மனோன்மணியம் சுந்தரனார் பல்கலைக்கழகம்

Manonmaniam Sundaranar University

Reaccredited with 'A' Grade (CGPA 3.13 Out of 4.0) by NAAC (3rd Cycle)

Tirunelveli - 627 012, Tamilnadu, India.

DIRECTORATE OF DISTANCE
&
CONTINUING EDUCATION

BANKING THEORY LAW AND PRACTICE

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BANKING THEORY LAW AND PRACTICE

Objectives

1. To create an idea of modern banking

2. To familiarise the students with the banking activities

Unit 1:

Banker and Customer Relationship between banker and customer-General and special relationship - Rights of the banker - Negotiable instruments -promissory note ,Bill of Exchange & Cheque (Meaning & Features) Proper Drawing of the cheque crossing (Definition & Types)- Endorsement (Definition & Kinds) - Material alternation

Unit II:

Banking System Indigenous Bankers-Commercial Banks - Co-Operative Banks – Land development banks-industrial development banks - NABARD -EXIM Bank-Foreign Exchange Banks

.Unit III:

Traditional Banking- Receiving Deposits -General Precautions-kinds of deposits-fixed -current-saving-recurring and others-lending loans and advances-principles of sound lending-forms of advances-loan, cash credit, overdraft and purchasing and discounting of bills. mode of charging security-lien, pledge, mortgage, assignment and hypothecation

Unit IV:

Modernized Banking -Core banking - Home banking - Retail banking - Internet banking - Online banking and Offline banking - Mobile banking -Electronic Funds Transfer - ATM and Debit Card - Smart Card - Credit Card - E-Cash-Swift-RTGS.

Unit V:

Reserve Bank of India- Functions of Reserve Bank of India - Methods of Credit Control.

Text Books

1. K.C. Sherlekar, Banking Theory Law and Practice, Himalaya Publishing House.

2. E.Gordon and K.Natarajan, Banking Theory Law and Practice, Himalaya Publishing House.

Reference Books

1. S.N.Lal, Banking Theory Law and Practice.

2. M.C.Tannen, Banking Theory Law and Practice. LexixNexix Vutterworth, Nagpoor.

3. S.S.Gulshan and Gulshank Kapoor, Banking Theory Law and Practice

4. S. Guruswamy, Banking Theory Law and Practice-3rd Edition, Vijay Nicole Imprints Private

Limited, Chennai.

UNIT-I

BANKER - CUSTOMER RELATIONSHIP

DEFINITION OF A 'BANKER'

The Banking Regulations Act (B R Act) 1949 does not define the term banker' but defines what banking is? As per **Sec.5 (b**) of the B R Act –Banking' means accepting, for the purpose of lending or investment, of deposits of money from the public repayable on demand or otherwise and withdraw able by cheque, draft, order or otherwise."

As per **Sec. 3** Indian Negotiable Instruments Act 1881, the word –banker includes any person acting as banker and any post office savings bank

According to Sec. 2 of the Bill of Exchange Act, 1882, banker includes a body of persons, whether incorporated or not who carry on the business of banking.'

Who is a 'Customer'?

The term Customer has not been defined by any act. The word customer' has been derived from the word custom', which means a habit or tendency' to-do certain things in a regular or a particular manner's .In terms of Sec.131 of Negotiable Instrument Act, when a banker receives payment of a crossed cheque in good faith and without negligence for a customer, the bank does not incur any liability to the true owner of the cheque by reason only of having received such payment. It obviously means that to become a customer account relationship is must. Account relationship is a contractual relationship.

BANKER-CUSTOMER RELATIONSHIP:

Banking is a trust-based relationship. There are numerous kinds of relationship between the bank and the customer. The relationship between a banker and a customer depends on the type of transaction. Thus the relationship is based on contract, and on certain terms and conditions.

These relationships confer certain rights and obligations both on the part of the banker and on the customer. However, the personal relationship between the bank and its

customers is the long lasting relationship. Some banks even say that they have generation-to-generation banking relationship with their customers. The banker customer relationship is fiducially relationship. The terms and conditions governing the relationship is not be leaked by the banker to a third party.

CLASSIFICATION OF RELATIONSHIP:

The relationship between a bank and its customers can be broadly categorized in to General Relationship and Special Relationship. If we look at **Sec 5(b)** of Banking Regulation Act, we would notice that bank‘s business hovers around accepting of deposits for the purposes of lending. Thus the relationships arising out of these two main activities are known as General Relationship. In addition to these two activities banks also undertake other activities mentioned in Sec.6 of Banking Regulation Act. Relationship arising out of the activities mentioned in Sec.6 of the act is termed as special relationship.

GENERAL RELATIONSHIP:

1. Debtor-Creditor: When a 'customer' opens an account with a bank, he fills in and signs the account opening form. By signing the form he enters into an agreement/contract with the bank. When customer deposits money in his account the bank becomes a debtor of the customer and customer a creditor. The money so deposited by customer becomes bank‘s property and bank has a right to use the money as it likes. The bank is not bound to inform the depositor the manner of utilization of funds deposited by him. Bank does not give any security to the depositor i.e. debtor. The bank has borrowed money and it is only when the depositor demands, banker pays. Bank‘s position is quite different from normal debtors.

Banker does not pay money on its own, as banker is not required to repay the debt voluntarily. The demand is to be made at the branch where the account exists and in a proper manner and during working days and working hours.

The debtor has to follow the terms and conditions of bank said to have been mentioned in the account opening form. {Though the terms and conditions are not mentioned in the account opening form, but the account opening form contains a declaration that the

terms and conditions have been read and understood or has been explained. In fact the terms and conditions are mentioned in the passbook, which is issued to the customer only after the account has been opened. In the past while opening account some of the banks had the practice of giving a printed handbill containing the terms and conditions of account along with the account open form. This practice has since been discontinued. For convenience and information of prospective customers a few banks have uploaded the account opening form, terms and conditions for opening account, rate charge in respect of various services provided by the bank etc., on their web site.

While issuing Demand Draft, Mail / Telegraphic Transfer, bank becomes a debtor as it owns money to the payee/ beneficiary.

2. Creditor–Debtor: Lending money is the most important activities of a bank. The resources mobilized by banks are utilized for lending operations. Customer who borrows money from bank owns money to the bank. In the case of any loan/advances account, the banker is the creditor and the customer is the debtor. The relationship when person deposits money with the bank reverses when he borrows money from the bank. Borrower executes documents and offer security to the bank before utilizing the credit facility. In addition to opening of a deposit/loan account banks provide variety of services, which makes the relationship more wide and complex. Depending upon the type of services rendered and the nature of transaction, the banker acts as a bailee, trustee, principal, agent, lessor, custodian etc.

SPECIAL RELATIONSHIP:

1. Bank as a Trustee: As per **Sec. 3** of Indian Trust Act, 1882 A "trust" is an obligation annexed to the ownership of property, and arising out of a confidence reposed in and accepted by the owner, or declared and accepted by him, for the benefit of another, or of another and the owner.‘ Thus trustee is the holder of property on behalf of a beneficiary.

As per **Sec. 15** of the Indian Trust Act, 1882 A trustee is bound to deal with the trust-property as carefully as a man of ordinary prudence would deal with such property if it were his own; and, in the absence of a contract to the contrary, a trustee so dealing is not responsible for the loss, destruction or deterioration of the trust-property.‘ A trustee has the right to reimbursement of expenses (Sec.32 of Indian Trust Act.).

In case of trust banker customer relationship is a special contract. When a person entrusts valuable items with another person with an intention that such items would be returned on demand to the keeper the relationship becomes of a trustee and trustier. A customer keeps certain valuables or securities with the bank for safekeeping or deposits certain money for a specific purpose (Escrow accounts) the banker in such cases acts as a trustee. Banks charge fee for safekeeping valuables

2. Bailee – Bailor: Sec.148 of Indian Contract Act, 1872, defines "Bailment" "bailor" and "bailee". A "bailment" is the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned or otherwise disposed of according to the directions of the person delivering them. The person delivering the goods is called the "bailor". The person to whom they are delivered is called, the "bailee".

Banks secure their advances by obtaining tangible securities. In some cases physical possession of securities goods (Pledge), valuables, bonds etc., are taken. While taking physical possession of securities the bank becomes bailee and the customer bailor. Banks also keeps articles, valuables, securities etc., of its customers in Safe Custody and acts as a Bailee. As a bailee the bank is required to take care of the goods bailed.

3. Lessor and Lessee: Sec.105 of ‗Transfer of property Act 1882‘ defines lease, Lessor, lessee, premium and rent. As per the section ―A lease of immovable property is a transfer of a right to enjoy such property, made for a certain time, express or implied, or in perpetuity, in consideration of a price paid or promised, or of money, a share of crops, service or any other thing of value, to be rendered periodically or on specified occasions to the transferor by the

transferee, who accepts the transfer on such terms.

Definition of Lessor, lessee, premium and rent:

(1)The transferor is called the lessor,

(2)The transferee is called the lessee,

(3)The price is called the premium, and

(4)The money, share, service or other thing to be so rendered is called the rent.

Providing safe deposit lockers is as an ancillary service provided by banks to customers. While providing Safe Deposit Vault/locker facility to their customers' bank enters into an agreement with the customer. The agreement is known as ―Memorandum of letting‖ and attracts stamp duty.

The relationship between the bank and the customer is that of lessor and lessee. Banks lease (hire lockers to their customers) their immovable property to the customer and give them the right to enjoy such property during the specified period i.e. during the office/ banking hours and charge rentals. Bank has the right to break-open the locker in case the locker holder defaults in payment of rent. Banks do not assume any liability or responsibility in case of any damage to the contents kept in the locker. Banks do not insure the contents kept in the lockers by customers.

4. Agent and Principal: Sec.182 of ‗The Indian Contract Act, 1872' defines ―an agent‖ as a person employed to do any act for another or to represent another in dealings with third persons. The person for whom such act is done or who is so represented is called ―the Principal‖.

Thus an agent is a person, who acts for and on behalf of the principal and under the latter's express or implied authority and the acts done within such authority are binding on his principal and, the principal is liable to the party for the acts of the agent.

Banks collect cheques, bills, and makes payment to various authorities viz., rent, telephone bills, insurance premium etc., on behalf of customers. . Banks also abides by the standing instructions given by its customers. In all such cases bank acts as an agent of its

customer, and charges for these services. As per Indian contract Act agent is entitled to charges. No charges are levied in collection of local cheques through clearing house. Charges are levied in only when the cheque is returned in the clearinghouse.

5. As a Guarantor: Banks give guarantee on behalf of their customers and enter in to their shoes. Guarantee is a contingent contract. As per sec 31,of Indian contract Act guarantee is a " contingent contract ". Contingent contract is a contract to do or not to do something, if some event, collateral to such contract, does or does not happen.
It would thus be observed that banker customer relationship is transactional relationship

RIGHTS OF THE BANKER

The rights of a banker that the banker can enjoy are as follows

1. Rights of general lien

One of the important rights of banker is the right of general lien. Lien means the right of the creditor to retain the goods or securities own by debtor until the debt due from him is repaid. There are some exceptional cases in which the right of general lien is not applicable.
These are:

- Safe custody deposit.
- Documents deposited for special purpose.
- Security held in trust.

2. Right of the set off

A banker possess the right of set off which enables him to combine two accounts in the name of same customer and to adjust the debit balance in one account with the credit balance in the other. The right of set off can be exercised subject to the fulfillment of the following conditions:

- The accounts must be in the same name in the same right.
- The right can be exercised in respects of debts due only not in respects of future debts or contingent debts.
- The amount of debts must be certain.
- The banker may exercise that right at his discretion.

3. Banker's right of appropriation

If the customer has more than one account or he has taken more than one loan from the banker, the banker has the right to appropriation these loans by the accounts.

4. Right to charge interest, incidental charges

As a creditor, a banker has the implied right to charge interest on the loans granted to the customer.

In the same way incidental charges like service charges, processing fees, appraisal charges, panel charges may be imposed by the banker to the customer.

Deposit are repayable on term and made by the customer but the period of limitation for the refund of bank deposit is three years with affect from the date a customer made a demand for his money.

CHEQUE-MEANING:-

A written order of a depositor upon a bank to pay the designated party or the bearer a specified sum of money on demand. The person who draws the cheque is called drawer and the person whom the payment is made called payee. The bank will be called the drawee.

ESSENTIONALS FOR A VALID CHEQUE

The following are essential requirements for a valid cheque

Printed versions:

- Name of the bank and branch
- IFSC code of the bank branch
- Cheque number
- MICR code
- Account category

Written versions:

- Date of the cheque - the validity period of the cheque is three months and it should not be a stale cheque or post dated cheque - to be written by the drawer
- Name of the payee - to be written by the drawer
- Amount in words - to be written by the drawer
- Amount in figures - to be written - The amount mentioned in figures and words should be identical and in case of any difference, only the amount mentioned in words will be taken into account and the cheque need not be returned - to be written by the drawer
- Signature of the drawer - should match with the signature as recorded in the system
- Out of the following five items namely - date of the cheque, amount mentioned in words. amount in figures, name of the payee and signature of the drawer; the absence of anyone or more of the items will make the cheque as invalid

Origin of Crossing

Crossing first originated in England when cheques were sent from one bank another. There was the possibility that a cheque might fall in the hands of wrong or unauthorized parties and thereby the original holder was likely to be put to a loss or inconvenience. Crossing also ensures safety in case of a clerk carrying check to the clearing house was assaulted and robbed. To avoid this disadvantage, the bankers introduced new system of crossing of

cheque. Crossing automatically means that a cheque should be presented for payment through bank.

MEANING AND OBJECT OF CROSSING OF CHEQUE

Cross of cheque means drawing two parallel transverse lines on the left hand top corner of a cheque. Crossing on cheque is a direction to a paying banker by drawer that payment should not be made across the counter. The payment on a crossed cheque can be collected only a through a banker. Therefore crossing product the holder of the cheque and reduced the possibilities of fraud.

Advantages of crossing

- If payment is made by means of crossed cheque receipt need not be obtain
- Account payee crossed cheque makes sure that only a particular person to whom the cheque or drawn can receive payment
- If crossed cheque is lost the finder of the cheque cannot en cash it without a help of a banker
- Payments made through cheque particularly crossed cheque enable and automating record of the amount in passbook.

Impact of crossing

Crossing serves the purpose of direction to the bank only or to a particular bank as a case may. Crossing may be written, stamped or printed. Whenever two parallel transverse lines appear on the cheque bank, will not make payment to its holder at the counter of bank.

The payment of a crossed cheque can only be obtained through the bank of the holder. Thus crossing affords security and production to the true owner of the cheque. The object

of crossing is to secure payment to a banking order to easily trace for whose benefit the money was received. Crossing is done to avoid losses arising from open cheque falling into the hands of wrong person however crossing of a cheque thus not affect its negotiability crossed cheque is negotiable by mere delivery if it is payable to bearer and by endorsement and delivery case it is payable to order but were the words no negotiable are added to the crossing the cheque is not negotiable though transferable.

Types of crossing

1. General crossing

Where a cheque bears across its face and addition of the words‖ and company‖ or any abbreviation thereof (&co) between to parallel transverse lines or two simple parallel transverse lines with or without words ―Not Negotiable,‖ it is known to be crossed generally. The paying banker shall make payment only to banker in case of a generally crossed cheque.

2. Special crossing

Where a cheque bears across its faces an addition of the name of a bank with or without the words ‗Not negotiable‖, the cheque is said to be crossed specially. The paying banker shall make payment, on such a cheque, only to the banker whose name is written on the face of a specially crossed cheque.

3. Restrictive crossing:

Where a cheque bears across its face such words ‗Account payee‖ or ‗A/C payee only‖ along with general or special crossing it is known as restrictive crossing or account payee crossing (account payee cheque). The addition of these words to the crossing restricts the transferability of the cheque. The payee, in such cheque, should obtain payment through his own account in the bank.

4. Not negotiable crossing:

Where a cheque bears across its face the words ―Not Negotiable‖ in addition to a general or special crossing, it is known as ―Not Negotiable‖ in addition to general or special crossing, it is known as ―Not Negotiable crossing.‖ A cheque with such words loses its characteristic of negotiability. The transferee of such cheque gets no better title than that of his transferor or previous holder. A person in possession of a negotiable instrument is permitted to alter it in certain respects without the consent of the drawer or the drawee (acceptor). In the same following respects without the consent of the drawer or of the banker on whom it is drawn:

a) If is a bearer cheque, he can convert it into an order cheque
b) If the cheque is uncrossed, he can cross it.
c) If the cheque is crossed generally, he can convert the crossing into a special crossing by adding the name of the banker to whom alone it can be paid.
d) He can add restrictive words on the cheque, such as, ―not negotiable or ―account payee only.

A banker in possession of a cheque which has been given to him by his customer for collection can also convert a general crossing into a special crossing.

Stale cheque:

If a cheque is not presented for payment within a reasonable time, it becomes stale or out-of-date cheque. What is a reasonable time depends upon the arrangement between the various banks and the customers; in India, the reasonable period is six months. No payment is made on stale cheque without getting it confirmed by the drawer.

Mutilated cheque:

Mutilated cheques are those cheques which have been damaged or mutilated in course of

circulation. Such cheques are not honoured by the bankers, in general, for payment.

Marked cheques:

In some countries (other than India) there is a practice that the cheques are marked or certified by the drawee bankers indicating that on the date of presentation, the banker had sufficient funds for payment of the cheque.

DEFINITION OF 'BANK ENDORSEMENT'

An endorsement by a bank for a negotiable instrument, such as a banker's acceptance or time draft, that assures the counterparty that the bank will stand behind the obligations of the creator of the instrument

SEVEN IMPORTANT KINDS OF ENDORSEMENTS

1. Blank or genera endorsement:

If the endorser signs his name only and does not specify the name of the endorsee, the endorsement is said to be in blank Sec. 16(1). The effect of a blank endorsement is to convert the order instrument into bearer instrument (Sec. 54), which may be transferred merely by delivery.

2. Endorsement in full or special endorsement:

If the endorser, in addition to his signature, also adds a direction to pay the amount mentioned in the instrument to, or to the order of, a specified person the endorsement is said to be in full [Sec. 16(1)].

If, for example, A, the holder of a bill of exchange, wants to make an endorsement in full to B, he would write thus: ―Pay to B or order, SdA4.‖ After such an endorsement it is only the endorsee, i.e., B, who is entitled to receive the payment of the instrument and to further negotiate the instrument by his endorsement.

A blank endorsement can easily be converted into an endorsement in full, According to Section 49, the holder of a negotiable instrument endorsed in blank may, without signing his own name, by writing above the endorser‘s signature a direction to pay to any other person as endorsee, convert the endorsement in blank into an endorsement in full; and since such holder does not sign himself on the instrument he does not thereby incur the responsibility of an endorser.

3. Partial Endorsement:

Section 56 provides that a negotiable instrument cannot be endorsed for a part of the amount appearing to be due on the instrument. In other words, a partial endorsement which transfers the rights to receive only a part payment of the amount due on the instrument is invalid.

Such an endorsement has been declared invalid because it would subject the prior parties to plurality of actions (one action by holder for part value and another action by endorsee for

part value) and will thus cause inconvenience to them.

Moreover, it would also interfere with the free circulation of negotiable instruments. It may be noted that an endorsement which purports to transfer the instrument to two or more endorses separately, and not jointly is also treated as partial endorsement and hence would beinvalid.

Section 56, however, further provides that where an instrument has been paid in part, a note to that effect ma; be endorsed on the instrument and it may then be negotiated for the balance. Thus, if in the above illustration the acceptor has already paid Rs 1,000 to A, the holder of the bill, A can then make an endorsement saying ―Pay B or order‖ Rs 1,000 being the unpaid residue of the bill. Such an endorsement would be valid.

4. Restrictive endorsement:

Stating the effect of endorsement, Section 50 provides that ―the endorsement of negotiable instrument followed by delivery transfers to the endorsee the property herein with the right of further negotiation.‖ However, Section 50 permits restrictive endorsement.

An endorsement which, by express words, prohibits the endorsee from further negotiating the instrument or restricts the endorsee to deal with his instrument as directed by the endorser is called ‗restrictive' endorsement.

The endorsee under a restrictive endorsement gets all the rights of an endorser except the right of further negotiation. In other words, such an endorsement entitles the endorsee to receive the payment on due date and sue the parties for it but he cannot further negotiate the instrument.

5. Conditional endorsement:

If the endorser of a negotiable instrument, by express words in the endorsement, makes his liability, dependent on the happening of a specified event, although such event may never happen, such endorsement is called a ‗conditional' endorsement (Sec. 52).

The law permits a conditional endorsement and therefore it does not in any way affect the negotiability of the instrument. Thus, endorsements can validly be made in the following terms:

(i) ―Pay B or order on his marriage ;‖(ii) ―Pay B on the arrival of Pearless ship at Bombay.

In the case of a conditional endorsement the liability of the endorser would arise only upon the happening of the event specified. But the endorsee can sue other prior parties, e.g., the maker, acceptor, etc., if the instrument is not duly met at maturity, even though the specified event did not happen.

6. Sans recourse endorsement (Sec. 52):

When the endorser expressly excludes his own liability on the negotiable instrument to the endorsee or any subsequent holder in case of dishonour of the instrument the endorsement is known as ‗sans recourse' endorsement. Such an endorsement is generally made by addingthe words ‗sans recourse' or ‗without recourse.' Thus, ―Pay X or order sans recourse‖ or
―Pay X without recourse to me‖ or ―Pay X or order at his own risk‖ is examples of this type of endorsement.

7. Facultative endorsement:

When the endorser expressly gives up some of his rights under the negotiable instrument, theendorsement is called a ‗facultative' endorsement. Thus, ―Pay X or order, notice of dishonour waived‖ is a facultative endorsement. As a result of such an endorsement the endorsee is relieved of his duty to give notice of dishonour to the endorser and the latter remains liable to the endorsee for the non-payment of the instrument, even though no notice of dishonour has been given to him.

MATERIAL ALTERATION

The term material alteration indicates alteration or change in the material parts of the instrument. It may be defined as any change, which alters the very nature of the instrument. Thus, it is the alteration, which changes and destroys the legal identity of the original instrument and causes it to speak a different language in legal effect from that which it originally spoke. A material alteration makes the instrument void, i.e., inoperative and affects the rights and obligations of the parties to the instrument. It, however, does not affect one who becomes a partyto an instrument subsequent to its material alteration, if any.

STATUTORY PROTECTION TO PAYING BANKER

1. Protection in case of order cheque:

In case of an order cheque, Section -85(1) provides statutory protection to the paying banker as follows: **"Where a cheque payable to order purports to be endorsed by**

or on behalf

of the payee, the drawee is discharged by payment in due course". However, two conditions must be fulfilled to avail of such protection.

(a) **Endorsement must be regular:** To avail of the statutory protection, the banker mustconfirm that the endorsement is regular.

(b) **Payment must be made in Due Course:** The paying banker must make payment in duecourse. If not, the paying banker will be deprived of statutory protection.

2. Protection in case of Bearer Cheque:

Section -85(2) provides protection to the paying banker in respect of bearer cheques as follows: **"Where a cheque is originally expressed to be payable to bearer, the drawee is discharged by payment in due course to the bearer thereof, notwithstanding any endorsement whether in full or blank appearing thereon and notwithstanding that any such endorsement purports to restrict or exclude further negotiation".** This section implies that a cheque originally issued as a bearer cheque remains always bearer. In other words it retains its bearer character irrespective of whether it bears endorsement in full or in blank or whether any endorsement restricts further negotiation or not. So the banks are not required to verify the regularity of the endorsement on bearer cheque, even if the instrument bears endorsement in full. The banker shall free from any liability (discharged) if he makes payment of an uncrossed bearer cheque to the bearer in due course. If such cheque is a stolenone and the banker makes its payment without the knowledge of such theft, he will be discharged of his obligation and will be protected under Section -85(2).

3. Protection in case of Crossed cheque:

The paying banker has to make payment of the crossed cheques as per the instruction of the drawer reflected through the crossing. If it is done, he is protected by Section -128. This section states **"Where the banker on whom a crossed cheque is drawn has paid the samein due course, the banker paying the cheque and (in case such cheque**

has come to the

hands of the payee) the drawer thereof shall respectively be entitled to the same rights, and be placed in if the amount of the cheque had been paid to and received by the true owner thereof".

It is clear that the banker who makes payment of a crossed cheque is by the Section -128 given protection if he fulfils two requirements (a) That he has made payment in deuce courseunder Section -10 i.e. in good faith and without negligence and according to the apparent tenor of the cheque, and (b)That the payment has been made in accordance with the requirement of crossing (Section -126), i.e. through any banker in case of general crossing and through the specified banker in case of special crossing.

Thus, the paying banker is free from any liability on a crossed cheque even if the payment was received by the collecting banker on behalf of a person who was not a true owner. For example, a cheque in favour of X is stolen by Y. He endorses it in his own favour by forging the signature of X and deposits it in his bank for collection. In this case, the paying banker shall be discharged if he makes payment as mentioned above and shall not be liable to pay the same to X, the true owner of the cheque.

The drawer of the cheque is also discharged since protection is also granted to him under thisSection. There is, however, one limitation to the protection granted under this Section. If the banker cannot avail of the protection granted by other Section of the Act, the protection under Section -128 shall not be available to him.

For example, if the paying banker makes payment of a cheque crossed with (a) Irregular endorsement or (b) A material alteration or (c) Forged signature of the drawer, he loses statutory protection granted to him under the Act for these lapses on his part. Hence he cannot avail of the statutory protection under Section -1289, even if he pays the cheque in accordance with the crossing.

STATUTORY PROTECTION TO COLLECTING BANKER

Section 131 of the Negotiable Instruments Act provides protection to a collecting

banker who receives payment of a crossed cheque or draft on behalf of his customers. According to Section 131 of the Act –a banker who has, in good faith and without negligence, received payment for a customer of a cheque crossed generally or specially to himself shall not, incase the title to the cheque proves defective, incur any liability to the true owner of the cheque by reason only of having received such payment.

The protection provided by Section 131 is not absolute but qualified. A collecting banker canclaim protection against conversion if the following conditions are fulfilled.

1. Good Faith and Without Negligence:

Statutory protection is available to a collecting banker when he receives payment in good faith and without negligence.

The phrase in –good faith means honestly and without notice or interest of deceit or fraud and does necessarily require carefulness. Negligence means failure to exercise reasonable care. It is not for the customer or the true owner to prove negligence on the part of the banker. The burden of proving that he collected in good faith and without negligence is on the banker. The banker should have exercised reasonable care and diligence. What constitutes negligence depends upon facts of each case.

Following are a few examples which constitute negligence:

(a) Failure to obtain reference for a new customer at the time of opening the account.

(b) Collection of cheques payable to trust accounts' for crediting to personal accounts of atrustee.

(c) Collecting for the private accounts of partners, cheques payable to the partnership firms.

(d) Omission to verify the correctness of endorsements on cheques payable to order.

(e) Failure to pay attention to the crossing particularly the —not negotiable crossing.

2. Collection for a Customer:

Statutory protection is available to a collecting banker if he collects on behalf of his customer only. If he collects for a stranger or noncustomer, he does not get such protection. As Jones aptly puts if –duly crossed cheques are only protected in their

collection, if handled for the customer‖. A bank cannot get protection when he collects a cheque as holder for value. In Great Western Railway Vs London and Country Bank it was held that ―the bank is entitled for protection as it received collection for an employee of the customer and not for the customer.‖

3. **Acts as an Agent:** A collecting banker must act as an agent of the customer in order to getprotection. He must receive the payment as an agent of the customer and not as a holder under independent title. The banker as a holder for value is not competent to claim protectionfrom liability in conversion. In case of forgery, the holder for value is liable to the true ownerof the cheque.

4. Crossed Cheques:

Statutory protection is available only in case of crossed cheques. It is not available in case uncrossed or open cheques because there is no need to collect them through a banker. Cheques, therefore, must be crossed prior to their presentment to the collecting banker for clearance. In other words, the crossing must have been made before it reached the hands of the banker for collection. If the cheque is crossed after it is received by the banker, protection is not available. Even drafts are covered by this protection.

UNIT II

Indigenous Banking System in India

Indigenous banking system is the system of banking that involves private firms or individuals who act as banks by providing financial services such as loans and accepting deposits. Indigenous banking system is made up of indigenous bankers who do not fall under the purview of the government. The system of indigenous banking dates back to the medieval period. This system continued till the middle part of the nineteenth century. Indigenous bankers formed the bulk of the Indian financial system in the ancient times. These bankers provided credit facilities to the individuals and businesses as well as to the governments at times. The indigenous banking system lost its charm with the advent of foreign banks and commercial banks. The business contracted further with the formation of co-operative banks and commercial banks in the late 1950s.

Functions of Indigenous Bankers

The indigenous bankers performed the following functions:

1. Accepting deposits from the public: It is one of the important functions of the bankers.

The deposits will be for a fixed period and can be of either fixed or current period.

2.Providing loans against security: Indigenous bankers provide loans against securities or assets such as land, vehicles, gold ornaments, etc.

3. Discounting Hundis: Hundis were important instruments of money exchange for the businesses in times before new instruments were introduced. Discounting Hundis is one of the most profitable businesses for the indigenous bankers.

Hundis are of two types 1) Darshni or Sight hundi, a hundi that is payable on demand and 2) Muddati Hundi, a hundi that is payable after a certain time period. The time period after which it becomes payable is mentioned at the face of the hundi.

4. Remittance: Indigenous bankers also provide remittance services by having separate branches or tie ups with other indigenous bankers across the country.

Commercial Bank

A commercial bank is a kind of financial institution that carries all the operations related to deposit and withdrawal of money for the general public, providing loans for investment, and other such activities. These banks are profit-making institutions and do business only to make a profit.The two primary characteristics of a commercial bank are lending and borrowing. The bank receives the deposits and gives money to various projects to earn interest (profit). The rate of interest that a bank offers to the depositors is known as the borrowing rate, while the rate at which a bank lends money is known as the lending rate.

Function of Commercial Bank:

The functions of commercial banks are classified into two main divisions.

(a) Primary functions

Accepts deposit : The bank takes deposits in the form of saving, current, and fixed deposits. The surplus balances collected from the firm and individuals are lent to the temporary requirements of the commercial transactions.

Provides loan and advances : Another critical function of this bank is to offer loans and advances to the entrepreneurs and business people, and collect interest. For every bank, it is the primary source of making profits. In this process, a bank retains a small number of deposits as a reserve and offers (lends) the remaining amount to the borrowers in demand loans, overdraft, cash credit, short-run loans, and more such banks.

Credit cash: When a customer is provided with credit or loan, they are not provided with liquid cash. First, a bank account is opened for the customer and then the money is transferred to the account. This process allows the bank to create money.

(b) Secondary functions

Discounting bills of exchange: It is a written agreement acknowledging the amount of money to be paid against the goods purchased at a given point of time in the future. The amount can also be cleared before the quoted time through a discounting method of a commercial bank.

Overdraft facility: It is an advance given to a customer by keeping the current account to overdraw up to the given limit.

Purchasing and selling of the securities: The bank offers you with the facility of selling and buying the securities.

Locker facilities: A bank provides locker facilities to the customers to keep their valuables or documents safely. The banks charge a minimum of an annual fee for this service.

Paying and gathering the credit : It uses different instruments like a promissory note, cheques, and bill of exchange.

Types of Commercial Banks:

There are three different types of commercial banks.

Private bank –: It is a type of commercial banks where private individuals and businesses own a majority of the share capital. All private banks are recorded as companies with limited liability. Such as Housing Development Finance Corporation (HDFC) Bank, Industrial Credit and Investment Corporation of India (ICICI) Bank, Yes Bank, and more such banks.

Public bank –: It is a type of bank that is nationalized, and the government holds a significant stake. For example, Bank of Baroda, State Bank of India (SBI), Dena Bank, Corporation Bank, and Punjab National Bank.

Foreign bank –: These banks are established in foreign countries and have branches in other countries. For instance, American Express Bank, Hong Kong and Shanghai Banking Corporation (HSBC), Standard & Chartered Bank, Citibank, and more such banks.

Cooperative bank

A Cooperative bank is a financial entity that is owned and operated by its members, who are both the owners and customers of the bank. In India, cooperative banks are governed by the States Cooperative Societies Act. The Reserve Bank of India (RBI) also

regulates cooperative banks, which are governed by the Banking Regulations Act 1949 and the Banking Laws (Co-operative Societies) Act, 1955.

A cooperative bank is a financial entity that is owned and operated by its members, who are also its customers.

Co-operative banks are frequently formed by people who belong to the same local or professional community or who share a common interest.

Co-operative banks typically offer a wide range of banking and financial services to their members (loans, deposits, banking accounts, etc).

They offer a limited range of banking services and specialize in agricultural products.

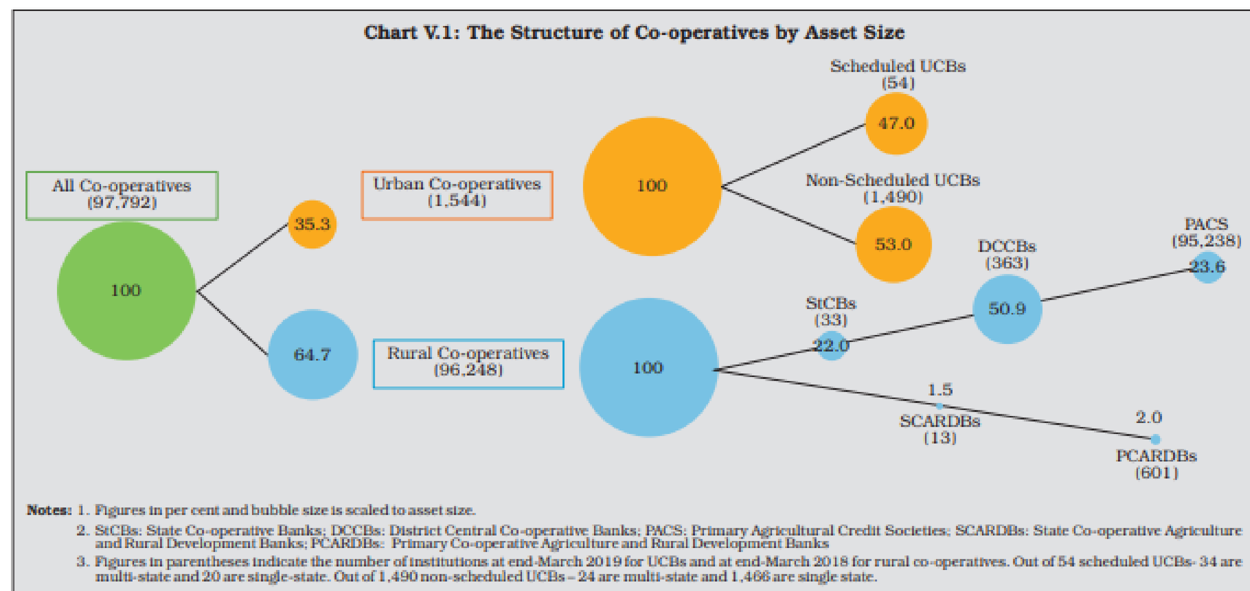
Cooperative banks are the primary financiers of agricultural activities, small-scale industries, and self-employment.

Cooperative banks operate on the principle of "no profit, no loss."

Anyonya Co-operative Bank Limited (ACBL) is India's first co-operative bank, headquartered in Vadodara,Gujarat.

Structure of Co-operative Banks

The structure of a Co-operative Bank is given in the image below:



The image below is as per the annual report released by the Reserve Bank of India in March 2019. Of the total number of Cooperative Banks in India, they can be divided into two types, which can further be subdivided:

- Urban Co-operative Banks
  - Non-Scheduled UCBs
  - Scheduled UCBs
- Rural Co-operative Banks
  - State Cooperative Banks
  - District Central Cooperative Banks
  - Primary Agricultural Credit Societies

Single-state UCBs are regulated by State Registrars of Co-operative Societies (RCS) and multi-state UCBs are governed by Central Registrar of Co-operative Societies (CRCS).

To know the important responsibilities that the Indian Banking sector possesses, visit the Functions of Banks page.

History of Co-operative Banks

The introduction of Co-operative Banks in India dates back to the early 20th century, which was a time of distress for the Indian society.

A timeline as to how the co-operative banking emerged in India has been given below:

- The Cooperative Credit Societies Act, 1904, was the first step taken for the co-operative society, which got accelerated with the introduction of the Cooperative Societies Act of 1912
- In post-independent India, Central Committee for Cooperative Training (1953) was set up by RBI for establishing co-operative training centres
- To solve the issue of the financial crisis in the rural areas, Rural Credit Survey Committee was set up 1954
- This co-operative movement spread through the banking sector as well and by 1950s, Co-operative Banks had started extending their reach to the public in both rural and urban areas

Advantages of Co-operative Banks

The Co-operative banks have acted as a boon to various sectors of Indian society and also played an important role in the development of the economy.

Given below are a few advantages of the Co-operative Banks in India:

- These banks have provided aid to the rural population by granting loans and credits with interest rates, lower in comparison to that asked by local money lenders
- They have their reach at every corner of the country and have managed to maintain a personal rapport with the customers
- Since the bank is owned and governed by the members themselves, they do not seek huge profits and believe in mutual help
- The interest rate on deposits is high and on loans is low
- They promote productive borrowing, in order to reduce the risk of loss
- Co-operative Banks have helped the farmers by providing them agricultural credits to buy basic products like fertilizer, seeds, etc.

Disadvantages of Co-operative Banks

Discussed below are a few disadvantages of the Co-operative Banks in India:

- To lend money, they need investors which are tough to find
- Over the years, the number of NPAs and over dues have been increasing
- Since the lack of investors and money, few of them have not been delivering the credits and money to the rural population
- Rather than small industrialists, the benefits from Co-operative Banks have been enjoyed by rich landowners
- The Co-operative Banks across the country are not equally developed. A few states have more functioning and beneficial units, while some states have faced loss
- Political interference has also been observed in these banks
- With new types of banks opening up, the Co-operative Banks are facing the risk of losing their customers

To overcome this loss, the RBI must take up steps regarding audit facilities and implementation of strict rules must be followed.

Industrial Development Bank of India (IDBI)

Prior to 1964, there was not any apex organization to coordinate the functions of various financial institutions. Then V. V. Bhatt rightly pointed out that the country needed a central development banking institution for providing "dynamic leadership in the task of promoting a widely diffused and diversified and yet viable process of industrialization."It was to fulfill this objective, the Government of India for the first time on July 1, 1964 established the Industrial Development Bank of India (IDBI) under the Act of Parliament as an apex and principal financial institution to coordinate the financial functions of various financial; institutions in the country.Initially, it was set up as wholly-owned subsidiary of the Reserve Bank of India. In February 1976, the IDBI was made an autonomous institution and its ownership passed on from the Reserve Bank of India to the Government of India. As it is not feasible for the IDBI to reach a large number of small-scale industries scattered all over the country, the flow of its assistance to the vast number of small-scale industries has, therefore, been indirect in the form of refinancing of loans granted by banks and the State Financial Corporations, (SFCs).That the IDBI has shown its particular interest in the development of small-scale industries is demonstrated by the setting up of the Small Industries Development Fund (SIDF) in May 1986, the National Equity Fund Scheme (NEFS) in 1988, and the Voluntary Executive Corporation Cell (VECC) for providing support in the nature of equity to tiny and small-scale industries engaged in manufacturing, cost not exceeding Rs. 5 lakhs.The scheme is administrated by the IDBI through nationalised banks. The IDBI has also introduced the single window assistance scheme for grant of term-loans and working capital assistance to new, tiny and small-scale enterprises. As per data available, IDBI has extended about one-third of total industrial assistance to small-sector alone. In order to make the IDBI's coordinating role more effective, the Narsimham Committee (1991) has suggested that the IDBI should give up its direct financing function and perform only promotional apex and refinancing role in respect of other institutions like SFCs and SIDBI. The direct lending function should be entrusted to a separate finance company especially set up for this purpose.

Functions of Industrial Development Bank of India (IDBI)

The Industrial Development Bank of India (IDBI) was set up in July 1964, as a wholly-owned subsidiary of the Reserve Bank of India. It was given complete autonomy in February 1976.

Today, the IDBI is regarded as an apex institution in the arena of development banking. The IFCI and the UT1 are the subsidiaries of the IDBI. As an apex development bank, the IDBI's major role is to co-ordinate the activities of other development banks and term-financing institutions in the capital market of the country.

The main functions of the IDBI may be stated as follows:

1. Planning, promoting and developing industries with a view to fill the gaps in the industrial structure by conceiving, preparing and floating new projects.

2. Providing technical and administrative assistance for promotion, management and expansion of industry.

3.Providing refinancing facilities to the IFCI, SFCs and other financial institutions approved by the government.

4. Coordinating the activities of financial institutions for the promotion and development of industries.

5. Purchasing or underwriting shares and debentures of industrial concerns.

6. Guaranteeing deferred payments due from industrial concerns and for loans raised by them.

7. Undertaking market and investment research, surveys and techno-economic studies helpful to the development of industries.

In short, the IDBI is the leader, coordinator and innovator in the field of industrial financing in our country. Its major activity is confined to financing, developmental, co-ordination and promotional functions.

With the passing of the IDBI (Amendment) Act, 1986, the IDBI has been empowered to provide assistance to diverse range of industrial activities including the activities of services sector of industries like informatics, health care, storage and distribution of energy and other services contributing to value addition. The scope of business of the IDBI has also been extended to cover consulting, merchant banking and trusteeship activities.

Under the 1986 Amendment, the authorised capital of the IDBI has been raised to Rs. 1,000 crores (with the possibility of further increasing it to Rs. 2,000 crores by the Central Government's notification) for sustaining the growing tempo of its operations.

NABARD

As we all know, the development in the rural areas has always been a lot slower than the urban areas, given the lack of resources and the lack of proper institutions. In an effort to improve the financial operations, promote sustainable agriculture, and enhance rural development, the government of India established NABARD. To understand the concept behind NABARD and to know about its roles and functions, let's go through it in a little more detail.

Meaning

National Bank for Agriculture and Rural Development or NABARD is the main regulatory body in the country's rural banking system and is considered as the peak development finance institution which is established and owned by the government of India. This bank aims to provide and regulate credit to the rural areas, which will be a first step towards enhancing the rural development in the country.

NABARD has been given many responsibilities related to the formulation of policies, planning, and operations in agriculture and financial development. NABARD carries these responsibilities efficiently and works towards promoting and developing man industries in the rural areas like the agriculture industry, cottage industries, other small scale industries, and rural crafts in an effort to create better infrastructure and better employment opportunities for the people living in these regions.

The Government of India established this bank considering all the guidelines of the National Bank for Agriculture and Development Act of 1981. To put it in simple terms, you can say that the National Bank for Agriculture and Rural Development or NABARD is the main and specific bank of the country for agriculture and rural development.

role of NABARD

Being the main regulatory body for agriculture and rural development, the National Bank for agriculture and rural development or NABARD has many important roles to play. These roles are as follows:

- The National Bank for Agriculture and Rural Development or NABARD provides investment and production credit for various developmental activities and projects taking place in rural areas, which will help enhance rural development and facilitate rural prosperity. As this bank is the center or the main financing agency for all such developmental projects, the responsibility falls on the bank to ensure that the projects receive the proper financing and promotion.
- The responsibility of coordinating all the financing activities in the rural areas with all institutions involved in the developmental projects falls on the NABARD. It has to stay in touch with all major institutions, including the Indian government, Reserve Bank of India or RBI, state governments, or any other major institutions that may be a part of the ongoing agriculture or rural development activities.
- NABARD takes action towards monitoring, formulating strategies for the rehabilitation schemes, restructuring credit institutions and training personnel, etc., through making an improvement in the credit delivery system's absorptive capacity and building a strong institution with an aim to achieve the same.
- The National Bank refinances all the financial institutions that finance the rural development projects for Agriculture and Rural Development or NABARD as it is the specific bank for looking after all agriculture and rural developments in the country.
- After the bank has refinanced a developmental project or activity taking place in the rural region, the responsibility of monitoring and evaluating the project or activity also falls on the NABARD.

- NABARD keeps all the client institutions in check and provides training facilities to all the institutions that are working towards rural upliftment or want to work for rural development in the future.
- Along with all the above roles, the National Bank for Agriculture and Rural Development also keeps the portfolio of the Natural Resource Management Programmes.
- NABARD also helps Self-Help Groups or SHGs through its SHG bank linkage programme that will boost the activities of SHGs in the rural areas and will be a helpful step in the rural development.

FUNCTIONS OF NABARD

Now that we have seen what NABARD stands for and the roles that it has to perform, let us go through the functions performed by the bank. In an effort to keep up with its roles, the National Bank for Agriculture and Rural Development undergoes four central functions. These four central functions performed by the NABARD are—credit functions, financial functions, supervisory functions, and development functions. To understand all these four functions performed by the NABARD, let’s go through all of them one by one.

1. Credit functions As the main provider of credit facilities in rural areas, the National Bank for Agriculture and Rural Development or NABARD performs the credit functions. Under these functions, the bank provides, regulates, and monitors the credit flow in the rural parts of the nation.
2. Financial functions NABARD has many client banks and institutions that help and assist in the developmental activities in rural areas. By performing the financial functions, the National Bank for Agriculture and Rural Development or NABARD provides loans to these client banks and institutions like handicraft industries, food parks, processing units, artisans and many more.
3. Supervisory functions As already discussed above, NABARD is the apex institution that looks after agriculture and rural development. This is why the responsibility of monitoring and regulating all the development activities and projects fall on this institution. Given this role, the NABARD performs supervisory functions in which it has to keep a check on all the client banks, institutions, credits and non-credits societies that are a part of the developmental tasks taking place in the rural areas.

4. Development Functions As you must be pretty much aware by now that the primary role of the National Bank for Agriculture and Rural Development or NABARD is to focus on developing sustainable agriculture and promote rural development, the bank performs development functions in an effort to stay true to this role. Under developmental functions, the NABARD helps rural banks prepare action plans for the developmental activities.

The National Bank for Agriculture or Rural Development or NABARD performs all the above roles and functions efficiently and has a great impact on the agricultural progress and rural development in the country.

EXIM BANK

EXIM Bank is popularly regarded as an 'Export-Import Bank'. It was established in the year 1982 under the Indian act of Export-Import Bank of India Act,1982 and has been set up to provide long-term finance to exporters as well as importers to meet their financial needs related to international trade of the country India. It is the biggest and the salient institution which is based on finance of export for the investment and trade of foreign countries with the country's economic growth. The 1st Chairman of the bank was R.C. Shah and who was also the first Managing director. Exim Bank lengthens the LOCs (Lines of Credit) to banks of regional development, financial overseas institutions, sovereign government and many more institutions for import and export of goods, services, trade, infrastructural equipment etc. from and to the country India.

The Indian Government owned the EXIM Bank and was regulated by the Reserve Bank of India. This bank is owned by the government of India. David Rasquinha is the recent Managing Director of EXIM Bank with Mumbai (Maharashtra) as it's headquarter. The Indian Government decided to launch Rs. 1,500 crore capital in next year (financial year) in the EXIM Bank. Rs. 1,300 crore capital has been infused by the Indian government for this bank which supports various new initiatives such as textile industry of India, schemes of concessional finance alteration etc.

The important functions of the EXIM Bank are as follows:

1. Financing of export and import of goods and services both of India and of outside India.

2. Providing finance for joint ventures in foreign countries.

3. Undertaking merchant banking functions of companies engaged in foreign trade.

4. Providing technical and administrative assistance to the parties engaged in export and import business.

5. Offering buyers' credit and lines of credit to the foreign governments and banks.

6. Providing advance information and business advisory services to Indian exports in respect of multilaterally funded projects overseas.

During the year 1994-95, the EXIM Bank introduced the 'Clusters of Excellence' programme for up-gradation of quality standards and obtaining ISO 9000 certification in various parts of the country.The Bank also entered into framework cooperation agreement with European Bank for Reconstruction and Development (EBRD) for acquiring advance information on EBRD funded projects in order to enter into co-financing proposals with EBRD in Eastern Europe and CIS.

EXIM Bank Functions

The bank's functions can be grouped under products and services. They are discussed briefly below:

Financial Products

- Buyer's credit – it is a credit facility program that encourages Indian exporters to explore new regions across the globe. It also facilitates exports for SMEs by offering credit to overseas buyers to import goods from India.
- Corporate banking – it offers a variety of financing programs to augment the export-competitiveness of Indian companies.
- Lines of credit – it offers extended a line of credit to Indian exporters to help them expand to new geographies and uses a line of credit as an effective market-entry tool.
- Overseas investment finance – it offers term loans to Indian companies for equity investments in their overseas joint ventures or wholly-owned subsidiaries.

- Project exports – encourages project exports from India and helps Indian companies secure contracts abroad.

Services

- Marketing advisory services – help Indian exporters in their globalization ventures by assisting in locating overseas distributors/partners, etc. Also, assists in identifying opportunities abroad for setting up plant projects or acquiring companies.
- Research and analysis – conducts research in the field of international economics, trade and investment, country profiles to identify risks, etc.
- Export advisory services – it offers information, advisory, and support services enabling exporters to evaluate international risks, exploit export opportunities and improve competitiveness.

UNIT – III

Traditional Banking

Banking has, for a very long time, been an old-fashioned industry. This is logical, seeing as banks have been around for hundreds of years at this point. Traditional banking refers to banks with a physical presence with a domestic banking license. These are the commonly known banks, such as ING, Bank of America, and Banco Santander to name a few. A traditional bank typically has:

- Physical presence;
- Regional headquarters in each country where they are active;
- Own-branded ATMs;
- Large number of employees;
- Face-to-face or one-to-one customer service;
- Dedicated account managers.

Although traditional banking solutions do generally provide online possibilities, this is mostly considered a by-product of the bank's services, whereas an online bank is completely focused on its user interface for its online banking platform.

Traditional banking has certain benefits and certain disadvantages.

Benefits:

- Being able to walk into a local branch and speak to a real person;
- Generally considered safe;
- Positive impact on the perspective of clients and suppliers (increase trustworthiness);
- Personalized service;
- Easier to handle cash payments and withdrawals;
- More financial products available.

Disadvantages:

- Lower accessibility (more strict KYC/AML requirements). Some traditional banks are risk-averse;

- Inability to do business with some countries;
- Potentially outdated online banking;
- Longer time needed to open accounts;
- Banking must take place during business hours;
- Potentially higher monthly fees;
- Clients have to deal with a lot of bureaucracy.

It should be said that traditional banks have ramped up their virtual operations in current times. Banking, in general, will probably be completely digital in the next 10 years. This means that getting a traditional bank account now may result in a completely online banking solution from a reputable, top global bank in the long term. This makes it attractive to open a traditional bank account in 2022.If you prefer a personalized touch to your banking, then traditional banking might be for you. If you are in an industry that requires trust and service from a bank, then a traditional bank account is definitely the better option. Doing Business International can assist in finding the perfect traditional banking solution for your business

KINDS OF DEPOSITS

There are four major types bank deposits which are as follows:

1. Saving deposit: Saving deposit account refers to the type of bank account which is opened by the people in order to save a part of their income. The rate of interest offered in such type of account is very nominal as there is no restriction towards the withdrawal and deposit limit in the account. It is the most suitable account for salaried class people as they can save a part of their monthly income in this type of account.

2. Current deposit: Current deposit account is a type of bank account which is opened by the people in order to do business transaction which is why it is also known as business account. In this type of bank account, withdrawals can be made throughout the tenure of the account without any notice in order to keep the efficient flow of business transactions so that there is no delay in business decisions. The rate of interest earned on such deposits are very nominal and lowest among all other bank deposits as these are solely made for transaction purpose and not savings purpose.

3. Recurring deposit: Recurring deposit account refers to the type of bank account where a fixed sum of money is deposited in the bank in monthly installment regularly for a fixed period of time. Withdrawals are not permitted until the expiry of the fixed period and on the expiry of the fixed

period, the total sum of money deposited in the bank account is paid to the depositor along with the accrued interest. The rate of interest earned in such deposits are higher than the rate of interest earned in saving deposit and current deposit but lower than the rate in fixed deposit.

4. Fixed deposit: Fixed deposit account is a type of account where a fixed sum of money is deposit for a fixed period of time with no withdrawals permitted until the expiry of the fixed period and on the expiry of the fixed period, the total sum of money deposited in the bank account is paid to the depositor along with the accrued interest. The rate of interest is usually high in order to attract such deposits from the people due to which the rate is directly proportional to the sum of money deposited in the bank account.

Principles of Sound Lending

Bank performs different functions. Lending of money to different kinds of borrowers is one of the most important functions of commercial bank. A major portion of its fund is used for this purpose and this is also the major sources of bank's income. However, lending is not without risk. The borrowers of a bank range from individuals to partnership, companies, institutions, societies etc. The nature of their activities, the location of business, financial stability, earning and repaying capacity, purpose of advance, securities all differ and their degree of risks also differ. Therefore, a banker must take proper precaution in this process. Some of the important considerations to be kept in mind by a banker in this respect are discussed below:

Safety: Safety means that the borrower should be able to repay the loan and interest in time at regular intervals without default. Banks are trustee of public money. Bank's deposits are always payable on demand. Bank has to maintain trust of depositor forever. As such the first and foremost principle of lending is to ensure safety of funds lent. Further, it is just not the capacity of the borrower to repay but also his willingness to repay. The former depends on his tangible assets and the success of his business. The latter depends on the borrower's character. Now the question is how to ensure safety of lending? To ensure the safety of lending the following factors may be considered:

Five Cs	Five Ps	Five Ms	Five Rs
Character/conduct	Person	Man	Reliability
Capacity	Purpose	management	Responsibility
Capital	Product	Money	Resources
Condition	Place	Materials	Respectability
Collateral	Profit	Market	Returns

Liquidity: The term liquidity refers to the extent of availability of funds with the banker for providing credit to borrowers. It is to be seen that money lent is not going to be locked up for a long time. The money should return to the bank as per the repayment schedule. This schedule that is drawn up by the banker has to adhere to the requirement that at any point of time the banker should possess liquidity to meet the withdrawals of the depositors. It is to be kept in mind that various deposits have various maturities and some of it would also be payable on demand. A bank's inability to meet the demand of its depositors can lead to a run on the bank which is a threat to its basic survival. Hence the banker has to always monitor the cash flows and carry out the exercise of ensuring liquidity with the borrower as this in turn means liquidity with the banker. Further, liquidity would also refer to the quality of assets, which should be easily convertible into cash without any loss of value. Thus the concept of liquidity entails the bankerto look for easy salability and absence of risk of loss on sale of asset, which has been taken as collateral.

Purpose: The purpose should be productive so that the money not only remain safe but also provides a definite source of repayment. Loans may be required for productive purposes, trading purposes, agriculture, transport, self-employment etc. If a loan is required for a non-productive or speculative purpose, the banker should be very much cautious in entertaining such proposals. It is very difficult to ensure that the loan has been utilized for the purpose for which it was sanctioned. Banker should take follow-up measures to ensure end use of fund exactly for the same purpose for which it is borrowed.

Profitability: Banks are not charitable institutions. All banks are profit-

earning institutions. The ultimate objective of lending is to earn profits. Banks receive interest on loans and advances lent, and they pay interest to their depositors. This difference between the receipts and payments will be the bank's gross profit. Banks further incur various expenses as any organization does. After accounting for all such expenses and provisions, banks have to earn reasonable amount as net profit (NIM) so that dividends can be paid to its shareholders. The trust and confidence level of the customer and investor will be high with a bank that has a good track record of profits and dividend rates. Hence it is important that whatever the business the bank engages itself with, the business be profitable enough not just to cover its costs but to ensure generation of surplus funds or margin. It is prudent for the banker to consider overall profitabilityof the entire business that is undertaken rather than the profitability against each component of business or service offered.

Security: The security offered by a borrower for an advance is as like as the insurance to the banker. It serves as the safety valve for an unforeseen emergency. So another principle of sound lending is the security of lending. Security offered against loan may be various. It may be a plot of land, building, flat, insurance policies; term deposits etc. There may even be cases where there is no security at all. The banker must realize that is it only a cushion to fall back upon in case of need. The security and its adequacy alone should not form the sole consideration for judging the viability of a loan proposal. Nevertheless, the security if accepted must be adequate and readily marketable, easy to handle and free from encumbrance. It is the duty of the banker to check the nature of the security and assess whether it is adequate for the loan granted.

Diversification: A prudent banker always tries to select the borrower very carefully and takes tangible assets as security to safeguard his interests. While this is no doubt an adequate measure, there are other unforeseen contingencies against which the banker has to guard himself. Further if the bank lends large amounts to a single industry or borrower, then the default by that customer can affect the banking industry as a whole and will affect the basic survival of the industry. To safeguard his interest against all such risks, the banker follows the principle of diversification of risks based on the famous maxim 'never keep all the eggs in one basket'. By lending funds to different sectors, a bank can save itself from the slump in some sectors by way of

prosperity in the others. Banks have to lend to a largenumber of industries and borrowers so that the risk gets diversified

National Interest: Even when an advance satisfies all the aforesaid principles, itmay still not be suitable. The advance may run counter to national interest. Bank has a significantrole in the economic development process of a country. They should keep in mind the national development plan/program while going for lending but maintaining safety, liquidity and profitability.

Different Forms Of Bankers Advances

Introduction

Money is a crucial aspect in an individual's life as well as for the business that are run by various companies. It is difficult to function without funds to face the competition in the market. Organizations and companies need funds to procure raw material for production, administrative services, capital, etc. These companies being competitive in nature are frequently investing to facilitate better products and services in comparison to others. On the other hand, individuals on a daily basis also require a supply of funds so as to meet their various requirements and live a hassle-free life. Apparently, neither the companies nor an individual is financially equipped with unlimited funds and thus loans and advances come into play and fill up the deficit in funds.

Different forms of banker's advances

1. Cash Credit

Cash credit is the method of lending money by banks to the customers where in the customers can borrow against the security of tangible assets and guarantees up to certain limit specified by the banker, known as 'cash credit limit'.

This system of cash credit is flexible because it allows the customer to borrow money as and when required according to his needs subject to the limit sanctioned. The arrangement of this system is

permanent in nature so the customer does not have to withdraw the entire amount at once.The bank may renew the limit of the cash credit by the end of the year if it deems the account of the customer to be running satisfactorily. Generally, cash credit is granted to the borrower against the security by way of pledge or hypothecation of tangible securities. This system of cash credit also facilitates funds against personal security.Interest is charged to the customer only on the amount utilized by him and not for the entire amount. A commitment charge can also be imposed by the bank if the customer does not use the cash limit to the foil extent i.e. only the unutilized amount of the cash credit. The borrower can deposit the surplus funds in the banks which might result in reduced interest charge.

2. Overdraft

Overdraft is a facility provided to a current account holder by the bank permitting to withdraw over and above the credit balance in the account. This facility is provided for a shorter period of time. With the overdraft facility, a customer is allowed to withdraw money as and when required provided that the total withdrawn amount does not exceed the agreed limit and the customer can also repay in the form of deposits at any point of time as per his convenience.The interest is charged only on the exact amount withdrawn by the customer from his account and for the period of its actual utilization. A provision of a temporary overdraft facility is also available. Interest charged on temporary overdrafts is imposed as and when the temporary overdraft is adjusted or at the end of the month, whichever is earlier.Overdrafts are generally granted against the security of government securities, shares & debentures, National Savings Certificates, LIC policies, bank's own deposits etc. and also on unsecured basis. However regular overdraft limits are sanctioned against some securities. Some collateral security may be taken by the bank and the bank might also grant advances against personal security of the borrower.The customer has to provide the bank with a written application or promissory note signed by him to avail the overdraft facility. The overdraft facility is usually an agreement of an expressed contract but in the absence of the express contract, overdraft facility can be granted by referring to the course of the business of the borrower. Thus it becomes necessary for the banks to obtain a letter and a promissory note incorporating the terms and conditions as well as the interest chargeable in respect of the overdraft facility.

3. Discounting of Bills

Bill of exchange is an instrument in writing containing of an unconditional order signed by the creditor, directing the debtor to pay a certain sum of money on maturity. Now, under the mechanism of discounting bills, the seller of goods draws a bill of exchange on the buyer as per the terms of the goods supplied.When the buyer does not have enough funds to buy goods then he takes helps from the bank, the bank then releases funds at a discounted rate to the seller before the credit period ends. This bill is then presented to the seller's client i.e. the buyer by the bank and the bank recovers the total amount of the goods from the buyer before the credit period matures.The discount on the bill of exchange depends upon the remaining time to maturity and the amount involved in it. The time period of the credit mostly depends upon the buyer's creditworthiness. When the buyer buys goods from the seller then the payment is to be made through letter of credit.In the mechanism of bill discounting, all the three parties i.e. the seller, buyer and banker have advantages and benefit profits. Firstly the seller gets money in advance for his working capital, secondly, the buyer gets a credit period against the letter of credit and thirdly the bank also earns some revenue.

Example – A is a car manufacturer and needs tyres for the manufacturing of his cars. B is a tyre manufacturer. A has been assigned with a project costing Rs 1 lakh to manufacture cars but A does not have enough funds to buy the tyres for the cars. Thus A goes to the bank for help and the bank pays a discounted rate of Rs 95,000 to B provided that A repays the whole amount to the bank within 3 months. After 3 months as A was in a good financial position, he paid the entire amount to the bank and hence the business ran smoothly.

4. Loan

The loan is the money borrowed from the bank on the condition that it is to be repaid in installments or all at once (lump-sum) on the agreed dates and at an agreed rate of interest. The bank charges interest on the entire amount whether or not the borrower withdraws the money from his account or not.The loan can be obtained with or without security. If the borrower wants loan further too then he has to apply for a fresh loan. Each bank has its own procedure of granting loans and the banks shall have the authority to accept or refuse the loan depending upon its own cash position and lending facility.

Types of loans

I. Demand Loan

Demand loans are the loans which are repayable on demand by the banks. The banks at any point of time can ask the borrower to repay the money with the required interest rate borrowed from the bank. This kind of loan is usually considered short term finance and have no fixed tenures. Demand loans are beneficial for start-up businesses, to fulfill daily and temporary working capital requirements, purchasing raw material and small assets, etc.

ii. Term Loan

Terms loans are medium to long term loans. Term loans are usually granted for longer period of time and have to be repaid within a definite time frame. The repayment tenure of such loans is also longer. In case of business loans, the repayment period of time is usually between 12 months to 60 months. Term loans can be granted on the basis of both fixed and floating rate of interest. When it comes to grant personal loan or home loan then the repayment tenure is 10 years or more depending upon the loan amount and rate of interest.

Conclusion

With the rapid growth and development of the world, the needs and requirements of an individual or companies keep on increasing. To meet such needs, one has to take help to avail funds for their progress. Banks play a vital role in such conditions and thus the world economy is dependent on the banking sector. The different forms of advances provided by the banks have made life easy for the entrepreneurs to start their business and also for the established businessmen who are in constant need of funds for their working capital.

LIEN

Lien means the right to retain the goods of the borrower until the debts are repaid. Lien is the right of a creditor to retain the properties belonging to the debtor until debt due to him is repaid. Lien gives a person only a right to retain the possession of the goods and not the power to sell unless such a right is expressly conferred by statute or by custom or by usage. A banker's lien is a general lien which is tantamount to an implied pledge. It confers upon the banker the right to sell the securities after serving reasonable notice to the borrower

Kinds of Lien

- A particular lien applies to one transaction or certain transactions only.
- General lien gives a right to a person to retain the goods not only in respect of a particular debt but also in respect of the general balance due form the owner of the goods to the person exercising the right of lien. It extends to all transactions.

Negative Lien

In case of negative lien. The possession of the security is with the debtor himself, who promises not to create any charge over them until the loan is repaid.

Banker's Lien

A banker's lien is always a general lien. A banker has a right to exercise both kinds of lien. A banker's lien is treated as an implied pledge: It must be noted that a banker's lien is generally described as an implied pledge. It means that a lien not only gives a right to retain the goods but also gives a right to sell the securities and goods of the customer after giving a reasonable notice to him. When the customer does not take any steps to clear his arrears. This right of sale is normally available only in the case of pledge. That is why lien is regarded as an implied pledge.

PLEDGE

Pledge is the bailment of goods as security for payment of a debt. Only movable goods can be pledged. Section 172 of contract Act, 1872, defines a pledge as, the 'bailment of goods as security for payment of a debt or performance of a promise." Only movable goods can be pledged. From the above definition we observe that,

1. A pledge occurs when goods are delivered for getting advance,

2. The goods pledged will be returned to the owner on repayment of the debt,

3. The goods serve as security for the debt.

The person who transfers the goods is called pledger and to whom it is transferred is called the pledgee.

ESSENTIALS OF PLEDGE

Delivery of goods: Delivery of goods is essential to complete a pledge. The delivery may be physical or symbolic. Physical delivery refers to physical transfer of goods from a pledger to the pledgee. Symbolic delivery requires no actual delivery of goods. But the possession of goods must be transferred to a pledgee. This may be done in any one of the ways:

1. Delivery of the key of the warehouse in which the goods are stored.

2. Delivery of the document of title to goods like bill of lading, Railway receipt, Warehouse warrant etc.

3. Delivery of transferable warehouse warrant if the goods are kept in a public warehouse.

Transfer of ownership: The ownership of goods remains with the pledger. The possession of the goods vests with pledgee till the loan is repaid.

Right in case of failure to repay: If the pledger fails to repay within the stipulated time, pledgee may,

1. sell the goods pledged after giving reasonable notice,
2. File a civil suit against the pledger for the amount due,

File a suit for the sale of the goods pledged and the realization of money due to him. When the pledgee decides to exercise the right of sale, he must issue a clear, specific and reasonable notice.

PRECAUTION AND GENERAL GUIDELINES FOR PLEDGEE

1. The godown must be in good condition and well-constructed.
2. Godown must be effectively under Bank's control.
3. Name board of the bank should be placed outside and inside of the godown.
4. Letter from the party for free accesses to the godown by bank personnel (Bank's prescribed form) to be obtained.
5. Letter of disclaimer from the owner of godown is to be obtained if the godown is rented one.
6. Godown keeper and godown Chowkider are to be posted for receiving/ delivery and to ensure security of the goods.
7. Insurance of godown is to be done against all risks. Bank clause should be inserted.
8. Periodical Inspection by the authorized person of the bank (monthly/fortnightly) should be conducted.
9. Value of stocks must be determined at landed cost/invoice cost/market price whichever is lower as per Head office guideline (circulars).
10. Restricted item must not be accepted for pledge.

11. Deliveries and rotations of the stocks is to be made as per existing rules/procedures and terms and conditions contained in the sanction advice.

12. Market value of the goods pledged should be ascertained frequently in order to retain proper margin and allow withdrawals within drawing power. No upward revaluation without H.O. approval.

13. Pledged goods must be stocked properly to facilitate counting and checking.

14. Stock report card on each stock mentioning Nos. of bales, bags, cases etc. must be maintained.

15. In case of chemicals, drugs and medicines the date of expiry should be written and technical personnel must be employed to ensure its quality.

- Hypothecation:

Hypothecation creates on equitable charge on movable property without possession. However, the hypothecation deed provides that the banker will have the right to take the goods hypothecated in its possession if the need arises. Hypothecation creates on equitable charge on movable property without possession. The mortgage of movable property for securing loan is called Hypothecation. In other words, in case of hypothecation, a charge over movable properties like goods, raw materials, goods in progress are created. Hypothecation is a charge against property for an amount of debt where neither ownership nor possession is passed to the creditor. Though the borrower is in actual physical possession, the constructive possession remains with the Bank as per the deed of hypothecation. The borrower holds the possession not in his own right as the owner of the goods but as the agent of the Bank. Being only an equitable charge on movable property without possession, hypothecation facility is risky as clean advances. So it is granted only to parties of undoubted means with the highest integrity. Moreover, bankers insist upon for giving some sort of collateral securities.

Features of Hypothecation:

- Charge against a property for an amount of debt,
- Goods remains in the possession of the borrower,

- Borrower binds himself to give possession of the hypothecated goods to the Bank when called upon to do so.
- It is a floating charge.
- It is rather precarious.

Being only an equitable charge on movable property without possession, hypothecation facility is risky as clean advances. So it is granted only to parties of undoubted means with the highest integrity.

Precaution and general guidelines for Hypothecation:

As goods under hypothecation remains in the possession of the borrower, extra care has to be exercised to see that the bank's security is complete, adequate, safe and available at times when required. The banker should take the following precautions:

1. He must get stock statements periodically which contain a declaration by the borrower regarding his title to goods and correctness of the quality, quantity etc.

2. On the basis of the statement, he should inspect the stock and books of accounts of the borrower.

3. An undertaking from the debtor in writing, stating that he has not hypothecated the same goods to any other bank must be obtained.

4. The banker should get a letter of hypothecation containing several clauses to protect his interest under all circumstances.

5. The banker should insist on the borrower insuring the goods against the risks. He should also get it endorsed and assigned in his favor.

6. A board reading "Stock Hypothecated to X Bank" should be displayed in the place where the goods are stored.

In case of hypothecation bank may be cheated in the following ways:

- The borrower declares wrongly the capacity of the storing place.
- A false platform between the loose stocks is erected.
- The borrower creates a hollow square in the middle of stocks. Kind of fraud is generally committed by the borrowers who have either built-up confidence with the bank or where the branch managers and other officials at the branch office have been got around by such borrowers.
- Often the borrower with intention to cheat the bank resorts to dumping deteriorated/obsolete stocks in between the good stocks.
- The borrower mixes inferior quality liquids or water with good liquids and commits fraud. The device is generally adopted by parties dealing in chemicals or oils.
- The borrower stores stocks of different qualities in the godown and cheats the bank. In such cases borrowers store goods of qualities different from these declared in lodgment memos.

MORTGAGE

A mortgage is a conveyance of an interest in property (land or any immovable property) for securing a debt. A legal mortgage is created by a registered deed and gives the mortgagee the right of sale in case of default of the borrower. The transferor is called a 'mortgagor', the transferee a 'mortgagee', the principal money and interest of which payment is secured for the time being are called 'mortgage money', and the instrument (if any) by which the transfer is affected is called a 'mortgage deed'. A mortgage is a method of creating charge on immovable properties like land and building.

Section 58 of the Transfer of Property Act 1882, define a mortgage as follows: "A mortgage is the transfer of an interest in specific immovable property for the purpose of securing the payment of money advanced or to be advanced by way of loan, an existing or future debt, or the performance of an engagement which may give rise to a pecuniary liability."

Characteristics of a Mortgage:

In terms of the definition, the following are the characteristics of a mortgage:

1. A mortgage can be affected only on immovable property. Immovable property includes land, benefits that arise out of land and things attached to earth like trees, buildings and machinery. But a machine which is not permanently fixed to the earth and is shift able from one place to another is not considered to be immovable property.

2. A mortgage is the transfer of an interest in the specific immovable property. This means the owner transfers some of his rights only to the mortgagee. For example, the right to redeem the property mortgaged.

3. The object of transfer of interest in the property must be to secure a loan or performance of a contract which results in monetary obligation. Transfer of property for purposes other than the above will not amount to mortgage. For example, a property transferred to Liquidate prior debt will not constitute a mortgage.

4. The property to be mortgaged must be a specific one, i.e., it can be identified by its size, location, boundaries etc.

5. The actual possession of the mortgaged property is generally with the mortgager.

6. The interest in the mortgaged property is re-conveyed to the mortgager on repayment of the loan with interest due on.

7. In case, the mortgager fails to repay the loan, the mortgagee gets the right to recover the debt out of the sale proceeds of the mortgaged property.

Forms of Mortgages

Section 58 of the transfer of Property Act enumerates six kinds of mortgages:

1. Simple mortgage.
2. Mortgage by conditional sale.
3. Usufructuary mortgage.
4. English mortgage.

5. Mortgage Ly deposit of title deeds.

6. Anomalous mortgage.

Rights of Mortgager

1. Rights of Redemption

2. Accession to Mortgaged Property:

3. Right to Transfer to Third Party

4. Right to Inspection and Production of Documents

Sub-Mortgage

A sub-mortgage is created when the mortgagee gives the mortgaged property as security for advance. The mortgaged security is the property of the mortgagee and so he has the right to re-mortgage for securing loans. The sub-mortgagee is placed in the position of the original mortgagee and entitled to receive the mortgage money, sue for the property and realize, the security. Therefore, a sub-mortgage is also known as 'mortgage of mortgagee.'

ASSIGNMENT

Assignment is transfer of ownership from one person/authority to another person/authority.

- Assignment means transfer of any existing or future right, property or debt by one person to another person.

- The person who assigns the property is called assignor and the person to whom it is transferred is called assignee.

- Usually, assignment is made of actionable claims such as book debts, insurance claims etc.

- In banking business, a borrower may assign to the banker

i) The book debts,

ii) Money due from government department

iii) Insurance policies

Type of Assignment

Assignment may be two types

. **Legal Assignment**: A legal Assignment is an absolute transfer of actionable claim. It must be in writing signed by the assignor. The assignor informs his debtor in writing intimating the assignee's names and address. The assignee also gives a notice to the debtor and seeks a confirmation of the balance due.

Equitable assignment: An equitable assignment is one which does not fulfill all the above requirement.In case of legal assignment, the assignee can sue in his own name. A legal assignee can also give a good discharge for the debt without the concurrence of the assignor.

- Set-off:

Set-off means the total or partial merging of a claim of one person against another in a counter claim by the latter against the former.

UNIT – IV

Introduction

Over the years, the banking operations have been atomized to a large extent and wide range of banking software's have been developed for accounting of transactions and core banking operations. Bank software's are becoming more sophisticated all the time. As new accounting methods develop and more people bank online, private banking software is being developed to streamline the processes.

Core Banking Solution (CBS)

Core banking is a term used to describe the services offered by a group of interconnected bank branches. Bank customers may access their funds and other transactions from any of the member branch offices. Core Banking Solutions (CBS) is a procedure which is realized in a centralized environment, i.e. under which the data pertaining to the customer's account, i.e. financial dealings, profession, family members, income, etc. is stored in the central server of the bank instead of the branch server. This task is accomplished through advanced software by using the services provided by specialized agencies. Core banking is the nerve centre of any banking operation. In core banking, customer of a specified branch of a particular area is a customer of the entire bank spreading its branch network across the world. Due to its benefits, a number of banks in India in recent years have taken steps to implement the core banking solutions with a view of building cordial relationship with the customer based on the information available and according to their need offers customized financial products to the customer.

Advantages:

The CBS process is beneficial both to the customers and the banks in the following ways:
Customer:

Transaction of business from any branch. Less number of errors, therefore higher accuracy in transactions. Better funds management due to immediate availability of funds.

Banks:

Standardization of process in the bank. Better customer service which leads to customer retention and increased customer dealings. Availability of exact and precise data & better use of

available infrastructure. Better MIS and reporting to external agencies such as Govt., RBI, etc. Increased business volume with better asset liability management.

Home Banking

Home banking is a form of banking that allows you to perform many financial transactions literally from the comfort of your own home. However, the term can be misleading because home banking is not solely limited to your home. If you have access to the internet or a telephone, home banking puts your bank-account information at your fingertips anywhere, at any time. Banking by mail is also a form of home banking. Technology continues to touch nearly every aspect of our lives every day, and banking is no exception. That's why understanding the many different aspects of home banking and how it works can help you make the right decision for your financial needs.

Types of Home Banking

Although its name signifies a tie to banking at home, there are actually a number of ways home baking can be administered.

Online banking : Online banking gives you the ability to handle your finances from the comfort of home. You can also complete transactions remotely anywhere at any time, as long as you have an eligible account and secure access to the internet.

Mobile banking: involves using your mobile phone to access your bank-account information. You can access the information through your bank's web page, text messaging, or by downloading its app.

Banking by mail: is a service that offers you the ability to mail deposits, payments, and information directly to your bank or credit union. You also have the option to receive a receipt for your transaction by mail.

Telephone Banking: Generally, this refers to using a telephone to contact your financial institution. Similarly, telephone banking can also be used to conduct transactions using an

automated system, such as checking your account balance, transferring funds, and determining if transactions or checks have cleared.

Pros

Real-time money management:

Home-banking technologies can present a faster and easier way to access financial services, track your spending, and manage your finances.

Greater convenience:

Home banking allows the ability to accomplish tasks on the go, which offers greater convenience for customers.

Often offered as a free service:

Home banking is provided by many financial institutions as a free service to customers.

Cons

- Increased difficulty reaching customer service: When consumers use home-banking services, it may be more difficult to access customer service if there is a discrepancy or something goes wrong.

- Risk of security breaches: Home banking can present privacy or security concerns when consumers use mobile devices to conduct their financial transactions.

Retail Banking

The relationship between the bankers and the customers is not the same like before. The market has undergone a sea change. The customers have become more demanding today. The transition from sellers market to buyers market has compelled the bankers to understand the pulse and needs of the customers.

It may not be incorrect to say that the banking products and services today are designed by the customers. The luxury of discretion to design the products and services by the bankers is not any more available to the bankers.

Bankers today have no choice except to alter their product mix, delivery channels and corporate structure to serve their functional role. Some of the products which were shunned by

the bankers and were treated as inflationary 20 years ago in nature like housing loan, consumer durables finance which otherwise were the prerogative of the bank employees have become targets of bank business and area of fierce competition and business mantra. Banks are vying with each other to sell across their ideas and products in the compelling hours of competition and the unexpected quarters say cooperative banks too have joined the fray.

Retail banking has wider connotation and is not the same as that of retail lending. Retail banking refers to the efforts of the bankers to reach up to the customers on both fronts of the balance sheet i.e., Liabilities side as well as Assets side. Under the liabilities side, we have deposits. Unless the banker designs the products according to the needs of the customers and facilitate better bargain to them in terms of rate interest, time and delivery channels, it is not easy for them to solicit business in this segment. The age of walk in deposits is gone. With interest deregulation in the sector of deposits with the sole exception of Savings Bank Account, where the apex monetary authority continues to decide the rate of interest, rest of the fields are open for competition.

In the Assets side, we have credit/loan schemes of the various banks. The job of the banker has become very difficult in this segment too. Bankers today are offering various sops to attract the potential customers. For instance, payment of free insurance premium by the bank comes along with the vehicle loan in respect of few banks. Some banks are prepared to offer total credit solutions along with housing loan, we mean here, they have enabled facility of consumer durables finance, vehicle finance in one go the customers who avail of housing loan from them.

This way, we understand retail banking includes designing delivery of customized products from both sides of the balance sheet.

The following channels are effectively utilized by the bankers to mobilize business from the potential clients:

Premises banking or banking at doorsteps

Automated Teller Machines

Debit Cards and Credit Cards Telephone banking

Internet Banking

Mobile Banking

Electronic Funds Transfer/Electronic Clearing System debit

Mobile banking

M-Banking: Mobile banking (M-banking) is a system that allows customers of a financial institution to conduct a number of financial transactions through a mobile device such as a mobile phone or tablet through specifically designed Mobile Banking Apps. It is the most convenient and easy way to stay connected with the bank. It refers to provision and availing of banking and financial services with the help of mobile telecommunication devices. The scope of offered services may include facilities to conduct bank and stock market transactions, to administer accounts and to access customised information. Mobile banking has until 2010 most often been performed via SMS, known as SMS Banking.

The typical mobile banking services may include:

(1) Mini-statements and checking of account history,

(2) Funds transfers between the customer's linked accounts,

(3) Paying third parties, including bill payments and third party fund transfers,

(4) Alerts on account activity or passing of set thresholds,

(5) Cheque book and card requests,

(6) Access to loan statements,

(7) Access to card statements,

(8) Status of requests for credit, including mortgage approval, and insurance coverage,

(9) Mutual funds/equity statements,

(10) Real-time stock quotes,

(11) Personalised alerts and notifications on security prices,

(12) Monitoring of term deposits

(13) Portfolio management services,

(14) ATM Location etc.

With the advent of technology and increasing use of smart phone and tablet based devices, the use of mobile banking functionality would enable customers connect across various services. The rapid growth of smart phones based on Google's Android Operating System have led to the increasing use of special client programs, called 'Apps' downloaded to the mobile devices. With further advancements in web technologies, more and more banks are launching mobile web based services. But, mobile banking is attractive and popular mainly among the younger and 'tech-savvy' customers.

Debit Cards:

A debit card is a plastic payment card that provides the cardholder electronic access to their bank account at a financial institution. Most cards relay a message to the cardholder's bank to withdraw funds from a payer's designated bank account. Debit cards usually allow for instant withdrawal of cash, acting as the ATM card for withdrawing cash. The card, where accepted, can be used instead of cash when making purchases. Unlike credit and charge cards, payments using a debit card are immediately transferred from the cardholder's designated bank account, instead of them paying the money back at a later date.

There are currently three ways that debit card transactions are processed, namely, (i) Online debit or PIN debit, (ii) Offline debit or signature debit, and (iii) The Electronic Purse System. One physical card can include the functions of all three types, so that it can be used in a number of different circumstances. In many countries, the use of debit cards has become so widespread that their volume has overtaken or entirely replaced cheques and, in some instances, cash transactions. Although many debit cards are of the Visa or Master Card brand, there are many other types of debit card, each accepted only within a particular country or region. The National Payments Corporation of India (NPCI) has launched a new card called RuPay.

Debit cards may also be used on the Internet. Internet purchases can be authenticated by the consumer entering their PIN. The online debit cards require electronic authorization of every

transaction and the debits are reflected in the user’s account immediately. The transaction may be additionally secured with the personal identification number (PIN) authentication system.

Credit Cards:

A credit card is a payment card issued to users as a system of payment. It allows the cardholder to pay for goods and services based on the holder's promise to pay for them. The issuer of the card creates a revolving account and grants a line of credit to the user from which he can borrow money for payment to a merchant or as a cash advance to the user. Credit cards may be treated as ‘convenient credit’ that allow the consumers a continuing balance of debt, subject to interest being charged. It can be used like currency by the owner of the card. It typically involves a third-party entity that pays the seller and is reimbursed by the buyer.

Credit cards may simply serve as a form of revolving credit. The main benefit to the cardholder is convenience. Compared to debit cards and checks, a credit card allows small shortterm loans to be quickly made to a cardholder who need not calculate a balance remaining before every transaction, provided the total charges do not exceed the maximum credit line for the card. A credit card issuing company, such as a bank or credit union, would enter into agreements with merchants for them to accept their credit cards. Each month, the cardholder is sent a statement indicating the purchases made with the card, any outstanding fees, and the total amount owed.

Electronic verification systems allow merchants to verify in a few seconds that the card is valid and the cardholder has sufficient credit to cover the purchase, allowing the verification to happen at time of purchase. The verification is performed using a credit card payment terminal or point-of-sale (POS) system with a communications link to the merchant's acquiring bank. Credit card issuers usually waive interest charges if the balance is paid in full each month, but typically will charge full interest on the entire outstanding balance from the date of each purchase if the total balance is not paid.

Credit cards are accepted in larger establishments in almost all countries, and are available with a variety of credit limits and repayment arrangements. Many credit cards offer rewards and benefits packages, such as enhanced product warranties at no cost, free loss/damage coverage on

new purchases and various insurance protections. Credit cards can also offer a loyalty program, where each purchase is rewarded with points, which may be redeemed for further goods and services or cash back.

ATM:

An Automated Teller Machine (ATM) is an electronic telecommunication device that enables the customers of a financial institution to perform financial transactions without the need for a human cashier, clerk or bank teller. It is also known as Automated Banking Machine (ABM). Using an ATM, customers can access their bank deposit or credit accounts in order to make a variety of transactions such as withdrawals, check balances, getting mini statements, etc. Most ATMs are connected to interbank networks, enabling people to withdraw and deposit money from machines not belonging to the bank where they have their accounts or in the countries where their accounts are held (enabling cash withdrawals in local currency).

On most modern ATMs, the customer is identified by inserting a plastic ATM card with a magnetic stripe or a plastic smart card with a chip that contains a unique card number and some security information. An ATM card is any payment card issued by a financial institution that enables a customer to access an Automated Teller Machine (ATM) in order to perform transactions such as deposits, cash withdrawals, obtaining account information, etc. It is also known as Bank Card, Money Access Card, Key Card or Cash Card. Most ATM cards today are Bank Cards such as debit or credit cards that have been ATM-enabled. Unlike an offline bank card that is signature based, an ATM card require authentication through a personal identification number (PIN).

Interbank networks allow the use of ATM cards at ATMs of financial institutions other than those of the institution that issued the cards. In some banking networks, the two functions of ATM cards and debit cards are combined into a single card called simply as a Debit Card or also commonly called as Bank Card. These are able to perform banking tasks at ATMs and also make point-of-sale transactions, with both features using a PIN. ATM cards can also be used on merchants' card terminals that deliver ATM features without any cash drawer. These terminals can also be used as cashless scrip ATMs by cashing the receipts they issue at the merchant's point of sale.

E-Cash

E-Cash: The purse contains electronic money, which has full monetary value, is usable at any outlet with an accepting device, and is at any time exchangeable for cash. Transport may be just one of a number of items where the e-cash can be used, and might not even be the main usage. The e-cash is subject to banking regulations, and would have to be issued and underwritten by a bank.

Though the handling requires a substantial level of technical competence, the major benefits of electronic purse are:

Cash handling is reduced as customers migrate to prepaid tickets.

- High degree of security.

- Innovative means of adding/renewing value can be utilized.

- Electronic purse can be offered for infrequent customers when it is desired to eliminate all cash transactions.

- Third parties can become involved in issuing value.

- Incentives such as free transfers, discounts and fare-capping can be offered to the customer in a secure and consistent way.

SWIFT :

Electronic payment systems for large payments have developed as the demands for international settlement of currency and securities transactions have increased. Society for Worldwide Interbank Financial Telecommunication known as SWIFT, currently dominates the field of inter- bank messaging but, is increasingly facing competition from other networks. SWIFT was set-up in 1973 and is based in Brussels. Its member banks, a consortium of more than 2,200 banks own it. SWIFT provides electronic payment services to around 4,300 financial institutions worldwide and presently processes around 500 million payment messages a year. Shares in SWIFT are based on the volume of message traffic. SWIFT has been criticised for relying on hub and spoke communications technology, which was originally conceived in the 1970s. Although the SWIFT system enjoys worldwide acceptance it is dependent on the same heritage of correspondent banks, which form the basis for all low value cross-border transfers.

Objectives :

The basic objectives of SWIFT are :

i) To Provide Processing and Communication Services: Work in partnership with its members to provide low-cost, competitive financial processing and communication services of the highest security and reliability.

ii) Automation of Transaction Process: Contribute significantly to the commercial success of its members through greater automation of the end-to-end financial transaction process, based on its leading expertise in message processing and financial standards setting.

iii) Capitalization on Position: Capitalize on its position as an international open forum for the world's financial institutions to address industry-level threats, issues and opportunities.

iv) Employment of People: Employ and recruit the best people, invest in the most beneficial resources and become a leading global organization respected for its professionalism, effectiveness, vision and management.

Operations of SWIFT in India:

SWIFT User Group is formed in India with the Chairman IBA as the Chair person and the Chief General Manager-in-Charge, Department of Information Technology, Reserve Bank of India as the Alternate Chairperson. Currently there are 92 institutions comprising banks, brokers and dealers, central depositories and clearing organizations, who are the user members of SWIFT in India:

Members 48 ,Sub-Members 36, Broker(s) and Dealer(s) 1 ,Central Depositories and Clearing 1 ,Non-Shareholding Banks 5 ,Representative Office(s) 1 Total 92

RTGS (Real Time Gross Settlement):

The real time gross settlement solution is a milestone in the history of Indian payment system. It is the key critical element. It provides the missing link in the process of the setting up of the Integrated payment and settlement system in the country. Now-adays, it is the preferred mode of the settlement of large value interbank payments in the world over. As a settlement process, RTGS minimizes settlement risks by settling individual payments in real time in the books of account held at the central bank. Under RTGS, the practically instant settlement ensures fast, secure, final and irrevocable settlement of payment transactions. The real time gross settlement system is designed to provide large value funds transfer and settlement in an on-line real time environment to the banking industry, with settlement on a gross basis. It will enhance competitiveness within the system. It gears up the banks to meet future challenges posed by the external environment. If this system is implemented with due precautions and proper action plan, it will certainly help the Indian Banking Industry to attain global standards. RTGS is an ultimate in the payment and settlement architecture in any country primarily for online, real time interbank payment and settlement of large value funds. RTGS payment system can also be called as one in which payment instructions between banks are processed and settled individually and continuously throughout the day.

Working of RTGS System :

Each participant of the RTGS will be required to open a dedicated settlement account for putting through its RTGS transactions. This account will be an intra-day account i.e. it would be operational only during the course of the RTGS day. The account is to be funded at the start of the day (SOD) from a current account which the participant holds under the present system at Deposit Account Department (DAD), RBI, Mumbai. Balances in the RTGS account at the end of the day of the RTGS day are swept back to participant's current account. The system enables the participants to place standing instructions with DAD, Mumbai to fund their RTGS account each morning duly specifying an actual amount or percentage of balance to be transferred to the RTGS settlement account every day at SOD. The system also provides funds to the RTGS account during the day from the participant's current account. Payment transactions emanating from a participant are ordinarily expected to be settled immediately after they are received which

is the essence of the real time system. The RTGS provides maintenance of participant wise payment queues in which payment transactions will be held in first-in-first-out basis. However, to enable the participants to take care of the urgent time-critical payments and to enable more effective funds management, the system allows the participant to assign priorities to the payment messages and thereby enables a particular transaction to be processed before another transaction which was submitted earlier.

Facilities Provided by RTGS :

It facilitates participants:

1) View of Transaction: To view their respective transactions held in payment queues, to cancel such transactions and even change their priorities.

2) Movement of Funds: Initiates movement of funds between various accounts held by it to optimize funds deployment and economies intra-day liquidity requirements.

3) Various Types of Transactions: By providing a wide array of transaction types which can be flexibly deployed to meet varying requirements.

4) Types of Interbank Transactions: By providing interbank transactions types which can be used to settle participant's financial obligations on their own account.

Benefits of RTGS :

The RTGS system has all round advantages to the bank, customer and the society at large. These advantages to the various segments of society are as follows :

A) Banks :

1) It offers immediate and irrevocable settlement.

2) It provides high-value intra-bank and inter-bank funds transfer.

3) It provides new opportunities for formulation of innovative products.

B) Customers :

1) It provides sophisticated online banking services.

2) It offers reliable high-value funds transfer.

3) It improves personal image with beneficiary.

C) Economy :

1) Reduces the Risk : RTGS will reduce the systemic risk that exists in the present settlement systems, like cascading affects on banks due to failure of one bank to meet its settlement commitments.

2) Improves Confidence of Outside Agencies : It improves confidence of outside agencies like World Bank in Indian Economy.

UNIT V

RESERVE BANK OF INDIA

The Reserve Bank of India Act, 1934, confers upon it the powers to act as note-issuing authority, banker’s bank to the Government. As the Central Bank of the country, the Reserve Bank of India performs both the Traditional Functions of a central bank and a variety of developmental and promotional functions. The Central Office of the Reserve Bank was initially established in Calcutta but was permanently moved to Mumbai in 1937. The Central Office is where the Governor sits and where policies are formulated. Though originally privately owned, since nationalisation in 1949, the Reserve Bank is fully owned by the Government of India. Preamble The Preamble of the Reserve Bank of India describes the basic functions of the Reserve Bank as: "...to regulate the issue of Bank Notes and keeping of reserves with a view to securing monetary stability in India and generally to operate the currency and credit system of the country to its advantage The Reserve Bank of India was established on April 1, 1935 in accordance with the provisions of."Central Board The Reserve Bank's affairs are governed by a central board of directors. The board is appointed by the Government of India in keeping with the Reserve Bank of India Act.

Functions of RBI

The functions of Reserve Bank of India (RBI) cab be broadly classified into to as follows:

Monetary Functions

a) Bank of Note Issue:

Under section 22 of the Reserve Bank of India Act, the bank has the sole right to issue bank notes of all denominations. The distribution of one rupee notes and coins and small coins all over the country is undertaken by the Reserve Bank as agent of the Government. The Reserve Bank has a separate Issue Department which is entrusted with the issue of currency notes. The assets and liabilities of the Issue Department are kept separate from those other Banking Department. Originally, the assets of the Issue Department were to consist of not less than two-fifths of gold coin, gold bullion or sterling securities provided the amount of gold was not less than Rs. 40 crores in value. The remaining three -fifths of the assets might be held in rupees coins, Government of

India rupee securities, eligible bills of exchange and promissory notes payable in India. Due to the exigencies of the Second World War and the post-war period, these provisions were considerably modified. Since 1957, the Reserve Bank of India is required to maintain gold and foreign exchange reserves of Rs. 200 crores, of which at least Rs. 115 crores should be in gold. The system as it exists today is known,-as the minimum reserve system.

b) Currency Chest:

RBI has made adequate administrative arrangements for undertaking the function of distribution of currency notes & coins. The Issue department has opened its offices in 10 leading cities for this purpose. More ever, currency chest have been maintained all over the country to facilitate the expansion and contraction of currency in the country.

Banker and agent to Government:

The Reserve Bank of India is to act as Government banker, agent and adviser. The Reserve Bank has the obligation to transact Government business, via to keep the cash balances as deposits free of interest, to receive and to make payments on behalf of the Government and to carry out their exchange remittances and other banking operations. The Reserve Bank of India helps the Government—both the Union and the States to float new loans and to manage public debt. The Bank makes ways and means advances to the Governments for 90 days. It makes loans and advances to the States and local authorities. It acts as adviser to the Government on all monetary and banking matters.

d) Bankers' Bank and Lender of the Last Resort or Father of Banks:

The Reserve Bank of India acts as the bankers' bank. The RBI controls the volume of reserves of the banks and determines their deposit credit creation ability. The banks hold all/ a part of their reserves with the RBI and in times of need, they borrow from the RBI. According to the provisions of the Banking Companies Act of 1949, every scheduled bank was required to maintain with the Reserve Bank a cash balance equivalent to 5% of its demand liabilities and 2 per cent of its time liabilities in India. By an amendment of 1962, the distinction between demand and time liabilities was abolished

and banks have been asked to keep cash reserves equal to 3 per cent of their aggregate deposit liabilities. The minimum cash requirements can be changed by the Reserve Bank of India. The scheduled banks can borrow from the Reserve Bank of India on the basis of eligible securities or get financial accommodation in times of need or stringency by rediscounting bills of exchange. Since commercial banks can always expect the Reserve Bank of India to come to their help in times of banking crisis the Reserve Bank becomes not only the banker's bank but also the lender of the last resort.

e) Loans & Advances:

Section 17(4) enables RBI to grant loans, & advances to the scheduled banks, repayable on demand or on the expiry of fixed periods not exceeding 90 days against the security.

f) Custodian of the Cash Reserves of Commercial Banks:

All commercial banks kept part of their cash balances as deposit with the central banks of the country, either because of convention or because of legal compulsion. They regularly draw currency from the central bank during the busy season and pay in surplus currency during slack season. Parts of these balances are meant for clearing purposes. That is all commercial banks keep deposit accounts with central bank, payment by one bank to the RBI will be simple book entry adjustment in the books of the central bank. The deposit balances with central bank are considered as cash reserves for general purposes.

g) Custodian of Foreign Balances of the Country:

The Reserve Bank of India has the responsibility to maintain the official rate of exchange. According to the Reserve Bank of India Act of 1934, the Bank was required to buy and sell at fixed rates any quantity of sterling in lots of not less than Rs. 10,000.The rate of exchange fixed was Re. I sh. 6d. Since 1935 the Bank was able to maintain the exchange rate fixed at 1sh. 6d though there were periods for extreme pressure in favour of or against the rupee.After India becomes a member of the International Monetary Fund in 1945, the Reserve Bank has the responsibility of maintaining fixed exchange rates with

all other member countries of the International Monetary Fund (I.M.F.) Besides maintaining the rate of exchange of the rupee, the Reserve Bank has to act as the custodian of India's reserve of international currencies. The vast sterling balances were acquired and managed by the Bank. Further, the RBI has the responsibility of administering the exchange controls of the country.

h) Controller of Credit:

The Reserve Bank of India is the controller of credit i.e. it has the power to influence the volume of credit created by banks in India. It can do so through changing the Bank rate or through open market operations. According to the Banking Regulation Act of 1949, the Reserve Bank of India can ask any particular bank or the whole banking system not to lend to particular groups or persons on the basis of certain types of securities. Since 1956, selective controls of credit are increasingly being used by the Reserve Bank. The Reserve Bank of India is armed with many more powers to control the Indian money market. Every bank has to get licence from the Reserve Bank of India to do banking business within India. The licence can be cancelled by the Reserve Bank if certain stipulated conditions are not fulfilled. Every bank will have to get the permission of the Reserve Bank before it can open a new branch. Each scheduled bank must send a weekly return to the Reserve Bank showing in detail, its assets and liabilities. This power of the Reserve Bank to call for information is also intended to give it effective control of the credit system. The Reserve Bank has also the power to inspect the accounts of any commercial bank.

Non-Monetary Functions

a). Supervisory Functions:

In addition to its traditional central banking functions, RBI has certain non-monetary functions of the nature of supervision of banks and promotion of sound banking in India. The RBI Act, 1934, and the Banking Regulation Act, 1949, have given RBI wide powers of supervision and control over commercial and co-operative banks relating to licensing and establishment, branch expansion, liquidity of their assets, management and methods of working, amalgamation, re-

construction and liquidation. RBI is authorised to carry out periodical inspections of the banks and a call for returns and necessary information from them. The nationalization of 14 major Indian scheduled banks in July 1969 has imposed new responsibilities on RBI for redirecting the growth of banking and credit policies towards more rapid development of the economy and realization of certain desired social objectives. The supervisory functions of RBI have helped a great deal in improving the standard banking in India to develop on sound lines and to improve the methods of their operation.

b) Promotional Functions:

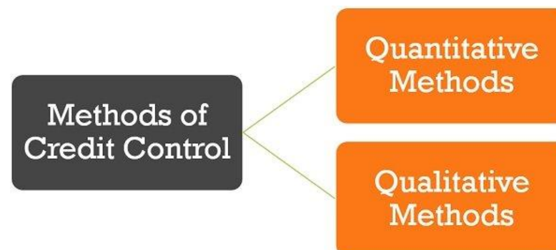
i) By encouraging the commercial banks to expand their branches in the semi-urban and rural areas, the Reserve Bank helps (i) to reduce the dependence of the people in these areas on the defective unorganized sector of indigenous bankers and money lenders, and (ii) to develop the banking habits of the people ii) 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, iii) Through the institutions like Unit Trust of India, the (Reserve Bank helps to mobilize savings in the country, iv) Since its inception, the Reserve Bank has been mating efforts to promote institutional agricultural credit by developing cooperative credit institutions. v) The Reserve Bank also helps to promote the process of industrialization in the country by setting up specialized institutions for industrial finance, vi) it also undertakes measures for developing bill market in the country

Credit Control

Definition: Credit Control is a function performed by the Central Bank (Reserve Bank of India), to control the credit, i.e. the demand and supply of money or say liquidity in the economy. With this function, the central bank regulates the credit granted by the commercial banks to its customers. It aims to achieve economic development with stability as well as to manage the inflationary and deflationary pressure. It involves limiting the credit volume created by the commercial bank, regulating the credit volume, directing credit to productive uses, and implementing measures that strengthen the structure of banks.

Methods of Credit Control

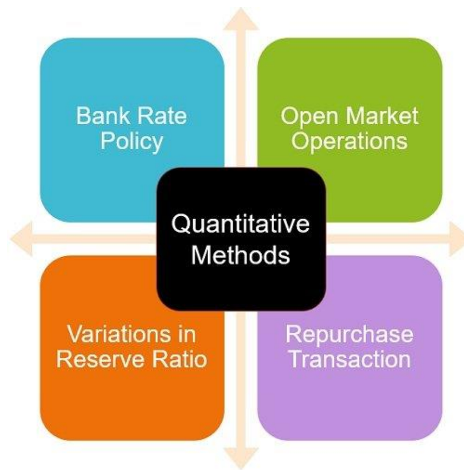
Different methods are used by the Central Bank to control credit, which is broadly classified into two main categories:



Quantitative Methods or General Methods

Quantitative Methods of Credit Control are related to Quantity or Volume of Money and are aimed at regulating the total volume of bank credit. These tools are indirect in nature and they tend to influence the loanable funds of the commercial banks.

The total quantity of deposits created by the commercial banks is expected to be controlled and adjusted using these methods. It maintains a balance between savings and investment.



1. **Bank Rate Policy**: Otherwise called a discount rate policy. It is described as the standard rate at which the central bank is ready to purchase and rediscount eligible instruments like government-approved bills and commercial papers. It has a great influence on the availability and cost of credit. When the central bank increases the bank rate, it may result in a reduction in the volume of borrowings by the commercial bank from RBI, whereas when the RBI reduces the bank rate, the borrowings become economical for the commercial bank and thus encourages credit expansion of the economy.

2. **Open Market Operations (OMO)**: It implies trading of eligible securities by the country's apex bank, i.e. RBI in both capital market and money market. When the central bank purchases or sells short term or long term securities, it leads to an increase or decrease in the financial resources of the commercial bank.

This will ultimately influence the credit creation of the banks.

3. **Variations in the Reserve Ratio**: We all know that commercial banks have to maintain a specified percentage of their net demand and time liabilities as Cash Reserves, with RBI. As well as a certain proportion of their net demand and time liabilities has to be maintained by the banks in the form of liquid assets. These reserve ratios are called Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR) respectively.

Even the slightest change in these ratios can affect the reserve position of the commercial banks, which in turn regulates the supply of money in the economy.

4. **Repo, i.e. Repurchase Option**: Repo or otherwise called Repurchase transactions are carried out by the central bank, to regulate the money market situation. As per this transaction, the Central bank grants loan to commercial banks against government-approved securities for a fixed period, at a specified rate, called as Repo Rate, on a condition that the borrower bank will repurchase the securities at the predetermined rate, once the period is over.

Qualitative Methods or Selective Methods

Qualitative Methods are used in addition to general credit control methods. there are a number of situations wherein quantitative methods may not work effectively and may cause harm to particular sectors. As the quantitative methods of credit control, control the volume of credit, as a whole. So, there are chances that it may affect genuine productive purposes.

In this way, the qualitative methods of credit control come into the picture, wherein the credit is made available to productive and priority sectors, while the others are restricted.

1. **Fixation of margin requirements**: In this technique, the central bank determines the margin which commercial banks and financial institutions need to maintain for the amount extended by them in the form of loans, against commodities, stocks and shares. The central bank also prescribes margin requirements for the underlying securities, so as to restrict speculative dealing in stock exchanges.

2. **Credit Rationing**: As per this method, the central bank attempts to restrict the upper ceiling of loans and advances to a particular sector. Moreover, in specific cases, the central bank may also fix the ceiling for different categories of loans and advances. Also, commercial banks

are expected to stick to this limit. This facilitates the lessingt of bank credit exposure to unwanted sectors.

3. **Regulation of Consumer Credit**: With an aim of regulating consumer credit, the apex bank determines the down payments and the length of the period over which installments are to be spread. At the time of inflation, higher restrictions are levied to control the prices by controlling demands whereas, at the time of depression, relaxations are provided so as to increase demand for goods.

4. **Control through directives**: In this technique, the central bank issues directives from time to time so as to regulate the credit created by the commercial banks. These can be written orders, warnings, notices, or appeals.

It can help in regulating lending policies of the commercial banks or to fix a maximum limit of credit for specific purposes and also to restrain the flow of bank credit into non-essential lines. It may result in diverting the credit to productive use.

5. **Moral Suasion**: As per this method, the Reserve Bank of India exercises a moral influence on the commercial banks, in the form of advice, suggestion, guidelines, directives, request, and persuasion.

This is to ensure cooperation from the central bank. However, if the commercial bank does not comply with the advice extended by RBI, then they are not subject to any penal action. The success of this method mainly relies on the cooperation between the two banks i.e. central and commercial. It is helpful in limiting credit at the time of inflation in the economy.

6. **Publicity**: As per this method, the central bank publishes numerous reports in the form of bulletins, to state the good and the bad in the system, as well as to educate people about its view regarding credit expansion and contraction. This can help in informing the commercial bank to direct the supply of credit in the desired sectors.

In this way, the commercial banks get guidance from the Central bank and can modify their lending policies accordingly.

7. **Direct Action**: This technique is used by the central bank to enforce both quantitative and qualitative methods, and used as an adjunct to other methods. Further, the apex bank is authorized to take action against those banks which do not comply with the instructions extended or directives as well as it may refuse to rediscount their bills of exchange and commercial papers.

Also, RBI can refuse to supply credit to these banks, whose borrowings are greater than their capital. Even, the central bank is authorized to put a ban on a particular bank, if they do not adhere to the directives.

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