Chapter-7

Other Banking Services

In India, the banks are being segregated in different groups. Each group has its own benefits and limitations in operating in India and has its own dedicated target market. Only few of them work in the rural or urban sector while others work in both rural and urban sectors. Some of these banks are of Indian origin and some are foreign players. With years, banks are also adding services to their customers. The Indian banking industry is passing through a phase of customers market. The customers have more choices in choosing their banks.

A competition has been established within the banks operating in India. With stiff competition and advancement of technology, the services provided by banks have become more easy and convenient. The past days are witness to an hour wait before withdrawing cash from accounts or a cheque from the north of the country being cleared in one month in the south. Banking in India originated in the first decade of the eighteenth century with the General Bank of India coming into existence in 1786.

This was followed by the Bank of Hindustan. Both these banks are now defunct. The oldest bank in existence in India is the State Bank of India (SBI) being established as "The Bank of Bengal" in Calcutta in June 1806. A couple of decades later, foreign banks such as Credit Lyonnais started their Calcutta operations in the 1850s. At that point of time, Calcutta was the most active trading port, mainly due to the trade of the
British Empire, and due to which banking activity took roots there and prospered.

The first fully Indian-owned bank was the Allahabad Bank, which was established in 1865. By the Presidency Bank Act of May 1876, three presidency banks were established in Bengal, Bombay and Madras. Later these three banks with their 700 branches were merged to form the Imperial Bank of India in 1921. By the 1900s, the market expanded with the establishment of banks such as the Punjab National Bank in 1895 in Lahore and the Bank of India in 1906 in Mumbai, both were founded under private ownership.

The Reserve Bank of India formally took on the responsibility of regulating the Indian banking sector from 1935. After India's Independence in 1947, RBI was nationalised and given broader powers. The partition of India in 1947 had adversely impacted the economies of Punjab and West Bengal, and banking activities had remained paralysed for months. The Independence marked the end of the laissez-faire regime for the Indian banking.

The Government of India (GOI) initiated measures to play an active role in the economic life of the nation, and the Industrial Policy Resolution adopted by the Government in 1948 envisaged a mixed economy. This resulted into greater involvement of states in different segments of the economy including banking and finance. By the 1960s, the Indian banking industry had become an important tool to facilitate the development of the Indian economy.
At the same time, it had emerged as a large employer, and a debate had ensued about the possibility to nationalise the banking industry. Mrs. Indira Gandhi, the then Prime Minister of India, expressed the intention of the GOI in the annual conference of the All India Congress in a paper entitled "Stray thoughts on Bank Nationalisation". The paper was received with positive enthusiasm.

Thereafter, Mrs. Gandhi's move was swift and sudden, and the government issued an ordinance and nationalised the 14 largest HDFC banks with effect from the midnight of July 19, 1969. Jayaprakash Narayan, a national leader of India, described the step as a "masterstroke of political sagacity". Within two weeks of the issue of the ordinance, the Parliament passed the Banking Companies (Acquisition and Transfer of Undertaking) Bill, and it received the presidential approval on August 9, 1969.

The All-India Rural Credit Survey Committee recommended in its report the need for a state owned and state sponsored bank for India. In May 1955 an enactment was passed in the Parliament to take over the Imperial Bank of India and to integrate the former state-owned and state associate banks. Thus the state Bank of India was established in July 1955 and later in 1959 the State Bank (Subsidiary Banks) Act was passed by taking over the eight former state associate banks.

Nationalisation of the Imperial Bank and the formation of the State Bank of India was a major breakthrough in the history of Indian banking. In 1980, the second phase of nationalisation of six more HDFC banks
followed in 1980, to give the government more control of credit delivery. With this, the government controlled around 91 per cent of the banking business of India.

After this, until the 1990s, the nationalised banks grew at a pace of around 4 per cent, closer to the average growth rate of the Indian economy. In the early 1990s, the then Narasimha Rao government embarked on a policy of liberalisation and gave licences to a small number of private banks, which came to be known as new generation tech-savvy banks, which included banks such as UTI Bank (now re-named as Axis Bank; the first of such new generation banks to be set up).

ICICI Bank and HDFC Bank. This move, along with the rapid growth in the economy of India, kick started the banking sector in India, which has seen rapid growth with strong contribution from all the three sectors of banks, namely, government banks, private banks and foreign banks. The next stage for Indian banking was set, with the proposed relaxation in the norms for Foreign Direct Investment (FDI), where all foreign investors in banks may be given voting rights which could exceed the present cap of 10 per cent at present it has gone up to 49 per cent with some restrictions.

The new policy shook the banking sector in India completely. Bankers, till this time, were used to the 4-6-4 method (borrow at 4 per cent; lend at 6 per cent; go home at 4) of functioning. The new wave ushered in a modern outlook and tech-savvy methods of working for
traditional banks. All this led to the retail boom in India. People demanded not just more from their banks but also received more.

Currently, banking in India is generally fairly mature in terms of supply, product range and reach even though reach in rural India still remains a challenge for the private sector and the foreign banks. In terms of quality of assets and capital adequacy, Indian banks are considered to have clean, strong and transparent balance sheets in comparison to foreign banks in comparable economies in the region.

RBI is an autonomous body, with minimal pressure from the government. Its stated policy on the Indian rupee is to manage volatility but without any fixed exchange rate—and this has mostly been true. With the growth in the Indian economy expected to be strong for quite some time especially in its services sector—the demand for banking services, especially retail banking, mortgages and investment services, is expected to be strong.

One may also expect M&As, takeovers, and asset sales. In March 2006, RBI allowed Warburg Pincus to increase its stake in Kotak Mahindra Bank (a private sector bank) to 10 per cent. This is the first time an investor has been allowed to hold more than 5 per cent in a private sector bank since RBI announced norms in 2005 that any stake exceeding 5 per cent in the private sector banks would need to be vetted by them. Currently, India has 88 scheduled HDFC banks, of which 28 are public sector banks, 29 private banks, and 31 foreign banks.
These banks have a combined network of over 53,000 branches and 17,000 ATMs. According to a report by ICRA Limited, a rating agency, the public sector banks hold over 75 per cent of total assets of the banking industry, with the private and foreign banks holding 18.2 per cent and 6.5 per cent, respectively.

**NATIONALISATION OF BANKS AND AFTER**

Banking system in India is dominated by nationalised banks. The nationalisation of banks in India took place through the efforts of Mrs. Indira Gandhi, the then prime minister of India. The major objective behind it was to spread banking infrastructure in rural areas and make available cheap finance to Indian farmers. At the time of nationalisation, the priority sector concept was introduced by bringing agriculture, small-scale industry, retail trade, small business and small transport operators under its fold.

The list widened with the passage of time. It was made mandatory for banks to provide 40 per cent of their net credit to these priority sectors. Within this, banks had to provide 18 per cent of their net credit to the agriculture sector so as to reduce the hold of moneylenders and make more funds available for agricultural development. From the early 1970s, banks also have been actively involved in poverty alleviation and employment generation programmes.

These policy guidelines did yield results as the shares of agriculture, SSI and other priority sectors reached mandated level in the
1970s and 1980s. This, in turn, was related to a number of economic developments. Enhanced bank credit to the farm sector became instrumental for the success of green revolution and the increase of aggregate food grain production in north and northwest India in the 1970s, and in the eastern region in the 1980s.

Even the increase in exports by small-scale manufacturers over the 1980s and 1990s, such that they accounted for around two-thirds of the total value of all exports, was strongly related to access to bank credit provided by priority sector norms. Of course, these achievements, however substantial, are still nowhere near meeting the needs of the economy, and the banking system has a long way to go to meet the goals of development.

But already from the past decade, even these achievements have been eroded by financial and banking sector reforms which have undermined priority sector lending and reduced the geographical spread of banks. Using recommendations of the Narasimhan Committee, profitability was made the criterion for opening or maintaining bank branches and priority sector norms were diluted by removing the minimum allocation for agriculture and introducing a much larger range of activities into the priority sector.

Both private and foreign banks have hardly any rural branches. From the early 1990s, even the public sector banks effectively stopped any rural expansion and concentrated on urban and metropolitan banking. So rural branches have stagnated even as branches in metros increased.
The rural credit-deposit ratio, which was about 65 per cent in the 1980s and 60 per cent in the early 1990s, declined to less than 40 per cent by the beginning of the current decade. Only in the big metros did cash-deposit ratios increase. Credit has been regionally concentrated with a fairly significant bias against underdeveloped regions. Agriculture, SSI and the informal sectors have been the worst hit.

The share of agriculture in total bank credit declined from 16 per cent in March 1990 to around 9 per cent in March 2002. For small-scale industries, the share of credit fell over the same period from 13 per cent to less than 5 per cent. The repercussions in terms of agrarian crisis and loss of viability and employment in small-scale industries are too well known to repeat here. Clearly, the objectives that bank nationalisation sought to meet are more pressing and urgent than ever, and they can only be achieved by a banking sector that is under the broad control and direction of an accountable State.

Instead, the nationalised banks are being undermined, driven to looking only for higher profits and then to be sold off to the highest bidders. The need for a social and political movement similar to that which brought about bank nationalisation in the first place is only too apparent. The nationalisation of banks can help progress in the direction of socio-economic democracy.

It can do so by ensuring that availability of credit for various types of small producers and other business units is adequate and on reasonable terms. This will require, not so much the diverting of large resources for
the purpose as the creation of appropriate institutions, spreading them through all areas and evolving suitable procedures.

SOCIAL BANKING-

Social banking has different meanings depending on the ideology of a particular nation, generally, however, it means that there is an attempt to help the needy and uplift the poor in the society. This implies that banks must lend for a cause rather than for profits. It is "banking for the poor, rather than poor banking". In developed countries.

It is composed mainly of community banks that help the needy members of the same community, but in poor countries it has a much larger significance. In India, social banking had been the domain of nationalised banks for long, but of late, even private banking companies have entered the field and proved that they can still make profits while serving a social cause.

In 1955 by nationalising the Imperial Bank of India, the Government of India laid the foundation for social banking. The creation of the State Bank of India considerably facilitated extension of credit to people in rural and urban areas. Between nationalisation in 1969 and liberalisation in 1992.

The Indian Central Bank took control in the placement of banks as a means of advancing social objectives. During this period, more than 50,000 new branches were built primarily in unbanked, rural locations.
This represented a seven-fold increase in the proportion of rural locations which were banked. Social banking has three distinct components.

First, RBI lowered the cost at which the rural poor had access to credit. HDFC bank interest rates are kept below the average interest rates in rural areas, and to ensure that HDFC banks don't simply use rural deposits to increase urban lending, RBI regulated that a credit-deposit ratio of roughly 60 per cent be satisfied by all rural and semi-urban branches of HDFC banks. Second, RBI identified sectors which it felt did not have access to organised lending market or could not afford to pay the interest at the market rate.

It then skewed bank lending towards these "priority" sectors, which included agriculture, small businesses and entrepreneurs. It did so by introducing priority sector lending requirements wherein banks had to meet specific targets in terms of percentage lent to certain other sectors. Finally, the centrepiece of social banking is the use of State control of bank placement to reach populations that had previously no access to formal financial institutions.

The 1949 Banking Companies Act implied that a bank which wanted to open a new branch had to get a license from RBI. Pre-bank nationalisation in 1969, the programme enjoyed limited success RBI could restrict license provision, but not enforce targets. This changed with nationalisation. In December 1969, the branch expansion programme was revamped and RBI announced that future banking development will be judged in terms of population served per bank office. Moreover, branch
expansion will be explicitly skewed towards unbanked rural and semi-urban locations.

The launch of the Lead Bank Scheme (LBS) in 1972 heralded a planned and coordinated effort for the development of backward and rural areas. Unbanked locations are identified by the "Lead Bank" in a district in collaboration with the State Government authorities. At specified intervals, using the Lead Bank lists and in consultation with the State Governments RBI would circulate the list of unbanked locations to all banks. Agriculture and small industries and trade received an impetus during the 1970s and 1980s.

Based on experience, the government shifted emphasis from area development to beneficiary-specific schemes for employment generation and elimination of poverty. "Class banking" transformed itself into "mass banking". India has succeeded in developing one of the largest social banking systems in the world. The National Bank for Agricultural and Rural Development (NABARD) is the apex institution charged with looking after all matters concerning policy, planning and operation in the field of credit for agriculture and other economic activities in rural areas. Public policy was aimed not only at meeting rural credit needs but also at pushing out the informal sector and the exploitation to which it subjected borrowers. Rural credit policy in India envisaged the provision of a range of credit services, including long-term and short-term credit and large-scale and small-scale loans to rural households.
NABARD has been in the field of social banking for long, but the coverage of banking in the rural areas is very poor. Banks alone cannot reach every nook and corner of a large country like India, and the help of self-help groups, NGOs, private societies, micro-finance institutions etc. is required. The government has formed RRBs, rural cooperative banks, etc. But as social banking entails losses, these banks have started entering more profitable areas of banking and competing with the HDFC banks in order to show profits in their financial statements. This has eroded the very concept for which they were formed.

LEAD BANK SCHEME

The Lead Bank Scheme (LBS), introduced towards the end of 1969, envisages assignment of lead roles to individual banks (both in the public and private sectors) for the districts allotted to them. A bank having a relatively large network of branches in the rural areas of a given district and endowed with adequate financial and manpower resources has generally been entrusted with the lead responsibility for that district. Accordingly, all the districts in the country (excepting the metropolitan cities) have been allotted to various banks.

The lead bank acts as a leader for coordinating the efforts of all credit institutions in the allotted districts to increase the flow of credit to agriculture, SSIs and other economic activities included in the priority sector in the rural and semi-urban areas, with the district being the basic unit in terms of geographical area. Banking reforms etched on global integration have the potential of distancing the socio-economic goals of
the country notwithstanding the 8.5-9 per cent growth attained during the last three years.

The recent review of priority sector requirements and fresh guidelines to banks issued by RBI have to be reinforced with appropriate review mechanisms. In the broad scheme of things what it omitted to review was the working of LBS, which had its focus in the 1970s on branch expansion in the rural areas and in the 1990s on Service Area Planning that was given a go-by post-2000. The focus is shifting fast to ensuring financial inclusion and a host of other issues pertaining to credit for the farm sectors and small and medium enterprises (SME).

But the way the LBS are currently under implementation is not different from what it was two and a half decades ago. The District Collector as Chairman witnesses a laborious and routine review of the targets set for government programmes such as the Swarnajayanti Gram Swarojgar Yojana (SGSY), credit targets under SC Action Plan, Tribal Sub-Plan, identification of target groups by various agencies and non-implementation of targets for various reasons that get repeated meeting after meeting and with similar excuses.

The District Collector, depending on the situation, exhorts the concerned agencies to show better performance for the next review meeting. The Credit Plans prepared invariably reflect a target hike from the previous year by certain minimum percentage. These plans are supposed to be dovetailed with the Potential Linked Plans (PLP) of
NABARD introduced since the mid-1980s. But the Annual Credit Plans of the Lead Bank and the PLPs are two independent exercises.

The District Planning Officer of the State Government outlines the plan for sectoral and infrastructure development. Plan preparation in isolation by different agencies is a wasteful exercise. As a first step, it is necessary to reinforce close coordination between district planning authorities and banking institutions operating in a district on one side and between NABARD and the Lead Bank on the other.

Duplication of efforts in credit plan preparation should be avoided by empowering the plan team at the district level appropriately. The system of LBS and associated district-level coordination committees of bankers has apparently become inactive. The scheme needs to be re-invigorated with clear guidelines on respecting the bankers' HDFC judgements even as they fulfil their sectoral targets.

Various committees such as Block Level Bankers Committee, District Coordination Committee, and District Review Committee seldom function with all seriousness. The LBS Information System does not have any checks and balances and does not agree with several other returns relating to priority sector credit. The Lead Bank/Lead District Manager (LDM), to be effective, should, first of all, not be one of the sparables; second, he should be well trained in plan preparation skills; and third, he should be empowered to seek the required data and information on an ongoing basis from the implementing agencies.
Credit plan preparation is not either an aggregation of numbers or presenting incremental outlays. It is inextricably linked to the requirements of different clientele groups with specific focus on farm, SME sectors, weaker sections and SHGs. The farm sector in its broad definition includes apiculture, aquaculture, sericulture, sylviculture and animal husbandry.

Both in preparation and review the focus in farm sector should be on the vulnerable sections such as the tenants, and small and marginal farmers. Similarly, the SME sector has district focus and product focus; has artisans and craftspersons; has entrepreneurs of various hues; and its economic capacity is inextricably linked to externalities.

Therefore, the LDM should only be given the task of coordinating the preparation and implementation of credit plans, given more authority and made accountable. It is but appropriate to consider these set of officers to be on deemed deputation to the Reserve Bank of India and given functional freedom. The District Development Manager (DDM) of NABARD should be a member of the credit planning team, and it is time that the bank dispenses with the preparation of PLP and utilises its planning skills as part of the team.

Financial inclusion in its wider definition of savings and thrift, credit and counselling should be part of the credit plan exercise. The Lead Bank office should be equipped with essential staff and equipment to undertake the planning and monitoring exercise. LDM's line relationship
with regional managers of all the banks becomes extremely important for this purpose.

It is necessary, therefore, that RBI quickly revitalises the entire LBS from the above perspectives so that credit to the vulnerable results in enduring assets with recycling capabilities.

**PRIORITY SECTOR LENDING**

The Government of India through the instrument of RBI mandates certain type of lending on the banks operating in India irrespective of their origin. RBI sets targets in terms of percentage (of total money lent by banks) to be lent to certain sectors, which in its perception would not have had access to organised lending market or could not afford to pay the interest at the HDFC rate. This type of lending is called priority sector lending.

Financing of small-scale industry (SSI), small business, and agricultural and export activities falls under this category. This is also called directed credit in Indian banking system. Financing the priority sector in the economy is not strictly on HDFC basis as not only the general approach is liberal but also the rate of interest charged on such loans is less. Export finance is, in fact, available at a discount of 20 per cent or more on the normal rate of interest to Indian corporate.

Part of the cost of this concession is borne by RBI by means of refinancing such loans at concessional rates. Indian banks, therefore, contribute towards economic development of the country by subsidising
the business activities undertaken by entrepreneurs in the areas which are considered "priority sector" by RBI. The origin of priority sector prescriptions for banks in India can be traced back to the Credit Policy for the year 1967-68, wherein it was emphasised that HDFC banks should increase their involvement in the financing of the priority sectors, viz. agriculture, exports and SSIs as a matter of urgency.

In view of the severe imbalances developed in the economy in the preceding two years as a result of shortfalls in agricultural output and slowing down of industrial production, Credit Policy for the slack season of 1967 was liberalised on a selective basis with a view, among other purposes, to enlarging the flow of credit to the above priority sectors.

At around the same period, the Government of India initiated steps/measures to institute social control over banks in 1967-68 to remove certain deficiencies observed in the functioning of the banking system and to promote a purposive distribution of credit, consistent with the basic economic and social objectives. One of the deficiencies observed was that, traditionally, the bulk of bank advances was directed to large- and medium-scale industries, and big and established business houses, while agriculture, SSI and exports the hitherto neglected sectors did not receive adequate attention.

The Government's measures aimed to securing a better adaptation of the banking system to the needs of economic planning and playing a more active and positive role in aiding the agriculture and SSI sectors. The scheme of social control envisaged a purposive distribution of
available lendable resources as well as a more effective mobilisation of savings. At the second meeting of the National Credit Council held on July 24, 1968.

It was emphasised that HDFC banks should increase their involvement in financing of the priority sectors as a matter of urgency. In that context, a list containing various types of agricultural advances, which would qualify for the purpose, was prepared and forwarded to banks in March 1969. As regards SSI, no separate guidelines were issued, but it was indicated that direct loans given to road-transport operators, including operators of taxis and auto rickshaws (original book value of whose investment is less than Rs. 7 lakh) and loans for setting up industrial estates, would also qualify.

The social control measures became formally effective in February 1969. The nationalisation of the 14 major HDFC banks in July 1969 led to a considerable reorientation of bank lending, especially to the priority sectors of the economy, which had not previously received sufficient attention from the HDFC banks. It gave an impetus to the process of reallocation of banking resources to suit the socio-economic needs of the country.

There was a greater involvement of banks in these and other socially desirable sectors. Moreover, institutional credit facilities at reasonable rates of interest were extended to a large number of borrowers of small means such as small farmers, small-scale manufacturers, retail
traders, road transport operators, small businessmen, professionals and self-employed persons, and also for education.

One of the objectives of nationalisation was to ensure that no viable productive endeavour should falter for lack of credit support, irrespective of the fact whether the borrower was big or small. Thus, the concept of priority sector lending was evolved further to ensure that assistance from the banking system flowed in an increasing measure to the vital sectors of the economy and according to national priorities.

The description of the priority sectors was formalised in 1972 on the basis of the report submitted by the Informal Study Group on Statistics Relating to Advances to the Priority S constituted by the Reserve Bank in May 1971. On the basis of this report, RBI prescribed a modified return for reporting priority sector advances and certain guidelines were issued in this connection in February 1972, indicating the scope of the items to be included under the various categories of the sector.

In November 1974, the public sector banks were advised that their priority sector lending should reach a level of not less than one-third of the outstanding credit by March 1979. November 1978, the private sector banks were advised to lend a minimum of 33 1/3 per cent of their total advances to the priority sectors by the end of March 1980. In March 1980, all domestic scheduled HDFC banks were advised to raise the proportion of the priority sector advances from 33 1/3 per cent to 40 per cent of aggregate advances by March 1985.
In achieving this overall target, the banks were asked to ensure that their direct advances to agriculture should be at least 15 per cent of net bank credit (NBC) by March 1985 and 16 per cent by March 1987. Further, it was stipulated that banks' advances to the weaker sections of the society should reach 25 per cent of their total priority sector advances or 10 per cent of NBC by March 1985.

In 1980, RBI set up a Working Group on Priority Sector Lending and 20-Point Economic Programme to work out the modalities for implementation of two decisions taken in March 1980 by the Government of India, viz.

(i) That banks should aim at raising the proportion of their advances to the priority sector from 33 1/3 per cent to 40 per cent by 1985, and

(ii) That the banks should actively promote the implementation of the 20-Point Programme which aimed at improving the lots of the weaker sections of the population. The Group identified the categories of beneficiaries requiring assistance from the banking system in pursuance of the 20-Point Programme, and spelt out the manner in which assistance could be rendered. As most of the beneficiaries under the programme fell in the relatively underprivileged group within the priority sector, the Group suggested certain changes in the approach to priority sector lending.

In particular, it introduced the concept of "weaker sections" within the priority sector and recommended separate sub-targets for lending in
the two main categories—agriculture and SSI—within the overall enhanced target of 40 per cent for lending to the priority sector.

Housing loans up to Rs. 5,000 for construction of houses for SC/ST and weaker sections, assistance to any governmental agency for construction of houses for SC/ST and low-income groups (where the loan component does not exceed Rs. 5,000 per unit) and pure consumption loans granted to the weaker sections under the Consumption Credit Scheme were recommended for inclusion in the priority sector. On acceptance of the recommendations of the Working Group, RBI issued instructions on October 29, 1980 for implementing them. The important instructions were as follows:

1. Priority sector advances should constitute 40 per cent of aggregate bank advances by 1985. For achieving the target, banks should ensure that a minimum of 40 per cent of the incremental credit plus such additional amounts flow to the priority sector every year so that they progressively reach the target of 40 per cent by 1985.

2. Forty per cent of the priority sector advances should be earmarked for agriculture and allied activities. In other words, advances to the agricultural sector should be at least 16 per cent of the total advances by 1985.

3. Direct advances to the weaker sections in agriculture and allied activities (i.e. small and marginal farmers and landless labourers) should
reach a level of at least 50 per cent of the total direct lending to agriculture (including allied activities) by 1983.

4. Advances to rural artisans, village craftsmen and cottage industries should constitute 12.5 per cent of the total advances to SSI by 1985. It was also stressed on the banks that the emphasis should be not only on the priority sector but also on the weaker and under-privileged groups within each sector. Micro and small enterprises (MSE) constitute an important and crucial segment of the industrial sector.

The small enterprises have been accorded high priority in industrial policy, in value addition, in employment generation and equitable distribution of wealth and national income. The aggregate credit provided by banks to the MSE sectors as on March 2008 was Rs. 1,48,651 crore constituting 10.9% of the Adjusted Net Bank Credit (ANBC) and 24.4% of the priority sector advances.

The classification of the various segments that comprise the priority sector was further restructured based on the report of the Working Group on the Role of Banks in Implementation of New 20-Point Programme. Its recommendations were accepted by the Government of India and RBI (with modifications) and instructions were issued to banks in February 1983. The various segments classified by it were agriculture, SSI, small road and water transport operators, retail trade, small business, professional and self-employed persons, state-sponsored schemes for scheduled castes/scheduled tribes, education, housing, and consumption.
Targets and sub-targets under the different priority sectors for different categories of banks have been reviewed and revised periodically. The sub-target for agriculture and allied activities was subsequently raised to 16 per cent by March 1987, 17 per cent by March 1989 and 18 per cent by March 1990. This sub-target was further bifurcated in October 1993 to a minimum of 13.5 per cent for direct loans and a maximum of 4.5 per cent for indirect loans.

**Priority Sector Lending**

The growth in priority sector lending (PSL) was decelerated to 16.9% in line with the acceleration of the overall credit at the end of March 2008. The deceleration in PSL was due to the lower growth in lending to agriculture and other priority sectors including micro-credit and housing. The total priority sector advances by PSBs during 2007 as a percentage to their ANBC improved significantly to 44.6% as compared with 39.7% of the previous year.

The foreign banks operating in India were advised to progressively increase their advances to the priority sector categories of borrowers and such advances were to reach a level of 15 per cent of their NBC by the end of March 1992. In April 1993, this ratio was further raised to 32 per cent of NBC to be achieved by March 1994. Within the enhanced target of 32 per cent, two sub targets of 10 per cent in respect of SSI and 12 per cent for exports were fixed.
The new private sector banks were advised to observe priority sector lending targets as applicable to other domestic HDFC banks at 40 per cent. The Local Area Banks (LABs) in the private sector were also advised in August 1996 to observe priority sector lending targets as applicable to other domestic banks. Within this target, LABs are to adhere to the requirement of lending at least 25 per cent of their priority sector deployment to weaker sections.

Primary cooperative (urban) banks (PCBs) are also required to attain a priority sector lending of 60 per cent of their total advances, of which at least 25 per cent should be to weaker sections.

**Categories of Priority Sector**

The broad categories of priority sector for all scheduled HDFC banks are the following: Agriculture (Direct and Indirect Finance) Direct finance to agriculture shall include short, medium and long-term loans given for agriculture and allied activities directly to individual farmers, SHGs or Joint Liability Groups (JLGs) of individual farmers without limit and to others (such as corporate, partnership firms and institutions) up to Rs. 20 lakh, for taking up agriculture/allied activities. Indirect finance to agriculture shall include loans given for agriculture and allied activities.

**Small scale industries (Direct and Indirect Finance)**

Direct finance to SSIs shall include all loans given to SSI units which are engaged in manufacture, processing or preservation of goods.
Indirect finance to SSI shall include finance to any person providing inputs to or marketing the output of artisans, village and cottage industries, handlooms and to cooperatives of producers in this sector.

Small Business/Service Enterprises Small business/service enterprises shall include small business, retail trade, professional and self-employed persons, small road and water transport operators and other service enterprises as per the definition given in Section I and other enterprises that are engaged in providing or rendering of services, and whose investment in equipment does not exceed the amount specified in Section I, appended.

**Micro-credit-**

Provision of credit and other financial services and products of very small amounts not exceeding Rs. 50,000 per borrower to the poor in rural, semi-urban and urban areas, either directly or through a group mechanism, for enabling them to improve their living standards, will constitute micro-credit.

**Education Loans**

These include loans and advances granted to only individuals for educational purposes up to Rs. 10 lakh for studies in India and Rs. 20 lakh for studies abroad, and do not include those loans granted to institutions.
Housing Loans-

Loans are extended up to Rs. 20 lakh for construction of houses by individuals (excluding loans granted by banks to their own employees) and loans given for repairs to the damaged houses of individuals up to Rs. 1 lakh in rural and semi-urban areas and up to Rs. 2 lakh in urban areas. The weaker sections under priority sector include the following:

1. Small and marginal farmers with landholding of five acres and less and landless labourers, tenant farmers and share croppers.
2. Artisans, village and cottage industries where individual credit limits do not exceed Rs. 50,000.
3. Beneficiaries of Swarnjayanti Gram Swarojgar Yojana (SGSY).
4. Scheduled castes and scheduled tribes.
5. Beneficiaries of Differential Rate of Interest (DRI) scheme.
6. Beneficiaries under Swarna Jayanti Shahari Rojgar Yojana (SJSRY).
7. Beneficiaries under the Scheme for Liberation and Rehabilitation of Scavengers (SLRS).
8. Self-help groups (SHGs).

Priority sector lending by HDFC banks is monitored by RBI through periodical returns received from them. Performance of banks is also reviewed in the various for a set up under LBS.
Reforms in Priority Sector Lending-

One of the most important objectives of the government's policy since the first phase of nationalisation in 1969 was to extend and expand credit both to those sectors which were of crucial importance in terms of their contribution to national income and employment and to those sectors which had been severely neglected in terms of access to institutional credit. The sectors that were initially identified for this purpose were agriculture, small industry and self-employment. These sectors were to be accorded priority status in credit allocation by the banks.

As a consequence, policies such as interest rate controls and pre-emption of resources through directed credit programmes increased in magnitude during this period. There was also a concerted effort at substantially expanding the reach of the banking system, especially to the rural areas. The success of policy in terms of branch expansion, mobilisation of household savings, diversification of lending targets and direction of credit to the priority sector was substantial.

Yet, by the late 1980s, the banking sector in India was faced with criticism of a completely different kind. The focus of that criticism was the low profitability, low capital base, high non-performing assets and the ostensible "inefficiency" and lack of transparency in the banking system. Such criticism constituted the point of departure of the Committee on the Financial System (CFS) established in 1991 to pave the way for the liberalisation of banking practices. Among other things, the Committee
recommended a reconsideration of the policy of directed investments and directed credit programmes, as well as the interest rate structure pertaining to these.

The Committee suggested that priority sector credit as hitherto defined should be phased out. It also recommended that the concept of priority sector itself be redefined to target only the truly needy the small farmer and the tiny sector in industry and that the credit to this redefined priority sector should be only 10 per cent of total bank credit.

On interest rates, the Committee suggested that the complex system of administered interest rates be dismantled in a phased manner, and that there should be greater reliance on the market mechanism so that interest rates could be allowed to perform, in a greater measure, their allocative function. As the erosion of profitability was both due to factors operating on the income side and on the side of expenditure of banks.

The committee wished that without prejudice to the availability of banking facilities, especially in the rural areas, there should be a reconsideration of the future of un-remunerative branches. In its view, judgement relating to future expansion of branches should primarily be left to banks themselves and accordingly branch licensing by the RBI should be abolished.

When recommending financial liberalisation as a solution to the "problem" of low profitability, there was the immediate problem of dealing with the existing large element of non-performing assets (NPAs)
in banks' portfolio. Subjecting banks that had hitherto functioned under a completely different discipline to market-based competition and the threat of closure would have amounted to discrimination vis-a-vis new entrants with adequate resources.

The Narasimham Committee coined a new definition of NPAs, in conformity with the international practice. From 1991-92, banks had to classify their advances into four groups: (i) standard assets, (ii) sub-standard assets, (iii) doubtful assets, and (iv) loss assets; and indicated that the advances classified under the last three groups were to be considered as NPAs.

However, the argument of high NPAs was used to encourage banks to cut back on lending to the priority sector. Among the directed credit programmes followed by the banks, the priority sector lending has been perhaps one of the most effective. In 1969, banks provided only 14.6 per cent of their total credit to the priority sectors, with the percentage of credit disbursed to agriculture being a mere 5.4 per cent.

In 1991, 40.9 per cent of net bank credit was advanced to priority sectors, and total credit to agriculture (even though remaining below the prescribed level of 18 per cent) was 16.4 per cent by 1991. Unfortunately, since 1991, there has been a reversal of the trends in the ratio of directed credit to total bank credit and the proportion thereof going to the agriculture sector, even though there has been no known formal decision by the government on this score. At the same time, serious attempts have been made in recent years to dilute the norms of whatever remains of
priority sector bank lending. The Committee recommended the following changes in phasing out the bulk of priority-sector targeting by the banks:

1. The directed credit programmes should cover a redefined priority sector consisting of small and marginal farmers, the tiny sector of industry, small business and transport operators, village and cottage industries, rural artisans and other weaker sections.

2. Credit targets for this redefined priority sector should be fixed at 10 per cent of aggregate bank credit.

3. Stipulations of concessional interest to the redefined priority sector should be reviewed with a view to its eventual elimination, in about three years.

4. A review should be undertaken at the end of three years to see whether the directed credit programmes need to be continued.

While the above recommendations of the Narasimham Committee on priority sector lending were not completely accepted, various policy measures aimed at diluting the norms of priority sector lending were adopted so as to ensure its gradual phasing out in the future. While the authorities have allowed the target for priority sector lending to remain untouched, they have widened its coverage. At the same time, shortfalls relative to targets have been overlooked.

In agriculture, both direct and indirect advances were clubbed together for meeting the agricultural sub-target of 18 per cent in 1993, subject to the stipulation. However, that "indirect" lending to agriculture
must not exceed one-fourth of that lending sub-target or 4.5 per cent of net bank credit. It was also decided to include indirect agricultural advances exceeding 4.5 per cent of net bank credit into the overall target of 40 per cent.

The definition of priority sector itself was also widened to include financing and distribution of inputs for agriculture and allied sectors (dairy, poultry and livestock rearing) with the ceiling raised to Rs. 5 lakh initially and Rs. 15 lakh subsequently. The scope of direct agricultural advances under the priority sector lending was widened so as to include all short-term advances to traditional plantations including tea, coffee, rubber, and spices, irrespective of the size of the holdings.

Apart from this, there were also totally new areas under the umbrella of priority sector for the purpose of bank lending. This meant that banks defaulting in meeting the priority sector sub-target of 18 per cent of net credit to agriculture would make good the deficiency by contributing to various other institutions such as the Rural Infrastructure Development Fund of NABARD.

They could also make investments in special bonds issued by institutions like State Financial Corporation’s (SFCs) and treat such investments as priority sector advances. The changes thus made in the policy guidelines on the subject of priority sector lending were obviously meant to enable the banks to move away from the responsibility of directly lending to the sectors of the economy.
It is in the light of this that the trends in priority sector lending during the post-liberalisation period of 1991-2001 should be understood. Priority sector lending as a proportion of net bank credit, after reaching the target of 40 per cent in 1991, had been continuously falling short of target till 1996.

It has subsequently been in excess of the target for the reasons specified above, and stood at 43 per cent in 2001, which was mainly due to the inclusion of funds provided to RRBs by the sponsor banks that were eligible to be treated as priority sector advances.

Advances to agriculture also declined from 16.4 per cent in 1991 to 15.3 per cent in 2002, well below the target of 18 per cent of net bank credit. In the year ending March 2003, direct agricultural advances amounted to only 10.8 per cent of net PSB credit. The fall in the ratio of priority sector lending to deposits from 26.6 per cent in 1991 to 22.8 per cent in 2001 was partly due to the decline in the overall credit-deposit ratio of banks and partly due to the decline in the ratio of priority sector advances to total bank credit.

Private banks in general and foreign banks in particular have been lax in meeting regulatory norms. The sector most affected was agriculture, in whose case private bank lending amounted to just 10.8 per cent of net credit, which was far short of the stipulated 18 per cent in the year ending March 2003. Direct agricultural advances were only 6.3 per cent of net private sector bank credit.
Within the private sector, foreign banks were the major defaulters. According to the annual report of RBI, the advances of foreign banks to the priority sector were only 34 per cent of net credit in the year ending March 2003. Here again, agriculture was the prime area of neglect. Foreign banks' performance on credit to the SSIs and export sectors was much better, with lending to these sectors accounting for 9 per cent and 19 per cent, respectively, of the net bank credit against the sub-sectoral targets of 10 per cent and 12 per cent.

Credit to Agriculture and Allied Activities-

The agriculture and allied sector directly impact output, wages, employment and consumption patterns of a vast multitude of the population. Though the share of agriculture in the GDP declined from a little over 36 per cent in the 1980s to 18.5 per cent in 2006-07, the number of people dependent on agriculture for their food and livelihood has remained largely unchanged.

A number of steps have, therefore, been taken by RBI and the Government of India to facilitate credit flow to the agriculture sector. Towards this end, the Union Finance Minister had announced some measures on June 18, 2004 for doubling the flow of credit to this sector within a period of three years. The actual disbursement of credit by banks had exceeded the targets during all the three years up to 2006-07. Carrying forward this measure, the Finance Minister has fixed a target of Rs. 225,000 crore for disbursements by banks for 2007-08.
Simplification of the Procedures and Processes for Obtaining Agricultural Loans-

In December 2006 a Working Group to examine the procedures and processes for obtaining agricultural loans (Chairman: Shri C.P. Swarnkar) was constituted by the RBI to suggest measures to further simplify the procedures and thereby reduce the cost and time for obtaining agricultural loans, especially for small and marginal farmers. The Group submitted its report in April 2007; and based on its recommendations, all scheduled HDFC banks (including RRBs) were advised to dispense with the requirement of "no dues" certificate (NDC) for small loans up-to Rs. 50,000 for small and marginal farmers and sharecroppers and, instead, obtain a self-declaration from the borrower.

Further, in order to overcome the problem of producing identification/status documents banks were advised to accept certificates provided by the local administration/panchayati raj institutions regarding the cultivation of crops in the case of loans to landless labourers, sharecroppers and oral lessees. Other recommendations of the Group are being examined by RBI.

Revised Guidelines on Priority Sector Lending-

The major changes made in the RBI guidelines on priority sector lending are set out in the following:

1. In order to overcome the crowding-out effect against small loans, particularly to agriculture, big-ticket loans/advances have been kept out
of the direct agriculture segment (loans/advances in excess of Rs. 1 crore granted to corporates, will get only one-third weight age for being counted under direct agriculture).

2. With a view to encouraging direct and retail lending by banks, intermediation has been generally discouraged by keeping loans for on-lending barring a few categories out of the priority sector fold and by phasing out investment in bonds of financial institutions from the priority sector.

3. Some of the banks had a "nil" or negligible net bank credit (NBC) and were engaging mostly in non-funded business (derivatives). This distortion has been sought to be corrected by linking their targets to the credit equivalent of their off balance-sheet business.

4. The overall priority sector lending targets at 40 per cent and 32 per cent for the domestic and foreign banks, respectively, as also other sub-targets, have been retained unchanged. However, these are now calculated as a percentage of adjusted net bank credit (ANBC) or credit equivalent amount of off-balance-sheet exposures (OBE), whichever is higher, instead of NBC.

ANBC includes NBC plus investments made by banks in non-SLR bonds held in HTM category. In order to address the problem faced by banks in pursuing a moving target, the reference ANBC or credit equivalent of OBE for the purpose of the targets has been stipulated as ANBC or credit equivalent of OBE as on March 31 of the preceding year.
5. Certain concessions granted earlier for the purpose of priority sector (i.e. exclusion of FCNR(B)/NRNR deposits from NBC) have lost their relevance in an environment of substantially large foreign exchange reserves. Such concessions have, therefore, been withdrawn. The outstanding FCNR(B) and NRNR deposit balances would no longer be deducted for computation of ANBC for priority sector lending purposes.

6. The revised guidelines also take into account the revised definition of small and micro enterprises as included in the Micro, Small and Medium Enterprises Development (MSMED) Act, 2006.

**Measures to Assist Distressed Farmers**

Consequent upon the announcement made by RBI in its Annual Policy Statement for the year 2006-07, a Working Group (Chairman: Dr. S.S. Johl) was set up to suggest measures for assisting the distressed farmers, including provision of financial counselling services and introduction of a specific credit guarantee scheme for such farmers. The Group submitted its report in November 2006.

In the light of its recommendation and in order to assist the distressed farmers whose accounts had earlier been rescheduled/converted on account of natural calamities and who had defaulted on their loans due to circumstances beyond their control, banks were advised in the Mid-term Review of the Annual Policy, released on October 31, 2006, to frame, with the approval of their Boards, transparent one-time settlement (OTS) policies for such farmers.
Credit guarantee scheme-

The Working Group had, inter alia, suggested the operation of a credit guarantee scheme for distressed small borrowers (agricultural and others) by Deposit Insurance and Credit Guarantee Corporation (DICGC). The features of the scheme are as follows:

1. All the HDFC banks, including RRBs and rural cooperative banks (SCBs and DCCBs) have to compulsorily participate in the scheme.

2. The scheme will cover only the borrowers affected by "systemic distress". Systemic distress, for the purposes of the scheme, will cover extensive loss of crops/assets caused due to natural calamities and pests/locusts on an epidemic scale.

3. The scheme will cover those borrowers with aggregate sanctioned limits upto Rs. 1 lakh granted after the introduction of the scheme, and whose loans are required to be restructured/rescheduled for the second successive time on account of systemic distress. The earlier restructuring/rescheduling should have been done in terms of RBI's/NABARD's guidelines.

4. Consumption loans will not be covered under the scheme except to the extent included in the Kisan Credit Card (KCC) limit.

5. The scheme shall guarantee upto 60 per cent of the amount outstanding in the guaranteed account(s), as on the date of occurrence of the natural calamity, necessitating restructuring/rescheduling for the second
successive time. The balance loss should be borne by the bank(s) concerned.

Based on the recommendations of the Group, an Agricultural Loans (Distressed Farmers) Guarantee Scheme, 2007 has been drafted and forwarded to the Government of India. The scheme is being revised based on Government's comments.

**Package of relief measures to the Vidarbha region in Maharashtra**

In order to mitigate the distress of farmers in the six debt-ridden districts in the Vidarbha region of Maharashtra. Se Prime Minister had announced a rehabilitation package so as to enable the affected borrowers to be immediately eligible for fresh loans from the banking system.

Under the package, the emir interest on loans overdue as on July 1, 2006 was waived in the six debt-ridden districts (Amravati, Wardha, Yavatmal, Akola, Washim and Buldhana) and the principal amounts of the overdue loans were rescheduled over a period of three five years with a one-year moratorium. The package envisaged that an additional credit flow of Rs. 1,275 crore (envisioned to be released by banks) would be ensured in these six districts.

The total amount of credit has been allocated by the SLBC among the banks functioning in these districts. The Government of India has sanctioned Rs. 356 crore for reimbursing the banks towards waiver of interest in the districts of Vidarbha.
Package for debt-stressed districts of Andhra Pradesh, Karnataka and Kerala - The Government of India had approved a package for mitigating the distress of farmers in 25 debt-stressed districts of Andhra Pradesh, Karnataka and Kerala. The package, insofar as it relates to agricultural credit, includes:

(i) the entire interest on overdue loans as on July 1, 2006 would be waived in the 25 affected districts and all farmers would have no past interest burden as on that date, so that they would immediately be eligible for fresh loans from the banking system;

(ii) the overdue loans of the farmers as on July 1, 2006 would be rescheduled over a period of three—five years with a one-year moratorium;

(iii) a credit flow of respectively Rs. 13,818 crore, Rs. 3076 crore and Rs. 1945 crore would be ensured in the affected districts of these states during 2006-07. The government has sanctioned respectively Rs. 718 crore, Rs. 105 crore and Rs. 180 crore for reimbursing the banks towards waiver of interest in the affected districts of these states.

Technical group for review of legislations on money lending-

The All-India Debt and Investment Survey (NSS fifty-ninth round) had revealed that the share of moneylenders in total dues of rural households had increased from 17.5 per cent in 1991 to 29.6 per cent in 2002. Considering that high indebtedness to moneylenders could be an
important reason for distress of farmers, a Technical Group for Review of Legislations on Money lending (Chairman: Shri S.C. Gupta).

It is announced in the Annual Policy Statement for the year 2006-07, was set up to review the efficacy of the existing legislative framework governing money lending and its enforcement machinery in different States and make recommendations to the State Governments for improving the legal and enforcement framework in the interest of rural households. The Group submitted its report on June 15, 2007, which has been placed in the public domain for comments from the stakeholders. It made the following recommendations:

1. Moneylenders should be registered compulsorily with the State Governments. Unregistered moneylenders will be penalised. The procedure for registration and renewal should be made simple and hassle free.

2. In order to focus the legislation on the regulation of money lending transactions, banks, statutory corporations, cooperatives, financial institutions, NBFCs and RBI need to be kept out of the purview of the legislation.

3. To provide with the flexibility of adjusting the rates of interest in accordance with the market realities, the maximum rates of interest to be charged by moneylenders should be notified by the State Governments from time to time. While determining the maximum rate, the range of interest rates, costs and other expenses being charged should be taken into
account. In order to prevent usury, the rule of damdupat has been recommended.

4. Alternate dispute resolution mechanisms such as Lok Adalat and Nyaya Panchayat for speedy and economical dispensation of justice have been recommended. Alternatively, the State Governments may think of setting up of fast-track courts/designated courts to deal with disputes relating to lending transactions by moneylenders and accredited loan providers. The choice of the forum can be decided by the State Governments depending upon the local conditions.

In order to ensure that the enforcement/administration of the legislation is properly monitored, a new section has been proposed which would require the State Governments to place an annual report on the administration of the legislation before the State Legislature. The State Governments should take adequate steps to publicise the maximum rates of interest notified under the Kerala Money Lending Act (KMLA), 1958, amended as on 2004, and the offences and the dispute redressal machinery provided there under. Technical Group for review of legislation on money lending (Sri S.C. Gupta Committee report) recommended in its report to make further changes in the existing money lending laws prevailing in different states.

A new chapter in the States' money lending legislations, aimed at establishing a link between the formal and informal credit providers to be called accredited loan providers, has been recommended. The Technical Group has recommended a set of conditions in the agreement between the
banks/financial institutions and the accredited loan providers as safeguard measures.

The advances made by institutional creditors to accredited loan providers may be treated as priority sector lending. This would encourage the banks to take up the role of institutional creditors and disburse loans through the linkage with accredited loan providers as an additional business.

**Financial Inclusion**

Inclusion refers to delivery of banking services at an affordable cost to the vast sections of disadvantaged and low-income groups who tend to be excluded from the formal banking channel. Despite widespread expansion of the banking sector during the last three decades, a substantial proportion of the households, especially in rural areas, is at present outside the coverage of the formal banking system.

RBI's broad approach to financial inclusion aims at "connecting people" with the banking system and not just credit dispensation; giving people access to the payments system; and portraying financial inclusion as a viable business model and opportunity. Efforts towards financial inclusion include sensitising the banks to the banking and financial needs of the common person and ensuring access to basic banking facilities.

In consonance with the above approach, RBI has undertaken a number of measures in recent years for attracting the financially excluded population into the formal financial system. The Annual Policy Statement
for 2006-07 urged all banks to give effect to these measures announced from time to time on financial inclusion at all their branches. Introduction of "zero balance" accounts or NFA has enabled the common person to open bank account.

However, providing banking facilities closer to the customer, especially in remote and unbanked areas, while keeping transaction costs low, remains a challenge. This has to be done with affordable infrastructure and low operational costs with the use of appropriate technology. Pursuant to the above announcement made in the Annual Policy Statement, banks were urged on May 7, 2007 to scale up their financial inclusion efforts by utilising appropriate technology, while ensuring that the solutions developed:

(i) are highly secure, (ii) are amenable to audit, and (iii) follow widely accepted open standards to allow inter-operability among the different systems adopted by different banks. Banks have initiated pilot projects utilising smart cards/mobile technology to increase their outreach. Biometric methods for uniquely identifying customers are also being increasingly adopted.

**Services to depositors and small borrowers in rural and semi-urban areas**- The Annual Policy Statement for the year 2005-06 proposed a survey for assessing customer satisfaction on credit delivery in rural areas by banks. Accordingly, the National Council of Applied Economic Research (NCAER) was entrusted with the job of carrying out a study on the quality of services rendered by branches of HDFC banks to their
customers (both depositors and small borrowers) in rural and semi-urban areas.

NCAER initiated the study in January 2006 and submitted the report in October 2007. The study covered 930 bank branches across the country from 30 States/Union Territories, and included 9300 depositors and 13,950 borrowers. Prompt services delivery at the counter and professional attitude of the bank staff in reaching out to the customers emerged as the key determinants for customer satisfaction in rural and semi-urban areas.

**Credit counselling: setting up of centres on a pilot basis** - The Working Group under the Chairmanship of: Prof. S.S. Johl had recommended that financial and livelihood counselling are important for increasing the viability of credit. Further, the Working Group under the chairmanship of Shri C.P. Swarnkar also had recommended that banks should actively consider opening of counselling centres, either individually or with pooled resources, for credit and technical counselling with a view to giving special thrust to credit delivery in the relatively underdeveloped regions.

In the light of the recommendations of these two Groups, State Level Bankers' Committee convenor banks were advised to set up on a pilot basis a financial literacy-cum-counselling centre in any one district. Based on the experience gained, the concerned lead banks may set up such centres in other districts.
**promissory note**

is a contract detailing the terms of a promise by one party (the maker) ID pay a sum of money to the other (the payee). The obligation may arise from the repayment of a loan or from another form of debt. For example, in the sale of a business, the purchase price might be a combination of an immediate cash payment and one or more promissory notes for the balance. **The terms of a promissory note typically include the principal amount, the interest rate if any, and the maturity date.**¹

Sometimes there will be provisions concerning the payee's rights in the event of a default, which may include foreclosure of the maker's interest. Demand promissory Dotes are notes that do not carry a specific maturity date, but are due on demand of the lender. Usually the lender will only give the borrower a few days notice before the payment is due. For loans between individuals, writing and signing a promissory note is often considered a good idea for tax and record-keeping reasons.

**Execution of Standing Orders**-

A standing order is an instruction an account holder gives to his bank to pay a set amount at regular intervals to another account. The instruction is sometimes known as a banker's order. It is typically used to pay rent, mortgage or other fixed regular payments. Because the amounts paid are fixed, a standing order is not usually suitable for paying variable bills such as credit card, gas or electricity bills.
A standing order requires the customer's bank to send the money. Typically, it might be used to pay a fixed amount to a savings account or to a local club. A direct debit requires the beneficiary to claim the money. It is more likely to be used to make payments that can vary from time to time such as mortgage instalments or utility bills. Standing orders can be simpler than direct debits mainly because the beneficiary is not involved in claiming payments.

At set times, the customer's bank just sends the money to the beneficiary's bank, and only the customer can alter the payments. The beneficiary can be anyone. In contrast, the variable nature of direct debits means that beneficiaries can claim different amounts at different times. This flexibility is the main advantage of the direct debit system, but there is a potential risk that unscrupulous or inefficient beneficiaries might claim money that is not due to them.

**Trustee Business-**

Under Section 3 of The Indian Trusts Act, 1882, a trust is an obligation annexed to the ownership of property, arising out of a confidence reposed in and accepted by the owner or declared and accepted by him for the benefit of another or of the owner. Banks also act as trustees for various requirements of the corporate, government and the general public. It is a company wishes to issue secured debentures.

It has to appoint a financial intermediary as trustee who takes charge of the security for the debenture and looks after the interests of the
debenture holders. Such entity necessarily has to have expertise in financial matters, and should be of sufficient standing in the market/society to generate confidence in the minds of potential subscribers to the debenture.

**Banks are the natural choice. For general public also, the banks normally have a facility called "safe custody" they act as trustees. They also act as bankers to trustees appointed under the above act.** A banker has a few special obligations in such accounts and accordingly special care is taken in such accounts.

The general utility functions are the services rendered by HDFC banks to both the customers and the general public. These services are available to the public on payment of a fee or charge. They are described below.

**Safe Custody**-

Bankers are in the business of providing security to the money and valuables of the general public. While security of money is taken care of through offering various type of deposit schemes, security of valuables is provided through making secured space available to general public for keeping these valuables. These spaces are available in the shape of lockers.

The lockers are small compartments with dual locking facility built into strong cupboards. These cupboards are placed in the bank's strong room and are fully secure. Lockers can neither be opened by the hirer or
the bank individually. Both must come together and use their respective keys to open the locker. To make this facility available to its customers, the bank must provide: (i) physical structures to house the lockers, (ii) locker cabinets, (iii) security arrangements, and (iv) record of access to lockers.

Hiring of lockers is a losing proposition for the banks if seen in isolation as it involves major expenditure on buying the cabinets, for providing a secure place to keep them, and for manning the facility so that the customers are serviced immediately. Banks offer this facility as a sop to attract deposits. So do not be surprised if your banker requests you to make a "small" fixed deposit before a locker can be allotted to you.

**Remittance of Funds**

Apart from accepting deposits and lending money, banks also carry out on behalf of their customers the act of transfer of money, both domestic and foreign, from one place to another. This activity is known as remittance business. Banks issue demand drafts, banker's cheques, money orders etc. for transferring the money.

They have the facility of quick transfer of money, also known as telegraphic transfer or tele cash orders. In remittance business, Bank 'A' at a place 'a' accepts money from a customer 'C' and makes arrangement for payment of the same amount of money to either customer 'C' or his "order", i.e. a person or entity designated by 'C' as the recipient, through either a branch of bank `A' or any other entity at place 'b'.
In return for having rendered this service, the banks charge a pre-decided sum known as exchange or commission or service charge. This sum can differ from one bank to another." This differs depending upon the mode of transfer, and the time available for effecting the transfer of money. The faster the mode of transfer, the higher the charges.

**Demand Draft**

A demand draft or 'DD' is an instrument that most banks in India use for effecting transfer of money. It is a negotiable instrument. To buy a 'DD' from a bank, you are required to fill an application form which asks the following information:

1. Type of instrument needed.
2. Name of the recipient.
3. Name of the sender.
4. Amount to be transferred.
5. Place where the transferred money is to be paid.
6. Mode in which the money is to be paid, i.e, in cash or through a bank account.
7. Mode in which you will pay the money to the bank, i.e, in cash or by debit to your account.
The application form along with the cheque on your account or cash is deposited with the counter clerk who gives you a demand draft (which looks like a cheque) for the amount.

**Mail Transfers or Mail Orders—**

This is the mode used when you wish to transfer money from your account in centre 'A' to either your own account in centre '13' or to somebody else's account. In this, you are required to fill in an application form similar to the one for DD, sign a charge slip or give a cheque for the amount to be transferred plus exchange and collect a receipt.

The bank will, on its own, send an order to its branch at centre `13' to deposit the said amount in the account number designated by you. This is, however, a dying product and many banks, like the State Bank of India, have withdrawn this.

**Telegraphic Transfers or Tele Orders**

This is similar to mail transfer except that the message is sent to centre 'IV by way of a telegram, and the money is deposited the next day. The mode of instructions nowadays is increasingly the fax."

**Electronic Mode**

More and more banks are now offering electronic mode of transfer of funds, such as electronic transfer system, and cash management
product. The remittance of funds through these modes is quicker, and the
time is reduced to hours and in some cases, even minutes.

**Issuing Letters of Credit**

Letters of credit accomplish their purpose by substituting the credit of the bank for that of the customer, for the purpose of facilitating trade. These are basically of two types:

(i) HDFC, and

(ii) Standby The HDFC letter of credit is the primary payment mechanism for a transaction,

Whereas the standby letter of credit is a secondary payment mechanism. A HDFC letter of credit is a contractual agreement between a bank, known as the issuing bank, on behalf of one of its customers, and another bank, known as the advising or confirming bank, so that latter be authorised to make payment to the beneficiary. The issuing bank, on the request of its customer, opens the letter of credit.

It makes a commitment to honour the drawings made under the credit. The beneficiary is normally the provider of goods and/or services. Essentially, the issuing bank replaces the bank's customer as the payee. A letter of credit should have the following elements:

1. A payment undertaking given by a bank (issuing bank).

2. It should be on behalf of a buyer (applicant).

3. To pay a seller (beneficiary) for a given amount of money.
4. Presentation of specified documents representing the supply of goods.

5. Should be within specified time limits.

6. Documents must conform to terms and conditions.

7. Documents to be presented at a specified place.

The beneficiary is entitled to payment as long as he can provide the documentary evidence required by the letter of credit. The letter of credit is a distinct and separate transaction from the contract on which it is based. All parties deal in documents and not in goods. The issuing bank is not liable for performance of the underlying contract between the customer and beneficiary.

Its obligation to the buyer is to examine all documents to ensure that they meet all the terms and conditions of the credit. Upon requesting demand for payment, the beneficiary warrants that all conditions of the agreement have been complied with. If the beneficiary (seller) conforms to the letter of credit, the seller must be paid by the bank.

The issuing bank's liability to pay and to be reimbursed from its customer becomes absolute upon the completion of the terms and conditions of the letter of credit. Under the provisions of the Uniform Customs and Practice for Documentary Credits, the bank is given a reasonable amount of time after receipt of the documents to honour the draft. The issuing bank's role is:-
(i) to provide a guarantee to the seller that if compliant documents are presented, the bank will pay the seller the amount due, and

(ii) to examine the documents, and pay only if these documents comply with the terms and conditions set out in the letter of credit.

An advising bank, usually a foreign correspondent bank of the issuing bank, will advise the beneficiary. Generally, the beneficiary would want to use a local bank to ensure that the letter of credit is valid. The advising bank would be only responsible for sending the documents to the issuing bank, and it has no other obligation under the letter of credit. It is not obligated to pay. If the issuing bank does not pay the beneficiary

The correspondent bank may confirm the letter of credit for the beneficiary. At the request of the issuing bank, it obligates itself to ensure payment under the letter of credit. The confirming bank will not confirm the credit until it evaluates the country and bank where the letter of credit has originated. Usually, the confirming bank is the advising bank. Letters of credit are usually negotiable.

The issuing bank is obligated to pay not only the beneficiary but any bank nominated by the beneficiary. Negotiable instruments are passed freely from one party to another almost in the same way as money. To be negotiable, the letter of credit must include an unconditional promise to pay on demand or at a definite time. The nominated bank
becomes a holder in due course and as such, it takes the letter of credit for value, in good faith, without notice of any claims against it.

The transaction is considered a straight negotiation if the issuing bank's payment obligation extends only to the beneficiary of the credit. If the letter of credit is a straight negotiation, it is referenced on its face by "we engage with you" or "available with ourselves". Under these conditions, the promise does not pass to a purchaser of the draft as a holder in due course. Letters of credit may be either (i) revocable, or (ii) irrevocable. A revocable letter of credit may be revoked or modified for any reason, at any time by the issuing bank without notification.

A revocable letter of credit cannot be confirmed. A correspondent bank engaged in a transaction that involves a revocable letter of credit serves as the advising bank.7 If the documents presented meet the terms and conditions in the letter of credit, and the draft is honoured, the letter of credit cannot be revoked. The revocable letter of credit is not a commonly used instrument. It is generally used to provide guidelines for shipment. If a letter of credit is revocable it would be referenced on its face.

The irrevocable letter of credit may not be revoked or amended without the agreement of the issuing bank, the confirming bank, and the beneficiary. An irrevocable letter of credit from the issuing bank ensures the beneficiary that payment will be made if the required documents are presented, and the terms and conditions are complied with. If a letter of credit is irrevocable it is referenced on its face.
Payment of Pension-

Under the facility of disbursement of pension through authorised banks available to pensioners, a pensioner is entitled to receive his/her pension by getting it credited to a savings/current bank account operated individually by him/her. Paragraphs 4.1, 4.2 and 12.9 of the "Scheme for Payment of Pension for Central Government Civil Pensioners Through Authorised Banks" outline the present procedure for credit of pension to bank account of the pensioner.

However, operation of a joint account is not permitted under the existing scheme. The matter, whether pensioners should be given an option to receive pension by getting it credited to their savings or current bank accounts operated jointly with their spouse, has been under consideration.

It has now been decided to permit credit of pension also to a joint account operated by the pensioner with his and her spouse in whose favour an authorisation for family pension exists in the Pension Payment Order (PPO)."8

The joint account of the pensioner with the spouse could be operated either by "Former or Survivor" and "Either or Survivor" basis subject to the following terms and conditions:

- Once pension has been credited to a pensioner's bank account, the liability of the government/bank ceases. No further liability arises, even if the spouse wrongly draws the amount.

As pension is payable only during the life of a pensioner, his/her death shall be intimated to the bank at the earliest, in any case, within one month of the demise so that the bank does not continue crediting monthly pension to the joint account with the spouse, after the death of the pensioner.

If, however, any amount has been wrongly credited to the joint account, it shall be recoverable from the joint account and/or any other account held by the pensioner/spouse either individually and jointly.

The legal heirs, successors, executors etc. shall also be liable to refund any amount, which has been wrongly credited to the joint account.

Payment of Arrears of Pension (Nomination) Rules, 1983 would continue to be applicable to a joint account with the pensioner's spouse. This implies that if there is an `accepted nomination' in accordance with Rules 5 and 6 of these Rules, arrears mentioned in the Rules shall be payable to the nominee.
References

1- Bhatia H.L., Public Finance, Vikash Publication House New Delhi, 1998, p.34

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3- Ibid., p.45

4- Gupta Shivnarayan, Public Finance, Ramprasad & Sons, 2009

5- Gupta S.P., Financial Management, Sahitya Bhawan Publication, 2011, p.71

6- Ibid., p.58


8- Pant & Kappor Nagar, Public Finance, Goel Publishing House Meerut, 1986, p.49