CHAPTER VIII

COST BASED INFORMATION SYSTEM USED IN SERVICE SECTOR (BANKING) FOR DECISION MAKING

Case study
Ichalkaranji Janata Sahakari Bank Ltd., branch Shahupuri, Kolhapur
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This chapter shows the detail case study of Ichalkaranji Janata Sah. Bank Ltd., Shahupuri, Kolhapur in the service sector. In this chapter, the introduction about the unit, reports prepared at present, details of staff and their duties, Cost Based Information System suggested for the unit etc. are given with different statements. Moreover the measures are suggested to improve the branch profitability.

9.1 INTRODUCTION ABOUT UNIT:

This is a well managed and profit making branch of the bank. The branch is established in 1985. During last 10 years the branch has progressed very well. There is a remarkable growth in the deposits and advances business of the branch.
8.2 Information System followed by the unit:

At present there is no Cost Based Information System in the bank. The regular information is reported to Head Office for further submission to Reserve Bank of India as per the general banking procedure. Similarly there is no system for evaluation of branch performance at Head Office level. Only the progress of the branch is observed by Head Office based on the volume of business, recovery of loans, growth of deposits etc. The Head Office gives target of loans and deposits to each branch. Computerisation is not available in the branch.

The Information Reporting system at present include following types of reports:

i. Daily trial balance
ii. Daily balance sheet
iii. Daily cash reserve liquidity report
iv. Monthly P & L account (Last Friday).
v. Monthly Balance Sheet (Last Friday).
vi. Monthly deposits, loans statement.
vii. Monthly director’s deposits, loans statement.
ix. Monthly undrawn position statement.
x. Monthly secured cash credit statement.
xi. Monthly staff loan statement.

xii. Monthly mortgage loan statement

xiii. Monthly overdues summary statement

xiv. Monthly loans and advances statement

xv. Monthly lead bank scheme return - LBS - 2

xvi. Monthly Lead bank department return

xvii. Monthly priority sector/weaker section advances position

xviii. Monthly overdues details.

8.3 Details of Staff and volume of business in the unit:

There is a total staff strength of 26 persons as below in shahupuri branch, which is selected for the purpose of research study:

Manager - 1
Officers - 4
Clerks - 15
Peons - 4
Watchmen - 2

<p>| |</p>
<table>
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</thead>
<tbody>
<tr>
<td>Total : 26</td>
</tr>
</tbody>
</table>

The allotment of work to the staff is as below:

1. Manager : General overall supervision, administration,
customers/visitors entertaining, safe deposit lockers, Inter branch and inter bank communications, liaison with H.O., deposit mobilisation, inspection visits etc.

ii. Officers:

Officer - 1: Advances section and other pending important work.

Officer - 1: Acting/Incharge manager, overall branch management, important matters.

Officers - 2: Passing Officers - voucher authorisation for all counter work.

iii. Clerks:

Clerks - 3: Cash Credit accounts.

Clerks - 2: Current accounts.

Clerks - 2: Savings, and Pygmy accounts.

Clerk - 1: Term Deposit, Recurring Deposits.

Clerk - 1: Advances.

Clerk - 1: Bills Collection, issue etc.

Clerk - 1: Typing and clearing work.

Clerks - 2: Cashiers.

Clerk - 1: DD, TT, MT, RR, work.

Clerk - 1: Statistical information, Returns.

The business volume of the branch is as under:

<table>
<thead>
<tr>
<th>Deposits type</th>
<th>Balance as on 31/03/94 (Rs. in Lacs)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Term Deposits</td>
<td>326</td>
</tr>
<tr>
<td>Current Accounts</td>
<td>63</td>
</tr>
<tr>
<td>Savings accounts</td>
<td>85</td>
</tr>
<tr>
<td>Call Deposits</td>
<td>149</td>
</tr>
<tr>
<td>---------------------</td>
<td>--------------------------------------</td>
</tr>
<tr>
<td></td>
<td><strong>683</strong></td>
</tr>
</tbody>
</table>

There are in all more than 5000 accounts in Deposits section and more than 300 accounts in Advances section.

<table>
<thead>
<tr>
<th>Deposits</th>
<th>Advances</th>
</tr>
</thead>
<tbody>
<tr>
<td>Term Deposits</td>
<td>1707. Short term loans 268</td>
</tr>
<tr>
<td>Current accounts</td>
<td>718 Medium term loans 45</td>
</tr>
<tr>
<td>Savings accounts</td>
<td>2362 Long term loans 25</td>
</tr>
<tr>
<td>Recurring accounts</td>
<td>137</td>
</tr>
<tr>
<td>Pygmy accounts</td>
<td>100</td>
</tr>
<tr>
<td>Other deposits</td>
<td>79</td>
</tr>
</tbody>
</table>
The other business volume is roughly as under:

- Local chq./DD clearing- out going: Avg. 220 to 280 per day.
- Local chq./DD clearing- incoming: Avg. 130 to 160 per day.
- Loan proposals (new): 8 to 12 per month.
- New Account openings:
  - Current A/cs: 5 to 10
  - S.B. Accounts: 20 to 25

Total number of vouchers are average 800 to 1000 per day which are bifurcated as below:

<table>
<thead>
<tr>
<th>Category</th>
<th>Count</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash credit</td>
<td>350</td>
</tr>
<tr>
<td>Current Accounts</td>
<td>250</td>
</tr>
<tr>
<td>Savings accounts</td>
<td>100</td>
</tr>
<tr>
<td>D.D., T.T. etc</td>
<td>100</td>
</tr>
<tr>
<td>Other</td>
<td>about 100 to 200</td>
</tr>
</tbody>
</table>

Staff position:

It is observed that the branch is having shortage of staff as compared to the volume of business. In case of leave of staff, the other person has to handle extra counter in addition to his own.

8.4 Cost Based Information System suggested for the unit:
It is observed that at present there is no system for branch performance evaluation. As such it is decided to suggest Cost Based Information System for performance evaluation in the branch.

The said system has five parts as below:

i. Staff time Allocation - Table 8 - A

ii. Salaries Allocation - Table 8 - B

iii. Expenses Allocation - Table 8 - C

iv. Income Allocation - Table 8 - D

v. Performance evaluation - Table 8 - E
i. Time Allocation Statement (Table 8-A)

Since the bank is a service unit, the time spent by different staff in the bank itself is a raw material for it. This aspect is considered in the first part. The staff working in the branch are considered individually as shown in the statement.

The time available per day is taken as 6.5 hours i.e. 390 minutes.

On the basis of the time spent by individuals for different work, the allocation of time has been made for different types of services. The basis considered in the statement are based on the data gathered through the discussion with the branch manager.

It is noted that the manager spends most of the time for general administration, customers/visitors entertainment, telephonic communication etc. Part of the time he uses for deposit mobilisation and advances documentation work. As per the observations the average time allocation is determined as below:
### Time spent by each person per day

<table>
<thead>
<tr>
<th></th>
<th>(Minutes)</th>
<th>(%)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Manager 1</strong> - Deposits mobilisation</td>
<td>58</td>
<td>15%</td>
</tr>
<tr>
<td>- Loans - documentation,</td>
<td></td>
<td></td>
</tr>
<tr>
<td>execution, visits</td>
<td>117</td>
<td>30%</td>
</tr>
<tr>
<td>- General Administration</td>
<td></td>
<td></td>
</tr>
<tr>
<td>supervision customer, visitors</td>
<td></td>
<td></td>
</tr>
<tr>
<td>entertaining etc. (common services)</td>
<td>215</td>
<td>55%</td>
</tr>
<tr>
<td></td>
<td>390</td>
<td>100%</td>
</tr>
</tbody>
</table>

Similarly, the work of all other staff including officers is observed. The person who are handling a single section are considered to be spending 100% time for that particular section. On the above basis, the time allocation is done as below:

<table>
<thead>
<tr>
<th></th>
<th>(Minutes)</th>
<th>(%)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Officer 1 - Loans section</strong></td>
<td>390</td>
<td>100%</td>
</tr>
</tbody>
</table>

**Officer 2 - Passing work for all sections** 390 --- 100%
As shown above the time spent per day is calculated which is further converted to time spent per month for each activity. For this purpose the month is presumed to be consists of 81 full days and 4 half days.
ii. Salaries Allocation Statement i (Table B-B)

On the basis of the time allocation statement the total salary per month of each employee has been allocated to respective services. For the purpose of simplicity the salaries are taken as below:

Manager Rs. 10,000/-
Officers - 2 Rs. 8,000/- each.
Officers - 2 Rs. 7,500/- each.
Clerks - 2 Rs. 6,000/- each.
Clerks - 3 Rs. 5,000/- each.
Clerks - 3 Rs. 4,500/- each.
Clerks - 7 Rs. 4,000/- each.
Peons - 4 Rs. 3,000/- each.
Watchmen - 2 Rs. 3,000/- each.

After allocating salary as above, a standard proportion has been arrived at below:

Current Accounts 11 %
Savings Accounts 9 % Deposit section 26 %
Term Deposits 6 %
Cash Credit 13 %
Loans 12 % Loans section 25 %
The above proportions have been rearranged in order of types of services as below:

a) Deposits section - Call Deposits - 1 %
   Current A/cs - 10 %
   Savings A/cs - 9 %
   Term Deposits - 5 %

   Bank Deposits - 1 %

b) Loans section - Short Term - 12 %
   Medium Term - 8 %
   Long Term - 4 %

   Bank Loans - 1 %

-----
26 %
c) DD/RR/TT
- DDs issued - 0.75 %
- DDs paid - 0.75 %
- MT/TT issued - 0.75 %
- MT/TT paid - 0.75 %
----- 3 %

d) Clearing
- Cheque/DD Out. - 1.5 %
- Cheque/DD In. - 1.5 %
----- 3 %
e) Bills section
- IBC - 1.5 %
- OBC - 1.5 %
----- 3 %
f) Common Services
- Common services - 31 %
- cash section - 6 %
- Returns - 3 %
---- 40%

As per the above calculations the final salary allocation and percentages is obtained as below:

<table>
<thead>
<tr>
<th>Category</th>
<th>Allocation</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Common services</td>
<td>Rs.39,000</td>
<td>31 %</td>
</tr>
<tr>
<td>Cash Credit</td>
<td>Rs.17,000</td>
<td>13 %</td>
</tr>
<tr>
<td>Current deposits</td>
<td>Rs.13,750</td>
<td>11 %</td>
</tr>
<tr>
<td>Savings, Pygmy etc.</td>
<td>Rs.10,875</td>
<td>9 %</td>
</tr>
<tr>
<td>Term deposits</td>
<td>Rs. 7,875</td>
<td>6 %</td>
</tr>
<tr>
<td>Loans</td>
<td>Rs.15,000</td>
<td>12 %</td>
</tr>
<tr>
<td>Section</td>
<td>Amount</td>
<td>Percentage</td>
</tr>
<tr>
<td>-------------------------------</td>
<td>---------</td>
<td>------------</td>
</tr>
<tr>
<td>Bills section</td>
<td>Rs. 4,000</td>
<td>3%</td>
</tr>
<tr>
<td>Clearing</td>
<td>Rs. 4,000</td>
<td>3%</td>
</tr>
<tr>
<td>Cash section</td>
<td>Rs. 8,000</td>
<td>6%</td>
</tr>
<tr>
<td>D.D./T.T.</td>
<td>Rs. 4,000</td>
<td>3%</td>
</tr>
<tr>
<td>Returns &amp; Statistics</td>
<td>Rs. 4,000</td>
<td>3%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>Rs.1,27,500</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

This statement is considered only to determine the percentage basis for salaries allocation.
iii. Expenses Allocation System (Table B-C)

The expenses of the branch are allocated on the basis of the proportions determined in the Salaries Allocation statement.

- Interest paid — Direct basis as (a) above,
- Salaries & benefits — at the percentages as per salaries allocation statement,
- Other expenses — Salaries basis.

The actual figures are modified to some extent in order to maintain confidentiality.

Alternatively the expenses can be allocated on some different basis also, such as number of vouchers, business volume etc. Moreover there can be different basis for different types of expenses also, depending upon the nature of such expenses.

E.g. the premises related expenses can be apportioned on the basis of number of staff in respective sections.
iv. Income Allocation System (Table B-D)

The incomes of the branch are allocated as below:

- Interest received - Direct basis as per (b) above,
- Comm. brokerage recd. - As per (c), (d), (e) above,
- Other income - fully allocated to common services.
### Expenses/Income Allocation Sheet

#### PERFORMANCE

<table>
<thead>
<tr>
<th>Basis for Allocation</th>
<th>0.75</th>
<th>0.75</th>
<th>0.75</th>
<th>0.75</th>
<th>3</th>
<th>1.5</th>
<th>1.5</th>
<th>1.5</th>
<th>1.5</th>
<th>40</th>
<th>46</th>
<th>100</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Expenses</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>39400</td>
<td>11980</td>
<td>535900</td>
<td></td>
</tr>
<tr>
<td>Net Incomes</td>
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<td></td>
<td></td>
<td></td>
<td>6620</td>
<td></td>
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<td>796500</td>
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<tr>
<td>Transfer of other incomes to loans &amp; deposits (40/60 basis)</td>
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<td>-39400</td>
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<tr>
<td>Trf.of common services cost to loans &amp; deposits (40/60 basis)</td>
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<td></td>
<td></td>
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<td></td>
<td>522788</td>
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<tr>
<td>Net expenses after adj.</td>
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<td>522788</td>
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<td>Net incomes after adj.</td>
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<td>722788</td>
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<tr>
<td>Business (Rupees)</td>
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<tr>
<td>Effective rate per month</td>
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<td>Effective rate per year</td>
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<tr>
<td>(Prime Rates considered for above)</td>
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</tbody>
</table>

#### Table 8-E
# Expenses/Income Allocation Sheet

<table>
<thead>
<tr>
<th>BASIS FOR ALLOCATION</th>
<th>SALARIES</th>
<th>1</th>
<th>10</th>
<th>9</th>
<th>5</th>
<th>1</th>
<th>26</th>
<th>12</th>
<th>8</th>
<th>4</th>
<th>1</th>
<th>25</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Expenses</td>
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<td>Net Incomes</td>
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<tr>
<td>Transfer of other incomes to loans &amp; Deposits (40/60 basis)</td>
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<tr>
<td>Trf. of common services cost to loans &amp; Deposits (40/60 basis)</td>
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<td>Net expenses after adj.</td>
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<td>Net incomes after adj.</td>
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<tr>
<td>Business (Rupees)</td>
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<tr>
<td>Effective rate per month</td>
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<td>Effective rate per year</td>
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</tr>
<tr>
<td>(Prime Rates considered for above)</td>
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</tr>
</tbody>
</table>

**Branch** Shahupuri, Kolhapur
Notes:

1. The expenses/incomes are to be allocated on direct basis as far as possible.

2. The common expense/incomes can be allocated either on:
   No. of vouchers basis, or
   Supervisory time/salaries basis, or
   Business volume basis.

3. In view of the confidentiality of the actual data,
   the above statement is prepared on the basis of hypothetical figures.
After getting allocation of incomes and expenses in the earlier statements as above, the other incomes and common services costs are reallocated to deposits and loan sections in respective proportions on a general 40:60 basis. Thus finally we get net expenses and net income allocation for the deposits section and loan section with details for each type of deposit and loan.

The overall business of the branch is considered with hypothetical figures for each type of deposits and loans in order to maintain the confidentiality and simplicity. Finally the effective rates of interest (on deposit as well advances) are arrived at according to business volume.

Thus the actual or prime rates are found to be changed to effective rates as below:

<table>
<thead>
<tr>
<th>Prime/Actual rate of interest</th>
<th>Effective rates</th>
</tr>
</thead>
<tbody>
<tr>
<td>Call Deposits 13 %</td>
<td>13.11 %</td>
</tr>
<tr>
<td>Current A/cs --</td>
<td>1.08 %</td>
</tr>
<tr>
<td>Savings A/cs 6 %</td>
<td>6.41 %</td>
</tr>
</tbody>
</table>
From the above system it is observed that the effective rates of interest on deposits are in fact more than the actual rates of interest paid and the effective rates of interest on loans are in fact less than the actual rates of interest received. Apart from this the other conventional profitability based norms for measurement of performance, several productivity and efficiency norms can also be used for evaluating performance. They are:

* Deposits per employee
* Profit per employee
* Ratio of non-performing assets to total assets.
8.5 Importance of Cost Based Information System:

The effective rates as per above system can be used as performance indicators for the branch and further those can be compared with other branches to evaluate them at head office level.

Such a Cost Based Information System can be applied to the branches of the bank with some modification as per the needs of the individual branches. Similarly such a system can be extended to determine cost of each service rendered by the branch such as, D.D. issued, MT/TT issued, clearing of cheques/ DD etc.. It can be noted in this context that the State Bank of India has given the assignment to The Institute of Cost & Works Accountants of India, Calcutta to carry out a study of service charges in the bank and to suggest an uniform service charges pattern for all banks on national level. Presently different banks are following different patterns of service charges. The bank should charge the customers only on the basis of cost of services, determined with the help of cost & management accounting techniques.

In this context it may be noted that The Union Minister of Commerce Mr. P. Chidambaram has recently criticised the functioning of banking sector for the
inefficiency in the area of encashment of cheques, opening of letter of credit, reconciliation of accounts, bad debts and irrationality in bank charges. Especially the minister has referred the charging of commission for issuing demand drafts on the basis of percentage of draft amount. (Reference-The Economic Times dt.02/04/1993).

The main business of the is to collect deposits and give them as loan. The difference between rates of interest on deposits and loans is the net income of the bank. From this income it has to cover all its establishment expenses, like staff salaries, general administration expenses etc. Since the rates of interest are governed by the Reserve Bank of India, the individual banks are left with no alternative but to manage its affairs effectively. Simultaneously they have to look into social aspect of the banking business also. The banks have to follow the policies to achieve social objectives such as, weaker section advances at lower interest, creation of employment, making available the banking services even in remote rural places etc. As such the banks have to render a minimum level of services, though some of which are uneconomic. In this context it may be noted that recently the banks have raised the limit of minimum balance in the current accounts to Rs.5,000 and in the savings accounts to Rs.1,000 to maintain the accounts with cheque book facility (refer Daily Pudhari dt.16/05/1995). The main reason behind this enhancement is
reported to be the cost of services. Since the expenditure (mainly on staff) of the banks (especially nationalised banks) is increasing day by day the cost of services is also increasing. Here it may be noted that now the banks have to undertake exhaustive cost study in order to exercise cost control and cost reduction by improving efficiency and productivity. This is essential to enable the banks to optimise profitability without increasing the burden on the customers.

Under the circumstances it is suggested that the bank should adopt cost based Information System in order to improve the performance keeping the social aspect and charge the customers on a rational basis.

A careful vigilant banker, can keep control on the recovery aspects to ensure that the bank's funds are only given to needy persons who can be educated on the virtues of promptness. Bank survive on recycled funds, and only if overdues are kept to the minimum. Poor recovery management can kill a bank. Good recovery management can bring good results to the bank. The bank has to follow certain steps, both at the pre sanction stage and at the post sanction follow up stage, for the better recovery management. The staff of the bank need to tune into the bank's strategy for recovery management. The staff need to be trained to keep organisation goals before them and feel
achievement is important for survival and for profits. A proper Information System if implemented in the bank, can take care of better recovery management.

8.6 Income recognition and Non Performing Assets

As per the Reserve Bank of India guidelines, every bank is now required to provide for Non Performing Assets. For the year ended 31/3/95, all loan accounts wherein the interest is in arrears for two quarters, are required to be treated as Non Performing Assets. Similarly the loan accounts are required to be classified as, out of order accounts, sub-standard assets, doubtful assets and loss assets and accordingly the provision is required to be made in the financial accounts of the bank. The computerisation of banking operations will help the classification of assets and compliance of Non-Performing assets and Income Recognition provisions. It takes much time for such classification by manual process. The computerisation will not only complete the entire exercise early but also with accuracy.

Now a days, in view of free economy and globalisation, many foreign banks are entering in our country. With the broad based capital structure of such banks, they can give loans at cheaper rates than our banks. As such the banks in our country are now facing competition
with such foreign banks. Under these circumstances the costing system will definitely help the banks to extend better services at lower costs and improve the performance by successfully facing the competition.

Computerisation of the banking operations is the need of the time. Today many banks are adopting full computerisation of their operations in order to give more efficient, accurate and reliable service to the clients. Moreover the computerisation of the banking operations reduces the risk of frauds and misappropriations.

As such a proper Computerised Cost Based Information System can be easily incorporated in the total branch computerisation package itself.

8.7 Measures suggested to improve bank's profitability:

1) Deposits in Current Account:

No interest is paid on current account deposits and, therefore, apparently there is no cost of such deposits to banks. But it is not so. Banks are after all maintaining the accounts of firms, business enterprises, industrial units/houses etc. which involves expenditure on staff, stationery and infrastructure. Therefore such service are not be provided free of cost. It is only in the interest
of bank to levy a reasonable charge on maintaining the current accounts of such units on the basis of number of cheques handled, volume of business routed through the account etc.—details in this regard can be worked out on the basis of cost benefit analysis.

ii) Establishment expenses:

A conscious effort needs to be made to bring down the establishment expenses to a more reasonable level.

iii) Other expenses:

There is more scope for cutting down the other expenses. Every staff member should have the will to reduce expenses. Proper and economic use of stationery and telephone facilities, suitable drafting of telegrams, proper use of other telecom facilities, economically using the vehicles of the bank etc. are some of the avenues.

iv) Implementation of Cost Based Information System:

The cost based Information System as suggested above may be implemented to evaluate the performance of the branch.