the total of broad money (cash plus demand deposits).

Central banks monitor the amount of money in the economy by measuring monetary aggregates such as M2. The effect of monetary policy on the money supply is indicated by comparing these measurements on various dates.

Money creation by the central bank

Monetary policy regulates a country's money supply, the amount of broad currency in circulation. Almost all modern nations have special institutions (such as the United States Federal Reserve System, the European Central Bank (ECB), and the People's Bank of China) for conducting monetary policy, often acting independently of the executive. In general, these institutions are called central banks and often have other responsibilities such as supervising the smooth operation of the financial system.

The primary tool of monetary policy is open market operations: the central bank buys and sells financial assets such as treasury bills, government bonds, or foreign currencies. Purchases of these assets result in currency entering market circulation, while sales of these assets remove currency. Usually, open market operations aim for a specific short term interest rate. In other instances, they might instead target a specific exchange rate relative to some foreign currency, the price of gold, or indices such as the Consumer Price Index. For example, the US Federal Reserve may target the federal funds rate, the rate at which member banks lend to one another overnight.

Other monetary policy tools to expand the money supply include decreasing interest rates by fiat; increasing the monetary base; and decreasing reserve requirements. Some other means are: discount window lending (as lender of last resort); moral suasion (cajoling the behavior of certain market players); and "open mouth operations" (publicly asserting future monetary policy). The conduct and effects of monetary policy and the regulation of the banking system are of central concern to monetary economics.

Quantitative easing

Quantitative easing involves the creation of a significant amount of new base money by a central bank by the buying of assets that it usually does not buy. Usually, a central bank will conduct open market operations by buying short-term government bonds or foreign currency. However, during a financial crisis, the central bank may buy other types of financial assets as well. The central bank may buy long-term government bonds, company bonds, asset backed securities, stocks, or even extend commercial loans. The intent is to stimulate the economy by increasing liquidity and promoting bank lending, even when interest rates cannot be pushed any lower.

Quantitative easing increases reserves in the banking system (i.e. deposits of commercial banks at the central bank), giving depository institutions the ability to make new loans. Quantitative easing is usually used when lowering the discount rate is no longer effective because interest rates are already close to or at zero. In such a case, normal monetary policy cannot further lower interest rates, and the economy is in a liquidity trap.

Physical currency

In modern economies, relatively little of the supply of broad money is in physical currency. The manufacturing of new physical money is usually the responsibility of the central bank, or sometimes, the government's treasury.

Contrary to popular belief, money creation in a modern economy does not directly involve the manufacturing of new physical money, such as paper currency or metal coins. Instead, when the central bank expands the money supply through open market operations (e.g. by purchasing government bonds), it credits the accounts that commercial banks hold at the central bank (termed high powered money). Commercial banks may draw on these accounts to withdraw physical money from the central bank. Commercial banks may also return soiled or spoiled currency to the central bank in exchange for new currency.

Money creation through the fractional reserve system

Through fractional reserve banking, the modern banking system expands the money supply of a country beyond the amount initially created by the central bank. There are two types of money in a fractional-reserve banking system: currency originally issued by the central bank, and bank deposits at commercial banks:

1. *central bank money* (all money created by the central bank regardless of its form, e.g. banknotes, coins, electronic money)
2. *commercial bank money* (money created in the banking system through borrowing and lending) – sometimes referred to as *checkbook money*

When a commercial bank loan is extended, new commercial bank money is created if the loan proceeds are issued in the form of an increase in a customer's demand deposit account (that is, an increase in the bank's demand deposit liability owed to the customer). As a loan is paid back through reductions in the demand deposit liabilities the bank owes to a customer, that commercial bank money disappears from existence. Because loans are continually being issued in a normally functioning economy, the amount of broad money in the economy remains relatively stable. Because of this money creation process by the commercial banks, the money supply of a country is usually a multiple larger than the money issued by the central bank; that multiple is determined by the reserve requirements or other financial ratios (primarily the capital adequacy ratio that limits the overall credit creation of a bank) set by the relevant banking regulators in the jurisdiction.

Money multiplier

The most common mechanism used to measure this increase in the money supply is typically called the *money multiplier*. It calculates the *maximum* amount of money that an initial deposit can be expanded to with a given reserve ratio – such a factor is called a *multiplier.* As a formula, if the reserve ratio is R, then the money multiplier m is the reciprocal, and is the maximum amount of money commercial banks can legally create for a given quantity of reserves.

In the re-lending model, this is alternatively calculated as a geometric series under repeated lending of a geometrically decreasing quantity of money: reserves lead loans. In endogenous money models, loans lead reserves, and it is not interpreted as a geometric series. In practice, because banks often

have access to lines of credit, and the money market, and can use day time loans from central banks, there is often no requirement for a pre-existing deposit for the bank to create a loan and have it paid to another bank.

The money multiplier is of fundamental importance in monetary policy: if banks lend out close to the maximum allowed, then the broad money supply is approximately central bank money times the multiplier, and central banks may finely control broad money supply by controlling central bank money, the money multiplier linking these quantities; this was the case in the United States from 1959 through September 2008.

If, conversely, banks accumulate excess reserves, as occurred in such financial crises as the Great Depression and the Financial crisis of 2007–2008 – in the United States since October 2008, then this equality breaks down, and central bank money creation may not result in commercial bank money creation, instead remaining as unlent (excess) reserves.[11] However, the central bank may shrink commercial bank money by shrinking central bank money, since reserves are required – thus fractional-reserve money creation is likened to a string, since the central bank can always *pull* money out by restricting central bank money, hence reserves, but cannot always *push* money out by expanding central bank money, since this may result in excess reserves, a situation referred to as "pushing on a string".

Alternative theories

There are also heterodox theories of how money is created. These include:

- Chartalism sees the state as creating money when it spends, and destroying it when it taxes. More importantly, the private banking system is not, in empirical terms, reserve-limited, so its creation of money is an endogenous process, driven by credit demand and lending willingness. This accounts for the power of the state's interest rate policy in governing most of the money supply in normal times. [12][13]
- Credit Theory of Money. This approach was founded by Joseph Schumpeter. Credit theory asserts the central role of banks as creators and allocators of money supply, and distinguishes between 'productive credit creation' (allowing non-inflationary economic growth even at full employment, in the presence of technological progress) and 'unproductive credit creation' (resulting in inflation of either the consumer- or asset-price variety).

PRESENT STRUCTURE OF COMMERCIAL BANKS IN INDIA:

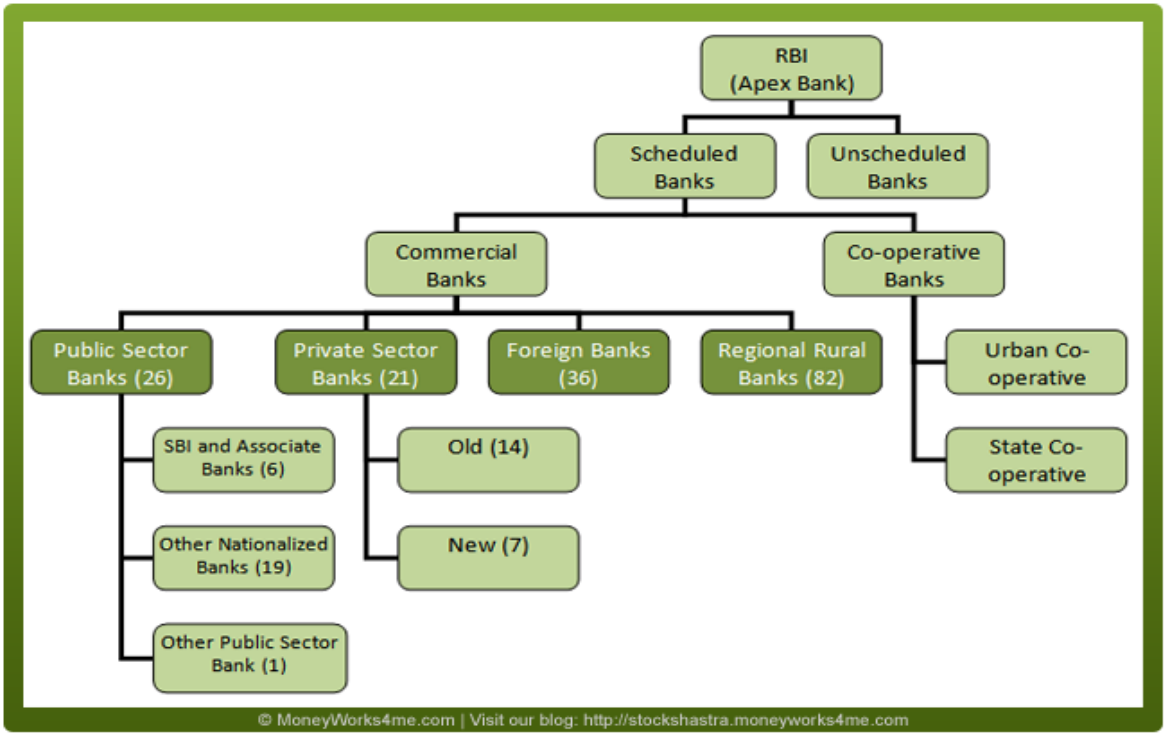
Banking in India in the modern sense originated in the last decades of the 18th century. The first banks were Bank of Hindustan (1770-1829) and The General Bank of India, established 1786 and since defunct.

The largest bank, and the oldest still in existence, is the State Bank of India, which originated in the Bank of Calcutta in June 1806, which almost immediately became the Bank of Bengal. This was one of the three presidency banks, the other two being the Bank of Bombay and the Bank of Madras, all three of which were established under charters from the British East India Company. The three banks merged in 1921 to form the Imperial Bank of India, which, upon India's independence, became the State Bank of India in 1955. For many years the presidency banks acted as quasi-central banks, as did their successors, until the Reserve Bank of India was established in 1935.

In 1969 the Indian government nationalised all the major banks that it did not already own and these have remained under government ownership. They are run under a structure know as 'profit-making public sector undertaking' (PSU) and are allowed to compete and operate as commercial banks. The Indian banking sector is made up of four types of banks, as well as the PSUs and the state banks, they have been joined since 1990s by new private commercial banks and a number of foreign banks.

Banking in India was generally fairly mature in terms of supply, product range and reach-even though reach in rural India and to the poor still remains a challenge. The government has developed

initiatives to address this through the State bank of India expanding its branch network and through the National Bank for Agriculture and Rural Development with things like microfinance.



As per Section 5(b) of the Banking Regulation Act 1949: "Banking" means the accepting, for the purpose of lending or investment, of deposits of money from the public, repayable on demand or otherwise, and withdawal by cheque, draft, order or otherwise."

All banks which are included in the Second Schedule to the Reserve Bank of India Act, 1934 are scheduled banks. These banks comprise Scheduled Commercial Banks and Scheduled Cooperative Banks.

Scheduled Commercial Banks in India are categorized into five different groups according to their ownership and / or nature of operation. These bank groups are:
(i) State Bank of India and its Associates,
(ii) Nationalized Banks,
(iii) Regional Rural Banks,
(iv) Foreign Banks and
(v) Other Indian Scheduled Commercial Banks (in the private sector).
(vi) Co-operative Banks

Besides **the Nationalized banks** (majority equity holding is with the Government), the State Bank of India (SBI) (majority equity holding being with the Reserve Bank of India) and the associate banks of SBI (majority holding being with State Bank of India), the commercial banks comprise foreign and Indian private banks. While the State bank of India and its associates, nationalized banks and Regional Rural Banks are constituted under respective enactments of the Parliament, the private sector banks are banking companies as defined in the Banking Regulation Act. These banks, along with regional rural banks, constitute the public sector (state owned) banking system in India. The Public Sector Banks in India are back bone of the Indian financial system.

The **cooperative credit institutions** are broadly classified into urban credit cooperatives and rural credit cooperatives. Scheduled Co-operative Banks consist of Scheduled State Co-operative Banks and Scheduled Urban Co-operative Banks.

Regional Rural Banks (RRB's) are state sponsored, regionally based and rural oriented commercial banks. The Government of India promulgated the Regional Rural Banks Ordinance on 26th September 1975, which was later replaced by the Regional Rural Bank Act 1976. The preamble to the Act states the objective to develop rural economy by providing credit and facilities for the development of agriculture, trade, commerce, industry and other productive activities in the rural areas, particularly to small and marginal farmers, agricultural labourers, artisans and small entrepreneurs.

Different types of bank categorized by functions, ownership and domicile
Banks can be classified into various types on the basis of their functions, ownership, domicile, etc. The following are the various types of banks:

1. Commercial Banks:
The banks, which perform all kinds of banking business and generally finance trade and commerce, are called commercial banks. Since their deposits are for a short period, these banks normally advance short-term loans to the businessmen and traders and avoid medium-term and long-term lending.

However, recently, the commercial banks have also extended their areas of operation to medium-term and long-term finance. Majority of the commercial banks are in the public sector. However, there are certain private sector banks operating as joint stock companies. Hence, the commercial banks are also called joint stock banks.

2. Industrial Banks:
Industrial banks, also known as investment banks, mainly meet the medium-term and long-term financial needs of the industries. Such long-term needs cannot be met by the commercial banks, which generally deal with short-term lending.

The main functions of the industrial banks are:
(a) They accept long-term deposits.
(b) They grant long-term loans to the industrialists to enable them to purchase land, construct factory building, purchase heavy machinery, etc.
(c) They help selling or even underwrite the debentures and shares of industrial firms,
(d) They can also provide information regarding the general economic position of the economy. In India, industrial hanks, like Industrial Development Bank of India, Industrial Finance Corporation of India, Slate Finance Corporations, are playing significant role in the industrial development of the country.

3. Agricultural Banks:
Agricultural credit needs are different from those of industry and trade. Industrial and commercial banks normally do not deal with agricultural finance. The agriculturists require:

(a) short-term credit to buy seeds, fertilizers and other inputs, and
(b) long-term credit to purchase land, to make permanent improvements on land, to purchase agricultural machinery and equipment, etc. In India, agricultural finance is generally provided by co-operative institutions. Agricultural co-operatives provide short-term loans and Land Development Banks provide the long-term credit to the agriculturists.

4. Exchange Banks:
Exchange banks deal in foreign exchange and specialise in financing foreign trade. They facilitate international payments through the sale, purchase of bills of exchange, and thus play an important role in promoting foreign trade.

5. Saving Banks:
The main purpose of saving banks is to promote saving habits among the general public and mobilise their small savings. In India, postal saving banks do this job. They open accounts and issue postal cash certificates.

6. Central Bank:
Central bank is the apex institution, which controls, regulates and supervises the monetary and credit system of the country. Important functions of the central bank are:
(a) It has the monopoly of note issue;
(b) It acts as the banker, agent and financial adviser to the state;
(c) It is the custodian of member banks reserves;
(d) It is the custodian of nation's reserves of international currency;
(e) It serves as the lender of the last resort;
(f) It functions as the bank of central clearance, settlement and transfer; and
(g) It acts as the controller of credit. Besides these functions, India's central bank, i.e., the Reserve Bank of India, also performs many developmental functions to promote economic development in the country.

7. Classification on the Basis of Ownership:
On the basis of ownership, banks can be classified into three categories:
(a) Public Sector Banks:
These arc owned and controlled by the government. In India, the nationalized banks and the regional rural banks come under these categories,
(b) Private Sector Banks:
These banks are owned by the private individuals or corporations and not by the government or co-operative societies,
(c) Cooperative Banks:
Cooperative banks are operated on the cooperative lines. In India, cooperative credit institutions are organised under the cooperative societies law and play an important role in meeting financial needs in the rural areas.

8. Classification on the Basis of Domicile:
On the basis of domicile, the banks are divided into two categories:
(a) Domestic Banks:
These are registered and incorporated within the country,
(b) Foreign Banks:
These are foreign in origin and have their head offices in the country of origin.

9. Scheduled and Non-Scheduled Banks:
In India, banks have been broadly classified into scheduled and non-scheduled banks. A Scheduled Bank is that which has been included in the Second Schedule of the Reserve Bank of India Act, 1934 and fulfills the three conditions
(a) it has paid-up capital and reserves of at least Rs. 5 lakhs. It ensures the Reserve Bank that its operations are not detrimental to the interest of the depositors;
(b) It is a corporation or a cooperative society and not a partnership or a single owner firm. The banks which are not included in the Second Schedule of the Reserve Bank of India Act are non-scheduled banks.

PRINCIPLES OF MANAGEMENT IN BANK
RECRUITMENT:
Recruitment is a process to discover the sources of manpower to meet the requirement of the staffing schedule and to employ effective measures for attracting that manpower in adequate numbers to facilitate effective selection of efficient personnel.

Recruiting is an ongoing project for any organization. From the moment an employment application is submitted, recruitment software should be there to rank it, match the applicant to job if necessary and place the information in a database that can share the information across different software applications or applicant tracking tasks, including scheduling interviews and sending out letters for every stage of the recruitment process.

Definitions:
It is the process of finding and attracting capable applicants of employment. The process begins when new recruits are sought and ends when their applications are submitted. The result is pool of applicant from which new employees are selected.
- K. ASWATHAPPA.

Recruitment is the process of searching for prospective employees and stimulating them to apply for the jobs in the organization.
- EDWIN. B. FLIPPO

Significance:
The general purpose of recruitment is to provide a pool of potentially qualified job candidates. Specifically, the purpose is to:

1. Determine the present and future requirements of the organization in conjunction with its personal planning and job-analysis activities.
2. Increase the pool of job candidates at minimum cost.
3. Help to increase the success rate of the selection process by reducing the number of visibly under qualified or over qualified job applicants.
4. Help to reduce the probability that job applicants, once recruited and selected, will leave the organization only after a short period of time.
5. Meet the organization's legal and social obligations regarding the composition of its workforce.
6. Begin identifying and preparing potential job applicants who will be appropriate candidates.
7. Increase organizational and individual effectiveness in the short term and long term.
8. Evaluate the effectiveness of various recruiting techniques and sources for all types of job applicants.

Objectives of recruitment:

1. To attract people with multi dimensional skills and experiences that suits the present and future organizational strategies.
2. To induct the outsiders with a new perspective to lead the company
3. To infuse fresh blood at all levels of the organization.
4. To develop an organizational culture that attracts competent people to the company.
5. To devise methodologies for assessing psychological traits.
6. To seek out non-conventional grounds of talent.
7. To design entry pay that competes on quality but not on quantum.
8. To anticipate and find people for positions that does not exist.

Recruitment policy:
The recruitment policy of any organization is derived from the personnel policy of the same organization. It includes:

- Government policies
- Personnel policies of other competing organizations
- Organization's personnel policies
- Recruitment sources
- Recruitment needs
- Recruitment cost
- Selection criteria and preference etc

Sources of recruitment:
The sources of recruitment are broadly divided into internal and external sources.

Internal Sources:
- Present permanent employees
- Present temporary or casual employees
- Retrenched or retired employees
- Dependents of deceased, disabled, present and retired employees.

Why do organizations prefer internal sources?
- It can be used as a technique for motivation.
- Morale of the employees can be improved.
- Suitability of the internal candidates can be judged better than the external candidates as "known devils are better than unknown angels".
- Cost of selection can be minimized.
- Trade unions can be satisfied.
- Stability of the employees can be ensured.

External Sources:
a) **Campus recruitment**:
Different types of organizations like industries, business firms, service organizations ,social organizations can get inexperienced candidates of different types from various educational institutions like colleges and universities. Many companies realize that campus recruitment is one of the best techniques for recruiting new blood. These include
- Short listing the institutes based on the quality of the students intake, faculty facilities and past track record.
- Offering the smart pay rather than high pay package.
- Presenting a clear image of the company and the corporate culture.
- Getting in early. Make an early bird offer.
- Include young line managers and business school and engineering school alumni in the recruiting team.

b) **Private employee agencies**:
Consultants in India perform the recruitment functions on behalf of a client company by charging fee. Line managers are relieved from recruitment functions so that they can concentrate on operational activities. Hence these agencies work effectively in the recruitment of executives.

c) **Public employee exchanges**:
The government set up public employment exchanges in the country to provide information about vacancies to the candidates and to help the organization in finding out suitable candidates.

d) **Professional Organizations:**
These organizations maintain complete bio-data of their members and provide the same to various organizations on requisition. They also act as an exchange between their members and recruiting firms in exchanging information, clarifying doubts etc.

e) **Data banks**:
The management can collect the bio-data of the candidates from different sources like employee exchange, educational training institutes, candidates etc and feed them in the computer. it will become another source and the company can get the particulars as and when it needs to recruit.

f) **Casual applicants**:

Depending upon the image of the organization, its prompt response, participation of the organization in the local activities, level of unemployment. Candidates apply casually for jobs through mail or handover the applications in the personnel department.

g) **Similar organizations**:
Generally experienced candidates are available in organizations producing similar products or are engaged in similar business. The management can get most suitable candidates from this source.

h) **Trade unions**:
Generally unemployed or underemployed persons or employees seeking change in employment put a word to the trade union leaders with a view to getting suitable employment due to latter's intimacy with management. In view of this fact and in order to satisfy the trade union leaders, management enquires trade unions for suitable candidates.

Reasons for external sources:

- Candidates can be selected without any pre-conceived notion or reservations.
- HR mix can be balanced with different background, experience and skill etc.
- Latest knowledge skill, innovative or creative talent can also be flowed in to the organization.
- Long run benefit to the organization in the sense that qualitative human resources can be brought.

Recruitment Techniques:
These are the techniques by which the management contracts prospective employees or provides necessary information or exchanges ideas or stimulates them to apply for jobs. Management uses different types of techniques to stimulate internal and external candidates. Techniques useful to stimulate internal candidates are:

- Promotions
- Transfers

Techniques useful to stimulate external candidates:

- Present employees

Modern sources and techniques of recruitment:
A number of modern recruitment sources and techniques are being used by the corporate sector in addition to traditional sources and techniques. These techniques include.
a) Walk-in:
The busy organizations and the rapid changing companies do not find time to perform various functions of recruitment. Therefore, they advise the potential candidates to attend for an interview directly and without a prior application on a specified date, time and at a specified place.
b) Consult-in:
The busy and dynamic companies encourage the potential job seekers to approach them personally and consult them regarding the jobs; the companies select the suitable candidates from among such candidates through the selection process.
c) Head Hunting (search consultants):
In this the professional organizations search for the most suitable candidates and advise the company regarding the filling up of the positions.
d) Body Shopping:
The prospective employees contact these organizations to recruit the candidates. These professional and training institutions are called body shoppers and these activities are known as body shopping.
e) Business Alliances:
Business alliances like acquisition, mergers and takeovers help in getting human resources. In addition, the companies do also have alliances in sharing their human resources on ad-hoc basis.
f) Tele-recruitment:
Organizations advertise the job vacancies through the World Wide Web (internet). The job seekers send their applications through e-mail or internet.

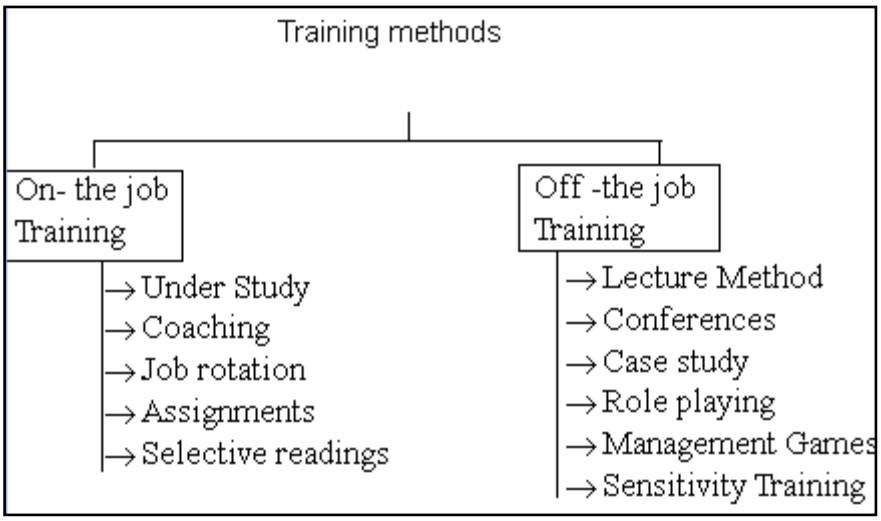
TRAINING:

Training is the acquisition of knowledge, skills, and competencies as a result of the teaching of vocational or practical skills and knowledge that relate to specific useful competencies. Training has specific goals of improving one's capability, capacity, productivity and performance.

Importance of Training:

1. Increased executive management skills.
2. Development in each executive of a broad background and appreciation of the company's overall operations and objectives.
3. Greater delegation of authority because executives down the like are better qualified and better able to assure increased responsibilities.
4. Creation of a reserve of qualified personnel to replace present incumanets and staff new positions.
5. Improved selection for promotion. .
6. Minimum delay in staffing new positions and minimum a distribution of operations during replacement in incumbents.
7. Provision for the best combination of youth, vigour and experience in top management and increased span of productive life in high level position.
8. Improved executive morale.
9. Attractive t6 the company of ambitious men who wish to move ahead as rapidly as their abilities permit.
10. Increased effectiveness and reduced costs, resulting in greater assurance of continued profitability.

Methods of Training:



A. On- the job training Methods: This type of training is also know as job instruction training. Under on - the job training method, the individual is placed on a regular job and taught the skills necessary to perfrorm that job. The trainee learns under the supervision and guidance of a qualified worker or instructor.

On-the - job training methods include the following:
(i) Under Study :This method makes the trainee an assistant to the current job holder. The trainee learns by experience, observation and imitation. It is a kind of mentoring that to help the employee to learn the skills of superior position.

(ii) Coaching : This method involves training by a superior about the knowledge and skills of a job to the junior or subordinate. The superior points out the mistakes committed by the trainee and make suggestions to improve upon.

(iii) Job rotation : This method involves movement of employees to different types of jobs to gain knowledge and functioning of various jobs within the organisation.Banks and insurance companies follow this approach. This method is also known as position rotation or cross training

(iv) Committee Assignment : In this method a committee consisting of a group of emplyees are given a problem and invited solutions. The employees solve the problem and submit the solution. The object of this method is to develop a team work among the employees.

(v) Selective readings: Selective reading may include professional journals and books. Some business organisations maintain libraries for their executives. This is a good method for assimilating knowledge.

B) Of -the job training Method: In off- the -job training, a trainee has to leave his place of working and devote his entire time for training purpose. During this period, the trainee does not contribute anything to the organization. These methods can be followed either in the organization itself or the trainee may be sent away for training courses organized by specialized institutions.

In our country, there are many organizations which have their own training institutes.

Prominent among them in the private sector are TISCO, Larsen & Tubro, ITC, Hindustan Unilever Ltd etc. And Steel Authority of India Ltd (SAIL), State Trading Corporation (STC), Life Insurence corporation, Coal India etc.in the public sector. Besides, there are special training institutes like

Administrative Staff College of India, National Productivity Council, All India Management Association, India Institute of Management etc.

Various methods of off-the job training are as follows:
(i) Lecture Method : Special courses and lectures are knowledge based training methods. These courses are organised for a short period. Lectures are supplemented by demonstrations. It also known as class room training.

(ii) Conferences: In order to overcome the limitations of lecture method many organisations have adopted guided-discussion type of conferences in their training programmes. In this method, the participants pool their ideas and experiences and draw conclusions.

(iii) Case Study: Case Study method of training has been developed by Harvard Business School of USA. Cases are widely used in a variety of programmes. This method increases the trainees power of observation. Case studies are generally used for teaching law, marketing, personnel management etc.

(iv) Role Playing: This mehod of training is used for improving human relations and development of leadership qualities. Role playing technique is used in group where various individuals are given roles of different managers. Dialogue spontaneously grows out of the situation. This method helps the trainee to develop insight into his behaviour and deal with others accordingly.

(v) Management Games: Management games are used to stimulate the thinking of people to run an organisation or its department. A game involves the participation of two or more teams depending on the situation. All the teams have to make decisions regarding the operation of their companies in the given situation. Strength and weakness of decisions are analysed in the light of the results.

(vi) Sensitivity Training: Sensitivity training was first used by National Training Laboratories at Bethel, USA. The training group called itself as T- group. Therefore, it is also called as T-Group training. It is a laboratory training method. The trainees can develop tolerance for others views, become less prejudiced, develop understanding for group process and listening skills.

After imparting training to the employees it becomes necessary to evaluate the training programme because organizations spend a sizeable amount on it. It is, therefore, necessary to examine what value is added to the performance by the training so that in future such training programmes may be arranged or abandoned if they fail to pay some benefit.

The effectiveness of the training Programme can by judged on the basis of the following criteria:
(a) Need: After training, the performance is evaluated .If there is positive demonstration from the workers the need is fulfilled. It is to ascertain whether the training has helped in achieving the results
(b) Change in behavior: The training should bring about change in the behavior of the employee as regards his performance of job. He should use the knowledge acquired by him during training for job performance.
(c) Value addition: Value addition is another criterion for assessment of training. It can be visualized through overall performance, change in trainees' personality, socialization, development etc.

PROMOTION:
A **promotion** is the advancement of an employee's rank or position in an organizational hierarchy system. Promotion may be an employee's reward for good performance, i.e., positive appraisal. Before a company promotes an employee to a particular position it ensures that the person is able to handle the added responsibilities by screening the employee with interviews and tests and giving them training or on-the-job experience. A promotion can involve advancement in terms of designation, salary and benefits, and in some organizations the type of job activities may change a great deal. The opposite of a promotion is a demotion.

Advantages of Promotion:

i. It is an important source of internal recruitment.
ii. It motivates employees.
iii. It increases job satisfaction.
iv. It increases morale.
v. It increases loyalty.
vi. It promotes self development of employees.
vii. Reduced training cost.
viii. Better industrial relations.
ix. No induction delay.

Disadvantages of Promotion:

i. Lack of new blood.
ii. Breeds Corruption
iii. Lack of capable or suitable employees.
iv. Not suitable for posts requiring innovative thinking.

Bases of Promotion

Promotion is given on the basis of seniority or merit or a combination of both. Let us discuss each one as a basis of promotion.

Seniority as a basis: It implies relative length of service in the same organization. The advantages of this are: relatively easy to measure, simple to understand and operate, reduces labour turnover and provides sense of satisfaction to senior employees. It has also certain disadvantages: beyond a certain age a person may not learn, performance and potential of an employee is not recognized, it kills ambition and zeal to improve performance.

Merit as a basis: Merit implies the knowledge, skills and performance record of an employee. The advantages are: motivates competent employees to work hard, helps to maintain efficiency by recognizing talent and performance. It also suffers from certain disadvantages like: difficulty in judging merit, merit indicates past achievement, may not denote future potential and old employees feel insecure.

Seniority-cum-Merit as basis: As both seniority and merit as basis suffer from certain limitations, therefore, a sound promotion policy should be based on a combination of both seniority and merit. A proper balance between the two can be maintained by different ways: minimum length of service may be prescribed, relative weightage may be assigned to seniority and merit and employees with a minimum performance record and qualifications are treated eligible for promotion, seniority is used to choose from the eligible candidates.

Merit Vs Seniority

MERIT	**SENIORITY**
Advantages:	
Motivates Employees	It is objective
Adds to job satisfaction.	Simple
Increases loyalty	Favoured by Union
	Increases Loyalty
	Reduces Turnover
Disadvantages	
It is subjective	Promotes Inefficiency
Complicated	Reduces motivation
Scope for Favoritism	Kills initiative and Innovative Thinking
Opposition by Union	Lowers morale of employees
Promotes Industrial Unrest	

CONTROL OF STAFF

The setting up of a good control system should be guided by certain important principles.

1. Principle of Reflection of Plans:
The more clear and complete the plans of the organisation and the more contr61s are designed to reflect these plans, the more effectively will controls serve its needs.

2. Principle of Prevention:
The truth of the saying 'Prevention is better than cure' is well-established. In control more attention should be directed to prevention of shortfalls than, remedying them after they occur. Peed forward control is very helpful in this respect.

3. Principle of Responsibility:
Responsibility for control particular measurement of deviations taking corrective action should be given to specific individuals at each stage of the operation.

4. Exception Principle:
The managers should concern themselves with exceptional cases i.e., those where the deviations from standards are very significant. Deviations of a minor mature may be left to subordinates for necessary action.

5. Principle of Critical Points:
All operations have got' certain vulnerable or critical points. It is these which cause most of the troubles - give rise to major deviations. The managers should pay more attention to the guarding of these points.

6. Principle of Pyramid:
Feedback data should first be communicated to the bottom of the pyramid i.e., those supervisors and even operating staff who is at the lowest levels. This will give the employees opportunity to control their own situations, apart from quickening remedial action.

The important provisions:

i. Punctuality
ii. Leave Rules
iii. Trade Union Activities

UNIT-II
INDIAN BANKING SYSTEM

SALIENT FEATURES OF INDIAN BANKING SYSTEM

1. Laws governing establishment of banks: Companies Act, 1956; Banking Regulation Act, 1949; Reserve Bank of India Act, 1934; Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970; Central or State Co-operative Acts.
2. Ownership: Public Sector Banks and Private Sector Banks
3. Capital Requirement: Scheduled Bank: Rs. 5.00 Lakhs; Nationalized Banks: Rs. 1500 Crore.
4. Capital Adequacy Norms: 8%
5. Mixed Banking
6. Increased credit to private sector
7. Control over the banks
8. Maintenance of CRR
9. Maintenance of SLR
10. Reserve Bank's Monopoly of Note Issue
11. Uniform Accounting Policy
12. Technology Changes
13. Internet Banking
14. Branch Banking
15. Diversification of Banking Operations
16. Cleaning NPAs
17. Chnaing trendof the payment system from cash to cashless.
18. UCID Code for bank's customers in India.
19. Implementation of business continuity plan.

Additional Reforms:

20. Prudential Measure
21. Competition Enhancing Measures.
22. Measures enhancing role of market forces.
23. Institutional and legal measures.
24. Supervisory Measures\
25. Technology Related Measures
26. Technological Developments in Scheduled Commercial Banks

Money Lenders:

According to the Indian Central Banking Enquiry Committee, "an indigenous banker is any individual or private firm receiving deposits and dealing in Hundies or lending money".

Their area of operation is limited, they know their customers intimately. They can watch whether the loan granted is used for the purpose or not. Therefore these types of bankers are existing even now. The Shroffs, the Marwaris, the Multanis, the Jains, the Sowcars, the Mahajans, Kharties, Seths and Banias are some of leading indigenous bankers.

The indigenous bankers can be classified into the following three categories:

(i) Those whose main business is banking
(ii) Those who combine their banking business with trading activities and
(iii) Those who act as commission agents. (For them the banking business is a side business).

In India the majority of the indigenous bankers belong to the second category. The number of villages in India is too large, while the size of each village is so small that any comprehensive scheme for opening branches of commercial banks to cover all the villages is not possible.

Therefore, the indigenous bankers have to continue to play a unique part mainly in rural finance. The indigenous bankers do not normally have contacts with other banking institutions in the country. Because, they are operating mostly with their own funds and not depend upon deposits.

But during the busy seasons, they rediscount the bills with the commercial banks and thus, the funds from the organised sector of the money market pass into the indigenous or the unorganized sector of the money market. Presently, they do not have such facility from the banking system.

Functions of Indigenous Bankers

Indigenous banking is mostly conducted as the family business. The banker inherits his banking business from his great grandfathers. His area of operation is limited and he knows his customers intimately. He knows all the details of his customers. Even after granting the loan, he can watch that it is actually utilized for the purpose for which it is obtained.

Therefore, these types of bankers are existing even now and there is no other system which can replace indigenous banking system. However, their importance has come down recently.

The indigenous bankers are functioning independently of each other. But in India, there are some organisations of these bankers to protect their common interest, viz., Multani, Shikarpuri Bankers' Association and Marwari Chamber of Commerce in Mumbai, Shroffs' Association in Ahmedabad, Calcutta and Mumbai, etc.

These organisations are the indigenous bankers. These organisations are in the form of guilds and help in settling disputes among themselves without recourse to courts.

The main functions of the indigenous bankers can be summarised as follows:

i. In India they are operating mainly in rural areas besides towns and cities.
ii. They maintain branches in important towns and cities with small establishment and are managed by their agents called 'gumastas'.
iii. They borrow funds by accepting deposits from the people (not permissible now by RBI).
iv. They provide credit facilities flexibly.
v. They lend to the rural people against securing of land, jewellery, etc. or sometimes on mere promissory notes.
vi. They provide loans to small traders and industrialists who cannot offer security acceptable to commercial banks.
vii. They provide remittance facilities to their customers.
viii. They draw and discount bills (known as Hundies) for their customers.
ix. They have close contact with their customers and their business. Hence they extend financial facilities according to their needs.
x. They are the advisors and consultants to their customers.

Indigenous Bankers and Commercial Banks

The indigenous bankers do not normally have contacts with other joint stock banking institutions in the country. Because, they are operating mostly on their own funds and not depend upon deposits from the others. Previously, during the busy seasons, they used to rediscount the bills with commercial banks and thus, the funds from the original sector of the money market pass into the indigenous or unorganized sector of the money market.

They also borrow from the commercial banks against demand promissory notes. The banks extend credit facilities to the approved indigenous bankers and the banks fix limits for the loan amount. Such facilities are not extended to them now because of RBI restrictions.

Indigenous Bankers and the RBI

Despite the predominant role played by the indigenous bankers in India's economic life' they have always remained outside the pale of organised banking. As early as 1931, the Banking Enquiry

Committee emphasised the necessity to unify the two sectors of the Indian money market and recommended the linking of the indigenous bankers to RBI control.

The committee especially recommended that appropriate steps should be taken to evolve a modern bill market on the western type in which the hundi, the traditional bill of exchange used by the indigenous bankers would figure actively.
Since 1935, when RBI was established many attempts were made by the Bank to bring the indigenous bankers under its orbit. RBI issued a draft scheme for direct linking of these bankers.

RBI suggested that the indigenous bankers should give up their trading and commission business, switch over to western system of accounting, develop the deposit side of banking activities, submit to RBI periodical statements of their affairs, etc. RBI desired that the ambiguous characters of the hundi should cease and that it should become a negotiable instrument always representing a genuine trade transaction.

Besides, the Bank desired the most important of the indigenous banks to play the role of discount houses as in London. An against these obligations, RBI promised to provide them with all the privileges enjoyed by the scheduled banks.

In other words, indigenous bankers would be entitled to borrow from or rediscount bills of exchange at RBI on the same terms and conditions as those available to the scheduled banks.

The indigenous bankers with their age-old traditions of independence, declined to accept the restrictions as well as the compensating benefits of securing accommodation from RBI on favourable terms. They disagreed with the suggestions regarding accepting deposits and giving wide publicity to their accounts and their state of affairs.

They were unwilling to give up their trading and commission business and confine themselves to banking business only. Besides, they did not consider that the privileges offered by RBI were adequate enough to compensate for the loss of their non-banking business. As a result, the scheme proposed by RBI to bring the indigenous bankers under its direct influence failed.

In 1954, the Shroff Committee recommended that RBI should take steps to encourage the rediscounting of hundies of the indigenous bankers by RBI through the scheduled banks. Similar proposals for the linking of the indigenous bankers with RBI and organised money market have been put forward among others by the Bombay Shroffs Association. But RBI has decided not to do anything further in this matter.

The Banking Enquiry Commission, 1972 believed that the best way to control indigenous bankers is through commercial banks. The RBI should exercise indirect influence over the business of indigenous bankers through the medium of commercial banks by laying down certain guidelines for their dealings with indigenous bankers.

The commercial banks, in their turn, should also call for regular returns from the indigenous bankers and require them to maintain adequate internal inspection procedures and be subject to external audit.

In the course of development of Banking Industry and Co-operative banking, the role of indigenous bankers has now, been relegated to the level of 'pawn brokers'.

Soon after nationalization of major commercial banks in July 1969 and ever since the establishment of Regional Rural Banks from 1975, Government and RBI have followed a policy of rural banking by telling these banks to open up as many rural branches as possible.

Thanks to this policy, today around 33,500 bank branches are operating from rural areas. The access of banking facility to rural masses made the indigenous bankers a non-entity in rural banking. They are now moneylenders for drunkards and lazy. The decent among have converted into Finance Companies and the more decent, into Registered Finance Companies.
Thus, the indigenous bankers have no role to play in today's rural India except in certain parts of the country where the level of education is very poor.

Defects of Indigenous Bankers:
The indigenous bankers suffer from the following defects:

***(i)* Combining banking and non-banking business:**
In India, the indigenous Bankers combine their banking business with their commission and other non-banking business. Hence, they cannot concentrate more on the banking business.

***(ii)* Un integrated system:**
In India, they are unorganized and un integrated. They do not have proper link with commercial banks and RBI. They operate independently.

***(iii)* Lack of sufficient capital:**
In India, most of them operate mainly on their own funds. Hence, they run their business with inadequate capital and are not able to cater to the financial needs of the borrowers.

***(iv)* Conservative approach:**
The majority of the indigenous bankers is conservative, lack adaptability and continues ancient methods of business. They follow the methods that they learnt from their forefathers without any improvement in time to time.

***(v)* Do not follow the sound policy of lending:**
While lending the indigenous banker does not follow the sound principles of lending, viz., safety, liquidity, feasibility, etc. Sometimes they grant loans against insufficient securities or even personnel securities.

***(vi)* Less importance to discounting of handiest:**
While financing to trade, they directly make cash advances and the volume of bills discounted is small.

***(vii)* Secrecy of accounts:**
The indigenous bankers maintain undue secrecy of their business. They do not publish their trading results and activities. Their operations were shrouded with utmost secrecy.

***(viii)* Not controlled by RBI:**
The indigenous bankers are not controlled by the RBI and thus forming part of the unorganised sector of the money market.

***(ix)* Higher rate of interest:**
The rate of interest charged by indigenous bankers is high when compared with the commercial banks.

Suggestions for Improvement
The following are the suggestions given by various committees for reforming indigenous bankers and to link them with the organised structure of banking.

i. The indigenous bankers should give up their side trade and confine themselves to banking properly.
ii. They should mordernise their methods of working and run their business like commercial banks.

iii. They should maintain their accounts properly and get them audited.
iv. They should concentrate more on deposit business and encourage deposits made by rural people.
v. Wherever possible, they should be amalgamated into economic units which can maintain adequate capital.
vi. They should be directly linked with Reserve Bank of India.
vii. There should not be any unhealthy competition between the indigenous banks and commercial banks.
viii. The facilities provided by the commercial bankers should be made available to the indigenous bankers also the Commercial banks should freely advance funds to indigenous bankers on Hundies discounted by them.
ix. With their close contact to intimate knowledge of the traders, they can function on par with that of London bill brokers.
x. The Bankers Books Evidence Act may be extended to indigenous bankers also.

It may, however, be stated as a matter of caution that indigenous bankers do not have any role to play in the modern banking which require great deal of sophistication, computerization, large capital, greater control and regulation from RBI. Hence, the historical facts are stated only for academic interest.

Types of Moneylenders
Moneylenders play an important role in rural financing. The moneylenders in the villages are of two types. They are,
(i) Professional moneylenders, and
(ii) Non-Professional moneylenders.

The professional moneylenders are the persons whose main occupation is money lending. They are known as Banias, Mahajans, Sowkers, etc. But, the non-professional moneylenders do the business of money lending as a side occupation. The rate of interest charged by moneylenders is very high and they indulge in many objectionable trade practices.

Indigenous Bankers vs. Moneylenders
The following are the important differences between Indigenous Bankers and moneylenders:

1. Business of banking
The Indigenous bankers practice their Moneylenders business cannot be banking business in its true meaning. Considered as banking business.

2. Acceptance of Deposits
The Indigenous banker used to accept Moneylenders do not accept deposits on current accounts as well as deposits but they simply fixed deposits (not permissible now). lend money (own funds)

3. Dealing in Hundies
They do not deal in hundies.

4. Purpose of lending
They generally provide finance to agriculture and tn.de and do not finance for consumption.

5. Security sought
They supply finance only for productive purposes on a proper security such as agricultural goods, lands, etc.
They are prepared to lend money even without a proper security. They do not distinguish between productive and unproductive expenditure.

6. Area of operation
They are largely based on rural areas.

7. Rate of Interest
The rates of interest charged by indigenous bankers are moderate and consistent with the market conditions.
The rates of interest charged by the moneylenders are very high.

8. Nature of Practice
They practice their business with accurate accounts and straight dealing with their customers.

They are known for their objectionable practices such as failure to issue receipts for part payments, maintaining false accounts, etc.

9. Relationship with customers
The relationship between indigenous bankers and their customers is always cordial.

They include Shroffs, Seths, Chettis, Kothiwalas, Marwaris, etc.
The moneylenders quarrel, harass and threaten their customers and in most of the cases they do not maintain friendly relations with their customers.

10. Examples
They include Banias, Mahajans, Sowkars, etc.

According to Dr. M. Muranjan, "The moneylenders and indigenous bankers still continue to be the backbone of Indian rural finance. Their part in rural finance is predominant in spite of the good progress made by the co-operative societies and commercial banks in rural areas. The system is well suited to **rural areas.**

NATIONALIZATION OF COMMERCIAL BANKS AND ITS EFFECTS
After independence the Government of India (GOI) adopted planned economic development for the country (India). Accordingly, five year plans came into existence since 1951. This economic planning basically aimed at social ownership of the means of production. However, commercial banks were in the private sector those days. In 1950-51 there were 430 commercial banks. The Government of India had some social objectives of planning. These commercial banks failed helping the government in attaining these objectives. Thus, the government decided to nationalize 14 major commercial banks on **19th July, 1969**. All commercial banks with a deposit base over Rs.50 crores were nationalized. It was considered that banks were controlled by business houses and thus failed in catering to the credit needs of poor sections such as cottage industry, village industry, farmers, craft men, etc. The second dose of nationalization came in **April 1980** when banks were nationalized.

Objectives behind Nationalization of Banks in India
1. **Social Welfare**: It was the need of the hour to direct the funds for the needy and required sectors of the Indian economy. Sector such as agriculture, small and village industries were in need of funds for their expansion and further economic development.
2. **Controlling Private Monopolies** : Prior to nationalization many banks were controlled by private business houses and corporate families. It was necessary to check these monopolies in order to ensure a smooth supply of credit to socially desirable sections.
3. **Expansion of Banking** : In a large country like India the numbers of banks existing those days were certainly inadequate. It was necessary to spread banking across the country. It could be done through expanding banking network (by opening new bank branches) in the un-banked areas.

4. **Reducing Regional Imbalance** : In a country like India where we have a urban-rural divide; it was necessary for banks to go in the rural areas where the banking facilities were not available. In order to reduce this regional imbalance nationalization was justified:
5. **Priority Sector Lending** : In India, the agriculture sector and its allied activities were the largest contributor to the national income. Thus these were labeled as the priority sectors. But unfortunately they were deprived of their due share in the credit. Nationalization was urgently needed for catering funds to them.
6. **Developing Banking Habits** : In India more than 70% population used to stay in rural areas. It was necessary to develop the banking habit among such a large population.

Demerits, Limitations - Bank Nationalization in India

Though the nationalization of commercial banks was undertaken with tall objectives, in many senses it failed in attaining them. In fact it converted many of the banking institutions in the loss making entities. The reasons were obvious lethargic working, lack of accountability, lack of profit motive, political interference, etc. Under this backdrop it is necessary to have a critical look to the whole process of nationalization in the period after bank nationalization.

The major limitations of the bank nationalization in India are:-

1. **Inadequate banking facilities** : Even though banks have spread across the country; still many parts of the country are unbanked. Especially in the backward states such as the Uttar Pradesh, Madhya Pradesh, Chhattisgarh and north-eastern states of India.
2. **Limited resources mobilized and allocated** : The resources mobilized after the nationalisation is not sufficient if we consider the needs of the Indian economy. Some times the deposits mobilized are enough but the resource allocation is not as per the expansions.

3. **Lowered efficiency and profits** : After nationalization banks went in the government sector. Many times political forces pressurized them. Banking was not done on professional and ethical grounds. It resulted into lower efficiency and poor profitability of banks.

4. **Increased expenditure** : Due to huge expansion in a branch network, large staff administrative expenditure, trade union struggle, etc. banks expenditure increased to a dangerous levels.

5. **Political and Administrative Inference**: Many public sector banks badly suffered due to the political interference. It was seen in arranging loan meals. It ultimately resulted in huge non-performing assets (NPA) of these banks and inefficiency.

These are several limitations faced by the banks nationalization in India.
Apart from this there are certain other limitations as well, such as weak infrastructure, poor competitiveness, etc.

But after *Economic Reform of 1991*, the Indian banking industry has entered into the new horizons of competitiveness, efficiency and productivity. It has made Indian banks more vibrant and professional organizations, removing the bad days of bank nationalization.

CLASSIFICATION OF BANKING INSTITUTIONS

Scheduled & Non-Scheduled Banks

In India the central banking authority is the Reserve Bank of India. It is also referred to as the Apex Bank. It functions under an act called The Reserve Bank of India Act, 1934. All the banks and other financial institutions operating in India come under the monitoring and control of RBI. RBI controls the banking sector in India through an Act called The Banking Regulations Act 1949. In the past, when there were very few banks, RBI used to include all the scheduled banks in its schedule. Nowadays, when the number of banks has gone up substantially, RBI has to change the schedule every now and then, hence irrespective of whether a bank finds its name in the schedule to the RBI Act or not, its

schedule status can be found out from its banking license. A Bank that is not a scheduled bank is referred to as non scheduled bank even in it is having banking license.

The difference lies in the type of banking activities that a bank can carry out in India. In the case of a scheduled bank, it is licensed by the RBI to carry on extensive banking operations including foreign exchange operations, whereas, a non-scheduled bank can carry out only limited operations. There are a number of factors considered by RBI to declare a bank as a scheduled bank, like the amount of share capital, type of banking activities that the bank is permitted to carry out etc. An example of difference between a scheduled and non-scheduled bank is dealing in Foreign Exchange.

Commercial & Co-operative Banks
Commercial banks are by far the most widespread banking institutions in India. They provide major products and services in India. A commercial bank is run on commercial lines, for profits of the organization.

A co-operative bank on the other hand is run for the benefit of a group of members of the co-operative body. A co-operative bank distributes only a very small portion of its profit as dividend, retaining a major portion of it in business.
All the nationalized banks in India and almost all the private sector banks are commercial scheduled banks. There are a large number of private sector co-operative banks and most of them are non-scheduled banks. In the public sector also, within a state, starting from the State capital, there are State Co-operative Banks and District Central Co-operative Banks at the District level. Under the District Central Co-operative Bank, there are Co-operative Societies.

At present, In India, the banks can be bifurcated into following categories.

Public Sector Banks or Nationalized Banks, *which are commercial and scheduled* Examples: State Bank of India, Bank of India etc.

Public Sector Banks, *which are co-operative and non-scheduled*-These are state owned banks like the Maharashtra State Co-operative Bank, Junnar Co-operative Society etc.

Private Sector Banks, *which are commercial and scheduled*-These could be foreign banks, as well as Indian Banks. Examples: Foreign Banks- CITI Bank, Standard Chartered Bank etc.
Indian Banks Bank of Rajasthan Limited, VYSYA Bank Limited etc.
Private Sector Banks, *which are co-operative and scheduled* These are large co-operative sector banks but which are scheduled banks. Examples: Saraswat Co-operative Bank Limited, Cosmos Co-operative Bank Limited etc.

Private Sector Banks, *which are co-operative and non-scheduled*-These are small co-operative banks but which are non-scheduled. Examples: Local co-operative banks which operate within a town or a city. Example: Mahesh Sahakari Bank Limited.

Regional Rural Banks. These are state owned. These banks have been established with a view to developing the rural economy by providing, for the purpose of development of agriculture, trade, commerce, industry and other productive activities in the rural areas, credit and other facilities, particularly to the small and marginal farmers, agricultural labourers and artisans and small entrepreneurs

Gramin Banks, that are also state owned. They operate at still smaller level than RRBs and serve at villages level.

Foreign banks, These banks have Head Office outside India and branch in India, Besides, the Reserve Bank of India (hereinafter referred to as RBI) acts as the central bank of the country. RBI is

responsible for development and supervision of the constituents of the Indian financial system (which comprises banks and non-banking financial institutions) as well as for determining, in conjunction with the central Government, the monetary and credit policies. They are also controlled by RBI.

Retail Banking Vs Wholesale Banking

Whole sale banking typically involves a small number of very large customers such as big corporations and governments, whereas retail banking consists of a large number of small customers who consume personal banking and small business services. Wholesale banking is largely inter-bank; banks use the inter-bank markets to borrow from or lend to other banks/ large customers, to participate in large bond issues and to engage in syndicated lending. Retail banking is largely intra-bank; the bank itself makes many small loans.

Most of the Indian public sector banks practice retail banking; they are slowly practising the concept of wholesale banking. On the other hand, most of the wellestablished foreign banks in India and the recent private sector banks practice wholesale banking alongside retail banking.

As a result of this difference, the composition of income for a public sector bank is different. While a major portion of the income for large public sector banks is from lending operations, in the case of any private sector bank in India, the amount of non-operating income (other than interest income) is substantially higher. The composition of other income is commission on bills/ guarantees/ letters of credit, counselling fees, syndication fees, credit report fees, loan processing fees, correspondent bank charges etc.

Global Banking

Global Banking activities are an extension of various activities listed above into the international market. Global banking primarily consists of trade in international banking services and establishment of branches and subsidiaries in foreign countries.

Special Kinds Of Bank Branches

Most Banks in India have special kind of branches. This is done to reap benefits of specialisation as activities done by these braches are quite complex and require specialised knowledge and attention. Types of some special branches are

i. Foreign exchange branches
ii. NPA recovery branches
iii. Service branches dealing in Clearing house operations/Corporate banking and Industrial finance branches
iv. Personal banking branches
v. Housing finance branch
vi. SSI branches
vii. Agricultural finance branches

RESERVE BANK OF INDIA

The **Reserve Bank of India** (**RBI**) is India's central banking institution, which controls the monetary policy of the Indian rupee. It was established on 1 April 1935 during the British Raj in accordance with the provisions of the Reserve Bank of India Act, 1934. The share capital was divided into shares of 100 each fully paid, which was entirely owned by private shareholders in the beginning. Following India's independence in 1947, the RBI was nationalized in the year 1949.

The RBI plays an important part in the development strategy of the Government of India. It is a member bank of the Asian Clearing Union. The general superintendence and direction of the RBI is

entrusted with the 21-member- Central Board of Directors—the Governor (currently Raghuram Rajan), four Deputy Governors, two Finance Ministry representative, ten government-nominated directors to represent important elements from India's economy, and four directors to represent local boards headquartered at Mumbai, Kolkata, Chennai and New Delhi. Each of these local boards consists of five members who represent regional interests, as well as the interests of co-operative and indigenous banks.

The bank is also active in promoting financial inclusion policy and is a leading member of the Alliance for Financial Inclusion (AFI).

Powers/ Functions of RBI:
The Reserve Bank of India performs various traditional central banking functions as well as undertakes different promotional and developmental measures to meet the dynamic requirements of the country.
The broad objectives of the Reserve Bank are:
a) Regulating the issue of currency in India;
b) keeping the foreign exchange reserves of the country;
c) establishing the monetary stability in the country; and
d) Developing the financial structure of the country on sound lines consistent with the national socio-economic objectives and policies.

Main functions of the Reserve Bank are described below:

1. Note Issue:
The Reserve Bank has the monopoly of note issue in the country. It has the sole right to issue currency notes of all denominations except one-rupee notes. One-rupee notes are issued by the Ministry of Finance of the Government of India. The Reserve Bank acts as the only source of legal tender because even the one-rupee notes are circulated through it. The Reserve Bank has a separate Issue Department, which is entrusted with the job of issuing currency notes. The Reserve Bank has adopted minimum reserve system of note issue. Since 1957, it maintains gold and foreign exchange reserves of Rs. 200 crore, of which at least Rs. 115 crore should be in gold.

2. Banker to Government:
The Reserve Bank acts as the banker, agent and adviser to Government of India:
i. It maintains and operates government deposits,
ii. It collects and makes payments on behalf of the government,
iii. It helps the government to float new loans and manages the public debt,
iv. It sells for the Central Government treasury bills of 91 days duration,
v. It makes 'Ways and Means' advances to the Central and State Governments for periods not exceeding three months,
vi. It provides development finance to the government for carrying out five year plans,
vii. It undertakes foreign exchange transactions on behalf of the Central Government,
viii. It acts as the agent of the Government of India in the latter's dealings with the International Monetary Fund (IMF), the World Bank, and other international financial institutions, (i) It advises the government on all financial matters such as loan operations, investments, agricultural and industrial finance, banking, planning, economic development, etc.

3. Banker's Bank:
The Reserve Bank acts as the banker's bank in the following respects:
(a) Every Bank is under the statutory obligation to keep a certain minimum of cash reserves with the Reserve Bank. The purpose of these reserves is to enable the Reserve Bank to extend financial assistance to the scheduled banks in times of emergency and thus to act as the lender of the last resort. According to the Banking Regulation Act, 1949, all scheduled banks are required to maintain with the Reserve Bank minimum cash reserves of 5% of their demand liabilities and 2%

of their time liabilities. The Reserve Bank (Amendment) Act, 1956 empowered the Reserve Bank to raise the cash reserve ratio to 20% in the case of demand deposits and to 8% in case of time deposits. Due to the difficulty of classifying deposits into demand and time categories, the amendment to the Banking Regulation Act in September 1972 changed the provision of reserves to 3% of aggregate deposit liabilities, which can be raised to 15% if the Reserve Bank considers it necessary,

(b) The Reserve Bank provide financial assistance to the scheduled banks by discounting their eligible bilk and through loans and advances against approved securities,

(c) Under the Banking Regulation Act,1949 and its various amendments, the Reserve Bank has been given extensive powers of supervision and control over the banking system. These regulatory powers relate to the licensing of banks and their branch expansion; liquidity of assets of the banks; management and methods of working of the banks; amalgamation, reconstruction and liquidation of banks; inspection of banks; etc.

4. Custodian of Exchange Reserves:

The Reserve Bank is the custodian of India's foreign exchange reserves. It maintains and stabilises the external value of the rupee, administers exchange controls and other restrictions imposed by the government, and manages the foreign exchange reserves. Initially, the stability of exchange rate was maintained through selling and purchasing sterling at fixed rates. But after India became a member of the international Monetary Fund (IMF) in 1947, the rupee was delinked with sterling and became a multilaterally convertible currency. Therefore the Reserve Bank now sells and buys foreign currencies, and not sterling alone, in order to achieve the objective of exchange stability. The Reserve Bank fixes the selling and buying rates of foreign currencies. All Indian remittances to foreign countries and foreign remittances to India are made through the Reserve Bank.

5. Controller of Credit:

As the central bank of the country, the Reserve Bank undertakes the responsibility of controlling credit in order to ensure internal price stability and promote economic growth. Through this function, the Reserve Bank attempts to achieve price stability in the country and avoids inflationary and deflationary tendencies in the country. Price stability is essential for economic development. The Reserve Bank regulates the money supply in accordance with the changing requirements of the economy. The Reserve Bank makes extensive use of various quantitative and qualitative techniques to effectively control and regulate credit in the country.

6. Ordinary Banking Functions:

The Reserve Bank also performs various ordinary banking functions:

a) It accepts deposits from the central government, state governments and even private individuals without interest,
b) It buys, sells and rediscounts the bills of exchange and promissory notes of the scheduled banks without restrictions,
c) It grants loans and advances to the central government, state governments, local authorities, scheduled banks and state cooperative banks, repayable within 90 days,
d) It buys and sells securities of the Government of India and foreign securities,
e) It buys from and sells to the scheduled banks foreign exchange for a minimum amount of Rs. 1 lakh,
f) It can borrow from any scheduled bank in India or from any foreign bank,
g) It can open an account in the World Bank or in some foreign central bank.
i. It accepts valuables, securities, etc., for keeping them in safe custody.
ii. It buys and sells gold and silver.

7. Miscellaneous Functions:
In addition to central banking and ordinary banking functions, the Reserve Bank performs the following miscellaneous functions:
(a) Banker's Training College has been set up to extend training facilities to supervisory staff of commercial banks. Arrangements have been made to impart training lo the cooperative personnel,
(b) The Reserve Bank collects and publishes statistical information relating to banking, finance, credit, currency, agricultural and industrial production, etc. It also publishes the results of various studies and review of economic situation of the country in its monthly bulletins and periodicals.

8. Forbidden Business:
Being the central bank of the country, the Reserve Bank:
(a) Should not compete with member banks and
(b) should keep its assets in liquid form to meet any situation of economic crisis.

Therefore, the Reserve Bank has been forbidden to do certain types of business:
(a) It can neither participate in, nor directly provide financial assistance to any business, trade or industry,
(b) It can neither buy its own shares not those of other banks or commercial and industrial undertakings,
(c) It cannot grant unsecured loans and advances,
(d) It cannot give loans against mortgage security,
(e) It cannot give interest on deposits.
(f) It cannot draw or accept bills not payable on demand,
(g) It cannot purchase immovable property except for its own offices.

9. Promotional and Developmental Functions:
Besides the traditional central banking functions, the Reserve Bank also performs a variety of promotional and developmental functions:
(a) By encouraging the commercial banks to expand their branches in the semi-urban and rural areas, the Reserve Bank helps (i) to reduce the dependence of the people in these areas on the defective unorganised sector of indigenous bankers and money lenders, and (ii) to develop the banking habits of the people
(b) By establishing the Deposit Insurance Corporation, the Reserve Bank helps to develop the banking system of the country, instills confidence of the depositors and avoids bank failures,
(c) Through the institutions like Unit Trust of India, the (Reserve Bank helps to mobilise savings in the country,
(d) Since its inception, the Reserve Bank has been mating efforts to promote institutional agricultural credit by developing cooperative credit institutions.
(e) The Reserve Bank also helps to promote the process of industrialisation in the country by setting up specialised institutions for industrial finance,
(f) it also undertakes measures for developing bill market in the country.

CONTROL OF CREDIT BY RBI
What is Credit Control: Credit Control is an important tool used by the Reserve Bank of India, a major weapon of the monetary policy used to control the demand and supply of money (liquidity) in the economy.

Why Credit Control is required: The basic and important needs of Credit Control in the economy are:

- To encourage the overall growth of the "priority sector" i.e. those sectors of the economy which is recognized by the government as "prioritized

- To keep a check over the channelization of credit so that credit is not delivered for undesirable purposes.
- To achieve the objective of controlling "Inflation" as well as "Deflation".
- To boost the economy by facilitating the flow of adequate volume of bank credit to different sectors.

What are the methods of Credit Control?
There are two methods that the RBI uses to control the money supply in the economy-

(1) Qualitative Method: By qualitative methods means the control or management of the uses of bank credit or manner of channelizing of cash and credit in the economy. Tools used under this method are:

(a) **Marginal Requirement:** Marginal Requirement of loan can be increased or decreased to control the flow of credit for e.g. – a person mortgages his property worth Rs. 1,00,000 against loan. The bank will give loan of Rs. 80,000 only. The marginal requirement here is 20%. In case the flow of credit has to be increased, the marginal requirement will be lowered.

(b) **Rationing of credit:** Under this method there is a maximum limit to loans and advances that can be made, which the commercial banks cannot exceed.

(c) **Publicity:** RBI uses media for the publicity of its views on the current market condition and its directions that will be required to be implemented by the commercial banks to control the unrest.

(d) **Direct Action:** Under the banking regulation Act, the central bank has the authority to take strict action against any of the commercial banks that refuses to obey the directions given by Reserve Bank of India.

(e) **Moral Suasion:** This method is also known as "Moral Persuasion" as the method that the Reserve Bank of India, being the apex bank uses here, is that of persuading the commercial banks to follow its directions/orders on the flow of credit.

(2) Quantitative Method: By Quantitative Credit Control we mean the control of the total quantity of credit. Different tools used under this method are:

(a) **Bank Rate:** Bank Rate also known as the Discount Rate is the official minimum rate at which the Central Bank of the country is ready to rediscount approved bills of exchange or lend on approved securities. When the commercial bank for instance, has lent or invested all its available funds and has little or no cash over and above the prescribed minimum, it may ask the central bank for funds. It may either re-discount some of its bills with the central bank or it may borrow from the central bank against the collateral of its own promissory notes. In either case, the central bank accommodates the commercial bank and increases the latter's cash reserves. This Rate is increased during the times of inflation when the money supply in the economy has to be controlled.

(b) **Open Market Operations:** Open Market Operations indicate the buying/selling of government securities in the open market to balance the money supply in the economy. During inflation, RBI sells the government securities to the commercial banks and other financial institution. This reduces their cash lending and credit creation capacities. Thus, Inflation can be controlled. During recessions, RBI purchases government securities from commercial banks and other financial institution. This leaves them with more cash balances for lending and increases their credit creation capacities. Thus, recession can be overcome.

(c) **Repo Rates and Reverse Repo Rates:** Repo is a swap deal involving immediate sale of securities and a simultaneous re purchase of those securities at a future date at a predetermined price.

Commercial banks and financial institution also park their funds with RBI at a certain rate, this rate is called the Reverse Repo Rate. Repo rates and Reverse repo rate used by RBI to make liquidity adjustments in the market.

(d) **Cash Reserve Ratio:** The money supply in the economy is influenced by the cash reserve ratio. It is the ratio of a bank's time and demand liabilities to be kept in reserve with the RBI. A high CRR reduces the flow of money in the economy and is used to control inflation. A low CRR increases the flow of money and is used to overcome recession.

(e) **Statutory Liquidity Ratio:** Under SLR, banks have to invest a certain percentage of its time and demand liabilities in Government approved securities. The reduction in SLR enhances the liquidity of commercial banks.

(f) **Deployment of Credit:** The RBI has taken various measures to deploy credit in different of the economy. The certain percentage of bank credit has been fixed for various sectors like agriculture, export, etc.

UNIT-III
MANAGEMENT OF DEPOSITS

DEPOSITS MOBILIZATION

In India commercial banks promote the habit of thrift and savings among public and mobilize deposits. The deposits of scheduled commercial banks were Rs. 1080 crore in 1947, Rs. 4646 crore in 1969 but it increased to Rs. 605410 crore in 1998 and it has risen further to Rs. 701871 crore as on March 1999.

Aggregate deposit of all scheduled commercial banks crossed one million crore rupees mark in 2001. The total deposit amounted to Rs. 11, 31,188 crore as at end March, 2002. The increase in deposits is attributed to the Five Year Plans, policy of the Government, rapid branch expansion and industrialization of our country, etc.

CLASSIFICATION AND NATURE OF DEPOSITS ACCOUNT

Kinds of Deposits

Demand Deposits

These are deposits which the customer can get back on demand or which are placed for very short time periods. For example:

Savings account deposits

This is the normal bank account that individuals and Hindu Undivided Families (HUFs) maintain. The account can be opened by individuals who are majors (above 18 years of age), parents / guardians on behalf of minors and Karta of HUFs. Clubs, associations and trusts too can open savings accounts as provided for in their charter. Banks insist on a minimum balance, which may be higher if the account holder wants cheque book facility. The minimum balance requirement tends to be lowest in the case of co-operative banks, followed by public sector banks, private sector Indian banks and foreign banks, in that order.

Banks do impose limits on the number of withdrawals every month / quarter. Further, overdraft facility is not offered on savings account. Traditionally, banks paid an interest on the lowest balance in the bank account between the 10th and the end of the month. Suppose the balance in the depositer's account in a particular month was as follows:

Current account deposits

This is maintained by businesses for their banking needs. It can be opened by anyone, including sole-proprietorships, partnership firms, private limited companies and public limited companies.
The current account comes with a cheque book facility. Normally, there are no restrictions on the number of withdrawals. Subject to credit-worthiness, the bank may provide an overdraft facility i.e. the account holder can withdraw more than the amount available in the current account. Current accounts do not earn an interest. Therefore, it is prudent to leave enough funds in current account to meet the day-to-day business needs, and transfer the rest to a term deposit.
CASA is a term that is often used to denote Current Account and Savings Account. Thus, a bank or a branch may have a CASA promotion week. This means that during the week, the bank would take extra efforts to open new Current Accounts and Savings Accounts.

Term Deposits

These are deposits that are maintained for a fixed term. The time period can be anything from 7 days to 10 years. This is not like a normal operating bank account. Therefore, cheque book facility is not offered. Benefit of term deposits is that the interest rate would be higher. Weakness is that if the investor needs the money earlier, he bears a penalty. He will earn 1% less than what the deposit would otherwise have earned, if it had been placed for the time period for which the money was left with the bank.

Banks may also offer the facility of loan against fixed deposit. Under this arrangement, a certain percentage of the fixed deposit amount may be made available as a loan, at an interest rate, which would be higher than the term deposit rate. This is an alternative to premature withdrawal.

Unlike interest rate on savings account, the interest in term deposits is de-regulated. Therefore, every bank decides its own interest rate structure. Further, it is normal to offer 0.50% extra interest to senior citizens. For large deposits of above Rs. 1 crore, the bank may be prepared to work out special terms.

The term deposits may also be structured as *recurring* i.e. the depositer would invest a constant amount every month / quarter, for anything from 12 months to 10 years. Benefit of such an account is that the interest rate on the future deposits is frozen at the time the recurring account is opened. Thus, even if interest rates on fixed deposits, in general, were to go down, the recurring deposits would continue to earn the committed rate of interest.

Interest rate in a recurring deposit may be marginally lower than the rate in a non-recurring term deposit for the same time period.

Hybrid Deposits / Flexi Deposits
These are value added facilities offered by some banks. For instance, a *sweep facility* may be offered in their CASA accounts. Under the facility, at the end of every day, surplus funds beyond the minimum balance required, is automatically swept into an interest earning term deposit account. When more money is required for the regular operations, it is automatically swept from the interest earning term deposit account. Benefit for depositers are:

• Superior interest earnings, as compared to normal CASA
• Less paperwork – no need to sign papers etc. for each sweep in or sweep out.
• Sweep out of money from the interest earning term deposit account does not attract premature withdrawal charges.

However, unlike in a normal term deposit, interest rate is liable to be changed by the bank at any time.

Non-Resident Accounts
These can be opened by Non-Resident Indians and Overseas Corporate Bodies with any bank in India that has an Authorised Dealer license.

• *Foreign Currency Non-Resident Account (FCNR)*
These are maintained in the form of fixed deposits for 1 year to 3 years. Since the account is designated in foreign currency (Pounds, Sterling, US Dollars, Japanese Yen and Euro), the account holder does not incur exchange losses in first converting foreign currency into rupees (while depositing the money) – and then re-converting the rupees into foreign currency (when he wants to take the money back).

The depositer will have to bring in money into the account through a remittance from abroad or through a transfer from another FCNR / NRE account. If the money is not in the designated foreign currency, then he will have to bear the cost of conversion into the designated currency. On maturity, he can freely repatriate the principal and interest (which he will receive in the designated currency that he can convert into any other currency, at his cost). Interest earned on these deposits is exempt from tax in India.

• *Non-Resident External Rupee Account (NRE)*
As in the case of FCNR,

o The money has to come through a remittance from abroad, or a transfer from another FCNR / NRE account.
o The principal and interest are freely repatriable.
o Interest earned is exempt from tax in India.

The differences are:
o It can be operated with a cheque, as in the case of any savings bank account.
o It is maintained in rupees. Therefore, a depositor bringing money in another currency will have to first convert them into rupees; and then re-convert them to the currency in which he wants to take the money out. If during the deposit period, the rupee becomes weaker, then that loss is to the account of the depositor.

• *Non-Resident Ordinary Account (NRO)*
As with a NRE account,
o It can be operated with a cheque, as in the case of any savings bank account.
o It is maintained in rupees with the resulting implications in terms of currency conversion losses for the depositer.

The differences from NRE are:
o The money can come from local sources – not necessarily a foreign remittance or FCNR / NRE account.
o The principal amount is not repatriable, though the interest can be repatriated.
o The bank will deduct tax at source, on the interest earned in the deposit.
o A non-resident can open an NRO account jointly with a resident.

Joint Accounts
Two or more individuals may open a joint account. Various options exist for operating the account:
• Jointly by A and B – Both A and B will have to sign for withdrawals and other operations. For example, high value transactions in a partnership firm may require the joint signature of two or more partners.
• Either or Survivor – Either of them can operate the account individually. After the demise of one, the other can operate it as survivor. This is the normal option selected by families.
• Former or Survivor – The first person mentioned as account-holder will operate it during his / her lifetime. Thereafter, the other can operate. This option is often selected by a parent while opening an account with the son / daughter.
• Latter or Survivor - The second person mentioned as account-holder will operate it during his / her lifetime. Thereafter, the other can operate. While opening the account, the operating option needs to be clearly specified.

Nomination
The bank account opening form provides for the account holder to select a nominee. In the event of demise of the account holder, the bank will pay the deposit amount to the nominee, without any legal formalities. The salient provisions regarding nomination facility in bank accounts are as follows:
• Nomination facility is available for all kinds of bank accounts – savings, current and fixed deposit.
• Nomination can be made only in respect of a deposit which is held in the individual capacity of the depositor and not in any representative capacity such as the holder of an office like Director of a Company, Secretary of an Association, partner of a firm and Karta of an HUF.
• In the case of a deposit made in the name of a minor, nomination shall be made by a person lawfully entitled to act on behalf of the minor.
• Nomination can be made in favour of one person only.
• Nomination favouring the minor is permitted on the condition that the account holder, while making the nomination, appoints another individual not being a minor, to receive the amount of the deposit on behalf of the nominee in the event of the death of the depositor during the minority of the nominee.

• Cancellation of, or variation in, the nomination can be made at any time as long as the account is in force. While making nomination, cancellation or variation, witness is required and the request should be signed by all account holders.
• When the nominee makes a claim to the bank account, two documents are normally asked for:
o Proof of death of depositer
o Identity proof of nominee
• Payment to nominee only releases the bank from its obligation on the account. The nominee would receive the money, in trust, for the benefit of the heirs. The legal heirs of the deceased person can claim their share of the deposit proceeds from the nominee.

Closure of Deposit Accounts
This might occur in different ways:
• Account-holder can request closure of the account, and give instructions on how the balance in the deposit should be settled.
• On death of the sole account holder, the account would be closed and balance paid to the nominee. If nominee is not appointed, then bank would pay the legal representative of the account holder.
• On receipt of notice of insanity or insolvency of the sole account holder, the bank will stop operations in the account.
• On receipt of notice of assignment of the bank account, the bank would pay the amount lying in the account to the assignee.
• On receipt of a court order or garnishee order from Income Tax authorities, the bank would stop the transactions in the bank account during the pendency of the order.

Deposit Insurance
Deposit Insurance and Credit Guarantee Corporation (DICGC) was set up by RBI with the intention of insuring the deposits of individuals. The deposit insurance scheme covers:
• All commercial banks, including branches of foreign banks operating in India, and Regional Rural Banks
• Eligible co-operative banks.
The insurance scheme covers savings account, current account, term deposits and recurring accounts. However, the following deposits are not covered by the scheme:
• Deposit of Central / State Government
• Deposit of foreign governments
• Inter-bank deposits
• Deposits received outside India
In order for depositers in a bank to benefit from the insurance scheme, the bank should have paid DICGC the specified insurance premium (10 paise per annum per Rs. 100 of deposit).

Under the Scheme, in the event of liquidation, reconstruction or amalgamation of an insured bank, every depositor of that bank is entitled to repayment of the deposits held by him in the same right and same capacity in all branches of that bank upto an aggregate monetary ceiling of Rs. 1,00,000/- (Rupees one lakh). Both principal and interest are covered, upto the prescribed ceiling.

MANAGEMENT OF ADVANCES
In finance, a **loan** is a debt provided by one entity (organization or individual) to another entity at an interest rate, and evidenced by a note which specifies, among other things, the principal amount, interest rate, and date of repayment. A loan entails the reallocation of the subject asset(s) for a period of time, between the lender and the borrower.

In a loan, the borrower initially receives or *borrows* an amount of money, called the *principal*, from the lender, and is obligated to *pay back* or *repay* an equal amount of money to the lender at a later time. Typically, the money is paid back in regular *installments*, or partial repayments; in an annuity, each installment is the same amount.

The loan is generally provided at a cost, referred to as interest on the debt, which provides an incentive for the lender to engage in the loan. In a legal loan, each of these obligations and restrictions is enforced by contract, which can also place the borrower under additional restrictions known as loan covenants. Although this article focuses on monetary loans, in practice any material object might be lent.

Acting as a provider of loans is one of the principal tasks for financial institutions. For other institutions, issuing of debt contracts such as bonds is a typical source of funding.

Types of loans

Secured

A secured loan is a loan in which the borrower pledges some asset (e.g. a car or property) as collateral.

A mortgage loan is a very common type of debt instrument, used by many individuals to purchase housing. In this arrangement, the money is used to purchase the property. The financial institution, however, is given security — a lien on the title to the house — until the mortgage is paid off in full. If the borrower defaults on the loan, the bank would have the legal right to repossess the house and sell it, to recover sums owing to it.

In some instances, a loan taken out to purchase a new or used car may be secured by the car, in much the same way as a mortgage is secured by housing. The duration of the loan period is considerably shorter — often corresponding to the useful life of the car. There are two types of auto loans, direct and indirect. A direct auto loan is where a bank gives the loan directly to a consumer. An indirect auto loan is where a car dealership acts as an intermediary between the bank or financial institution and the consumer.

Unsecured

Unsecured loans are monetary loans that are not secured against the borrower's assets. These may be available from financial institutions under many different guises or marketing packages:

- credit card debt
- personal loans
- bank overdrafts
- credit facilities or lines of credit
- corporate bonds (may be secured or unsecured)
-

The interest rates applicable to these different forms may vary depending on the lender and the borrower. These may or may not be regulated by law. In the United Kingdom, when applied to individuals, these may come under the Consumer Credit Act 1974.

Interest rates on unsecured loans are nearly always higher than for secured loans, because an unsecured lender's options for recourse against the borrower in the event of default are severely limited. An unsecured lender must sue the borrower, obtain a money judgment for breach of contract, and then pursue execution of the judgment against the borrower's unencumbered assets (that is, the ones not already pledged to secured lenders). In insolvency proceedings, secured lenders traditionally have priority over unsecured lenders when a court divides up the borrower's assets. Thus, a higher interest rate reflects the additional risk that in the event of insolvency, the debt may be uncollectible.

Demand

Demand loans are short term loans that are atypical in that they do not have fixed dates for repayment and carry a floating interest rate which varies according to the prime lending rate. They can be "called" for repayment by the lending institution at any time. Demand loans may be unsecured or secured.

Subsidized
A subsidized loan is a loan on which the interest is reduced by an explicit or hidden subsidy. In the context of college loans in the United States, it refers to a loan on which no interest is accrued while a student remains enrolled in education.

Concessional
A concessional loan, sometimes called a "soft loan," is granted on terms substantially more generous than market loans either through below-market interest rates, by grace periods or a combination of both.[3] Such loans may be made by foreign governments to poor countries or may be offered to employees of lending institutions as an employee benefit.

Target markets
Personal or commercial
Loans can also be subcategorized according to whether the debtor is an individual person (consumer) or a business. Common personal loans include mortgage loans, car loans, home equity lines of credit, credit cards, installment loans and payday loans. The credit score of the borrower is a major component in and underwriting and interest rates (APR) of these loans. The monthly payments of personal loans can be decreased by selecting longer payment terms, but overall interest paid increases as well. For car loans in the U.S., the average term was about 60 months in 2009.

Loans to businesses are similar to the above, but also include commercial mortgages and corporate bonds. Underwriting is not based upon credit score but rather credit rating.

Loan payment
The most typical loan payment type is the fully amortizing payment in which each monthly rate has the same value over time.

The fixed monthly payment **P** for a loan of **L** for **n** months and a monthly interest rate **c** is:

$$P = L \cdot \frac{c\,(1+c)^n}{(1+c)^n - 1}$$

Abuses in lending
Predatory lending is one form of abuse in the granting of loans. It usually involves granting a loan in order to put the borrower in a position that one can gain advantage over him or her. Where the moneylender is not authorized, they could be considered a loan shark.

Usury is a different form of abuse, where the lender charges excessive interest. In different time periods and cultures the acceptable interest rate has varied, from no interest at all to unlimited interest rates. Credit card companies in some countries have been accused by consumer organizations of lending at usurious interest rates and making money out of frivolous "extra charges".
Abuses can also take place in the form of the customer abusing the lender by not repaying the loan or with an intent to defraud the lender.

INVESTMENT MANAGEMENT
Investment management is the professional asset management of various securities (shares, bonds and other securities) and other assets (e.g., real estate) in order to meet specified investment goals for the benefit of the investors. Investors may be institutions (insurance companies, pension funds, corporations, charities, educational establishments etc.) or private investors (both directly via investment contracts and more commonly via collective investment schemes e.g. mutual funds or exchange-traded funds).

The term asset management is often used to refer to the investment management of collective investments, while the more generic fund management may refer to all forms of institutional

investment as well as investment management for private investors. Investment managers who specialize in *advisory* or *discretionary* management on behalf of (normally wealthy) private investors may often refer to their services as money management or portfolio management often within the context of so-called "private banking".

The provision of investment management services includes elements of financial statement analysis, asset selection, stock selection, plan implementation and ongoing monitoring of investments. Coming under the remit of financial services many of the world's largest companies are at least in part investment managers and employ millions of staff.

Fund manager (or investment adviser in the United States) refers to both a firm that provides investment management services and an individual who directs fund management decisions.

At the heart of the investment management industry are the managers who invest and divest client investments.
A certified company investment advisor should conduct an assessment of each client's individual needs and risk profile. The advisor then recommends appropriate investments.

Asset allocation
The different asset class definitions are widely debated, but four common divisions are stocks, bonds, real-estate and commodities. The exercise of allocating funds among these assets (and among individual securities within each asset class) is what investment management firms are paid for. Asset classes exhibit different market dynamics, and different interaction effects; thus, the allocation of money among asset classes will have a significant effect on the performance of the fund. Some research suggests that allocation among asset classes has more predictive power than the choice of individual holdings in determining portfolio return. Arguably, the skill of a successful investment manager resides in constructing the asset allocation, and separately the individual holdings, so as to outperform certain benchmarks (e.g., the peer group of competing funds, bond and stock indices).

Long-term returns
It is important to look at the evidence on the long-term returns to different assets, and to holding period returns (the returns that accrue on average over different lengths of investment). For example, over very long holding periods (e.g. 10+ years) in most countries, equities have generated higher returns than bonds, and bonds have generated higher returns than cash. According to financial theory, this is because equities are riskier (more volatile) than bonds which are themselves more risky than cash.

Diversification
Against the background of the asset allocation, fund managers consider the degree of diversification that makes sense for a given client (given its risk preferences) and construct a list of planned holdings accordingly. The list will indicate what percentage of the fund should be invested in each particular stock or bond. The theory of portfolio diversification was originated by Markowitz (and many others). Effective diversification requires management of the correlation between the asset returns and the liability returns, issues internal to the portfolio (individual holdings volatility), and cross-correlations between the returns.

Investment styles
There are a range of different styles of fund management that the institution can implement. For example, growth, value, growth at a reasonable price (GARP), market neutral, small capitalisation, indexed, etc. Each of these approaches has its distinctive features, adherents and, in any particular financial environment, distinctive risk characteristics. For example, there is evidence that growth styles (buying rapidly growing earnings) are especially effective when the companies able to generate such growth are scarce; conversely, when such growth is plentiful, then there is evidence that value styles tend to outperform the indices particularly successfully.

CHEQUES

A **cheque** (or **check** in American English) is a document that orders a payment of money from a bank account. The person writing the cheque, the *drawer*, has a transaction banking account (often called a current, cheque, chequing or checking account) where their money is held. The drawer writes the various details including the monetary amount, date, and a payee on the cheque, and signs it, ordering their bank, known as the *drawee*, to pay that person or company the amount of money stated.

A cheque is a special type of bill of exchange.
A 'cheque, is a bill of exchange drawn on a specified banker, expressed to be payable only on demand (Sec.6).
Although a cheque is a bill of exchange, yet is have two additional characteristics, namely:
(i) A cheque is always drawn on a specified banker with whom the drawer has deposited the money;
(ii) It is always payable on demand.

Thus all cheques are bills of exchange but all bills of exchange are not cheques.

Crossing of Cheques:

Cheques are of two types, open cheques and crossed cheques. Open cheques are those which are paid over the counter of the bank. In other words, they need not be put through a bank account. Open cheques are liable to great risk in the course of circulation.

They may be either lost or stolen and the finder or thief can get it encased at the bank unless the drawer has in the meantime countermanded payment. With a view to avoiding such risks, and protect the owner of cheque, a system of crossing was introduced.

Crossing is a direction to the banker not to pay the cheque across the counter but to pay to a bank only or to particular bank in an account with the bank. Thus crossing provides a protection and safeguard to the owner of the cheque as by securing payment through a banker; it can easily be detected to whose use the money is received. Crossing does not, however, affect the negotiability or transferability of a cheque. But where the words 'not negotiable' are added, the cheque is not negotiable. The practice of crossing is confined to cheques only and cannot be extended to any other instrument.

Modes of crossing:

To cross a cheque, two transverse parallel lines are drawn on the left hand corner of the cheque. It is also usual to write the words "& Co", in between these two lines. However, it is not necessary to write these words. A crossing is a direction to the paying banker not to pay the money to the holder at the counter.

Types of Crossing:

Crossing are of the following types:
(1) General crossing;
(2) Special crossing;
(3) However, there is yet another type of crossing which is recognized by usage and custom, called restrictive crossing:
(4) Not negotiable crossing.

1. General Crossing:

In a general crossing, simply two parallel transverse lines, with or without the words 'not negotiable' in between, may be drawn. Such a cheque is crossed generally.
The effect of general crossing is that the payment of the cheque will not be made at the counter, it can be collected only through a banker.

2. Special Crossing:
In a special crossing, the name of a banker with or without the words 'not negotiable' is written on the cheque. Such a cheque is crossed specially to that banker.
It should be noted that two transverse parallel lines are necessary for a general crossing, whereas for a special crossing, no such lines are necessary.
The effect to special crossing is that the paying banker will be the amount of the cheque only through the bank named in the cheque.

3. Restrictive crossing:
Besides the two statutory types of crossing discussed above, there is one more type of crossing namely, restrictive crossing. This type of crossing has been recognised by usage and custom of the trade.
In a restrictive crossing the words 'Account Payee' or Account Payee Only' are added to the general or special crossing.
The effect of restrictive crossing is that the payment of the cheque will be made by the bank to the collecting banker only for the account payee named. If the collecting banker collects the amount for any other person, he will be liable for wrongful conversion of funds.
It should be noted that the duty of the paying banker is only to ensure that the payment is made through the named bank, if there is any. He is not liable, in case the collecting banker collects the cheque for any other person than the account payee. In that case collecting banker will be liable to the true owner.

4. Not negotiable Crossing (Sec. 130):
A person taking is cheque crossed generally or specially, bearing in either case the words 'not negotiable' shall not be able to give a better title to the holder than that of the transferor.
The effect of a not negotiable crossing is that the cheque can be transferred but the transferee will not acquire a better title to the cheque. Thus a cheque is deprived of its essential feature of negotiability.
The objects of "not negotiable" crossing is to protect the drawer against loss or theft in the course of transit.

Example:
A cheque was drawn in favour of a firm B & Co. The cheque was crossed 'not negotiable'; one of the partners, A in fraud of his Co-partner B, endorsed the cheque to P who encashed it. Held that B, who under the terms of the partnership agreement was entitled to the cheque could recover the amount from P as A could not transfer better title than he himself had [Fisher v. Roberst]
Who may cross a cheque? As a rule, it is the drawer who can cross a cheque. However, Sec. 125 provides that even a holder can cross the cheque. It further provides that a banker can cross the cheque specially for collecting to another banker as his agent for collection.

Between a Bill of Exchange and a Cheque:
Although a cheque is a bill of exchange and there is too much of similarity between the two, yet there are the following points of difference between a bill and a cheque;

i. A bill of exchange may be drawn on any person. A cheque is always drawn on a specified banker with whom the drawer has deposited money. 'A bill' can be drawn even on a bank.
ii. Certain types of bills of exchange must be accepted before they are presented for payment. In case of a cheque, acceptance is not at all necessary.
iii. A bill of exchange has to be stamped according to the Indian Stamp Act. Stamp is not at all necessary on a cheque.
iv. A bill of exchange may be payable on demand or after a certain period. A cheque is always payable on demand.
v. A bill of exchange cannot be made payable to bearer on demand. A cheque can be made payable on demand.

vi. In a bill three days of grace are allowed to the acceptor for payment. In case of a cheque, no such grace period is allowed and it is payable immediately on demand, of course, during working hours of the bank.

vii. In case a bill of exchange is not presented for payment, the drawer is discharged from his liability. Failure to present the cheque discharges the drawer, only when he has suffered any loss due to the failure of the holder to present the cheque for payment within a reasonable time of its issue. In such a case the loss is limited to the loss suffered by the drawer due to non - presentment.

Bank Draft of Demand Draft:

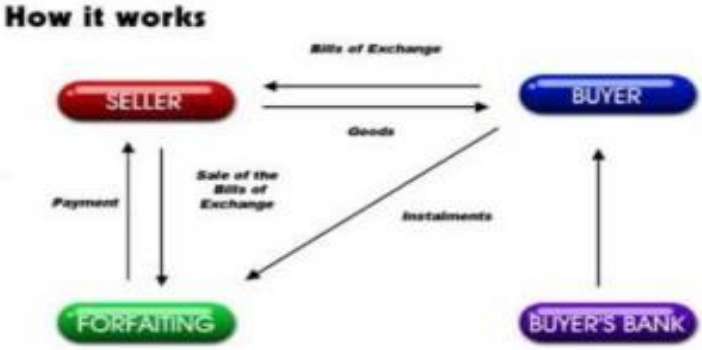
A bank draft or a demand draft, is a bill of exchange drawn by one bank on its own branch or any other bank. The essential features of a bank draft are:

1. It is always drawn by a bank upon its own branch or another bank.
2. It is always payable on demand and it cannot be made payable to bearer.
3. Ordinarily, payment of ^demand draft cannot be stopped or countermanded. It is because of this reason that payment is demanded through a bank draft.

BILLS AND THEIR ENDORSEMENT

A non-interest-bearing written order used primarily in international trade that binds one party to pay a fixed sum of money to another party at a predetermined future date.

Bills of exchange are similar to checks and promissory notes. They can be drawn by individuals or banks and are generally transferable by endorsements. The difference between a promissory note and a bill of exchange is that this product is transferable and can bind one party to pay a third party that was not involved in its creation. If these bills are issued by a bank, they can be referred to as bank drafts. If they are issued by individuals, they can be referred to as trade drafts.



Endorsement:

Endorsement means the signature of the maker/ drawer or a holder of a negotiable instrument, either with or without any writing, for the purpose of negotiation. The endorsement is done by the payee or endorsee, as the case may be by signing on the instrument customarily on its back & where the space is insufficient on a slip of paper annexed thereto called “allonge”.

There are five kinds of endorsement:

1. **Blank endorsement:** If the endorser signs his name only, the endorsement is said to be in blank and it becomes payable to bearer, e.g. Mahbubul Haq.

2. **Special or Full endorsement:** An endorsement “in full” or a special endorsement is one where the endorser not only puts his signature on the instrument but also writes the name of a person to whom or to whose order the payment is to be made. Example: Pay to Mr. Rafiqul Islam or order-Sd/Sarafat All.

3. **Conditional endorsement:** In conditional endorsement the endorser puts his signature under such a writing which makes the transfer of title subject to fulfillment of some conditions of the

happening of some events. Example: Pay to Mr. Sarwar Jahan or order after his marriage-Sd/Badrul Kamal.

4. **Restrictive endorsement:** An endorsement is called restrictive when the endorser restricts or prohibits further negotiation. Example: "Pay to Miss. / A. Pereira only" Sd/Hosne Ara.

5. **Partial endorsement:** In Partial endorsement only a part of the amount of the bill is transferred or the amount of the bill is transferred to two or more endorsees severally. This does not separate as a negotiation of the instrument. The law lays down that an endorsement must relate to the whole instrument. However, where the amount has been partly paid, a note to that affect may be endorsed on the instrument which may then be negotiated for the balance. This is not done in case of cheques or banker's drafts.

GOVERNMENT SECURITIES

A bond (or debt obligation) issued by a government authority, with a promise of repayment upon maturity that is backed by said government. A government security may be issued by the government itself or by one of the government agencies. These securities are considered low-risk, since they are backed by the taxing power of the government.

A **government bond** is a bond issued by a national government, generally with a promise to pay periodic interest payments and to repay the face value on the maturity date. Government bonds are usually denominated in the country's own currency. Bonds issued by national governments in foreign currencies are normally referred to as "sovereign bonds", although the term sovereign bond may also refer to bonds issued in a country's own currency.

Risks

Credit risk

Government bonds in a country's own currency are sometimes taken as an approximation of the theoretical risk-free bond, because it is assumed that the government can raise taxes or create additional currency in order to redeem the bond at maturity. There have been instances where a government has defaulted on its domestic currency debt, such as Russia in 1998 (the "ruble crisis") (see national bankruptcy).

Currency risk

Currency risk is the risk that the value of the currency a bond pays out will decline compared to the holder's reference currency. For example, a German investor would consider United States bonds to have more currency risk than German bonds (since the dollar may go down relative to the euro); similarly, a United States investor would consider German bonds to have more currency risk than United States bonds (since the euro may go down relative to the dollar).

Inflation risk

Inflation risk is the risk that the value of the currency a bond pays out will decline over time. Investors expect some amount of inflation, so the risk is that the inflation rate will be higher than expected. Many governments issue inflation-indexed bonds, which protect investors against inflation risk by linking both interest payments and maturity payments to a consumer prices index.

PROCEDURE OF E-BANKING

Online banking (or **Internet banking** or **E-banking**) allows customers of a financial institution to conduct financial transactions on a secured website operated by the institution, which can be a retail bank,virtual bank, credit union or building society.

To access a financial institution's online banking facility, a customer having personal Internet access must register with the institution for the service, and set up some password (under various names) for customer verification. The password for online banking is normally not the same as for [telephone

banking]. Financial institutions now routinely allocate customers numbers (also under various names), whether or not customers intend to access their online banking facility. Customers numbers are normally not the same as account numbers, because number of accounts can be linked to the one customer number. The customer will link to the customer number any of those accounts which the customer controls, which may be cheque, savings, loan, credit card and other accounts. Customer numbers will also not be the same as any debit or credit card issued by the financial institution to the customer.

To access online banking, the customer would go to the financial institution's website, and enter the online banking facility using the customer number and password. Some financial institutions have set up additional security steps for access, but there is no consistency to the approach adopted.

Features

Online banking facilities offered by various financial institutions have many features and capabilities in common, but also have some that are application specific.

The common features fall broadly into several categories

- A bank customer can perform non-transactional tasks through online banking, including -
  - viewing account balances
  - viewing recent transactions
  - downloading bank statements, for example in PDF format
  - viewing images of paid cheques
  - ordering cheque books
  - download periodic account statements
  - Downloading applications for M-banking, E-banking etc.
- Bank customers can transact banking tasks through online banking, including -
  - Funds transfers between the customer's linked accounts
  - Paying third parties, including bill payments (see, e.g., BPAY) and telegraphic/wire transfers
  - Investment purchase or sale
  - Loan applications and transactions, such as repayments of enrollments
  - Register utility billers and make bill payments
- Financial institution administration
- Management of multiple users having varying levels of authority
- Transaction approval process
- the process of banking has become much faster

Some financial institutions offer unique Internet banking services, for example

- Personal financial management support, such as importing data into personal accounting software. Some online banking platforms support account aggregation to allow the customers to monitor all of their accounts in one place whether they are with their main bank or with other institutions.

Procedure in E-Banking

i. Request for opening new account and opt for Internet Banking facility at the branch.
ii. User-id/passwords would be provided as per the procedure defined above.
iii. Activation of the users would be as per the above procedure.
iv. Login into Internet banking services with a valid User-id & password.
v. Click on the Requests option
vi. Select “Request for Transaction Password”
vii. Submit the details for transaction passwords (like address, user-id etc.)
viii. The transaction password will be created at HO and sent directly on the address mentioned in the request.
ix. On receipt of transaction password, login into the services

x. Select “Request for activation of Transaction password”.
xi. Submit the details.
xii. Activation would be done within 24 hours of receiving the request.

Unit – 4
Banking regulation Act, 1949

Definitions

1. According to Section 1, the Act is called the Banking Regulation Act 1949. It extends to the whole of India. It came into force on 16th March, 1949.
2. According to Section 5(b), "banking" means the accepting of deposits of money from the public for the purpose of lending or investment, repayable on demand or otherwise and withdrawal by cheques, draft, and order or otherwise. It may be noted that "banking does not include other commercial activities carried on by a banking company".

Main provisions of Banking Regulation Act, 1949

1. **Management of a Bank –** With the regard to the management of a banking company, Section 10 provides as follows –
   a. A banking company cannot employ or be managed by a managing agent.
   b. It cannot employ "any person" who has been adjudicated insolvent, or has been convicted by a criminal Court for any act of moral turpitude; who is a director of any other company; who is engaged in any other business or vocation; whose term of office as a person managing the company is for more than 5 years at any one time; whose total remuneration or its part taken the form of commission or of a share in the profits of the company; and whose remuneration is excessive in the opinion of the Reserve Bank of India. It may be noted here that "any person" does not include the managerial or administrative staff.
   c. The board of directors of a banking company shall include not less than 51% of its total number of members, persons with professional or other practical experience in the matter such as accountancy, agriculture and rural economy, banking, cooperation, economics, finance, law, small scale industry etc.
   d. Every banking company shall be managed by a whole-time chairman who shall be entrusted with the management of the whole of its affairs. The chairman shall exercise his powers subject to the superintendence, control, and direction of the board of directors. The chairman shall be one of the directors. Where a chairman is appointed on part-time basis, such appointment shall be with the previous approval of the Reserve Bank of India. The whole-time chairman shall hold office maximum for 5 years, but shall be eligible for re-election of appointment.
   e. Section 16 prohibits common directors and states a banking company cannot have a person director, who is a director of any other banking company.
2. **Capital and Reserve –** Section 12 states that the subscribed capital of a banking company cannot be less than 50% of the authorised capital, and the paid-up capital cannot be less than 50% o the subscribed capital. Further, the capital of the company shall consist of ordinary shares or equity shares only. A shareholder cannot exercise his voting rights on poll in excess of 10% of the total voting rights of all the shareholders of the banking company. According to section 17, every banking company shall create a Reserve Fund (known as statutory Reserve Fund), and before declaring any dividend, transfer to it at least 20% of its profit each year. When the amount in the Reserve fund together with the amount in the share premium account equals the paid-up capital, then (and not before that) the Central Government on the recommendation of the Reserve Bank, can allow a banking company not to transfer the stipulated 20% of profit to the reserve fund.
3. Licensing of banking companies – According to Section 22, a banking company cannot carry on banking business in India unless it holds a licence issue in that behalf by the Reserve Bank.
   a. The banking company is or will be in a position to pay its present or future depositors in full as their claims accrue.
   b. The affairs of the company are not being or likely to e conducted in a manner detrimental to the interest of its present or future depositors.
   c. The general character of the proposed management of the company will not be prejudicial o the public interest or the interest of its depositors.

   d. The company has adequate capital structure and earning prospects.
   e. The public interest will be served by the grant of a licence to the company to carry on banking business in India.
4. Opening of New branches and transfer of existing branches – Section 23 provides that without obtaining the prior permission of the Reserve Bank, a banking company cannot open a new branch. It cannot change the location of an existing branch. The same restriction applies to opening or transferring branches outside India. However, a temporary branch may be opened for a maximum period of one month for the purpose of affording banking facilities to the public on the occasion of an exhibition, a conference, or a 'mela' or any other similar occasion, if the banking company already has a branch in that city, town, or village.
5. Inspection – According to Section 35, the Reserve Bank on its own or on being directed by the Central Government, can cause an inspection of any banking company and its books and accounts; may also cause scrutiny of its affairs and books and accounts, and the officers of the company shall have to fully cooperate with it.
6. **Procedure for amalgamation of banking companies –** According to Section 44 A, a banking company cannot be amalgamation with another banking company, unless a scheme containing the terms of such amalgamation has been placed in draft before the shareholders of each of such companies separately, and approved by a resolution passed y a 2/3rd majority of shareholders of each of the said companies, present either in person or by proxy at a meeting called for the purpose.

Powers or Rights or Functions of Reserve Bank under the Banking Regulation Act, 1949

With a view to controlling and regulating the banking companies and banking institution in the interest of depositors and shareholders, the Reserve Bank enjoys the following powers or rights or functions under various provisions of the Banking Regulation Act, 1949 –

1. Power to appoint chairman or managing director – Section 10BB provides that where the office of the whole-time chairman of the Board of Directors or a Managing director is vacant, then the Reserve Bank may appoint an eligible person to the whole-time Chairman or Managing Director, if in its opinion the continuation of such vacancy is likely to adversely affect the interests of the banking company.
2. Power to publish information – According to Section 28, the Reserve Bank may publish any information obtained by it under this act in such consolidated form as it thinks fit, if it considers that doing so will be in the public interest.
3. Power to give directions – Section 35A provides that if it is necessary in the interest of the public or of the banking policy or of the depositors or of the banking company or of the proper management of any banking company, then the Reserve Bank may issue from time to time such directions as it deems fit to banking companies generally or to pay banking company in particular, and they shall be bound to comply with such directions.
4. Power to remove managerial and other persons from office – Under Section 36AA, Reserve Bank may remove from office any chairman, director, chief executive officer or to the officer or employee of a banking company, if it is necessary to do so (i) in the public interest, or (ii) for preventing the affairs being conducted in a manner detrimental to the interest of depositors, or (iii) for securing he proper management of the company.
5. Power to appoint additional directors – According to section 36AB, Reserve Bank may appoint from time to time one or more or persons to hold office as additional directors of a banking company, if in the opinion of the Reserve Bank it is necessary to do so, in the interest of banking policy or in the public interest or in the interest of the company or its depositors.

PRIVATISATION OF BANKS – NARSIMHAN COMMITTEE REPORT

Introduction

After independence a need was badly felt to overhaul the banking system in India. The State Bank of India was governed by the State Bank of India Act, 1955 and other: State Banks were governed by the

State Banks of India (Subsidiaries Banks) Act, 1959 and the other commercial banks by the Companies Act, 1956. The provisions of these Acts were not uniform, sufficient and effective. In order to regulate the banking system, the much needed Banking Regulation Act, was passed in 1949.
The Banking Regulation Act has been amended a number of times since its inception. In 1968, a landmark amendment was made to provide for social control on banks in India.

Narsimhan Committee Report
The process of bank reforms started in 1949 with the passing of the Banking Regulation Act, 1949. This provided a general framework for the organization, management, monitoring and regulation of the banking sys-tem. However, a need was badly felt to further reform the banking system.
In 1991, Narsimhan Committee on Financial System was appointed. The Committee was to consider all aspects of the structure, organisation, functions and procedures of the financial system. The Committee observed that the financial and banking system faced the following problems:

1. Decline in efficiency.
2. Decline in productivity, and consequently.
3. Reduction in profits.

The reasons for this sorry state of affairs were:

1. Low rate of interest on directed investment.
2. Low rate of interest on directed loans and advances.
3. Unnecessary expenditure on unremunerative branch expansion.
4. Inadequate provision for loss on investment.
5. Overstaffing in metropolitan and urban centres.
6. Excessive administrative and political interference in the management of financial institutions.

In view of deteriorating financial health it warned that immediate remedial steps should be taken otherwise it may further reduce the value and return on banks' savings deposits. It may also shake the confidence of the depositors and other investors.
The Committee made a number of recommendations to remedy the sorry state of banking system. The important ones are:

1. The Cash Reserve Ratio should be increased.
2. The Reserve Bank should use open market operations instead of cash reserve ratio to control credit.
3. Directed credit programme should be discontinued.
4. Interest rate should be deregulated and concessional interest rates should be discontinued.
5. Inadequacy of capital in the banking system should be removed. Banks and financial institutions should achieve a 4% capital adequacy ratio in relation to risk weighted assets in 5 years time. The capital adequacy ratio should be raised to 10% over a period of time.
6. There should be more transparency in Financial Statements of banks as recommended by the International Accounting Standard Committee.
7. Debt recovery system should be streamlined. Assets Reconstruction Fund should be established to take over bad and doubtful debts of the bank at a discount.
8. Banks should be restructured on the following broad pattern:
   a. 3 to 4 large banks (including State Bank of India) which could be international in character.
   b. 8 to 10 national banks with branches throughout the country engaged in universal banking.
   c. Local banks which could operate in a specific region, rural banks (including Regional Rural Banks) whose operations could be confined to rural areas.

   The reorganization should be based on market requirements and should be viable.
9. Government should assure that there will be no more nationalization of banks and should not discriminate between public and private sector banks.
10. There should not be any check on opening bank branches. Banks should be free to decide where they want to open a branch and opening of branches by foreign banks should be made more liberal.
11. Major Banks should be allowed to open more foreign branches.

12. Medium and large sized banks should have three tier structures, i.e., head office, zonal office and branches. For every large bank like State Bank of India four-tier system, i.e., head office, zonal office, regional office and branches.
13. There was excessive Government control on banks and financial institutions. It should be removed. Instead there should be greater emphasis on internal control and internal audit checks.
14. Double control by the Reserve Bank and the concerned Ministry of the Government should end.
15. Appointment of the Chief Executive (CMD) of banks should be depoliticalised. Their term of appointment should be ensured. Representative of the Reserve Bank on the banks' Board should be discontinued.
16. Banks should be encouraged to give term loans.
17. 23. State Government's dominance over State Financial Institutions (SFI) should be checked. SFI should work independently on business principles.
18. 24. Concessional finance to Development Financial Institutions through SLR should be phased out gradually.
19. Capital market should be freed from Government or SERI control.
20. A large number of new institutions in the financial market like merchant banks, mutual funds, venture capital funds, leasing companies have sprung up. There is an urgent need to regulate them. SEBI may be assigned this responsibility. Restrictions on venture capital fund should be removed. Norms and guidelines for banks and financial institutions should be laid down in respect of adequacy of capital, debt equity ratio, income recognition, provision for doubtful debts, disclosure requirements, adoption of accounting and financial policies and valuation of assets etc.

Banking sector Reforms in India

1. Motivation to private sector Banks
2. Computerization of Banks
3. Mobile Banking
4. Evening Banks
5. Customer Oriented
6. Less formalities
7. Diversification in banking
8. Training facilities
9. Crop insurance scheme
10. Flexibility for interest ratio

UNIT – V

The companies Act, 1956 requires a banking company to maintain at its registered office proper books of account with respect to:

1. All receipts and disbursements of money and the matters in respect of which the receipt and disbursements take bank.
2. The assets and liabilities of the bank.

Where a banking company has a branch office, book of accounts relating to the transactions effected at the branch office be kept at the branch. At an interval of not more than 3 months, summarized accounts shall be sent to the banking company at its registered office.

Books to be maintained by a Bank

1. Cash Book or Register
2. Cash Scroll
3. Payment Book
4. Token Book
5. Supplementary Day Book
6. Ledgers
7. Loans and Advances Register
8. Bills Receivables and Payable Register
9. Transfer Diary/Register
10. Security Register
11. Investment Register
12. Branch Ledger

Statement of Advances

Statements of Advances – The Reserve Bank may call for any information every half year regarding the investment of a banking company and the classification of its advances in respect of industry, commerce and agriculture.

Statement of Non-Performing Assets

According to the Guidelines issued by the Reserve Bank of India w.e.f. March 31, 2004 a non-performing asset means an advance where:

1. Interest and/or installment of principal remain overdue for a period of 180 days in respect of term loan;
2. The account remains out of order for a period of more than 90 days in respect of overdraft/ cash credit (OD/CC). An account shall be treated as 'out of order 'if the outstanding balance remains continuously in excess of the sanctioned limit of overdraft or cash credits.
3. The bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted.
4. Interest and/or instilment of principal remain overdue for two harvest seasons but for a period not exceeding two half years (Two periods of six months each) in the case of an granted for agricultural purposes; and
5. Any amount to be received remains overdue for a period of more than 90 days in respect of other accounts.

Appraisal of loan Application

1. Purpose of the loan – A loan may be taken for a productive purpose such as trade and commerce or for a non-productive such as marriage or religious ceremony. Priority should be given to productive purposes over non-productive ones.
2. Security for loan – For safety of the loan it should be adequately secured. A banker should prefer secured loans as against unsecured ones. However, due to social control over the banks, security consideration is not considered an important factor these days.
3. Character – The most important factor to be carefully examines, is the character of the borrower. Character is the sum total of honesty, integrity, creditworthiness, capacity to repay, sense of responsibility, good habits and reputation enjoyed by the customer.
4. Ability to run the enterprise – if the borrower is fully capable of running the enterprise and has necessary skill and experience, his chances of success are high. As such there is little or no risk in granting loans.
5. Adequate capital – An entrepreneur should have an adequate capital of his own. If his capital is inadequate there are greater chances of failure of his business.
6. Soundness of the project – The baker should carefully examine the project report to ascertain its technical feasibility, economic necessity, financial viability and soundness.

Development Banking in India

1. Industrial finance corporation of India (IFCI)
2. Industrial Development Bank of India (IDBI)
3. Industrial Credit and Investment Corporation of India (ICICI)

Industrial Finance Corporation of India (IFCI)

a. **Incorporation –** Industrial Finance Corporation of India (IFCI) is the first national level development bank. IFCI was established on 1st July, 1948 under an Act of Parliament.
It was converts into an autonomous corporation in 1993 to provide greater especially when accommodation from traditional sources of finance.

b. **Objectives –** Its basic objective is to provide medium and long-term finance especially when accommodation from traditional sources of finance or capital market is inadequate or not available.

c. **Management –** The Board of Directors of the IFCI consists of a whole time chairman and 12 directors. The chairman is appointed by the Central Government in consultant with the Industrial Development Bank of India. Two directors are nominated by the Central Government and four by the IDBI. The remaining six directors are elected by the shareholders other than the IDBI.

d. Functions

1. It guarantees loans floated by the industrial concerns in the open market,
2. It underwrites the issues of stock, shares, bonds and debentures floated by the industrial concerns.
3. It can subscribe directly to the stocks and shares of industrial units.
4. It can sanction loans and advances to public limited companies and co-operative societies, but not to private limited company or a partnership firm.
5. It can grant only medium-term and loan-term credit assistance to industrial units.

Industrial Development Bank of India (IDBI)

a. **Incorporation –** Industrial development Bank of India (IDBI) was established on July 1st, 1964 as wholly owned subsidiary of the Reserve Bank of India. On 16th Feb., 1976 it was converted into an wholly owned undertaking of the Government of India.

b. **Objectives –** It has also undertaken rehabilitation of sick units, for which, it is authorized to take over management or possession of the sick unit. It can prepare viable scheme of reconstruction, merger or amalgamation for rehabilitating sick units.

c. Functions

1. **Refinance of Industrial Loans –** It renders assistance by refinance the term loans extended by SFCs, SIDCs, commercial co-operative banks and RRBs to industrial concerns.
2. **Bills Rediscounting Scheme –** This scheme is meant to help the use of indigenous machinery by industrial concerns. Under this scheme, the purchaser draws the bill in favour of the manufacturer of machinery who discounts it with his banker who in turn gets it rediscounted from the IDBII. This facility is provided mainly to sugar, jute, cotton textiles, cement and engineering industries.
3. **Seed Capital Scheme –** Under this scheme, financial assistance is available to new entrepreneurs for meeting the gap in promoter's contribution as well as equity where no issue of public shares is done.
4. **Resources Support to Other Institutions –** The IDBI provides resource support to other financial institutions by subscribing to their shares and bonds/debentures such as IFCI, ICIC, SFCs, SIDCs, NSIC, and TCOs etc.

Industrial Credit and Investment Corporation

a. **Incorporation –** Industrial Credit and investment Corporation of India (ICICI) was established on 5th January, 1955.it was established on the recommendation of the International Bank for Reconstruction and Development (IBRD). ICICI merged with ICICI Bank Ltd. w.e.f. May, 2002. Now it has become a full-fledged Scheduled Bank rendering all types of financial and banking services.

b. **Objectives –** Its main objectives is to channelize funds provided by the World Bank and to build a capital market in the country.

c. Functions

1. Leasing Finance
2. It also acts as trustees for the convertible and non-convertible debenture holders.
3. Financial ssistance4 is also available in the form of foreign currency loans to import capital goods.
4. It also underwrites shares and debentures. Again, it guarantees loan repayable in rupee terms.
5. It provides assistance for development and expansion programmes to private sector industries.