

REGULATION OF BANKING BUSINESS

- The Banking Regulation Act empowers the Reserve Bank to issue directions for regulating terms and conditions of making of loans and advances and other matters including acceptance of deposits.
- It also imposes certain restrictions on loans and advances to the directors of banking companies, and companies and firms in which they are interested.
- The Act contains provisions for the creation of a reserve fund and the transfer of a percentage of profits to that fund.
- There are also provisions for maintenance of cash reserve, liquid assets, and assets in India

POWER TO ISSUE DIRECTIONS

Banking Regulation: The Act authorizes the Reserve Bank to issue directions to banks under Sections 21 and 35A of the Act.

Section 21 gives the power to regulate advances by banking companies,

Section 35A gives wide powers generally to RBI to issue directions in the public interest or in the interest of banking policy.

Nature of Directions: The directions issued by the Reserve Bank in the exercise of powers under Sections 21 and 35A of the BR Act, being statutory directions, are binding on the banks.

Bonafide: The powers of the Reserve Bank to issue directions have to be exercised with bonafide intentions.

Caution and Advice: Apart from giving directions, the Reserve Bank may also caution or give advice to banking companies. Section 36 of the BR Act provides that the RBI may caution or prohibit or advise banking

companies generally or any banking company in particular against any transaction or class of transactions.

ACCEPTANCE OF DEPOSITS

- Banks accept different types of deposits, both time and demand deposits, from the public subject to the terms and conditions of the deposits.
- The period of the deposit and rate of interest applicable to the deposit are matters to be agreed between the depositor and the bank under the terms of the deposit, subject to any directions given by the Reserve Bank in this regard.

Returns on Unclaimed Deposits: Banks have to file a return every year on their unclaimed deposits under Section 26 of the BR Act.

- The return has to be filed within 30 days of the end of each calendar year in the form and manner prescribed and should cover all deposits not operated for 10 years.
- In the case of fixed deposits, the period of ten years starts from the expiry of the period of the deposit.
- Setting up of a Depositor Education and Awareness Fund (DEAF) to take over inoperative deposit account(s) which have not been claimed or operated for a period of 10 years or more, within a period of 3 months from the expiry of the said period of ten years.

LOANS AND ADVANCES

The Reserve Bank is empowered u/s _____ of the BR Act to issue directions to control advances by banking companies.



The Reserve Bank may determine the policy in relation to advances and issue directions when it is satisfied that it is necessary to give directions:

- In the public interest
- In the interests of depositors
- In the interests of banking policy

Selective Credit Control

Purpose: To ensure that prices of essential commodities like sugar, jaggery, etc are not increased with a motive of profit maximization by hoarding with the help of bank finance, these restrictions have been put in place.

- These cover the quantum of credit that can be extended and also the rate at which it can be extended.

Methods and tools

- By making the borrowing more costly for certain purposes
- by imposing stringent conditions on lending
- By giving concessions for certain desired types of activities.

Tools employed

- minimum margins for lending against selected commodities;
- ceilings on the levels of credit; and
- Charging of minimum rate of interest on advances against specified communities

Restrictions on loans and advances (Section 20 of BR Act)

- **Advances against Banks own shares:** No banking company shall grant loans or advances on the security of its own shares.

Loan To Directors of Other Banks

- **Loan up to Rs. 500 lacs:** The bank can sanction loans to directors or their relatives, up to Rs. 500 lacs but the same has to be reported to the Board.
- **Above Rs. 500 lacs:** Loans to Directors / their relatives can be given with the consent of the Board.

Regulation Of Interest Rates

- (Sec 21 & Sec 35A) While giving directions on interest rates, there should not be any discrimination against any class of depositors or loanees, or banks.
- Any differential treatment should be justifiable in law as not being against the principles of equality.

Applicability of Benchmark Rate

- All categories of loans should be priced only with reference to the benchmark Rate except, (a) DRI advances (b) loans to banks' own employees (c) loans to banks' depositors against their own deposits.
- Banks are not permitted to resort to any lending below this Rate.

Rate of Interest Scrutiny by Court SEC 21(A)

- **Rate of interest charged by banks not to be subject to scrutiny by courts:** A transaction between the banking company and its debtor

shall not be reopened by any court on the ground of excessive charging of rate of interest.

INTERNET BANKING GUIDELINES

The Reserve Bank has issued guidelines in respect of internet banking. These guidelines cover:

- technology and security issues;
- legal issues;
- Regulatory and supervisory issues.

RESERVE FUNDS

- **Creation of Reserve Fund:** Every banking company incorporated in India has to create a reserve fund under Section 17(1) of the BR Act out of the profits as shown in the profits and loss account prepared under Section 29 of the Act.
- Every year, a sum equivalent to not less than 25% of such profits has to be transferred to the reserve fund, such transfer of profits to reserve fund has to be made before any dividend is declared.
- **Foreign Banks:** Section 11(2) of BR Act requires them to deposit and keep deposited with the Reserve Bank an amount calculated at 20% of the profit for each year in respect of all the business transacted through their branches in India.
- The amount may be deposited in cash or unencumbered approved securities or partly in cash and partly in unencumbered approved securities.
- It provides for exemption by the Central Government on the recommendation of the Reserve Bank, where the deposits already

made are considered adequate in relation to the deposit liabilities of the banking company.

CASH RESERVE by Non-Scheduled Banks

(Section 18 of BR Act)

- Banking companies, which are not, scheduled banks the cash reserve is to be maintained either by itself or by way of a current account with RBI of NDTL (Net Demand and time liabilities) in India as on last Friday of the second preceding fortnight.

Cash Reserve Ratio

- CRR refers to the cash reserve that is to be maintained with the RBI of a percentage of NDTL u/s 42(1) of the RBI Act so as to ensure liquidity and solvency of the banks.

Penalties: When the balance maintained by any scheduled bank falls below the stipulated minimum, such a bank shall be liable to pay penal interest to the Reserve Bank.

- During the first fortnight, when such shortage occurs, the penal interest shall be 3% above the bank rate and
- if the shortage continues in the next fortnight, the penal interest shall increase to 5% above the bank rate.
- Where the shortfall persists in the third fortnight, every director, secretary of the bank who is a wilful party thereto shall be punishable with a fine.

Statutory Liquidity Ratio (SLR) [Section 24 of BR Act]

- Every bank must have a particular portion of their Net Demand and Time Liabilities (NDTL) in the form of cash, gold, or other liquid assets by the end of the day.
- The ratio of these liquid assets to the demand and time liabilities is called the Statutory Liquidity Ratio (SLR).
- The Reserve Bank of India (RBI) has the authority to increase this ratio by up to 40%.
- RBI is also responsible for regulating the flow of money and the stability of prices to run the Indian economy. Statutory Liquidity Ratio is one of its many monetary policies for the same.

Components of Statutory Liquidity Ratio

- Cash in hand
- Gold owned by bank
- Balance with RBI in excess of the one u/s 42 of RBI Act
- Investment in unencumbered approved securities

ASSETS IN INDIA

- ***Quarterly position of assets:*** Every banking company has to maintain in India a certain amount of assets as required under Section 25 of the Banking Regulation Act.
- Accordingly, at the close of business on the last Friday of every quarter, such assets shall not be less than 75% of the demand and time liabilities of the banking company in India.

- **NOMINATION FACILITY**

Sections	Deals with nomination in
Section 45Z A	Deposit Accounts
Section 45Z C	Safe Custody of articles accounts
Section 45Z E	Lockers

- ***Nomination can only be made in the name of natural persons*** that is an individual including a minor or insolvent person or NRI and cannot be made in the name of firm, company, etc.
- ***In joint accounts*** should be made by all jointly.
- ***In a minor guardian-operated account*** it can be made by the guardian and in the case of a minor self-operated account, nomination is not allowed.
 - Nomination can be **made, cancelled, or altered anytime** during which the deposit account is maintained.
 - Nominee is having the ***status of trustee*** for legal heirs in receiving the money or articles and is not the owner.
 - ***Variation or cancellation of nomination all jointly operated accounts*** including either or survivor, former or survivor, will be valid only if signed by all the depositors together.
- ***On the change of title of the account*** (due to addition or deletion) the nomination is cancelled automatically.

- **Safety lockers:** for single name and joint (e/s or f/s) one nominee is allowed. But for jointly operated lockers the maximum number of nominees can be two.

NOMINATION FORMS

Type	Registration	Cancellation	Variation
Deposit	DA -1	DA – 2	DA - 3
Safe Custody	SC - 1	SC – 2	SC - 3
Locker	SL- 1 or SL 1A Joint	SL - 2	SL- 3 or SL 3A Joint

Q1. Liquid assets like cash in hand, bank balance, and investment in gold only covered u/s 24 of the Banking Regulation Act. (true/false)

ANS: FALSE

Q2. Nomination in deposit vault (locker) accounts Section 45ZA of Banking Regulation Act deals. (true/false)

ANS: FALSE

Q3: U/s 26 of Banking Regulation Act, the banks are required to file a return with RBI relating to _____?

ANS: UNCLAIMED DEPOSITS



Q4. Banking companies that are not scheduled banks maintains cash reserve ratio u/s 18 of Banking Regulation Act (true/false)

ANS: True

Q5. The directions issued by the Reserve Bank in the exercise of powers under Sections 21 and 35A of the BR Act, being statutory directions, depends on the discretion of banks to follow. (true/false)

ANS: False

Q6. Regulation of credit to different sections of the economy is known as _____.

ANS: Selective Credit Control

Q7: Under section 11 of banking regulation Act, the foreign banks have to deposit _____ of their profit for each year arising out of their business in India with RBI:

ANS: 20% Of Their Profit For Each Year

Q8. Section 17(1) of the BR Act fulfil its provision out of the profits as shown in the profits and loss account prepared under Section_____.

ANS: Of The Act

Q9. Banks are required to maintain assets not less than 75% of the paid-up capital. (true/false)

ANS: False, Demand And Time Liabilities Of The Banking Company In India.

Q10. Any differential treatment should be justifiable in law in case of interest. (true/false)

ANS: True, As Not Being Against The Principles Of Equality.

Q11. Only scheduled banks have a duty to maintain cash reserve under Section 42 of the Reserve Bank of India Act. (true/false)

ANS: True

Q12. Directions issued by RBI must satisfied that these directions are issued in the public interest, in the interests of lender, in the interests of banking policy. (true/false)

ANS: False, in the interests of depositor



**LEARNING
SESSIONS**

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