JAIIB/DBF PRINCIPLES & PRACTICES OF BANKING (PAPER-1) CAPSULE PDF

1. MODULE-A
   Indian Financial System

2. MODULE-B
   Function of Banks

3. MODULE-C
   Banking Technology

4. MODULE-D
   Support Services- Marketing of Banking Services/ Products

5. MODULE-E
   Ethics in Banks and Financial Institutions
JAIIB/DBF Principles & Practices of Banking Capsule Notes

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MODULE A – INDIAN FINANCIAL SYSTEM

Unit 1: Indian Financial System – An Overview
Unit 2: Banking Regulation
Unit 3: Retail Banking, Wholesale and International Banking
Unit 4: Role of Money Markets, Debt Markets & Forex Market
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Unit 1: Indian Financial System – An Overview

Financial Market

Financial system a network of financial institutions (COMMERCIAL BANKS, BUILDING SOCIETIES, etc.) and markets (MONEY MARKET, STOCK MARKET), dealing in a variety of financial instruments BANK DEPOSITS, STOCKS and SHARES, etc.), which are engaged in money transmission activities and the provision of LOAN and CREDIT facilities. The financial institutions and markets occupy a key position in the economy as intermediaries in channelling savings and other funds to borrowers and investors. In doing this one of their main roles is to reconcile the different requirements of savers and borrowers, thereby facilitating a higher level of saving and investment in the economy than would otherwise be the case.
### Regulatory Authority

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<td>2) Regulating all pension funds</td>
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### Central Bank Authority

**i) Commercial Bank:** A commercial bank is a type of bank that provides services such as accepting deposits, making business loans, and offering basic investment products that is operated as a business for profit. Public Sector Bank, Private sector Bank, Foreign Bank etc ...

**ii) Non-Banking Financial Companies (NBFC):** A Non-Banking Financial Corporation is a company incorporated under the *Companies Act 2013 or 1956* which is engaged in the business of Loans and Advances, Acquisition of stocks, equities, debt etc issued by the government or any local authority. The main objective of this type of a company is to accept deposits under any scheme or manner.
According to section 45-I (c) of the RBI Act, a Non-Banking Company carrying on the business of a financial institution will be an NBFC. It is governed by the Ministry of Corporate Affairs as well as the Reserve Bank of India.

The following NBFC’s are not required to obtain any registration with the Reserve Bank of India:

- Core Investment Companies – (assets are less than 100 crore or public funds not taken)
- Merchant Banking Companies
- Companies which are engaged in the business of stock-broking
- Housing Finance Companies
- Companies engaged in the business of Venture Capital.
- Insurance companies holding a certificate of registration issued by IRDA.
- Chit Fund Companies as defined in the Sec 2 clause (b) of the Chit Fund Act, 1982
- Nidhi Companies

iii) Primary Dealers (PDs): Primary dealers are registered entities with the RBI who have the license to purchase and sell government securities. They are entities who buy government securities directly from the RBI (the RBI issues government securities on behalf of the government), aiming to resell them to other buyers.

iv) Financial Institutions (FIs): Financial institutions are companies in the financial sector that provide a broad range of business and services including banking, insurance, and investment management. Governments of the country consider it important to oversee and to regulate financial institutions as they play an integral part in the economy of the country.

FIs are development financial institutions which provide long term-funds for industry and agriculture.

v) Cooperative Banks: Cooperative credit society in 1904 led to formation of cooperative banks. Presently, registered under Cooperative Society Act, 1965 and regulated by NABARD & RBI. These banks run for social welfare and not for profit maximization.

They are owned and operated by members itself to provide financial service to agriculturist and small businessmen.

Their main function is to get the deposit from members and public and grant loans to farmers (even farmer who is not member) and small industrialists in both rural and urban area.
vi) Payment and Settlement system: They are covered by the Payment and Settlement Systems Act, 2007 (PSS Act), legislated in December 2007 and regulated by the Reserve Bank of India and the Board for Regulation and Supervision of Payment and Settlement Systems. India has multiple payments and settlement systems, both gross and net settlement systems.

vii) Management of Government Debt: Sovereign debt management is the process of establishing and executing a strategy for managing the government’s debt in order to raise the required amount of funding, achieve its risk and cost objectives, and to meet any other sovereign debt management goals the government may have set, such as developing

viii) Bankers to Government: The RBI acts as banker to the government the Central as well as state governments. As such, it transacts all banking business of the government, which involves the receipt and payment of money on behalf of the government and carrying out of its exchange, remittance and other banking operations (Bonds and Treasury Bill).

ix) Lender of Last resort to banks: The Central Bank provides Liquidity supports on a temporary basis through the facility of repurchase (REPO) of security to banks to meet their short-term liquidity requirements.

x) Cash Reserve Ratio (CRR): Section 42(i) of RBI Act 1934, cash reserve ratio (CRR) is the amount of funds that all scheduled Commercial Banks (SCBs) are required to maintain with RBI. The cash reserve is either stored in the bank’s vault or is sent to the RBI. Banks do not get any interest on the money that is with the RBI under the CRR requirements.

Under Section 42 of RBI Act 1934

Maximum- 20%
Minimum- 3%

xi) Statutory Liquidity Ratio (SLR): The Reserve Bank of India or RBI mandates that banks store a proportion of their deposits in the form of cash so that the same can be given to the bank’s customers if the need arises. The percentage of cash required to be kept in reserves, vis-a-vis a bank’s total deposits, is called the Cash Reserve Ratio.

Minimum- 0%
Maximum- 40%

**Equity and Debt Market**

i) Stock Exchanges: A stock exchange, securities exchange or bourse is a facility where stockbrokers and traders can buy and sell securities, such as shares of stock and bonds and other financial instruments.
ii) Brokers: - A broker is an individual or firm that charges a fee or commission for executing buy and sell orders submitted by an investor. A broker also refers to the role of a firm when it acts as an agent for a customer and charges the customer a commission for its services.

iii) Equity and Debt Raisers: "Debt" involves borrowing money to be repaid, plus interest, while "equity" involves raising money by selling interests in the company. Essentially you will have to decide whether you want to pay back a loan or give shareholders stock in your company.

iv) Investment Bankers (Merchant Bankers): An Investment bank is a financial services company or corporate division that engages in advisory-based financial transactions on behalf of individuals, corporations, and governments.

v) Foreign institutional investors: A foreign institutional investor (FII) is an investor or investment fund registered in a country outside of the one in which it is investing. Institutional investors most notably include hedge funds, insurance companies, pension funds, and mutual funds.

vii) Custodians: A custodian is a financial institution that holds customers' securities for safekeeping in order to minimize the risk of their theft or loss. A custodian holds securities and other assets in electronic or physical form.

viii) Depositories: A depository is a building, office, or warehouse in which something is deposited for storage or safeguarding. Depositories may be organizations, banks, or institutions that hold securities and assists in the trading of securities.

ix) Mutual Funds: A mutual fund is a company that pools money from many investors and invests the money in securities such as stocks, bonds, and short-term debt. The combined holdings of the mutual fund are known as its portfolio. Investors buy shares in mutual funds.

x) Markets like registrars: The registrar accounts for all issued and outstanding shares, as well as the number of shares owned by each individual shareholder.

Insurance Regulatory and Development Authority

i) Multi Commodity Exchange of India (MCX): The Multi Commodity Exchange of India Limited (MCX), India's first listed exchange, is a state-of-the-art, commodity derivatives exchange that facilitates online trading of commodity derivatives transactions, thereby providing a platform for price discovery and risk management.

ii) Let us sum up: Sum insured is the maximum value for a year that your Insurance Company can pay in case you are hospitalized. Any amount above and beyond the sum insured will have to be taken out from your own pocket. For instance, suppose your sum insured is 2 lacs and you are hospitalized twice in a period of 12 months.
Unit 2- Banking Regulation

The Reserve Bank of India (RBI) is India’s central bank, also known as the banker’s bank. The RBI controls monetary and other banking policies of the Indian government. The Reserve Bank of India (RBI) was established on April 1, 1935, in accordance with the Reserve Bank of India Act, 1934. The Reserve Bank is permanently situated in Mumbai since 1937.

Establishment of Reserve Bank of India

The Reserve Bank is fully owned and operated by the Government of India.

The Preamble of the Reserve Bank of India describes the basic functions of the Reserve Bank as:

- Regulating the issue of Banknotes
- Securing monetary stability in India
- Modernising the monetary policy framework to meet economic challenges

The Reserve Bank’s operations are governed by a central board of directors, RBI is on the whole operated with a 21-member central board of directors appointed by the Government of India in accordance with the Reserve Bank of India Act.

The Central board of directors comprise of:

- **Official Directors** – The governor who is appointed/nominated for a period of four years along with four Deputy Governors
- **Non-Official Directors** – Ten Directors from various fields and two government Official
Organisation Structure

The Reserve Bank of India comes under the purview of the following Acts:

- Reserve Bank of India Act, 1934
- Public Debt Act, 1944
- Government Securities Regulations, 2007
- Banking Regulation Act, 1949
- Foreign Exchange Management Act, 1999
• Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002
• Credit Information Companies (Regulation) Act, 2005
• Payment and Settlement Systems Act, 2007

**Objectives**

The primary objectives of RBI are to supervise and undertake initiatives for the financial sector consisting of commercial banks, financial institutions and non-banking financial companies (NBFCs).

**Some key initiatives are:**

i. Restructuring bank inspections
ii. Fortifying the role of statutory auditors in the banking system

**Major Functions of RBI**

**Monetary Authority**

• Formulating and implementing the national monetary policy.
• Maintaining price stability across all sectors while also keeping the objective of growth.

**Direct Instruments:**

• CRR
• SLR

**Indirect Instruments:**

**Liquidity Adjustment Facility (LAF):** A liquidity adjustment facility (LAF) is a tool used in monetary policy, primarily by the Reserve Bank of India (RBI), that allows banks to borrow money through repurchase agreements (repos) or for banks to make loans to the RBI through reverse repo agreements.

**Repo/Reverse Repo Rate:** Repo or repurchase rate is the benchmark interest rate at which the RBI lends money to all other banks for a short-term. When the repo rate increases. Reverse Repo Rate (RRR) Reverse Repo rate is the short-term borrowing rate at which RBI borrows money from other banks. The Reserve Bank of India uses this method to reduce inflation when there is excess money in the banking system. Borrowing from RBI becomes more expensive and hence customers or the public bear the outcome of high-interest rates.
Open Market Operation (OMO): Open market operations is a tool that the RBI uses to smoothen liquidity conditions through the year and regulate money supply in the economy. Open market operations is the sale and purchase of government securities and treasury bills by RBI or the central bank of the country. Since 2012, RBI has been using this instrument as a pure LAF, liquidity instrument.

Marginal Standing Facility (MSF): Marginal Standing Facility is a new Liquidity Adjustment Facility (LAF) window created by Reserve Bank of India in its credit policy of May 2011. MSF is the rate at which the banks are able to borrow overnight funds from RBI against the approved government securities.

Bank Rate: A bank rate is the interest rate at which a nation’s central bank lends money to domestic banks, often in the form of very short-term loans. Managing the bank rate is a method by which central banks affect economic activity.

Regulatory and Supervisory

- Set parameters for banks and financial operations within which banking and financial systems function.
- Protect investors interest and provide economic and cost-effective banking to the public.

Foreign Exchange Management

- Oversees the Foreign Exchange Management Act, 1999.
- Facilitate external trade and development of foreign exchange market in India.

Currency Issuer

- Issues, exchanges or destroys currency and not fit for circulation.
- Provides the public adequately with currency notes and coins and in good quality.

Developmental role

- Promotes and performs promotional functions to support national banking and financial objectives.

Related Functions

- Provides banking solutions to the central and the state governments and also acts as their banker.
- Chief Banker to all banks: maintains banking accounts of all scheduled banks.
Banker to Banks

- Enables smooth and swift clearing and settlements of inter-bank transactions.
- Provides efficient means of funds transfer for all banks.
- Enables banks to maintain their accounts with RBI for statutory reserve requirements and maintenance of transaction balances.

Regulatory restrictions on lending

In terms Banking Regulation Act, 1949, RBI provides a framework of the rules, regulations, and instructions with regard to bank lending. Accordingly, it has issued following directions to scheduled commercial banks on statutory and other restrictions on loans and advances.

- A bank cannot grant any loans and advances on the security of its own shares.
- Enter into any commitment for granting any loan or advance to or on behalf of (a) any of its Directors, (b) any firm in which any of its Directors is interested as Partner, Manager, Employee or Guarantor.
- Under section 19 of Banking Regulation Act 1949, a bank cannot hold shares in a company as (a) pledgee or mortgagee in excess 30 percent of paid up of that company or 30 percent of bank’s paid capital and reserves whichever is less. (b) in the management of which Managing Director or Manager of the bank is interested.
- Bank’s aggregate investment in shares, certificate of deposits, bonds etc. shall not exceed the 40 percent of banks owned funds as at the end of previous year.
- A bank cannot grant credit facilities against Certificate of deposits, Term deposits issued by other banks or money market mutual funds.
- Banks shall adhere to selective credit control directives of RBI while releasing loans against sensitive commodities.
- Banks should not sanction a new or additional facility to borrowers appearing in RBI’s list of Wilful defaulters for a period of 5 years from the date of publication of the list by RBI.
- There are certain restrictions on Grant of Loans & Advances or award contracts to Officers and Relatives of Officers of Banks. No officer or any Committee comprising, inter alia, an officer as member, shall, while exercising powers of sanction of any credit facility, sanction any credit facility to his/her relative. Such a facility shall ordinarily be sanctioned only by the next higher sanctioning authority. Credit facilities sanctioned to senior officers of the financing bank should be reported to the Board.

Inclusion of Urban Co-operative banks in the Second Schedule to the Reserve Bank of India Act 1934
The Reserve Bank today allowed urban cooperative banks (UCBs) with total deposits of over Rs 750 crore to graduate to scheduled bank category.

If UCBs fulfill certain listed criteria, it will eligible for inclusion in the second schedule, RBI said in a notification.

All the public sector banks, private sector banks, foreign banks, regional rural banks are part of the second schedule.

As per the government’s notification, with effect from April 01, 2013, only those primary co-operative banks whose demand and time liabilities are not less than Rs 750 crore would be treated as a ‘financial institution’ for the purpose Sub-Clause (iii) of clause (a) of Sub-section (6) of section 42 of RBI Act 1934, i.e, for the purpose of inclusion of UCBs in the Second Schedule of the Reserve Bank of India Act, 1934.

UCBs desirous of seeking inclusion in the schedule should fulfill certain other criteria including continuous net profit for the previous three years, capital adequacy ratio of 12 per cent and gross non-performing assets of less than 5 per cent.

Besides, the bank needs to comply with Cash Reserve Ratio and Statutory Liquidity Ratio requirements and there should be major regulatory and supervisory concerns.

Such UCBs can submit their application along with relevant documents to the Regional Office concerned of Urban Banks Department.

Unit-3: Retail banking, Wholesale and International Banking

Retail Banking

Retail banking, also known as Consumer banking, refers to the offering of banking services to retail customers instead of institutional customers, such as companies, corporations and/or financial institutions.

Today’s Retail banking sector is characterized by three basis features:

- Multiple products (deposits, credit cards, insurance, investments and securities)
- Multiple channels of distribution (call centre, branch, Internet and Kiosk)
- Multiple customer groups (Consumer, small business and corporate)
Retail Products

The Typical products offered in the Indian retail banking segment are:

Retail Deposit Products

- Saving Bank Account
- Recurring Deposit Account
- Current Deposit Account
- Term Deposit Account
- Zero Balance Account for salaried class people
- Basis Saving Bank Deposit Account (BSBDA) for the common man
- Senior Citizen Deposit Account, etc.

Retail Loan Products

- Home loans to resident Indians for purchase of land and construction of residential house/purchase of ready built house/for repairs and renovation of an existing house.
- Home loans to Non-Resident Indians
- Auto loans- for purchase of new/used four-wheelers and two-wheelers
- Consumer loans- for purchase of white goods and durables
- Personal loans- for purchase of jewels, for meeting domestic consumption etc.
- Educational loans- for pursuing higher education both in India and abroad
- Trade related advances to individuals- for setting up business, retail trade etc.
- Crop loans to agricultural farmers
- Credit cards etc.

Retail Services

- Safe Deposit lockers
- Depository services
- Bancassurance Products etc.

Drives of Retail Banking in India

Appreciable Growth Rate
Economic prosperity and the following escalation in purchasing power have given a boost to a consumer boom. **From 1992 India's economy nurtured at an average rate of 6.8% and continue to grow at a comfortable rate.**

**Changes in demographic profile**

Change in consumer demographics shows vast potential for growth in consumption both qualitatively and quantitatively. It has been forecasted that BRIC nations has bright future, in which India's demographic advantage will have a key role.

**Today the average age of borrower has dropped from 40 years about five years ago to, now, an estimated 30 years.** In the future the average age is predicted to reduce further and hence it will indicate well for the housing finance market in terms of increased borrowers.

**Decline in Average house costs**

There has been a decline in **average house cost to annual income ratio by 4-5 times from high of 11-14 a decade ago.** This has also lead to an affordable EMI as a percentage of monthly income.

**Aggressive Lending by Banks**

Banks found a respite in housing loans as a means to deploy funds on back of lull in credit off take by the corporate segment. To add to that the segment called for lower risk weights, provided attractive spread and has lower level of delinquency.

**Tax Breaks**

The recent budgets provided for several tax and fiscal enticements for deploying funds in the housing sector. The Reserve Bank of India (RBI) had also addressed commercial banks to allocate at **least 3 per cent of their incremental deposits in housing loans.** At the same time the policy of the Reserve Bank of India about the inclusion of Mortgage backed securities as a part of priority sector lending for banks and reducing the risk-weight on home loans from 100 per cent to 50 per cent made the sector more attractive for the banks.

**Others growth Drivers**

Technological factors played a chief role. Convenience banking in the form of debit cards, internet and phone banking, anywhere and anytime banking has attracted many new consumers into the banking field. **Technological innovations connecting to increasing use of credit / debit cards, ATMs, direct debits and phone banking** has added to the development of retail banking in India.

Treasury income of the banks, which had reinforced the bottom lines of banks for the past few years, has been on the decline during the last two years. In such a situation, retail business offers a good vehicle of profit maximization.
Drop in interest rates have also backed the growth of retail credit by creating the demand for such credit.

**Wholesale and International Banking**

**What is Wholesale Banking**

Wholesale banking refers to the complete banking solution provided by the merchant banks to the large scale business organizations and the government agencies or institutions. To avail the facility of wholesale banking, the companies need to possess a strong financial statement and operate on a large scale. Usually, multinational companies are the clients of wholesale banking.

**Wholesale Banking Product**

**Fund-based Services**

(i) Term lending  
(ii) Short –term Finance  
(iii) Working Capital Finance  
(iv) Bill Discounting  
(v) Structured Finance  
(vi) Export Credit

**Non-fund based Services**

(i) Bank Guarantee  
(ii) Letter of credit  
(iii) Collection of Bills and Documents

**Value-added services**

(i) Cash Management services  
(ii) Channel Financial  
(iii) Vendor financing  
(iv) Real time Gross settlement  
(v) Corporate Salary Accounts  
(vi) Syndication Services  
(vii) Forex Desk  
(viii) Money Market Desk  
(ix) Derivatives Desk  
(x) Employees Trust  
(xi) Tax collection  
(xii) Bankers to Right/Public Issue  
(xiii) National Electronic Funds Transfer (NEFT)  
(xiv) Electronic Clearing Service (ECS)

**Internet Banking Services**

(i) Payment Gateway Services  
(ii) Corporate Internet Banking  
(iii) Supply Chain Management  
(iv) Supply Chain Partners

**What is International Banking**

An international bank is a financial entity that offers financial services, such as payment accounts and lending opportunities, to foreign clients. These foreign clients can be individuals and companies, though every international bank has its own policies outlining with whom they do business.

**Example:** Suppose Microsoft, an American company is functioning in London. It is in need of funds to meet its working capital requirements. In such scenario, Microsoft can avail the banking services in form of loans, overdraft or any other financial service through banks in
London. Here, the residential bank of London shall be giving its services to an American company.

**Need of Exporters in International Banking**

- Export Packing Credit
- Export Bill Negotiation
- Export Bill Purchase and Discounting
- Export Bill Collection Services
- Bank Guarantees
- Rupees Advance against Export Bills
- Export Latter of Credit Advising
- Export Latter of Credit Confirmation
- Supplier’s Credit

**Need of Importers in International Banking**

- Import Collection Bill Services
- Direct Import Bills
- Advance Payment towards Imports
- Import letters of Credit
- Arranging for Buyer’s and Supplier’s Credit
- Bank Guarantees

**Remittance Service**

**EEFC Account Service:** Bank provide facilities to maintain an Exchange Earners Foreign Currency in all permitted currencies.

**Receipt of foreign Inward Remittances Services:** Banks receive from aboard and credit them to the Indian beneficiaries accounts.

**Payment Services to Abroad (Outward Remittances):** Banks as Authorised Dealers in foreign Exchange provide remittance facilities in foreign to any country for any permitted Purpose up the limits permitted by RBI.

**UNIVERSAL Banking**

**What is a Universal bank? Definition and examples**
A Universal bank is a bank that combines the three main services of banking under one roof. The three services are **wholesale banking, retail banking, and investment banking**. In other words, it is a retail bank, a wholesale bank, and also an investment bank. As well as being able to offer an all-encompassing service, universal banks can reap the synergies that exist when they operate in the three services simultaneously.

For example: BNP Paribas, Deutsche Bank, Morgan Stanley, and JP Morgan Chase are universal banks. Citigroup, Bank of America, UBS, Credit Suisse, HSBC, and Barclays are also universal banks.

**Universal Banking in India**

Basically Universal Banking is like a one stop shop where all financial products are available for customers. From core banking to asset management, wealth management to risk management, mutual funds to Retail, home loans and personal loans.

Previously RBI has encouraged universal banking in India, however, with the 2008 financial market collapse and too big too fail approach, the concept and idea of getting into different businesses which aren't profitable is not gathering steam.

From an Indian perspective I would say ICICI Bank and SBI are India centered , would be considered as universal bank operating in India.

**American Depository Receipt and Global Depository Receipt**

**Definition of ADR**

American Depository Receipt (ADR), is a negotiable certificate, issued by a US bank, denominated in US$ representing securities of a foreign company trading in the United States stock market. The receipts are a claim against the number of shares underlying. ADR’s are offered for sale to American investors. By way of ADR, the US investors can invest in non-US companies. The dividend is paid to the ADR holders, is in US dollars.

**Definition of GDR**

GDR or Global Depository Receipt is a negotiable instrument used to tap the financial markets of various countries with a single instrument. The receipts are issued by the depository bank, in more than one country representing a fixed number of shares in a foreign company. The holders of GDR can convert them into shares by surrendering the receipts to the bank.

**Comparison Chart**

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<th>BASIS FOR COMPARISON</th>
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<th>GDR</th>
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<tr>
<td>BASIS FOR COMPARISON</td>
<td>ADR</td>
<td>GDR</td>
</tr>
<tr>
<td>----------------------</td>
<td>---------------------------------------------------------------------</td>
<td>---------------------------------------------------------------------</td>
</tr>
<tr>
<td>Acronym</td>
<td>American Depository Receipt</td>
<td>Global Depository Receipt</td>
</tr>
<tr>
<td>Meaning</td>
<td>ADR is a negotiable instrument issued by a US bank, representing non-US company stock, trading in the US stock exchange.</td>
<td>GDR is a negotiable instrument issued by the international depository bank, representing foreign company's stock trading globally.</td>
</tr>
<tr>
<td>Relevance</td>
<td>Foreign companies can trade in US stock market.</td>
<td>Foreign companies can trade in any country's stock market other than the US stock market.</td>
</tr>
<tr>
<td>Issued in</td>
<td>United States domestic capital market.</td>
<td>European capital market.</td>
</tr>
<tr>
<td>Listed in</td>
<td>American Stock Exchange such as NYSE or NASDAQ</td>
<td>Non-US Stock Exchange such as London Stock Exchange or Luxemburg Stock Exchange.</td>
</tr>
<tr>
<td>Negotiation</td>
<td>In America only.</td>
<td>All over the world.</td>
</tr>
<tr>
<td>Disclosure Requirement</td>
<td>Onerous</td>
<td>Less onerous</td>
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<tr>
<td>Market</td>
<td>Retail investor market</td>
<td>Institutional market</td>
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</tbody>
</table>

**Participatory Notes**

Participatory notes also called P-Notes are offshore derivative instruments with Indian shares as underlying assets. These instruments are used for making investments in the stock markets. However, they are not used within the country. They are used outside India for making investments in shares listed in the Indian stock market. That is why they are also called offshore derivative instruments.

Participatory notes are issued by brokers and FIIs registered with SEBI. The investment is made on behalf of these foreign investors by the already registered brokers in India. For
example, Indian-based brokerages buy India-based securities and then issue participatory notes to foreign investors. Any dividends or capital gains collected from the underlying securities go back to the investors.

**Why are participatory notes used?**

Investing through P-Notes is very simple and hence very popular amongst FIIs. Overseas investors who are not registered with SEBI have to go through a lot of scrutiny, such as know-your-customer norms, before investing in Indian shares. To avoid these hurdles, foreign investors take this route. Also, since the end beneficiary of these notes is not disclosed, many investors who want to remain anonymous use it. These instruments aid investors who do not want to register with SEBI and reveal their identities to take positions in the Indian market.

**Advantages of participatory notes**

**Anonymity:** Any entity investing in participatory notes is not required to register with SEBI, whereas all FIIs have to compulsorily get registered. It enables large hedge funds to carry out their operations without disclosing their identity.

**Ease of trading:** Trading through participatory notes is easy because they are like contract notes transferable by endorsement and delivery.

**Tax saving:** Some of the entities route their investment through participatory notes to take advantage of the tax laws of certain preferred countries.

**Disadvantages of P-notes**

Indian regulators are not very happy about participatory notes because they have no way to know who owns the underlying securities. It is alleged that a lot of unaccounted money made its way to the country through the participatory note route.

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**Unit 4- Role of Money Markets, Debt Markets & Forex Market**

**Call Money Market**

The money market is a market for short-term financial assets that are close substitutes of money. The most important feature of a money market instrument is that it is liquid and can be turned into money quickly at low cost and provides an avenue for equilibrating the short-term surplus funds of lenders and the requirements of borrowers.
• The loans are of short-term duration varying from 1 to 14 days, are traded in call money market
• The money that is lent for one day in this market is known as "Call Money"
• It exceeds one day (but less than 15 days) it is referred to as "Notice Money"
• Term Money refers to Money lent for 15 days or more in the Inter Bank Market.

Participants in the Market

Participants in the call money market are banks and related entities specified by the RBI. Scheduled commercial banks (excluding RRBs), co-operative banks (other than Land Development Banks) and Primary Dealers (PDs), are permitted to participate in call/notice money market both as borrowers and lenders. As per the new regulations, Payment Banks are also allowed to participate in CMM as both lenders and borrowers.

Functioning of the Call Money Market

Loans are availed through auction/negotiation. The auction is made on interest rate. Highest bidder (who is ready to give higher interest rate) can avail the loan. Average interest rate in the call market is called call rate. Dealing in call money is done through the electronic trading platform called Negotiated Trading System (NDS). This call money rate is an important variable for the RBI to assess the liquidity situation in the economy. The CMM is known as the most sensitive segment of the financial system.

Borrowing Limits

Scheduled commercial banks are permitted to borrow to the extent of 125% of their capital funds in the call/notice money market, however their fortnightly average borrowing outstanding should not exceed more than 100% of their capital funds (Tier I and Tier II capital). At the same time SCBs can lend to the extent of 50% of their capital funds on any day, during a fortnight, but average fortnightly outstanding lending should not exceed 25% of their capital funds. Co-operative Banks are permitted to borrow up to 2% of their aggregate deposits as at the end of March of the previous financial year in the Call/ Notice money market.

There is no limit for lending. Primary Dealers can borrow on an average in a reporting fortnight up to 225% of the total Net Owned funds (NOF) as at the end, March of the previous financial year and lend on an average in a reporting fortnight up to 25% of their NOF.

Money Market Instruments

Treasury Bills (T-Bills)

Issued by the Central Government, Treasury Bills are known to be one of the safest money market instruments available. However, treasury bills carry zero risk. I.e. are zero risk
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Online Mock Tests

instruments. Therefore, the returns one gets on them are not attractive. Treasury bills come with different maturity periods like 3-month, 6-month and 1 year and are circulated by primary and secondary markets. Treasury bills are issued by the Central government at a lesser price than their face value. The interest earned by the buyer will be the difference of the maturity value of the instrument and the buying price of the bill, which is decided with the help of bidding done via auctions.

Note: Currently, there are 3 types of treasury bills issued by the Government of India via auctions 91-day, 182-day and 364-day treasury bills.

Certificate of Deposits (CDs)

A Certificate of Deposit or CD, functions as a deposit receipt for money which is deposited with a financial organization or bank. However, a Certificate of Deposit is different from a Fixed Deposit Receipt in two aspects. The first aspect of difference is that a CD is only issued for a larger sum of money. Secondly, a Certificate of Deposit is freely negotiable. First announced in 1989 by RBI, Certificate of Deposits have become a preferred investment choice for organizations in terms of short-term surplus investment as they carry low risk while providing interest rates which are higher than those provided by Treasury bills and term deposits. CDs are also issued at a discounted price and their tenor ranges between a span of 7 days up to 1 year. However, banks issue Certificates of Deposits for durations ranging from 3 months, 6 months and 12 months. They can be issued to individuals (except minors), trusts, companies, corporations, associations, funds, non-resident Indians, etc.

Commercial Papers (CPs)

Commercial Papers can be compared to an unsecured short-term promissory note which is issued by highly rated companies with the purpose of raising capital to meet requirements directly from the market. CPs usually feature a fixed maturity period which can range anywhere from 1 day up to 270 days. Commercial Papers promise higher returns as compared to treasury bills and are automatically not as secure in comparison. Commercial papers are actively traded in secondary market.

(i) The tangible net worth of the company, as per the latest audited balance sheet, is not less than Rs.4cr.

(ii) Company has been sanctioned working capital limit by banks or all India financial institutions.

(iii) The borrowal account of the company is classified as a Standard Asset by the financing Banks and institutions.

Repurchase Agreements (Repo)
Repurchase Agreements, also known as Reverse Repo or simply as Repo, loans of a short duration which are agreed upon by buyers and sellers for the purpose of selling and repurchasing. These transactions can only be carried out between RBI approved parties. Repo / Reverse Repo transactions can be done only between the parties approved by RBI. Transactions are only permitted between securities approved by the RBI like treasury bills, central or state government securities, corporate bonds and PSU bonds.

**Banker’s Acceptance (BA)**

Banker’s Acceptance or BA is basically a document promising future payment which is guaranteed by a commercial bank. Similar to a treasury bill, Banker’s Acceptance is often used in money market funds and specifies the details of the repayment like the amount to be repaid, date of repayment and the details of the individual to which the repayment is due. Banker’s Acceptance features maturity periods ranging between 30 days up to 180 days.

**Collateralized Borrowing And Lending Obligation (CBLO):**

CBLOs were developed by the Clearing Corporation of India (CCIL) and Reserve Bank of India (RBI). It is a money market instrument that represents an obligation between a borrower and a lender as to the terms and conditions of the loan. The details of the CBLO include an obligation for the borrower to repay the debt at a specified future date and an expectation of the lender to receive the money on that future date, and they have a charge on the security that is held by the CCIL. CBLOs are used by those who are heavily restricted or have been phased out of the interbank call money market.

**Debt Capital Market**

The Indian debt market is a market meant for trading (i.e. buying or selling) fixed income instruments. Fixed income instruments could be securities issued by Central and State Governments, Municipal Corporations, Govt. Bodies or by private entities like financial institutions, banks, corporates, etc. Simply put, a bond/debt can be defined as a loan in which an investor is the lender. The issuer of the bond pays the investor interest (at a predetermined rate and schedule) in return for the amount invested. The Indian debt market offers a variety of debt instruments, offered by the Government and non-Government entities. The factors that are propelling the growth of the market are:

- Introduction of new instruments
- Increased liquidity
- Deregulation of interest rates
- Improved settlement systems

The debt market in India comprises broadly two segments, viz.,
• Government Securities Market and
• Corporate Debt Market.

The latter is further classified as Market for:
• PSU Bonds and
• Private Sector Bonds.

The corporate bond market, broadly comprises of corporate sector raising debt through public issuance in capital market and also through private placement basis.

**FOREX (Foreign Exchange Market)**

The foreign exchange market is a global online network where traders buy and sell currencies. It has no physical location and operates 24 hours a day.

**Interbank Market**

The interbank market is a network of banks that trade currencies with each other. Each has a currency trading desk called a dealing desk. They are in contact with each other continuously. That process makes sure exchange rates are uniform around the world.

The minimum trade is 1 million of the currency being traded. Most trades are much larger, between 10 million and 100 million in value. As a result, exchange rates are dictated by the interbank market.

**LIBOR**

LIBOR, which is an acronym of London Interbank Offer Rate, refers to the interest rate that UK banks charge other financial institutions for short-term loans. The loan maturities vary from one day to one year. LIBOR acts as a benchmarking base for short-term interest rates for prices of securities such as currency swaps, interest rate swaps, or mortgages.

LIBOR comprises seven maturities, quoted for deposits of each of five major currencies – CHF (Swiss Franc), EUR (Euro), GBP (Pound Sterling), JPY (Japanese Yen), and USD (US Dollar).

**MIBOR**

MIBOR is the acronym for Mumbai Interbank Offer Rate, the yardstick of the Indian call money market. It is used as a reference rate for floating rate notes, corporate debentures, term deposits, interest rate swaps and forward rate agreements. The pricing of overnight indexed swaps, a type of overnight interest rate swap used for hedging interest rate risk is based on overnight MIBOR.
Based on the recommendation of the Committee for the Development of Debt Market, the National Stock Exchange (NSE) launched the Mumbai Interbank Offer Rate (MIBOR) and Mumbai Interbank Bid Rate (MIBID) in June, 1998. Subsequently, the NSE developed a benchmark rate for the term money market, like the 14-day, 1-month and 3-month MIBOR.

**Foreign Exchange Management Act (FEMA)**

The Foreign Exchange Management Act (FEMA) was an official Act that consolidated and amended laws governing foreign exchange in India. The primary objective of FEMA act was “facilitating external trade and payments and promoting the orderly development and maintenance of foreign exchange market in India”. FEMA was enacted by the Parliament of India in the winter session of 1999 to replace the Foreign Exchange Regulation Act (FERA) of 1973.

**Important FEMA Guidelines and Features**

Most significantly, FEMA regarded all forex-related offences as civil offences, whereas FERA regarded them as criminal offences. Additionally, there were other important guidelines such as:

- FEMA did not apply to Indian citizens who resided outside India. This criterion was checked by calculating the number of days a person resided in India during the previous financial year (182 days or more to be a resident). It was noted that even an office, a branch, or an agency could be a ‘person’ for the purpose of checking residency.
- FEMA authorized the central government to impose restrictions on and supervise three things – payments made to any person outside India or receipts from them, forex, and foreign security deals.
- It specified the areas around acquisition/holding of forex that required specific permission of the Reserve Bank of India (RBI) or the government.
- FEMA put foreign exchange transactions into two categories – capital account and current account. A capital account transaction altered the assets and liabilities outside India or inside India but of a person resident outside India. Thus, any transaction that changed overseas assets and liabilities for an Indian resident in a foreign country, or vice versa, was classified as a capital account transaction. Any other transaction fell into the current account category.

**Important Provisions of the Act**
**Section 3:** Prohibits dealings in foreign exchange except through and authorized person. This section states that on person can, without general or special permission of the RBI:

(i) Deal in or transfer any foreign exchange or foreign securities to any person not being an authorized person.

(ii) Make any payment to or for the credit of any person resident outside India in any manner.

(iii) Receive otherwise through an authorized person, any payment by order or on behalf of any person resident outside India in any manner.

**Section 4:** Restrains any person resident in India from acquiring, holding, owning, possessing or transferring any foreign exchange, foreign security or any immovable property situated outside India except as specifically provided in the Act. The term “foreign exchange” and “foreign security” are defined in sections 2(n) and 2(o) respectively of the Act. The Central govt. has made Foreign Exchange Management Rules 2000.

**Section 6:** Deals with Capital account transactions. This section allows a person to draw or sell foreign exchange form or to an authorized person for a capital account transaction.

**Section 7:** Deals with export of goods and services. Every exporter is required to furnish to the RBI or any other authority, a declaration, etc, regarding full export value.

**Section 8:** Cast the responsibility on the person resident in India who have any amount of foreign exchange due or accrued in their favour to get the same realized and repatriated to India within the specific period and the manner specified by RBI.

**Section 10 and 12:** Deal with duties and liabilities of the authorized person.

**Section 13 and 15:** of the Act Deal with penalties and enforcement of the orders of Adjudicating Authority as well power to compound contraventions under the Act.

**Section 36 and 37:** Pertains to the establishment of Directorate of Enforcement and the power the investigate the violation of any provisions of Act, rule regulation, notification directions or order issued in exercise of the power under this Act.

**Unit 5- Role and Function of Capital Market and SEBI**

**Capital Market**

**What is Capital Market**

Capital Market, is used to mean the market for long term investments, that have explicit or implicit claims to capital. Long term investments refers to those investments whose lock-in period is greater than one year.
In the capital market, both equity and debt instruments, such as equity shares, preference shares, debentures, zero-coupon bonds, secured premium notes and the like are bought and sold, as well as it covers all forms of lending and borrowing.

**Functions of Capital Market**

- Mobilization of savings to finance long term investments.
- Facilitates trading of securities.
- Minimization of transaction and information cost.
- Encourage wide range of ownership of productive assets.
- Quick valuation of financial instruments like shares and debentures.
- Facilitates transaction settlement, as per the definite time schedules.
- Offering insurance against market or price risk, through derivative trading.
- Improvement in the effectiveness of capital allocation, with the help of competitive price mechanism.

**Types of Capital Market**

- Primary Market
- Secondary Market

**Primary Market:** Otherwise called as **New Issues Market**, it is the market for the trading of new securities, for the first time. It embraces both initial public offering and further public offering. In the primary market, the mobilisation of funds takes place through prospectus, right issue and private placement of securities.

**Origination/ Initial Public Offerings:** In a public offering, the issuer makes an offer for the new investor to enter is shareholding family. Origination is referred to as examine, evaluate, and process new project proposals in the primary market. It begins prior to an issue is present in the market. It is done with the help of commercial bankers.

**Further Public offering (FPO):** An FPO is made when an already listed company makes either a fresh issue of securities to the public or an offer for sale to the public, through an offer document. An offer for sale in such a scenario is allowed.

**Distribution:** For the success of issue, brokers and dealers are given job distribution who directly contact with investors.

**Right Issue (IR):** Right Issue is when listed company propose to issue fresh securities to its existing shareholders as on a recoded data.
Secondary Market: Secondary Market can be described as the market for old securities, in the sense that securities which are previously issued in the primary market are traded here. The trading takes place between investors, that follows the original issue in the primary market. It covers both stock exchange and over-the-counter market.

The following are the main financial products/instruments dealt in the secondary Market:

**Equity:** Equity is ownership of assets that may have debts or other liabilities attached to them. Equity is measured for accounting purposes by subtracting liabilities from the value of an asset.

Equity = Assets – Liabilities

Various type of Equity:

- Equity share
- Right Issue/Right Share
- Bonus share
- Preferred stock/Preference share
- Cumulative Preference share
- Cumulative Convertible preference share
- Participating Preference share

**Government securities:** Popularly known as G-Secs, are issued by Reserve Bank of India (RBI) on behalf of the central or state governments. These securities are absolutely risk-free and guaranteed by the government. Generally, investors think that G-Secs are meant for banks, financial institutions and large corporations, but as small investors, every individual can also make an investment.

**Debentures:** Debenture is a medium- to long-term (Half yearly) debt instrument used by large companies to borrow money, at a fixed rate of interest.

**Bond:** A bond is a negotiable certificate evidencing indebtedness. It is normally unsecured. A Bond (debt security) security is generally issued by a company, municipality or a government agency.

**Coupon Bond:** These are normal bonds on which the issuer pays the investor/holder interest at the predetermined rate (Known as coupon) at agreed intervals. Normally twice a year. The maturity if the bond is known by the period for which it is issued.

**Zero Coupon Bond:** A bond issued at a discount and repaid at a face value is called a Zero Coupon Bond.
Convertible Bond: A bond giving the investor the option to convert the bond into equity at a fixed conversion price is referred to as a Convertible Bond.

**Applications Supported by Blocked Amount (ASBA)**

**What is ASBA?**

ASBA [Applications Supported by Blocked Amount] is a system of blocking the funds of applicants of IPOs in their respective accounts and release the funds to the Company from such blocked accounts only after the allotment to the extent of allotment made and unblock the remaining amount in the account.

**Features of ASBA**

- ASBA IPO Applications will be received at the Designated Branches
- On receipt of ASBA applications, the Branches will mark lien in the specific account of the customer to the extent of amount applied for through the system.
- This amount gets blocked in the account and money will however continue to remain in the account of the customer till the date of allotment.
- The details of the IPO application and the amount blocked would be passed to the Exchange and Registrar through the system.
- The amount held in the account of the customer would continue to earn interest as applicable to the account.
- Any withdrawals or debits to the extent of blocked amount are not permitted in the account till the finalisation of allotment of shares. However, balance in the account over and above the blocked amount is free from any charge.
- When the Registrar completes the process of allotment, based on the instructions released from the Registrars, the system will debit the account to extent of the allotment and will unblock the account.

**Advantages of ASBA**

- No issue of Cheque / Purchase of DDs and hence no clearing
- Applicant can make 5 applications from a single deposit account
- Money lies in the a/c and earns interest
- Lien marked only to the extent of the bid amount
- Money to be appropriated on allotment to the extent of shares allotted
• No physical refund involved, no hassles of lost / delayed refunds
• Shorter turnaround time for entire IPO processing.

Qualified Institutional Placement

A Qualified Institutional Placement is a capital raising tool wherein a listed company can issue equity shares, fully and partly convertible debentures, or any security other than warrants that are convertible into equity shares. But unlike in an IPO or an FPO, only institutions or qualified institutional buyers can participate in a QIP.

Restrictions on Allotment

Certain restrictions have been imposed wherein it is mentioned that in any whatsoever, the Qualified Institutional Placement cannot be made to the Promoter or any of his relatives or to any manner who may be related to the promoter in any way. Also a Minimum number of of QIBs to whom shares are allotted shall not be less than Two, in cases where the issue size is <= Rs.250 crores.

Five, where the issue size is >= Rs.250 crores.

Advantages of a QIP

• This mode of qualified institutional placement is essentially the most expeditious method by which capital can be raised without undergoing any cumbersome process. Generally, by other methods like FPO and rights issues, it takes a lot of time and money to undergo the documentation and approval.

• It saves ancillary expenses which otherwise are involved when securities are issued by some any other mode.

• In cases where a company cannot directly buy from the market a large stake as it might create market volatility, in this way issuing shares by increasing capital is one of the ways to attract investors.

• Better bargains take place by means of QIP, as it gives the opportunity to raise and purchase as well at better-bargained costs.

• Finally, in case of QIP the formula to arrive at a floor price, is the average stock price of the last two weeks, but in case of preferential allotment, it is the average stock price of last six months from the cut-off date. The cut-off date for calculation of average stock price is the date which is 30 days prior to the date when shareholders“ meeting is held and the decision of fresh equity issue is taken.
SEBI – Securities and Exchange Board of India

What is SEBI?

SEBI is a statutory regulatory body established on the 12th of April, 1992 SEBI Act 1992. It monitors and regulates the Indian capital and securities market while ensuring to protect the interests of the investors formulating regulations and guidelines to be adhered to. The head office of SEBI is in Bandra Kurla Complex, Mumbai.

Functions of SEBI

- SEBI is primarily set up to protect the interests of investors in the securities market.
- It promotes the development of the securities market and regulates the business.
- SEBI provides a platform for stockbrokers, sub-brokers, portfolio managers, investment advisers, share transfer agents, bankers, merchant bankers, trustees of trust deeds, registrars, underwriters, and other associated people to register and regulate work.
- It regulates the operations of depositories, participants, custodians of securities, foreign portfolio investors, and credit rating agencies.
- It prohibits inner trades in securities, i.e. fraudulent and unfair trade practices related to the securities market.
- It ensures that investors are educated on the intermediaries of securities markets.
- It monitors substantial acquisitions of shares and take-over of companies.
- SEBI takes care of research and development to ensure the securities market is efficient at all times.

Authority and Power of SEBI

Power of SEBI to Regulate or Prohibit Issue of Prospectus, offer Document or Advertisement Soliciting Money for issue of Securities: Without prejudice to the provisions of the Companies Act, 1956 (1 of 1956), SEBI may, for the protection of investors.

Quasi-Judicial: SEBI has the authority to deliver judgements related to fraud and other unethical practices in terms of the securities market. This helps to ensure fairness, transparency, and accountability in the securities market.

Quasi-Executive: SEBI is empowered to implement the regulations and judgements made and to take legal action against the violators. It is also authorised to inspect Books of accounts and other documents if it comes across any violation of the regulations.
Quasi-Legislative: SEBI reserves the right to frame rules and regulations to protect the interests of the investors. Some of its regulations consist of insider trading regulations, listing obligation, and disclosure requirements. These have been formulated to keep malpractices at bay.

Despite the powers, the results of SEBI’s functions still have to go through the Securities Appellate Tribunal and the Supreme Court of India.

**Registration of stock brokers, sub-brokers, share transfer agents, etc.**

- No stock broker, sub-broker, share transfer agent, banker to an issue, trustee of trust deed, registrar to an issue, merchant banker, underwriter, portfolio manager, investment adviser and such other intermediary who may be associated with securities market shall buy, sell or deal in securities except under, and in accordance with, the conditions of a certificate of registration obtained from the Board in accordance with the regulations made under this Act:

- Provided further that any certificate of registration, obtained immediately before the commencement of the Securities Laws (Amendment) Act, 1995, shall be deemed to have been obtained from the Board in accordance with the regulations providing for such registration.

- Provided that a person buying or selling securities or otherwise dealing with the securities market as a depository, participant, custodian of securities, foreign institutional investor or credit rating agency immediately before the commencement of the Securities Laws (Amendment) Act, 1995, for which no certificate of registration was required prior to such commencement, may continue to buy or sell securities or otherwise deal with the securities market until such time regulations are made under clause (d) of sub-section (2) of section 30.

- Provided that any person sponsoring or causing to be sponsored, carrying or causing to be carried on any venture capital funds or collective investment schemes operating in the securities market immediately before the commencement of the Securities Laws (Amendment) Act, 1995, for which no certificate of registration was required prior to such commencement, may continue to operate till such time regulations are made under clause (d) of sub-section (2) of section 30.
Unit 6- Factoring, Forfaiting Services and Off-Balance Sheet items

Factoring

Factoring implies a financial arrangement between the factor and client, in which the firm (client) gets advances in return for receivables, from a financial institution (factor). It is a financing technique, in which there is an outright selling of trade debts by a firm to a third party, i.e. factor, at discounted prices.

Process of Factoring

In finer terms factoring is a relationship between the factor and the client, in which the factor purchases the client’s account receivables and pay up to 80% (sometimes 90%) of the sum immediately, at the time of entering into the agreement. The factor pays the balance sum, i.e. 20% of the amount which includes finance cost and operating cost, to the client when the customer pays the obligation.

- Borrowing company or the client sells the book debts to the lending institution (factor).
- Factor acquires the receivables and extend money against the receivables, after deducting and retaining the following sum, i.e. an adequate margin, factor’s commission and interest on advance
- Collection from the customer is forwarded by the client to the factor and in this way, the advance is settled.

Other services are also provided by the factor which includes:

- Finance
- Collection of debts
- Maintenance of debts
- Protection of Credit Risk
- Maintenance of debtors ledger
- Debtors follow-up
• Advisory services
• The factor gets control over the client’s debtors, to whom the goods are sold on credit or credit is extended and also monitors the client’s sales ledger.

Types of Factoring

Recourse and Non-recourse Factoring: In this type of arrangement, the financial institution, can resort to the firm, when the debts are not recoverable. So, the credit risk associated with the trade debts are not assumed by the factor.

On the other hand, in non-recourse factoring, the factor cannot recourse to the firm, in case the debt turn out to be irrecoverable.

Disclosed and Undisclosed Factoring: The factoring in which the factor’s name is indicated in the invoice by the supplier of the goods or services asking the purchaser to pay the factor, is called disclosed factoring.

Conversely, the form of factoring in which the name of the factor is not mentioned in the invoice issued by the manufacturer. In such a case, the factor maintains sales ledger of the client and the debt is realized in the name of the firm. However, the control is in the hands of the factor.

Domestic and Export Factoring: When the three parties to factoring, i.e. customer, client, and factor, reside in the same country, then this is called as domestic factoring.

Export factoring, or otherwise known as cross-border factoring is one in which there are four parties involved, i.e. exporter (client), the importer (customer), export factor and import factor. This is also termed as the two-factor system.
Advance and Maturity Factoring: In advance factoring, the factor gives an advance to the client, against the uncollected receivables.

In maturity factoring, the factoring agency does not provide any advance to the firm. Instead, the bank collects the sum from the customer and pays to the firm, either on the date on which the amount is collected from the customers or on a guaranteed payment date.

Advantages of Factoring

- Factoring replaces high cost market credit and enables purchases on cash basis for availing cash discount.
- The Customer gets instant finance against each invoice.
- Low margin (Up to 20%) thereby improvement cash flow.
- The customer gets large credit/grace period
- Each invoice is following up for payment by the factor on the due date and thereafter.
- MIS reports and sales ledger administration is totally taken care of by the factor.
- Factoring accelerates receivables turnover and improves operating cycle, resulting in more production, larger scale, higher profits and increased ROI.

Forfaiting Services

Forfaiting is a mechanism, in which an exporter surrenders his rights to receive payment against the goods delivered or services rendered to the importer, in exchange for the instant cash payment from a forfaiter. In this way, an exporter can easily turn a credit sale into cash sale, without recourse to him or his forfaiter.

Process
**Advantage of Forfaiting**

Forfaiting provide a flexible, creative alternative to traditional international trade financing methods and is particularly useful for transactions with buyers in developing nations. The following are the advantages of forfaiting to the exporters:

(i) **Forfaiting provided 100% financing** - without recourse and not occupying exporter’s credit line. This is to say once the exporter obtains the financed fund, he will be exempted from the responsibility to repay the debt.

(ii) **Forfaiting improves cash flow of the exporter** - by converting receivables into current cash inflow and it is beneficial to the exporter to improve his liquidity and his ability to improve further the fund raising capability.

(iii) **Forfaiting saves administration cost** - by using forfaiting, the exporter will be freed from the management of the receivables. The relative costs, as a result, will be reduced greatly.

(iv) **Forfaiting increase trade opportunity** - with forfaiting, the exporter is able to grant credit to his buyer freely and thus, be more competitive in the market.

**Comparison Chart**
<table>
<thead>
<tr>
<th>BASIS FOR COMPARISON</th>
<th>FACTORING</th>
<th>FORFAITING</th>
</tr>
</thead>
<tbody>
<tr>
<td>Meaning</td>
<td>Factoring is an arrangement that converts your receivables into ready cash and you don't need to wait for the payment of receivables at a future date.</td>
<td>Forfaiting implies a transaction in which the forfaite purchases claims from the exporter in return for cash payment.</td>
</tr>
<tr>
<td>Maturity of receivables</td>
<td>Involves account receivables of short maturities.</td>
<td>Involves account receivables of medium to long term maturities.</td>
</tr>
<tr>
<td>Goods</td>
<td>Trade receivables on ordinary goods.</td>
<td>Trade receivables on capital goods.</td>
</tr>
<tr>
<td>Finance up to</td>
<td>80-90%</td>
<td>100%</td>
</tr>
<tr>
<td>Type</td>
<td>Recourse or Non-recourse</td>
<td>Non-recourse</td>
</tr>
<tr>
<td>Cost</td>
<td>Cost of factoring borne by the seller (client).</td>
<td>Cost of forfaiting borne by the overseas buyer.</td>
</tr>
<tr>
<td>Negotiable Instrument</td>
<td>Does not deals in negotiable instrument.</td>
<td>Involves dealing in negotiable instrument.</td>
</tr>
<tr>
<td>Secondary market</td>
<td>No</td>
<td>Yes</td>
</tr>
</tbody>
</table>

**OFF-BALANCE SHEET ITEM**

Also known as Off-Balance sheet items, Off-Balance sheet assets or liabilities, and Incognito Leverage. They are either a liability or an asset which are not shown on a company’s/Bank balance sheet as the business is not a legal owner of the respective item.
Off-Balance sheet items are generally shown in the notes to accounts along with the financial statements. These assets and liabilities may be used by a company/Bank; however, the legal ownership may or may not belong to them. In this case, the consumption of assets and payment of liabilities may ultimately be an indirect responsibility.

The term is very common with asset management companies, brokerage firms, wealth managers, etc. In this case, the assets being managed by firms do not belong to them but to the clients, so they are not recorded on the balance sheet.

There are item Include:

(a) Direct Credit substitutes, e.g. general guarantees of indebtedness (including stand by CLs serving as financial guarantees for loans and securities) and acceptance (including endorsements with the character of acceptance).

(b) Certain transaction-related contingent item (e.g performance bonds, bid bonds warranties and standby LCs related to particular transactions).

(c) Short-term self liquidating trade-related contingencies (such as documentary credits collateralized by the underlying shipment)

(d) Take-out finance in the books of taking over institution

(i) Unconditional take-out finance

(ii) Conditional take-out finance

(iii) Non-funded exposures to commercial real estate

(e) Foreign exchange open position

(f) Open position in gold

Bank Guarantee

A guarantee means giving something as security. A bank guarantee is when a bank offers surety and guarantees for different business obligation on behalf of their customers within certain regulations. It is generally a promise made by the bank to any third person to undertake the payment risk on behalf of its customers.

Bank guarantee is given on a contractual obligation between the bank and its customers. Such guarantees are widely used in business and personal transactions to protect the third party from financial losses.

Advantage of Bank Guarantees

• Bank guarantee reduces the financial risk involved in the business transaction.
• Due to low risk, it encourages the seller/beneficiaries to expand their business on a credit basis.
• Banks generally charge low fees for guarantees, which is beneficial to even small-scale business.
• When banks analyse and certify the financial stability of the business, its credibility increases and this, in turn, increase business opportunities.
• Mostly, the guarantee requires fewer documents and is processed quickly by the banks (if all the documents are submitted).

**Disadvantage of Bank Guarantees**

• Sometimes, the banks are so rigid in assessing the financial position of the business. This makes the process complicated and time-consuming.
• With the strict assessment of banks, it is very difficult to obtain a bank guarantee by loss-making entities.
• For certain guarantees involving high-value or high-risk transactions, banks will require collateral security to process the guarantee.

**Types of Guarantees**

**Financial Guarantee** – These guarantees are generally issued in lieu of security deposits. Some contracts may require a financial commitment from the buyer such as a security deposit. In such cases, instead of depositing the money, the buyer can provide the seller with a financial bank guarantee using which the seller can be compensated in case of any loss.

**Performance Guarantee** – These guarantees are issued for the performance of a contract or an obligation. In case, there is a default in the performance, non-performance or short performance of a contract, the beneficiary’s loss will be made good by the bank.

**Deferred payment guarantee:** This refers to a bank guarantee or a payment guarantee that is offered to the exporter for a deferred period or for a certain time period. When a buyer purchases capital goods or machinery, the seller will give credit to the buyer when the buyer’s bank gives a guarantee that it will pay the unsettled dues of the buyer to the seller. Under this type of guarantee, payment will be made in installments by the bank for failure in supplying raw materials, machinery or equipment.

**Letter of Credit**
A letter of credit is a document that guarantees the buyer’s payment to the sellers. It is issued by a bank and ensures the timely and full payment to the seller. If the buyer is unable to make such a payment, the bank covers the full or the remaining amount on behalf of the buyer. A letter of credit is issued against a pledge of securities or cash. Banks typically collect a fee, ie, a percentage of the size/amount of the letter of credit.

**Parties to a Letter of Credit**

- Applicant (importer) requests the bank to issue the LC
- Issuing bank (importer’s bank which issues the LC [also known as the Opening banker of LC])
- Beneficiary (exporter)
- Advising Bank
- Confirming Bank

**Types of Credit**

**Sight Credit:** Under this LC, documents are payable at the sight / upon presentation of the correct documentation.

For example, a businessman can present a bill of exchange to a lender along with a sight letter of credit and take the necessary funds right away. A sight letter of credit is more immediate than other forms of letters of credit.

**Acceptance Credit/ Time Credit:** The Bills of Exchange which are drawn and payable after a period, are called usance bills. Under acceptance credit, these usance bills are accepted upon presentation and eventually honoured on their respective due dates.

**Revocable and Irrevocable Credit:** A revocable LC is a credit, the terms and conditions of which can be amended/ cancelled by the Issuing Bank. This cancellation can be done without prior notice to the beneficiaries.

An irrevocable credit is a credit, the terms and conditions of which can neither be amended nor cancelled. Hence, the opening bank is bound by the commitments given in the LC.

**Confirmed Credit:** Only Irrevocable LC can be confirmed. A confirmed LC is one when a banker other than the Issuing bank, adds its own confirmation to the credit. In case of confirmed LCs, the beneficiary’s bank would submit the documents to the confirming banker.

**Back-to-Back credit:** In a back to back credit, the exporter (the beneficiary) requests his banker to issue an LC in favour of his supplier to procure raw materials, goods on the basis of the export LC received by him. This type of LC is known as Back-to-Back credit.
Transferable Credit: While an LC is not a negotiable instrument, the Bills of Exchange drawn under it are negotiable. A Transferable Credit is one in which a beneficiary can transfer his rights to third parties. Such LC should clearly indicate that it is a ‘Transferable’ LC.

### Differences between Letter of Credit (LOC) and Bank Guarantee (BG)

<table>
<thead>
<tr>
<th>Particulars</th>
<th>LOC</th>
<th>BG</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Nature</strong></td>
<td>LOC is an obligation accepted by a bank to make payment to a beneficiary if certain services are performed.</td>
<td>BG is an assurance given by the bank to the beneficiary to make the specified payment in case of default by the applicant.</td>
</tr>
<tr>
<td><strong>Primary liability</strong></td>
<td>Bank retains the primary liability to make the payment and later collects the same from the customer.</td>
<td>The bank assumes to make the payment only when the customer defaults to make payment.</td>
</tr>
<tr>
<td><strong>Payment</strong></td>
<td>Bank makes the payment to the beneficiary as and when it is due. It need not wait for a default to be made by the customer.</td>
<td>Only when the customer defaults the payment to the beneficiary, the bank makes the payment.</td>
</tr>
<tr>
<td><strong>Way of working</strong></td>
<td>LOC ensures that the amount will be paid as long as the services are performed as per the agreed terms.</td>
<td>BG assures to compensate for the loss if the applicant does not satisfy the specified conditions.</td>
</tr>
<tr>
<td><strong>Number of parties involved</strong></td>
<td>There are multiple parties involved here - LOC Issuing bank, its customer, the beneficiary (third party), and advising bank.</td>
<td>There are only three parties involved - banker, its customer, and the beneficiary (third party).</td>
</tr>
<tr>
<td><strong>Suitability</strong></td>
<td>Generally, this is more appropriate during the import</td>
<td>Suits any business or personal</td>
</tr>
<tr>
<td>Particulars</td>
<td>LOC</td>
<td>BG</td>
</tr>
<tr>
<td>------------</td>
<td>-----</td>
<td>----</td>
</tr>
<tr>
<td>and export of goods and services.</td>
<td>transactions.</td>
<td></td>
</tr>
<tr>
<td>Risk</td>
<td>Bank assumes more risk than the customer.</td>
<td>Customer assumes the primary risk.</td>
</tr>
</tbody>
</table>

**Forward Rate Agreement (FRA) and Interest Rate Swap (IRS)**

**Forward Rate Agreement (FRA)**

- FRAs are forwards hence they are private contracts between counterparties.
- The forward rate is locked in a FRA contract.
- Buyer benefits when borrowing rate increases.
- Seller benefits when borrowing rate decreases.

**Interest Rate Swap (IRS)**

- Interest rate swap (IRS) is a type of swap and hence belongs to the class of derivatives. Its price is derived by market interest rates.
- An interest rate swap is a financial agreement between parties to exchange fixed or floating payments over a period of time.

**Unit 7: Risk Management; Basel I, II & III Accords**

**Risk Management**

In the course of their operations, banks are invariably faced with different types of risks that may have a potentially adverse effect on their business. Banks are obliged to establish a comprehensive and reliable risk management system, integrated in all business activities and providing for the bank risk profile to be always in line with the established risk propensity.

**Risk Management Function**
• Risk management strategy and policies, as well as procedures for risk identification and measurement, i.e. for risk assessment and risk management;
• Appropriate internal organisation, i.e. bank’s organizational structure;
• Effective and efficient risk management process covering all risks the bank is exposed to or may potentially be exposed to in its operations;
• Adequate internal controls system;
• Appropriate information system;
• Adequate process of internal capital adequacy assessment.
• Strong MIS for reporting, monitoring and controlling risks
• Well laid out procedures, effective control and comprehensive risk reporting framework.
• Periodical review and evaluation.

**Type of Risk Management**

**Liquidity risk** is the risk of potential occurrence of adverse effects on the bank’s financial result and capital due to the bank’s inability to meet the due liabilities caused by the withdrawal of the current sources of funding, that is, the inability to raise new funds (funding liquidity risk), aggravated conversion of property into liquid assets due to market disruption (market liquidity risk).

**Credit risk** is the risk of potential occurrence of adverse effects on the bank’s financial result and capital due to debtor’s default to meet its obligations to the bank.

Credit risk may take the following forms:

(a) **Direct lending**: Principal and/or interest amount may not be repaid.

(b) **Guarantees or letter of credit**: Funds may not be forthcoming from the constituents upon crystallization of the liability.

(c) **Securities trading business**: Funds/ securities settlement may not be effected.

(d) **Cross-border exposure**: The availability and free transfer of foreign currency funds may either cease or restrictions may be imposed by the sovereign.

**Market risks** entail foreign exchange risk, price risk on debt securities, price risk on equity securities, and commodity risk.

**Interest rate risk** is the risk of possible occurrence of adverse effects on the bank’s financial result and capital on account of banking book items caused by changes in interest rates.
Foreign exchange risk is the risk of possible occurrence of adverse effects on the bank’s financial result and capital on account of changes in foreign exchange rates.

Operational risk is the risk of possible adverse effects on the bank’s financial result and capital caused by omissions (unintentional and intentional) in employees’ work, inadequate internal procedures and processes, inadequate management of information and other systems, as well as by unforeseeable external events. Operational risk also includes legal risk.

**BASEL NORM**

**Basel is a city in Switzerland** which is also the headquarters of Bureau of International Settlement (BIS).

The Bank for International Settlements (BIS) established on 17 May 1930, is the world’s oldest international financial organisation. There are two representative offices in the Hong Kong and in Mexico City.

**BASEL- I**

- In 1988, The Basel Committee on Banking Supervision (BCBS) introduced capital measurement system called Basel capital accord, also called as Basel 1.
- It focused almost entirely on credit risk, It defined capital and structure of risk weights for banks.
- The minimum capital requirement was fixed at 8% of risk-weighted assets (RWA).
- India adopted Basel 1 guidelines in 1999.
- In India, however banks are required to maintain a minimum Capital-to-risk weighted Asset ratio (CRAR) of 9% on an ongoing basis.

**BASEL- II**

In 2004, Basel II guidelines were published by BCBS, which were considered to be the refined and reformed versions of Basel I accord.

**Three Pillars of Basel II**

(i)First Pillar: Minimum capital Requirement

(a)Calculation of minimum capital requirements and constituents of capital

(b)Credit Risk

-Standardized Approach

-Internal Ratings-based Approach
- Securitisation Framework
(c) Market Risk
(d) Operational Risk

(ii) Second Pillar: Supervisory review process

(iii) Third Pillar: Market Discipline.

**First Pillar: Minimum capital Requirement**

The Capital base of the bank consist of the following three types of capital element. **Tier 1, Tier 2 and Tier 3 capital.** The sum of Tier 1, Tier 2 and Tier 3 element will be eligible for inclusion in the capital base, subject to the following limits.

(a) Total of Tier 2 (Supplementary) elements will be limited to a maximum of 100% of the Tier 1 element.
(b) Subordinated term debt will be limited to a maximum of 50% of Tier 1 elements.
(c) Tier 3 capital will be limited to 250% of a bank’s Tier 1 capital that is required to support market risks.
(d) Where general provisions/general loan –loss reserves include amounts reflecting lower valuations of assets or latent but unidentified losses present in the balance sheet, the amount of such provisions or reserves will be limited to a maximum of 1.25% point.
(e) Asset revaluation reserves, which take the form of latent gains on unrealized securities, will be subject to a discount of 55%.

**Second Pillar: Supervisory review process**

The section discusses the key principles of supervisory review, risk management guidance and supervisory transparency and accountability, produced by the committee with respect to banking risks. This includes guidance relating to, among other things, the treatment of interest rate risk in the banking book, credit risk, operational risk etc.

**Four key of Principles of Supervisory Review:**

The Committee has identified four key principles of supervisory review, which complement those outlined in the extensive supervisory guidance that has been developed by the committee.

**Principle 1:** Banks should have a process for assessing their overall capital adequacy in relation to their risk profile and a strategy for maintaining their capital levels.

**Principle 2:** Supervisors should review and evaluate Bank’s internal capital adequacy assessments and strategies, as well as their ability to monitor and ensure their compliance with
regulatory capital ratios. Supervisors should take appropriate supervisory action if they are not satisfied with the result of this process.

**Principle 3:** Supervisors should expect banks to operate above the minimum regulatory capital ratios and should have the ability to require banks to hold capital in excess of the minimum.

**Principle 4:** Supervisors should seek to intervene at an early stage to prevent capital from falling below the minimum levels required to support the risk characteristics of a particular bank and should require rapid remedial action if capital is not maintained or restored.

**Third Pillar: Market Discipline**

- Disclosure Requirements
- Guiding Principles
- Achieving Appropriate Disclosure

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**BASEL - III**

Basel III or Basel 3 released in December, 2010 is the third in the series of Basel Accords. These accords deal with risk management aspects for the banking sector. So we can say that Basel III is the global regulatory standard on bank capital adequacy, stress testing and market liquidity risk. (Basel I and Basel II are the earlier versions of the same, and were less stringent).

The RBI issued Guidelines based on the Basel III reforms on capital regulation on May 2 2012, to the extent applicable to banks operating in India. The Basel III capital regulation has been implemented from April 1, 2013 in India in phase and it will be fully implemented as on March 31, 2019.

**Aims of the Basel III**

- Improve the banking sector’s ability to absorb ups and downs arising from financial and economic instability
- Improve risk management ability and governance of banking sector
- Strengthen banks’ transparency and disclosures

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**What are the major changes proposed in Basel III over earlier accords i.e. Basel I and Basel II?**
Better Capital Quality: One of the key elements of Basel 3 is the introduction of much stricter definition of capital. Better quality capital means the higher loss-absorbing capacity. This in turn will mean that banks will be stronger, allowing them to better withstand periods of stress.

Capital Conservation Buffer: Another key feature of Basel III is that now banks will be required to hold a capital conservation buffer of 2.5%. The aim of asking to build conservation buffer is to ensure that banks maintain a cushion of capital that can be used to absorb losses during periods of financial and economic stress.

Countercyclical Buffer: This is also one of the key elements of Basel III. The countercyclical buffer has been introduced with the objective to increase capital requirements in good times and decrease the same in bad times. The buffer will slow banking activity when it overheats and will encourage lending when times are tough i.e. in bad times. The buffer will range from 0% to 2.5%, consisting of common equity or other fully loss-absorbing capital.

Minimum Common Equity and Tier 1 Capital Requirements: The minimum requirement for common equity, the highest form of loss-absorbing capital, has been raised under Basel III from 2% to 4.5% of total risk-weighted assets. The overall Tier 1 capital requirement, consisting of not only common equity but also other qualifying financial instruments, will also increase from the current minimum of 4% to 6%. Although the minimum total capital requirement will remain at the current 8% level, yet the required total capital will increase to 10.5% when combined with the conservation buffer.

Leverage Ratio: A review of the financial crisis of 2008 has indicted that the value of many assets fell quicker than assumed from historical experience. Thus, now Basel III rules include a leverage ratio to serve as a safety net. A leverage ratio is the relative amount of capital to total assets (not risk-weighted). This aims to put a cap on swelling of leverage in the banking sector on a global basis. 3% leverage ratio of Tier 1 will be tested before a mandatory leverage ratio is introduced in January 2018.

Liquidity Ratios: Under Basel III, a framework for liquidity risk management will be created. A new Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) are to be introduced in 2015 and 2018, respectively.

Systemically Important Financial Institutions (SIFI): As part of the macro-prudential framework, systemically important banks will be expected to have loss-absorbing capability beyond the Basel III requirements. Options for implementation include capital surcharges, contingent capital and bail-in-debt.

Comparison of Capital Requirements under Basel II and Basel III

<table>
<thead>
<tr>
<th></th>
<th>Basel II</th>
<th>Basel III</th>
</tr>
</thead>
<tbody>
<tr>
<td>Common Equity</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tier 1 Capital</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Capital</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

As a percentage of risk weighted assets
### Minimum Total Capital

<table>
<thead>
<tr>
<th></th>
<th>Minimum Total Capital</th>
<th>January 2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>A = (B + D)</td>
<td>Minimum Total Capital</td>
<td>8.0</td>
</tr>
<tr>
<td>B</td>
<td>Minimum Tier 1 Capital</td>
<td>4.0</td>
</tr>
<tr>
<td>C</td>
<td>Of which: Minimum common equity Tier 1 capital</td>
<td>2.0</td>
</tr>
<tr>
<td>D</td>
<td>Maximum Tier 2 Capital (Within Total capital)</td>
<td>4.0</td>
</tr>
<tr>
<td>E</td>
<td>Capital conservation buffer (CCB)</td>
<td>--</td>
</tr>
<tr>
<td>F = C + E</td>
<td>Minimum Common Equity Tier 1 capital + CCB</td>
<td>2.0</td>
</tr>
<tr>
<td>G = A + E</td>
<td>Minimum Total capital + CCB</td>
<td>8.0</td>
</tr>
</tbody>
</table>

### Minimum Regulatory Capital Prescriptions (as percentage of risk weighted assets)

<table>
<thead>
<tr>
<th></th>
<th>Basel II Current</th>
<th>Basel III (March 31, 2018)</th>
<th>Basel II (January 2019)</th>
</tr>
</thead>
<tbody>
<tr>
<td>A = (B + D)</td>
<td>Minimum Total Capital</td>
<td>9.0</td>
<td>9.0</td>
</tr>
<tr>
<td>B</td>
<td>Minimum Tier 1 Capital</td>
<td>6.0</td>
<td>7.0</td>
</tr>
<tr>
<td>C</td>
<td>Of which: Minimum common equity Tier 1 capital</td>
<td>3.6</td>
<td>5.5</td>
</tr>
<tr>
<td>D</td>
<td>Maximum Tier 2 Capital (Within Total capital)</td>
<td>3.0</td>
<td>2.0</td>
</tr>
<tr>
<td>E</td>
<td>Capital conservation buffer (CCB)</td>
<td>--</td>
<td>2.5</td>
</tr>
</tbody>
</table>
F=C+E
Minimum Common Equity Tier 1 capital +CCB
3.6
8.0
7.0

G=A+E
Minimum Total capital +CCB
--
11.5
10.5

H
Leverage Ratio (Ratio to total Assets)
--
4.5
3.0

Unit 8- CIBIL, Fair Practices Code for Debt Collection, BCSB

CIBIL (Credit Information Bureau (India) Limited)

CIBIL (Credit Information Bureau (India) Limited) is a Credit Bureau or Credit Information Company. This company is engaged in maintaining the records of all the credit-related activities of companies as well as individuals including credit cards and loans. The registered member banks and several other financial institutions periodically submit their information to CIBIL. Based on the information and record provided by these institutions, CIBIL issues a CIR (Credit Information Report) as well as a credit score.

Govt. of India enacted an Act called Credit Information Companies (regulation) Act in 2005. Soon thereafter the RBI issued notification regarding the framework for functioning of credit information bureaus.

As on date the RBI has issued authorization to 4 credit information companies to operate. A credit information company (CIC) or popularly known as credit bureau collects the credit information from bank and other lenders, prepares a credit history, compiles credit scores and thereafter provides the information on a particular proponent to the lender for a fee. The information provided by CIC helps the lender to take an objective decision, quickly, based on the information which include data such as loans credit card facilities availed from one or different lenders, re-payment record, current balance on each of the facility, new credit hungry), defaults in repayment of dues, suit filed information etc.

Membership to a CIC

Credit Institutions (Banks, RRBs, Co-operative banks, NBFC, Public Financial Institution, Housing Financial Institution etc. Companies engaged in the business of credit cards and other similar cards and companies dealing with distribution of credit in any other manner or any
other institution which the Reserve Bank may specify, from time to time, for this purpose),
Insurance Companies, Companies providing cellular or telephone services, Credit Rating
Agencies, Asset Reconstruction Companies.

**Product offerings by CIBIL**

CIBIL offers three products viz. **credit score, a credit report for individuals and credit
report for companies:**

**Credit score**

Credit score refers to a **3 digit numeric value** which represents the creditworthiness of an
individual. The creditworthiness ranges **between 300 to 900 with 900 being the highest and
300 being the least.** This score is computed with the help of the credit history of an individual.
Banks and most of the financial institutions prefer extending credit to an individual whose **score
is 750 and more.** Individuals with good credit scores are less likely to default on their loan
payments.

**Credit report**

Credit report contains the credit information that **CIBIL fetches from various financial
institutions.** This detailed report contains information about an individual’s history of
borrowing and repayment routine, including defaults and delays. The important parts of this
report are credit Score, individual’s personal information, employment details, contact
information and account details.

**Credit report for companies**

Credit report for companies constitutes details about a company’s credit history. The several
segments in a company credit report speak about potential lenders, existing credit which the
company has, any pending lawsuits and outstanding amount. A good credit report is essential
for approval of any loans, whereas a bad report could damage/reduce the chances of the loan
being granted to the company.

**Fair Practices Code for Debt Collection**

**Demand for Lenders Liability Law**

The Securitisation and Reconstruction of Financial Asset and Enforcement of Security Interest
Act **was enacted in India in 2002.** The Act allowed bank to take possession of assets of
defaulting companies without going through the cumbersome legal process. In many countries,
banks are mandated by law to respect the right and interest of borrowers, depositors and the
other customers.
All the banks in India have framed their own set of fair practices codes as per the guidelines and implemented it from November 1, 2003.

The ‘Code of Bank’s Commitment to Customers’ was released by Dr. Y.V Reddy, the then Governor, Reserve Bank of India, in an inaugural function held at RBI on 1 July, 2006.

Application for Loans and their Processing

(a) Loan application form in respect of priority sector and advances of up to Rs. 2 lakhs should be comprehensive. It should include information about the fees/charges, if any, payable for processing. The amount of such fees is refundable in the case of non-acceptance of application. A meaningful comparison with that of other banks can thus be made and the informed decision can be taken by the borrower.

(b) Banks and financial institutions shall give acknowledgement for receipt of all loan applications. The time frame, within which loan application up to Rs. 2 lakhs will be disposed, should also be indicated in acknowledgement of such applications.

(c) Banks/financial institutions should scrutinize the loan application within a reasonable period of time. If additional details/documents are required, they should intimate the borrowers immediately.

(d) In the case of small borrowers seeking loans up to Rs. 2 lakhs, the lenders should convey in writing, the main reason/reasons which, in the opinion of the bank after due consideration, have led to rejection of the loan applications within the stipulated time.

Banking Codes and Standards Board of India (BCSBI)

In November 2003, RBI constituted the Committee on Procedures and Performance Audit of Public Services under the Chairmanship of Shri. S.S Tarapore (Former Deputy Governor) to address the issues relating to availability of adequate banking services to the common man. The mandate to the committee included identification of factors that inhibited the attainment of best customer services and suggestion steps to improve the quality of banking services to individual customers.

The Banking Codes and Standards Board of India (BCSBI) is an independent banking industry watchdog that protects consumers of banking services in India. The board oversee compliance with the "Code of Bank's Commitment to Customers". It is not a compensation mechanism and looks into an individual complaint only to the extent it points to any systemic compliance failure. It is an independent and autonomous body, registered as a separate society under the Societies Registration Act, 1860 on 18 February 2006. The Reserve Bank of India extended financial support to the Board, meeting its expenses for the first five years.
Main aims

- The plan, evolve, prepare, develop, promote and publish voluntary, comprehensive Code and Standards for banks, to provide fair treatment to their customers.
- To function as an independent and autonomous watchdog to monitor and ensure that the Codes and Standards are adhered to.
- To conduct and undertake research of Codes and Standards currently in use around the world.
- To enter into covenants with banks on observance of codes and standards and to train employees of such banks about the Codes.
- To help people affected by natural calamities.

Monitoring of Implementation of the Code

BCSBI monitors the implementation of the codes through the following methods:

(a) Obtains from member banks an Annual Statement of Compliance (ASC)
(b) Visits branches to find out the status of ground-level implementation of Codes
(c) Studies complaints received from customers and order/awards issued by Banking Ombudsmen/ Appellate Authority to find out whether there is any system-wide deficiency.
(d) Organizes an annual conference with Principal Code Compliance officers of the Member banks to discuss implementation issues.

Initiatives by BCSBI

BCSBI undertakes campaigns and initiatives to spread awareness of the Codes amongst customers and Banks such as:

(i) Provides faculty support to training establishment of Banks
(ii) Participates in On-location workshops held by member banks to increase coverage
(iii) Associates with customer awareness Programmes conducted by Banking Ombudsmen
(iv) Provides credit counseling services in Mumbai
(v) Publishes quarterly newsletter entitled “Customer Matter” containing matters of interest to customers

Unit 9- Recent Developments in the Financial System
Indian Government appointed a committee under the chairmanship of Sukhamoy Chakravarty in 1985 to review the Indian monetary system. Later, working group on the money market (Chairmanship of Narayan Vaghul, 1988), a number of measures were taken up by the RBI to widen and deepen the money market through institution jointly by RBI, Public sector bank and financial institutions, commenced operations in April 1988, to deal in short term money market instruments with the primary objective of improving liquidity. The introduction of new instruments, broadening of participants base and strengthening of institutional infrastructure have been pursued during the 1990s, based on the framework provided by the Narayanan Vaghul and the Narasimham Committee II.

As per the recommendations of these study groups and with the financial sector reforms initiated in the early 1990s, the government has adopted following major reforms in the Indian money market.

i) Deregulation of the Interest Rate

ii) Money Market Mutual Fund (MMMFs)

iii) Liquidity Adjustment Facility (LAF)

iv) Electronic Transactions

v) Establishment of the CCIL

iv) Development of New Market Instruments : The government has consistently tried to introduce new short-term investment instruments. Examples: Treasury Bills of various duration, Commercial papers, Certificates of Deposits, MMMFs, etc. have been introduced in the Indian Money Market.

**Commercial paper**

Commercial paper is an unsecured money market instrument issued in the form of a Promissory note was introduced in India in 1990. It enables highly rated corporate borrowers to diversify their sources of short-term borrowings and to provide an additional instrument to investors. Information on CP issuance as reported by the Issuing and Paying Agents (IPAs) on the NDS platform has been made available on the Reserve Bank’s website with effect from July 2005, to enhance transparency and facilitate wider dissemination.

**Maturity**

- Minimum: 7 days
- Maximum: 1 year

**Certificate of deposit**
A certificate of deposit is a negotiable money market instrument which is issued in dematerialised form or as a Usance Promissory Note, for funds deposited at a bank or other eligible financial institution for a specified time period. CD were introduced in India in 1989. The minimum maturity period of CP is 7 days with effect from 29 Apr 2005.

**Maturity**

- Minimum: 7 days
- Maximum: 1 year

**Note:** FIs can issue CDs for a period **not exceeding 3 years** from the date of issue.

The Reserve Bank has taken many initiatives towards introducing and upgrading safe and efficient modes of payment systems in the country to meet the requirements of the public at large.

Since paper based payments occupy an important place in the country, Reserve Bank had introduced Magnetic Ink Character Recognition (MICR) technology for speeding up and bringing in efficiency in processing of cheques.

Later, a separate High Value Clearing was introduced for clearing cheques of value Rupees one lakh and above. This clearing was available at select large centres in the country (since discontinued).

Recent developments in paper-based instruments include launch of Speed Clearing (for local clearance of outstation cheques drawn on core-banking enabled branches of banks), introduction of cheque truncation system (to restrict physical movement of cheques and enable use of images for payment processing), framing CTS-2010 Standards (for enhancing the security features on cheque forms) and the like.

In pursuance of the recommendations of the committee on banking sector reforms (Chairmanship M. Narasimham,1998), the process of transforming the call/ notice money market into a pure inter-bank market was **completed in August 2005.**

**Payment and Settlement Systems:** In India, the payment and settlement system are regulated by the Payment and Settlement systems Act, 2007 (PSS Act) which was legislated in December 2007. The PSS Act as well as the Payment and Settlement System Regulations, 2008 framed there under came into effect from August 12, 2008. In terms of section 4 of the PSS act, no person other than the RBI can commerce or operate a payment system in India unless authorized by RBI. RBI has since authorized payment system operator of pre-paid payment instruments, card schemes, cross border in bound money transfer, Automated Teller Machine networks and centralized clearing arrangements.

**Electronic Payments:** The continued increase in the volume of cheques added pressure on the existing set-up, thus necessitating following cost-effective alternative systems.
i) Electronic Clearing Service (ECS) Credit: The RBI introduced the ECS (Credit) scheme during the 1990s to handle bulk and repetitive payment requirements (Like salary, interest, Dividend payments) of corporates and other institutions During September 2008, the RBI launched a new service known as National Electronic Clearing Service (NECS), at National clearing Cell (NCC), Mumbai. NECS (credit) facilitates multiple credits to beneficiary accounts with destination branches across the country against a single debit of the account of the sponsor bank.

ii) Regional ECS (RECS): RECS has been launched during the year 2009. RECS, a miniature of the NECS isconfined to the bank branches within the jurisdiction of a Regional Office of RBI.

iii) Electronic Clearing Service (ECS) Debit: The ECS scheme was introduced by RBI to provide a faster method of effecting periodic and repetitive collections of utility companies.

iv) National Electronic Funds Transfer (NEFT) System: In November 2005, a more secure system was introduced for facilitating one to one funds transfer requirement of individuals/Corporates.

v) Real Time Gross Settlement (RTGS) System: This was introduced in 2004 and settles all inter-bank payments and customer transactions above Rs 2 lakhs.

vi) Clearing Corporation of India Limited (CCIL): CCIL was setup in April 2001 by banks, financial institutions and primary dealers, to function as an industry services organization for clearing and settlement of trades in money market, government securities and foreign exchange markets.

vii) Electronic Funds Transfer: This retail fund transfer system introduced in the 1990s enabled an account holder of bank to electronically transfer funds to another holder with any other participating bank.

Other Payment Systems

Pre-paid Payment systems

Pre-paid instruments are payment instruments that facilitate purchase of goods and services against the value stored on these instruments. The value stored on such instruments represents the value paid for by the holders by cash, by debit to a bank account, or by credit card. The pre-paid payment instruments can be issued in the form of smart cards, magnetic stripe cards, internet accounts, internet wallets, mobile accounts, mobile wallets, paper vouchers, etc.

The use of pre-paid payment instruments for cross border transactions has not been permitted, except for the payment instruments approved under Foreign Exchange Management Act, 1999 (FEMA).
Reserve Bank brought out a set of operating guidelines on mobile banking for banks in October 2008, according to which only banks which are licensed and supervised in India and have a physical presence in India are permitted to offer mobile banking after obtaining necessary permission from Reserve Bank.

**ATMs / Point of Sale (POS) Terminals / Online Transactions**

As on Feb, 2014, there are over 1,50,008 ATMs (76836 onsite and 73172 offsite) in India. Savings Bank customers can withdraw cash from any bank terminal up to 5 times in a month without being charged for the same (refer RBI circulars for latest changes).

Reserve Bank has mandated re-crediting of failed transactions within 7 working day and mandated compensation for delays beyond the stipulated period.

As on Feb, 2014, there are over 10 lakh POS terminals in the country, which enable customers to make payments for purchases of goods and services by means of credit/debit cards.

To facilitate customer convenience the Bank has also permitted cash withdrawal using debit cards issued by the banks at PoS terminals.

Further, to reduce the risks arising out of the use of credit/debit cards over internet/IVR (technically referred to as card not present (CNP) transactions), Reserve Bank mandated that all CNP transactions should be additionally authenticated based on information not available on the card and an online alert should be sent to the cardholders for such transactions.

**National Payments Corporation of India**

The Reserve Bank encouraged the setting up of National Payments Corporation of India (NPCI) to act as an umbrella organisation for operating various Retail Payment Systems (RPS) in India. NPCI became functional in early 2009. NPCI has taken over National Financial Switch (NFS) from Institute for Development and Research in Banking Technology (IDRBT).

Oversight of the payment and settlement systems is a central bank function whereby the objectives of safety and efficiency are promoted by monitoring existing and planned systems, assessing them against these objectives and, where necessary, inducing change. By overseeing payment and settlement systems, central banks help to maintain systemic stability and reduce systemic risk, and to maintain public confidence in payment and settlement systems.

“Rupay” is the country’s own card payment network developed by National Payments Corporation of India (NPCI). It was dedicated to the national by the Hon. Former President of India Shri Pranab Mukherjee on May 8, 2014. “Rupay” minimize the dependency on the international schemes.

**The Depositor Education and Awareness Fund Scheme, 2014**
Pursuant to the amendment of the **Banking Regulation Act 1949, section 26A** has been interest in that **Act, empowering Reserve Bank to establish The Depositor Education and Awareness Fund (The Fund)** Under the provisions of this section the amount to the credit of any account of the **credit of any account in India** with any bank which has been operated upon for a period of ten years or any deposit or any amount remaining unclaimed for **more than 10 years shall be credited to the fund, within a period of 3 months from** the expiry of the said period 10 years.

**Transfer of Funds**

- The amount to be credited to the fund includes credit balance in any deposit account maintained with banks with have not been operated upon **for ten years or more**, or any amount remaining unclaimed for **10 years or more** as under:-
  - Saving bank deposit account
  - Fixed or term deposit account
  - Cumulative/ recurring deposit accounts
  - Current deposit accounts
  - Other deposit accounts in any form or with any name
  - Cash credit accounts
  - Loan accounts after due appropriation by the bank
  - Margin money against issue of letter of credit/ Guarantee etc any security deposit etc.

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## MODULE B – FUNCTIONS OF BANKS
### Jaiib/DBF Paper 1 (Module B)

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Unit 1 - Bankers-Customer Relationship

Banking

The term “Banking” has been comprehensively defined under the Banking Regulation Act 1949. According to Section 5(b) of the Banking Regulation Act, the term “Banking” means accepting for the purpose of lending or investment of deposits of money received from the public, repayable on demand or otherwise and withdrawable by cheque, draft, order or otherwise.

An Individual is not allowed to act as a bank and he/she cannot use this term in the business. A firm consisting of not more than ten partners or a company incorporated under Indian Companies Act, 1956 can be bank, a banker or a banking company. Under section 5(c) of the Banking Regulation Act, “Banking Company” means any company that transacts the business of banking in India. Section 7(1) of the Banking Regulation Act prohibits use of the words ‘banker’ or ‘banking’ or ‘banking company’ by a company other than a banking company. Section 7(2) of the said Act further prohibits the use of such words by an individual or a group of individual or a firm.

Important Function of a Bank covered under Section 6 are:

- Discounting of bills
- Collection of cheques and bills
- Remittances
- Safe custody of articles
- Hiring safe deposit lockers
- Conducting foreign exchange transactions
- Conducting (Central/State) government transactions
- Issuing letters of credit and guarantees

Banker-Customer Relationship

Banker: According to Section 3 of the Negotiable Instrument act the term “banker” includes any person acting as a Banker.

Customer: A person who has a bank account in his name and for whom the banker undertakes to provide the facilities as a banker is considered to be a customer.
To constitute a customer the following requirements must be fulfilled;

The bank account may be savings, current or fixed deposit must be operated in his name by making a necessary deposit of money.

The dealing between the banker and customer must be of the nature of the banking business. The general relationship between banker and customer.

**Debtor- Creditor (Bank is a Debtor and Customer is a Creditor)**

On the opening of an account, the banker assumes the position of a debtor. A depositor remains a creditor of his banker so long as his account carries a credit balance.

The relationship with the customer is reserved as soon as the customer account is overdrawn.

Banker becomes a creditor of the customer who has taken a loan from the banker and continues in that capacity fills the loan is repaid.

The demand should be made in a proper manner. The customer should demand payment not verbally or by a mere telephone call but by cheque, draft, withdrawal form, order or otherwise. Further, demand should be made during the working days and working hours under section 25 and 65 of Negotiable Instruments Act, 1881, respectively.
Creditor- Debtor (Bank is a creditor and Customer is a Debtor)

When the bank lends money to the customer, the customer is the borrower and the bank is the lender. The relationship between the banker and the customer is therefore that of a creditor and a debtor.

Banker as a Trustee

Ordinarily a banker is a debtor of his customer in the report of the deposit made by the letter but in certain circumstances, he acts as trustee also.

A trustee hold holds money or asset and performs certain functions for the benefit of some other person called the beneficiary.

For example; If the customer deposits securities or other values with the banker for the safe custody, the letter acts as a trustee of his customer.

Bailee and Bailor Relationship (Bank- Bailee and Customer- Bailor)

As per the section 148 of the Indian Contract Act, 1872, a bailment is a contract where one person delivers goods to another person for some purpose. The person delivering the goods is the Bailor and the person receiving the goods is the Bailee. After the accomplishment of the purpose, the Bailee needs to return these goods to the Bailor or dispose of them according to the directions of the Bailor. Let us now discuss the duties of bailee and bailor.

The finder of lost goods (Section 71 Indian Contract Act) should return any increase in goods/animal to the true owner. Under section 164 (Indian Contract Act), The finder has to take care of such goods as an ordinary prudent man.

Banker as an Agent

A banker acts as an agent of his customer and performs a number of agency functions for the conveniences of his customer.

For example, he buys or sells securities on behalf of his customer, collects check/cheques on his behalf and makes payment of various dues of his customer.

Relationship of Lessor and Lessee (Bank as a Lessor and Customer as a Lessee)

Similarly, when a customer hires a safe deposit locker from the bank, the relation between the bank and the customer is lessor and lessee. The bank is the lessor (licensor) and the hirer of safe deposit locker is the lessee (licensee/tenant).

Indemnifier and Indemnified (Bank is Indemnified or Indemnity holder and Customer is Indemnifier)

A contract by which one party promises to save the other from loss caused to him by the conduct of the promisor or the conduct of any other person is called a contact of indemnity.
Section 124 (Indian Contract Act 1872). In the case of banking, this relationship happens in transactions of issue of duplicate demand draft, fixed deposit receipt etc.

**Banker Customer Relationship can be Summarized for Different Types of Transactions as under**

<table>
<thead>
<tr>
<th>Transaction</th>
<th>Bank</th>
<th>Customer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deposit in the bank</td>
<td>Debtor</td>
<td>Creditor</td>
</tr>
<tr>
<td>Loan from bank</td>
<td>Creditor</td>
<td>Debtor</td>
</tr>
<tr>
<td>Safe custody</td>
<td>Bailee</td>
<td>Bailor</td>
</tr>
<tr>
<td>Locker</td>
<td>Lessor</td>
<td>Lessee</td>
</tr>
<tr>
<td>Collection Of cheque</td>
<td>Agent</td>
<td>Principal</td>
</tr>
<tr>
<td>Purchase of a Draft</td>
<td>Debtor</td>
<td>Creditor</td>
</tr>
<tr>
<td>Payee of a Draft</td>
<td>Trustee</td>
<td>Beneficiary</td>
</tr>
<tr>
<td>Pledge</td>
<td>Pawner(Pledgee)</td>
<td>Pawnee (Pledger)</td>
</tr>
<tr>
<td>Mortgage</td>
<td>Mortgagee</td>
<td>Martgagor</td>
</tr>
<tr>
<td>Standing instruction</td>
<td>Agent</td>
<td>Principal</td>
</tr>
<tr>
<td>Sale/Purchase of securities on behalf of a customer</td>
<td>Agent</td>
<td>Principal</td>
</tr>
<tr>
<td>Money deposited but instructions not given for its disposal</td>
<td>Trustee</td>
<td>Beneficiary</td>
</tr>
<tr>
<td>Articles left by mistake</td>
<td>Trustee</td>
<td>Beneficiary</td>
</tr>
<tr>
<td>Shares given for sale</td>
<td>Agent</td>
<td>Principal</td>
</tr>
<tr>
<td>Hypothecation</td>
<td>Hypothecatee</td>
<td>Hypothecator</td>
</tr>
</tbody>
</table>

**Different Deposit Products or Services**

**Deposit Products**

The major functions of a bank are to mobilise deposit from the public and to invest and lend these deposits to individuals, firms and corporate institutions.
Types of Deposits

- Demand Deposits
- Time Deposits

<table>
<thead>
<tr>
<th>Demand Deposits</th>
<th>Time Deposits</th>
</tr>
</thead>
<tbody>
<tr>
<td>Payable on Demand</td>
<td>Rapid after expiry of the Deposit Period</td>
</tr>
<tr>
<td>Low interest rates or no Interest</td>
<td>High Interest rates, which vary according to period</td>
</tr>
<tr>
<td>It includes current, saving, overdue deposits and Unclaimed Deposits</td>
<td>Time Deposits from 7 days to 120 months period with or without reinvestment plans.</td>
</tr>
<tr>
<td>Interests is paid on half yearly basis in saving accounts</td>
<td>Interest is generally paid every quarter.</td>
</tr>
</tbody>
</table>

Feature of Demand Deposits

Savings Bank Account

As the name suggests this type of account is suitable for people who have a definite income and are looking to save money. For example, the people who get salaries or the people who work as laborers. This type of account can be opened with a minimum initial deposit that varies from bank to bank. Money can be deposited at any time in this account.

Withdrawals can be made either by signing a withdrawal form or by issuing a cheque or by using an ATM card. Normally banks put some restriction on the number of withdrawal from this account. Interest is allowed on the balance of deposit in the account. The rate of interest on savings bank account varies from bank to bank and also changes from time to time. A minimum balance has to be maintained in the account as prescribed by the bank.

Current Deposit Account

Big businessmen, companies, and institutions such as schools, colleges, and hospitals have to make payment through their bank accounts. Since there are restrictions on the number of withdrawals from a savings bank account, that type of account is not suitable for them. They need to have an account from which withdrawal can be made any number of times.

Banks open a current account for them. Like a savings bank account, this account also requires a certain minimum amount of deposit while opening the account. On this deposit, the bank does not pay any interest on the balances. Rather the account holder pays a certain amount each year as an operational charge.
Feature of Time/ Term Deposits

Fixed Deposit Account

Some bank customers may like to put away money for a longer time. Such deposits offer a higher interest rate. If money is deposited in a savings bank account, banks allow a lower rate of interest. Therefore, money is deposited in a fixed deposit account to earn interest at a higher rate.

Note: This period of deposit may range from 15 days to three years or more during which no withdrawal is allowed.

Recurring Deposit Account

While opening the account a person has to agree to deposit a fixed amount once in a month for a certain period. The total deposit along with the interest therein is payable on maturity. However, the depositor can also be allowed to close the account before its maturity and get back the money along with the interest till that period.

The account can be opened by a person individually, or jointly with another, or by the guardian in the name of a minor. The rate of interest allowed on the deposits is higher than that on a savings bank deposit but lower than the rate allowed on a fixed deposit for the same period.

The Recurring Deposit Accounts may be of the following types:

Home Safe Account or Money Box Scheme
Cumulative-cum-Sickness deposit Account
Home Construction deposit Scheme/Saving Account
CASA Deposit Account:

CASA is the acronym for Current and Savings account, which is commonly used in the banking industry across West Asia and South-East Asia. Banks usually receive the majority of their funds from various kinds of deposit schemes like current accounts, Savings Accounts and term deposits.

CASA deposit is the amount of money that gets deposited in the Current and Savings Accounts of bank customers. The bank pays very low or no interest for deposits in current accounts whereas the deposits in Savings Accounts receives slightly higher interest rates. It is the cheapest and major source of funds for banks. This fund source is in turn used to distribute Home Loans, Personal Loans etc.

Reinvestment Deposit Account:

This is special term deposits. This plan helps you to earn interest on interest, thus giving you a two-fold income. You deposit your money with us for any period between six
months to 10 years, and we pay you interest on your deposited money plus on the interest you earn.

**Hybrid deposits or flexi deposits**

Hybrid deposits or flexi deposits which combine the features of demand and term deposits. These deposits are introduced in recent times by some banks to meet customers’ financial needs and convenience and are known by different names in different banks.

### Different Between NRE and NRO account

<table>
<thead>
<tr>
<th>Basis</th>
<th>NRE Account</th>
<th>NRO Account</th>
</tr>
</thead>
<tbody>
<tr>
<td>Acronym</td>
<td>Non Resident External Account</td>
<td>Non Resident Ordinary Account</td>
</tr>
<tr>
<td>Meaning</td>
<td>It is an account of an NRI to transfer foreign earnings to India</td>
<td>It is an account of an NRI to manage the income earned in India</td>
</tr>
<tr>
<td>Taxability</td>
<td>Interest earned is tax free</td>
<td>Interest earned is taxable</td>
</tr>
<tr>
<td>Repatriability</td>
<td>Can repatriate</td>
<td>Can repatriate the interest amount, the principle amount can be repatriated within the set limits</td>
</tr>
<tr>
<td>Joint Account</td>
<td>Can be opened by two NRIs</td>
<td>Can be opened by an NRI along with an Indian citizen or another NRI</td>
</tr>
<tr>
<td>Deposits and Withdrawals</td>
<td>Can deposit in foreign currency, and withdraw in Indian currency</td>
<td>Can deposit in foreign as well as Indian currency, and withdraw in Indian currency</td>
</tr>
<tr>
<td>Exchange Rate Risk</td>
<td>Prone to risk</td>
<td>Not prone to risk</td>
</tr>
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</table>

### Service to Customers and Investors

**Merchant Banking:** Merchant banking can be defined as a skill-oriented professional service provided by merchant banks to their clients, concerning their financial needs, for adequate consideration, in the form of fee.

**Services offered by Merchant Banks**

Merchant Banks offers a range of financial and consultancy services, to the customers, which are related to:

- Marketing and underwriting of the new issue.
- Merger and acquisition related services.
- Advisory services, for raising funds.
• Management of customer security.
• Project promotion and project finance.
• Investment banking
• Portfolio Services
• Insurance Services.

Merchant banking helps in reinforcing the economic development of the country, by acting as a source of funds and information to the business entities.

**Merchant Banker**

Any person, indulged in issue management business by making arrangements with respect to trade and subscription of securities or by playing the role of manager/consultant or by providing advisory services, is known as a merchant banker. The activities carried out by merchant bankers are:

• Private placement of securities.
• Managing public issue of securities
• Satellite dealership of government securities
• Management of international offerings like Depository Receipts, bonds, etc.
• Syndication of rupee term loans
• Stock broking
• International financial advisory services.
• In India, the functions of the merchant bankers are governed by the Securities and Exchange Board of India (SEBI) Regulations, 1992.

**Lease financing**

Lease financing is the source of payment which comes when the owner of assets (lesser) ready to provide their assets to another person in exchange of that lessor provides some agreed payment. In this way, the lessor leases the assets for a period of time on rent and lesser gets funds from the lessor. The periodical payment made by the lessee to the lessor is called the lease rental.

Under lease financing, the lessee is given the right to use the asset but the ownership lies with the lessor and at the end of the lease contract, the asset is returned to the lessor or an option is given to the lessee either to purchase the asset or to renew the lease agreement.
Advantages of lease financing

To the Lessor:

- **Assured regular income**: the lessor get lease rental by leasing an asset during the period of the lease which is an assured regular income.

- **The benefit of tax**: as ownership lies with the lessor, the tax benefit is enjoyed by the lessor by way of depreciation of respect of the leased asset.

To the lessee:

- **Tax benefits**: a company is able to enjoy the tax advantage on lease payments as payments can be deducted as a business expense.

- **Cheaper**: leasing is a source of financing which is cheaper than almost all sources of all the source of financing.

Disadvantages of lease financing

To the Lessor:

- Double taxation: sales tax may be charged twice; first at the time of purchase of assets and second at the time of leasing the asset.

- Unprofitable in case of inflation: lessor gets a fixed amount of lease rental every year and they cannot increase this even if the cost of the asset goes up.

To the Lessee:

- **Ownership**: the lessee will not become the owner of the asset at the end of lease agreement unless he decides to purchase it.
• **Compulsion:** finance lease is non-cancellable and even if a company does not want to use the asset, the lessee is required to pay the lease rentals.

**Plastic Money**

Plastic money is a term used to represent the hard plastic cards used in day to day life in place of actual banknotes. They come in several forms such as debit cards, credit cards, store cards and pre-paid cash cards. The plastic cards began to be used widely after 1970 when the specific standards were set for a magnetic strip. In 1981, the concept of Credit cards was introduced in India and was on the verge of an exceptional boom.

Today the domestic card industry is applied with different types of cards from gold, silver, global, smart to secure, co-branded credit cards, etc. the list is endless. There is enormous growth potential in the domestic card industry.

**Types Of Plastic Money**

**Charge Card:** A charge card has similar features of credit cards. However, after using a charge card, it is necessary to pay the whole amount of bill till the due date. If the person defaults to pay the amount of the charge card, then he has to pay the late payment charges.

**Visa & MasterCard:** Visa & MasterCard are international non-profit organizations. They are dedicated to promoting the growth of the business of cards across the globe. They have designed a wide network of merchant institutions by keeping in mind that the customers might use their credit cards to make several transactions worldwide.

**Debit Cards:** The debit card is an encoded plastic card which is issued by banks and has replaced with the cheques. It allows the customers to pay in exchange for goods and services without carrying cash. It is a multipurpose card, as it can be used as an ATM to withdraw the money and check the balance of the bank account. It is issued by bank free of cost with the savings or current account. It is one of the best online-payment tools where the amount of purchase is immediately subtracted from the account of the customer and credited to the merchant’s account. It has overcome the delay in the payment process.

There are presently two ways in which debit cards transactions are processed:

i) Online debit (also known as a PIN)

ii) Offline debit (also known as signature debit)
ATM Cards: These cards are typically used at ATMs to withdraw money, transfer funds and make deposits. ATM cards are used by inserting the card into a machine and enter a PIN or personal number for security purpose. The system checks the account for sufficient funds before allowing any transaction.

Advantages Of Plastic Money

- **Convenience:** Plastic money provides an easy way to make financial transactions without carrying cash. It also provides the benefits of anywhere and anytime banking.
- **Check Counterfeiting:** The proposed plastic currency notes will reduce the chances of counterfeiting.
- **Long life of Plastic Currency Notes:** The proposed plastic currency notes will have the life of five years as against one-year life of paper currency notes.
- **Check on Black Money:** It is possible to trace the financial transactions done through cards. Developing a culture of plastic money will make it easy for the government to trace black suspected black money sources.
- **Supports Growth of E-commerce:** The use of cards has supported the growth of e-commerce. Growth of e-commerce enhances cost-effectiveness and alternative channels to improve economic growth.
- **Power of Purchasing:** Debit or Credit cards made it easier to buy things. Now we do not have any need to carry money in a large amount. Plastic money is accepted at any time and everywhere.
- **Time-Saving:** one can purchase anything from any place through a credit card or debit card without spending money on fare or cash transaction. You have to provide your card details to seller store or corporations and settle your order. It saves time in the transaction by debit and credit card.
- **Safety:** In case, if an individual loses the cards, then he/she may contact the bank or financial institution, which provide the cards. The financial institution or bank will block the account and no-one can draw a single penny without your permission.

Disadvantages Of Plastic Money
Shops using other Vendors: Numerous shops accept credit cards of a specific company only. In this situation, money is the only mode of payment for those who use a credit card of another company.

Less Availability: There are several cases where the firms do not let their cards to be utilized in specific areas wherever they have a regional dispute.

An issue with Magnetic Strip: The Credit card consists of the magnetic strip that can get worn out due to extensive use of it. If it happens while travelling, and credit card is the only form of money with the person, then he/she must wait till the time they receive a new card. The new card may take a minimum of forty-eight hours to get active.

Increased Debt and rates of high-interest: Credit Card from Corporations and financial institutions charge high-interest rate on more money if the person fails to pay off till the fixed date of the particular month. These interests are the earnings, for which they provide the additional shopping for limits then the money. It is not a good idea to owe loan on high-interest rates and spend it in necessary things or purchasing.

Fraud: In the case of stolen credit cards, the thief may use it directly to get the information. In today’s world, it is possible to get a clone of any debit or credit card, which works like original and can be a substantial loss. Thus be aware of the frauds of credit cards.

Unit 2 - KYC/ AML/ CFT norms

Anti-Money Laundering (PMLA Act 2002)

The offence of money laundering has been defined in Section 3 of the Prevention of Money Laundering Act,2002 (PMLA) as “whosoever directly or indirectly attempts to indulge or knowingly assists or knowingly is a party or is actually involved in any process or activity connected with the proceeds of crime and projecting it as untainted property shall be guilty of offence of money laundering”.

Stages of Money laundering

Placement: Placement is the first stage in the money laundering process. It refers to the physical disposal of proceeds of criminal activity.
Layering: “Layering” refers to the separation of illicit proceeds from their sources by creating complex layers of financial transactions. Layering conceals the audit trial and provides anonymity.

Integration: The third phase is integration, which means placing laundered proceeds into the legitimate economy as normal funds.

The act was amended in the year 2005, 2009 and 2012.

On 24 Nov 2017, In a ruling in favour of citizens' liberty, the Supreme Court has set aside a clause in the Prevention of Money Laundering Act, which made it virtually impossible for a person convicted to more than three years in jail to get bail if the public prosecutor opposed it. (Section 45 of the PMLA Act, 2002, provides that no person can be granted bail for any offence under the Act unless the public prosecutor, appointed by the government, gets a chance to oppose his bail. And should the public prosecutor choose to oppose bail, the court has to be convinced that the accused was not guilty of the crime and additionally that he/she was not likely to commit any offence while out on bail- a tall order by any count.) (It observed that the provision violates Articles 14 and 21 of the Indian Constitution)

Any person who directly or indirectly:

- Attempts to indulge.
- Assists the person who is actually involved in any process.
- Is a party to the activity connected with the proceeds of crime.

As the supply of illegal arms, drug trafficking, and prostitution, which can generate huge amounts of money and projecting or claiming it as untainted property; shall be guilty of the offence of Money Laundering.

The Act was formulated for the following objectives:

- Prevent money-laundering.
- Combat/prevent channelising of money into illegal activities and economic crimes.
- Provide for the confiscation of property derived from, or involved/used in, money-laundering.
- Provide for matters connected and incidental to the acts of money laundering.

Special Court
Section 43 of Prevention of Money Laundering Act, 2002 (PMLA) says that the Central Government, in consultation with the Chief Justice of the High Court, shall, for trial of offence punishable under Section 4, by notification, designate one or more Courts of Session as Special Court or Special Courts for such area or areas or for such case or class or group of cases as may be specified in the notification.

List of Offences

Under PMLA, the commission of any offence, as mentioned in Part A and Part C of the Schedule of PMLA will attract the provisions of PMLA.

Some of the Acts and offences, which may attract PMLA, are enumerated below:

Part A enlists offences under various acts such as:

Indian Penal Code, Narcotics Drugs and Psychotropic Substances Act, Prevention of Corruption Act, Antiquities and Art Treasures Act, Copyright Act, Trademark Act, Wildlife Protection Act, and Information Technology Act.

Part B specifies offences that are Part A offences, but the value involved in such offences is Rs 1 crore or more.

Part C deals with trans-border crimes and reflects the dedication to tackle money laundering across global boundaries.

Obligations Under Prevention of Money Laundering Act, 2002

Section 12 of PMLA, 2002 casts the following reporting obligation of banking companies to the Director, Financial intelligence Unit- India (FIU-IND), besides obligations of record keeping and preservation of information.

Cash Transaction Report (CTR)

All cash transactions of the value of more than Rs 10 lakhs or its equivalent in foreign currency.

All series of cash transactions integrally connected to each other, which have been valued below Rs 10 lakhs or its equivalent in foreign currency where such series of transactions have taken place within a month and the aggregate value of such transactions exceeds Rs 10 lakhs.

All cash transaction where forged or counterfeit currency notes or banknotes have been used as genuine and where any forgery of a valuable security has taken place. However, individual transactions for below Rs 50000 are not to be included in CTR.

Suspicious Transactions Report (STR)

If there are reasonable grounds to believe that the transaction involves proceeds of crime. Suspicious Transaction Report (STR) should be furnished within 7 days of arriving at
a conclusion that any transaction, whether cash or non-cash, or a series of transactions integrally connected are of suspicious nature.

Know your Customer

What is KYC?

KYC is an acronym for “Know your Customer”, a term used for customer identification process. It involves making reasonable efforts to determine true identity and beneficial ownership of accounts, source of funds, the nature of customer’s business, reasonableness of operations in the account in relation to the customer’s business, etc which in turn helps the banks to manage their risks prudently. The objective of the KYC guidelines is to prevent banks being used, intentionally or unintentionally by criminal elements for money laundering.

Is there any legal backing for verifying identity of clients?


What are the features to be verified and documents required to be obtained from customers?

The features to be verified and documents that may be obtained vary depending upon the type of customers. The same are furnished below:

<table>
<thead>
<tr>
<th>Features</th>
<th>Documents</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accounts of individuals</td>
<td>(i) Passport (ii) PAN card (iii) Voter’s Identity Card (iv) Driving License (v) *Job Card issued by NREGA duly signed by an officer of the State Govt (vi) The letter issued by the Unique Identification Authority of India (UIDAI) containing details of name, address and Aadhaar number (vii) Identity card (subject to the bank’s satisfaction) (viii) Letter from a recognized public authority or public servant verifying the identity and residence</td>
</tr>
<tr>
<td>Legal name and any other names used</td>
<td></td>
</tr>
<tr>
<td>Correct permanent address</td>
<td>of the customer to the satisfaction of bank. (i) Telephone bill (ii) Bank account statement (iii) Letter from any recognized public authority (iv) Electricity bill (v) Ration card (vi) Letter from employer (subject to satisfaction of the bank) (any one document which provides customer information to the satisfaction of the bank will suffice)</td>
</tr>
<tr>
<td>Accounts of companies</td>
<td>(i) Certificate of incorporation and Memorandum &amp; Articles of Association (ii) Resolution of the Board of Directors to open an account and identification of those who have authority to operate the account (iii) Power of Attorney granted to its managers, officers or employees to transact business on its behalf (iv) Copy of PAN allotment letter (v) Copy of the telephone bill</td>
</tr>
<tr>
<td>Name of the company</td>
<td></td>
</tr>
<tr>
<td>Principal place of business</td>
<td></td>
</tr>
<tr>
<td>Mailing address of the company</td>
<td></td>
</tr>
<tr>
<td>Telephone/Fax Number</td>
<td></td>
</tr>
<tr>
<td>Accounts of partnership firms</td>
<td>(i) Registration certificate, if registered (ii) Partnership deed (iii) Power of Attorney granted to a partner or an employee of the firm to transact business on its behalf (iv) Any officially valid document identifying the partners and the persons holding the Power of Attorney and their addresses (v) Telephone bill in the name of firm/partners</td>
</tr>
<tr>
<td>Legal name</td>
<td></td>
</tr>
<tr>
<td>Address</td>
<td></td>
</tr>
<tr>
<td>Names of all partners and their addresses</td>
<td></td>
</tr>
<tr>
<td>Telephone numbers of the firm and partners</td>
<td></td>
</tr>
<tr>
<td>Accounts of trusts &amp; foundations</td>
<td>(i) Certificate of registration, if registered (ii) Power of Attorney granted to transact business on its behalf (iii) Any officially valid document to identify the trustees, settlors, beneficiaries and those holding Power of Attorney, founders/managers/directors and their addresses (iv) Resolution of the managing body of the foundation/association (v) Telephone bill</td>
</tr>
<tr>
<td>Names of trustees, settlors, beneficiaries and signatories</td>
<td></td>
</tr>
<tr>
<td>Names and addresses of the founder, the managers/directors and the beneficiaries</td>
<td></td>
</tr>
<tr>
<td>Telephone/fax numbers</td>
<td></td>
</tr>
</tbody>
</table>
| Accounts of Proprietorship Concerns Proof of the name, address and activity of the concern | Registration certificate (in the case of a registered concern)  
• Certificate/licence issued by the Municipal authorities under Shop & Establishment Act,  
• Sales and income tax returns  
• CST/VAT certificate  
• Certificate/registration document issued by Sales Tax/Service Tax/Professional Tax authorities  
• Licence issued by the Registering authority like Certificate of Practice issued by Institute of Chartered Accountants of India, Institute of Cost Accountants of India, Institute of Company Secretaries of India, Indian Medical Council, Food and Drug Control Authorities, registration/licensing document issued in the name of the proprietary concern by the Central Government or State Government Authority/ Department, etc. Banks may also accept IEC (Importer Exporter Code) issued to the proprietary concern by the office of DGFT as an identity document for opening of the bank account. etc.  
• The complete Income Tax return (not just the acknowledgement) in the name of the sole proprietor where the firm's income is reflected, duly authenticated/ acknowledged by the Income Tax Authorities.  
• Utility bills such as electricity, water, and landline telephone bills in the name of the proprietary concern. Any two of the above documents would suffice. These documents should be in the name of the proprietary concern. |
Unit 3- Bankers’ Special Relationship

**Mandate**

- A mandate contract is an agreement between the **parties whereby the mandatary shall have the obligation to perform a task on behalf of the mandator, and the mandator shall only have to pay remuneration, if so agreed upon or provided for by law.**
- The customer informing the bank that he has authorized a person (mandate) to operate the account on his behalf.
- The signatures of the mandate are obtained in the mandate letter and are verified by the customer.
- The mandate is normally issued for a **short and temporary period.**
- A mandate is **not acceptable from institutions. Institutions can issue a power of attorney.**

**Power of attorney**

- **Power of attorney (authorization) is a document in which individuals, representatives at law of legal entities authorize other persons to represent or act on his (her) behalf in establishment and/or performance of civil transactions.**

Two types of POA are generally granted:

- General or Universal
- Special or Limited

**Note:** The mandate and power attorney are the rights cast upon a third person to act on behalf of the principal person/s. The rights of mandate and power of attorney holders are very similar in the operation of bank accounts but they are issued for different reasons and purposes. A mandate is a simple letter of authority, signed by a constituent authorizing the bank to permit a certain named person to operate the account on his/her behalf.
Letter of authority

A letter of authority is to either divulge sensitive material or to delegate a specific task. Whereas a power of attorney gives someone else complete power to act and make decisions on their behalf; here the power could be regarding a specific task, such as purchase of a property, a business deal, etc., or the power could be absolute, i.e. complete power to make all decisions on their behalf.

Comparison between Power of Attorney and Letter of Authority

<table>
<thead>
<tr>
<th></th>
<th>Power of Attorney</th>
<th>Letter of Authority</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Type</strong></td>
<td>Legal document</td>
<td>Legal document</td>
</tr>
<tr>
<td><strong>Function</strong></td>
<td>Delegates power to another person or entity to act and make decisions on their behalf</td>
<td>Delegate sensitive legal, health or financial obligation to another person or entity</td>
</tr>
<tr>
<td><strong>Purpose</strong></td>
<td>To act as you and make decisions on your behalf.</td>
<td>To be present on your behalf and carry out a task.</td>
</tr>
<tr>
<td><strong>Authority</strong></td>
<td>Complete Authority – Can do everything on their behalf</td>
<td>Partial Authority – Can only do something on their behalf</td>
</tr>
<tr>
<td><strong>Contents</strong></td>
<td>Must specify full particulars of the concerned parties and provide precise, in-depth details for clarity and communication purposes.</td>
<td>Must specify full particulars of the concerned parties and provide precise, in-depth details for clarity and communication purposes.</td>
</tr>
<tr>
<td><strong>Power</strong></td>
<td><strong>More Powerful</strong></td>
<td><strong>Less Powerful</strong></td>
</tr>
<tr>
<td>------------</td>
<td>------------------</td>
<td>------------------</td>
</tr>
<tr>
<td><strong>Task used for</strong></td>
<td>Should be used for more complicated or specialized tasks</td>
<td>Should be used for less complicated tasks</td>
</tr>
<tr>
<td><strong>Details</strong></td>
<td>More detailed</td>
<td>Less detailed</td>
</tr>
<tr>
<td><strong>Directions</strong></td>
<td>Sets out the directions in which the tasks should be complete</td>
<td>May or may not specify the directions in which the tasks should be completed</td>
</tr>
<tr>
<td><strong>Notarized</strong></td>
<td>Notarized Certificate</td>
<td>Simple letter. No notary requires.</td>
</tr>
<tr>
<td><strong>Uses</strong></td>
<td>Business Deal, Property Purchase, Make medical decisions on your behalf, etc.</td>
<td>Pick up government documents on your behalf, gain access to your private information or files, collect information on your behalf, pay bills or collect revenue on your behalf, etc.</td>
</tr>
</tbody>
</table>

**Garnishee order**

**What is a garnishee order?**

- A garnishee order is typically issued when a creditor you owe money to has obtained a default judgement from a court or other authority against you. The judgement then allows the creditor to issue a court order that instructs a third party such as your employer, bank or financial institution to redirect your wages or holdings to the creditor you owe money to. Once a garnishee order has been issued, your employer, bank or financial institution is legally obligated to comply with it.
• It is a process of law in favour of judgment- creditor for a debt due from the judgment- debtor (bank customer) upon a third party for attachment. The order is issued the Indian Civil Procedure Code, Order 21 Rule 46, of the Act.

How a garnishee order works

• A default judgement is usually obtained by a creditor either when a debt has gone unpaid, you haven’t been able to come to any agreement with the creditor about repaying the debt, or other alternative debt collection avenues have been exhausted.
• If a garnishee order is made against you, then your bank, financial institution, or employer will likely be notified rather than you. Garnishee orders can be served to anyone that owes you money, such as tenants or contractors.

A garnishee order made to your employer

• If your employer receives a garnishee order, they are required to pay the ordered amount to your creditor out of your wage or salary. The payments will be taken regularly until your debt is paid in full, the court orders the payments to stop or you deploy a formal remedy that will cease the order – such as filing for bankruptcy.

A garnishee order made on your bank accounts

• Garnishee orders can be made on banks and financial institutions, compelling them to put a freeze on your accounts. If this happens, your creditor can typically take the full amount owing from your account, if you have the funds available.

A garnishee order made against others who owe you money

• A court can serve a garnishee order against anyone who owes you money, so tenants, contractors or anyone else with an outstanding debt to you can be garnished without your involvement. They will usually be ordered to pay a lump sum rather than make ongoing payments.

How you may be able to stop a garnishee order

Pay the debt in full

• True, if you were in a position to pay your debt in full, you likely wouldn’t be in this situation to begin with; but if you can find a way to do so, your problem may be resolved and the order could be stopped.

Make alternative repayment arrangements

• Here’s where you might have some wiggle room to negotiate. If you get in touch with your creditor you may be able to discuss other arrangements to pay back the
debt in a way that works for both of you. Your creditor may be open to decreasing the repayment amount and giving you more time to repay.

**Apply to pay by instalments through the court**

- If you’ve tried to negotiate with your creditor but they have declined your proposed alternative arrangements, you can also apply to the court to pay by instalments. You can start this process by lodging a statement of your financial position to support your application and, if the court accepts your application, the garnishee order will be stopped.

**Use the Bankruptcy Act**

- Generally, if you call on the Bankruptcy Act, it is likely your garnishee order will be stopped. If you have any other unsecured debts, this action will also likely resolve those as well.

**Banker’s Lien**

Lien is the right of the banker to retain possession of the goods and securities owned by the debtor until the debt due from the latter is paid. The banker’s lien is an implied pledge. A banker acquires the right to sell the goods which came into his possession in the ordinary course of banking business, in case the debt is not paid. **Section 171 of the Indian Contract Act 1872**, gives to the banker an absolute right of general lien on all goods and securities received by the banker.

**Where is right can apply?**

**To sell:** A banker’s general lien gives the right to sell the debtor’s properties.

**To a specific person:** The right under section 171 is given not only to the banker but also to factors, wharfingers, attorneys of high courts and policy brokers. As such, no separate agreement is required.

**Against the customer:** The right is exercised on the goods and securities of the customer only. The right cannot be exercised when the debtor has a joint account.

**Where is right cannot Apply?**

**Safe Custody Article:** When a customer deposits securities, ornaments and other valuable for their safe custody with a banker, the letter acts as trustee/bailee, therefore the bank cannot exercise the right of lien unless covered by a special agreement.

**Documents/ Money deposited for specific purpose:** Document/money deposited with a specific purpose cannot be taken under lien.
Immature Debts: Lien cannot be exercised when the debt has not yet matured. The bank discounts a 90 days bill for Rs 50000 maturity on 17-11-14 could not have a lien over it before its maturity date.

Banker's Rights- Right of Appropriation

Section 59, 60, 61 of Indian Contract Act, deal with appropriation of payments. If a customer maintains more than one account with a bank and he deposits some amount then he has the first right to indicate to which account the amount should be credited. If he does not exercise this right, then bank can credit the amount to any of his accounts including an account which is time barred by limitation. Clayton's rule is related to appropriation of payments and is applicable in case of running borrowal accounts like cash credit or overdraft. This rule is applicable in case of death, insolvency, insanity of a joint borrower or partner or guarantor or retirement of a partner or revocation of guarantee by guarantor. As per Clayton's rule, credit entry will set off debits in the chronological order of time. This means that first item on the debit side will be discharged first by a credit and so on. For example in a firm's cash credit account, there was a debit balance of Rs 5 lac when one of the partners died. The bank continued operations in the account. Rs 4 lac were deposited and Rs 3 lac were withdrawn. The estate of deceased partner is liable only for one lac i.e 5 lac minus Rs 4 lac.

RIGHT OF SET OFF?

The contract between the banker and borrower is a contract between debtor and creditor. The contract implies that the borrower promised to repay the money borrowed by him. Right of set off is the right of the bank to combine the two accounts of the same person where one account which is in credit balance and the other account is in debit balance in order to cover a loan default. The banker can exercise the right of set-off only when the money owed to him is a sum certain, which is due and where there is no agreement, express or implied to the contrary.

Unit 4- Banking Ombudsman scheme and COPRA Act

Banking Ombudsman Scheme

What is Banking Ombudsman?

- Banking ombudsman, a quasi-judicial authority is formed with an intent to resolve the complaints of the customers of the Bank.
• Section 35A of the Banking Regulation Act, 1949 deals with Banking Ombudsman Scheme. It came into effect in 1995 and presently the Banking Ombudsman Scheme 2006 is in operation.

• The scheme covers not just scheduled Commercial Banks but also Regional Rural Banks and Scheduled Primary Co-operative Banks. Recently, RBI also extended the concept of Banking Ombudsman to NBFC’s as well.

**Areas of customer redressal available with the Ombudsman mechanism**

• Non-payment or unreasonable delay in the payment/collection/issue of cheques, drafts, bills etc.;
• Non-acceptance, without sufficient cause, of small denomination notes and coins tendered for any purpose, and for charging of commission in respect thereof;
• Non-payment or delay in payment of inward remittances;
• Non-adherence to prescribed working hours;
• Delay/failure to provide any banking facility (other than loans and advances) which has been promised in writing by the Bank;
• Delay/ non-credit of proceeds to the respective parties’ accounts, non-payment of deposit or non-observance of the RBI directives, with respect to the rate of interest on bank deposits;
• Complaints from NRIs having accounts in India in relation to their remittances from abroad, deposits and other bank related matters;
• Refusal to open deposit accounts without any valid reason for this refusal;
• Levying charges without adequate prior notice to the customer;
• Non-adherence to RBI instructions on ATM/Debit Card/Prepaid Card/Credit Card operations in India by the bank or its subsidiaries;
• Non-adherence to RBI instruction with regard to Mobile Banking/Electronic Banking service in India;
• Non-disbursement or delay in disbursement of pension (to the extent the grievance can be attributed to the action on the part of the bank concerned, but not with regard to its employees);
• Refusal to accept or delay in accepting payment towards taxes, as asked by Reserve Bank/Government;
• Failure/Delay with regard to the issue, service or redemption of Government securities;
• Forced closure of deposit accounts without any notice or without giving sufficient reason;
• Refusal to close or delay in closing accounts;
• Not following the fair practices code as adopted by the bank;
• Non-observance of Reserve Bank guidelines on engagement of recovery agents by banks;
• Non-adherence to RBI guidelines on allied-banking activities like sale of insurance or mutual fund or other investment products by banks;
• Any other matter relating to the violation of RBI directives.
Limit on the amount of compensation

- **Limit on the amount of compensation (Award):** The amount, to be paid by the bank to the complainant (The person registering the complaint) by way of compensation for any loss suffered by the complainant is the lower of
  - Loss suffered due to any act or omission of the Bank
  - ₹ 20 lakhs (₹ Two Million)
- **In case of mental agony and harassment:** The Banking Ombudsman may award compensation not exceeding ₹1 lakh (₹ One Hundred Thousand) to the complainant. While passing an award (giving compensation), the Banking Ombudsman will consider the following factors
  - Time lost by the complainant
  - Expenses incurred by the complainant
  - Harassment and mental agony suffered by the complainant
- After a receipt of complaint, the Banking Ombudsman will try to settle the complaint through conciliation (agreement) between the aggrieved parties. If a complaint is not settled by an agreement within a period of one month, the Ombudsman proceeds to pass an award. However, before doing so, reasonable opportunity of being heard is given to the complainant and the Bank.
- If one is unhappy with the decision of the Banking Ombudsman, an option is given to file an appeal with the Appellate Authority within a period of 30 days from the date of the receipt of award. Further, if the Appellate Authority is satisfied an extension of another 30 days may be given.

**Ombudsman Scheme for Non-Banking Financial Companies, 2018**

- The RBI introduced an NBFC Ombudsman scheme to redress complaints with regard to NBFCs in 2018.
- The NBFC Ombudsman is a senior official appointed by the RBI to redress customer complaints against NBFCs for deficiency in certain services covered under the grounds of complaint specified under Clause 8 of the Scheme. Four NBFC Ombudsman have been appointed with their offices located at Chennai, Kolkata, New Delhi and Mumbai.

**Consumer Protection Act, 1986 (COPRA Act)**

- The Consumer Protection Act was passed in 1986 and it came into force from 1 July, 1987. The main objectives of the Act are to provide better and all round protection to consumers and effective safeguards against different types of exploitation such as defective goods, deficient services and unfair trade practices. It also makes provisions for simple, speedy and inexpensive machinery for redressal of consumer’s grievances.

**Basic rights of consumers include**
• Right to be protected against marketing of goods and services that are hazardous to life and property
• **Right to be informed about the quality, quantity, standard, and price of goods or services** so as to protect the consumer against unfair trade practices
• Right to receive assured access, wherever possible, to a variety of goods and services at competitive prices
• Right to be heard and to be assured that consumers interests will receive due consideration at appropriate forums.
• Right to seek redressal against unfair trade practices.

The salient features of Consumer Protection Act (CPA), 1986 are as follows

• It applies to all goods, services and unfair trade practices unless specifically exempted by the Central Government.
• It covers all sectors-private, public or co-operative.
• It provides for establishment of consumer protection councils at the central, state and district levels to promote and protect the rights of consumers and a three-tier quasi-judicial machinery to deal with consumer’s grievances and disputes.

**To file the complaint**

• The complaint should be filed within two years of buying the product or using the service
• It needs to be in writing. Letters should be sent by registered post, hand-delivered, email, or fax. Do not forget to take an acknowledgment
• The complaint should mention the name and address of the complainant and the person/entity against whom the complaint is being filed. Copies of relevant documents must be enclosed
• The consumer must mention details of the problem and the demand on the company for redressal. This could be a replacement of the **product, removal of defect(s), refund, or compensation for expenses incurred, and for physical/mental torture.** The claims, however, need to be reasonable
• You should preserve all bills, receipts, and proof of correspondence related to the case. Avoid using voice mail or telephone because such interactions are normally difficult to prove
• There is no compulsion to hire a lawyer. The main cost consists of correspondence and traveling to the **consumer forum for the hearing**
• Maintain a complete record of the emails and documents sent and received

**Appeal**

• An appeal is a legal instrument which enables persons dissatisfied with the findings of a consumer court to approach a higher court to present his case and seek justice. In the context of consumer forums:
• An appeal can be made with the state commission against the order of the district forum within 30 days of the order, which is extendable for further 15 days (Section 15)
• An appeal can be made with the National Commission against the order of the state commission within 30 days of the order or within such time as the National Commission allows (Section 19)
• An appeal can be made with the Supreme Court against the order of the National Commission within 30 days of the order or within such time as the Supreme Court allows (Section 23)

Penalties

• The consumer courts (district court, state commission, and National Commission) are given vast powers to enforce their orders. If a defaulter does not appear in court despite notices and reminders, the court may decide the matter in his absence. The forum can sentence the defaulter to a maximum of three years’ imprisonment and impose a fine of Rs10,000. Forums can issue warrants to produce defaulters in court. They can use the police and revenue departments to enforce orders.

Unit 5- Payment and Collection of cheques and other Negotiable Instruments

Negotiable Instruments Act 1881

The Negotiable Instruments Act, 1881 deals with three kinds of instruments which are widely used in commercial transactions. They are promissory notes, bills of exchange and cheque. Of these instruments, a cheque is used in day to day banking transactions. The Act contains numerous provision about cheques.

A Negotiable Instrument means Promissory Note, Bill of exchange or Cheque payable either to order or to the bearer.

Cheque

Section 6 defined a cheque as follows:

A cheque is a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand and it include the electronic image of a truncated cheque and a cheque in the electronic form.

There is a statutory obligation on the part of a banker to make payment of cheque if:

• The cheque is properly drawn
• There is sufficient balance in the account
• There is no legal restraint on the bank’s duty to pay.

When a cheque is presented for payment, the following aspects should be looked into:

• Promissory Note: A promissory note is a financial instrument that contains a written promise by one party (the note’s issuer or maker) to pay another party (the note’s payee) a definite sum of money, either on demand or at a specified future date

• Bill of Exchange: A bill of exchange is a binding agreement by one party to pay a fixed amount of cash to another party as of a predetermined date or on demand.

• Drawee: The maker of Bill of Exchange or cheque is called the drawer, the person thereby directed to pay is called the Drawee.

• Holder: A holder is a person who legally obtains the negotiable instrument, with his name entitled on it, to receive the payment from the parties liable.

• Holder in Due Course: A holder in due course (HDC) is a person who acquires the negotiable instrument bonafide for some consideration, whose payment is still due

• Payment in Due Course: Payment in accordance with the apparent tenor of the instrument in good faith and without negligence to any person in possession thereof under circumstances which do not afford a reasonable ground for believing that he is not entitled to receive payment of the amount therein mentioned.

• Negotiation: It depends on what form of negotiation you are referring to. If it is negotiating a cheque for example you are referring to a negotiable instrument.

• Endorsement: The act of a person who is a holder of a negotiable instrument in signing his or her name on the back of that instrument, thereby transferring title or ownership is an endorsement. An endorsement may be in favour of another individual or legal entity. An endorsement provides a transfer of the property to that other individual or legal entity. The person to whom the instrument is endorsed is called the endorsee. The person making the endorsement is the endorser.

The Branch on which it is drawn:
Date: A Cheque may bear a future date (Post-dated), current date or an antedate. If a cheque bears a date 3 months prior to the date of presentation.

It is considered to be stale cheque which cannot be paid without revalidation by the drawer.

A post-dated cheque cannot be paid because in such cases, the bank runs the risk of getting stop payment instructions.

Payee: A payee is a person or organization that receives a payment. Payment can be in any form, including cash, a check, a money order, or an electronic transfer of funds. The payee receives the payment from the payer (or “payor” if you prefer), which is the person or organization that makes the payment.

Order cheque or bearer cheque: In simple words a cheque which is payable to any person who presents it for payment at the bank counter is called 'Bearer cheque'. When the word "or bearer" printed on the cheque is cancelled, the cheque is called an order cheque. An order cheque is one which is payable to a particular person.

Crossing a Cheque: A crossing is an instruction to the paying banker to pay the amount of cheque to a particular banker and not over the counter. The crossing of the cheque secures the payment to a banker.

Section 126– Cheque bears across its face an addition of two parallel transverse lines. The banker on whom it is drawn shall not pay it otherwise than to a banker.

Section 129- Banker paying a cheque crossed generally otherwise than to a banker shall be liable to the true owner of the cheque for any loss he may sustain owing to the cheque having been so paid.

Section 128: Banker will lose the protection as given in section 128 of the act.

Section 124: Where a cheque bear across its face an addition of the name of a banker, either with or without the words “Not negotiable”.

Section 126: When a cheque is crossed specially, the banker on whom it is drawn shall not pay otherwise than to the banker to whom it is crossed or his agent for collection.

Section 129: Banker paying a cheque crossed specially otherwise than to a banker to whom it is crossed or his agent for collection shall be liable to the true owner of the cheque for any loss he may sustain owing to the cheque having been so paid.

Section 128: Payment will not be regarded as payment in due course and the banker will loss protection as given in section 128 of the Act.

Section 127: Where a cheque is crossed specially to more than one banker, except when crossed to an agent for the purpose of collection the paying banker shall refused payment thereof.
**Instrument contains any endorsement:** According to **section 15 of the N.I act**, when the maker or holder of a negotiable instrument signs the same, otherwise than as such maker, for the purpose of negotiation, on the back or face thereof or on a slip of paper annexed thereto, he is said to endorse the same.

**Any alteration:** According to **section 87 of the N.I Act**, any material alteration of a negotiable instrument renders the same void as against anyone who is a party thereto at the time of making such an alteration and does not consent thereto, unless it was made in order to carry out the common intention of the original parties.

**Signature of the Drawer:** The signature of the drawer on the cheque is an authority given by the account holder to debit his account with the amount of the cheque.

**Stop- Payment instruction:** Before making payment of the cheque, the bank should see that is no stop payment instruction with respect to the cheque.

**Payment in Due Course- Section 10 (N.I Act 1881)**

"**Payment in due course**" means payment in accordance with the apparent tenor of the instrument in good faith and without negligence to any person in possession thereof under circumstances which do not afford a reasonable ground for believing that he is not entitled to receive payment of the amount therein mentioned.

Protection is available to the paying banker in case of forgery of endorsement in an **order cheque under section 85(1)**, forgery of endorsement in a banker cheque under **section 85(2)**, in case of a materially altered **cheque under section 89** and in case of a **crossed cheque under section 128 if the N.I act**. The condition for getting protection is that the payment made of the cheque should be in due course.

**Liability of the Paying Bank –Section 31**

As per **section 31 of the N.I act**, the drawee bank is under a liability to honour a cheque drawn on its account that is having a sufficient balance.

Sufficient and adequate funds: Following are the circumstance when funds are sufficient and adequate, but not properly applicable.

(a)When payment of a cheque is stopped

(b)When drawer is dead and its intimation received

(c)When funds under a garnishee order/income tax officer/ sales tax department are attached.

(d)When the funds are earmarked for specific purpose.

(e) When the funds are set off by the bank.

(f) When the balance is not a clear balance.
Protection available to the paying banker: A paying banker is entitled for protection under the NI Act in the following cases:

(a) Forged endorsements in an order cheque under Section 85(1)
(b) Forged endorsements in a bearer cheque under section 85(2)
(c) Forged endorsements in a draft under section 85(A)
(d) Material alteration in a cheque under section 89
(e) Payment of a crossed cheque under section 128.

**Crossing of Cheque**

Crossing of a cheque is nothing but instructing the banker to pay the specified sum through the banker only, i.e. the amount on the cheque has to be deposited directly to the bank account of the payee.

**Types of Crossing a cheque**

**General Crossing:** When across the face of a cheque two transverse parallel lines are drawn at the top left corner, along with the words & Co., between the two lines, with or without using the words not negotiable. When a cheque is crossed in this way, it is called a general crossing.

**Restrictive Crossing:** When in between the two transverse parallel lines, the words ‘A/c payee’ is written across the face of the cheque, then such a crossing is called restrictive crossing or account payee crossing. In this case, the cheque can be credited to the account of the stated person only, making it a non-negotiable instrument.

**Special Crossing:** A cheque in which the name of the banker is written, across the face of the cheque in between the two transverse parallel lines, with or without using the word ‘not negotiable’. This type of crossing is called a special crossing. In a special crossing, the paying banker will pay the sum only to the banker whose name is stated in the cheque or to his agent. Hence, the cheque will be honoured only when the bank mentioned in the crossing orders the same.

**Not Negotiable Crossing:** When the words not negotiable is mentioned in between the two transverse parallel lines, indicating that the cheque can be transferred but the transferee will not be able to have a better title to the cheque.

**Double Crossing:** Double crossing is when a bank to whom the cheque crossed specially, further submits the same to another bank, for the purpose of collection as its agent, in this situation the second crossing should indicate that it is serving as an agent of the prior banker, to whom the cheque was specially crossed.

**Bouncing (Dishonour) of Cheques**
This Notice is a Notice which shall be given by the unpaid Creditor (Payee) to the defaulting Debtor (Drawer) through an Advocate in case of dishonour of Cheque under section 138 of Negotiable Instrument Act.

The Notice here is a sample Legal Notice issued by the Advocate of the Payee specifying a 15 days time given to the Drawer in fault to pay the unpaid Cheque amount. It further specifies that if the amount is not paid within 15 days from the receipt of the Notice, the unpaid Payee has right to file legal complaint and initiate Legal Proceeding against the defaulting Drawer.

Due to following reason, the balance in the customer account is considered not available or application for payment:

(a) Payment is stopped by the customer
(b) Death of the Customer
(c) Garnishee order/ attachment orders from courts and/ or revenue authorities
(d) Set-off rights to recover debts due to bank from the customer.

When a cheque is returned unpaid by the bank for reasons:

(a) Insufficient funds
(b) No Arrangement
(c) Exceeds arrangement
(d) Payment stopped
(e) Refer to drawer
(f) Closure of account by drawer

Dishonour of a cheque for Insufficiency of funds/exceed arrangement in the Account- Section 138

(a) The cheque has been presented within 3 months of its validity period.
(b) A demand for payment is made by notice within 30 days of the return of cheque
(c) The Drawer fails to make payment within 15 days of receipt of notice

Section 141- Offences by Companies
Section 143- Summary Trial by Court
Section 144- Made of service of summons
Section 145- Evidence on Affidavit
Section 146- Bank’s slip Prima facie Evidence of certain facts
Section 147 - Offences to Compoundable

Endorsement of Cheques

Endorsement means signing at the back of the instrument for the purpose of negotiation. The act of the signing a cheque, for the purpose of transferring to the someone else, is called the endorsement of Cheque. Section 15 of the Negotiable Instrument Act 1881 defines endorsement. The endorsement is usually made on the back of the cheque. If no space is left on the Cheque, the Endorsement may be made on a separate slip to be attached to the Cheque.

There are six Kinds of Endorsement

Endorsement in Blank / General: An endorsement is said to be blank or general when the endorser puts his signature only on the instrument and does not write the name of anyone to whom or to whose order the payment is to be made. (Section 16)

Endorsement in Full / Special: An endorsement is 'special' or in 'full' if the endorser, in addition to his signature also mention the name of the person to whom or to whose order the payment is to be made. There is direction added by endorse to the person specified called the endorsee, of the instrument who now becomes its payee entitled to sue for the money due on the instrument. (Section 16)

Conditional Endorsement: The conditional endorsement is negotiation which takes effect on the happening of a stated event, or not otherwise. Section 52 of the Negotiable Instrument Act 1881 provides - The endorser of a negotiable instrument may, by express words in the endorsement, exclude his own liability thereon, or make such liability or the right of the endorsee to receive the amount due thereon depend upon the happening of a specified event, although such event may never happen.

Restrictive Endorsement (Section 50): Restrictive endorsement seeks to put an end the principal characteristics of a Negotiable Instrument and seals its further negotiability. This may sound a little unusual, but the endorsee is very much within his rights if he so signs that its subsequent transfer is restricted.

This prevents the risk of unauthorized person obtaining payment through fraud or forgery and the drawer losing his money.

Endorsement Sans Recourse (Without liability Section 52): Sans Recourse which means without recourse or reference. As such a when the property in a negotiable instrument is transferred sans recourse, the endorser, negatives his liability and excludes himself from responsibility to all subsequent endorsees. It is one of the commonest form of qualified endorsement and virtually prohibits negotiation since the endorser says in effect.

Facultative Endorsement: Faculatative Endorsement is an endorsement where the endorser waives some right to which he is entitled. For example, the endorsee is liable to
give notice of dishonor to the endorser and normally failure to give notice will absolve the endorser from his liability.

**Unit 6- Opening accounts of various types of customers**

A banker deals with different types of customers like **Individuals, Partnership firms, Companies, co-operative societies etc.** While opening and in the conduct of accounts of these persons, the banker has to comply with the law application to each of them. Bankers also open current accounts for proprietary concerns, partnership firms, Companies, limited liability partnership firm etc.

**Personal Accounts**

**Accounts of Individual**

- An individual can be a person holding a bank account for personal use. Such customers must comply with existing regulations and bankers must ensure that they do not open and use bank accounts for illegal purposes. The customer should be properly introduced to the bank. The introduction is necessary for terms of banking practice and also for the purpose of protection.

**Joint Account Holder**

A joint account is an account opened by **two or more persons. Instruction for opening the account may be any one of the following:**

- Either or Survivor
- Both Jointly
- Former or Survivor
- Anyone or Survivor

**Rules for Claim of Joint Account**
• On the death of any of the joint account holders, the survivors are entitled to the whole account.
• No right of set off can be exercised in the case of a joint account for the amounts due to the bank in the an individual capacity.
• A deposit made by a Hindu of his money jointly with his wife or any other person, payable to either or survivor, does not, on his death, constitute a gift by him to the other person. The deposit amount in the absence of anything to the contrary, should be presumed to belong to the husband and should therefore pass on the legal heirs of the husband, including the wife who is the survivor.

Accounts of Minor

• A minor is a person who has not completed eighteen years of age. Any contract entered by minor is void and is not enforceable by law. As per section 11 of the Indian Contract Act 1872, “when the age of maturity has been provided by law to be 18 years, any person less than that age, even by a day, would be a minor in law”. This prevents minor to acquire property, dispose property or enter into any type of agreement.
• Guardian means a person having the care of the person of a minor or of his property or both person and property. Guardians may be categorised into following three types:
  • Natural guardian
  • Testamentary Guardian
  • Legal Guardian appointed by a court

Accounts of other Customer

Hindu Undivided Family (HUF)

Hindu Undivided Family (HUF) is not defined under the Income Tax Act but is covered under the Hindu Law. By definition, HUF consists of all individuals who are lineally descended from a common ancestor and also comprises of unmarried daughters. HUF is not formed by a contract but by the status of a family i.e., it is created automatically in any Hindu Family. Having a common ancestor is a pre-requisite to form a HUF.

Create HUF
There are 3 steps involved in creating a HUF. They are mentioned below:

Step 1: Create A HUF Deed

- It is a formal legal document on a stamp paper which clearly states the names of the ‘Karta’ and the co-parceners (other members). In addition to this, another declaration is provided by each family member where they declare the name of ‘Karta’ and agree that
  - the ‘Karta’ has the right to monitor all the transactions of the HUF account on their behalf
  - the members declared in the deed are the only members of the HUF
  - the ‘Karta’ has the authority of the HUF account

Step 2: Apply For HUF PAN Card

- The HUF is considered as a separate entity for tax purposes, it needs to have a separate PAN card. You need to fill the form 49A to apply for the PAN Card. It can be done both offline as well as online.

Step 3: Open HUF Bank Account

- A HUF needs to have a separate bank account which will get all the payments. It can be opened in any bank.

Partnership Firm Account

Section 4 of the Indian Partnership Act, 1932 defines a partnership as a relationship subsisting between persons who have agreed to share the profits of a business carried on by all or any of them acting for all.

How should be the agreement between partners formed?

- Partnership deed is an agreement between the partners in which rights, duties, profits shares and other obligations of each partner is mentioned.
- Partnership deed can be written or oral, although it is always advisable to write a partnership deed to avoid any conflicts in the future.
Following details are required in a partnership deed:

A. General Details:
1. Name and address of the firm and all the partners
2. Nature of business
3. Date of starting of business Capital to be contributed by each partner
4. Capital to be contributed by each partner
5. Profit/loss sharing ratio among the partners

B. Specific Details:
Apart from these, certain specific clauses may also be mentioned to avoid any conflict at a later stage:
1. Interest on capital invested, drawings by partners or any loans provided by partners to firm
2. Salaries, commissions or any other amount to be payable to partners
3. Rights of each partner, including additional rights to be enjoyed by the active partners
4. Duties and obligations of all partners
5. Adjustments or processes to be followed on account of retirement or death of a partner or dissolution of firm.
6. Other clauses as partners may decide by mutual discussion

**Limited Companies**

Company is legal entity and can open accounts in the same way as any other person. There are three types of Limited Companies:

- Public Ltd
- Private Ltd

**Government Companies:** Where 51% of the share are held by the government. The word “limited” is not required to follow the company’s name in such companies.

<table>
<thead>
<tr>
<th>Features</th>
<th>Public limited company</th>
<th>Private limited company</th>
</tr>
</thead>
<tbody>
<tr>
<td>Minimum members</td>
<td>7</td>
<td>2</td>
</tr>
<tr>
<td>Minimum directors</td>
<td>3</td>
<td>2</td>
</tr>
<tr>
<td>Maximum members</td>
<td>Unlimited</td>
<td>200 Section 2(68)</td>
</tr>
<tr>
<td>Minimum capital</td>
<td>5 lakhs (Section 3(i),(iv) of the company Act, 1956)</td>
<td>1 lakh</td>
</tr>
<tr>
<td>----------------</td>
<td>--------------------------------------------------</td>
<td>-------</td>
</tr>
<tr>
<td>Invitation to public</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>Issue of prospectus</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>Quorum at AGM</td>
<td>5 Members</td>
<td>2 Members</td>
</tr>
<tr>
<td>Certificate for commencement of Business (Mandatory)</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>Term used at the end of name</td>
<td>Limited</td>
<td>Private Limited</td>
</tr>
<tr>
<td>Managerial remuneration</td>
<td>No restriction</td>
<td>Can not exceed more than 11% of Net Profits</td>
</tr>
<tr>
<td>Statutory meeting (Mandatory)</td>
<td>Yes</td>
<td>No</td>
</tr>
</tbody>
</table>

**Note:** For Banking in Private limited Maximum number allowed is 20 - Section 3 (i) (iii) of the companies act 1956.

**Trusts**

Mr X wants to pass his bungalow (property) to Mr Y for the benefit of his minor granddaughter. Mr X passes his property to Y, because he reposes (has) confidence on Y. This is nothing but the essence of a trust.

In simple words, a trust is nothing but transfer of property by the owner (Mr X) to another person on whom the owner has confidence (Mr Y) for the benefit of a third person (Granddaughter of X).

**Who are the Parties in a Trust?**

**Author/Settlor/Trustor/Donor (Mr X):** The person who wants to transfer his property and reposes confidence on another for the creation of the trust.

**Trustee (Mr Y):** The person who accepts the confidence for the creation of the trust

**Beneficiary (Mr X’s granddaughter):** The person who will benefit from the trust in the near future.

**What are the objectives of a trust in general?**

The main objective is that the trust should be created for a lawful purpose.

For example, if Mr X had stolen money from a bank and given it to Mr Y with the intention of giving the money to poor children then, in this case the trust itself is void as the very main purpose* is unlawful.
*So how do we actually understand as to whether the purpose is lawful or unlawful? The answer to it lies in Section 4 of the Act.

**As per Section 4, all purposes are said to be lawful unless it:**

- Is forbidden by law
- Defeats the provisions of law
- Is fraudulent
- Involves injury to another person or his property
- Immoral or against to public policy

**Who can create a Trust?**

_A trust may be created by:_

- Every person who is competent to contracts: This includes an individual, AOP, HUF, company etc
- If a trust is to be created by on or behalf of a minor, then the permission of a Principal Civil Court of original jurisdiction is required.
- Further, it also depends on the law in force that is prevailing at that particular point of time and the extent to which the author of the trust may intend to dispose of his property.

**Which are the types of trusts that can be created?**

**Private Trusts:** A private trust is for a closed group. In other words, the beneficiaries can be identified. Eg: A trust created for the relatives and friends of the author.

**Public Trusts:** A public trust is created for a large group ie. the public in large. Eg: Non-Profit NGO's Charitable Institutions for the general public.

**What are the registration mandates for a Private Trust?**

_Section 5 of the Act states that with respect to:_

**Immovable property:** A private trust must be created by a non-testamentary instrument in writing. Further, the non-testamentary instrument needs to be signed by the author of the trust or the trustee and has to be registered. However, if the non-testamentary instrument is created by a will, registration is not necessary.

**Movable property:** A trust in relation to movable property can be declared as in the case of immovable property or by transferring the ownership of the property to the trustee. Hence, registration is not mandatory.
Nomination Facility

The Banking Regulation Act, 1949 has been amended by section 37 of the Banking law (Amendment) Act, 1983 by introducing new section 45 ZA to ZF which provide, inter alia, for information facilities to Banks customer in respect of deposit account, safe deposits, safe vault lockers. The relevant rules framed by the central government with reference to the above sections are termed “the banking companies (nominations) rules 1985”. These rules have come in force with effect from 29 march 1985.

Nomination should be made by the depositor or all depositors in the prescribed format.

- **Form DA-1**- for making nominations by the depositors,
- **Form DA-2**- for cancellation of the said nominations to be made by the depositors.
- **Form DA 3**- for variations of the said nominations to be made by the depositors.

Unit 7- Ancillary Services

Remittance

Remittance means **transfer of funds on branch of a bank to another of the same bank or a different bank**. Customer can make remittance within city through banker’s cheques and for remitting funds from one centre to another through Demand Draft (DD), Mail Transfer (MT), Telegraphic Transfer (TT), National electronic funds transfer (NEFT), and Real Time Gross Settlement (RTGS) at specified service charges.

Demand Drafts (DD) and Banker’s Cheque (BC)

<table>
<thead>
<tr>
<th>BASIS FOR COMPARISON</th>
<th>BANKER’S CHEQUE</th>
<th>DEMAND DRAFT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Meaning</td>
<td>Banker's Cheque or Payment Order is a cheque issued for making the payments within the same city.</td>
<td>Demand draft is a negotiable instrument used to transfer money from one person at one city to another person in another city.</td>
</tr>
<tr>
<td>Special feature</td>
<td>All banker's cheque are pre-printed with &quot;NOT NEGOTIABLE&quot;.</td>
<td>Demand draft of Rs. 20000 or more should be issued with &quot;A/c payee&quot; crossing.</td>
</tr>
</tbody>
</table>
### BASIS FOR COMPARISON

<table>
<thead>
<tr>
<th></th>
<th>BANKER’S CHEQUE</th>
<th>DEMAND DRAFT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Clearance</td>
<td>It can be cleared in any branch of the same city.</td>
<td>It can be cleared at any branch of the same bank.</td>
</tr>
<tr>
<td>Validity</td>
<td>3 months</td>
<td>3 months</td>
</tr>
<tr>
<td>Scale</td>
<td>Bankers cheque can be cleared in any branch of the bank provided it comes under the local jurisdiction</td>
<td>Demand Draft can be cleared at any branch of the same bank irrespective of the city.</td>
</tr>
</tbody>
</table>

### Mail Transfer (MT)

A mail transfer is a way of remitting money from one place to another through a bank. In case payee is a customer, his account is credited. It is used for both internal and international remittances. Bank charges commission for this service.

### Telegraphic Transfer (TT)

Telegraphic transfer, also known as Wire transfer, is an electronic method of transferring funds. In this method, money is transferred from one bank to another via cable services or telegraphs. Earlier, overseas payments via telegraphic transfer was a popular method. Though, telegraph is not used for transfers today, name still remains the same for the transfer of funds electronically or for any wire transfer transactions. Telegraphic transfers are safe and convenient way to transfer funds to people staying overseas. Telegraphic transfer or wire transfer is the most common means of transferring funds overseas.

### What is the Information Required for Telegraphic Transfer?

Here are the important points to be provided for telegraphic transfer:

- Name of the remitter
- Bank account details of remitter
- Payment currency
- Amount to be remitted
- Name of the beneficiary
- Account number of beneficiary or IBAN (International Bank Account Number) for payments to UAE and Europe
- Name and address of beneficiary bank
- Beneficiary bank’s SWIFT (Society for Worldwide Interbank Financial Telecommunication) code and BIC Code (Bank Identifier Code)
- Details of intermediary bank
- Reason or purpose of transfer

### National Electronic Funds Transfer System (NEFT)/ Real Time Gross Settlement System (RTGS)

<table>
<thead>
<tr>
<th>Comparison Category</th>
<th>NEFT</th>
<th>RTGS</th>
<th>IMPS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Settlement Type</td>
<td>Half hourly batches</td>
<td>Real time</td>
<td>Real time</td>
</tr>
<tr>
<td>Minimum Transfer Limit</td>
<td>Re.1</td>
<td>Rs.2 lakh</td>
<td>Re.1</td>
</tr>
<tr>
<td>Maximum Transfer Limit</td>
<td>No Limit</td>
<td>No limit</td>
<td>Rs.2 lakh</td>
</tr>
<tr>
<td>Service Timings</td>
<td>8:00 AM – 7:00 PM all working days except 2nd and 4th Saturday of the month</td>
<td>8:00 AM – 6:00 PM all working days</td>
<td>Available 365 days 24/7</td>
</tr>
<tr>
<td>Transaction Charges</td>
<td>No charges for inward transactions (at destination bank branches for credit to beneficiary accounts)</td>
<td>No charges for inward transactions</td>
<td>Charges for remittance through IMPS are decided by</td>
</tr>
</tbody>
</table>

However, maximum amount per transaction is limited to Rs.50,000/- for cash-based remittances within India and to Nepal under the Indo-Nepal Remittance Facility Scheme.
<table>
<thead>
<tr>
<th>Comparison Category</th>
<th>NEFT</th>
<th>RTGS</th>
<th>IMPS</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>outward transactions for amount:</td>
<td>the individual member banks and PPIs. The taxes are included.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Rs.2 lakh – Rs.5 lakh: not exceeding Rs.25</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Above Rs.5 lakh: not exceeding Rs.50</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>GST is also applicable</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Payment Options</td>
<td>Online and Offline</td>
<td>Online and Offline</td>
<td>Online</td>
</tr>
</tbody>
</table>

**Mobile Banking In India**

Mobile banking started in India in 2002, and back then, transactions were carried out through SMS. Today, almost all banking transactions can be performed using a computer, laptop or a smartphone. Everything from checking account statements to paying credit card bills, utility bills and transferring funds can be done online.

Mobile banking began as an offshoot of internet banking to further aid convenience and ease of access. In 2018, almost all banks have mobile phone applications for financial transactions. These apps remove the requirement of having a computer or laptop to transfer funds, and with continued advancements, have made visits to the bank a rarity.

Note: In 2008, ICICI Bank was the first bank to launch mobile banking in India.

**Safe Deposit Lockers**

Safe Deposit locker is a facility extended to the customer to enable them to keep their valuables/ documents etc, in a specially designed locker on payment of prescribed rentals. The relationship between the bank and the hirer of the lockers is that of a “Lessor and Lessee” or “Bailor and Bailee” (Licensor and Licensee).

Nomination: Section 45 of the Banking Regulation Act deals with the nomination facilities in lockers services. Procedure pertaining to safe deposit lockers is detailed hereunder:

In the case of a singly operated locker, nomination can be made in favour of only one individual.

Where the safe deposit locker is hired by two or more individual jointly, nomination can be made by them in favour of one or more persons.
Important Guidelines of RBI on lockers

1. As per the guidelines banks cannot force customers to buy FD to open a bank locker. But, as a security cover banks can ask customers for a caution money deposit equivalent to three years rent and amount for a forced opening of the locker. This is done because there are instances where the locker is not used by the lock hirers and even the rent is not paid for it.

2. It is mandatory to have an agreement between the locker hirer and the bank. This agreement contains the basic terms and conditions like illegal items would not be stored in the locker, regular payment of dues and so on. The locker hirer should collect the copy of the agreement.

3. Banks have to carry out KYC checks on customers, before providing the locker facility. This has to be done for both old and new customers.

4. All the applications for the bank locker facility must contain a waitlist number.

5. Banks have to take all the necessary steps to safeguard and protect the bank lockers.

6. Locker keys must be embossed with the bank/branch identification code for identifying the owner of the keys.

7. The locker hirer can appoint a single nominee to the bank locker. If the nominee is appointed, he should be given the due rights by the bank.

8. If the bank locker is not operated for a long time, the banks can notify the locker hirer to either operate the locker or to surrender it. The banks should make a request for a written reply, which states the reasons for not operating the locker. If the bank has not received any reply and the locker is still not operated, it has all the right to open the locker forcibly after sending a formal notice to the hirer.

Portfolio Management

What is a Portfolio?

A portfolio refers to a collection of investment tools such as stocks, shares, mutual funds, bonds, cash and so on depending on the investor’s income, budget and convenient time frame.

Following are the two types of Portfolio:

i) Market Portfolio

ii) Zero Investment Portfolio

What is Portfolio Management?
• The art of selecting the right investment policy for the individuals in terms of minimum risk and maximum return is called as portfolio management.
• Portfolio management refers to managing an individual's investments in the form of bonds, shares, cash, mutual funds etc so that he earns the maximum profits within the stipulated time frame.
• Portfolio management refers to managing money of an individual under the expert guidance of portfolio managers.
• In a layman’s language, the art of managing an individual's investment is called as portfolio management.

Need for Portfolio Management

• Portfolio management presents the best investment plan to the individuals as per their income, budget, age and ability to undertake risks.
• Portfolio management minimizes the risks involved in investing and also increases the chance of making profits.
• Portfolio managers understand the client’s financial needs and suggest the best and unique investment policy for them with minimum risks involved.
• Portfolio management enables the portfolio managers to provide customized investment solutions to clients as per their needs and requirements.

Portfolio Management Scheme- RBI Guidelines

• PMS services are provided at the customer’s risk, without guaranteeing them a pre-determined return;
• The services are provided to parties in respect of their long-term investible funds;
• The minimum period, for which funds are placed by the clients, should be one year;
• Funds accepted for portfolio management should not be entrusted to another bank for management;
• Funds are expected to deployed essentially in capital market instruments such as shares, debentures, bonds securities etc, but are
not to be employed for lending in call money/ bill market and lending to/ Placement with corporate bodies;

- The undeployed funds are the same as outside borrowings of the bank and Cash Reserve Ratio (CRR)/ SLR has to be maintained on such funds;

**Merchant Banking**

Role of Merchant Banking in India. basically provide services in the field of marketing, management, legal and financial matters to their clients. Its role ranges from aiding the
person in starting the business, provide ways for raising funds, plays an efficient role in expanding the operations and also helps in reconstructing and reviving of sick business units.

The main business of merchant banking as summarized aptly by Narasimhan Committee in its reports is “Management and Underwriting of new issues, syndication of credit and provision of advisory services to corporate clients on fund raising and other financial aspects.

Following other activities are also covered under merchant banking:

(i) Payment of interest/ Dividend warrants/ refund orders
(ii) Bridge loan against issues

**Unit 8- Cash Management Services and its Importance**

**Important of Cash Management**

Just like a ‘no cash situation’ in our day to day lives can be a nightmare, for a business it can be devastating. Especially for small businesses, it can lead to a point of no return. It affects the credibility of the business and can lead to them shutting down. Hence, the most important task for business managers is to manage cash.

Management needs to ensure that there is adequate cash to meet the current obligations while making sure that there are no idle funds. This is very important as businesses depend on the recovery of receivables. If a **debt turns bad (irrecoverable debt)** it can jeopardize the cash flow. Therefore, cash management is also about being cautious and making enough provision for contingencies like **bad debts, economic slowdown, etc.**

**Development In Cash Management Service**

Cash Management has changed significantly during the last two decades for Two Reasons. **First**: Over the years there was an upward trend in interest rates that increased the opportunity cost of holding cash. This encouraged financial managers to search for more efficient ways of managing cash. **Second**: Technological developments, particularly computerized electronic funds transfer mechanism changed the way cash is managed.

**Importance of Cash Management System**
Cash management refers to a broad area of finance involving the collection, handling, and usage of cash. It involves assessing market liquidity, cash flow, and investments.

In banking, cash management, or treasury management, is a marketing term for certain services related to cash flow offered primarily to larger business customers.

Bank: It may be used to describe all bank accounts (such as checking accounts) provided to businesses of a certain size, but it is more often used to describe specific services such as cash concentration, zero balance accounting, and clearing house facilities. Sometimes, private banking customers are given cash management services.

Treasury management: Financial instruments involved in cash management include money market funds, treasury bills, and certificates of deposit.

**Types of Cash Management Services**

**Products Offered by Banks Under Collections (Paper and Electronic)**

- Local cheque collections
- High value (0 Day clearing)
- Magnetic ink character recognition (MICR)
- Outstation cheque collections
- Cheques drawn on branch locations
- Cheques drawn on correspondent bank locations
- Cheques drawn on coordinator locations
- House cheque collections
- Outside network cheque collections
- Cash collections
- ECS-Debit
- Post dated cheque collection
- Invoice collections
- Capital market collections

**Products Offered by Banks Under Payments (Paper and Electronic)**

- Demand drafts/banker's cheques
- Customer cheques
Principles of Lending

The Business of lending is not without certain risks, especially when the lending banks depend largely on the borrowed funds. The cardinal principles of lending are, therefore, as follows:

- Safety
- Liquidity
- Diversity
- Purpose
- Stability
- Profitability

**Liquidity:** Liquidity is an important principle of bank lending. Bank lend for short periods only because they lend public money which can be withdrawn at any time by depositors. They, therefore, advance loans on the security of such assets which are easily marketable and convertible into cash at a short notice.

**Safety:** The safety of funds lent is another principle of lending. Safety means that the borrower should be able to repay the loan and interest in time at regular intervals without default. The repayment of the loan depends upon the nature of security, the character of the borrower, his capacity to repay and his financial standing.

**Diversity:** In choosing its investment portfolio, a commercial bank should follow the principle of diversity. It should not invest its surplus funds in a particular type of security but in different types of securities. It should choose the shares and debentures of different types of industries situated in different regions of the country. The same principle should
be followed in the case of state governments and local bodies. Diversification aims at minimising risk of the investment portfolio of a bank.

**Purpose:** Loans for undesirable and speculative purposes cannot be granted. Although the earnings on such business activities may be higher, ever then a bank cannot resort to these loans.

**Stability:** Another important principle of a bank’s investment policy should be to invest in those stocks and securities which possess a high degree of stability in their prices. The bank cannot afford any loss on the value of its securities. It should, therefore, invest its funds in the shares of reputed companies where the possibility of decline in their prices is remote.

**Profitability:** This is the cardinal principle for making investment by a bank. It must earn sufficient profits. It should, therefore, invest in such securities which were sure a fair and stable return on the funds invested. The earning capacity of securities and shares depends upon the interest rate and the dividend rate and the tax benefits they carry.

## Non- Fund Based Limits

While ascertaining the credit needs of the borrowers, the bankers should assess both the fund based and non fund based limits required by him together and sanction them as a package. The Non-fund based limits are normally of two types:

(i) Bank Guarantees

(ii) Letters of Credit

**Bank Guarantees:** A bank guarantee refers to a promise provided by a bank or any other financial institution that if a certain borrower fails to pay a loan, then the bank or the financial institution will take care of the losses. The bank will assure the original creditor through this bank guarantee that if the borrower does not meet his or her liabilities, then the bank will take care of them.

While issuing the bank guarantee, the banker has to keep in mind the instructions of RBI with regard to certain purposes that prohibit the issue of bank guarantee and also the extended liability period that has been occasioned consequent to amendment of **Section 128 of Indian Contract** act with respect of Guarantees issue in favour of the government departments.

**A bank guarantee is a contract between 3 different parties and they include:**

i) The applicant (the party that requests a bank guarantee from the bank and borrows from a creditor)

ii) The beneficiary (the party that receives a partial guarantee)
iii) The bank (the party that agrees to sign and assures payment in case the applicant fails to repay the loan)

**Letter of Credit (L/C):** A letter of credit is a document that guarantees the buyer's payment to the sellers. It is Issued by a bank and ensures the timely and full payment to the seller. If the buyer is unable to make such a payment, the bank covers the full or the remaining amount on behalf of the buyer.

While sanctioning the letter of credit limits for the purchase of raw materials, the banker has to collect the following particulars:

(a) Value of raw materials consumed in the ensuring year as projected
(b) Value of raw materials that are purchased on credit out of the above
(c) Time taken for advising the letter of credit to the beneficiary
(d) Time for shipment and the consignment to reach the customer's destination
(e) Credit period (usance period) agreed between the beneficiary and the customer
(f) Credit period projected and reckoned for calculation of the maximum permissible bank finance (MPBF) while sanctioning the funded limits to the borrower customer

**Example:**

Value of raw material consumption projected: Rs 3600 lakhs
Value of raw material (to be) bought on credit: Rs 2400 lakhs
Time for advising L/C: 10 days
Shipment time: 20 days
Credit period agreed upon between the seller and the customer OR the credit period projected as available in CMA format considered for calculation of MPBF while sanctioning funded limits, whichever is less: 30 days

Time required for one cycle of operation of L/C will be 10+20+30= 60 days

Assuming 360 days in a year, there could be 6 rotations/ cycles in a year. If the raw material consumed, to be bought on credit is Rs 2400 lakh in a year, the limit of L/C per rotation/cycle will work out to.

\[
2400\text{lakhs}/6=400\text{lakh}
\]

**Term Loan and Working Capital Loan**

**Term Loan:** A term loan is a loan that is repaid in regular intervals over a pre-agreed period of time. The time period of a term loan can last between one to ten years;
however certain term loans may last as long as 30 years. Term loans are divided into two main categories.

**Fixed Rate Term Loan:** A fixed interest rate loan is a loan where the interest rate does not vary during the term of the loan.

**Floating Rate Term Loan:** In a floating interest rate loan, interest rate fluctuates during the term of the loan.

**Working Capital Loan:** A working capital loan is a short term loan with the aim of financing the day to day business operations of a company. Working capital loans are not used to inject capital into the business or to purchase long-term assets or investments. Instead, it is used for aspects such as to settle accounts payables, pay monthly interest or with regard to any aspect that is involved with current assets and current liabilities.

**Working Capital Requirement = Inventory+ Accounts Receivables – Accounts payable**

**Difference between Term Loan and Working Capital Loan**

<table>
<thead>
<tr>
<th>Term Loan</th>
<th>Working Capital Loan</th>
</tr>
</thead>
<tbody>
<tr>
<td>Term loan is a form of borrowing where the payments can be made over a predetermined period of time in regular intervals.</td>
<td>Working capital loan is a loan taken out to finance routine business operations to minimize shortfalls in working capital.</td>
</tr>
<tr>
<td>Term loans may be short, medium or long term.</td>
<td>Working capital loans are short term loans. (Quarterly and Half Yearly)</td>
</tr>
<tr>
<td>Repayment of a term loan is done by many installments.</td>
<td>Repayment of a working capital loan is done by a limited number of installments.</td>
</tr>
<tr>
<td>The amount of the loan is based on the cost of running the business, since such loans are customized in accordance with the regular expenses incurred to run a business.</td>
<td>Covers high-cost investments like business expansion, purchase of expensive plant and machinery, etc.</td>
</tr>
</tbody>
</table>

**Estimation of working Capital Needs**

The Conditions of commercial banks for lending on a short term basis are rigorous. A customer has to satisfy his bank about his character, capacity, capital and collateral, in brief he has to establish his creditworthiness. If the overall appraisal is satisfactory, the bank will finance only the residual gap in the customers resources, after taking into consideration the expected availability from all other sources of funds.
There are four methods of estimating the working capital requirement of a borrower:

(i) The Operating cycle method
(ii) The Projected net working capital method
(iii) The Projected turnover method
(iv) The cash budget

There methods required the preparation of:

(i) Projected financial statements
(ii) Projected fund flow statements
(iii) Projected cash flow statements/cash budgets

**Operating cycle method**

Operating cycle method for estimating working capital is based on the duration of the operating cycle. Longer the period of the cycle, bigger will be the working capital requirements. Operating cycle means the cycle of raw material to work in progress to finished goods to accounts payable and finally to cash. Operating cycle time is the time taken starting from raw material purchases to its conversion into cash.

In order to provide a relief to borrowers who face such a situation, the banks as part of their loan policy, decided as follows:

(i) While assessing working capital requirement, creditors will not be set off against stock.

(ii) The borrowers will submit detail age-wise list of sundry creditors and sundry debtors as well as the stock statement.

(iii) Only those debtors will be considered who are outstanding for less than the period specified (up to 180 days maximum) from a case to case basis.

(iv) The borrower will have to hypothecate his entire book debts to the bank

(v) The bank will not finance the borrower’s book debts if creditors exceed debtors.

**Example of Operating cycle:**

- Procurement of raw material: 30 days
- Conversion/process time: 15 days
- Average time of holding of finished goods: 15 days
- Average collection period: 30 days
• Total operating cycle: 90 days
• Operating cycle in a year: 4
• Total operating expenses per annum: 60 lakhs
• Total turnover per annum: 70 lakhs
• Working capital requirement: 16/4 = 15 lakhs

The Projected net working capital method

The Margin requirements have to be met by the borrower from the accruals during the course of the year and other long term funds, in the form of net working capital. The projected net working capital, of higher than the current level maintained by the borrower, would be built up progressively with the growth in production, sales and profits.

Projected Turnover method

Banks, as a matter of policy and based on RBI guidelines, assess the working capital requirements including those of village industries, tiny industries (SSI units and traders) with a fund based working capital limit of up to Rs 5 cr. by the turnover method.

Turnover Method is used to assess the working capital requirement of any borrower based on the turnover of the business. This method was originally suggested by the P.J. Nayak Committee for the Small Scale Industries in India in need of working capital from banks.

RBI has given following instructions:

(a) 20% of their projected annual gross sales turnover may be considered as minimum working capital finance by banks.
(b) In order to ensure that a minimum margin supports the working capital needs of a borrower, a 5% contribution is given promoters.
(c) Guideline for the turnover method is framed, assuming an average operating cycle of 3 months. If the cycle is more than 3 months, the borrower should bring in a proportionately higher stake in relation to his requirement of the bank finance.
(d) Drawing power is calculated through stock statement. Unpaid stacks are not to be financed, as it would result in double financing.

Example of calculating working capital requirement under projected annual turnover method:

Projected sales: Rs. 1000000

Working capital requirements: 25% of projected sales = Rs 250000

Margin (Contribution of Owner): 5% of projected sales = Rs 50000
Working capital to be funded by bank: Rs200000

**Cash Budget System**

The current loan policies of most banks state that, for an assessment of the working capital needs of a borrower who enjoys or requires fund based limits in excess of Rs 10crs. The cash budget system should be used.

**Cash budget has to have the following steps in sequence when prepared for a quarter.**

(a) Actual receipts and payments during the first, the second and the third month.

(b) The Position of the cash surplus/deficit is computed at monthly intervals. A surplus is generated of the receipts exceed the payment and a cash deficit occurs if payments are more than the receipts during the month.

(c) The opening cash balance for the first month is adjusted against the cash surplus/deficit that is generated during the month. The adjusted figure is the closing balance at the end of the first month, which becomes the opening balance for the next month viz… the second month.

(d) A cash surplus generated during a month results in a higher closing cash balance via- to vis opening balance of the month, Conversely, a cash deficit during the month would cause a lower level of the closing cash balance as compared to the opening balance.

(e) If the enterprise has a net position on borrowed funds (The company maintain cash credit/overdraft account), a cash surplus generated during a month brings down the level of the borrowed funds at the end of the month.

**Base Rate system**

The concept of base rate was **introduced on July 1, 2010**, at all banks across India. Before the base rate system, **BPLR (Benchmark Prime Lending Rate), (Chairman: Shri Deepak Mohanty)** was employed. However, with the implementation of base rate system, the credit pricing became more transparent. Here is an article that explains in-depth about the base rate and other related information, which you might require for assistance to comprehend better.

The base rate is the minimum rate of interest that is set by a **country’s central bank for lending a loan**. This rate is usually taken as the standard interest rate by all the banks functioning in that country. Once the base rate is announced by the central bank, no bank is permitted to offer any type of loan to its customers at a rate that is lower than the base rate that has been set by the central bank of a nation.

**As per RBI guidelines (as in July 2012), the following categories of loans could be priced without reference to Base Rate :**

(a) DRI Advances;
(b) Loans to banks’ own employees including retired employees;
(c) Loans to banks’ depositors against their own deposits

**Difference between Benchmark Prime Lending Rate (BPLR) and Base Rate**

**Benchmark Prime Lending Rate (BPLR)** is the rate at which commercial banks charge their customers who are most credit worthy. According to the Reserve Bank of India (RBI), banks can fix the BPLR with the approval of their Boards. However, the RBI stipulates the interest rates as BPLR is influenced by the Repo rate and Cash Reserve Ratio (CRR) apart from individual bank's policy.

However, the BPLR system failed to bring transparency in the lending rates of the banks. The calculations of BPLR is not that transparent and sometimes the banks under this system could lend to customers below the BPLR. So, Base Rate was introduced subsequently.

**Base rate** is the minimum interest rate of a bank, below which it cannot lend, except for DRI allowances, loans to bank's own employees and loans to bank’s depositors against their own deposits. The base rate system has replaced the BPLR from July 1, 2010. Since then the BPLR is gradually losing its importance except for the loans taken before July 1, 2010. In such cases, RBI has allowed to continue with BPLR at which the loans were approved. They were, however, given the option of switching to the base rate before the expiry of their loans. RBI does not fix the base rate. Individual banks fix their own base rates and so each bank has its own base rate.

**Who Calculates The Base Rate In India?**

The RBI (Reserve Bank of India) calculates the base rate in India. The RBI sets this to bring uniform rates to all banks in India.

A base rate comprises of all the elements of lending rates, which are common among the borrowers of various categories.

**Note:** Lending rate is the rate of interest that a bank lends to its customers. A lending rate includes the operating cost of a product, tenor premium, credit risk premium, and the borrower-specific cost. Therefore, it differs from one segment to the other.

**How Is Base Rate Calculated?**

The calculation of base rate is based on different factors. A few of them are:

- Deposit cost
- Administrative cost
- Unallocated overhead cost
The amount of profit a bank earns in the last financial year

**Applicability Of The Base Rate**

- Every loan category should be priced based on the base rate that has been set by the Reserve Bank of India. But a few loans can be priced without referring to the current base rate. These include the DRI advances, loans to a bank’s depositor on their deposits, and loans to a bank’s employees.

- The base rate set by the central bank or the RBI also serves as a reference benchmark for the floating rate of a loan.

- Any modifications in the base rate are applicable to all the existing loans that are associated with the current base rate.

- The base rate set by the central bank is always minimum. Therefore, no bank is allowed to give a rate below than what is set to its customers.

It is mandatory for every bank to review its base rate on a quarterly basis. This action has to be taken only after the ALCOs (Asset Liability Management Committees) or the board approves it. Since the primary intention of implementing the base rate system is to sustain transparency in the prices of a lending product, every bank has to reveal its base rate details at all the branches and their official websites too.

Any modifications in the base rate have to be conveyed to the public frequently via appropriate channels. In addition, it is compulsory for all the banks to give proper details to the RBI regarding the minimum & maximum lending rates on a quarterly basis.

**Credit Management**

Credit management is the process of granting credit, setting the terms it's granted on, recovering this credit when it's due, and ensuring compliance with company credit policy, among other credit related functions. The goal within a bank or company in controlling credit is to improve revenues and profit by facilitating sales and reducing financial risks.

A credit manager is a person employed by an organization to manage the credit department and make decisions concerning credit limits, acceptable levels of risk, terms of payment and enforcement actions with their customers. This function is often combined with Accounts Receivable and Collections into one department of a company. The role of credit manager is variable in its scope and Credit managers are responsible for:

- Controlling bad debt exposure and expenses, through the direct management of credit terms on the company's ledgers.
• Maintaining strong cash flows through efficient collections. The efficiency of cash flow is measured using various methods, most common of which is Days Sales Outstanding (DSO).

• Ensuring an adequate Allowance for Doubtful Accounts is kept by the company.

• Monitoring the Accounts Receivable portfolio for trends and warning signs.

• Hiring and firing of credit analysts, accounts receivable and collections personnel.

• Enforcing the "stop list" of supply of goods and services to customers.

• Removing bad debts from the ledger (Bad Debt Write-Offs).

• Setting credit limits.

• Setting credit terms beyond those within credit analysts' authority.

• Setting credit rating criteria.

• Setting and ensuring compliance with a corporate credit policy.

• Pursuing legal remedies for non-payers.

• Obtaining security interests where necessary. Common examples of this could be PPSA's, letters of credit or personal guarantees.

• Initiating legal or other recovery actions against customers who are delinquent.

### Credit Monitoring

Credit Monitoring is the tracking of an individual's credit history, for any changes or suspicious activities. A credit monitoring service is will show an individual's credit report provide them with new information regarding new credit inquiries, accounts etc. The individual also can ensure if this information is actually genuine. Credit Monitoring can also be used by individuals to keep a check on their credit score, as well as keep track of them, giving them the option to be well of their credit history before applying for loans and mortgages. The process of monitoring takes many steps to ensure negligent loans in parameters of the credit policy followed when it comes to delinquency. The credit management section will ensure the collection of the loans.

#### Step Involved Credit Monitoring

• Identify the potential NPAs when the loan default is for two months.

• Study the causes- whether default is due to inherent weaknesses or due to temporary liquidity or cash flow problem.
• Offer contingency help immediately in the form of ad-hoc limits if cash flow mismatches are genuine.

• If limit are found to be inadequate lending to loan default during the year, ask the borrower to submit the renewal proposal and enhance suitably.

• Visit the factory immediately, if the stock statement is not submitted and verify the securities.

• Keep the documents live, scrutinize them periodically.

• Implement the report of the concurrent auditor, statutory auditor, branch inspector, credit audit, regional manager's report etc.

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**Unit 10- Priority Sector Advances**

Priority Sector Lending is an important role given by the (RBI) to the banks for providing a specified portion of the bank lending to few specific sectors like agriculture and allied activities, micro and small enterprises, poor people for housing, students for education and other low income groups and weaker sections. This is essentially meant for an all round development of the economy as opposed to focusing only on the financial sector.

**What are the Targets and Sub-targets for banks under priority sector**

The targets and sub-targets for banks under priority sector are as follows:

<table>
<thead>
<tr>
<th>Categories</th>
<th>Domestic scheduled commercial banks (excluding Regional Rural Banks and Small Finance Banks) and Foreign banks with 20 branches and above</th>
<th>Foreign banks with less than 20 branches</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total Priority Sector</strong></td>
<td>40 per cent of Adjusted Net Bank Credit or Credit Equivalent Amount of Off-Balance Sheet Exposure, whichever is higher.</td>
<td>40 per cent of Adjusted Net Bank Credit or Credit Equivalent Amount of Off-Balance Sheet Exposure, whichever is higher, to be achieved in a phased manner by 2020.</td>
</tr>
</tbody>
</table>
### Different categories under priority sector

**Priority Sector includes the following categories:**

(i) Agriculture  
(ii) Micro, Small and Medium Enterprises  
(iii) Export Credit  
(iv) Education  
(v) Housing  
(vi) Social Infrastructure  
(vii) Renewable Energy  
(viii) Others  

**Agriculture:**

Direct finance to agriculture shall include short, medium and long term loans given for agriculture and allied activities directly to individual farmers, Self-Help Groups (SHGs) or Joint Liability Groups (JLGs) of individual farmers without limit and to others (such as corporate, partnership firms and institutions) **up to Rs. 2crs.,** for taking up agriculture/allied activities.

Indirect finance to agriculture shall include loans given for agriculture and allied activities as specified in Section I, appended.
This distinction between direct and indirect agriculture is dispensed with. Instead, the lending to agriculture sector has been re-defined to include (i) Farm Credit (which will include short-term crop loans and medium/long-term credit to farmers) (ii) Agriculture Infrastructure and (iii) Ancillary Activities.

**Indirect Finance to Agriculture**

(i) If the aggregate loan limit per borrower is more than Rs 2 cr. in respect of para 20.3.1 (ii) above, the entire loan will be treated as indirect finance to agriculture.

(ii) Loans up to Rs 5 crs. to producer companies set up inclusively by only small and marginal farmer under part IXA of companies Act 1956 for agricultural and allied activities.

**Other Indirect Agriculture Loans**

(i) Loans up to Rs 5 crs. per borrower to dealers/sellers of fertilizers, pesticides, seeds, cattle feed, poultry feed, agricultural implements and other inputs.

(ii) Loans up to Rs 5 crs to cooperative societies of farmers for disposing of the produce of members.

**Micro and Small Enterprises**

**Manufacturing Sector:**

- Enterprises: Investment in plant and Machinery
- Micro Enterprises: Do not exceed Rs 25 lakhs
- Small Enterprises: More than Rs 25 lakhs but does not exceed 5 crs.

**Service Sector:**

- Enterprises: Investment in equipment
- Micro Enterprises: Do not exceed Rs 10 lakhs
- Small Enterprises: More than Rs 10 lakhs but does not exceed 2 crs.

**Education**

Education loans include loans and advances granted to only individuals for educational purposes.

- Up to Rs. 10 lakh for studies in India
- Rs. 20 lakh for studies abroad.
Housing

In terms of the above Master Direction for RRBs, loans to individuals up to ₹ 20 lakh for purchase/construction of a dwelling unit per family provided the overall cost of the dwelling unit does not exceed ₹ 25 lakh are eligible to be classified under priority sector. In terms of the Compendium for SFBs, loans to individuals up to ₹ 28 lakh in metropolitan centres (with population of ten lakh and above) and ₹ 20 lakh in other centres, are eligible to be classified under priority sector, provided that the cost of dwelling unit does not exceed ₹ 35 lakh and ₹ 25 lakh, respectively.

In order to bring the RRBs and SFBs at a level playing field with other Scheduled Commercial Banks, it has now been decided to enhance the housing loan limits for eligibility under priority sector lending. Accordingly, in respect of RRBs and SFBs, housing loans to individuals up to ₹ 35 lakh in metropolitan centres (with population of ten lakh and above) and ₹ 25 lakh in other centres, provided the overall cost of the dwelling unit in the metropolitan centres and at other centres does not exceed ₹ 45 lakh and ₹ 30 lakh, respectively will be eligible for classification under Priority Sector Lending.

Furthermore, the existing family income limit of ₹ 2 lakh per annum, prescribed under Para 9.4 of the above Master Direction for RRBs/Para 5.4 of the Compendium for SFBs, eligible for loans to housing projects exclusively for the purpose of construction of houses for Economically Weaker Sections (EWS) and Low Income Groups (LIG), is revised to ₹ 3 lakh per annum for EWS and ₹ 6 lakh per annum for LIG, in alignment with the income criteria specified under the Pradhan Mantri Awas Yojana.

Social infrastructure

Bank loans up to a limit of ₹50 million per borrower for building social infrastructure for activities namely schools, health care facilities, drinking water facilities and sanitation facilities including construction/ refurbishment of household toilets and household level water improvements in Tier II to Tier VI centres.

Renewable Energy

Bank loans up to a limit of ₹150 million to borrowers for purposes like solar based power generators, biomass based power generators, wind mills, micro-hydel plants and for non-conventional energy based public utilities viz. street lighting systems, and remote village electrification. For individual households, the loan limit will be ₹1 million per borrower.

Weaker Sections

Priority sector loans to the following borrowers will be considered under Weaker Sections category:

- Small and marginal farmers
- Artisans, village and cottage industries where individual credit limits do not exceed ₹0.1 million
- Beneficiaries under Government Sponsored Schemes such as National Rural Livelihood Mission (NRLM), National Urban Livelihood Mission (NULM) and Self Employment Scheme for Rehabilitation of Manual Scavengers (SRMS)
- Scheduled Castes and Scheduled Tribes
- Beneficiaries of Differential Rate of Interest (DRI) scheme
- Self Help Groups
- Distressed farmers indebted to non-institutional lenders
- Distressed persons other than farmers, with loan amount not exceeding ₹0.1 million per borrower to prepay their debt to non-institutional lenders
- Individual women beneficiaries up to ₹0.1 million per borrower
- Persons with disabilities
- Overdraft limit to PMJDY account holder up to ₹10,000/- with age limit of 18-65 years.
- Minority communities as may be notified by Government of India from time to time.

**Non-achievement of Priority Sector targets**

- Small Finance Banks having any shortfall in lending to priority sector shall be allocated amounts for contribution to the Rural Infrastructure Development Fund (RIDF) established with NABARD and other Funds with NABARD/NHB/SIDBI/ MUDRA Ltd., as decided by the Reserve Bank from time to time. The achievement will be arrived at the end of financial year based on the average of priority sector target/sub-target achievement as at the end of each quarter.
- While computing priority sector target achievement, shortfall / excess lending for each quarter will be monitored separately. A simple average of all quarters will be arrived at and considered for computation of overall shortfall / excess at the end of the year. The same method will be followed for calculating the achievement of priority sector sub-targets. (Illustrative example given in Annex)
The interest rates on banks’ contribution to RIDF or any other Funds, tenure of deposits, etc. shall be fixed by Reserve Bank of India from time to time.

The misclassifications reported by the Reserve Bank's Department of Banking Supervision would be adjusted/ reduced from the achievement of that year, to which the amount of declassification/ misclassification pertains, for allocation to various funds in subsequent years.

Non-achievement of priority sector targets and sub-targets will be taken into account while granting regulatory clearances/approvals for various purposes.

**Common guidelines for priority sector loans**

Small Finance Banks should comply with the following common guidelines for all categories of advances under the priority sector.

(i) **Rate of interest**: The rates of interest on bank loans will be as per directives issued by our Department of Banking Regulation from time to time.

(ii) **Service charges**: No loan related and adhoc service charges/inspection charges should be levied on priority sector loans up to ₹25,000. In the case of eligible priority sector loans to SHGs/ JLGs, this limit will be applicable per member and not to the group as a whole.

(iii) **Receipt, Sanction/Rejection/Disbursement Register**: A register/ electronic record should be maintained by the bank, wherein the date of receipt, sanction/rejection/disbursement with reasons thereof, etc., should be recorded. The register/electronic record should be made available to all inspecting agencies.

(iv) **Issue of Acknowledgement of Loan Applications**: Banks should provide acknowledgement for loan applications received under priority sector loans. Bank Boards should prescribe a time limit within which the bank communicates its decision in writing to the applicants.

**Unit 11- Agricultural Finance**

India’s Economic is basically an agricultural economy. Nearly 70% of our population depend upon agriculture.

**Short term Loans**

Loans repayable up to **18 months are termed as short loans**. This includes: **Crop loan and the limits sanctioned through Kisan Credit Cards scheme** for raising crops, loan against gold ornaments for agricultural purposes.
Medium/ Long Term Loan

The Period of credit under this category is more than 30 months. This includes loan for the purpose of minor irrigation, farm/land development, farm mechanization, plantation, horticulture, dairy farming, sheep/goat rearing, piggery and poultry etc.

Crop loan

Crop loan is a short-term advance that is given to the farmers and agriculturists by banks and co-operative societies. The loan amount can be used to purchase improved seeds, fertilizers, machinery etc. The crop loans are provided as agriculture is a priority sector.

Revised Scheme for Issue of Kisan Credit Card (KCC)

The Kisan Credit Card (KCC) scheme was launched in 1998 with the aim of providing short-term formal credit to farmers. Owner cultivators as well as tenant farmers can avail loans to meet their agricultural needs under this scheme at attractive rates of interest. The government has also simplified the application process to increase interest among farmers. Repayment is also simplified and dependent on the harvesting season, reducing the farmers’ debt burden.

Longer Repayment Period for Kisan Credit Card (KCC) Loans

- Most of the banks in India which offer the Kisan Credit Card (KCC) loans are looking for a longer loan repayment tenure for the loans. This has been suggested as the agriculture sector is under significant pressure. The cycle of the loans provided under the Kisan Credit Card scheme has been proposed to be increased to 36 or 48 months from the 12 months. This was proposed at the state level bankers’ consultancy meet in West Bengal.

- In addition to the enhancement of the loan repayment tenure, the banks have also proposed that the farmers should be allowed to avail extra loans even after failing to repay the previous loan. However, in order to do that, they should service the interest. Public sector banks have started a 3-stage consultation process recently on the basis of the directions passed by the Department of Financial Services.

- The main focus of the consultation process would be to discuss 9 important issues. These include credit offered to MSMEs and agriculture sectors, digital banking, direct transfer of benefits, and education loans. The previous meeting was an intra-bank meet. However, this time the meeting will be an inter-bank meet at a state level.

Features of Kisan Credit Cards
Credit to meet the financial requirements of agricultural and other allied activities.

Ancillary credit for crop production and other contingencies.

Investment credit for agricultural requirements such as dairy animals, pump sets etc.

 Produce marketing loans.

 Post-harvest expenses.

 Insurance coverage for Kisan Credit Card holders, including asset insurance and personal accident insurance scheme (PAIS).

 All farmers who are eligible for the Kisan Credit Card will be issued a smart card cum debit card in addition to the Kisan Credit Card.

 The facility of revolving credit is available for any amount of withdrawals and repayments made within the credit limit. However, instalments of the amount withdrawn have to be repaid within 12 months.

 Based on the annual review, banks will determine the validity of the existing credit card.

 Credit limits can be increased at the issuing bank’s discretion to accommodate for changes in cropping pattern, increase in operating costs, etc. as an incentive for good record on credit card usage.

 Conversion/rescheduling of loans also permissible in case of damage to crops due to natural calamities.

 According to the RBI, the fixing of Kisan Credit Card interest rates as well as credit limits can be set by the respective issuing bank. The average interest rate applicable ranges from 9-14% p.a.

 In addition, there are certain subsidies and schemes that the government offers farmers with regard to the interest rate. These would depend on the repayment history and general credit history of the cardholder.

Benefits of Kisan Credit Cards

 Flexible repayment options and hassle-free disbursement procedure.

 Single credit facility/ term loan for all agricultural and ancillary requirements.

 Assistance in the purchase of fertilizers, seeds, etc. as well as in availing cash discounts from merchants/ dealers.
Credit is available for a **period of up to 3 years** and repayment can be made once the harvest season is over.

- Minimal documentation and maximum flexibility offered for withdrawal of the required funds from the issuing bank.
- Funds can be withdrawn from any of the bank’s branches across the country.

**Eligible for a Kisan Credit Card Loan Scheme?**

- Are an individual farmer who is an owner-cultivator.
- Belong to a group and are joint borrowers. The group has to be owner-cultivators.
- Are a sharecropper, tenant farmer, or an oral lessee.
- Are a self-help group (SHG) or joint liability group (JLG) of sharecroppers, farmers, tenant farmers, etc.

**Eligible beneficiaries under this scheme under fisheries and animal husbandry are:**

**Inland Fisheries and Aquaculture:** Fish farmers, fishers, SHGs, JLGs, and women groups. As a beneficiary, you must own or lease any activity related to fisheries. This includes owning or leasing a pond, an open water body, a tank, or a hatchery among others.

**Marine Fisheries:** You own a registered boat or any other type of fishing vessel and you have the necessary license or permissions for fishing in estuaries or the sea.

**Poultry:** Individual farmers or joint borrowers, SHGs, JLGs, and tenant farmers of sheep, rabbits, goats, pigs, birds, poultry, and have sheds they have owned, rented, or leased.

**Dairy:** Farmers, dairy farmers, SHGs, JLGs, and tenant farmers who own, lease, or rent sheds.

**Scale of finance in KCC?**

**Based on the type of farming you undertake, the KCC limit varies.**

- For single-crop farmers: Scale of finance for the crop (decided by the District Level Technical Committee) $\times$ area cultivated $+$ **10% of limit** towards post-harvest or household consumption $+$ **20% towards repairs** and maintenance of the farm + crop insurance.
- The limit for each successive year will be **increased by 10%**.
- Farmers with multiple crops: The same pattern is followed as for single-crop farmers.
- Marginal farmers: **Up to Rs.50,000.**
What security should be provided at the time of application?

At the time of application, the following security is to be provided:

- **For card limits up to Rs.1 lakh** - Hypothecation of crops as per prevailing RBI guidelines.
- **For card limits up to Rs.3 lakh** – Hypothecation of crops, additional collateral security at the issuing bank’s discretion.

Insurance under Kisan Credit Card Scheme

- The Kisan Credit Card provides for personal accident insurance which farmers can opt for. Farmers will receive coverage of **up to Rs.50,000 in the event of death** and **Rs.25,000 in the event of an accident resulting in disability**. The premiums payable would be decided by the bank in conjunction with the insurance provider.
- This coverage is optional and farmers who choose to opt for it should meet the eligibility criteria as ascertained by the bank and insurance provider.

Selected Activities Under Agricultural Finance

**Agricultural Term Loan**

**Purpose:** Agricultural Term Loans (ATL) aims to rejuvenate poor Indian Farmers who always becomes prey of local money lenders. RBI and NABARD regulate agricultural loans and providing refinance to banking institutions (commercial, rural, cooperative etc.) on reasonable terms. It helps to deregulate rate of interest and increased flow of credit to the agriculture sector.

**Note:** Banks gives agricultural term loans in the form of direct finance to cultivators to create assets facilitating crop production / income generation. Repayments **span not less than 3 years and not exceeding 15 years.** Activities broadly covered are land development, minor irrigation, farm mechanization, plantation and horticulture, dairying, poultry, sericulture, dry land, waste land development schemes, etc.

**Eligibility:** All categories of farmers-small / medium-and agricultural labourers are eligible for agricultural term loans, provided they have necessary experience in the activity and the required land area.

**Land Development**

**Purpose:** Credit for land development project, in the form of direct finance to cultivators, for better productivity. Loan under this head cover various activities like land clearance (removal of bushes, tress, etc).

**Eligibility:** All farmer owning agricultural land are eligible.
Minor Irrigation

- Water conservation and water harvesting
- Drought proofing including afforestation and tree plantation
- Irrigation canals including micro and minor irrigation works
- Provision of irrigation facilities, plantation, horticulture, etc.
- Renovation of traditional water bodies, including desilting of tanks
- Flood control and protection works, including drainage in water-logged areas.

Farm Mechanisation

Mechanised agriculture is the process of using agricultural machinery to mechanise the work of agriculture, greatly increasing farm worker productivity. In modern times, powered machinery has replaced many farm jobs formerly carried out by manual labour or by working animals such as oxen, horses and mules.

The entire history of agriculture contains many examples of the use of tools, such as the hoe and the plough. The ongoing integration of machines since the Industrial Revolution however has allowed farming to become much less labour-intensive.

Financial to Horticulture

**Purpose:** Loans for development of fruit orchards like mango, chikoo, guava, grapes etc. as well as short-term fruit crops (banana, pineapple etc), flower in open and greenhouse (rose, carnation, jasmine etc) and vegetable crop (potato, tomato, peas etc) are financed.

Poultry farming

Poultry farming is the form of animal husbandry which raises domesticated birds such as chickens, ducks, turkeys and geese to produce meat or eggs for food.

Dairy farming

Dairy farming is a class of agriculture for long-term production of milk, which is processed (either on the farm or at a dairy plant, either of which may be called a dairy) for eventual sale of a dairy product.

Vermi Culture (Vermicompost)

Vermicompost is the product of the decomposition process using various species of worms, usually red wigglers, white worms, and other earthworms, to create a mixture of decomposing vegetable or food waste, bedding materials, and vermicast. Vermicast is the end-product of the breakdown of organic matter by earthworms.
Minimum Support Price

Minimum Support Price (MSP) is a form of market intervention by the Government of India to insure agricultural producers against any sharp fall in farm prices. The minimum support prices are announced by the Government of India at the beginning of the sowing season for certain crops on the basis of the recommendations of the Commission for Agricultural Costs and Prices (CACP). MSP is price fixed by Government of India to protect the producer - farmers - against excessive fall in price during bumper production years. The minimum support prices are a guarantee price for their produce from the Government. The major objectives are to support the farmers from distress sales and to procure food grains for public distribution. In case the market price for the commodity falls below the announced minimum price due to bumper production and glut in the market, government agencies purchase the entire quantity offered by the farmers at the announced minimum price.

Crops covered

Government announces minimum support prices (MSPs) for 22 mandated crops and fair and remunerative price (FRP) for sugarcane. The mandated crops are 14 crops of the kharif season, 6 rabi crops and two other commercial crops. In addition, the MSPs of toria and de-husked coconut are fixed on the basis of the MSPs of rapeseed/mustard and copra, respectively. The list of crops are as follows.

- Cereals (7) - paddy, wheat, barley, jowar, bajra, maize and ragi
- Pulses (5) - gram, arhar/tur, moong, urad and lentil
- Oilseeds (8) - groundnut, rapeseed/mustard, toria, soyabean, sunflower seed, sesamum, safflower seed and nigerseed
- Raw cotton
- Raw jute
- Copra
- De-husked coconut
- Sugarcane (Fair and remunerative price)
- Virginia flu cured (VFC) tobacco

National Agricultural Insurance Scheme

National Agricultural Insurance Scheme (NAIS) was introduced by the Government of India to provide insurance coverage and financial subsidy to the farmers in the event of
crop losses suffered on account of natural calamities, pests and diseases. This scheme aims to help stabilise farm incomes, particularly in disaster years.

**Eligibility Criteria**

This scheme is applicable to all farmers including both the farmers-loanee and non-loanee farmers irrespective of their size of holding. This National Agricultural Insurance Scheme covers the following groups of farmers listed below:

Based on compulsory form, all farmers including sharecroppers and tenant farmers growing the notified crops in the notified areas and availing Seasonal Agricultural Operations (SAO) loans from Financial Institutions (i.e.) Loanee Farmers.

Based on voluntary form, all other farmers growing notified crops (i.e., Non-Loanee farmers) are eligible to opt for the Scheme.

**Features of the Scheme**

The below following are some of the main features and benefits of applying for a National Agricultural Insurance Scheme.

- Corps Covered
- Food crops (Cereals, Millets and Pulses)
- Oilseeds
- Sugarcane, Cotton and Potato

**Limit of Coverage**

At the option of insured farmers, the SI may extend to the value of the threshold yield of the insured crop. Further, a farmer may also ensure his crop beyond the threshold yield value level up to 150% of average yield value of notified area on premium payment at commercial rates.

**Premium Rates**

A premium subsidy of 50% applies to the small and Marginal farmers to be shared equally by the Indian Government and State/ UT Government. The premium bonus will be phased out in a period of 3 to 5 years, subject to analysis of the financial results and the reply of the farmers at the end of the 1st year of the implementation of the Scheme.

The below tabulated are the premium rates of the crops:

<table>
<thead>
<tr>
<th>Season</th>
<th>Crops</th>
<th>Premium Rates</th>
</tr>
</thead>
</table>
### Kharif
- Bajra and Oilseeds
- Other crops (cereals, other millets and pulses)

<p>| | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>3.5% of Sum Insured or Actuarial rate, whichever is less</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2.5% of Sum Insured or Actuarial rate, whichever is less</td>
<td></td>
</tr>
</tbody>
</table>

### Rabi
- Wheat
- Other crops (other cereals, millets, pulses and oilseeds)

<p>| | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1.5% of SI or Actuarial rate, whichever is less</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2.0% of Sum Insured or Actuarial rate, whichever is less</td>
<td></td>
</tr>
</tbody>
</table>

### Kharif and Rabi
- Annual Commercial / annual Horticultural crops
- Actuarial rates

**Note:** The actuarial rates would be applied at District/ Region/ State level at the option of the State Government/ UT.

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### Unit 12- Micro, Small and Medium Enterprise in India

The **Micro, Small and Medium Enterprises Development (MSMED) Act, 2006**, governs the coverage and investment ceiling of MSMEs in India.

According to the Act, there are **two categories of MSMEs in the country** –

**Manufacturing:** Manufacturing Enterprises-he enterprises engaged in the manufacture or production of goods pertaining to any industry specified in the first schedule to the industries **(Development and regulation) Act, 1951** or employing plant and machinery in the process of value addition to the final product having a distinct name or character or use. The Manufacturing Enterprise are defined in terms of investment in Plant & Machinery.

**Service Enterprises:** The enterprises engaged in providing or rendering of services and are defined in terms of investment in equipment. The limit for investment in plant and machinery / equipment for manufacturing / service enterprises, as notified,vide S.O. 1642(E) dtd.29-09-2006 are as under
Manufacturing Sector

<table>
<thead>
<tr>
<th>Enterprises</th>
<th>Investment in plant &amp; machinery</th>
</tr>
</thead>
<tbody>
<tr>
<td>Micro Enterprises</td>
<td>Does not exceed twenty five lakh rupees</td>
</tr>
<tr>
<td>Small Enterprises</td>
<td>More than twenty five lakh rupees but does not exceed five crore rupees</td>
</tr>
<tr>
<td>Medium Enterprises</td>
<td>More than five crore rupees but does not exceed ten crore rupees</td>
</tr>
</tbody>
</table>

Service Sector

<table>
<thead>
<tr>
<th>Enterprises</th>
<th>Investment in equipments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Micro Enterprises</td>
<td>Does not exceed ten lakh rupees</td>
</tr>
<tr>
<td>Small Enterprises</td>
<td>More than ten lakh rupees but does not exceed two crore rupees</td>
</tr>
<tr>
<td>Medium Enterprises</td>
<td>More than two crore rupees but does not exceed five crore rupees</td>
</tr>
</tbody>
</table>

Performance & Credit Rating Scheme

This scheme seeks to establish independent, trusted third party opinion on capabilities and credit-worthiness of MSEs, and makes credit available at attractive interest rates and will ensure better productivity. Under this scheme (as per the turnover of the MSE) a percent of Rating Agency charges are reimbursed by Ministry of SSI.

Scheme Benefits & Highlights

The fee to be paid to the rating agencies shall be based on the turnover of the Small-Scale Units which has been categorized into three slabs. The slabs of the Turnover and the Share of Ministry of SSI towards the fee charged by the Rating Agency is as follow:

Turnover of MSE Re-imbursement of fee through NSIC:

1. Up to Rs. 50 lakh - 75% of the fee or INR25,000 (whichever is less)
2. Above Rs. 50 to 200 lakh - 75% of the fee or INR30,000 (whichever is less)
3. More than Rs. 200 lakh - 75% of the fee or INR40,000 (whichever is less)

Credit Guarantee

Any collateral / third party guarantee free credit facility (both fund as well as non fund based) extended by eligible institutions, to new as well as existing Micro and Small Enterprise, including Service Enterprises, with a maximum credit cap of of 200 lakh (Rupees Two Hundred lakh only) are eligible to be covered. Recently, guarantee coverage made eligible to select NBFCs and Small Finance banks.

The guarantee cover available under the scheme is to the extent of 50%/ 75% / 80% & 85% of the sanctioned amount of the credit facility. The extent of guarantee cover is 85%
for micro enterprises for credit up to 5 lakh. The extent of guarantee cover is 50% of the sanctioned amount of the credit facility for credit from 10 lakh to 100 lakh per MSE borrower for retail trade activity.

The extent of guarantee cover is 80% (i) Micro and Small Enterprises operated and/or owned by women; and (ii) all credits/loans in the North East Region (NER) for credit facilities up to 50 lakh. In case of default, Trust settles the claim up to 75% of the amount in default of the credit facility extended by the lending institution for credit facilities up to 200 lakh.

<table>
<thead>
<tr>
<th>Category</th>
<th>Maximum extent of Guarantee where credit facility is</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Upto 5 lakh</td>
</tr>
<tr>
<td>Micro Enterprises</td>
<td>85% of the amount in default subject to a maximum of 4.25 lakh</td>
</tr>
<tr>
<td>Women entrepreneurs/ Units located in North East Region (incl. Sikkim) (other than credit facility up to 5 lakh to micro enterprises)</td>
<td>80% of the amount in default subject to a maximum of 40 lakh</td>
</tr>
<tr>
<td>All other category of borrowers</td>
<td>75% of the amount in default subject to a maximum of 37.5 lakh</td>
</tr>
<tr>
<td>Activity</td>
<td>From 10 lakh upto 100 lakh</td>
</tr>
<tr>
<td>MSE Retail Trade</td>
<td>50% of the amount in default subject to a maximum of 50 lakh</td>
</tr>
</tbody>
</table>

**What is the CGTMSE?**

The whole idea behind this trust is to provide financial assistance to these industries without any third party guarantee/ or collateral. These schemes provide the assurance to the lenders that in case of default by them a guarantee cover will be provided by trust in the ratio of 50/75/80/85 percent of the amount so given. The objectives of this fund are:

To check the financial viability of the project of these companies

To give term loans and composite credit schemes

As per this scheme, a loan of up to Rs. 200 lakhs can be given to MSMEs. A special preference is given to the women entrepreneurs who are eligible for this scheme. Loans are also provided to borrowers who are located in the Northeastern States of India including Sikkim and Jammu and Kashmir.

**What are the fees charged by the CGTMSE?**
The fees charged by the trust fund is a percentage of 1% p.a of the amount so sanctioned:

- 0.75% – for credit of up to Rs. 5 Lakhs
- 0.85% for credit above Rs. 5 Lakhs but up to Rs. 100 Lakh

The credit guarantee available under this scheme is 75/80% of the amount so given to a maximum cap of Rs. 62.5 Lakh / 65 Lakh for a credit facility of up to Rs. 50 Lakhs. The percentage guarantee is 85% for microenterprises for a sum of up to Rs. 5 lakhs. The percentage of guarantee is 50% of the amount so sanctioned for a credit of above Rs. 50 Lakhs with a maximum limit of Rs. 100 Lakhs. The tenure of the guarantee is a block of 5 years.

**Time Norms for Disposal of Applications**

With the switch over to the simple turnover method for all advance on the SME segment up to Rs. 5crs, the time for processing of the applications and sanction has to be curtailed as under (from the date of submission of complete paper by the borrower):

<table>
<thead>
<tr>
<th>Limits</th>
<th>Time Limit not exceeding</th>
</tr>
</thead>
<tbody>
<tr>
<td>Up to and including Rs25000/-</td>
<td>4 Business Days</td>
</tr>
<tr>
<td>Over Rs 25000 and Up to Rs 10lakhs</td>
<td>8 Business Days</td>
</tr>
<tr>
<td>Over Rs 10 lakhs up to 5 crs.</td>
<td>12 Business Days</td>
</tr>
<tr>
<td>Over 5 Crs.</td>
<td>20 Business Days</td>
</tr>
</tbody>
</table>

**Unit 13- Government Sponsored Scheme**

**Swarnajayanti Gram Swarozgar Yojana**

*Swarnajayanti Gram Swarozgar Yojana (SGSY)* was enacted in the dawn of the financial year of 1999-2000 as a replacement of six other affiliated schemes. The initiative was designed as an integrated program that caters to the self-employment of the rural poor. It is funded by the Centre and the State in a 75:25 ratio and is implemented by commercial banks, regional banks and cooperative banks. Other financial institutions, Panchayat Raj institutions, District Rural Development Agencies (DRDAs), Non-Government Organizations (NGOs), and technical institutions in the district will also undertake the process of planning, implementing and monitoring the scheme. This article seeks to create awareness of this self-employment scheme.
Following existing Scheme:

- Integrated Rural Development Program (IRDP)
- Training of Rural Youth for Self-Employment (TRYSEM)
- Development of Women and Children in Rural Areas (DWCRA)
- Supply of Improved Toolkits to Rural Artisans (SITRA)
- Ganga Kalyan Yojana (GKY)
- Million Wells Scheme (MWS)

Purpose:

The scheme is established with the intent of bringing the assisted low-income families (also referred to as swarozgaris) above the poverty line by providing them with an appreciable sustained income over a period of time. This shall be fulfilled by organizing the rural poor into Self-Help Groups (SHGs) through the process of social mobilization, training, capacity building and provision of income generating assets.

The scheme envisages the development of activity clusters with an emphasis on key activities identified in the block, both for the group as well as for individual assistance. These activity clusters will be in geographic clusters of neighbouring villages within a reasonable radius.

Self-Help Groups

The Self-Help Groups (SHGs) will be organized by ‘Swarozgaris’ drawn from the BPL list approved by the Gram Sabha. The scheme facilitates the formation of Self-Help Groups (SHGs), who will be assisted on a loan-cum-subsidy.

Coverage of the Scheme

The scheme caters to the rural communities such as those with land, landless labour, educated unemployed, rural artisans and the disabled. The assisted low-income families could be either individuals or groups and would be selected from Below Poverty Line (BPL) families by a three-member team comprising of a Block Development Officer (BDO), banker and sarpanch.

The scheme specifically focuses on the vulnerable sections of the rural poor. The SC/ST would gain the bulk of assistance (50%), while a proportion of the remaining funds would be earmarked for women and the disabled.

The scheme is aimed at the development of Swarozgaris through training courses that are designed in accordance with the activities selected and the requirements of each swarozgari.
The scheme entails the following processes:

**Group Creation** – This stage covers the assessment of the skill level of the members.

**Capital Creation** – This involves the use of a rotating fund system. Here, the members are facilitated to hone their skills through experience.

**Implementation** – the final stage deals with the identification and nurturing of abilities and group skills. The implementation is processed according to the pace desired by the respective groups.

The subsidy allocation for the scheme is as follows:

- A uniform subsidy of **30% of the total project cost** is allowed under the scheme, subject to a **ceiling of Rs. 7,500**.

- A subsidy of **50% of the total project cost**, subject to a ceiling of **Rs. 10,000** is extended to SC/STs and disabled persons.

- A subsidy of **50% of the total project cost**, subject to a ceiling of **Rs. 1.25 lakh or per capita subsidy of Rs. 10,000** (whichever is less) is provided to Self-Help Groups (SHGs) and individual swarozgaris.

- No monetary limits on subsidy have been specified for irrigation projects.

- Subsidy under these provisions is back-ended. The banks are prohibited from charging interest on the subsidy portion of the loan amount.

- As already stated, special emphasis will be laid on vulnerable groups among the rural poor

**Security Norms**

For **Individual Loans up to Rs. 50000 and group loans up to Rs. 5 lakhs**, the assets created out of the bank loan would be hypothecated to the bank as primary security.

**Swarna Jayanti Shahari Rozgar Yojana**

Swarna Jayanthi Shahari Rozgar Yojana was launched as a replacement of three other schemes that addressed poverty alleviation, namely Nehru Rozgar Yojana (NRY), Urban Basic Services for the Poor (UBSP), and Prime Minister's Integrated Urban Poverty Eradication Program (PMIUPEP). The scheme was later refurbished in the year 2009 with revised guidelines. This article seeks to provide awareness of this welfare initiative.

**Funding Pattern**
The scheme will be funded on a ratio of 75:25, wherein the Central Government contributes the majority and the state governments the least. The ratio of funding differs for special category states, where the same has been affixed as 90:10 in a similar proportion between the Central and State Governments.

The states classified as special category includes:

- Arunachal Pradesh
- Sikkim
- Tripura
- Jammu & Kashmir
- Himachal Pradesh
- Uttarakhand
- Assam
- Manipur
- Meghalaya
- Mizoram
- Nagaland

Purpose:

The scheme is primarily aimed at providing profitable employment to the urban unemployed and the underemployed poor by encouraging the setting up of self-employment ventures or provision of wage employment. Its other objectives include:

Promotion of skill development and training programs so as to provide the urban poor with access to employment opportunities opened up by the market to undertake self-employment.

The Empowerment of the community to address the issues of urban poverty through suitable self-managed community structures like Neighborhood Groups (NHGs), Neighborhood Committees (NHC), Community Development Society (CDS), etc.

Components of the Scheme

The scheme consists of five major components, which are:

- Urban Self-Employment Program (USEP)
- Urban Women Self-Help Program (UWSP)
• Skill Training for Employment Promotion amongst Urban Poor (STEP-UP)
• Urban Wage Employment Program (UWEP)
• Urban Community Development Network (UCDN)

**Urban Self-Employment Program**

This component is further classified into two sub-components, which includes:

Assistance to individual urban poor beneficiaries for setting up profitable self-employment ventures (loan and subsidy).

Technology/marketing/infrastructure/knowledge and other support provided to the urban poor for setting up their enterprises as well as marketing their products (technology, marketing and other support).

**Target Groups**

The benefits of USEP are extended to the **BPL (Below the Poverty Line)** segment of the urban population. The program lays special emphasis on women, people associated with the Scheduled Castes (SC)/Scheduled Tribes (ST), differently-abled people and such other categories as may be indicated by the Government from time-to-time.

**Identification of Beneficiaries**

The beneficiaries will be spotted through a **house-to-house survey, with a focus on slums and low-income settlements**. Model Formats for executing slum survey, household survey and livelihoods survey will be laid out by the Ministry of Housing & Urban Poverty Alleviation. Community strucutures such as Neighborhood Groups, Neighborhood Committees and Community Development Societies are entrusted with the task of identifying the beneficiaries through the assistance of the City/Town Urban Poverty Alleviation Cell (UPA Cell). Assistance for this purpose could also be sought from NGOs or other identified bodies.

**Focus Sectors**

For the purpose of self-employment, the focus areas include the production sector, the services sector, and the business sector.

**Financing Pattern**

Listed below are the particulars of financing pattern under the program:

- **Maximum allowable subsidy** – 25% of the Project Cost subject to a maximum of Rs. 50,000.
- **Margin** – 5% of the project cost.
• Collaterals – Nil

• Permitted Financial Support to Micro Business Centres – up to Rs. 80 lakhs per MBC (efforts must for the gradual self-sustenance of these MBCs).

**Urban Women Self-Help Program (UWSP)**

This particular component proposes the following:

- Assistance to groups of urban poor women for setting up profitable self-employment ventures – UWSP (Loan & Subsidy).

- Revolving Funds for Self-Help Groups (SHGs)/Thrift and Credit Societies (T&CSs) formed by the urban poor women – UWSP (Revolving Fund).

**Urban Women Self-Help Group Programme (Loan & Subsidy)**

This program envisages the provision of a special incentive for the urban poor women who are on the pursuit of self-employment ventures in a group as opposed to individual effort. Groups of urban poor women may adopt an economic activity in accordance with their skill, training, aptitude, and local conditions. Apart from income generation, this group strategy entails the empowerment of the urban poor women by making them independent and providing a conducive atmosphere for self-employment.

The UWSP group will be entitled to a subsidy of **Rs. 3,00,000/35% of the cost of project/Rs. 60,000 per Member of the Group (the lower of the three)**. The remaining sum will be mobilized as Bank Loan and Margin.

**Urban Women Self-Help Program (Revolving Fund)**

While the UWSP group sets itself as a Self-Help Group (SHG)/Thrift and Credit Society (T&CS), they shall also be entitled to a lump sum grant of **Rs. 25,000** as revolving fund at the **rate of Rs. 2000 (at the max) per member**. Such funds are also extended to a simple Self-Help Group/Thrift and Credit Society.

Revolving funds are meant for the use of SHG/T&CS for purposes such as:

- Procurement of raw material and marketing.

- Infrastructure support (for income generation and other group activities).

- Expenses within the range of Rs. 500 (to meet the travel costs of group members for visits to bank, town UPA Cell, etc).

**Prime Minister’s Employment Generation Programme**
Generation of sustainable and continuous self-employment opportunities in urban and rural areas of the country.

Providing sustainable and continuous employment to a large segment of rural and urban unemployed youth, traditional and prospective artisans through the establishment of micro-enterprises

Facilitating the financial institution's participation for higher credit flow to the micro sector

**Eligibility**

- Individuals with age of **18 years or more**
- Passing standard VIII is required for a project above **Rs 5 lakh in the service sector and above Rs 10 lakh in the manufacturing sector**
- Institutions registered **under Societies Registration Act- 1860**
- Production based co-operative societies
- Self-help groups and charitable trust

**Salient features of the scheme**

- The Scheme is implemented through Khadi and Village Industries Commission, State Khadi and Village Industries Commission Directorates, State Khadi and Village Industries Boards and District Industries Centres and banks in Urban and Rural areas in the ratio of 30:30:40 between Khadi and Village Industries Commission / Khadi and Village Industries Boards / DIC respectively.
- Assistance under the PMEGP is only available to new units that are to be established.
- There is no income ceiling for setting up projects.
- Existing units or units that are already availing any government subsidy (State or Central) are ineligible.
- Any industry including coir based projects (excluding those mentioned in the negative list) can take advantage of this scheme.
- The per capita investment under the scheme should not exceed Rs 1 lakh in plain areas and Rs 1.5 lakh in hilly areas.
- Maximum project cost Rs 10 lakh in the service sector and Rs 25 lakh in the manufacturing sector is this limit.

**Areas of Operation**

Rural area, as stated under Khadi and Village **Industries Commission Act 2006** – Scheme, means the area comprised in any village and includes the area comprised in any town. The
population should not exceed twenty thousand or such other figure as the Central Government may specify from time to time.

In the urban area, only District Industries Centres (DIC) are included.

**Margin**

- The margin **money contribution is 5%** of the cost of the project for **special category borrowers and 10% for General category borrowers**.

- Illustration: Suppose Miss Nishitha applies to **XYZ bank for Rs 8 lakh loan**, the bank might finance only **80% of the loan amount (ie Rs 6,40,000/-)**. The **balance 20% (ie Rs 1,60,000/-)** is called as margin money and Nishita has to make arrangements for the same.

**Subsidy**

**General Category:** The eligible **subsidy is 25%** of the cost of the project in rural areas and **15% in urban areas**.

**Special Category:** The eligible **subsidy is 35%** of the cost of the project in rural areas and **25% in urban areas**.

**Quantum of margin money subsidy**

<table>
<thead>
<tr>
<th>Categories of beneficiaries under PMEGP</th>
<th>Beneficiary's own contribution (of project cost)</th>
<th>Rate of Subsidy</th>
</tr>
</thead>
<tbody>
<tr>
<td>General Category</td>
<td>10%</td>
<td>Urban 15% Rural</td>
</tr>
<tr>
<td>Special Category (including SC/ST/OBC /Minorities/ Women, Ex-Servicemen, Physically handicapped, NER, Hill, and Border areas etc)</td>
<td>5%</td>
<td>25% 35%</td>
</tr>
</tbody>
</table>

**How does this scheme work?**

Let’s assume Mr. Don, a young new entrepreneur from Bangalore Urban, wants to apply for the PMEGP scheme

**Estimated Project Cost** – Rs 10 lakh

**Mr. Don’s Contribution (Mandatory as per PMEGP)** – Rs 1 lakh (10% of Rs 10 lakh)

**Amount Received By Mr. Don** – Rs 9 lakh
Note: The margin money (ie 15% of the Project Cost – Rs 1,50,000/-) generally withheld by the bank will be reimbursed to the bank by KVIC within 24 hours of acceptance of the PMEGP application. Hence, entrepreneurs like Mr. Don can get the required capital to proceed with their venture very easily/

Note:

Banks will finance capital expenditure in the form of a term loan and working capital in the form of cash credit. Projects can also be financed in the form of composite loan consisting of capital expenditure and working capital.

The bank credit will be ranging **between 60-75%** of the cost after deducting (Margin Money) subsidy and the owner’s contribution.

Though banks will claim subsidy on the basis of the projections of capital expenditure mentioned in the project report, Margin Money can be availed only on the actual availment of capital expenditure and excess if any, is to be refunded to KVIC.

Working Capital component should be utilized in such a manner that at one point it should touch **100% limit of the cash credit within 3 years** of the lock-in period of margin money and not less than **75% utilization of the sanctioned limit**.

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**Unit 14- Self Help Groups**

**What are SHGs?**

Self-Help Groups (SHGs) are informal associations of people who choose to come together to find ways to improve their living conditions.

It can be defined as self governed, peer controlled information group of people with similar socio-economic background and having a desire to collectively perform common purpose.

Villages face numerous problems related to poverty, illiteracy, lack of skills, lack of formal credit etc. These problems cannot be tackled at an individual level and need collective efforts.

Thus SHG can become a vehicle of change for the poor and marginalized. SHG rely on the notion of “Self Help” to encourage self-employment and poverty alleviation.

**Functions**

- It looks to build the functional capacity of the poor and the marginalized in the field of employment and income generating activities.
- It resolves conflicts through collective leadership and mutual discussion.
• It provides collateral free loan with terms decided by the group at the market driven rates.

• Such groups work as a collective guarantee system for members who propose to borrow from organised sources. The poor collect their savings and save it in banks. In return they receive easy access to loans with a small rate of interest to start their micro unit enterprise.

• Consequently, Self-Help Groups have emerged as the most effective mechanism for delivery of microfinance services to the poor.

Need for SHGs

• One of the reasons for rural poverty in our country is low access to credit and financial services.

• A Committee constituted under the chairmanship of Dr. C. Rangarajan to prepare a comprehensive report on 'Financial Inclusion in the Country' identified four major reasons for lack of financial inclusion:

• Inability to provide collateral security,

• Poor credit absorption capacity,

• Inadequate reach of the institutions, and Weak community network.

• The existence of sound community networks in villages is increasingly being recognised as one of the most important elements of credit linkage in the rural areas.

• They help in accessing credit to the poor and thus, play a critical role in poverty alleviation.

• They also help to build social capital among the poor, especially women. This empowers women and gives them greater voice in the society.

• Financial independence through self-employment has many externalities such as improved literacy levels, better health care and even better family planning.

Genesis of SHG

• The Genesis of SHG in India can be traced to formation of Self-Employed Women’s Association (SEWA) in 1970.

• The SHG Bank Linkage Project launched by NABARD in 1992 has blossomed into the world’s largest microfinance project.
• NABARD along with RBI permitted SHGs to have a savings account in banks from the year of 1993. This action gave considerable boost to the SHG movement and paved the way for the SHG-Bank linkage program.

• In 1999, Government of India, introduced Swarn Jayanti Gram Swarojgar Yojana (SGSY) to promote self-employment in rural areas through formation and skillling of SHGs.

• The programme evolved as a national movement in 2011 and became National Rural Livelihoods Mission (NRLM) – world's largest poverty alleviation programme.

• Today, State Rural Livelihood Missions (SRLMs) are operational in 29 states and 5 UTs (except Delhi and Chandigarh).

• NRLM facilitated universal access to the affordable cost-effective reliable financial services to the poor like financial literacy, bank account, savings, credit, insurance, remittance, pension and counselling on financial services.

Benefits of SHGs

Social integrity – SHGs encourages collective efforts for combating practices like dowry, alcoholism etc.

Gender Equity – SHGs empowers women and inculcates leadership skill among them. Empowered women participate more actively in gram sabha and elections.

There is evidence in this country as well as elsewhere that formation of Self-Help Groups has a multiplier effect in improving women’s status in society as well as in the family leading to improvement in their socio-economic condition and also enhances their self-esteem.

Pressure Groups – their participation in governance process enables them to highlight issues such as dowry, alcoholism, the menace of open defecation, primary health care etc and impact policy decision.

Voice to marginalized section – Most of the beneficiaries of government schemes have been from weaker and marginalized communities and hence their participation through SHGs ensures social justice.

Financial Inclusion – Priority Sector Lending norms and assurance of returns incentivize banks to lend to SHGs. The SHG-Bank linkage programme pioneered by NABARD has made access to credit easier and reduced the dependence on traditional money lenders and other non-institutional sources.

Improving efficiency of government schemes and reducing corruption through social audits.
Alternate source of employment – it eases dependency on agriculture by providing support in setting up micro-enterprises e.g. personalised business ventures like tailoring, grocery, and tool repair shops.

Changes In Consumption Pattern – It has enabled the participating households to spend more on education, food and health than non-client households.

Impact on Housing & Health – The financial inclusion attained through SHGs has led to reduced child mortality, improved maternal health and the ability of the poor to combat disease through better nutrition, housing and health – especially among women and children.

Banking literacy – It encourages and motivates its members to save and act as a conduit for formal banking services to reach them.

Capacity Building of the Self-Help Groups

SHGs that are in existence for about 6 months and have demonstrated the potential of a viable group enters the stage, wherein it receives the revolving fund of Rs 25000 from the bank as a cash credit facility and also embarks on further capacity building of its entire team. DRDAs will arrange to provide the revolving fund to such groups, meeting their share from out the SGSY fund. Of this, a sum of Rs10000 is given to the bank by the DRDA. Banks may charge interest only on the sum exceeding Rs 10000. The Subsidy of Rs 10000 released by DRDA is adjusted against the loan at the end of cash credit period on the request of the group.

Unit 15- Credit Cards, Home Loans, Personal Loans, Consumer Loans

Credit Card

A credit card, in physical terms, is a plastic card issued by a bank or a financial institution. The card issuer, either a bank or a financial institution, provides a credit card to eligible individuals with a maximum credit limit. Cardholders can make purchases using the card within the specified limit on credit. The used amount should be paid back at a later date, typically within 30 to 45 days, called grace period or interest-free period, from the date of purchase.

If the used credit on the card is cleared on-time, banks will not charge any interest. Whereas unpaid dues on card will attract finance charges till they are cleared in full.

Credit Card Operations of banks- RBI Guidelines
Pursuant to the announcement made in the Annual Policy Statement 2004-05, the Reserve Bank of India had constituted a Working Group on Regulatory Mechanism for Cards. The Group has suggested various regulatory measures aimed at encouraging growth of credit cards in a safe, secure and efficient manner as well as to ensure that the rules, regulations, standards and practices of the card issuing banks are in alignment with the best customer practices. The following guidelines on credit card operations of banks have been framed based on the recommendations of the Group as also the feedback received from the members of the public, card issuing banks and others. All the credit card issuing banks / NBFCs should implement these guidelines immediately.

Each bank / NBFC must have a well documented policy and a Fair Practices Code for credit card operations. In March 2005, the IBA released a Fair Practices Code for credit card operations which could be adopted by banks / NBFCs. The bank / NBFC’s Fair Practice Code should, at a minimum, incorporate the relevant guidelines contained in this circular. Banks / NBFCs should widely disseminate the contents thereof including through their websites, at the latest by November 30, 2005.

Guidelines for Implementation

**Issue of cards**

- Banks / NBFCs should independently assess the credit risk while issuing cards to persons, specially to students and others with no independent financial means. Add-on cards i.e. those that are subsidiary to the principal card, may be issued with the clear understanding that the liability will be that of the principal cardholder.
- As holding several credit cards enhances the total credit available to any consumer, banks / NBFCs should assess the credit limit for a credit card customer having regard to the limits enjoyed by the cardholder from other banks on the basis of self declaration/ credit information.
- The card issuing banks / NBFCs would be solely responsible for fulfillment of all KYC requirements, even where DSAs / DMAs or other agents solicit business on their behalf.
- While issuing cards, the terms and conditions for issue and usage of a credit card should be mentioned in clear and simple language (preferably in English, Hindi and the local language) comprehensible to a card user. The Most Important Terms and Conditions (MITCs) termed as standard set of conditions, as given in the Appendix, should be highlighted and advertised/ sent separately to the prospective customer / customers at all the stages i.e. during marketing, at the time of application, at the acceptance stage (welcome kit) and in important subsequent communications.

**Interest rates and other charges**

- Card issuers should ensure that there is no delay in dispatching bills and the customer has sufficient number of days (at least one fortnight) for making payment before the interest starts getting charged.
• Card issuers should quote annualized percentage rates (APR) on card products (separately for retail purchase and for cash advance, if different). The method of calculation of APR should be given with a couple of examples for better comprehension. The APR charged and the annual fee should be shown with equal prominence. The late payment charges, including the method of calculation of such charges and the number of days, should be prominently indicated. The manner in which the outstanding unpaid amount will be included for calculation of interest should also be specifically shown with prominence in all monthly statements. Even where the minimum amount indicated to keep the card valid has been paid, it should be indicated in bold letters that the interest will be charged on the amount due after the due date of payment. These aspects may be shown in the Welcome Kit in addition to being shown in the monthly statement.

• The bank / NBFC should not levy any charge that was not explicitly indicated to the credit card holder at the time of issue of the card and getting his / her consent. However, this would not be applicable to charges like service taxes, etc. which may subsequently be levied by the Government or any other statutory authority.

• The terms and conditions for payment of credit card dues, including the minimum payment due, should be stipulated so as to ensure that there is no negative amortization.

• Changes in charges (other than interest) may be made only with prospective effect giving notice of at least one month. If a credit card holder desires to surrender his credit card on account of any change in credit card charges to his disadvantage, he may be permitted to do so without the bank levying any extra charge for such closure.

Wrongful billing

• The card issuing bank / NBFC should ensure that wrong bills are not raised and issued to customers. In case, a customer protests any bill, the bank / NBFC should provide explanation and, if necessary, documentary evidence to the customer within a maximum period of sixty days with a spirit to amicably redress the grievances.

• To obviate frequent complaints of delayed billing, the credit card issuing bank / NBFC may consider providing bills and statements of accounts online, with suitable security built therefor.

Use of DSAs / DMAs and other agents

• When banks / NBFCs outsource the various credit card operations, they have to be extremely careful that the appointment of such service providers do not compromise with the quality of the customer service and the bank / NBFC’s ability to manage credit, liquidity and operational risks. In the choice of the service provider, the bank / NBFCs have to be guided by the need to ensure confidentiality of the customer’s records, respect customer privacy, and adhere to fair practices in debt collection.
• The Code of Conduct for Direct Sales Agents (DSAs) formulated by the Indian Banks’ Association (IBA) could be used by banks / NBFCs in formulating their own codes for the purpose. The bank / NBFC should ensure that the DSAs engaged by them for marketing their credit card products scrupulously adhere to the bank / NBFC’s own Code of Conduct for credit card operations which should be displayed on the bank / NBFC’s website and be available easily to any credit card holder.

• The bank / NBFC should have a system of random checks and mystery shopping to ensure that their agents have been properly briefed and trained in order to handle with care and caution their responsibilities, particularly in the aspects included in these guidelines like soliciting customers, hours for calling, privacy of customer information, conveying the correct terms and conditions of the product on offer, etc.

Credit Card Advantage and Disadvantage

Advantages

• **Purchasing Power**: Credit Cards enable users to make big ticket purchases they might not otherwise be able to afford.

• **Rewards**: Many cards offer rewards programs that will accrue points, discounts, or other benefits like frequent flyer miles.

• **Convenience**: Credit cards reduce the need to carry cash. Most retailers accept credit cards and they are pretty much required for online purchases.

• **Trackability**: The electronic record keeping that comes with credit cards make it easy to track your spending and identify fraud.

• **Use during an emergency**: There are times when money is the simple solution to an emergency. If you get hit with an unexpected expense, credit cards can be the quick and easy solution you need.

• **Builds credit history**: Responsible use of a credit card over time builds your credit history, qualifying you for

Disadvantages

• **Overspending**: Credit cards can make life easier, but they can also make overspending easier as well. With a credit card, you’re spending money you don’t necessarily have yet. If you’re not careful, this can quickly lead to unexpected debt.

• **Interest and fees**: Using credit is essentially borrowing. And you’re not borrowing for free. Mismanaging a credit card can lead not only to a high balance, or maxed-out card, but also to debt in the form of interest and fees.

• **Fraud**: Credit cards (and other electronic forms of payment) carry unique dangers. Credit cards can be stolen, their numbers can be copied, and they can be used to steal your money and identity.

• **Mounting Debt**: If you carry a balance on your credit card from month to month, it can be very easy for charges and interest to rack up. Many people don’t expect credit cards to be gateways to
better interest rates and other financial benefits. Extra debt, but if you’re not careful, that’s exactly what happens.

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**Home Loans**

Generally take a home loan for either buying a **house/flat or a plot of land for construction of a house, or renovation, extension** and repairs to your existing house.

**How much loan am I eligible for?**

Before you start the home loan process, determine your total eligibility, which will mainly depend on your repaying capacity. Your repayment capacity is based on your **monthly disposable/surplus income**, which, in turn, is based on factors such as total monthly income/surplus less monthly expenses, and other factors like spouse’s income, assets, liabilities, stability of income, etc.

**Procedure and Practices for Home Loans**

**What Is The Procedure For Home Loan?**

The steps to complete the home loan process are as follows:

1. **Step 1**: Fill The Loan Application Form & Attach The Documents
2. **Step 2**: Pay The Processing Fee
3. **Step 3**: Discussion With The Bank
4. **Step 4**: Valuation Of The Documents
5. **Step 5**: The Sanction/Approval Process
6. **Step 6**: Processing The Offer Letter
7. **Step 7**: Processing The Property Papers Followed By A Legal Check
8. **Step 8**: Processing A Technical Check & The Site Estimation
9. **Step 9**: The Final Loan Deal, Signing The Agreement, & Disbursal

**Fill The Loan Application Form & Attach The Documents**

Once the formal application is filled, the next step is to attach all the valid documents required by the bank with it. Usually, this includes the:

- Applicant’s income proof
- Applicant’s identity (or ID) proof
• Applicant’s age proof
• Applicant’s address proof
• Applicant’s employment details
• Applicant’s educational proof (school/diploma/degree certificates)
• Applicant’s bank statements
• Property details on which the loan is applied (if finalized)

Note: Most banks offer doorstep service. Hence, an applicant doesn’t have to spend his or her time waiting at the bank and having the documents submitted. However, a few banks might still want the applicant to visit their respective workplace at least once.

There are three important reasons banks ask for all the above proofs from an applicant:

One: to authenticate the applicant.

Two: to obtain valid clues on the applicant’s financial health.

Three: to check if the applicant is eligible and has sufficient income to pay back the loan.

Explanation Of Each Document

1. Income Proof: This is the applicant’s actual proof of income. This usually encloses a copy of the each:

   ITR (Income Tax Returns) for the last 3 years
   Annual accounts/Computation of Income (if any)
   Salary slips for the last six months
   Form 16 or Form 16A for the last three months
   Bank statements for the last 6 months
   Other bank accounts (active) if it reflects the current income

Note: You may also be asked to submit a few other employment details but this differs from one bank to the other. Overall, the documents mentioned above are mandatory.

Loan to Value (LTV) Ratio

As per the guidelines issued by RBI June 21, 2013 the norms have been revised and the following LTV ratios have to be maintained by banks in respect of Individual housing loans.

<table>
<thead>
<tr>
<th>Category of Loan</th>
<th>LTV Ratio (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>
(a) Individual Housing loan

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Up to Rs 20 lakhs</td>
<td>90</td>
</tr>
<tr>
<td>Above Rs 20 lakhs and Up to Rs 75 lakhs</td>
<td>80</td>
</tr>
<tr>
<td>Above 75 lakhs</td>
<td>75</td>
</tr>
</tbody>
</table>

(b) CRE - RH

**Personal Loans**

A personal loan is an unsecured advance offered by both banks and non-banking financial corporations to any eligible individual. It is very important to be aware of your personal loan eligibility details as this will simplify and quicken your application process. Each bank has separate minimum criteria for income, age, employment type, credit score, job status, etc. You will need to meet these criteria in order to apply for a personal loan from a particular lender. Personal loan eligibility criteria varies across lenders based on the borrower's profile and relationship with the bank.

*The general requirements and limits are outlined below:*

- **Minimum Age:** limit 21 – 28 years
- **Maximum Age:** limit 58 – 68 years
- **Type of Employment:** Salaried, Business owner, Self-employed professional, Retired, Student & Home maker
- **Employment Status:** Employed/In-business for at least 2 – 5 years
- **Minimum Net Monthly Income:** Rs. 5,000 and above
- **Work Experience:** 1 to 3 years & Above
- **Credit Score:** CIBIL score of 750 or more
- **Maximum EMI:** Up to 65% of Income

**Documentation Required**

- Duly-filled and signed application form
- 2 passport-size photographs
- Cheque – Processing fee

Proof of:
• **Identity** – Voter ID/ Passport Copy/ Driving License / PAN Card (any one)

• **Address** – Passport Copy/ Utility Bill (Electricity, Water)/ Rental Agreement/ Ration Card (any one)

• **Income (depending on type of employment)** – Latest Salary Slips (3 months) / Bank Statements (3 – 6 months) / Passbook (3 – 6 months)/ Current Salary Certificate (any one)

• **Tax paid** – Latest Form 16/ Income Tax Return

• **KYC Documents** – Address proof, proof of date of birth, identity proof

### Consumer Loans

**Purpose**

A Consumer Loan is a loan that banks offer to customers to **buy household goods and appliances** and even personal devices.

These include **television sets, air-conditioners, home theatre systems, refrigerators, laptops, mobile phones, cameras and even modular kitchens.**

**Documents required for Consumer Loans?**

You need minimal documentation when you apply for Consumer Loans. These include:

- Income proof
- Identity and signature proof
- Address proof
- Recent photographs
- Self-employed individuals and professionals may need to submit different documents. Please confirm with your bank when you apply.

**Margin:**

Normally a margin of 10-20% is stipulated.

**Repayment:**

Banks allow period of 3 to 5 years for repayment of consumer loan. Normally repayment is allowed in EMI.
Unit 16- Documentation

Documentation is one of the vital areas in the credit Portfolio of a Bank. The purpose of taking documents are to fix the terms and conditions between the bankers and the borrowers, to identify the borrowers, to identify the securities, to count the period of limitation, to resort to legal remedies in case of need and so on.

Need for Documents

- The Documents are necessary to be procured for the following reasons:
- To identify the borrower
- To identify the security
- To have a written evidence of the transactions of lending made by the bank
- To ensure due repayment of the legal step for recovery of the loan, in the event of non-payment by the borrower or guarantor.

Different types of Documents

- Demand Promissory Notes (DPN)
- Agreements
- Forms

Demand Promissory Notes (DPN): Where no specification for a fixed period for the repayment of loan is given, the bankers take the DPN. In DPN, the borrower makes a promise to the banker to repay the loan amount on demand with agreed rate of interest. The form of DPN should be in conformity with section 4 of the Negotiable Instruments Act, 1881. The form of a DPN varies normally to suit the situation such as fixed rate of interest, floating rate of interest, single borrower, joint borrowers etc.

As per section 35 of the Indian stamp act, if a DPN is unstamped or under stamped, the defect cannot be rectified even by paying a penalty.

Agreement: The form of an agreement should be in conformity with the Indian Contract Act. The terms and conditions are set out in the agreement. The amount of loan, rate of interest, rate of penal interest, percentage of margin, period of repayment, right of the bankers, in case of default of loan, details of security charged are included agreement. The agreement attract a stamp duty as per Indian Stamp Act.

Forms: Forms are not in the nature of promise or agreement. These are obtained to specify clearly the intention of the borrower.

Documentation Procedure
Selection of Correct Set of Documents:

**Stamping:** Section 12 of Indian Stamp Act provides for cancellation of adhesive stamp so that the same cannot be used again.

**Amount of Duty:** In a case Promissory Note, Bill of Exchange, share Transfer, Receipt, letter of credit, Policy of Insurance, are under stamped in terms of the amendment of sec 35 of Indian Stamp Act.

- Filling
- Execution
- Legal Formalities
- Keeping Documents Valid (in force)

**Revival of time barred debts**

Any contract that is executed by an executant without for any consideration is void in the eyes of law. As per section 25 (3) of the Contract Act, a fresh promise made for repaying the time barred debt is a valid consideration and the same is enforceable in a court of law. Therefore, it is possible to revive a time barred debt by obtaining a fresh express promissory note from the borrower(s) and Guarantor(s) promising to repay the time-barred dues.

The essential ingredient of section 25(3) of Indian Contract Act is that the creditor claims the amount of debt subject to the conditions.

- The promise must be written and signed by the promisor or his agent generally or specially authorized in that behalf.
- The promise may be to pay the whole or part of the debt and the debt must be which the creditor would have enforced for payment but for the law of limitation.

The difference between section 18 of limitation act and section 25(3) of contract act is that under the former act, an acknowledgement obtained from the party before the expiry of the period of limitation would extends the validity period of the document for further period of 3 years, whereas a promise made under section 25(3) to pay debt after the expiry of limitation period, should be an express and not implied promise. Normal practice by the bankers is to obtain a fresh DPN (or set of documents) along with a letter signed by the promisor or his/her authorized agent to pay the time barred dues.

**Stamping of Documents**
The Indian Stamp Act 1899, contains provisions regarding instruments chargeable with duty, mode of using stamps, time of stamping instruments etc.

**Section 17:** All instruments chargeable with duty and executed by any person in India shall be stamped before or at the time of execution.

**Section 18:** Every instrument, other than a bill of exchange and promissory note, which are chargeable with duty and executed out of India may be stamped within three months after it has been first received in India.

**Section 19:** First holder in India, of any bill of exchange payable otherwise than on demand on promissory note drawn or made out of India shall affix there to the proper stamp and cancel the same before he presents the same for acceptance or payment or endorses or otherwise negotiates the same in India.

**Section 35:** The act provide that any person shall not admit an instrument, not duty stamped in evidence for any purpose.

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**Unit 17-Different Modes of Charging Securities**

Bank tend to safeguard their advances by taking different kinds of securities. The main purpose of taking a security is to fall back on it in case the loan is defaulted. Bank take movable properties immovable properties or a debt as securities for a loan. The method of creating charge over a property depends upon the nature of property and nature of charge.

**Types of charges**

Bank charge over property confines itself to one or more of the following six types of charges.

- Assignment
- Lien
- Set-off
- Hypothecation
- Pledge
- Mortgage
- Appropriation

**Assignment**

It is a mode of providing securities to a banker for an advance. It is transfer of a right, property or a debt. The transfer is called assignor and the transferee assignee.
Borrowers generally assign the actionable claims to the banker as security for an advance. It is transfer of right, Property or debt. The transferor is called assignor and the transferee assignee. Borrowers generally assign the actionable claims to the banker as securities for an advance.

**Section 130 of the transfer of property Act**: The transfer of an actionable claim can be effected only by the execution of an instrument in writing, signed by duly authorized agent.

**Section 3 of the Transfer of property act**: Defines an actionable claim to any debt other than a debt secured by mortgage of immovable property, or by hypothecation of or pledge of movable property or two beneficial interest in movable property, not in the possession of the claimant, which the civil courts recognize as affording grounds of relief.

All the rights and remedies of the transferor vest in the transferee. The transferee of an actionable claim takes it, subject to all the liabilities and equities to which the transferor was subject on the date of transfer.

**Lien**

Lien is the right of the banker to retain possession of the goods and securities owned by the debtor until the debt due from the latter is paid. The banker’s lien is an implied pledge. A banker acquires the right to sell the goods which came into its possession in the ordinary course of banking business, in case the debt is not paid.

**Section 171 of the Indian contract act 1872** gives to the banker an absolute right of general lien on all goods and securities received by the banker.

**Set-off**

Set off means total or partial merging of a claim of one person against another in a counter claim by the latter against the former. It is in effect, the combining of accounts of the debtor and creditor, to arrive at the former. It is in effect, the combining of accounts of the debtors and creditors, to arrive at the met balance payable to one or the other. The right of set off is a statutory right and can also arise out of an agreement between parties.

**Salient features of Set off**

- Both debts must be for certain sums. A debt accruing due to cannot be set off against the debt already due.
- The banker cannot set off the credit balance in the account of guarantor till the liability of the guarantor is determined.
- The credit balance in the current account cannot be set off against a contingent liability of a bill discounted but not yet due.
• A banker cannot set off a debt due to him upon a loan account repayable on demand or at a specified date against a credit balance in the current account until the demand is made or due date arrives.
• The parties must be mutually indebted in the same right.
• The credit balance in the partner’s account can be set off against the debit balance of a partnership account since the liability of the partner is joint and several.
• Right of set-off is exercisable between two firms, which have separate names but are composed of same set off is exercisable between two firms, which have separate names but are composed of same set of partners.
• The credit balance in the personal account of a sole proprietor can be set off against the debit balance of the sole proprietary concern and vice versa.
• When the right set off is available to the bank, lien right cannot apply. These two different rights cannot be exercised simultaneously at the same time.

**Automatic right of set off arises in the following circumstances**

• On the death, insanity or insolvency of the customers.
• On the insolvency of a partner of a firm or winding up of a company
• On receipt of a garnishee order.
• On receipt of notice of assignment of a customer’s credit balance.

**Hypothecation**

The term hypothecation means a charge in or upon any movable property, existing or future, created by a borrower in favour of a secured creditor, without delivery of possession of the movable property to such creditor, as a security for financial assistance and includes floating charge and crystallization of such charge in to fixed charge on movable property. The mortgage of movable property is called hypothecation.

**Pledge**

Pledge means **bailment of goods for purpose** of providing security for payment of debt or performance of promise. *(As per the section 172 of Indian Contract Act 1872).*

The person, whose goods are bailed is **called the Pawnor**, the person who takes the goods as security is **called the Pawnee**.

**The followings are the legal implications of a pledge:**

• The ownership of the property is retained by the pawnor, which is subject only to the qualified interest which passes to the pawnee by the bailment.
One of the main and most essential requirements of a pledge is the actual or constructive delivery of the goods to the pawnee. By constructive delivery, it is meant that there need be no physical transfer of goods from the custody of the pawnee or of the any person authorized to hold them on his behalf.

**Goods may be delivered by one of the following ways**

- By handing over the key of the godown, in which the goods are kept.
- By attornment i.e. if goods are in public warehouse, the warehouseman acknowledges to the pawnee that he will hold the goods thereafter on behalf of the pawnee.
- Handling over the document of title to goods such as railway receipt, bill of lading, warehouse receipts etc.
- Even if goods are in possession of the pawnor, he may acknowledge that he holds them thereafter for and on behalf of the pawnee.
- An agreement of pledge may be implied from the nature of the transaction or the circumstances of the case. However, an agreement in writing clearly laying down the terms and conditions leaves no ambiguity.

**Mortgage**

Mortgage is a transfer of interest in immovable property to secure an advance loan or an existing debt or a debt or performance of an obligation.

**Transfer of property act contemplates six types of mortgage**

- Simple mortgage
- Mortgage by conditional sale
- Usufructuary mortgage
- English mortgage
- Mortgage by deposit of title deeds
- Anomalous mortgage

**In simple mortgage:** the mortgage is by deposit of title des and in English mortgage, the possession of the mortgage properties is not given to the mortgage

**In usufructuary mortgage** and in mortgage by conditional sale, possession of the mortgaged properties is normally given to the mortgage
In the case of simple mortgage and mortgage by deposit of title deeds, the mortgagee has a right to proceed against the property mortgaged and also personally against the mortgagor.

Mortgage is to be created by way of deed and requires to be registered under the registration act.

Mortgage by deposit of title deeds is not required to be created by way of a deed and does not require registration.

The rule of priority in case of successive mortgages is in the order of the time they are created.

Limitation period for filing a suit for foreclosure is thirty years that date mortgage debt becomes due.

Limitation period for filing a suit for sale of mortgages property is twelve years from the date mortgage debt become due.

Enforcement of mortgage is government by the code of civil procedure 1908. Suit for sale of mortgages properties should be filed in the court within whose jurisdiction the mortgage property is situated.

In a suit for sale of mortgaged properties, the court first passes a preliminary decree and thereafter final decree.

Right of Appropriation

When a debtor has several debt with a creditor, section 59, 60 and 61 of the Indian Contract Act 1872, deal with appropriation of payment made by the debtor to the creditor. The principle also applies to the loans obtained from a bank. We should also understand clearly the different between right of appropriation and right of off. When a Fixed deposit receipt of appropriated before maturity it is under the right of appropriation and when it is appropriated after maturity the right of set off is exercised.

Unit 18- Types of Collaterals and Their Characteristics

Banks are financial intermediaries where the resources of the public are mobilized and lent to various sectors of the economy. The money mobilized from the public by way of deposit is repayable as and when demanded by the depositors. Therefore, bankers take utmost care to see that the money lent to various types of borrowers is repaid as per the
repayment schedule along with interest. In order to safeguard the advance, bankers normally take securities, on which they fall back in case the borrowers commit default.

There are different types of Collaterals and their Characteristics.

**Land and Buildings**

This type of security is not self-liquidating nature. In the event of the bank wanting to sell the property for recovering its advance, it can do so through the legal process. Normally, banks have to file a suit before the civil court for recovery, if the amount due in the loan account is less than Rs 10 lakhs and before the Debt Recovery Tribunal (DRT), if the amount due is Rs. 10 lakhs and above.

**Characteristics of Land and Building**

- Examining the Title to the Property
- Document to be called for from the Mortgagor
- Valuation of Property
- Leasehold Properties

**GOODS**

Banks advance loans routinely against the security of goods such as agricultural goods, raw material, semi-finished goods. An advance goods may be extended by way of keeping goods as pledge Hypothecation. i.e, key cash credit or open cash credit. The nature of the change created may be either a pledge or hypothecation. When the possession of the goods is transferred to the banker, as in the cash of key cash credit, the nature of charge created is pledge.

**Characteristics of Goods**

- Precautions of advance against Goods
  (a) The borrowers should be dealing in the goods for a sufficient period
  (b) No advance should be made for speculation or hoarding purpose
  (c) The goods charged to the bank should have been fully paid
  (d) The goods should command good demand in the market
  (e) The age of the stock should be taken into consideration
    - Storing of Goods
    - Inspection of stocks
Documents of Title to Goods

Section 2(4) of Sale of goods Act defines a document of title to goods as “a document used in the ordinary course of business as a proof of possession or control of goods authorising or purporting to authorize either by endorsement or delivery, the possessor of the documents to transfer or to receive the goods there by represented.

Characteristics of Document of title to goods

• The Essential Requisites of a Document of Title to Goods

• Merits of this Security: By mere pledge of the instruments, goods are pledged and serve as a good security. The person in possession of the document can transfer the goods by endorsement and delivery. The Transferee thereafter is entitled to take delivery of goods in his own rights. The Document are easily transferable and the formalities involved are minimum.

• Demerits of this Security: Possibly for fraud and Dishonesty, Forged and Altered Documents

• Precautions to be taken by the Banker

Advances Against Life Insurance Policies

Life insurance policies are acceptable either as a primary or collateral Security for an advance.

Points to be taken into Consideration

Before making an advance, the point to be taken into consideration are:

• The Policy must be in force and the premium paid up to date. The latest premium receipt must be kept on record by the bank.

• The policy should be an original, duly stamped and signed by the issuing authority.

• The policy should be free from restrictive/onerous clauses.

• The insurance company should have admitted to the age of the assured.

Generally, The following life policies are not acceptable as security
• Children endowment policy.
• Policies taken out specifically for purposes like estate duty,
• Children Deferred policy
• Policies with nominations under Section 6 of the Married Women's Property Act.

**Advance Against Share**

**General guidelines applicable to advances against shares/debentures/bonds**

• Statutory provisions regarding the grant of advances against shares contained in sections 19(2) and (3) and 20(1)(a) of the Banking Regulation Act', 1949 should be strictly observed. Shares held in dematerialised form should also be included for the purpose of determining the limits under sections 19(2) and 19(3), ibid.

• Banks should be concerned with what the advances are for, rather than what the advances are against. While considering grant of advances against shares/debentures banks must follow the normal procedures for the sanction appraisal and post-sanction follow-up.

• Advances against the primary security of shares/debentures/bonds should be kept distinct and separate and not combined with any other advance.

• Banks should satisfy themselves about the marketability of the shares/debentures and the net worth and working of the company whose shares/debentures/bonds are offered as security.

• Shares/debentures/bonds should be valued at prevailing market prices when they are lodged as security for advances.

• Banks should exercise particular care when advances are sought against large blocks of shares by a borrower or a group of borrowers. It should be ensured that advances against shares are not used to enable the borrower to acquire or retain a controlling interest in the company/companies or to facilitate or retain inter-corporate investments.

• No advance against partly paid shares shall be granted. Whenever the limit/limits of advances granted to a **borrower exceeds Rs. 10 lakhs**, it should be ensured that the said shares/debentures/bonds are transferred in the bank's name and that the bank has exclusive and unconditional voting rights in respect of such shares. For this purpose the aggregate of limits against shares/debentures/bonds granted by a bank at all its offices to a single borrower should be taken into account. Where securities are held in dematerialised form, the requirement relating to transfer of shares in bank's name will not apply and banks may take
their own decision in this regard. Banks should however avail of the facility provided in the depository system for pledging securities held in dematerialised form under which the securities pledged by the borrower get blocked in favour of the lending bank. In case of default by the borrower and on the bank exercising the option of invocation of pledge, the shares and debentures get transferred in the bank’s name immediately.

• Banks may take their own decision in regard to exercise of voting rights and may prescribe procedures for this purpose.

• Banks should ensure that the scripts lodged with them as security are not stolen/duplicate/fake/benami. Any irregularities coming to their notice should be immediately reported to RBI.

• The Boards of Directors may decide the appropriate level of authority for sanction of advances against shares/debentures. They may also frame internal guidelines and safeguards for grant of such advances,

• Banks operating in India should not be a party to transactions such as making advances or issuing back-up guarantees favouring other banks for extending credit to clients of Indian nationality/origin by some of their overseas branches, to enable the borrowers to make investments in shares and debentures/bonds of Indian companies.

**Loan Against Term Deposits**

**Eligibility Criteria for Availing Loan Against Fixed Deposit**

To be eligible for a loan against FD, the basic criteria is that you must hold a fixed deposit with the bank you are availing the loan from and any of below-given individuals/entities can avail the loan:

• Resident Indian citizens
• Family Trusts
• Hindu Undivided Family (HUF)
• Clubs, societies, and associations
• Sole proprietorships, group companies, and partnership firms

**Documentation Required to Avail Loan Against Fixed Deposit**

To avail a loan against fixed deposit, you will need to provide the below-given documents:

• Application form duly signed
Duly signed agreement

Fixed/Term Deposit receipts duly discharged in favor of the bank

Please note that these may vary from lender to lender.

**How to Obtain Loan Against Fixed Deposit**

Most lenders allow you to avail a loan against fixed deposit online except in few cases where you will need to visit the nearest branch of the bank. Some of the banks that offer the facility of availing a loan against fixed deposit online through their respective websites are the State Bank of India, HDFC Bank, Axis Bank, and Deutsche Bank. In the case of Federal Bank, you will need to visit the nearest branch of the bank.

**Features and Benefits of Loan Against Fixed Deposit**

*Lower interest rates* – Since your fixed deposit acts as a security for a loan, the interest rate charged on these loans are lower. The interest rates on these loans are usually lower than the interest rates on personal loans by about 2% to 2.5%. Hence, the equated monthly instalments (EMIs) on these loans are also lower.

*Minimal paperwork* – Since banks already have your details which you furnished during the opening of your FD, the documentation required for availing the loan against your FD will be minimal. You will not be required to submit documents such as your proof of income, Income Tax Returns (ITR), etc.

*No credit score check* – When you apply for any kind of loan, lenders will have a look at your credit score before they offer you a loan. However, in the case of a loan against FD, your CIBIL or credit score will not be considered while evaluating your eligibility. Hence, such loans can be a good option for people who have low or no credit score.

*The loan amount will depend on the FD amount* – If you have to avail a personal loan, the maximum loan amount that you can avail will depend on various factors such as your credit score, income, tenure, etc. However, in the case of loan against FD, the maximum loan amount will depend on the money you have invested in the FD account. This means that if you have invested a higher amount in your FD, you will be eligible for a higher loan amount.

*No prepayment penalty* – When you prepay any loan, the banks lose out on the interest and hence, they will charge you a penalty for the same. However, in the case of a loan against FD, no penalty is charged as banks do not lose out on the interest amount. Instead, they profit from it as they do not have to pay you any interest on the loan amount.

**Loan against gold ornaments**
A gold loan is a method of availing finance/loan against your gold ornaments or jewellery such as bangles, necklaces, bracelets, earrings, pendants, watches, gold coins, etc.

**Who can avail a gold loan?**

Any Indian citizen can avail a gold loan from banks or non-banking financial institutions (NBFCs) and generally the age criteria ranges from a minimum of 18 years to a maximum of 75 years. This might vary from lender to lender.

**Features of Gold Loans**

**Purpose:** You can avail a gold loan from any available lender in order to finance various needs, such as for educational purposes, medical emergencies, going on a holiday, and so on.

**Security:** The gold that has been pledged with the bank or the financial institution acts as the security or collateral against which the loan amount is provided.

**Tenure options:** The tenure options can range from a minimum of 3 months to a maximum of 36 months.

**Fees:** The other fees and charges that might be applicable on a gold loan are – processing fee, late payment charges/penalty for non-payment of interest, valuation fees, etc.

**Repayment Options:** There are three main options offered by lenders to borrowers for the repayment of a gold loan. These are:

i) Repayment in Equated Monthly Installments (EMI)

ii) Payment of interest upfront and repayment of the principal loan amount at the end of the loan tenure.

iii) Payment of interest on a monthly basis and repayment of the principal loan amount at the end of the loan tenure.

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**Unit 19-Non-Performing Assets**

In line with the international practices and as per the recommendations made by the Committee on the Financial System (Chairman Shri M. Narasimham), the Reserve Bank of India has introduced, in a phased manner, prudential norms for income recognition, asset classification and provisioning for the advances portfolio of the banks so as to move towards greater consistency and transparency in the published accounts.

The policy of income recognition should be objective and based on record of recovery rather than on any subjective considerations. Likewise, the classification of assets of banks
has to be done on the basis of objective criteria which would ensure a uniform and consistent application of the norms. Also, the provisioning should be made on the basis of the classification of assets based on the period for which the asset has remained non-performing and the availability of security and the realisable value thereof.

**Definition**

An asset, including a leased asset, becomes non-performing when it ceases to generate income for the bank. Non-performing Asset (NPA) shall be an advance where

Interest and/or instalment of principal remain overdue for a **period of more than 90 days in respect of a term loan,**

The account remains ‘out of order’ for a period of **more than 90 days,** in respect of an Overdraft/Cash Credit (OD/CC),

The bill remains overdue for a period of **more than 90 days in the case of bills purchased and discounted,**

Interest and/or instalment of principal remains overdue for two harvest seasons but for a period not exceeding two half years in the case of an advance granted for agricultural purposes, and

Any amount to be received remains overdue for a period of more than 90 days in respect of other accounts.

**Out of Order’ status**

An account should be treated as 'out of order' if the outstanding balance remains continuously in excess of the sanctioned limit/drawing power. In cases where the outstanding balance in the principal operating account is less than the sanctioned limit/drawing power, but there are no credits continuously for six months as on the date of Balance Sheet or credits are not enough to cover the interest debited during the same period, these accounts should be treated as 'out of order'.

**‘Overdue’**

Any amount due to the bank under any credit facility is ‘overdue’ if it is not paid on the due date fixed by the bank.

**Income Recognition**

**Income recognition - Policy**

The policy of income recognition has to be objective and based on the record of recovery. Internationally income from non-performing assets (NPA) is not recognised on accrual
basis but is booked as income only when it is actually received. Therefore, the banks should not charge and take to income account interest on any NPA.

However, interest on advances against term deposits, NSCs, IVPs, KVPs and Life policies may be taken to income account on the due date, provided adequate margin is available in the accounts.

Fees and commissions earned by the banks as a result of re-negotiations or rescheduling of outstanding debts should be recognised on an accrual basis over the period of time covered by the re-negotiated or rescheduled extension of credit.

If Government guaranteed advances become NPA, the interest on such advances should not be taken to income account unless the interest has been realised.

**Reversal of income**

If any advance, including bills purchased and discounted, becomes NPA as at the close of any year, interest accrued and credited to income account in the corresponding previous year, should be reversed or provided for if the same is not realised. This will apply to Government guaranteed accounts also.

In respect of NPAs, fees, commission and similar income that have accrued should cease to accrue in the current period and should be reversed or provided for with respect to past periods, if uncollected.

**Reporting of NPAs**

Banks are required to furnish a Report on NPAs as on 31st March each year after completion of audit. The NPAs would relate to the banks’ global portfolio, including the advances at the foreign branches. The Report should be furnished as per the prescribed format given in the Annexure.

While reporting NPA figures to RBI, the amount held in interest suspense account, should be shown as a deduction from gross NPAs as well as gross advances while arriving at the net NPAs. Banks which do not maintain Interest Suspense account for parking interest due on non-performing advance accounts, may furnish the amount of interest receivable on NPAs as a foot note to the Report.

Whenever NPAs are reported to RBI, the amount of technical write off, if any, should be reduced from the outstanding gross advances and gross NPAs to eliminate any distortion in the quantum of NPAs being reported.

**ASSET CLASSIFICATION**

**Categories of NPAs**
Banks are required to classify non-performing assets further into the following three categories based on the period for which the asset has remained non-performing and the realisability of the dues:

- Sub-standard Assets
- Doubtful Assets
- Loss Assets

**Sub-standard Assets**

*With effect from 31 March 2005,* a sub-standard asset is one, which has remained NPA for a period less than or equal to 12 months. In such cases, the current net worth of the borrower/guarantor or the current market value of the security charged is not enough to ensure recovery of the dues to the banks in full. In other words, such an asset will have well defined credit weaknesses that jeopardise the liquidation of the debt and are characterised by the distinct possibility that the banks will sustain some loss, if deficiencies are not corrected.

**Doubtful Assets**

*With effect from 31 March 2005,* an asset is to be classified as doubtful, if it has remained NPA for a period exceeding 12 months. A loan classified as doubtful has all the weaknesses inherent in assets that were classified as sub-standard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently known facts, conditions and values – highly questionable and improbable.

**Loss Assets**

A loss asset is one where loss has been identified by the bank or internal or external auditors or the RBI inspection but the amount has not been written off wholly. In other words, such an asset is considered uncollectible and of such little value that its continuance as a bankable asset is not warranted although there may be some salvage or recovery value.

**Guidelines for classification of assets**

**Accounts with temporary deficiencies**

The classification of an asset as NPA should be based on the record of recovery. Bank should not classify an advance account as NPA merely due to the existence of some deficiencies which are temporary in nature such as non-availability of adequate drawing power based on the latest available stock statement, balance outstanding exceeding the limit temporarily, non-submission of stock statements and non-renewal of the limits on the due date, etc. In the matter of classification of accounts with such deficiencies banks may follow the following guidelines:
Banks should ensure that drawings in the working capital accounts are covered by the adequacy of current assets, since current assets are first appropriated in times of distress. Drawing power is required to be arrived at based on the stock statement which is current. However, considering the difficulties of large borrowers, stock statements relied upon by the banks for determining drawing power should not be older than three months. The outstanding in the account based on drawing power calculated from stock statements older than three months, would be deemed as irregular. A working capital borrowal account will become **NPA if such irregular drawings are permitted in the account for a continuous period of 180 days even though** the unit may be working or the borrower's financial position is satisfactory.

Regular and ad hoc credit limits need to be reviewed/ regularised not later than three months from the due date/date of ad hoc sanction. In case of constraints such as non-availability of financial statements and other data from the borrowers, the branch should furnish evidence to show that renewal/ review of credit limits is already on and would be completed soon. In any case, delay beyond six months is not considered desirable as a general discipline. Hence, an account where the regular/ ad hoc credit limits have not been reviewed/ renewed within 180 days from the due date/ date of ad hoc sanction will be treated as NPA.

**Asset Classification to be borrower-wise and not facility-wise**

It is difficult to envisage a situation when only one facility to a borrower becomes a problem credit and not others. Therefore, all the facilities granted by a bank to a borrower will have to be treated as NPA and not the particular facility or part thereof which has become irregular.

If the debits arising out of devolvement of letters of credit or invoked guarantees are parked in a separate account, the balance outstanding in that account also should be treated as a part of the borrower’s principal operating account for the purpose of application of prudential norms on income recognition, asset classification and provisioning.

**Advances against Term Deposits, NSC’s, KVP/IVP, etc**

Advances against term deposits, NSCs eligible for surrender, IVPs, KVPs and life policies need not be treated as NPAs. Advances against gold ornaments, government securities and all other securities are not covered by this exemption.

**Loans with moratorium for payment of interest**

In the case of bank finance given for industrial projects or for agricultural plantations etc. where moratorium is available for payment of interest, payment of interest becomes 'due' only after the moratorium or gestation period is over. Therefore, such amounts of interest
do not become overdue and hence NPA, with reference to the date of debit of interest. They become overdue after due date for payment of interest, if uncollected.

In the case of housing loan or similar advances granted to staff members where interest is payable after recovery of principal, interest need not be considered as overdue from the first quarter onwards. Such loans/advances should be classified as NPA only when there is a default in repayment of instalment of principal or payment of interest on the respective due dates

**Provisioning Norms**

**Loss assets**

The entire asset should be written off. If the assets are permitted to remain in the books for any reason, **100 percent** of the outstanding should be provided for.

**Doubtful assets**

**100 percent of the extent to** which the advance is not covered by the realisable value of the security to which the bank has a valid recourse and the realisable value is estimated on a realistic basis.

In regard to the secured portion, provision may be made on the following basis, at the rates ranging from **25 percent to 100 percent** of the secured portion depending upon the period for which the asset has remained doubtful:

**Period for which the advance has been considered as doubtful - Provision requirement (%)**

- Up to one year - 25
- One to three years - 40
- More than three years - 100

**Sub-standard assets**

A **general provision of 10 percent** on total outstanding should be made without making any allowance for DICGC/ECGC guarantee cover and securities available.

**Standard assets**

From the year ending 31.03.2000, the banks should make a general provision of a **minimum of 0.25 percent** on standard assets on global loan portfolio basis.

The provisions on standard assets should not be reckoned for arriving at net NPAs.
The provisions towards Standard Assets need not be netted from gross advances but shown separately as 'Contingent Provisions against Standard Assets’ under 'Other Liabilities and Provisions - Others' in Schedule 5 of the balance sheet.

**Advances covered by ECGC/DICGC guarantee**

In the case of advances guaranteed by DICGC/ECGC, provision should be made only for the balance in excess of the amount guaranteed by these Corporations. Further, while arriving at the provision required to be made for doubtful assets, realisable value of the securities should first be deducted from the outstanding balance in respect of the amount guaranteed by these Corporations and then provision made as illustrated hereunder:

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Unit 1- Essentials of Bank Computerisation

Bank Computerisation

The Concept of Bank Computerisation Practically stated after 1980-81 and more precisely gained pace in the year 1983-84, after setting up a committee in the year 1983 under the chairmanship of the then Deputy Governor of RBI, Dr. C. Rangarajan. This Committee was set up to study the possibilities and stages involved in bank computerisation and to prepare guidelines for the same. The report submitted by the committee in the year 1984 was know as First Rangarajan Committee Report on bank mechanization.

Another Committee was constituted in 1988 was know as first Rangarajan Committee Report on bank mechanization.

Need for Computerisation

The four Major objectives of computerization in banking are to improve

- Customer Service
- Housekeeping
- Decision-making
- Productivity and profitability


Stand-Alone Computer System

Using the stand-Alone computer system is normally the initial stage of computerization at a bank. The single user-computer system is a small system, which as its name implies, is used by only one person at a time.

Multi-user System

The Multi-user systems, as their names signify, are computers to which several people can access at the same time. Mini computers, Main Frame Computers, Micro-Computers and the more powerful Super Computers all fall under this category.

Network

LAN (Local Area Network)

A Local Area Network (LAN) is a group of computer and peripheral devices which are connected in a limited area such as school, laboratory, home, and office building. It is a widely useful network for sharing resources like files, printers, games, and other application. The simplest type of LAN network is to connect computers and a printer in someone's home or office. In general, LAN will be used as one type of transmission medium.

It is a network which consists of less than 5000 interconnected devices across several buildings.

Characteristics of LAN

Here are important characteristics of a LAN network:

- It is a private network, so an outside regulatory body never controls it.
- LAN operates at a relatively higher speed compared to other WAN systems.
- There are various kinds of media access control methods like token ring and ethernet.

Advantages of LAN

Here are pros/benefits of using LAN:

- Computer resources like hard-disks, DVD-ROM, and printers can share local area networks. This significantly reduces the cost of hardware purchases.
- You can use the same software over the network instead of purchasing the licensed software for each client in the network.
- Data of all network users can be stored on a single hard disk of the server computer.
- You can easily transfer data and messages over networked computers.
- It will be easy to manage data at only one place, which makes data more secure.
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- Local Area Network offers the facility to share a single internet connection among all the LAN users.

**Disadvantages of LAN**

Here are the important cons/ drawbacks of LAN:

- LAN will indeed save cost because of shared computer resources, but the initial cost of installing Local Area Networks is quite high.
- The LAN admin can check personal data files of every LAN user, so it does not offer good privacy.
- Unauthorized users can access critical data of an organization in case LAN admin is not able to secure centralized data repository.
- Local Area Network requires a constant LAN administration as there are issues related to software setup and hardware failures.

**Network Device**

There are various network Devices used in a LAN, The basic network devices used in a LAN are

- NICs (Network Interface Cards)
- Hubs
- Switches
- Bridges
- Routers
- Gateways
- Firewalls
- WAPs
- Modems etc.

**WAN (Wide Area Network):**

WAN (Wide Area Network) is another important computer network that which is spread across a large geographical area. WAN network system could be a connection of a LAN which connects with other LAN’s using telephone lines and radio waves. It is mostly limited to an enterprise or an organization.

**Characteristics of LAN:**
The software files will be shared among all the users; therefore, all can access to the latest files.
Any organization can form its global integrated network using WAN.

Advantages of WAN

Here are the benefits/pros of using WAN:

- WAN helps you to cover a larger geographical area. Therefore business offices situated at longer distances can easily communicate.
- Contains devices like mobile phones, laptop, tablet, computers, gaming consoles, etc.
- WLAN connections work using radio transmitters and receivers built into client devices.

Disadvantage of WAN

- The initial setup cost of investment is very high.
- It is difficult to maintain the WAN network. You need skilled technicians and network administrators.
- There are more errors and issues because of the wide coverage and the use of different technologies.
- It requires more time to resolve issues because of the involvement of multiple wired and wireless technologies.
- Offers lower security compared to other types of networks.

Uninterruptible power supply (UPS)

An uninterruptible power supply (UPS) is a device that allows a computer to keep running for at least a short time when the primary power source is lost. UPS devices also provide protection from power surges.

A UPS contains a battery that "kicks in" when the device senses a loss of power from the primary source. If an end user is working on the computer when the UPS notifies of the power loss, they have time to save any data they are working on and exit before the secondary power source (the battery) runs out. When all power runs out, any data in your computer’s random access memory (RAM) is erased. When power surges occur, a UPS intercepts the surge so that it does not damage the computer.

Core Banking Solution

What is the Core Banking System?

Core Banking solutions are vital to the day-to-day functioning of any bank. It is an integral part of the banking technology which aims to serve their clients and customer with the best services. In simple words, core banking solutions are account-management back-end and front-end processes.
Core is short for “Centralized Online Real-time Exchange.” As the name suggests, it is a centralized system or a network created by a bank and its branches. This allows the customers of the bank to access, manage and perform basic transactions from any branch of the bank they hold an account in. Thus, core banking software allows the banks to create a centralized data center.

**Core banking solutions offer the following advantages to the bank:**

- Improved operations which address customer demands and industry consolidation
- Errors due to multiple entries eradicated
- Easy ability to introduce new financial products and manage changes in existing products
- Seamless merging of back office data and self-service operations.

**Features of Core Banking Solution:**

- Customer-On Boarding.
- Managing deposits and withdrawals.
- Transactions management
- Interest. Calculation and management.
- Payments processing (cash, cheques/checks, mandates, NEFT, RTGS etc.).
- Customer relationship management (CRM) activities.
- Designing new banking products.
- Loans disbursal and management.
- Accounts management
- Establishing criteria for minimum balances, interest rates, number of withdrawals allowed and so on.

**Unit 2- Payment System and Electronic Banking**

**Electronic Payment system**

E-payment system is a way of making transactions or paying for goods and services through an electronic medium without the use of check or cash.

**Automated Teller Machines (ATM)**
The Automated Teller Machine, or ATM, enables people to withdraw and deposit money from their bank accounts using machines.

The Committee headed by Dr. C. Rangarajan recommended the setting up of ATM in India.

**ATM Models in India:**
- Online
- Offline
- Stand-alone
- Networked

**HWAK (The Intelligent Auto-teller and Netware Management System)**

Intelligent auto-teller systems are a special breed of auto-teller machines capable of thinking for themselves, that means they are fast, impose less demands on your banking systems and serve the customers more like a personal banker than less sophisticated auto-teller systems.

HWAK provides unsurpassed service even without benefit of a reliable communication network.

**Benefits of HWAK are:**
- Customer satisfaction.
- High availability
- Online and offline auto-recovery
- Anytime full banking service
- Low cost, shorter queues and less number of tellers with ease of use
- Quick and early implementation
- Enhanced security and audit control
- Network management
- Predictable cost of ownership
- Comprehensive ‘One Stop’ autobanking.

**White Label ATMs (WLA)**
Automated Teller Machines (ATMs) set up, owned and operated by non-bank entities are called “White Label ATMs” (WLAs). They provide the banking services to the customers of banks in India, based on the cards (debit/credit/prepaid) issued by banks.

**Key facts related:**

- Non-bank entities shall commence setting up and operating WLAs only after it has been authorised to do so by the RBI under the **Payment and Settlement Systems Act, 2007**.

- Taking over of ATMs operated by banks would not be permitted. Entities may ensure to draw a strategic plan for installation of such WLAs based on the criteria set during authorization. White Label ATM Operators (WLAO) may also indicate the value added services it proposes to offer at the WLA while seeking authorisation.

- WLAO is permitted to have more than one Sponsor Bank. All the transactions of WLAs serviced by this Sponsor Bank would be settled through it.

- Cash Management at the WLAs will be the responsibility of the Sponsor Bank, who may if required, make necessary arrangements with other banks for servicing cash requirements at various places.

- WLAO may establish connectivity with any of the authorised ATM Network Operators/ Card Payment Network Operators and ensure that the settlement of all the transactions at the WLAs shall be done only in the books of the Sponsor Bank through the ATM Network Operators/ Card Payment Network Operators with whom the WLAO has established connectivity.

- Maintenance and servicing of the WLAs shall be the sole responsibility of the WLAO.

**As per the new guidelines, it has been decided to allow:**

- The WLA Operators to buy wholesale cash, above a threshold of 1 lakh pieces (and in multiples thereof) of any denomination, directly from the Reserve Bank (Issue Offices) and Currency Chests against full payment.

- The operators to source cash from any scheduled bank, including Cooperative Banks and Regional Rural Banks.

- The operators to offer bill payment and Interoperable Cash Deposit services, subject to technical feasibility and certification by National Payments Corporation of India (NPCI).

- The display advertisements pertaining to non-financial products / services anywhere within the WLA premises, including the WLA screen, except the main signboard. However, it shall be ensured that the advertisements running on the screen disappear once the customer commences a transaction.
Banks to issue co-branded ATM cards in partnership with the authorised WLA Operators and may extend the benefit of ‘on-us’ transactions to their WLAs as well.

All guidelines, safeguards, standards and control measures applicable to banks relating to currency handling, and cyber-security framework for ATMs, shall also be applicable to the WLA Operators.

**National Payment Corporation of India (NPCI)**

National Payments Corporation of India (NPCI), an initiative of the Reserve Bank of India (RBI) and Indian Banks’ Association (IBA), is an umbrella organisation for operating retail payments and settlement systems in India.

NPCI has ten core promoter banks—State Bank of India, Punjab National Bank, Bank of Baroda, Canara Bank, Bank of India, HDFC Bank, Citibank, HSBC, and ICICI Bank.

The organisation functions under the provisions of the **Payment and Settlement Systems Act, 2007** in order to create robust payments and settlement infrastructure for India.

It is a non-profit organisation set up **under the provisions of Section 25 of Companies Act, 1956 (now, Section 8 of Companies Act, 2013)**. NPCI aims to provide infrastructure to the whole banking industry, both physical and electronic payment and settlements system.

**Rupay Card**

RuPay was introduced in 2012 by NPCI and functions within the domestic boundaries. RuPay cardholders can use the service for ATM withdrawals, online transactions, and card payments. RuPay card has a comparatively lower processing cost and processing time in comparison to Visa and MasterCard. RuPay cards are available all over the country including urban and rural areas.

**Benefits of RuPay Card**

A brainchild of RBI, RuPay is exclusively crafted to meet the needs and requirements of Indian customers. Here are some of the benefits that RuPay customers stand to get.

- **Security of Information Related to Indians:** Customer data and transaction details pertaining to RuPay card transactions will not be passed outside India.
- **Safe Transactions:** With SMS alerts and notifications that are sent to the customer’s phone number after every transaction, RuPay cardholders can be ensured of a secure transaction.
- **Designed for India:** RuPay cards have been customized keeping in mind the product and service requirements of Indians.
• **Greater Reach in Rural Areas:** When it comes to the RuPay cards transactions, all the processing happens within the country. This results in lower cost of settlement and clearing for the transactions made using RuPay debit card. Banks will profit immensely from this as costs for transaction processing becomes affordable.

• **Greater Reach in Rural Areas:** Consumers in rural areas can easily apply and get a RuPay card.

• **Payment Solutions across Platforms:** RuPay debit card is designed to provide complete interoperability between payment channels including mobile technology, ATMs, cheques etc.

## Plastic Cards

### Types of Plastic Cards

**Debit Card**

Debit card is linked to the account of the cardholder i.e one who owns the cards. They are usually issued by Banks and financial institutions. When ones use a debit card the money is immediately deducted directly from one’s account associated with the card. One can buy things as long as there is money in account. A debit card is a way to “pay now” Say you have Rs 10,000 in your account. The amount you can spend, or withdraw, through your card cannot exceed this limit.

**Credit Card**

Credit Card is a small plastic card that is issued by financial institutions such as banks. As the name Credit when one buys using credit card, one is buying by taking loan. One needs to pay back later(there are no free lunches in life!). There is a limit to which one can buy on a credit card. So, even if you have only Rs 10,000 in your account but your credit limit is Rs 50,000, you are free to spend up to Rs 50,000. You could also have Rs 1,00,000 in your account, but your credit limit is only Rs 50,000. You need to repay the amount bought on credit by a due date.

**Charge card**

Charge card carries all the features of credit cards. However, after using a charge card you will have to pay off the entire amount billed, by the due date. If you fail to do so, you are likely to be considered a defaulter and will usually have to pay up a steep late payment charge. In case of credit card, one can pay late payment fee if one misses the due date. Popular charge cards are American Express cards also called as Amex cards

**Smart Card**
It contains an electronic chip that is used to store cash. There is no requirement of any signature, identification and payment authorization. The exact amount is deducted from the smart card during payment and is collected by the smart card reader machines.

**Member Card**

A small card issued to and held by a member of a club, society or other organisation, verifying the member's membership for a given period.

Membership cards and discount offers are important elements of marketing programs designed to build customer loyalty. Consumers and business customers can apply for membership cards offered by companies that sell products or services that they buy frequently.

**Electronic Banking**

Electronic banking has many names like e banking, virtual banking, online banking, or internet banking. It is simply the use of electronic and telecommunications network for delivering various banking products and services. Through e-banking, a customer can access his account and conduct many transactions using his computer or mobile phone.

**Anytime Banking**

ATMs have eliminated the time limitations of customer service and offer a host of banking services, including deposit, withdrawals, requisitions, instructions and transfers.

**Anywhere Banking**

With the introduction of ATMs and tele-banking, financial details can be accessed from remote locations and basic transactions can be effected even outside the bank.

**Home Banking (Corporate and Personal)**

Home Banking Versus Online Banking

Online banking is generally available for both individuals and small businesses. Additional services, such as certificates of deposit (CDs), and business, personal and mortgage loans, often still occur at physical branch locations.

**Corporate Banking**

Remote Banking has become very popular among corporate customers especially big business/ industrial house which are already automated. More and More banks are providing customer terminals right in the customer’s office, which facilitates the customers to operate the account without physically coming to the bank.

*At present, by utilizing remote banking facility, corporate customers will be able to get the following services:*
Getting their current balance or getting their statement of accounts for any pre-defined period

- Ordering cheque banks
- Ordering/Transferring intra-bank and inter-bank fund transfers
- Instructing stop payments of cheques
- International remittances
- Opening letter of credits

**Personal Banking**

Personal banking is a type of banking service and product line offered by banks to retail customers, that is consumers rather than businesses, intermediaries and institutions. Banks worldwide offer personal banking products that typically include savings and transaction facilities such as a bank transaction account, debit cards/EFT, an interest bearing floating account (savings account) and a fixed interest deposit account for a specific agreed period (certificates of deposit / term deposit) which can vary according to the bank. In addition it also includes debt facilities such as loans, mortgages and credit cards.

**Example:**

The customers of personal banking services and products are commonly the general public that includes adult individuals, retirees, students, children who may be citizens, residents and non-residents depending on the requirements of the country or bank. While affluent individuals may also use personal banking services, they may also be offered private banking services by banks which can include more sophisticated services and investments.

**Internet banking:**

Most online payments are done via internet banking option. It has become one of the most convenient payment methods for transferring money. Most banks have created their own apps that can be downloaded on the phone and used any time. Through mobile devices, users can make transactions through mobile apps, net banking facilities, or internet fund transfer services such as IMPS (Immediate Payment Services), NEFT (National Electronic Fund Transfer), and RTGS (Real-time Gross Settlement).

**Mobile Banking**

Mobile banking has simplified the lives of many people and given them the option to send money, receive money, check account balance, pay bills, etc. using their mobile phones. And the best part is that banks offer mobile banking services for free.
Electronic Commerce (E-Commerce)

E-Commerce or Electronic Commerce means buying and selling of goods, products, or services over the internet. E-commerce is also known as electronic commerce or internet commerce. These services provided online over the internet network. Transaction of money, funds, and data are also considered as E-commerce. These business transactions can be done in four ways: Business to Business (B2B), Business to Customer (B2C), Customer to Customer (C2C), Customer to Business (C2B). The standard definition of E-commerce is a commercial transaction which is happened over the internet. Online stores like Amazon, Flipkart, Shopify, Myntra, Ebay, Quikr, Olx are examples of E-commerce websites. By 2020, global retail e-commerce can reach up to $27 Trillion.

Cheque Truncation

Section 6 of the Negotiable Instruments Act, defined cheque as “a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand”. This section has been amended in September 2002 to include truncations and cheques within the definition of cheque.

What is Cheque Truncation System?

Cheque Truncation System (CTS) is a cheque clearing system undertaken by the Reserve Bank of India (RBI) for quicker cheque clearance. As the term proposes, truncation is the course of discontinuing the flow of the physical cheque in its way of clearing. Instead of this an electronic image of the cheque is transferred with vital essential data. Cheque Truncation System brings elegance to the whole activity of cheque processing & clearing and offers numerous benefits to banks like time and cost savings, cost effectiveness, including human resource rationalization, business process re-engineering and enhanced customer service.

Benefits of Cheque Truncation System

- Time, money and manpower expended on physical transfer of cheques from banks to clearing house are eliminated
- Clearing related frauds become less plausible
- Probability of cheques misplaced in transit is eliminated
- CTS is more advanced and more secure.
- It provides quicker clearance of cheques
- Reduces operational risk and risks related to paper clearing
• There are no extra charges levied for the collection of cheques drawn on a bank located within the grid, further providing no geographical restrictions.

Unit 3- Data Communications Networks and EFT Systems

Data Communication Networks

Data communications helps in drastically cutting and the time involved in transferring data from the point of origin to the computer and information from the computer to the point of use.

Components of Data Communications Networks

Data communications typically consists of various data communication components. When the components operate together for the sharing of resources, they are said to form a network. It has three basic components.

Transmission Devices and Interface Equipment

The data is transmitted along the communication path between computer devices using electrical signals and bit sequences to represent number and characters.

Modem: A modem is a device or program that enables a computer to transmit data over, for example, telephone or cable lines. Computer information is stored digitally, whereas information transmitted over telephone lines is transmitted in the form of analog waves. A modem converts between these two forms.

Transmission Medium

For Communications between computers, the data has travel through some medium during its transmission. The prevalent technologies for data communications media are terrestrial, microwave and satellites.

(a) Terrestrial Cables (Three types)

• Twisted Pair
• Coaxial Cable
• Optical fibre
(b) **Microwave systems:** A microwave system is a system of gear used for microwave data transmission. The typical microwave system includes radios located high atop microwave towers, which are used for the transmission of microwave communications using line of sight microwave radio technology.

(c) **Communication satellite:** A satellite is a body that moves around another body in a mathematically predictable path called an Orbit. A communication satellite is nothing but a microwave repeater station in space that is helpful in telecommunications, radio, and television along with internet applications.

A repeater is a circuit which increases the strength of the signal it receives and retransmits it. But here this repeater works as a transponder, which changes the frequency band of the transmitted signal, from the received one.

The frequency with which the signal is sent into the space is called Uplink frequency, while the frequency with which it is sent by the transponder is Downlink frequency.

**Transmission Processors**

The Purpose of communication processors is to enhance is to data communication between two points. Communications processors can be broadly categorized as:

- Message Switches
- Multiplexers
- Front end processors

**Modes of transmission**

- Simplex
- Half-Duplex
- Full Duplex

**Network Scenario in India: Major Networks**

The Committees on communication networks for banks, set up in 1987 under the chairmanship of “T.N Anantharam Lyer” executive director, RBI, had strongly recommended for the establishment of a cooperative communication network especially for the banking industry.

**INET**

INET was set up by the department of telephones in the year 1991. It is a fast, reliable, flexible and quite cost effective data communication network.

**NICNET**
NICNET has been set up by the National Informatics Centre (NIC), a Government of India organization. It is India’s largest Wide Area Network (WAN). The Master Earth station is installed in New Delhi, to provide access to satellites and operates from around 2000 VSAT terminals.

**INDONET**

It was set up by CMC Ltd. In the 1980 and was among the first countrywide networks in India.

**RBI Net**

After recognising the pressing need to harness information technology for intra-bank and inter-bank communications in the 1980s, RBI commissioned the BANKNET in 1991. 

*RBI Net is also being used by several departments of banks for various applications such as:*

- **Transmission of section 42(2) o the RBI Act, 1934, data** by commercial banks to regional offices of department of banking operations and development (DBOD) and furnishing of consolidated data by the regional offices of DBOD to central DBOD.
- Press relations division daily news summary of important financial matters.
- Department of economic analysis and policy macroeconomic indicators on a weekly basis.

**Emerging Trends in Communications Networks for Banking**

**RBI’s VSAT Network**

The Indian Financial Network (INFINET) is a Closed User Group (CUG) Network for the exclusive use of Member Banks and Financial Institutions. It was set up by the Reserve Bank in 1999 through the Institute for Development and Research in Banking and Technology (IDRBT) Hyderabad. The Institute explored capability, methods, procedure to expand the network using a blend of communication technologies such as VSATs and Terrestrial Leased Lines. In order to have a careful combination of technologies in the INFINET, a Leased Line Network (LLN), connecting 21 major cities has been seamlessly integrated with it. The LLN is a mix of 2 Mbps and 64 Kbps lines. The LLN provides gateways to banks from each of these 21 cities. The Network Management System (NMS) of
the LLN is located at the INFINET Hub at Hyderabad. The Backup NMS is located in the Main Office of RBI in Mumbai.

Among various inter-bank and intra-bank applications ranging from simple messaging, MIS, EFT (Retail), Electronic Clearing Service (ECS) for both Credits and Debits, online dealing and trading in Government securities, Centralized Funds Management System (CFMS) for Banks and Financial Institutions, Anywhere banking/Anytime Banking (ATM), Inter-Branch Reconciliation, Structured Financial Messaging System (SFMS) and Electronic Funds transfer (RTGS/NEFT) System, transmission of Inter-city Cheque Realisation advices, government securities trading, and currency chest accounting are done through this service. VSAT technology service can also be used for one-way and/or interactive communications via satellite. Presently, the network consists of over 950 VSATs located in 127 cities of the country. All Banks and financial institutions in the country are eligible to become members of the INFINET.

**Internet**

The Internet is a global network of networks. It is a system of computers which allows user computers exchange data, message, files etc.

- The Internet is a global network of networks. It is a system of computers which allows user computers exchange data, message, files etc.
- Serial Line Protocol (SLIP)
- Point to Point Protocol (PPP)

**Internet Access Service**

- E-mail
- Usenet
- Gopher
- File Transfer Protocol (FTP)
- World Wide Web (WWW)

**SWIFT (Society for Worldwide Interbank Financial Telecommunication)**

SWIFT message types are the format or schema used to send messages to financial institutions on the SWIFT (Society for Worldwide Interbank Financial Telecommunication) network. The original message types were developed by SWIFT.
and retrospectively made into an ISO standard, ISO 15022. In many instances, SWIFT message types between custodians follow the ISO standard. This was later supplemented by a XML based version under ISO 20022.

SWIFT India Domestic Services Pvt Ltd (“SWIFT India” or “the Company”), founded on similar principles, is a financial messaging services provider formed by SWIFT SCRL and Indian banks, for the domestic Indian financial community and by the community.

Through shared resources and capital, SWIFT India functions with the objective of enabling harmonised exchange of structured financial information between domestic participants in the domestic Indian community, thereby

(a) Reducing costs and risks,

(b) Expanding the reach of automated, standardised and secure exchange of information across the industry,

(c) Enabling new instruments, opportunities and markets for the industry.

**Message types:**

- Real-time and bulk messages
- File transfer of structured and unstructured information

**Security:**

- Role-based access control
- Maker-checker controls
- 3 layers of asymmetric encryption to ensure integrity, authenticity and confidentiality
- Hardware security modules
- Support for local Controller of Certifying Authorities (CCA) licensed public key infrastructure (PKI)

**International and domestic standards:**

- Support for international ISO 15022 (MT) and ISO 20022 (MX) message formats, including domestic to international message transformation
- Support for local market practices and flows
- Support for local addressing schemes such as the Indian Financial System Codes (IFSC)

**Value added message features:**

- Guaranteed delivery
- Delivery confirmation and non-delivery warning
• Broadcast messages
• Syntax and rule-book message validation
• Non-repudiation proof of message transmission in case of dispute
• Message retrieval for 124 days in case of messages lost or corrupted by either sender or receiver
• Store-and-forward for when counterparties are not online

**Back-office integration for straight-through-processing**

• Message transformation
• Multiple protocols (including SOAP, MQ, file transfer, etc)
• Custom workflows

**Premium support**

• Standard 24/7 online and phone support
• Other premium support features such as onsite support, pro-active network monitoring and health checks, coordinated business continuity exercises, and others. Visit Support & Training for more information.

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**Unit 4- Role Of Technology Upgradation and Its Impact on Banks**

**Trades in Technology Development**

The Advancements in software tools, computer hardware and telecommunications have shifted the focus of the banks towards computerization from data processing to information services.

• Data Warehousing
• Data Mining

**Data Warehousing**

What is Data Warehousing?
Data warehousing is the process of constructing and using a data warehouse. A data warehouse is constructed by integrating data from multiple heterogeneous sources that support analytical reporting, structured and/or ad hoc queries, and decision making. Data warehousing involves data cleaning, data integration, and data consolidations.

Using Data Warehouse Information

There are decision support technologies that help utilize the data available in a data warehouse. These technologies help executives to use the warehouse quickly and effectively. They can gather data, analyze it, and take decisions based on the information present in the warehouse. The information gathered in a warehouse can be used in any of the following domains –

- **Tuning Production Strategies** – The product strategies can be well tuned by repositioning the products and managing the product portfolios by comparing the sales quarterly or yearly.
- **Customer Analysis** – Customer analysis is done by analyzing the customer's buying preferences, buying time, budget cycles, etc.
- **Operations Analysis** – Data warehousing also helps in customer relationship management, and making environmental corrections. The information also allows us to analyze business operations.

Integrating Heterogeneous Databases

To integrate heterogeneous databases, we have two approaches –

- Query-driven Approach
- Update-driven Approach

**Query-Driven Approach**

This is the traditional approach to integrate heterogeneous databases. This approach was used to build wrappers and integrators on top of multiple heterogeneous databases. These integrators are also known as mediators.

**Process of Query-Driven Approach**

- When a query is issued to a client side, a metadata dictionary translates the query into an appropriate form for individual heterogeneous sites involved.
- Now these queries are mapped and sent to the local query processor.
- The results from heterogeneous sites are integrated into a global answer set.

Disadvantages
Query-driven approach needs complex integration and filtering processes.
This approach is very inefficient.
It is very expensive for frequent queries.
This approach is also very expensive for queries that require aggregations.

Update-Driven Approach

This is an alternative to the traditional approach. Today’s data warehouse systems follow update-driven approach rather than the traditional approach discussed earlier. In update-driven approach, the information from multiple heterogeneous sources are integrated in advance and are stored in a warehouse. This information is available for direct querying and analysis.

Advantages

This approach has the following advantages –

- This approach provide high performance.
- The data is copied, processed, integrated, annotated, summarized and restructured in semantic data store in advance.
- Query processing does not require an interface to process data at local sources.

Functions of Data Warehouse Tools and Utilities

The following are the functions of data warehouse tools and utilities –

- **Data Extraction** – Involves gathering data from multiple heterogeneous sources.
- **Data Cleaning** – Involves finding and correcting the errors in data.
- **Data Transformation** – Involves converting the data from legacy format to warehouse format.
- **Data Loading** – Involves sorting, summarizing, consolidating, checking integrity, and building indices and partitions.
- **Refreshing** – Involves updating from data sources to warehouse.

Data Mining

What is Data Mining?

Data mining is looking for hidden, valid, and potentially useful patterns in huge data sets. Data Mining is all about discovering unsuspected/ previously unknown relationships amongst the data.
It is a multi-disciplinary skill that uses machine learning, statistics, AI and database technology.

The insights derived via Data Mining can be used for marketing, fraud detection, and scientific discovery, etc.

Data mining is also called as Knowledge discovery, Knowledge extraction, data/pattern analysis, information harvesting, etc.

**Business understanding:**

In this phase, business and data-mining goals are established.

- First, you need to understand business and client objectives. You need to define what your client wants (which many times even they do not know themselves)
- Take stock of the current data mining scenario. Factor in resources, assumption, constraints, and other significant factors into your assessment.
- Using business objectives and current scenario, define your data mining goals.
- A good data mining plan is very detailed and should be developed to accomplish both business and data mining goals.

**Data understanding:**

In this phase, sanity check on data is performed to check whether its appropriate for the data mining goals.

- First, data is collected from multiple data sources available in the organization.
- These data sources may include multiple databases, flat file or data cubes. There are issues like object matching and schema integration which can arise during Data Integration process. It is a quite complex and tricky process as data from various sources unlikely to match easily. For example, table A contains an entity named cust_no whereas another table B contains an entity named cust-id.
- Therefore, it is quite difficult to ensure that both of these given objects refer to the same value or not. Here, Metadata should be used to reduce errors in the data integration process.
- Next, the step is to search for properties of acquired data. A good way to explore the data is to answer the data mining questions (decided in business phase) using the query, reporting, and visualization tools.
- Based on the results of query, the data quality should be ascertained. Missing data if any should be acquired.

**Benefits of Data Mining:**

- Data mining technique helps companies to get knowledge-based information.
• Data mining helps organizations to make the profitable adjustments in operation and production.
• The data mining is a cost-effective and efficient solution compared to other statistical data applications.
• Data mining helps with the decision-making process.
• Facilitates automated prediction of trends and behaviors as well as automated discovery of hidden patterns.
• It can be implemented in new systems as well as existing platforms.
• It is the speedy process which makes it easy for the users to analyze huge amount of data in less time.

Disadvantages of Data Mining

• There are chances of companies may sell useful information of their customers to other companies for money. For example, American Express has sold credit card purchases of their customers to the other companies.
• Many data mining analytics software is difficult to operate and requires advance training to work on.
• Different data mining tools work in different manners due to different algorithms employed in their design. Therefore, the selection of correct data mining tool is a very difficult task.
• The data mining techniques are not accurate, and so it can cause serious consequences in certain conditions.

Role and Uses of Technology Upgradation

Technology has allowed banks to offer much more to their customers like the facilities of card and telephone access, anytime and anywhere banking through 24hrs ATMs, credit card, debit card and POS (Point of sale) access. The technology has made it possible for the customers to have fingertip access to their accounts worldwide.

Data and Message Transferring

• Electronic Data Interchange (EDI): Banks have been using EDI in the form of SWIFT messages.
• Electronic Mail

Corporate Websites

• Dissemination of information
• Financial Advice
• To highlight non-banking activities
• A node for commerce
• Selling financial products
• Gateway to the Internet
• Account services

Management Information System (MIS):

A management information system is an information system used for decision-making, and for the coordination, control, analysis, and visualization of information in an organization. The study of the management information systems testing people, processes and technology in an organizational context.

• Computer-based Information systems
• Decision Support Systems (DSS)

Impact of ‘IT’ on Banks

• Changes in Organisational Structure and Orientation
• Impact on Service Quality (Changes In Customer Aspirations)
• Impact on Human Resources (Role Transition, Training Needs)
• Impact on Privacy and Confidentiality of Data

Unit 5- Security Considerations

Risk Concern Areas

The Customer Demands have triggered a fierce competition among banks and financial companies for the application of information technology in their operations to help them offer innovative products and services at reduced costs. This also helps those entering new geographical areas.

• Data and software: Data is critical resource, necessary for an organisation’s continuing operations. Incorrect data can have serious implications in decision making, as well. The increasing availability and use of expert system and the potential impact erroneous data can result in playing havoc with an organisation’s business.
Infrastructure: Banks have to invest heavily for implementing technology-based tools and solutions. In addition to software and data, same hardware components are required for operations of the computer and communication systems.

Peopleware: Peopleware refers to the group of persons directly or indirectly involved in managing and running the computerized systems.

**Different types of Threats**

The threats to computerized system manifests in the form of business interruptions as under:

- Errors and omissions in data and software
- Unauthorised disclosure of confidential information
- Computer abuse and mis-utilisation of banks assets
- Computer/cyber frauds

**Accidental Damages:** Computers and communications systems have found their applications to be quite extensive in banking and other financial organisations. However, at the same time, these systems are vulnerable to damages caused accidentally, both due to human failures and natural calamities.

- Environmental Hazards
- Human Error and Omissions
- Unreliable systems

**Malicious Damages:** Risk of malicious damages to computerized systems can be from disgruntled employees who wish to disrupt the services or from individuals with malafide intentions, using the technology for perpetrating fraud for financial gains.

- Interruptions in Services
- Frauds

**Control Mechanism**

Implementation of effective control mechanism is required management of risks associated with the use of IT tools.

Physical Control

Internal Control
1. Accounting Control
2. Administrative Control

Operational Control

1. Audit Trails (i) Accounting Audit Trail (ii) Operations Audit Trail
2. Checksum
3. Data Encryption

Computer Audit

Banks can achieve effective, secure and reliable computer systems only through the use of appropriate control techniques discussed above. The control techniques selected, varies from bank to bank, reflecting the particular risks within each bank and the costs of related security and control procedures.

A regular programme of independent tests of security and control procedures by auditors help in identifying lapses before the banking operations land into serious risk. The generic organizational function aimed at evaluation of the asset safeguarding, data integrity, system effectiveness, and system efficiency in computerized systems is termed as “Computer Audit”.

Information System Audit (IS Audit)

An information system (IS) audit or information technology (IT) audit is an examination of the controls within an entity's Information technology infrastructure. These reviews may be performed in conjunction with a financial statement audit, internal audit, or other form of attestation engagement. It is the process of collecting and evaluating evidence of an organization's information systems, practices, and operations. Obtained evidence evaluation can ensure whether the organization's information systems safeguard assets, maintains data integrity, and are operating effectively and efficiently to achieve the organization's goals or objectives.

Information Systems Audit Methodology

PHASE 1: Audit Planning
PHASE 2 – Risk Assessment and Business Process Analysis
PHASE 3 – Performance of Audit Work
PHASE 4: Reporting
**Benefit of IS Audit**

It would identify the risks of exposure to an existing computerized environment. On Identification of the risks, remedial measure can be taken to protect the interests of an organisation.

It would deter people/employees/users from indulging in corruption/manipulation of data, frauds etc. An undesired activity will be detected through implementation of IS audit.

**Information System Security (IS Security)**

Information systems security, also known as INFOSEC, is a broad subject within the field of information technology (IT) that focuses on protecting computers, networks, and their users. Almost all modern companies, as well as many families and individuals, have justified concerns about digital risks to their well-being.

**Need for IS Security**

- To Comply with law of the land and regulator’s guidelines.
- To comply with business policy.
- To comply with business partner’s requirements.

**IS Security in Banking**

Banks must meet their customers requirement for security aspects in special way on many levels, whether it is with their saving, taking advantage of over-the-counter services at a branch office, withdrawing money from the teller machines, making deposits via the cash recycling system, online banking etc.

**Threats to IS Security**

- E-mail Viruses
- Phishing Attacks
- Hackers Attack
- Vishing
- Smishing

**Evaluation Requirements**

The IT resources continuously undergo changes in the form of development of new applications, acquisition of new hardware, turnover of trained employees etc.

- Computer Hardware
Legal Framework For Electronic Transactions

At present, many legal provisions recognize the paper-based records and documents that should bear signature. Since, electronic commerce eliminates the need for paper-based transactions. Therefore to facilitate e-commerce, there was a need for enactment/amendment of necessary Law.

Indian Parliament enacted a comprehensive information Technology Bill, which received the Present’s assent on 9 June 2000.

Consequent upon the recognition given to the electronic records, electronic documents and electronic signatures, incidental amendments have also been made in the following Acts:

- The Indian Penal Code, 1860
- The Indian Evidence Act, 1872
- The Banker’s Bank Evidence Act, 1891
- The Reserve Bank of India Act, 1934

The Act purports to include the work “electronic record” along with the word “record”/“document” appearing generally in various sections of these act.

The amendment to Indian Penal Code, 1860, also states that for the purpose of the Section 466 (dealing with forgery of records) a “register” shall include any list, data or record of any entries maintained in the electronic form as defined in the IT Act 2000.

Bankers Books Evidence Act, 1891 redefines banker's books as ledgers, daybooks, cash books and account Books used in the ordinary business of the Bank.

The RBI act, 1934 has been amended by the IT act, 2000, empowering the central board to make regulations for fund transfers through electronic means between the banks or between the banks and other financial institutions.

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<table>
<thead>
<tr>
<th>Paper</th>
<th>Description</th>
<th>Fee</th>
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<tr>
<td>JAIIB/DBF Paper-I</td>
<td>(Principle and Practices of Banking) Online Mock Tests</td>
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<tr>
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**MODULE D - SUPPORT SERVICES – MARKETING OF BANKING SERVICES/PRODUCTS**

**Jaiib/DBF Paper 1 (Module D)**
Index

Unit 1- Marketing An Introduction
Unit 2- Social Media Marketing
Unit 3- Consumer Behavior and Product
Unit 4- Pricing
Unit 5- Distribution: Meaning, Functions, Factors and Types
Unit 6- Channel Management
Unit 7- Promotion
Unit 8- Role of Direct Selling Agent/ Direct Marketing Agent in a Bank
Unit 9- Marketing Information Systems

Unit 1- Marketing An Introduction

Market

The word “Market” in common parlance refers to the place where goods can be bought or sold.

A market consists of all the potential customers sharing a particular need or want who might be able to engage in an exchange to satisfy that need or want.

Types of Market

<table>
<thead>
<tr>
<th>Basis of Classification</th>
<th>Types of Market</th>
</tr>
</thead>
<tbody>
<tr>
<td>Geographical Area</td>
<td>Local Market, Regional Market, National Market, World/Global Market</td>
</tr>
<tr>
<td>Product</td>
<td>Cotton/Tea/Vegetable market, Share Market, Bullion Market, Capital Market, Real Estate Market, Retail Loan Market</td>
</tr>
<tr>
<td>Nature of Transaction</td>
<td>Cash/Spot Market, Future Market, Commodity Market</td>
</tr>
</tbody>
</table>
Marketing is the process of determining consumer demand for a product or services, motivating its sale and Distributing it into ultimate consumption at a profit.

**Marketing- A Management Function**

Marketing provides entrepreneurship by identifying opportunities in customer requirements and mobilizing resources to capitalize on them. Marketing forms an interface with the existing and potential customers. It passes through the management functions of analyzing, planning, implementing and controlling.

**Selling vs Marketing**

<table>
<thead>
<tr>
<th>BASIS FOR COMPARISON</th>
<th>SELLING CONCEPT</th>
<th>MARKETING CONCEPT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Meaning</td>
<td>Selling concept is a business notion, which states that if consumers and businesses remain unattended, then there will not be ample sale of organization’s product.</td>
<td>Marketing concept is a business orientation which talks about accomplishing organizational goals by becoming better than others in providing customer satisfaction.</td>
</tr>
<tr>
<td>Associated with</td>
<td>Compelling consumer's mind towards goods and services.</td>
<td>Directing goods and services towards consumer's mind.</td>
</tr>
<tr>
<td>Starting point</td>
<td>Factory</td>
<td>Target Market</td>
</tr>
<tr>
<td>Focuses on</td>
<td>Product</td>
<td>Customer needs</td>
</tr>
<tr>
<td>Perspective</td>
<td>Inside-out</td>
<td>Outside-in</td>
</tr>
</tbody>
</table>
### Marketing Management

Marketing management is the process of decision making, planning, and controlling the marketing aspects of a company in terms of the marketing concept, somewhere within the marketing system. Before proceeding to examine some of the details of this process, comments on two aspects will be helpful background.

**According to Philip Kotler,** “Marketing Management is the art and science of choosing target markets and building profitable relationship with them. Marketing management is a process involving analysis, planning, implementing and control and it covers goods, services, ideas and the goal is to produce satisfaction to the parties involved”.

**Functions of Marketing Management**

- Analysis
- Planning
- Implementation
- Control

**Important of Marketing for Banks**
Marketing can support banking business only when the minimum 2 of the above are competent enough. There is no point in doing marketing for a business if the product is not worth it, it’s just waste of money and effort as sooner or later customer would find out the value of the product and was it worth their investment/time.

Same rule applies to customer service and digital technology.

Marketing is no doubt necessary for banking as the competition is intense and nearly everyone wants to keep their hard earned money safe and secured. But to gain someone’s trust and for a long time Banks needs to fundamentally change the sales and marketing dynamics and include the above three in its core.

**Products and Services**

**What is Product?**

According to Philip Kotler “A product is anything tangible or intangible that can be offered to a market for attention, acquisition use or consumption that might satisfy a need or want”.

**Characteristics of Physical Products**

- Tangible
- Homogeneous
- Production and distribution separated from consumption
- Core value produced in factory
- Customers do not participate in the production process
- Can be stored
- Transfer of ownership possible

**What is a service?**

Philip Kotler and Paul N. Bloom define services as any activity or benefit that one party can offer to another, which is basically intangible and does not result in the ownership of anything. They added that its production may or may not be tied to a tangible product.

**Characteristics of Service Products**

Intangibility: Intangibility is an important consideration that complicates the functional responsibility of a marketing manager, specially while influencing and motivating the prospects/customers. The goods of tangible nature can be displayed, the prospects or buyers can have a view and they can even test and make a trial before making the buying decisions. The selling processes are thus found easier.
Inseparability: This is also a feature that complicates the task of professionals while marketing the services. The inseparability focuses on the fact that the services are not of separable nature. Generally, the services are created and supplied simultaneously.

Heterogeneity: Another feature is heterogeneity which makes it difficult to establish standard. The quality of services can’t be standardised. The prices charged may be too high or too low. In the case of entertainment and sports, we find the same thing. The same type of services can’t be sold to all the customers even if they pay the same price.

Perishability: This means that the service “units” cannot be stoked. If a seat is unfulfilled when the plane leaves or the play starts, it cannot be stored and sold next day or next week, that revenue is lost forever.

Different between Physical Goods and Services

<table>
<thead>
<tr>
<th>Physical Goods</th>
<th>Services</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tangible</td>
<td>Intangible</td>
</tr>
<tr>
<td>Homogeneous</td>
<td>Heterogeneous</td>
</tr>
<tr>
<td>Production and distribution separated from consumption</td>
<td>Production, distribution and consumption are simultaneous process</td>
</tr>
<tr>
<td>A Thing</td>
<td>An activity or process</td>
</tr>
<tr>
<td>Core value produced in factory</td>
<td>Core value produced in buyer seller interactions</td>
</tr>
<tr>
<td>Customers do not participate in the production process</td>
<td>Customers participate in the production</td>
</tr>
<tr>
<td>Can be kept in stock</td>
<td>Cannot be kept in stock</td>
</tr>
<tr>
<td>Transfer of ownership</td>
<td>No transfer of ownership</td>
</tr>
</tbody>
</table>

Marketing of Financial Services

The characteristics of services viz, intangibility, inseparability, heterogeneity and perishability are all present in financial services, too. Some assume special meaning in the context of financial services. Intangibility has two aspects:

At one level, it is concerned with the fact that services are impalpable in the sense that they have no physical form.

Many services are intangible from a conceptual point of view, in that are not easily defined and may be difficult to understand. (Bateson)
Types of Financial Markets in India

- The credit Market
- Equity and term lending market
- Gilt-edged securities market
- Insurance market
- Mutual funds
- Consumer finance market
- The money market
- Debt market
- Leasing and hire purchase
- Foreign exchange market
- Stock markets

Marketing of Banking Services

Bank marketing is the aggregate of functions, directed at providing services to satisfy customers' financial (and other related) needs and wants, more effectively and efficiently than the competitors keeping in view the organizational objectives of the bank.

This definition highlights the following points:

- Bank Provide services
- Aim is to satisfy customer needs and wants of specific nature
- The nature of needs and wants of the customer is primarily financial, while some may be incidental to or related to these.
- The competitive element, efficiency and effectiveness are major factors in the process.
- Organizational objective are still the driving force.

Marketing Mix

It is a marketing tool that combines a number of components in order to strengthen and solidify a product's brand and to help sell the product or service. Companies have to come up with strategies to sell their products, and coming up with a marketing mix is one of them.
Marketing Mix 4P’s

A marketing expert named E. Jerome McCarthy created the Marketing 4Ps in the 1960s. This classification has been used throughout the world. Business schools teach this concept in basic marketing classes.

The marketing 4Ps are also the foundation of the idea of marketing mix.

1. **Promotion**: How the awareness is created among the customers.
2. **Place**: Where the customer wants delivery of product.
3. **Price**: What the customer is ready to pay for this product.
4. **Product**: What are the features of the product.

**4Cs Marketing Model**

The 4Cs marketing model was developed by Robert F. Lauterborn in 1990. It is a modification of the 4Ps model.

It is not a basic part of the marketing mix definition, but rather an extension.
4Ps to 4Cs

Cost – According to Lauterborn, price is not the only cost incurred when purchasing a product. Cost of conscience or opportunity cost is also part of the cost of product ownership.

Consumer Wants and Needs – A company should only sell a product that addresses consumer demand. So, marketers and business researchers should carefully study the consumer wants and needs.

Communication – According to Lauterborn, “promotion” is manipulative while communication is “cooperative”. Marketers should aim to create an open dialogue with potential clients based on their needs and wants.

Convenience – The product should be readily available to the consumers. Marketers should strategically place the products in several visible distribution points.

The Marketing Mix 7P’s
Brand Image

Today's generation is quite impressionable and hence in order to enhance their personality, or to meet social standards, they gravitate towards branded products that are creating a stir in the market. This brand image is simply an impression or an imprint of the brand developed over a period of time in the consumer’s mindset.

This image of a brand is ultimately a deciding factor that determines the product sales. The brand image is very important, as it is an accumulation of beliefs and views about that particular brand. The character and value of the brand is portrayed by its image, as it is the main component in the scheme of things.

The brand image is eventually the mirror through which the company’s key values are reflected.

**Why Brand is Important?**
User Association: Brand is used as prestige or success by associating with glamorous personalities.

Value Proposition: Buying decisions are affected or influenced with brand value.

Experience: A proven track of good performance only can create brand. It creates faith among customers.

How Brand are Build?

- Quality
- Positioning
- Strong communication
- Time and consistency
- Innovation
- Consistent customer satisfaction
- Early entry in Market

Colours Play an Important Part in Logo

Orange: The Colour of dynamism, an organization, responsive to market condition & Customer needs.

Blue: The colour of trust and depth.

Maroon: The colour of warmth an organization that goes beyond the basics to understand its customers and provide them with products and services with a view to building lasting relationships.

Grey: The colour of stability.

White: The colour of ethics and organization which has set for itself high standards of corporate governance standards which guide its professionals who are committed to the highest levels of integrity and work ethics.

Electric orange: The colour of dynamism- brighter & Sharper.

Unit 2- Social Media Marketing

What is Social Media Marketing

Social media marketing is the use of social media platforms and websites to promote a product or service. Although the terms e-marketing and digital marketing are still
dominant in academia, social media marketing is becoming more popular for both practitioners and researchers. Most social media platforms have built-in data analytics tools, which enable companies to track the progress, success, and engagement of ad campaigns. Companies address a range of stakeholders through social media marketing, including current and potential customers, current and potential employees, journalists, bloggers, and the general public. On a strategic level, social media marketing includes the management of a marketing campaign, governance, setting the scope (e.g. more active or passive use) and the establishment of a firm’s desired social media “culture” and “tone.”

When using social media marketing, firms can allow customers and Internet users to post user-generated content (e.g., online comments, product reviews, etc.), also known as "earned media," rather than use marketer-prepared advertising copy.

Some of the Popular Social Marketing Networks

- Twitter
- Facebook
- Pinterest
- Google+
- LinkedIn
- Youtube
- Instagram

Reason of Social Media Impact on Marketing

- Brand Recognition
- Community
- Repeat Exposure
- Authority
- Influence
- Website Traffic
- Cost-effective
- Improved brand loyalty
- Healthier customer satisfaction

Benefits of Social Media
• Improved Social Signals (Which is a factor in the search ranking algorithm)
• Company Branding
• Improved Brand Awareness
• Word-of-mouth advertising
• Increased customer loyalty and trust
• Improved audience reach and influence

**Unit 3- Consumer Behavior and Product**

**Consumer Behavior**

**Maslow’s Hierarchy Needs**

While considering the marketing of a product, whether a physical or a service product, we must understand the customer’s need as per Maslow’s theory of hierarchy of needs and human behavior:

**Physiological Needs**

- Food
- Water
- Breathing
- Homeostasis

**Security and Safety Needs**

- Financial security
- Heath and wellness
- Safety against accidents and injury

**Social Needs**

- Friendships
- Romantic attachments
- Family
- Social groups
Community groups
Churches and religious organizations

Esteem Needs
Self-respect
Recognition
Status
Success

Self-actualization
Self-fulfillment

Family Life Cycle

The Family life cycle is divided into four stages and the financial status and Banking

<table>
<thead>
<tr>
<th>Stage</th>
<th>Financial Situation</th>
<th>Banking Needs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Young Bachelor</td>
<td>Per capita income high, no Dependents. Few financial burdens.</td>
<td>Credit cards, auto loan, low cost banking services</td>
</tr>
<tr>
<td>Half nest (Married with young children)</td>
<td>Home buying priority, low liquidity</td>
<td>Mortgage loan, credit card, overdraft, durables loan</td>
</tr>
<tr>
<td>Full nest (Older couple, grown up children)</td>
<td>Income stabilized, good financial position</td>
<td>Home improvement, equity investment flexi-deposit, investment services</td>
</tr>
<tr>
<td>Empty nest (Older couple)</td>
<td>Significantly reduced income</td>
<td>Social security services, some loans</td>
</tr>
</tbody>
</table>

Customer Relationship Management

Relationship marketing is the attracting, maintaining and nurturing relationship with customer in a multi-service organization aimed at customer relations.

Objective of Relationship Marketing

- Long term customer retention
• Relationship with external market who influence or provide referrals
• Integrating marketing activities, customer service and quality standards

Note: CRM concept and the database becomes the focal point for all marketing activities from customer loyalty programmes to internal communication.

Comparison between Transaction Marketing and Relationship Marketing

<table>
<thead>
<tr>
<th>Transaction Marketing</th>
<th>Relationship Marketing</th>
</tr>
</thead>
<tbody>
<tr>
<td>Single sale focus</td>
<td>Customer Retention Focus</td>
</tr>
<tr>
<td>Product Feature Oriented</td>
<td>Product Benefit Oriented</td>
</tr>
<tr>
<td>Short –time frame</td>
<td>Long time scale</td>
</tr>
<tr>
<td>Low Emphasis on Customer Service</td>
<td>High Emphasis on customer Service</td>
</tr>
<tr>
<td>Moderate Customer Contact</td>
<td>High Customer Contact</td>
</tr>
<tr>
<td>Moderate Quality Concern</td>
<td>High Quality Concern</td>
</tr>
</tbody>
</table>

Activities under CRM

• Establish and maintain a customer information information database
• Planning customer contact points
• Analyzing informal customer feedback
• Conducting customer satisfaction survey
• Managing communication programmes
• Hosting special events
• Auditing and reclaiming lost customers

Gap Analysis
Gap 1: Difference between Customer Expectations and Perceptions of needs by Management. Occurs when the company management does not understand what customers really want.

Gap 2: Difference between Perception of needs by Management and Specification of the service. Occurs when Management understand what customers want but this does not translate into correct specifications and orders to the rest of the company.

Gap 3: Difference between Specification of the service and the Service produced. Occurs when the people who “produce” the service are unable, unwilling or do not know how to reach the specified standard.

Gap 4: Difference between the Service produced and Communication. Occurs when the service expectations formed by customers based on corporate communication are not met.

Gap 5: There is no clear consensus on what this gap means. Initially, it meant the difference between Expectations and Perception of service, which may arise when the customer sees a characteristic of service quality as something undesirable. But this gap is also now used to identify overall customer dissatisfaction, which appears as the result of the sum of the other gaps. At Openmet, we prefer the first of the two versions because it adds to the analysis of the causes of dissatisfaction.
Product

Kotler has defined product as:
A product is anything that can be offered to a market for attention, acquisition, use or consumption that might satisfy a want or need.

Product Personality

- The Core Features
- The Associated Features
- The Brand Name and Logo
- The Package and Label

Product Levels

The five product levels are:

Core benefit: The fundamental need or want that consumers satisfy by consuming the product or service. For example, the need to process digital images.

Generic product: A version of the product containing only those attributes or characteristics absolutely necessary for it to function. For example, the need to process
digital images could be satisfied by a generic, low-end, personal computer using free image processing software or a processing laboratory.

**Expected product:** The set of attributes or characteristics that buyers normally expect and agree to when they purchase a product. For example, the computer is specified to deliver fast image processing and has a high-resolution, accurate colour screen.

**Augmented product:** The inclusion of additional features, benefits, attributes or related services that serve to differentiate the product from its competitors. For example, the computer comes pre-loaded with a high-end image processing software for no extra cost or at a deeply discounted, incremental cost.

**Potential product:** This includes all the augmentations and transformations a product might undergo in the future. To ensure future customer loyalty, a business must aim to surprise and delight customers in the future by continuing to augment products. For example, the customer receives ongoing image processing software upgrades with new and useful features.

**Product Planning**

Product Planning comprises the process of developing and maintaining a portfolio of products, which satisfy the needs and wants of customers from different segments.

*The following are main tasks in managing the product mix:*

- Appraisal of each product line and each product item
- Decision on packaging
- Product differentiation and positioning
- Managing brands and developing brand equity
- New product development
- Managing the product life cycle of products/brands
- Managing product quality

**Product Life Cycle**

The product life cycle has 4 very clearly defined stages, each with its own characteristics that mean different things for business that are trying to manage the life cycle of their particular products.

**Introduction Stage** – This stage of the cycle could be the most expensive for a company launching a new product. The size of the market for the product is small, which means sales are low, although they will be increasing. On the other hand, the cost of things like research
and development, consumer testing, and the marketing needed to launch the product can be very high, especially if it’s a competitive sector.

**Growth Stage** – The growth stage is typically characterized by a strong growth in sales and profits, and because the company can start to benefit from economies of scale in production, the profit margins, as well as the overall amount of profit, will increase. This makes it possible for businesses to invest more money in the promotional activity to maximize the potential of this growth stage.

**Maturity Stage** – During the maturity stage, the product is established and the aim for the manufacturer is now to maintain the market share they have built up. This is probably the most competitive time for most products and businesses need to invest wisely in any marketing they undertake. They also need to consider any product modifications or improvements to the production process which might give them a competitive advantage.

**Decline Stage** – Eventually, the market for a product will start to shrink, and this is what’s known as the decline stage. This shrinkage could be due to the market becoming saturated (i.e. all the customers who will buy the product have already purchased it), or because the consumers are switching to a different type of product. While this decline may be inevitable, it may still be possible for companies to make some profit by switching to less-expensive production methods and cheaper markets.

**New Product Development**

The Process of product development comprises of following five main stage:

- Idea generation and screening
- Concept development and testing
- Product development
- Test marketing
- Commercial launch

**Product Strategies**

Marketing strategies which are on the product element are called product strategies.

**i) Product Modification**

- Quality Improvement
- Feature Improvement
- Style Improvement

**ii) Product Elimination**
The Major reasons for product elimination are:

- Sales keep declining continuously and there is no possibility of increasing sales.
- Profits keep declining continuously and there is no possibility of improving profits.
- Product prices are declining continuously and it may be difficult for the firm to supply at the prevailing market price.
- Excessive administration expenditure and time.

iii) Diversification

Diversification refers to entering attractive opportunities which are outside the existing business of the firm. Three types of diversification are generally observed:

**Concentric Diversification:** A type of diversification in which a company acquires or develops new products or services (closely related to its core business or technology) to enter one or more new markets.

**Horizontal Diversification:** Horizontal diversification involves the extension of a production of products or service above and beyond the industry, in which the company operates.

**Conglomerate Diversification:** Conglomerate diversification is growth strategy that involves adding new products or services that are significantly different from the organization's present products or services.

Other Aspects of Product Development

- Branding
- Packaging
- Labeling

**Unit 4 - Pricing**

**Important Of Pricing**

When marketers talk about what they do as part of their responsibilities for marketing products, the tasks associated with setting price are often not at the top of the list. Marketers are much more likely to discuss their activities related to promotion, product development, market research and other tasks that are viewed as the more interesting and exciting parts of the job. Yet pricing decisions can have important consequences for the
marketing organization and the attention given by the marketer to pricing is just as important as the attention given to more recognizable marketing activities.

**Objective of Pricing**

- Maximum Profit
- Survival
- Market Share
- Cash Flow
- Status quo
- Product Quality
- Communication Image

**Different Between Short Term Objective and Long-term Objective**

<table>
<thead>
<tr>
<th>Short Term Objective</th>
<th>Long Term Objective</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profit Maximization</td>
<td>Profit Optimization</td>
</tr>
<tr>
<td>Minimum return on sales turnover</td>
<td>Minimum return on investment</td>
</tr>
<tr>
<td>Achieving a particular sales level</td>
<td>Achieving a particular market share</td>
</tr>
<tr>
<td>Deeper penetration of the market</td>
<td>Entering new market</td>
</tr>
<tr>
<td>Keeping parity with competition</td>
<td>Providing commodities/services at prices that will stimulate economic development</td>
</tr>
<tr>
<td>Fast turnaround or early cash recovery</td>
<td>Stabilizing prices and margins in the market</td>
</tr>
</tbody>
</table>

**Factors Influencing Pricing**

<table>
<thead>
<tr>
<th>Internal Factors</th>
<th>External Factors</th>
</tr>
</thead>
<tbody>
<tr>
<td>Objectives of the firm—both corporate and marketing</td>
<td>Market characteristics—pertaining to demand, customer, competition</td>
</tr>
<tr>
<td>Characteristics of the product</td>
<td>Buyer's behavior and bargaining power</td>
</tr>
<tr>
<td>Life cycle stage of the product</td>
<td>Competitors policy</td>
</tr>
</tbody>
</table>
Pricing Methods

The Pricing Methods are the ways in which the price of goods and services can be calculated by considering all the factors such as the product/service, competition, target audience, product’s life cycle, firm’s vision of expansion, etc. influencing the pricing strategy as a whole.

The pricing methods can be broadly classified into two parts:

- Cost Oriented Pricing Method
- Market Oriented Pricing Method
**Cost-Oriented Pricing Method:** Many firms consider the Cost of Production as a base for calculating the price of the finished goods. Cost-oriented pricing method covers the following ways of pricing:

**Cost-Plus Pricing:** It is one of the simplest pricing method wherein the manufacturer calculates the cost of production incurred and add a certain percentage of markup to it to realize the selling price. The markup is the percentage of profit calculated on total cost i.e. fixed and variable cost.

E.g. If the Cost of Production of product-A is Rs 500 with a markup of 25% on total cost, the selling price will be calculated as:

\[
\text{Selling Price} = \text{cost of production} + \frac{\text{Cost of Production} \times \text{Markup Percentage}}{100}
\]

\[
\text{Selling Price} = 500 + 500 \times 0.25 = 625
\]

Thus, a firm earns a profit of Rs 125 (Profit=Selling price- Cost price).

**Markup pricing** - This pricing method is the variation of cost plus pricing wherein the percentage of markup is calculated on the selling price. E.g. If the unit cost of a chocolate is Rs 16 and producer wants to earn the markup of 20% on sales then mark up price will be:

\[
\text{Markup Price} = \frac{\text{Unit Cost}}{1 \text{- desired return on sales}}
\]

\[
\text{Markup Price} = \frac{16}{1-0.20} = 20
\]

Thus, the producer will charge Rs 20 for one chocolate and will earn a profit of Rs 4 per unit.

**Target-Return pricing** - In this kind of pricing method the firm set the price to yield a required Rate of Return on Investment (ROI) from the sale of goods and services. E.g. If soap manufacturer invested Rs 1,00,000 in the business and expects 20% ROI i.e. Rs 20,000, the target return price is given by:

\[
\text{Target return price} = \frac{\text{Unit Cost} + (\text{Desired Return} \times \text{capital invested})}{\text{unit sales}}
\]

\[
\text{Target Return Price} = \frac{16 + (0.20 \times 100000)}{5000} \text{Target Return Price} = \text{Rs 20}
\]

Thus, Manufacturer will earn 20% ROI provided that unit cost and sale unit is accurate. In case the sales do not reach 50,000 units then the manufacturer should prepare the break-even chart wherein different ROI’s can be calculated at different sales unit.

**Market-Oriented Pricing Method:** Under this method price is calculated on the basis of market conditions. *Following are the methods under this group:*

**Perceived-Value Pricing:** In this pricing method, the manufacturer decides the price on the basis of customer’s perception of the goods and services taking into consideration all the elements such as advertising, promotional tools, additional benefits, product quality, the channel of distribution, etc. that influence the customer’s perception.
E.g. Customer buy Sony products despite less price products available in the market, this is because Sony company follows the perceived pricing policy wherein the customer is willing to pay extra for better quality and durability of the product.

**Value Pricing:** Under this pricing method companies design the low priced products and maintain the high-quality offering. Here the prices are not kept low, but the product is re-engineered to reduce the cost of production and maintain the quality simultaneously.

E.g. Tata Nano is the best example of value pricing, despite several Tata cars, the company designed a car with necessary features at a low price and lived up to its quality.

**Going-Rate Pricing** - In this pricing method, the firms consider the competitor’s price as a base in determining the price of its own offerings. Generally, the prices are more or less same as that of the competitor and the price war gets over among the firms.

E.g. In Oligopolistic Industry such as steel, paper, fertilizer, etc. the price charged is same.

**Auction Type Pricing:** This type of pricing method is growing popular with the more usage of internet. Several online sites such as eBay, Quikr, OLX, etc. provides a platform to customers where they buy or sell the commodities.

**Differential Pricing:** This pricing method is adopted when different prices have to be charged from the different group of customers. The prices can also vary with respect to time, area, and product form.

E.g. The best example of differential pricing is Mineral Water. The price of Mineral Water varies in hotels, railway stations, retail stores.

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**Pricing Strategies**

**Geographical Pricing:** Geographical pricing, in marketing, is the practice of modifying a basic list price based on the geographical location of the buyer. It is intended to reflect the costs of shipping to different locations.

**Psychological Pricing:** Psychological pricing (also price ending, charm pricing) is a pricing and marketing strategy based on the theory that certain prices have a psychological impact. Retail prices are often expressed as "odd prices": a little less than a round number, e.g. $19.99 or £2.98.

**Discriminatory Pricing:** Price discrimination is a microeconomic pricing strategy where identical or largely similar goods or services are transacted at different prices by the same provider in different markets.

**Market Skimming Pricing:** A pricing approach in which the producer sets a high introductory price to attract buyers with a strong desire for the product and the resources to buy it, and then gradually reduces the price to attract the next and subsequent layers of the market.
Pricing Discounts and Allowances: The seller generally allows some discount to the buyer. It is usually expressed as a percentage of sale prices. A seller may allow either of the trade and cash discounts or both of them.

Promotion Pricing: Price promotions or promotional pricing is the sales promotion technique which involves reducing the price of a product or services in short term to attract more customers & increase the sales volume.

Product mix: The product mix is the collection of products and services that a company chooses to offer its market. Pricing strategies range from being the cost leader to being a high-value, luxury option for consumers.

Market penetration pricing: Market penetration pricing is a pricing strategy that sets a low initial price for a product. The goal is to quickly attract new customers based on the low cost. The strategy is most effective for increasing market share and sales volume while discouraging competition.

Bank Pricing

There are two major costs, which have to be considered while pricing bank products:

- Interest Cost
- Servicing Cost

Factors which impact in bank pricing:

- Risk and return
- Monetary Policy
- Capital adequacy
- Cost- benefit analysis

Unit 5- Distribution: Meaning, Functions, Factors and Types

Distribution Channel

A distribution channel is a chain of businesses or intermediaries through which a good or service passes until it reaches the final buyer or the end consumer. Distribution channels can include wholesalers, retailers, distributors, and even the Internet.

Function of Distribution Channel
**Product Promotion:** Sales promotional activities are mostly performed by the producer but sometimes middlemen also participate in these activities like special displays, discounts etc.

**Matching:** The Distribution channel partners, shape and fit the offer to the buyer’s needs, including alterations, grading, assembling and packaging. They also help in providing variety of offerings from different sources to the consume.

**Negotiation:** Middlemen negotiate the price, quality, guarantee and other related matters about a product with the producer as well as customer.

**Physical Distribution:** Marketing channels are responsible for assembly, storage, sorting, and transportation of goods from manufacturers to customers.

**Marketing:** Distribution channels are also called marketing channels because they are among the core touch points where many marketing strategies are executed. They are in direct contact with the end customers and help the manufacturers in propagating the brand message and product benefits and other benefits to the customers.

**Risk Taking:** Middlemen have to bear the risk of distribution like risk from damage or spoilage of goods etc. when the goods are transported from one place to another or when they are stored in the god-owns.

---

**Types of Distribution Channels**

Channels of distribution can be divided into the direct channel and the indirect channels. Indirect channels can further be divided into one-level, two-level, and three-level channels based on the number of intermediaries between manufacturers and customers.

**Direct Channel or Zero-level Channel (Manufacturer to Customer)**

Direct selling is one of the oldest forms of selling products. It doesn’t involve the inclusion of an intermediary and the manufacturer gets in direct contact with the customer at the point of sale. Some examples of direct channels are peddling, brand retail stores, taking orders on the company’s website, etc.

**Indirect Channels (Selling Through Intermediaries)**

When a manufacturer involves a middleman/intermediary to sell its product to the end customer, it is said to be using an indirect channel. Indirect channels can be classified into three types:

**One-level Channel (Manufacturer to Retailer to Customer):** Retailers buy the product from the manufacturer and then sell it to the customers. One level channel of distribution works best for manufacturers dealing in shopping goods like clothes, shoes, furniture, toys, etc.
Two-Level Channel (Manufacturer to Wholesaler to Retailer to Customer): Wholesalers buy the bulk from the manufacturers, breaks it down into small packages and sells them to retailers who eventually sell it to the end customers. Goods which are durable, standardised and somewhat inexpensive and whose target audience isn’t limited to a confined area use two-level channel of distribution.

Three-Level Channel (Manufacturer to Agent to Wholesaler to Retailer to Customer): Three level channel of distribution involves an agent besides the wholesaler and retailer who assists in selling goods. These agents come handy when goods need to move quickly into the market soon after the order is placed. They are given the duty to handle the product distribution of a specified area or district in return of a certain percentage commission. The agents can be categorised into super stockists and carrying and forwarding agents. Both these agents keep the stock on behalf of the company. Super stockists buy the stock from manufacturers and sell them to wholesalers and retailers of their area.

Factors Influencing Channel selection

Producers have to decide the types of channels for distribution of their products. The major factors influencing this decision are discussed below:

- Market Characteristics
- Product Characteristics
- Competition Characteristics
- Company Characteristics
## Channels for Banking Services

- Branches
- Telephones Banking and call centres
- ATM
- Personal Computer
- Plastic Cards
- Virtual Branches and Automated video Banking

### Mobile Banking

**Advantage**

- With Mobile Banking, users of mobile phones can perform several financial conveniently and securely from their mobile.
- A person can check his/her account balance, review recent transaction, transfer fund, pay bills, locate ATMs, mange investments etc.
• Mobile banking is available round the clock 24/7/365
• Mobile banking is said to be even secure than online/internet banking. ETC ETC.

Disadvantages

• Mobile banking users are at risk of receiving fake SMS messages and scams.
• The loss of a person’s mobile device often means that criminals can gain access to your mobile banking PIN and other sensitive information.

Internet Banking

Most online payments are done via internet banking option. It has become one of the most convenient payment methods for transferring money. Most banks have created their own apps that can be downloaded on the phone and used any time. Through mobile devices, users can make transactions through mobile apps, net banking facilities, or internet fund transfer services such as IMPS (Immediate Payment Services), NEFT (National Electronic Fund Transfer), and RTGS (Real-time Gross Settlement).

Advantages

• Easy To Operate
• Convenience Of Making Payments
• Round The Clock Availability
• Time Saving and Efficient
• Account Activity Tracking

Disadvantages

• No Online Banking Without Internet Access
• Threat Transaction Security
• Securing Your Password

Unit 6- Channel Management

Market channel System
Most producers do not sell their goods directly to the final users; between them stands a set of intermediaries performing a variety of functions. These intermediaries constitute a marketing channel. Some intermediaries such as wholesalers and retailers buy, take title to and resell the merchandise. They are called merchants.

Other brokers, manufactures representatives, sales agents-search for customers and may negotiate on the producer’s behalf but do not take title to the goods. They are called agents.

Still Other- Transportation companies, independent warehouses, banks, and advertising agencies-assists in the distribution process but neither do they take title to goods nor do negotiate purchases or sales and they are called facilitators.

Market channels are set interdependent organizations involved in process of marketing a product or service available for use or consumption. Marketing channel decision are the most critical decisions faced by management. The company's channel decisions involve relatively long-term commitment to other firms, company’s pricing, advertising decisions, etc.

### Channel levels

- **Zero level:** Direct marketing channel e.g: Internet sale, door to door sale
- **One level:** Contains one selling intermediary such as a retailer
- **Two level:** Contains two selling intermediaries viz, wholesaler and retailer
- **Three level:** Wholesaler, who sells to jobbers, who in turn sell to retailers

### Channel Dynamics

**Vertical Marketing system (VMS):** In conventional channels no members like producer, wholesaler or retailers have any dependency on each other. They are completely independent.

**Horizontal Marketing system:** It is one in which two or more unrelated companies put together resources or programmers to exploit an emerging marketing opportunity. In this companies use another company's established channel.

**Multi-channel marketing systems:** With the proliferation of customer segments and channel possibilities, more companies have adopted multi-channel marketing. It occurs when a single firm use two or more marketing channels to reach one or more customer segments.
• Increased market coverage.
• Lower channel cost- for instance activating mobile banking rather than corresponding individually with customers.
• More Customized selling- using the technological advancement to mutual advantage and using the technical/ marketing personnel to sell more complex products.

**Unit 7- Promotion**

**Role of Promotion in Marketing**

Promotion is the exercise of communicating the properties of different elements of marketing mix to the customers with the intention of influencing them.

**Persuasion:** Promotion aims at persuading the consumers so that they start acting in favour of the firm. Persuasion seeks to bring about a change in attitude.

**Inform:** Promotion aims at conveying information about the properties of products to the prospects, to influence their desires and transform them into action.

**Reminding:** Promotion seeks to remind the customers about the offerings of the firm with a view to retaining their business and have a higher share in it.

**Reinforcing:** Promotion also aims at reinforcing the customer satisfaction. This helps in increasing the number of habitual customers.

**Promotion Mix**

The Promotion Mix refers to the blend of several promotional tools used by the business to create, maintain and increase the demand for goods and services.
Advertising: The advertising is any paid form of non-personal presentation and promotion of goods and services by the identified sponsor in the exchange of a fee. Through advertising, the marketer tries to build a pull strategy; wherein the customer is instigated to try the product at least once.

Personal Selling: This is one of the traditional forms of promotional tool wherein the salesman interacts with the customer directly by visiting them. It is a face to face interaction between the company representative and the customer with the objective to influence the customer to purchase the product or services.

Sales Promotion: The sales promotion is the short term incentives given to the customers to have an increased sale for a given period. Generally, the sales promotion schemes are floated in the market at the time of festivals or the end of the season. Discounts, Coupons, Payback offers, Freebies, etc. are some of the sales promotion schemes.

Public Relations: The marketers try to build a favourable image in the market by creating relations with the general public. The companies carry out several public relations campaigns with the objective to have a support of all the people associated with it either directly or indirectly.

Direct Marketing: With the intent of technology, companies reach customers directly without any intermediaries or any paid medium. The e-mails, text messages, Fax, are some of the tools of direct marketing.

Promotion Mix Strategies

There are two basic promotion mix strategies-

Push Strategy: In this, Promotion efforts are directed at the channel members to induce them to purchase the products and sell them to the final consumer. This is done through personal selling and trade promotions.

Pull Strategy: In this, the promotion efforts are directed to the final consumer to induce them to buy the product. Consumers will then demand the product from the retailer, who, in turn, will demand from the wholesaler and producers. This product experiences the “Pull” of demand.

Factors Influencing the Promotion Mix

Three major factors affecting the choice of promotion mix are

Type of Product:

Type of product plays an important role in deciding on promotion mix. Product can be categorized in terms of branded products, non-branded products, necessity products, luxury products, new products, etc. All these types of products need different promotional tools. For example, advertising is suitable for the branded and popular products. Personal
selling may be fit for non-branded products. Advertising, personal selling, sales promotion and publicity – all four tools – are used for a newly launched product to get a rapid consumer acceptance.

**Readiness of Buyer:**

Different promotional tools are required at different stages of buyer readiness. Such as, at the comprehension stage, the blend of advertising and personal selling plays a vital role. Whereas at the conviction stage, personal selling is more effective. At the time of sales closure, the blend of sales promotion and personal selling is likely to be more effective.

Hence, the advertising and publicity are more effective at the early stages of buying decision process while the sales promotion and personal selling are more effective during the later stages.

**Stage of Product Life Cycle:**

Product passes through four stages of its life cycle. Each stage poses different threats and opportunities. Each stage needs separate marketing strategies. Each of the promotional tools has got different degree of suitability with stages of product life cycle.

*It can be concluded that, in normal situations:*

- Advertising, personal selling, and, even, sales promotion are used during the introduction stage. However, advertising is given more priority,
- More intensive advertising and sales promotional techniques are used during the second stage,
- More rigorous advertising along with personal selling are followed in the third stage, and
- Company prefers to curb the expenses in forth stage, and promotional efforts are reduced.

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**Unit 8 - Role of Direct Selling Agent/ Direct Marketing Agent in a Bank**

**Direct Selling**

Direct selling refers to selling products directly to the consumer in a **non-retail environment. Instead, sales occur at home, work, online, or other non-store locations.**

**Direct Marketing**
Direct marketing is an advertising strategy that relies on the individual distribution of a sales pitch to potential customers. **Mail, email, and texting are among the delivery systems used.** It is called direct marketing because it generally eliminates the middleman such as advertising media.

**Benefit of Direct Marketing**

- It saves time and introduces customer to the various range of products.
- It is convenient, easy and hassle free for the customer.
- Various products are available at customer’s disposition
- It opens various delivery channels to the customer.
- Banks can offer a real time, customized and personalized marketing,
- It reduces the operational cost.
- It saves man hours and manpower in banks.
- It enables the banker to cater to the needs of individuals, both the commoner and the techno savvy.
- It enables the banker to use his available time for doing marketing jobs.
- It enables deployment of available manpower for other jobs

**Banker as a Direct selling Agent (DSA)/ Direct Marketing Agent (DMA) and his Job Role**

In The primary responsibility of the Banking Direct Selling Agent/Representative is branch management and in-branch services, teller and platform services, financial product sales, customer services, and management of lending risk to retail customer base. He builds a client base for banking direct sales through prospecting, networking, and referrals.

*A typical job description for the Banking Direct Selling Agent Representative role may include:*

- Develops new business prospects in specific geographic areas through cold calls.
- Interacts with existing customers to increase sales of the bank’s products and services.
• Requires a high school diploma or equivalent and **2-4 years of experience in the field** or in a related area.
• Familiar with standard concepts, practices, and procedures within a particular field.

**Code of Conduct for Direct selling Agents/ Direct Marketing Agents**

1. Tele-calling a Prospect (a prospective customer)

• A prospect is to be contacted for sourcing a bank product or bank related product only under the following circumstances:
• When prospect has expressed a desire to acquire a product through the bank’s internet site/call centre/Branch or through the Relationship Manager at the bank or has been referred to by another prospect/customer or is an existing customer of the bank who has given consent for accepting calls on other products of the bank.
• When the prospect’s name/telephone no/ address is available & has been taken from one of the lists/directories/databases approved by the DSA Manager/Team leader, after taking his/ her consent.
• The TME should not call a person whose name/number is flagged in any “do not disturb” list made available to him/her.

2. Leaving messages and contacting persons other than the prospect.

• Calls must first be placed to the prospect. In the event the prospect is not available, a message may be left for him/her. The aim of the message should be to get the prospect to return the call or to check for a convenient time to call again. Ordinarily, such messages may be restricted to:
  • Please leave a message that ______________ (Name of officer) representing HDFC called and requested to call back at __________ (phone number)’’.
• As a general rule, the message must indicate:
• That the purpose of the call is regarding selling or distributing a bank product of HDFC Bank
3. No misleading statements/misrepresentations permitted

**TME/BDE should not** –

- Mislead the prospect on any service / product offered;
- Mislead the prospect about their business or organization’s name, or falsely represent themselves.
- Make any false / unauthorised commitment on behalf of Axis Bank for any facility/service.

4. Telemarketing Etiquettes

**PRE CALL**

No calls prior to 0930 Hrs or post 1900 Hrs unless specifically requested.

- No serial dialing
- No calling on lists unless list is cleared by team leader

**DURING CALL**

- Identify yourself, your company and your principal
- Request permission to proceed
- If denied permission, apologize and politely disconnect.
- State reason for your call
- Always offer to call back on landline, if call is made to a cell number
- Never interrupt or argue
- To the extent possible, talk in the language which is most comfortable to the prospect
- Keep the conversation limited to business matters
- Check for understanding of “Most Important Terms and Conditions” by the customer if he plans to buy the product
- Reconfirm next call or next visit details
- Provide your telephone no, your supervisor’s name or your bank officer contact details if asked for by the customer.
- Thank the customer for his/her time

**POST CALL**

- Customers who have expressed their lack of interest for the offering should not be called for the next 3 months with the same offer
– Provide feedback to the bank on customers who have expressed their desire to be flagged “Do Not Disturb”

– Never call or entertain calls from customers regarding products already sold. Advise them to contact the Customer Service Staff of the bank.

5. Gifts or bribes

TME/BDE’s must not accept gifts from prospects or bribes of any kind. Any TME/BDE offered a bribe or payment of any kind by a customer must report the offer to his/her management.

6. Precautions to be taken on visits/contacts

DSA/DMA should:

• Respect personal space – maintain adequate distance from the prospect.

• Not enter the prospect’s residence/office against his/her wishes;

• Not visit in large numbers – i.e. not more than one DMA and one supervisor, if required.

• Respect the prospect’s privacy.

• If the prospect is not present and only family members/office persons are present at the time of the visit, he/she should end the visit with a request for the prospect to call back.

• Provide his/her telephone number, supervisor’s name or the concerned bank officer’s contact details, if asked for by the customer.

• Limit discussions with the prospect to the business – Maintain a professional distance.

7. Other important aspects – Appearance & Dress Code

DSA/ DMAs must be appropriately dressed –

**For men this means**

– Well ironed trousers;

– Well ironed shirt, shirt sleeves preferably buttoned down.

**For women this means**

– Well ironed formal attire (Saree, Suit etc.);

– Well groomed appearance.

Jeans and/or T Shirt, open sandals are not considered appropriate.

8. Handling of letters & other communication
Any communication sent to the prospect should be only in the mode and format approved by the Bank.

**Channels of Delivery in a Bank**

_The channels through which a bank offers its services are:_

- ATM Counters
- Net Banking
- Phone Banking
- Mobile Banking
- Real time Gross settlement system/ SWIFT
- Single Window system
- Online trading Account
- Cash Management Scheme/CMS
- Linking Banking and Insurance Related Products
- POS Machines
- Kioks

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**Unit 9- Marketing Information Systems**

**Marketing Information Systems**

"A marketing information system is a continuing and interacting structure of people, equipment and procedures to **gather, sort, analyse, evaluate, and distribute pertinent, timely and accurate information for use by marketing decision makers to improve their marketing planning, implementation, and control**."  

**Functions of Marketing information system**

- Collecting and assembling data
- Processing of data
- Analyzing the data
- Storage of data
• Dissemination of information

**Components of Marketing information system**

- **Internal records system**: The Company can collect information through its internal records comprising of sales data, customer database, product database, financial data, operations data, etc.

- **Market intelligence system**: The marketing intelligence system provides the data about the happenings in the market, i.e. data related to the marketing environment which is external to the organization. It includes the information about the changing market trends, competitor’s pricing strategy, change in the customer’s tastes and preferences, new products launched in the market, promotion strategy of the competitor, etc.

- **Marketing research system**: The Marketing Research is the systematic collection, organization, analysis and interpretation of the primary or the secondary data to find out the solutions to the marketing problems. Several Companies conduct marketing research to analyze the marketing environment comprising of changes in the customer’s tastes and preferences, competitor’s strategies, the scope of new product launch, etc.

- **Marketing management and science system**: It includes several software programs that can be used by the marketers to analyze the data, collected so far, to
take better marketing decisions. With the use of computers, the marking managers can save the huge data in a tabular form and can apply statistical programs to analyze the data and make the decisions in line with the findings.

**Advantage of Marketing information system**

- The MKIS framework provides a set of procedures and methods for regular, planning, purpose-oriented and systematic collection of data, its analysis, storage and retrieval.
- It helps in improving the data capture process, checks for reliability, consistency and quality of data.
- The operation of collecting, processing and transmitting data becomes smooth and the information flow to the decision-makers takes place in a ready for decision form.
- Provides tailor made information for specific needs.
- If facilitates repetitive use of the same information for different purposes.
- It also helps in sorting out conflicting information, which otherwise would lead to confusion and misdirect the decisions.
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Jaiib/DBF Paper 1, Module E- Ethics in Banks and Financial Institutions

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Unit 1- Ethics, Business Ethics & Banking: An Integrated Perspective

Ethics and Business values: Myth and Reality

Business Value

Business value are an informal term and it explains the core principles or standards that guide the way business is done. Values sum up what your business stands for and what makes it special.

Business ethics

Established principle and standard that guide behaviour in the world of business.

Different Between Business Ethics and Business Values

<table>
<thead>
<tr>
<th>Business Ethics</th>
<th>Business Values</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ethics refers to the guidelines for conduct, that address questions about morality</td>
<td>Value is defined as the principles and ideals, which help them in making judgment of what is more important.</td>
</tr>
<tr>
<td>Moral Principle system</td>
<td>Induces thinking</td>
</tr>
<tr>
<td>What is morally or incorrect in the given situation?</td>
<td>What we want to be or achieve?</td>
</tr>
<tr>
<td>Magnitude of rightness or wrongness of one’s options.</td>
<td>It explains the level of significance.</td>
</tr>
</tbody>
</table>

Myths vs Reality

Myth No. 1: Entrepreneurs are Essentially Inventors

Many aspirations die in the bud due to the existence of this perceived prerequisite. Entrepreneurship is often confused with the invention, where it's taken as a condition to be able to tangibly invent an app, system, product or a new equation in order to create market value. For example, the way Ola/Uber disrupted travel and Airbnb/Oyo Rooms disrupted hotel stays.

Reality: Entrepreneurs are Ideators

Entrepreneurship is a phenomenal journey which is flagged off with something as basic and simple as an idea. Entrepreneurs arise from an existing gap, and the right idea to fill
that gap. Once the idea stands out as disruptive, innovation and invention automatically fall in line. Work it up to the top before someone else works on it to build an empire.

**Myth No. 2: Entrepreneurs are Mainly Motivated by Money**

While money is the big game, it definitely isn't the end game. Money making makes for a very narrow viewpoint for those who certainly wish to establish a business. There are a larger passion and a bigger purpose that every budding entrepreneur holds or must hold onto than just making big bucks.

**Reality: Entrepreneurs are Motivated by Passion**

Most entrepreneurs believe in taking a risk and living life on the edge. They carry small phones but wider visions, live on bare necessities but live for huger possibilities. For any new business, the first few years are all about reaching a breakeven, profits become a part once execution is patiently handled and aimed for. Passion is the biggest motivation.

**Myth No. 3: Entrepreneurs Have to be Risk-takers**

A myth almost ingrained in the market almost believed to be a fact. Risk taking is more of an attitude when it comes to entrepreneurship. In the sea of bigger things, risk-taking is only one of the sailing boats. Very often many fierce risk takers fail due to the lack of ability to be risk avengers or that of being on the safe side of the spectrum at all times.

**Reality: Entrepreneurs Have to be Challenge-takers**

As an entrepreneur, all you need to be is a relentless challenger, which encompasses taking risks as well as avoiding them. To pose your idea as the distinguisher, all that you need is the attitude of a go-getter. The always prepared to face the adversity attitude should always come in play while facing obstacles, financial ups-downs and severe, cut-throat competition. Nothing is as strong as a strong will.

**Myth No. 4: Entrepreneurs are Born**

Where do we think they plan for the idea, while they develop in the womb? This is one of the biggest scandals of a myth, which makes thousands of people miss the chance of being the next big entrepreneur. Intelligence, high scores, family blood, none of these actually guarantees your ticket to the top.

**Reality: Entrepreneurs are Made**

Nothing begets dedication, will-power and courage. You aren't born an entrepreneur, you become one. The greatest entrepreneurs come from very average set-ups with almost no fortune in the bloodline. There will never be a shortcut to Hard work.

**Business Ethics**
Ethics means the set of rules or principles that the organization should follow. While in business ethics refers to a code of conduct that businesses are expected to follow while doing business.

Through ethics, a standard is set for the organization to regulate their behavior. This helps them in distinguishing between the wrong and the right part of the businesses.

Business ethics compromises of all these values and principles and helps in guiding the behavior in the organizations. Businesses should have a balance between the needs of the stakeholders and their desire to make profits.

While maintaining these balances, many times businesses require to do tradeoffs. To combat such scenarios, rules and principles are formed in the organization.

This ensures that businesses gain money without affecting the individuals or society as a whole. The ethics involved in the businesses reflect the philosophy of that organization.

**Principles of Business Ethics**

**Integrity**

Whenever there is great pressure to do right instead of maximizing profits, this principle is tested. The executives need to demonstrate courage and personal integrity, by doing what they think is right.

These are the principles, which are upright, honorable. They need to fight for their beliefs. For these principles, they will not back down and be hypocritical or experience.

**Loyalty**

No ethical behavior can be promoted without trust. And for trust, loyalty needs to be demonstrated. The executives need to be worthy of this trust while remaining loyal to the institutions and the person. There should be friendship in the time of adversity and support and devotion for the duty.

**Honesty**

The ethical executives are honest while dealing with their regular work. They also need to be truthful and do not deliberately deceive or mislead the information to others. There should be an avoidance of the partial truths, overstatements, misrepresentations, etc. Thus, they should not have selective omission by any means possible.

**Respect and Concern**

These are two necessarily different forms of behavior in the organization. But they go in tandem that is why they have been put under one principle. When the executive is ethical he is compassionate, kind, and caring.

**Fairness**
The executives need not be just fair in all the dealings, but they also should not exercise the wrong use of their power. They should not try to use over each or other indecent manners to gain any sort of advantage. Also, they should not take undue advantage of anything or other people’s mistakes.

Leadership

Any executive, if ethical, should be a leader to others. They should be able to handle the responsibilities. They should be aware of the opportunities due to their position. The executives need to be a proper role model for others.

Ethical Foundation of Banking: Finance Depends on Trust

Need and Important of Ethics in Banking

Bank need to deliver high quality services to its customers, which are driven by high ethical standards and therefore maintain the same in its work culture, management and also with the quality of its employees. Banks can only work well when the public trust them. Warranting safety of banking activities is certainly a challenging task. It depends heavily both on the economic condition of the country and in the environment of an open economy, the tendencies of development of countries worldwide as well.

Ethics help in dealing with dilemmas

Any banking business however well-placed, at times, it may have to confront moral dilemmas in their regular course of business. Banks have to deal with complex dilemmas in decision making, which is not about distinguishing between right and wrong, but between right versus less right. This, a Bank needs to adhere to a set of strong moral principles, which helps its employees in navigating through the obstacle of ethical choice, while making important decision.

Guards Reputation/ Goodwill

This is a two-pronged process, First, bank’s ethical practices aid in safeguarding depositor’s interest, thus, maintaining the stability of the system and preserving the reputation of the bank.

Second, Employees adhering to ethical practices prevent the breaches of law and corrupt activities. Besides this, it will also protect stakeholder’s interest and enhance the bank’s competitiveness and brand image.

Helps avoid risk

A well-defined code of ethics following by the superiors will ensure that the bank at all times maintain high ethical standards and have preventive and corrective measures against unethical practices by any of the staff members.
Principles of ethical banking

Banks are dependent on people to carry out its business who are reflection of the ethical standards of follows. Therefore, it is important for banking professionals to know what is expected from them and also help them to avoid temptations and pressures. Principles of ethics in banking business provide a guideline to the banking professional, which helps them in dealing with ethical issue.

**Principle of trust**- Trust is the confidence in quality or attribute of a person or a thing. It also includes truth of a statement. It includes both trustfulness and trustworthiness. In business, trust always means trustworthiness- which is established by trustfulness. It inspires customers, investors, regulators and lenders to feel confident in an individual, a product or an organization.

*The other standard banking code of conduct includes*- 

- Integrity
- Neutrality
- Reliability
- Transparency

**Ethical Foundation of Being a professional**

Professionals must possess knowledge of law and comply with all applicable laws and regulations of the government, even in the event of conflict. Professionals should disassociate themselves from violation of laws or rules and regulations.

Professionals must take reasonable care and judgment in maintaining their independence and objectivity in their activities. Accepting gift, benefits, compensation etc.

Professional must not engage in any conduct of dishonesty, deceit, fraud, or an action, which might affect their reputation and integrity.

**Professionalism in Banking**

The image and reputation of a bank as well as people’s confidence in a bank depends heavily on the behaviour of its employees, their ability to interact and show attention to their co-workers and clients.

**Unit 2- Ethics at the Individual Level**

**Values, Norms, Belief and their Role**

**Values**
Values refer to the important and enduring beliefs or principles, based on which an individual makes judgements in life. It is at the centre of our lives which act as a standard of behaviour. They severely affect the emotional state of mind of an individual. They can be personal values, cultural values or corporate values.

Values are forces that cause an individual to behave in a particular manner. It sets our priorities in life, i.e. what we consider in the first place. It is a reason behind the choices we make. It reflects what is more important for us. So, if we are true to our values and make our choices accordingly, then the way we live to express our core values. Moreover, if you understand an individual’s values, you can easily identify what is important for them.

**Differences Between Ethics and Values**

*The fundamental differences between ethics and value are described in the given below points:*

- Ethics refers to the guidelines for conduct, that address question about morality. Value is defined as the principles and ideals, which helps them in making the judgement of what is more important.

- Ethics is a system of moral principles. In contrast to values, which is the stimuli of our thinking.

- Values strongly influence the emotional state of mind. Therefore it acts as a motivator. On the other hand, ethics compels to follow a particular course of action.

- Ethics are consistent, whereas values are different for different persons, i.e. what is important for one person, may not be important for another person.

- Values tell us what we want to do or achieve in our life, whereas ethics helps us in deciding what is morally correct or incorrect, in the given situation.

- Ethics determines, to what extent our options are right or wrong. As opposed to values, which defines our priorities for life.

**Norms**

Norms are expectations of proper behaviour and not the requirements of that behaviour. Norms are the ways an individual expects all the people to act in a given situation. They are inconsistent but universal. Norms are not published, therefore, may not be obeyed and cannot be made obligatory except by sanctions of a group who use penalties as condemnation or exclusion.

Norms are informal guidelines about pertaining to behaviour and actions, which are considered normal (what is correct and incorrect) social behaviour in a particular group or social unit.

**Beliefs**
Beliefs in the ethical code are standards of thoughts. Beliefs are criteria of intangible thought that does not necessarily evoke action. It may stimulate or force certain pursuit in the environment that corresponds with one to behave in a certain manner.

Beliefs are among the most primitive and central of mental constructs, and yet there is little agreement as to what they are or how they should be constructed.

**Role of Norms, beliefs and values in management**

A corporate culture is a set of values, beliefs, norms and goals and ways of solving problems, which is shared by the employees of an organization.

**Core Values**

Core value are the fundamental beliefs of a person or organization. These guiding principles dictate behavior and can help people understand the different between right and wrong. Core values also help companies to determines if they are on the right path and fulfilling their objectives by creating an unwavering guide.

Every organization must have a set of core values, which are referred to as the Business or Corporate values. The below mentioned are the few of core values practiced by Fortune 500 Companies across the world:

- Customer services
- Employee care
- Quality
- Ethics
- Integrity
- Growth and stability
- Innovation
- Flexibility
- Social Responsibility

**Morality and Personal Values**

**Morality**

Morals are one’s guiding principles. Morals are those principles that have internalized automatic response to the situations. They are part of who we are our unique personality. Moral standards are first absorbed as child family friends and various social influences.
Different moral standards emerge from the different value systems which people and society hold. Moral standards include the norms we have about the kinds of actions we believe are morally right and wrong and also the values we place on the kind of objectives we believe are morally good and morally bad.

**Personal Values**

Individual values- system is like a fingerprint. It is unique in case of each individual. Because it in the form of a combination of different instrument and terminal values. And this combination varies from person to person. Therefore, in the context of an organization when different business managers come across similar ethical dilemma, their interpretation of the situation and responsive actions may differ significantly.

*Personal values serve five purposes in organizations*

- Values serve as standards of behaviour.
- Guidelines for decision-making and conflict-resolution
- Values affect our thoughts and actions.
- It influences the perception and motivation of employees.
- It also has strong influence on behaviour and attitude.

**Personal Ethics and Business Ethics: Individual Integrity and Responsibility**

**Personal Ethics**

Personal ethics is a category of philosophy that determines what an individual believes about morality and right and wrong. This is usually distinguished from business ethics or legal ethics. These branches of ethics come from outside organizations or governments, not the individual's conscience.

**Business ethics**

Business ethics refers to implementing appropriate business policies and practices with regard to arguably controversial subjects. Some issues that come up in a discussion of ethics include corporate governance, insider trading, bribery, discrimination, social responsibility, and fiduciary responsibilities.

**Conflict Between Personal ethics and Business Ethics**

The organization's ethics dilemmas are often resolved and decision taken by committees and formal and informal group and not by an individual. Moreover, the decision that are
taken are based in business goals and exclude individual goals. Ethical clashes or dilemmas may arise in several situations like:

- The individual ethics may clash with the group ethics predominant in the organization.

- The individual ethics of a single powerful person in the organization may be predominant in the organization. If that individual is ethical and works for the good of all the shareholders, it results in positive outcome but if that person is unethical, it may result in negative impact on the organization.

- In some cases, employees may be taught to ignore an issue, which he or she thinks is unethical.

**Individual Integrity and responsibility**

Integrity is explained as firm adherence to a code of values. For an individual or for a Business, Integrity is the quality or state of being complete or undivided. In other words, it means being true to our values and ourselves and also keeping our commitment not only towards others but to ourselves also. In the individual value-set, Integrity is the core value, which makes an individual complete or undivided.

Why is it important to restore integrity? - This is mainly because it gives you the ability to powerfully deal with not only specific situation but also in other areas of one’s life.

**Individual Responsibility**

Responsibility is defined as a moral, legal or mental accountability. This makes an individual a cause of doing something with a motive or an agent of some action.

An Individual’s responsibility is taking on accountability for our personal situation. Suppose of an organization declares that we are responsible for what we do and what we have, who we are and for all the conversations we have and situation we are in. Therefore, individual responsibility is the commitment one makes to himself for being an agent in the world, i.e. the cause of who we are and what we have.

**Ethical Reasoning and Real-world Application**

Ethical reasoning is the process recognizing, which decision requires ethical judgments, determining potential reasonable course of action, finding support for potential course of action, and then selecting the course of action best supported.

General purpose: Firstly, an individual is trying to determine the ethical goals or an objective that he or she is trying to achieve.
Raise questions: The key ethical question person is trying to answer, that is identification of issues he or she facing and then formulating key ethical question embedded in the issues, keeping in mind the relevant point of views.

Use information: One must identify the information, collect all the data and facts, which will enable a person to understand and consider the requirement of evidences or observations relevant to others. Individual’s own experiences also helps in developing suitable reasons.

Utilizes concepts: The key ethical concepts and principles that would assist in developing a thought process. Identification of ethical definitions, theories, models etc. that is applicable for reasoning through the issues.

Makes assumption: The main assumptions pre-suppositions used in reasoning in the ethical issue. Assumptions should also be justified for reasoning. Assumptions must also be evaluated from the perspective of understanding the ethical issues along with available alternatives.

**Ethics Dilemmas: Resolving Ethical Dilemmas**

An ethical dilemma (ethical paradox or moral dilemma) is a problem in the decision-making process between two possible options, neither of which is absolutely acceptable from an ethical perspective. Although we face many ethical and moral problems in our life, most of them come with relatively straightforward solutions.

On the other hand, ethical dilemmas are extremely complicated challenges that cannot be easily solved. Therefore, the ability to find the optimal solution for ethical dilemmas is critical to everyone.

Every person can encounter an ethical dilemma in almost every aspect of their life, including personal, social, and professional.

*An ethical dilemma exists when one is faced with having to a make choice among following alternatives:*

- Significant Value--- Conflicts among differing interests.
- Real alternatives that is equally justifiable.
- Significant consequences on stakeholders in situation.

**Resolving Dilemmas**

*Steps for dealing with ethical dilemma are as follows-*

- Acknowledge that there is a moral issue.
- Ascertain the people who will be affected by the decision. Also, determine your role.
• Gather the facts about sequence of occurrence of event. Because the more facts we know, we can better comprehend the situation.

• Ascertain your test for right versus wrong. How would you define the problem, if you were to stand on the other side of the fence.

• Ascertain the test for right versus right theory, for example trust vs loyalty, justice vs Mercy etc.

• Apply the resolution principle. Work through all three approaches to resolve the dilemma, namely.

• Thinking based on end-do whatever produces the greatest good for maximum people.

• Rule based thinking-follow the rule strictly.

• Care based thinking –treat other with love and compassion. Do to others, what you would like the do to you.

• Your approach must look reasonable and persuasive

• Investigate, if there is any third way out of the situation

• Make decision and take action

• Revisit and reflect on the decision.

A Framework for Ethical Decision-Making

Making good ethical decisions requires a trained sensitivity to ethical issues and a practiced method for exploring the ethical aspects of a decision and weighing the considerations that should impact our choice of a course of action. Having a method for ethical decision making is essential. When practiced regularly, the method becomes so familiar that we work through it automatically without consulting the specific steps. This is one reason why we can sometimes say that we have a “moral intuition” about a certain situation, even when we have not consciously thought through the issue. We are practiced at making ethical judgments, just as we can be practiced at playing the piano, and can sit and play well “without thinking.” Nevertheless, it is not always advisable to follow our immediate intuitions, especially in particularly complicated or unfamiliar situations. Here our method for ethical decision making should enable us to recognize these new and unfamiliar situations and to act accordingly.

The more novel and difficult the ethical choice we face, the more we need to rely on discussion and dialogue with others about the dilemma. Only by careful exploration of the problem, aided by the insights and different perspectives of others, can we make good ethical choices in such situations.
Ethical decision-making has involved weighing of four factors as under:

- The desired outcome of a decision.
- The means used to achieve the desired outcome,
- The motivation behind the decision; and
- The possible consequences of decision.

**Unit 3- Ethical Dimension Employees**

**Obligation to Bank: Obligations of Bank**

- Obligation to Honour Cheques
- Obligation to Maintain Secrecy
- Obligation to follow all financial instructions of customers
- Obligation to keep records in order
- Obligation to give Notice before closing the account
- Besides the Obligation towards the bank's customers, they also have got the obligation to follow all the laws, guidelines, directives and policies of the regulator-RBI

**Right of Bank**

*For fulfilling the obligations towards the customers, bankers enjoy the following rights:*

**Right of General Lien:** A general lien authorizes a bank to retain and securities till all the bank's claims against the customer are satisfied. A lien is an implied such that if a default is made by the debtor, the bank, by giving a reasonable notice to the borrower, can sell and recover the amount due to it. No other valuables, cash, etc, kept in lockers or fixed deposits etc, should be set off against the claim.

**Right to charge interest and commission:** Bank has implied right to charge interest on loans and advances and commission on services rendered to the customer.

**Closure of Account:** The Bank has the right to close a customer's account if it is inoperative for the specified duration, provided it informs in writing to the customer to respond within a stipulated time.

**Obligation to Third Parties: Fiduciary Responsibilities**

**Obligations under the KYC for regulated Entities**
As per the Master Direction issued by RBI on February 25, 2016 (which was updated as on April 20, 2018), know as the RBI (KYC) direction 2016, the following are the directives issued for the Regulated Entities (REs refer to Bank, Asset Management Companies, Investment Managers/ Advisors, Portfolio Managers etc).

For the purpose of verifying the identity of customers at the time of commencement of an account-based relationship, REs, shall at their option, rely on customer due diligence done by a third party, subject to the following conditions:

- Records or the information of the customer due diligence carried out by the third party is obtained within two days from the third party or from the Central KYC Records Registry.
- Adequate steps are taken by REs to satisfy themselves that copies of identification data and other relevant documentation relating to the customer due diligence requirements shall be made available from the third party upon request without delay.
- The third party is regulated, supervised or monitored for, and has measures in place for, compliance with customer due diligence and record-keeping requirements in line with the requirements and obligations under the PML Act.
- The third party shall not be based in a country or jurisdiction assessed as high risk.
- The ultimate responsibility for customer due diligence and undertaking enhanced due diligence measures, as applicable, will be with the RE.

REs shall frame a Customer Acceptance Policy.

- No account is opened in anonymous or fictitious/benami name.
- No account is opened where the RE is unable to apply appropriate CDD measures, either due to non-cooperation of the customer or non-reliability of the documents/information furnished by the customer.
- No transaction or account-based relationship is undertaken without following the CDD procedure.
- The mandatory information to be sought for KYC purpose while opening an account and during the periodic updation, is specified.
- ‘Optional’/additional information, is obtained with the explicit consent of the customer after the account is opened.
• REs shall apply the CDD procedure at the UCIC level. Thus, if an existing KYC compliant customer of a RE desires to open another account with the same RE, there shall be no need for a fresh CDD exercise.

• CDD Procedure is followed for all the joint account holders, while opening a joint account.

• Circumstances in which, a customer is permitted to act on behalf of another person/entity, is clearly spelt out.

• Suitable system is put in place to ensure that the identity of the customer does not match with any person or entity, whose name appears in the sanctions lists circulated by Reserve Bank of India.

For Non-Banking Financial Companies

Simplified procedure for opening accounts by Non-Banking Finance Companies (NBFCs): In case a person who desires to open an account is not able to produce documents, as specified in Section 16, NBFCs may at their discretion open accounts subject to the following conditions:

(a) The NBFC shall obtain a self-attested photograph from the customer.

(b) The designated officer of the NBFC certifies under his signature that the person opening the account has affixed his signature or thumb impression in his presence.

(c) The account shall remain operational initially for a period of twelve months, within which CDD as per Section 16 shall be carried out.

(d) Balances in all their accounts taken together shall not exceed rupees fifty thousand at any point of time.

(e) The total credit in all the accounts taken together shall not exceed rupees one lakh in a year.

(f) The customer shall be made aware that no further transactions will be permitted until the full KYC procedure is completed in case Directions (d) and (e) above are breached by him.

(h) The customer shall be notified when the balance reaches rupees forty thousand or the total credit in a year reaches rupees eighty thousand that appropriate documents for conducting the KYC must be submitted otherwise the operations in the account shall be stopped when the total balance in all the accounts taken together exceeds the limits prescribed in direction (d) and (e) above.

Employees are advised to follow Code of Conduct laid down by the Bank. Abuse of official position for personal gains or providing gains to friends, family members and other with selfish motive amounts to violation of employee’s to the Bank. Examples of abuse of power can be:

- Bank employee goes for a personal travel and claims reimbursement as official travel
- Showing discrimination to the customers based on their proximity to the employee (his relatives friends, etc, showing special preference)
- Use of official resources for personal use
- False claims beyond the fixed perquisites

**Insider Trading**

In India, SEBI (Insider Trading) Regulation, 1992 framed under the Section 11 of the SEBI Act, 1992 intends to curb and prevent the menace of insider trading in securities. An insider is a person who is an accepted member of a group or organization who has special knowledge regarding his firm.

**Proprietary Data**

Proprietary Data refers to the information relating to the intellectual property right and trade secrets of any company. All employees are expected to keep confidentially of the data relating to all stakeholders, customers, vendors, promoters, investors and other who are associated with the Bank.

**Bribes**

Bribes refers to paying money or gift to a person with a motive of getting some favour done. Bank’s Services regulations provide details of dos and don'ts with respect to bribes.

**Obligations to third Parties**

When the Bank is outsourcing its functions to the Third Parties, it needs to have clear, transparent contracts and agreements with all terms & conditions incorporated. Especially in service contracts, the service level agreement have to be defined minutely and ensure that the Third party do not cause an inconvenience to the Bank customer.

**Job Discrimination**

Job discrimination is when an employee is treated badly by a supervisor or boss for something they cannot control, like their age or race. Mistreatment can range from verbal or sexual harassment, withholding benefits, withholding opportunities for advancement, pay, or someone being fired from their job.
Sexual Harassment

Sexual harassment is a type of harassment technique with explicit or implicit sexual overtones, including the unwelcome or inappropriate promise of rewards in exchange for sexual favors. Sexual harassment includes a range of actions from verbal transgressions to sexual abuse or assault.

The Guidelines and norms prescribed included the definition of sexual harassment and details as under:

- Physical Contact
- A demand or respect for sexual favours
- Sexually coloured remarks
- Showing pornography
- Any other unwelcome physical, verbal or non-verbal conduct or sexual nature

Managing Conflict of Interests

The Dictionary meaning of conflict of interest is “a situation in which a person is in a position to derive personal benefit from actions or decisions made in their official capacity.”

Some examples for conflict of interest are:

- A given bank and its client/clients
- Among the employees of a bank
- Employee of a bank and a client
- Between a given bank and one or more of its clients
- Provision of bank’s services to two or more clients

HRM Ethics

Human Resource Management (HRM) deals with work force management, manpower planning and other employee related activities in an organization. Therefore, we can say that it is a special branch of management where ethics play a crucial role. HRM concerns human issues, especially those related with compensation, development, industrial relations, health and safety issues. However, there are sufficient disagreements in managing HRM issues that stem from various quarters.
Unit 4- Work Ethic and The Workplace

What is Work Ethos?

Work ethic is a belief that hard work and diligence have a moral benefit and an inherent ability, virtue or value to strengthen character and individual abilities. It is a set of values centered on importance of work and manifested by determination or desire to work hard. Social in-grainment of this value is considered to enhance character through hard work that is respective to an individual's field of work.

Factors of a good work ethics

- **Goal-oriented actions**: It is not about making plans or the next logical steps; it's about getting things done so that the work invested wouldn't be counter-productive.
- **Prioritized focus**: Focusing on qualitative activities that a person is responsible for and in areas where they can make a difference or a high impact based on objectives.
- **Being available and reliable**: Spending time on the work and building oneself up for the task.
- **Conscientiousness**: A desire to do a task well, being vigilant and organized.
- **Creating a rewarding routine/system**: Engaging in tasks that provide strength and energy which can be transferred to your ultimate goals, creating a habit and a habitat for success.
Embracing positivism: Shape a problem with the statement "good, (action) (problem)", e.g. "I'm tired and it is time for a workout" leads to "Good. Workout tired".

Something Bigger Than the self

There is a hierarchy in which one needs to think about the purpose of one's life

The hierarchy can be as under:

- Oneself
- Family
- Community
- Religion
- Society at large
- Global causes (Like peace, human right, environment etc)

Ethical Behaviour at The Workplace: Benefit

- Asset Protection and Assurance
- Productivity will increase
- Team Work will develop
- Public Image and Brand Value Increases
- Adaptive to changes
- Decision making and implementing is always easy
- Trouble-free working environment
- There is no one left negative
- Less Legal Issues
- The company will Touch New level of Success

Recognising Ethical WorkPlaces

The following are some of the ways and means to recognize an ethical workplace:

- Respectful treatment of all categories of customers by the front- office personnel;
- Employees’ awareness of the business process and quick and to the point clear answers to queries;
- Giving correct and authentic information to customers on matters like interest rates/premature withdrawals of term deposits, actual eligibility for insurance claim on assets like house/flat etc.
- Guiding a person on a short visit for multi-currency travel card and whether to take fixed exchange rate or to go in for real-time exchange rate;
- Strict adherence to minimal prescribed documentation as prescribed by the regulator/ internal management and not insisting for additional documents from the borrower;
• Appropriate attire befitting the profession of the employee, and it should provide comfort to all customers who need to speak to the employee;
• Acceptable body language of the employees at the workplace.
• Fair and appropriate treatment given to all co-employees. Etc, Etc

Unethical Behaviours: Causes and Remedies

Causes

The major causes for unethical behaviour at workplace are as follows:

• Non-availability of code of Ethics Manual
• Lack of fear of Action
• Unrealistic Targets
• Influence of Co-employees
• Unprincipled Leadership
• Means are not appreciated

Remedies

Many of the preventive or remedial measures have already been discussed earlier. The following can be tried some of the remedies to rectify unethical behaviour at workplace.

• Developing Ethics Manual
• Starting Conversations about ethics in the organization
• Nipping of unethical behaviour in the bud
• Frequent utilization of the Manual
• Imitable behavior by the Top Management
• Appreciation and Rewards for ethical behaviour
• Encouragement of counter viewpoints and discussions in meetings
• Care for reputation rather than results

Some of the following situations gives a comprehension about some of the unethical practices at the workplace:

• Abuse of the official email
• Pre-employment Tests
• Personal Habits
• Data Leakage
• Helping Friends in Social Decision

Ethics of a Banker

A Banker can be evaluated for the ethical commitment at three stages of his/her career-

• At the initial stages up to **first 5-7 years** of taking up banking as career,
• At the middle management stage, typically after **7-15 years into banking sector**, and
• At the senior management level, normally **after 15 years** into banking service.

The following are some of the major ethical qualities expected of a banker throughout his/her career-

• Honesty and Integrity
• Commitment to Customers
• Confidentiality
• Fair treatment
• Transparency
• Duty-Mindedness

**Whistleblowing in Banks**

In the Indian context, the Government of India had passed a resolution on **April 21, 2004 authorizing the Central Vigilance Commission (CVC)** as the ‘Designated Agency’ to receive written complaints or disclosure on any allegation of corruption or of misuse of office and recommend appropriate action. The jurisdiction of the CVC in this regard is restricted to employees of the Central Government or of any corporation established by it or under any Central Act, Government companies, societies or local authorities owned or controlled by the Central Government.

As a proactive measure for strengthening financial stability and with a view to enhancing public confidence in the robustness of the financial sector, RBI has formulated a scheme called "**Protected Disclosures Scheme for Private Sector and Foreign Banks**". The salient features of the Scheme are as under:

**Scope and Coverage**

As Public Sector Banks and Reserve Bank of India (since it is an entity established under Central Statute) have already been brought under the purview of Government of India scheme, with a view to avoid duplication, this Scheme would cover all private sector and foreign banks operating in India.

The complaints under the Scheme would cover the areas such as corruption, misuse of office, criminal offences, suspected / actual fraud, failure to comply with existing rules and regulations such as **Reserve Bank of India Act, 1934, Banking Regulation Act 1949, etc.** and acts resulting in financial loss / operational risk, loss of reputation, etc. detrimental to depositors' interest / public interest.

• Under the Scheme, employees of the bank concerned (private sector and foreign banks operating in India), customers, stake holders, NGOs and members of public can lodge complaints.
• Anonymous / pseudonymous complaints will not be covered under the Scheme and such complaints will not be entertained.
• Reserve Bank of India (RBI) will be the Nodal Agency to receive complaints under the Scheme. RBI would keep the identity of the complainant secret, except in cases where complaint turns out to be vexatious or frivolous and action has to be initiated against the complainant as mentioned in the below point.
• The institution against which complaint has been made can take action against complainants in cases where motivated / vexatious complaints are made under the Scheme, after being advised by RBI. An opportunity of hearing will, however, be given by the concerned bank to the complainant before taking such action.
• Final action taken by RBI on the complaint will be intimated to the complainant.

**Unit 5- Banking Ethics: Changing Dynamic**

**Ethics and Technology**

**Role of Information Technology in Banking**

The banking industry is going through a period of rapid change to meet competition, challenges of technology and the demand of end user. Clearly technology is a key differentiator in the performance of banks. Banks need to look at innovation not just for product but for process also.

Today, technology is not only changing the environment but also the relationship with customers. Technology has not broken barriers but has also brought about superior products and channels. This has brought customer relationship into greater focus. It is also viewed as an instrument of cost reduction and effective communication with people and institutions associated with the banking business. The RBI has assigned priority to the upgradation of technological infrastructure in financial system. Technology has opened new products and services, new market and efficient delivery channels for banking industry. IT also provides the framework for banking industry to meet challenges in the present competitive environment. IT enables to cut the cost of global fund transfer.

**Important events in evolution of Information Technology:-**

- Introduction of MICR based cheque processing
- Arrival of card based payments
- Introduction of Electronic Clearing Services
- Introduction of RTGS/NEFT
- Introduction of Cheque Truncation System (CTS) or Image-based Clearing System (ICS)
- Introduction of Core Banking Solutions (CBS)
• Introduction of Automated Teller Machine (ATMs)
• Introduction of Phone and Tele Banking
• Introduction of Internet and Mobile Banking

Background

Committees headed by Dr. C. Rangarajan, RBI’s Committee on Mechanisation in the Banking Industry (1984) and RBI’s Committee on computerisation in Bank (1988) laid the foundation for larger-scale introduction of IT in India’s Banking Sector. Further, The Reserve Bank of India Constituted a committee called ‘Committee on Technology Issues relating to the Payments system, cheque Clearing and Securities Settlement in the Banking Industry (1994) under the Chairmanship of Shri W S Saraf. This Committee made a number of recommendations that covered payment systems including Establishment of an Electronic Fund Transfer (EFT) system, introduction of Electronic Clearing Service Credit for low value repetitive transactions such as interest, dividend, salary, pension payment and an Electronic Debit Clearing for payments to utility companies. Large scale induction of computers and communication technology in service branches, etc, were also part of the recommendations.

Role of Ethics in Technology

Using theories and methods from multiple domains, technoethics provides insights on ethical aspects of technological systems and practices, examines technology-related social policies and interventions, and provides guidelines for how to ethically use new advancements in technology. Technoethics provides a systems theory and methodology to guide a variety of separate areas of inquiry into human-technological activity and ethics. Moreover, the field unites both technocentric and bio-centric philosophies, providing "conceptual grounding to clarify the role of technology to those affected by it and to help guide ethical problem solving and decision making in areas of activity that rely on technology." As a bio-techno-centric field, technoethics "has a relational orientation to both technology and human activity"; it provides "a system of ethical reference that justifies that profound dimension of technology as a central element in the attainment of a 'finalized' perfection of man.'

Ethics address the issues of what is ‘right’, what is ‘just’, and what is ‘fair’. Ethics describe moral principles influencing conduct; accordingly, the study of ethics focuses on the actions and values of people in society (what people do and how they believe they should act in the world).

Technology is the branch of knowledge that deals with the creation and use of technical means and their interrelation with life, society, and the environment; it may draw upon a variety of fields, including industrial arts, engineering, applied science, and pure science. Technology "is core to human development and a key focus for understanding human life, society and human consciousness."
Data Security and Privacy

With the increased intervention of technology in the banking sector globally, the need for sophisticated laws to protect customer information has gained significant attention. While several countries have enacted comprehensive legislations to protect customer's sensitive information, some countries are still in the process of introducing legislations to keep up with the changing pace of technology. In India, banks are regulated by the Reserve Bank of India (RBI) and the RBI through various notifications, circulars, directions and guidelines from time to time, obligates banks to maintain customer confidentiality and protect the privacy of customers' data.

The government of India also introduced the Information Technology (Reasonable Security Practices and Procedures and Sensitive Personal Data or Information) Rules, 2011 with an aim of creating a robust legislation, which would protect customer's sensitive personal data by only allowing banks to release data when the customer has explicitly consented to such disclosure. The Rules also permit banks to only collect sensitive personal information for lawful purposes connected with the function or activity of banks and when the collection of the information is necessary for such purpose.

CREDIT INFORMATION

However, while providing the necessary protection to customers there is also a need to ensure that banks are not victimized for no fault of theirs by not being able to recover their debts from defaulting customers. To meet this end, the Credit Information Companies Act, 2005 (CIC Act) was introduced in India in 2005. Credit Information Companies (CICs) are independent third party organizations that provide credit information to banks and financial institutions and assess credit worthiness of individuals based on their past repayment and default records. Banks can, through such information, determine whether they should provide credit facilities to the client. A CIC is required to furnish information to its members and has to maintain principles of privacy enumerated under Section 20 of the CIC Act.

INFORMATION UTILITIES

Recently, with the introduction of the Insolvency and Bankruptcy Code, 2016 (the Code), a new concept of the Information Utilities (IU) was brought into the picture and subsequently notified with effect from 1 April 2017. An IUs under the Code is an infrastructure facility which, like the CIC, is to create a financial information database of all entities availing credit in the country with the aim to enable better decision making by creditors and to ensure discipline among debtors. To ensure data privacy, IUs are required to store all the information received in a facility located in India and should have high quality data storage systems to avoid loss/ corruption of data. The information stored with an IU can only be accessed by certain specific categories of persons, which includes inter
alía any user who submitted the information, National Company Law Tribunal, insolvency professionals and the Insolvency and Bankruptcy Board of India.

**Intellectual Property Right and Patents**

**Intellectual Property** refers to creation of an asset by any individual or anyone using his or her creativity, innovation. Such intellectual property (IP) belongs to that individual and any unauthorised use of such IP is strictly under the applicable law of land. Some example of IP is artistic works; and symbols, innovative process, method etc.

**Intellectual property included into two categories:**

- Intellectual Property includes patents for inventions, trademarks, industrial designs and geographical indications.
- Copyright covers literary works (such as novels, poems and plays), films, music, artistic works (drawing, paintings etc) and architectural design.

**What is Patent?**

A patent is a form of intellectual property that gives its owner the legal right to exclude others from making, using, selling and importing an invention for a limited period of years (Generally 20 years), in exchange for publishing an enabling public disclosure of the invention.

**Ethics of Information Security**

As technology is taking over most of the Banking activities; threats associated with the use of technology also need to be tackled. The IT team of the bank or financial institution in a way becomes the custodian of the information of its customers/dealings/activities.

**The following aspects relating to information security may be worth following by the employees:**

- Making the employee (IT and non-IT) be aware of their professional obligations relating to the information security of the bank, customers and other stakeholders.
- Notifying from time to time the existing laws and crimes as and when the cyber laws get amended in the country or internationally (for off-shore transaction).
- Making the bank employees (especially the IT employees) aware of the patterns of IT attacks on bank customers/servers/other assets like ATMs, etc. and to familiarize the profiles of attackers and patterns of the thefts, modus operandi, if any.

**Cyber Threats**

**Need for cyber Security Awareness**
Despite the Indian Banking system having completed its process of computerization and online-ready transactions, a significant proportion of the customers of banks are still not adequately well-versed with the importance of cyber security. Banks are making their sincere efforts to educate and bring in awareness among their customers on the importance of memorizing their passwords. Firstly, setting the password itself is not taken seriously by many customers.

There are four characteristics advised by typical IT personnel of banks while setting a password. The passwords are ideally to be:

- Personal
- Unique
- Secret
- Complex

Cyber Security Framework in Bank

Reserve Bank of India, thought its Notification dated June 2, 2016, advised all commercial banks in India’s to have in place a cyber- security policy with the the approval of their Boards. RBI gave about 4 months timeframe to the commercial banks to set up such cyber security policy and give a compliance conformation to the RBI. RBI notification directed the commercial Banks further on this aspect us under:

“In order to address the need for the entire bank to contribution to a cyber-safe environment, the Cyber Security Policy should be distinct and separate from the broader IT policy/ IS security policy so that it can highlight the risk from cyber threats and the measures to address/mitigate these risks.

Banks need to promote the following enabling programs

- Take preventive steps
- Provide guidelines steps
- Engage state- of- the art IT security protection systems
- Build confidence in staff and customers

Digital rights management (DRM)

Digital rights management (DRM) is a systematic approach to copyright protection for digital media. The purpose of DRM is to prevent unauthorized redistribution of digital media and restrict the ways consumers can copy content they’ve purchased. DRM products were developed in response to the rapid increase in online piracy of commercially marketed material, which proliferated through the widespread use of peer-to-peer file exchange programs. Typically DRM is implemented by embedding code that prevents copying, specifies a time period in which the content can be accessed or limits the number of devices the media can be installed on.
Although digital content is protected by copyright laws, policing the Web and catching law-breakers is very difficult. DRM technology focuses on making it impossible to steal content in the first place, a more efficient approach to the problem than the hit-and-miss strategies aimed at apprehending online poachers after the fact.

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