

“Banking”



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CURTAIN RAISERS TO THE COURSE

- ◎ Evolution of Banking
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BANKING BUSINESS & REGULATION

- ⦿ Discussion on Basic Banking business
- ⦿ Present Scenario
- ⦿ Constitution of Banks
- ⦿ Regulation of Banks
- ⦿ Regulation of Board of Directors of Banks by RBI & SEBI

BANKING

Definition of Banking:

- ◎ No exhaustive definition in common law. The usual characteristics are:
 - > The conduct of current accounts;
 - > Payment of cheques; and
 - > The collection of cheques for customers.
- ◎ However, this is not equivalent to a definition and these are not the sole characteristics- *Paget's Law of Banking*, 12th edn. at 107-109.

BANKING

The Law Lexicon defines Banking as the business or employment of a banker, the business of establishing a common fund for lending money, discounting notes, issuing bills, receiving deposits, collecting the money or notes deposited, negotiating the bills of exchange. It is wide enough to embrace every transaction coming within the legitimate business of a banker e.g. lending money on security of goods or documents (*Tennant V. Union Bank of Canada, 1894, AC 31*)

EVOLUTION OF BANKING

PRESIDENCY BANKS

- Establishment of the Bank of Calcutta in Calcutta on 2 June 1806. It was Re-designed as the Bank of Bengal (2 January 1809) as the first joint-stock bank of British India sponsored by the Government of Bengal. The Bank of Bombay (15 April 1840) and the Bank of Madras (1 July 1843) followed the Bank of Bengal.
- Primarily Anglo-Indian creations, the three presidency banks came into existence either as a result of the compulsions of imperial finance or by the felt needs of local European commerce and were not imposed from outside in an arbitrary manner to modernise India's economy. Their evolution was, however, shaped by ideas culled from similar developments in Europe and England, and was influenced by changes occurring in the structure of both the local trading environment and those in the relations of the Indian economy to the economy of Europe and the global economic framework.

INNOVATION IN BANKING

The establishment of the Bank of Bengal marked the advent of limited liability, joint-stock banking in India. So was the associated innovation in banking, viz. the decision to allow the Bank of Bengal to issue notes, which would be accepted for payment of public revenues within a restricted geographical area. It meant an accretion to the capital of the banks, a capital on which the proprietors did not have to pay any interest. The concept of deposit banking was also an innovation because the practice of accepting money for safekeeping (and in some cases, even investment on behalf of the clients) by the indigenous bankers had not spread as a general habit in most parts of India. But, for a long time, and especially upto the time that the three presidency banks had a right of note issue, bank notes and government balances made up the bulk of the investible resources of the banks.

GOVERNANCE

The three banks were governed by royal charters, which were revised from time to time. Each charter provided for a share capital, four-fifth of which were privately subscribed and the rest owned by the provincial government. The members of the board of directors, which managed the affairs of each bank, were mostly proprietary directors representing the large European managing agency houses in India. The rest were government nominees, invariably civil servants, one of whom was elected as the president of the board.

The Business of the Banks

It was initially confined to discounting of bills of exchange or other negotiable private securities, keeping cash accounts and receiving deposits and issuing and circulating cash notes.

Loans were restricted to Rs. 1 lakh and the period of accommodation confined to three months only. The security for such loans was public securities, commonly called Company's Paper, bullion, treasure, plate, jewels, or goods 'not of a perishable nature' and no interest could be charged beyond a rate of twelve per cent. Loans against goods like opium, indigo, salt wool, cotton, cotton piece goods, mule twist and silk goods were also granted but such finance by way of cash credits gained momentum only from the third decade of the nineteenth century. All commodities, including tea, sugar and jute, which began to be financed later, were either pledged or hypothecated to the bank. Demand promissory notes were signed by the borrower in favour of the guarantor, which was in turn endorsed to the bank. Lending against shares of the banks or on the mortgage of houses, land or other real property was, however, forbidden.

The Business of the Banks

Indians were the principal borrowers against deposit of Company's paper, while the business of discounts on private as well as salary bills was almost the exclusive monopoly of individuals Europeans and their partnership firms. But the main function of the three banks, as far as the government was concerned, was to help the latter raise loans from time to time and also provide a degree of stability to the prices of government securities.

Major change in the conditions

With the passing of the Paper Currency Act of 1861, the right of note issue of the presidency banks was abolished and the Government of India assumed from 1 March 1862 the sole power of issuing paper currency within British India. The task of management and circulation of the new currency notes was conferred on the presidency banks and the Government undertook to transfer the Treasury balances to the banks at places where the banks would open branches. None of the three banks had till then any branches (except the sole attempt and that too a short-lived one by the Bank of Bengal at Mirzapore in 1839) although the charters had given them such authority. But as soon as the three presidency banks were assured of the free use of government Treasury balances at places where they would open branches, they embarked on branch expansion at a rapid pace. By 1876, the branches, agencies and sub agencies of the three presidency banks covered most of the major parts and many of the inland trade centres in India. While the Bank of Bengal

Presidency Banks Act

The presidency Banks Act, which came into operation on 1 May 1876, brought the three presidency banks under a common statute with similar restrictions on business. The proprietary connection of the Government was, however, terminated, though the banks continued to hold charge of the public debt offices in the three presidency towns, and the custody of a part of the government balances. The Act also stipulated the creation of Reserve Treasuries at Calcutta, Bombay and Madras into which sums above the specified minimum balances promised to the presidency banks at only their head offices were to be lodged. The Government could lend to the presidency

Presidency Banks Act

The decision of the Government to keep the surplus balances in Reserve Treasuries outside the normal control of the presidency banks and the connected decision not to guarantee minimum government balances at new places where branches were to be opened effectively checked the growth of new branches after 1876. The pace of expansion witnessed in the previous decade fell sharply although, in the case of the Bank of Madras, it continued on a modest scale as the profits of that bank were mainly derived from trade dispersed among a number of port towns and inland centres of the presidency.

Rapid Commercialisation

- India witnessed rapid commercialisation in the last quarter of the nineteenth century as its railway network expanded to cover all the major regions of the country. New irrigation networks in Madras, Punjab and Sind accelerated the process of conversion of subsistence crops into cash crops, a portion of which found its way into the foreign markets. Tea and coffee plantations transformed large areas of the eastern Terrains, the hills of Assam and the Nilgiris into regions of estate agriculture par excellence. All these resulted in the expansion of India's international trade more than six-fold. The three presidency banks were both beneficiaries and promoters of this commercialisation process as they became

Evolution of the Regulator

Imperial Bank and the Reserve Bank of India

- The presidency Banks of Bengal, Bombay and Madras were merged in 1921 to form the Imperial Bank of India.
- The RBI was established on April 1, 1935 in accordance with the provisions of the Reserve Bank of India Act, 1934.
- The establishment of the RBI as the central bank of the country in 1935 ended the quasi-central banking role of the Imperial Bank by converting it into a purely commercial bank through an act passed in Parliament in May 1955 and the State Bank of India was constituted on 1 July 1955.

RBI in Government Control

- The RBI Act passed in 1934 constituted RBI as an apex bank without major government ownership. Banking Regulations Act was passed in 1949. This regulation brought Reserve Bank of India under government control. Under the act, RBI got wide ranging powers for supervision & control of banks. The Act also vested licensing powers & the authority to conduct inspections in RBI.
- In 1959, SBI took over control of eight private banks floated in the erstwhile princely states, making them as its 100% subsidiaries

Set up of Banks (which were later nationalised)

Prior to RBI

- 1865 Allahabad Bank
- 1895 Punjab National Bank
- 1906 Bank Of India
- 1906 Corporation Bank
- 1907 Indian Bank
- 1908 Bank Of Baroda
- 1908 Punjab & Sindh Bank
- 1910 Canara Bank
- 1911 Central Bank of India
- 1920 Union Bank of India
- 1923 Andhra Bank
- 1925 Syndicate Bank

Set up of Banks (which were later nationalised)

Based on RBI licence

1935 Bank of Maharashtra

1937 Indian Overseas Bank

1937 Vijaya Bank

1938 Dena Bank

1938 UCO Bank

1943 Oriental Bank of Commerce

1950 United Bank of India (formed by merger of 4 small banks in Bengal)

Case Study and Research No. I for Course Participants

“EVOLUTION OF BANKING AND CONSOLIDATION IN THE INDIAN BANKING SECTOR”

- Should be of atleast of 15,000 words and additionally supported by annexures of atleast 3 detailed practical cases in Indian banking industry and 2 global cases

Nationalisation

Nationalisation

- By the 1960s, the Indian banking industry became an important tool to facilitate the development of the Indian economy and a large employer, and a debate ensued about the possibility to nationalize the banking industry. Indira Gandhi, the-then Prime Minister of India expressed the intention of the Government in the annual conference of the All India Congress Meeting in a paper entitled "*Stray thoughts on Bank Nationalisation.*" and then nationalised the 14 largest commercial banks with effect from the midnight of July 19, 1969. 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 9th August, 1969.
- A second dose of nationalisation of 6 more commercial banks followed in 1980. The stated reason for the nationalisation was to give the government more control of

Summary of Arguments - For Nationalization of Banks

1. To achieve the socialist pattern of functioning within the society.
 - In order to serve better the needs of development of the economy in conformity with the national policy and objective.
 - Nationalization will channelise the credits to important areas like agriculture, small-scale and exports and banking units will expand in rural areas

2. Rules being violated
 - Restrictions imposed by social control measures were capable of being flouted-the purpose was to **curb indirect influence** (e.g. the restraints on the advances to directors and their interested concerns could be mutually adjusted amongst bankers in such way that the purpose of such restraints is lost).

Summary of Arguments - Against Nationalization of Banks

1. Refuted the findings of the arguments in favour of nationalization of banks
 - (The credit given to agriculture increased from 30 crores to 97 crores)
2. To short period to judge the results of “social control”
 - (168 days from 1-2-1968 to 19-7-1969)
3. No pressing need to confirm to a social pattern of functioning.
4. Criticised the Public Sector functioning
 - Shifting to public sector makes things from bad to worse
 - Pointed the lack of dynamism in public sector
 - Opens doors to corruption and favoritism
 - Due to lack of competition quality of services has dropped
 - Other charges made by the nationalized banks have increased progressively
5. Regarding foreign banks- it clearly stated that banking industry is not nationalized in all socialist countries.
6. No decision making power exercised due to the control by reserve

R.C. Cooper v. Union of India AIR 1970 SC 564

- (i) Banking - banking business - Sections 4, 5, 6, 15(2) and 22 of Banking Companies (Acquisition and Transfer of Undertaking) Act, 1969, Banking Companies (Acquisition and Transfer of Undertaking) Ordinance, 1969, Sections 5, 6 (1) and 27 of Banking Regulation Act, 1949 and Articles 14, 19, 19 (1), 31 and 31 (2) of Constitution of India - petitioner held shares and had accounts in certain banks - petitioner was also Director in one of these banks - Banking Companies (Acquisition and Transfer of Undertaking) Ordinance, 1969 was promulgated on 19.06.1969 - Ordinance provided for acquisition and transfer of undertakings of certain banking companies - named banks after being acquired by new banks had no managerial, administrative or other staff and was incompetent to use word "Bank" in its name - named banks were liable to be dissolved by a notification of a Central Government - Banking Companies (Acquisition and Transfer of Undertaking) Act, 1969 was introduced subsequently which replaced Ordinance with certain modifications - under

R.C. Cooper v. Union of India AIR 1970 SC 564

- principles for determination of compensation of named banks and manner of payment was also modified - petitioner claims that Act and Ordinance impair his fundamental rights guaranteed under Articles 14, 19 and 31 and are invalid - petitioner challenged Ordinance on grounds that it was promulgated in exercise of powers under Article 123 and was invalid since conditions precedent to exercise power did not exist - petitioner contended that in enacting Act Parliament encroached upon State List in Seventh Schedule of Constitution so it was outside legislative competence of Parliament - petitioner also challenged Act on grounds that it violated freedom of trade guaranteed under Article 301 of Constitution of India - Counsel for respondents contended that petitions are not maintainable as no fundamental right of petitioner was directly impaired by enactment of Ordinance and Act - counsel also contended that petitioner was not owner of property of named bank to be acquired by new bank so he was incompetent to maintain petitions complaining that his fundamental rights were impaired - Apex Court held that there was nothing on record to suggest that petitions were not maintainable - restrictions imposed upon rights of named banks to carry on non-banking business is unreasonable - interests of named banks and shareholders vitally affected by reason of transfer of undertaking - in pre-decided cases it was held that shareholders of a company competent to challenge invalid provisions infringing fundamental rights or causing direct injury - jurisdiction of Court to grant relief cannot be denied when by state action right of individual shareholder are

Case Study and Research No. II for Course Participants

- The Supreme Court ruled that action taken or deemed to be taken in exercise of powers under the Act was unauthorized !!
- Course Participants to research the basis settled by the Supreme Court for nationalisation.

Private Sector Banks

Private Sector Banks

- In 1980, government acquired 6 more banks with deposits of more than Rs.200 crores. Nationalisation of banks was to make them play the role of catalytic agents for economic growth. The Narsimham Committee report suggested wide ranging reforms for the banking sector in 1992 to introduce internationally accepted banking practices.
- Under the then Narsimha Rao government, the Banking Regulation Act was amended in 1993 which saw the entry of new private sector banks in India. (UTI Bank was the first private

Banking Business & Regulation

Discussion on Basic Banking business

Business of Banking

- In India, banking is defined in section 5 (b) of the BRA as:

“(b) ‘banking’ means the accepting, for the purpose of lending or investment, of deposits of money from the public, repayable on demand or otherwise, and withdrawable by cheque, draft, order or otherwise.”

- Under section 49A of the BRA, no person other than a bank is authorised to accept deposits withdrawable by cheque. The Savings Bank Scheme run by the Government, a Primary Credit Society and any other person notified by the government are exempted from this prohibition.

Section 6(1) of the Banking Regulation Act

Form and business in which banking companies may engage

- (a) the borrowing, raising, or taking up of money;
- (b) acting as agents for any government or local authority or any other person or persons;
- (c) contracting for public and private loans and negotiating and issuing the same;
- (d) the effecting, insuring, guaranteeing, underwriting, participating in managing and carrying out of any issue....
- (e) carrying on and transacting every kind of guarantee and indemnity business.....;
- (f) managing, selling and realising any property which may come into the possession of the company.....
- (g) acquiring and holding and generally dealing with any property which may form the security or part

Section 6(1) of the Banking Regulation Act
Form and business in which banking companies may
engage

- (h) undertaking and executing trusts;
- (i) undertaking the administration of estates as executor, trustee or otherwise;
- (j) establishing and supporting or aiding in the establishment and support of associations, institutions, funds, trusts and conveniences calculated to benefit employees or ex-employees.....
- (k) the acquisition, construction, maintenance and alteration of any building or works necessary or convenient for the purpose of the company;
- (l) selling, improving, managing, developing, exchanging, leasing, mortgaging,.... disposing of or turning into account or otherwise dealing with all or any part of the property and rights of the company;
- (m) doing all such other things as are incidental or conducive to the promotion or advancement of the business of the company;

How can one enter into banking business in India?

Section 22 of Banking Regulation Act, 1949 along with the RBI's rules have to be complied with:

- To carry on banking business, a license is required to be obtained from RBI.
- To obtain such license, an application in writing is to be made to RBI.
- RBI issues a license when it is satisfied from a perusal of requisite records that the company is adequately solvent and that its affairs and general character of management are not prejudicial to public interest or interest of future depositors.
- In case of a company incorporated outside India, RBI is required to assure itself that the government or law of the country in which it is incorporated does not discriminate in any manner against the banking companies registered in India.
- As per the RBI guidelines for entry of new banks in private sector vide press release dated 22.01.1993, only a public

How can a banking company open a new place of business in India or change the location of its existing place of business?

- As per section 23(1) of the Banking Regulation Act, 1949, permission of RBI is required to:
 - open a new place of business in India;
 - change the location of an existing place of business;
 - open a new place of business outside India; or
 - change the location of existing place of business outside India.

Can a banking company engage in trade activity?

- As per section 8 of the Banking Regulation Act, 1949, a banking company is enjoined not to undertake any buying or selling or bartering of goods except in connection with the realisation of security given to or held by it. However, a trade activity connected with a bill of exchange is ³⁹ allowed to be

Can a banking company hold immovable property in India?

- As per section 9 of the Banking Regulation Act, 1949, a banking company is prohibited from holding immovable property except as required for its own use for any period exceeding seven years from the acquisition thereof. However, a banking company may within the above period of 7 years, deal with or trade in any property for facilitating the disposal thereof.

Can a banking company create a charge on its assets?

- Section 14 of the Banking Regulation Act, 1949 prohibits any creation of charge on unpaid capital of the banking company.
- However, in order to create a floating charge on its assets, a banking company is required to obtain a certificate from the RBI under section 14 A of the Banking Regulation Act, 1949 certifying that the charge is not detrimental to the interests of the company.
- Unless such certificate is issued, the charge would be invalid, However, in case the issue of certificate is refused, the aggrieved banking company may appeal to the Central Government within 90 days

Is there any restriction on opening of branches by a banking company?

- A banking company is free to open any number of branches subject to satisfaction of capital adequacy and prudential accounting norms and RBI's policy laid down from time

Present Scenario

Participants in Banking System

- The major participants of the Indian financial system are the commercial banks, the financial institutions (FIs), encompassing term-lending institutions, investment institutions, specialized financial institutions and the state-level development banks, Non-Banking Financial Companies (NBFCs) and other market intermediaries such as the stock brokers and money-lenders.

Present Scenario

- Currently , overall, banking in India is considered as 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 foreign banks.
- 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 are expected to be strong. M&As, takeovers, asset sales⁴⁵ and much more

Population

- According to the publication of RBI - "*A Profile of Banks 2006-2007*" India has a total of 81 Scheduled Commercial Banks (excluding regional rural banks) i.e. 29 foreign banks, 20 nationalised/public sector banks, 8 banks in the State Bank Group and 24 other scheduled commercial banks which includes private sector banks.

Constitution of Banks

Constitution of Banks

- ◎ Banks in India fall under one of the following categories:
 - > Body corporate constituted under a special statute (Public sector banks including nationalised banks, SBI and its associates (subsidiaries) and Regional Rural Banks)
 - > Company registered under the Companies Act, 1956 or a foreign company (Private banks and foreign banks)
 - > Co-operative society registered under a central or state enactment on co-operative societies.

RESERVE BANK OF INDIA

Central bank and supreme monetary authority

Scheduled banks

Commercial banks

Co-operatives

Foreign banks

Regional rural banks

Urban cooperatives

State cooperatives

Public sector banks

Private sector banks

Old

New

State bank of India and associate banks

Other nationalised banks

Constitution of Banks

- Public Sector banks

- › By the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 and Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980 the Central Government nationalised (took over the business undertakings) of certain banking companies and vested them in newly created statutory bodies (corresponding new banks) constituted under section 3 of the 1970/1980 Act. These banks are governed by the statutes creating them as also some of the provisions of the BRA and the RBI Act, 1934. (Important judgment pertaining to bank nationalisation - *R.C. Cooper v. UoI* AIR 1970 SC

Constitution of Banks

○ Banking Companies

- › A banking company as defined in section 5 (c) of the BRA is a company which transacts in the business of banking. Such a company may be a company constituted under section 3 of the Companies Act, 1956 or a foreign company within the meaning of section 591 of that Act.
- › All private sector banks are banking companies.
- › These banks are governed by the Companies Act, 1956 in respect of their constitution and by the BRA and the RBI Act with regard to their business of banking.

Constitution of Banks

- ◉ Cooperative banks - A cooperative bank is a cooperative society registered or deemed to have been registered under any Central Act relating to multi-state cooperative societies, or any other central or state law relating to cooperative societies.
 - > The Banking Laws (Application to Cooperative Societies) Act, 1965 extended certain provisions of the BRA and the RBI Act to the cooperative banking sector.

Constitution of Banks

- RBI as the Central Bank and Regulator of Banks [It is responsible for enforcing the two main legislations regulating banks in India – The Banking Regulation Act, 1949 (“BRA”) and The Reserve Bank of India Act, 1934 (“RBI Act”).]
- Government Regulation of Banks
- Regulation by other authorities.

Regulation of Banks in India

Regulation of Banks in India

- RBI is the sole authority for issue and management of currency in India under section 22 of the RBI Act.
- RBI is the banker to the Central Government under section 20 of the RBI Act and therefore it compulsorily must undertake banking business for the Central Government. However, in case of state governments, their banking business is undertaken by the RBI based on agreements as provided in section 21A. It

RBI as a Central Bank and Regulator of Banks

- RBI is the primary regulator of the banks in India. Role of RBI as a regulator of the banking sector is mainly because RBI has been entrusted with the enforcement of the provisions of the BRA. It has the power to license, appoint and remove banking boards/personnel, power relating to winding up and amalgamation and generally has wide ranging powers for regulation of banking business .
- The RBI also inspects banks and exercises supervisory powers, and may issue directions from time to time in public interest of the banking system with ⁵⁶ respect to interest rates

Government as a Regulator of Banks

- Apart from RBI, Central Government has also been conferred extensive powers under the RBI Act and BRA either directly or indirectly over banks.
- Under section 7 (1) of the RBI Act, it has the powers to issue directions to the RBI whenever considered necessary in public interest after consultation with the Governor-Thus, C. G. can exercise control over banks by influencing decision making of⁵⁷ RBI

Government as a Regulator of Banks

- C.G. also has the appellate authority in matters in which RBI has been conferred the power to decide at the first instance. For eg. Appeal lies to the C.G. for removal of managerial personnel under sections 10B and 36AA of the BRA and also in case of cancellation of banking license under section 22 of the BRA, etc.
- C.G. has the power to suspend the operation of BRA or to give exemption from any provisions of the BRA on recommendation/representation of the RBI under sections 4 and 53 of the BRA.
- It has the powers to notify other forms of business which a bank may undertake under section 6 (1) (o) of the BRA. Even rule making powers under sections 52 and 45Y are vested with the C.G.

Government as a Regulator of Banks

- Other powers of C.G.
 - › Approval for formation of subsidiary for certain business under section 19 of BRA;
 - › Notification of banks for the purpose of maintenance of assets under section 24(2);
 - › Notification with reference to accounts and balance sheet under section 29;
 - › Issue of directions for inspection of banks under section 35;
 - › Power to acquire undertakings of banks (section 36 AE);
 - › Appointment of court liquidator;
 - › Suspension of business and amalgamation of banks under section 45 of BRA.
- The above provisions confer wide powers on CG to regulate banks. These are in addition to the powers conferred on the government as majority shareholder or full owner of public sector banks under statutes constituting them.

Regulation by other authorities

- Section 6 of the BRA provides that banks may undertake certain non-banking business in addition to the business of banking (for eg. SEBI in respect of matters pertaining to dealings in securities like shares and debentures).
- Banks are also subject to control of authorities under the Companies Act, 1956 in respect of company matters. Similarly, a bank is answerable to labour authorities regarding labour issues.

Regulation of the Board of Directors of a Banking Company

Whole-time director

Basic Provisions under Companies Act

Every public company, or a private company which is a subsidiary of a public company, having a paid-up share capital of Rupees five crores must have a managing or whole-time director or a manager. (Under the entire Companies Act, 1956 the term manager does not mean a manager as we understand it normally like Assistant Manager/Deputy Manager/Senior Manager/Chief Manager. Manager under the Companies Act, 1956 means a person having substantial powers of the management of the company and one who is in control of the entire affairs of the company under the supervision of the board.

DIRECTORS

Basic Provisions under Companies Act

Every public company must have at least three directors. A public company having (a) a paid-up capital of five crore rupees or more; (b) one thousand or more small shareholders, can elect a director by small shareholders. Small shareholders means a shareholder holding shares of nominal value of twenty thousand rupees or less. A private company must have at least two directors.

A company can have a maximum number of twelve directors and to increase this number, the approval of Central Government is required.

A person cannot be a director of more than fifteen companies (excluding a private company, an unlimited company, an association not carrying on business for profit or which prohibits the payment of a dividend, alternate

Regulation of Board of Directors of Banks by SEBI and RBI

- December 1995 (CII), CII set up a task force to design a voluntary code of corporate governance
- April 1998 (CII), the Desirable Corporate Governance: A Code, was released
- 1999(SEBI) SEBI set up the Kumar Mangalam Birla Committee in 1999 to design a mandatory-cum-recommendatory code for listed companies
- February 2000(SEBI) Clause 49 in Listing agreement was introduced by circular no. 10 dated February 21, 2000 (on the basis of recommendation of Kumar Mangalam Birla committee report dated May 7, 1999). And it was made effective from March 31, 2001.

Regulation of Board of Directors of Banks by SEBI and RBI

- March 2000(SEBI) However SEBI had at that time exempted body corporates such as public and private sector banks, financial institutions, insurance companies and those incorporated under separate statute from the said clause.
- October 2001(RBI) The formal policy announcement in regard to corporate governance was first made by Dr. Bimal Jalan in the Mid-Term Review of the Monetary and Credit Policy on October 21, 2001. Pursuant to this announcement, a Consultative Group was constituted in November 2001 under the Chairmanship of Dr. A.S. Ganguly.

Regulation of Board of Directors of Banks by SEBI and RBI

- **2002(DCA)** DCA set up the Naresh Chandra Committee Report in 2002. The key recommendation related to financial and non-financial disclosures and independent auditing and board oversight of management.
- **2002(SEBI)** The Narayana Murthy Committee was set up by SEBI in 2002 to review clause 49 and suggest measures to improve corporate governance standards.
- **April 2002(RBI)** the Consultative Group of Directors of banks and FIs set up by Reserve Bank of India to review the supervisory role of Boards had submitted its report to RBI (Dr. Ganguly

Regulation of Board of Directors of Banks by SEBI and RBI

- **June 2002(SEBI)** SEBI proposed that the SEBI Committee's guidelines may be taken up for adoption by commercial banks listed in stock exchanges so that they can harmonize their existing **corporate governance** requirements with the requirements of SEBI, wherever considered appropriate.
- **June 2002(RBI)** RBI issued a circular to the effect that the recommendations of Dr Ganguly Group be placed before the Board of Directors of the bank and based on the decision taken by the Board, the recommendations can be adopted and implemented in the Bank

Regulation of Board of Directors of Banks by SEBI and RBI

- August 2003 (SEBI) The revised clause 49 was introduced vide circular no. 31 dated August 26, 2003 (on the basis of recommendation of N. R. Narayana Murthy committee report dated February 8, 2003)
- June 2004 (RBI) RBI stipulated 'Fit and proper' criteria for directors of banks w.e.f. June 25, 2004
- October 2004 (SEBI) New clause 49 issued vide SEBI Circular ⁶⁸no. 12 dated October

Regulation of Board of Directors of Banks by SEBI and RBI

- **February 2005 (RBI)** The RBI Circular dated February 28, 2005 on Guidelines on Ownership and Governance Structure emphasises the compliance on the RBI Circular on Dr Ganguly's Group recommendations read with the Fit and Proper criteria for directors stipulated vide RBI circular dated June 25, 2004.
- **March 2005(SEBI)** SEBI Circular no. 29 dated March 29, 2005 extended the date of compliance from April 1, 2005 to
1, 2006

Dr Ganguly Group's recommendation

A. Recommendations which may be implemented by all banks

- (i) Responsibilities of the Board of Directors
- (ii) Role and responsibility of independent and non-executive directors
- (iii) Training facilities for directors
- (iv) Submission of routine information to the Board
- (v) Agenda and minutes of the board meeting
- (vi) Committees of the Board
 - (a) Shareholders' Redressal Committee
 - (b) Risk Management Committee
 - (c) Supervisory Committee
- vii. Disclosure and transparency

Dr Ganguly Group's recommendation

B. Recommendations applicable only to public sector banks

- (i) Information flow
- (ii) Company Secretary

Dr Ganguly Group's recommendation

- C. Recommendations applicable only to private sector banks
 - ⦿ Eligibility criteria and 'fit and proper' norms for nomination of directors.
 - ⦿ Commonality of directors of banks and non banking finance companies (NBFC)
 - ⦿ Composition of the Board

Fit and proper criteria for Directors in private sector banks w.e.f. June 25, 2004

- (1) The banks in private sector should undertake a process of due diligence to determine the suitability of the person for appointment/continuing to hold appointment as a director on the Board, based upon qualification, expertise, track record, integrity and other fit and proper criteria. Banks should obtain necessary information and declaration from the proposed/existing directors for the purpose.
- (2) The process of due diligence should be undertaken by the banks in private sector at the time of appointment/renewal of appointment

Fit and proper criteria for Directors in private sector banks w.e.f. June 25, 2004

- (3) The boards of the banks in private sector should constitute Nomination "Committees" to scrutinize the declarations.
- (4) Based on the information provided in the signed declaration, Nomination "Committees" should decide on the acceptance and may make references, where considered necessary to the appropriate authority/persons, to ensure their compliance with the requirements

Fit and proper criteria for Directors in private sector banks w.e.f. June 25, 2004

- (5) Banks should obtain annually a simple declaration that the information already provided has not undergone change and where there is any change, requisite details are furnished by the directors forthwith.
- (6) The board of the bank must ensure in public interest that nominated/elected directors execute the deeds of covenants as

Qualifications of Directors under Banking Regulation Act

- Not less than fifty-one per cent of the total number of members of the Board of Directors of a banking company shall consist of persons, who shall have special knowledge or practical experience in respect of one or more of the following matters, namely, accountancy, agriculture and rural economy, banking, co-operation, economics, finance, law, small-scale industry, or any other matter the special knowledge of, and practical experience, which would, in the opinion of the Reserve Bank, be useful to the banking company

Qualifications of Directors under Banking Regulation Act

- Not less than two shall be persons having special knowledge or practical experience in respect of agriculture and rural economy, co-operation or small-scale industry; and shall not have substantial interest in, or be connected with, whether as employee, manager or managing agent of any company, not being a company registered under section 25 of the Companies Act, 1956 or any firm which carries on any trade, commerce or industry and which, in either case, is not a small-scale industrial concern, or be proprietors of any trading, commercial or industrial concern, not being a small-scale industrial concern

Whole Time Chairman & CEO permitted under Section 10B of the Banking Regulation Act

- *Notwithstanding anything contained in any law for the time being in force or in any contract to the contrary, every banking company.... shall have one of its Directors, who may be appointed on a whole-time or a part-time basis as Chairman of its Board of Directors, and where he is appointed on a whole-time basis as Chairman of its Board of Directors, he shall be entrusted with the management of the whole of the affairs of the banking company:*
- *PROVIDED that the Chairman shall exercise his powers subject to the superintendence, control and direction of the Board of Directors.*

Case Study and Research No. III for Course Participants

“IMPACT OF GLOBALISATION ON THE INDIAN BANKING SECTOR”

- Should be of atleast of 15,000 words and additionally supported by annexures of various novel retail as well as corporate banking products (in detail) evolved/evolving in the developed nations in the last five years

Any Questions.....

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Thank You