FOURTH REPORT

STANDING COMMITTEE ON FINANCE (1993-94)

(TENTH LOK SABHA)

MINISTRY OF FINANCE — BANKING DIVISION
WORKING OF THE PUBLIC SECTOR BANKS

Presented to Lok Sabha on 23 December, 1993
Laid in Rajya Sabha on 23 December, 1993

LOK SABHA SECRETARIAT
NEW DELHI

December, 1993/Agrahayana, 1915 (Saka)

F.C. No. 004

Price: Rs. 12.00

Published under Rule 382 of the Rules of Procedure and Conduct of Business in Lok Sabha (Seventh Edition) and printed by Manager, P.L. Unit, Government of India Press, Minto Road, New Delhi.

CONTENTS

COMPOSITION OF THE STANDING COMMITTEE ON FINANCE (1993-94)

Dr. Debiprosad Pal—*Chairman*

MEMBERS

Lok Sabha

2. Shri P. Chidambaram
3. Shri Magunta Subbarama Reddy
4. Prof. K.V. Thomas
5. Shri Chandulal Chandrakar
6. Dr. K.V.R. Chowdary
7. Shri Chhitubhai Gamit
8. Shri Prithviraj D. Chavan
9. Shri S.B. Sidnal
10. Smt. Maragatham Chandrasekhar
11. Shri P.C. Chacko
12. Shri Prakash V. Patil
13. Shri Mahendra Kumar Singh Thakur
14. Shri B. Akbar Pasha
15. Shri Sushil Chandra Varma
16. Shri Jeewan Sharma
17. Shri Chetan P.S. Chauhan
18. Shri Deeliphhai Sanghani
19. Shri Manabendra Shah
20. Shri Sartaj Singh Chhatwal
21. Shri Harin Pathak
22. Shri George Fernandes
23. Shri Abdul Ghafoor
24. Shri Srikanta Jena
25. Shri Satyapal Singh Yadav
26. Shri Nirmal Kanti Chatterjee
27. Prof. Susanta Chakraborty
28. Shri T.J. Anjalose
29. Shri Bhogendra Jha
30. Shri Kadambur M.R. Janardhanan

Rajya Sabha

*31. Vacant
32. Shri Krishna Kumar Birla
33. Shri Triloki Nath Chaturvedi
34. Shri Gurudas Das Gupta
35. Shri K.R. Jayadevappa

Note: * Dr. Murli Manohar Joshi resigned from the Membership of this Committee w.e.f. May 13, 1993, and Shri Labhshankar Bhatt, M.P. from Rajya Sabha retired from Rajya Sabha Membership. Both the vacancies have not yet been filled up.

36. Dr. Shrikant Ramchandra Jichkar
*37. Vacant
38. Shri Ghulam Rasool Matto
39. Shri Chimanbhai Mehta
40. Shri Kamal Morarka
41. Shri Rajubhai A. Parmar
42. Shri Ashis Sen
43. Shri Surinder Kumar Singla
44. Shri Arangil Sreedharan
45. Shri S. Vidhuthalai Virumbi

SECRETARIAT

1. Shri G.L. Batra — *Additional Secretary*
2. Shri Satish Loomba — *Deputy Secretary*
3. Shri P. K. Bhandari — *Under Secretary*

Note: * Dr. Murli Manohar Joshi resigned from the Membership of this Committee w.e.f. May 13, 1993, and Shri Labhshankar Bhatt, M.P. from Rajya Sabha retired from Rajya Sabha Membership. Both the vacancies have not yet been filled up.

INTRODUCTION

I, the Chairman of Standing Committee on Finance, having been authorised by the Committee to submit the Report on its behalf, present the Fourth Report on the Ministry of Finance, Department of Economic Affairs (Banking Division) relating to 'Working of the Public Sector Banks'.

2. As the banks play an important role in the mobilisation of resources for the overall development of the economy, the Committee took up the examination of the working of the banks in depth. The Committee has suggested some measures for improvement in the functioning of the public sector banks.

3. The Committee took oral evidence of the representatives of the Banking Division, Department of Economic Affairs of the Ministry of Finance and the Reserve Bank of India on the 2nd and 16th July, 1993 on the working of the banking system.

4. In dealing with the question of audit of banks, the Committee felt that the audit of accounts of Banks needs to be improved so as to avoid system failures and financial scandals. The Committee, has recommended, *inter-alia*, that the frequency of Statutory audit of the branches of banks should be increased from the present once in three years to atleast once in two years. The Committee has also recommended that the audit of public sector banks should be brought within the purview of the Comptroller and Auditor General of India as is the case with other public sector undertakings.

5. The Committee has noticed that in the recent past, cases of frauds and malpractices in the banks have increased. It has, therefore, recommended that there should be a separate independent authority for vigilance in banks, the staff for which should be from outside the banks. The Chief Vigilance Officers should be appointed by RBI or CVC from outside, and should have a separate channel of promotion.

6. The Committee has also examined the functioning of Regional Rural Banks and has felt unhappy over the sad plight of the RRBs. The financial position of these banks is deteriorating and the Government appears to be complacent in improving the viability of these banks. The Committee has recommended that the Government should examine the question of reducing the number of RRBs by way of merger etc. to make them viable. As the main objective of the Rural Banks is to meet credit needs of the weaker sections of society in rural areas, the Committee has recommended that a 'National Rural Bank of India' should be set up and all RRBs should be brought under its control.

7. The Committee also examined the questions of privatisation and merger of banks, but owing to paucity of time at its disposal, it could not finalise the issue. This will be dealt separately at a later date.

8. The Committee wishes to express its thanks to the Ministry of Finance for furnishing the desired information.

9. The Committee considered and adopted this Report in its meeting held on 14.12.1993. For facility of reference, the recommendations/observations of the Committee have been printed in thick type.

NEW DELHI;
15, *December*, 1993
24 *Agrahayana*, 1915 (Saka)

DR. DEBIPROSAD PAL,
Chairman,
Standing Committee on Finance.

CHAPTER I

AUDIT OF ACCOUNTS OF BANKS

1.1 Banks play a crucial role in the all round development of the country and an efficient banking system is an important input in its economic infrastructure. Since the mobilisation of public savings and its channelisation for productive uses is necessary, the country's economy cannot reach the take off stage in the absence of a good banking system. Despite commendable progress made by the banks in India in terms of expansion of branches and diversification of activities, the nationalised banks have been facing serious problems in the last few years because of accumulating lossess and consequent erosion of capital. The recent securities scam and other frauds have tended to shake the public confidence in the entire banking system. It is in this context that the Standing Committee on Finance examined the question of audit of Banks.

1.2 The Committee took oral evidence of the representatives of the Banking Division Department of Economic Affairs of the Ministry of Finance and the Reserve Bank of India on 2nd and 16th of July, 1993 on the working of the banking system.

1.3 While explaining to the Committee the present system of audit of banks, the representatives of the Banking Division and the Reserve Bank of India stated that the audit of the annual accounts of banks is done by statutory auditors whose appointment is approved by the Government of India. The criteria for empanelment of Auditors are drawn up by a Standing Advisory Committee of the Reserve Bank of India which has representatives from RBI, Banking Department of the Union Government C&AG and NABARD. The Committee meets sometime in July or August every year and draws up criteria for empanelment of auditors. This Committee also recommends the remuneration and other benefits receivable by the auditor. Once the criteria are approved, then the Comptroller & Auditors General is requested to give the names of all the audit firms which satisfy the criteria. The list is then sent to the Banking Department for their approval. After the approval of the Government, the names are forwarded to the different banks for the appointment of those auditors by the Board of Directors of the Banks. The tenure of each firm of auditors is normally 4 years but with respect to each institution which is audited, all the auditors are not the same. Every year a number of additions and deletions in the pannel are made to rotate the auditors as well as to maintain some continuity.

1.4 The witnesses further explained that the statutory auditors do the audit at the head office of the banks and do not look into the aspect of individual accounts. They submit their report which is known as the Long From Audit Report (LFAR) introduced in 1985. LFAR is submitted after the accounts are audited but it does not appear alongwith the balance sheet. The Central auditors make a report to the Central Government taking into account the broad directions in the conduct of audit.

1.5 In reply to a question from the Committee whether the audit checks that the amount was actually spent for the purpose for which it was advanced, the witness stated that the statutory auditors do not look into it. However, this is done by a large number of branch auditors who look into the accounts of the branches. They also look into the general performance of the banks and there are comments offered by the branch officers. These are put together by the Statutory Central Auditors. As for periodicity of the audit, the witness explained, that the large branches which have a business turnover of Rupees One Crore and above, are audited branch auditors every year. The remaining branches are audited once in three years by rotation. In addition, there is a continuing system of auditing by the Bank's internal audit every 12 to 18 months.

1.6 In reply to another query of the Committee whether any special instructions were issued to the auditors to examine the heavy amounts advanced by the banks and the use to which those were put, the witness explained that the Government were considering the recommendation of the Ghose Committee in frauds to introduce the system of concurrent audit for very large branches. The Government also proposed to have a Board for Supervision under the aegis of Reserve Bank of India dealing specifically with audit to bring about uniformity in audit system of all the banks. Reacting to the suggestion that the audit of banks be put under the control of the Comptroller and Auditor General of India, the witness so stated that it may not serve the desired purpose. It may result in pushing down the loans to some extent as the lending would them become very difficult. An element of discretion in lending money was inevitable and the question was to see whether there was any subjectivity in granting loans. Moreover, the private banks and the foreign banks could not be brought under the purview of C&AG, according to the witness.

1.7 The Committee were told that the Long From Audit Reports (LFAR) deal with the actual working of systems and procedures in the banks including the measures of internal control etc. On being asked as to what procedures existed for monitoring the receipt of these Long From Audit Reports, action taken by the banks on the irregularities mentioned therein, the witnesses from R.B.I. could not give a satisfactory answer.

1.8 The Committee note with concern the frauds and irregularities that have taken place in the banking system in the recent past. There appears to be a total failure of audit in banks. The Committee feels that the audit of accounts in Banks needs to be improved so as to avoid system failures and financial scandals. The Committee, therefore, recommends that the frequency of audit of banks should be increased from the present once in three years to atleast once in two years. It should be ensured that efforts are made to cover maximum number of branches. The norm regarding annual audit of large branches should be followed scrupulously. The RBI should take initiative to see that audit reports are properly scrutinised and are complied with by the bank management. The system of follow up the corrective action on these reports should be strengthened. A time limit should be fixed for compliance of audit objections. In the context of rising frauds and irregularities, the Committee is of the view that a detailed audit which operates simultaneously with the transcations will be very useful. The Committee, therefore, recommend that the concurrent audit of large branches should be introduced immediately. The Committee further recommends that the Standing Advisory Committee of RBI should also evaluate the performance of audit firms and any acts of omissions and commissions on their part should be strictly dealt with.

1.9 The Committee strongly recommends that Parliamentary accountability of Banks should be enforced through audit of Banks by Comptroller & Auditor General of India for which the modalities should be worked out at the earliest. In this context, the Committee are at a loss to understand as to why the entire banking and financial sector of the economy has been kept outside the purview of C&AG audit. The Committee is not happy to note that the entire nationalised banking sector alongwith financial institutions, like IFC, IDBI, ICICI and the LIC are not at present covered by CAG audit though these institutions account for a major portion of the country's economic and financial infrastructure and are important agencies to carry out Government policies for development and public welfare. This Committee does not feel that there is any merit in the Ministry's argument that the banking sector should not be brought under CAG audit because CAG audit was primarily rule bound and banking activity necessarily involved a measure of discretion. There is also no weight in the argument that the nationalised banks and financial institutions would be discriminated against vis-a-vis the foreign banks, since the latter would be outside the purview of CAG audit. This Committee, therefore, recommends that the audit of the nationalised banks and other financial institutions which are Government owned or Government controlled should be brought under the control of C&AG who should select and appoint Statutory Auditors and carry out a supplementary audit through its own officers just as is done in the case of Government companies and other public sector undertakings. Bringing the banks under the CAG audit would ensure that a vital component of the economy is not left outside the purview CAG's jurisdiction. This would also go a long way in restoring public confidence and credibility of the banks and other financial institutions.

CHAPTER II

VIGILANCE AND SECURITY IN PUBLIC SECTOR BANKS

2.1 The Banking Division (Department of Economic Affairs) is entrusted with the job of keeping a close watch on the working of vigilance machinery in all Public Sector Banks functioning in the country. The Department is also entrusted with the work of ensuring proper security arrangements in these banks. The Department analyses and monitors the reports on the anti-corruption measures and security arrangements in the banks on a quarterly basis. With a view to ensure a greater degree of independence and impartiality in the functioning of Chief Vigilance Officers, arrangements have been made by RBI to take officers from RBI or other banks to appoint them as Chief Vigilance Officers in the banks.

2.2 The last decade has witnessed an enormous growth of bank branches and diversification of banking activities but the control and supervision has not been strengthened in commensurate terms. This has led to a decline in service, discipline and accountability. The result is that there have been increased cases of frauds and malpractices in the banks.

2.3 The witness informed the Committee that in 1991, the Government of India ordered that a high level Committee be set-up by RBI to go into all the aspects of the matter and come out with recommendations. This Committee was appointed under the Chairmanship of Deputy Governor, Shri Amitava Ghosh. CBI and other professionals were also represented on this Committee. After a detailed examination, the Report of the Committee has been accepted and the RBI has made an implementation schedule. The recommendations were divided into 3 categories:—

(i) Those recommendations which the banks can implement by themselves;

(ii) Those where the RBI has to give directions and also take action to implement the same; and

(iii) Those where the approval of the Government is necessary.

2.4 The witness also informed the Committee that instructions have been issued and implementation has started. 53 recommendations have been implemented and the remaining 5 are yet to be implemented. The Committee's recommendations are for preventive vigilance. They have identified the vigilance prone areas. The Chief Vigilance Commissioner has suggested that a Vigilance Officer should be appointed from outside and not from the bank. He is to report directly to CMD and his performance will be watched by the Chief Vigilance Commissioner. A new CR format for this has been devised. The Chief Vigilance Officer has a right to entertain complaints against the CMD or give factual information to the Chief Vigilance Commissioner (CVC). If there are failures and malpractices committed by him, the Chief Vigilance Officer need not sleep over it.

2.5 In a written reply, the Ministry of Finance (Department of Economic Affairs) have indicated the number of cases where the services of corrupt bank officials were terminated and suspensions made, as under:

I. Fraud Cases		1990	1991	1992
(i)	No. of Employees convicted	82	82	51
(ii)	No. of employees given penalities (Major/Minor)	738	829	849
(iii)	No. of employees out of (ii) above dismissed/discharged/ removed.	304	289	275
(iv)	No. of employees against whom prosecution is pending in the courts.	637	640	737
(v)	No. of employees against whom departmental proceedings are pending.	1278	1563	7118
II. Corrupt Practices				
(i)	No. of employees convicted	38	16	6
(ii)	No. of employees given major/ minor penalties	613	664	737
(iii)	No. of employees out of (ii) above dismissed/discharged/removed.	101	81	105
(iv)	No. of employees against whom prosecution is pending in the courts.	286	283	264
(v)	No. of employees against when departmental proceedings are pending.	1120	1217	1263

2.6 The second aspect of this Chapter pertains to the security in Public Sector Banks. The Committee examined this aspect in detail with the witnesses from the Ministry. The witness informed the Committee that the Government was seriously concerned about the security aspect of the banks as well as the banking operations in trouble prone areas particulary in Jammu & Kashmir. In the valley, it was not possible for any bank to function. The Committee was informed that even with regard to other difficult areas like North-East and Punjab, the Government, at a heavy cost, was engaged in providing adequate security to banks.

The witness stated that there is a State-level Security Committee set-up by RBI for each State. This Committee holds regular meetings and gives information to the RBI about the Security position. When a bank has not been able to function due to security reasons they have to report to the RBI as well as to the Government of India. There is a Security Cell in the RBI to monitor the incidents and issue suitable instructions. Each public sector bank has a Chief Security Officer and meetings of CSOs' are held regularly to find out the problems and their solutions.

2.7 The Report of the Sub-Committee of IBA appointed to evolve guidelines on Secuirty Arrangements in Banks were circulated to Banks by Government on 4.8.83 for implementation. Most of the measures have been implemented by public sector banks to prevent cases of robbery in main branches functioning in urban areas particulalry in cosmopolitan cities.

2.8 The Committee is constrained to observe that Chief Vigilance Officers and Vigilance Officers are taken from the executive and senior management cadres. Their source of information is complaints that are received by them and vigilance cases are not initiated by them sou-moto. Surprise visits to check movable and immovable property disproportionate to the known sources of income of an officer, conspicuous standard of living, check on luxurious spending etc., are not undertaken by the vigilance at their own initiative. Vigilance does not probe thoroughly the malpractices, embezzlement, mis-appropriation of funds and frauds practised by their colleagues in the banks. It is unreasonable to expect that a Vigilance Officer will question the defaulting senior executives belonging to the same banking service as he is also in the same promotional channel.

2.9 The Committee, therefore, recommends that there should be a separate independent authority for Vigilance in Banks, the staff for which should be from outside the banks. The Chief Vigilance Officers should be appointed by RBI or CVC from outside, having separate channel of promotion. The Chief Vigilance Officer should send regular reports on quarterly basis to Central Vigilance Commission and to the Department of Banking, Ministry of Finance. The Reports should name the delinquent officers. The Ministry should ensure proper follow up action on vigilance reports within the prescribed time frame.

2.10 The Committee also recommends that the Ministry of Finance should frame certain rules governing the re-employment of retired senior executive in the private companies. The rules should prescribe penal action in case of violation as it has been seen that Senior Executives are very liberal in granting loans to the private companies when they are on the verge of

retirement, after which they manipulate their re-employment in these companies. The Committee recommends that the provision of no employment within 2 years of retirement should be strictly followed.

The Committee further recommends that preventive vigilance should also be encouraged in the banks. For this the help of staff unions and the Customers' Committees etc. should be taken.

2.11 With regard to the security aspect of the banks the Committee notes with concern the prevailing security environment in various states affecting the banking operations and the money which the Government have to spend on the protection of the bank properties as well as bank employees. The Committee recommends that the State Government should be entrusted with the responsibility of beefing up security for the banks. The question of providing suitable type of weapons to the bank security guards should be taken up with the Ministry of Home Affairs and examined in the light of prevailing security environment in each state.

CHAPTER III

FORMATION OF NATIONAL RURAL BANK OF INDIA

3.1 India is a land of villages where more than 70% of its population lives. The people are predominantly dependent on agriculture. Their standard of living is generally low and they have to borrow money from local village money lenders at high interest rates to carry out their economic/business activities. To meet the credit needs of weaker sections of the society, Regional Rural Banks were established on 2nd October, 1975. However, no bank has been set up after 1986. They function under the general supervision and guidance of their Board of Directors and conform to the guidelines issued by NABARD/RBI as well as Government of India. The Chairmen are appointed by the Nationalised banks sponsoring the RRBs.

3.2 The Regional Rural Banks through its 14,539 branches cover 392 of the 478 districts in the country. There are 196 RRBs operating in the country in all the States except Sikkim and Goa. The Credit support provided by RRBs amounts to Rs. 4090.86 crores (outstanding) in 123.99 lakh accounts and the sum of Rs. 5867.83 crores was mobilized by way of deposits in 345.26 lakh accounts as in March, 1992. Rs. 5 crore was provided in the budget of Regional Rural Banks for 1993-94 while Rs. 11 crore was the budget provision in 1992-93. The issued capital of each of the RRBs is being raised from Rs. 25 lakhs to Rs. 100 lakhs in a phased manner in pursuance of the recommendation of the working Group on RRBs (Kelkar Committee). In the ongoing second phase, the issued capital is being raised to Rs. 75 lakhs and 140 RRBs have been identified for this purpose out of which 128 were to be covered by March, 1992. Parity in pay scales of employees of RRBs with those of commercial banks has been brought about *w.e.f.* January, 1991.

3.3 In a written reply, the Ministry explained that the percentage of overdues outstanding had marginally increased from 31.26% as of March, 1991 to 32.12% as of March, 1992. The overdues in absolute terms stood at Rs. 1314.24 crores as of March, 1992 recording an increase of 18.93% or by Rs. 209.24 crores over March, 1991. The per bank and per branch overdue amount as of March 1992 stood at Rs. 670.53 lakhs and Rs. 9.04 lakhs, respectively as against Rs. 563.77 lakhs and Rs. 7.61 lakhs respectively as on March. 1991. The total overdues for different purposes were as follows: ST(23.50%), Agricultural Investments (14.42%), Allied Activities (13.38%) and Non-Agricultural purposes. (48.70%).

3.4 It was further stated by the Ministry that the financial position of RRBs has been a source of continuous anxiety. The losses incurred by these banks have been increasing year after year. The net loss for the year 1991-92 reached the level of Rs. 245.70 crores (against Rs. 71.50 crores during 1990-91). Out of 196 RRBs, only 23 RRBs were in a position to earn profit amounting to Rs. 12.96 crores during the year ending March 1992. As a result of recurring losses, the accumulated losses which stood at Rs. 368 crores as at the end of March 1991 have gone upto Rs. 614 crores as at the end of March 1992. The figures relating to year ending 31st March, 1993 are not available.

3.5 The Ministry have attributed the losses by RRBs to the following causes:—

(a) A narrow or negative margin on lendings due to high cost of funds. There is not much scope for the RRBs to cross-subsidise their lendings at low-interest predominantly to the target group comprising small farmers, rural artisans, cottage and village industries and other small borrowers in rural areas.

(b) *High overhead costs.* Establishment expenses have gone up substantially after the implementation of NIT Award.

(c) High servicing cost because of a large number of small accounts.

(d) Low level of business per employee due to restricted area of operations type of clientele and the nature of transactions undertaken.

(e) Lack of scope for undertaking remunerative busineess like foreign exchange transactions, merchant banking and other commercial transactions.

3.6 The Ministry further stated that the following measures have been taken to improve the viability of the RRBs as also to enable them to meet the credit needs of the weaker section of society:

(i) RRBs have been allowed with effect from 12 September, 1992 to finance non-target borrowers to the extent of 40 per cent of their fresh loans.

(ii) Sponsor Banks have been instructed to pay minimum 13.5 per cent interest on all term deposits of RRBs kept with the sponsor banks for maintenance of SIR under section 24 of the B.R. Act.

(iii) RRBs have been allowed 7.5 per cent interest from 1.4 93 on current account balances with commercial banks (sponsor banks as well as non-sponsor banks) as against 6.5 per cent hitherto allowed.

(iv) RRBs have been extended a package of refinance schemes for financing tiny industrial units upto Rs. 10 lakhs for which also cent percent refinance is available from NABARD.

(v) RRBs have been allowed to finance transport vehicles under Small Road Transport Operators' Scheme (STRO) for which cent percent retinance is available from NABARD.

(vi) Relaxation in eligibility criteria has been allowed to the RRBs functioning in North-eastern region, for drawal of refinance from the NABARD.

It may be mentioned that despite the recent policy decision to finance non-target group, RRBs' main focus continues to be on the target group. While the intention of instructions to finance non-target group is to improve the profitability of the RRBs, they have to extend compulsorily at least 60 per cent of the fresh loans to target group.

3.7 During evidence the representatives of the Ministry of Finance stated as under:—

> The majority of 196 regional rural banks are not doing well. There are many options available. Firstly, it has to be seen whether they can be merged with the sponsored banks or whether we can set-up rural subsidiary banks or whether there should be a National Rural Bank of India. There have been Committees which have gone into these questions. The Kothari Committee of 1989 suggested that this should be merged with the sponsored banks. The Narasimham Committee suggested that there should be rural subsidiaries. There was another suggestion made by some employee organisations of the RRB that there should be a National Rural Bank of India. The RBI thought that the best option would be to merge the regional rural banks with the sponsored banks. This is in line with the recommendation of the Kothari Committee. This matter is currently under examination of the Government at the highest level.

3.8 The Committee note with concern that the cases of defaults in RRBs are on the high side though their performance in achieving the objectives of providing credit to economically weaker sections and channelising their savings is laudable. In the matter of deposits, the rural banks are placed on better footing than the nationalised banks.

The Committee express their unhappiness over the sad plight of RRBs. The financial position of these banks is deteriorating and the Government appears to be complacent in improving viability of these banks. The Committee recommends that the Government should examine the question of reducing the number of RRBs by way of merger etc. to make them viable. More facilities should be extended to those banks like drawal of refinance from NABARD. The relaxation in eligibility criteria for refinance allowed to RRBs in North-Eastern region should be extended to

RRBs in other states also. RRBs can also consider lending funds to industries being set-up in backward areas.

3.9 The Committee also express their resentment over the fact that rural banks are operating only as agencies of commercial banks to collect funds from rural people and siphon them off to the cities. The Committee, therefore, feels that some C.D. ratio should be fixed for these banks to ensure that funds collected from the rural people are available to them for the economic development of that.

3.10 The main objective of the Rural Banks is to meet credit needs of the weaker sections of Society in rural areas. The Committee, therefore, recommen that a 'National Rural Bank of India' should be set up and all RRBs should be brought under its control. This step would go a long way in improving the viability of Rural Banks. The Government should allocate sufficient capital to it to ensure its expansion and development. The National Bank should guide RRBs and monitor their activities. The Government may consider whether the National Rural Bank of India should be a single Central Bank or their should be several Zonal Rural Banks with independent headquarters and functioning.

3.11 The Committee was informed by the Govt. that out of 196 RRBs there are 173 RRBs which are loss-making and 23 RRBs which are making profit. In this connection the Committee feels that the factors contributing to the sucess of some RRBs should be identified so that the working of loss making RRBs could also be improved.

CHAPTER IV

TOP LEVEL APPOINTMENTS

4.1 The Board of Directors of Nationalised Banks are constituted by the Central Government by virtue of powers conferred by Section 9 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980, in accordance with the Nationalised Banks (Management and Miscellaneous Provisions) Schemes 1970 and 1980. The Boards of nationalised banks are required to include *inter-alia* an official each from Central Government and RBI and two directors representing workmen staff and other non-workmen staff of respective banks. The other Directors represent depositors, farmers, workers, artisans or persons having special knowledge or experience in the field of accounting, small scale industries etc. According to Clause 3 of the Scheme, the Board of Directors of nationalised banks consist of not more than two whole-time Directors. One of the whole-time Director is to be the Managing Director and any Director on the Board can be appointed as Chairman. It is thus permissible for the same person to be appointed as Chairman and Managing Director. This practice is being followed at present. The Managing Director is the Chief Executive Officer of the nationalised Banks and exercises powers and duties as are delegated to him by the Board of Directors. Also being the Chairman of the Board, he presides over the meeting of the Board. The Managing Director and whole-time Directors are appointed for five years and the tenure of non-official Directors is three years.

4.2 The second whole-time Director, who is designated as Executive Director is envisaged as being second in command of the bank. He is expected to assist the Chief Executive in formulation of operational policies and evaluation of strategies for development of organisation on the same lines. He is also expected to discharge duties and exercise powers delegated to him by the Board, thereby reducing the load of work on the Chief Executive. During the absence of Chief Executive, he is also expected to look after the current duties of that post.

4.3 In a written information furnished by the Ministry of Finance, the position of vacancies of whole-time directors on the Boards of Public Sector Banks as on August 27, 1993 is as under:

Sl. No.	Detail of vacancy	Date from which the post of whole-time Directors is lying vacant
1.	Managing Director, State Bank of India	26.6.93
2.	Chairman and Managing Director, Andhra Bank	1.7.92
3.	Chairman and Managing Director, Bank of Maharashtra	6.5.93
4.	Executive Director, Central Bank of India	5.2.92
5.	Executive Director, Vijaya Bank	22.6.92
6.	Executive Director, Indian Bank	1.7.92
7.	Executive Director, Bank of Maharashtra	13.7.93

4.4 In a written reply, the Ministry also furnished the position of vacancies of non-official directors/members on the Central and Local Boards of State Bank of India and Board of Directors of the Nationalised Banks:

Sl. No.	Name of Bank	Total No. of posts of Non-Official Directors as per the statutes	No. of posts filled	No. of posts vacant
1	2	3	4	5
1.	*Reserve Bank of India*			
	—Central Board	10	8*	2
	—Local Boards	20 (5 members on each of the 4 Local Boards)	16*	4

1	2	3	4	5
2.	*State Bank of India*			
	—Central Board	6	—	6
	—Local Boards	78 (6 members on each of the 13 Local Boards)	39*	39
3.	*Nationalised Banks*			
	1. Cental Bank of India	9	4*	5
	2. Bank of India	9	5*	4
	3. Punjab National Bank	9	5*	4
	4. Bank of Baroda	9	6*	3
	5. UCO Banks	9	6*	3
	6. Canara Bank	9	3*	6
	7. United Bank of India	9	1*	8
	8. Dena Bank	9	4*	5
	9. Syndicate Bank	9	4*	5
	10. Union Bank of India	9	6*	3
	11. Allahabad Bank	9	5*	4
	12. Indian Bank	9	4*	5
	13. Bank of Maharashtra	9	5*	4
	14. Indian Overseas Bank	9	5*	4
	15. Andhra Bank	9	5*	4
	16. Corporation Bank	9	5*	4
	17. New Bank of India	9	4*	5
	18. Oriental Bank of Commerce	9	6*	3
	19. Punjab & Sind Bank	9	3*	6
	20. Vijaya Bank	9	4*	5
		294	153	141

*The tenure of these directos have already expired and they are continuing pending appointment of their successors.

4.5 When asked during the evidence regarding the procedure adopted for appointment/promotion, for Chairman and other members on the Board of Directors of Nationalised Banks, the representatives of the Ministry, stated as under:

> "There is a feeder cadre for Chairman of banks and Executive Directors of Banks. We would like to have a person who has experience in financial services and banks. The feeder cadre is from the 20 Nationalised Banks, the State Bank of India, the seven subsidiary banks and the banking financial institutions. And beyond that what we have is a few private banks and few foreign banks in the country."

On being asked about salary structure of Indian Banks *vis-a-vis* foreign banks, the witness deposed as follows:

> "The salary structure of foreign banks as well as the private sector banks is somewhat out of the tune with our salary structure."

4.6 When the Committee referred to the availability position of persons for such high posts, the witness informed the Committee as under:

> "There is a limited availability of persons who fulfil the criteria having put in 20-25 years as General Manager. We have for staff position a certain feeder cadre."

4.7 On the question of quality of feeder cadre available for promotion, the witness admitted that there was a need to improve the quality of people coming into Banking Service. The problem was not so much in the selection procedure but in feeder cadre where is a lot of scope for improvement. He observed that the training operations of Deputy General Manager need improvement as they are to manage the high posts.

4.8 When asked about the method of selection of whole-time Directors in the banks, the witness informed the Committee that an Appointment Board was constituted way back in January 1990. The Board meets under the Chairmanship of Governor, RBI. The Board consists of *inter-alia*, the Secretary (Banking) and Deputy Governor, RBI. The Board periodically makes recommendations for filling up of vacancies arising from time to time.

4.9 In a written reply, the Ministry informed the Committee that while making recommendations, the Board takes into account the track record of the Executives, their length of service, and the possibility of inter-bank shifting of the Executive is also considered by the Board, wherever necessary. For the purpose of appointment of Executive Directors in nationalised banks, the panel is prepared by a Sub-Committee of the Appointment Board and after interviewing eligible General Managers in

Nationalised Banks and Chief General Managers in Associate Banks of State Bank of India, recommendations are made by the Board out of the panel. The recommendations of the Appointment Board are considered by the Government and appointments are made after the required formalities are completed.

4.10 When asked about the appointment of other members on the Board of Directors of the nationalised banks, the witness informed the Committee that people have been identified and recommended by Government to fill up the vacant posts. However, in case of appointments to the post of Chairman, since the approval of Appointments Committee of Cabinet is needed, it would take some more time to finalise the names.

4.11 The Committee is distressed to note that out of twenty nationalised banks, three banks are without full fledged Managing Director/Chairman. It is surprising to note that the post of Chairman and Managing Director of Andhra Bank is vacant for more than one year. The Committee further notes that post of Executive Director are lying vacant in four nationalised banks, ranging from one and half year to one month. The Committee considers this situation as most unfortunate and cannot but deplore the lackadiasical manner in which Governemnt have handled the matter. The Committee is of the view that for effective functioning of any organisation and particularly nationalised banks, which cater to the needs of people at large, there ought not to be any vaccum in top management. The delay in appointment to such high posts not only hampers the smooth functioning of banks, but also has a cascading negative effect on corporate goals and implementation of financial policies. The Committee also finds that in terms of Nationalised Banks (Miscellaneous Provision) Scheme 1970-1980, while the Government has assumed unbridled powers to appoint or remove at will both whole time and other Directors, the non-appointment of Chairman/ Managing Directors and Executive Directors leads to the irresistible conclusion of usurping powers of the Board of Directors by the Ministry through over-centralisation.

4.12 The Committee is informed that Non-Official Directors reprsent the interests of varied field such as of staff and non-workmen staff, depositors, farmers, workers, artisans, small-scale industries etc. The Committee further observes that in none of the nationalised banks, the vacancies of non-official Directors, as stipulated in the statute, have been fillied up. The Committee are perturbed to note that the tenures of these Directors have already expired and they are continuing in their positions pending appointment of their successors. Even in the RBI, which is the nodal bank and is the Banker of banks, there exist a large number of vacancies both at Central and Local Boards. The Committee is at a complete loss to understand the manner in which the interest of artisans farmers, depositors, whose interest these Non-Official Directors represent, would be served, in the absence of their representatives on the Board of Directors. The Committee

desires that the Government should explain to it the reasons for not filling up the vacancies of Non-Official directors on the Board of Directors of the banks.

4.13 The Committee, therefore, recommends that in future no vacancy should remain unfilled for any length of time including the post of both Chairman-cum-Managing Director and Executive Director. Under no circumstances should both these posts remain vacant simultaneously. The Government should do some advance planning in the matter of filling up the vacancies on the Boards of Directors of various Banks. The Appointment Board should prepare bank-wise, a list of Directors, official as well as non-official, who are due to retire in the calender year and should take immediate steps to fill up those vacancies. The Committee desires that the Government should ensure with certainty that non-official Directors automatically cease to be in office after the date of expiry of their term and not remain in office till the appointment of new Directors. The Committee recommends that quarterly Reports be sent to this Committee regarding vacancy position on the Board of Directors and the action taken by the Government to fill up those vacancies.

4.14 The Committee further recommends that the Appointment Board should also be restructured to include a group of eminent persons such as retired Governors of RBI, Judges of Supreme Court and High Courts, former C&AG and other widely respected persons in the financial field. The Board should also be empowered to make recommendations regarding removal of Directors from the Board of Banks.

4.15 The Committee also note that there is limited availability of persons for filling up the posts of Chairman-cum-Managing Directors and the Executive Directors. The Committee recommends that the area of consideration for such posts should be further enlarged by including persons from the private sector and the universities, non-banking financial institutions and State financial institutions etc. so that a wider choice is available.

4.16 The Committee also observes that there is a shortage of manpower in banking sector as the banking career has not remained that attractive as it once used to be. There are frequent instances of people leaving Bank Service to join the All India Civil Services. The Committee, therefore, recommends that immediate steps be taken to make the banking career more attractive and purposeful. The Government should also examine the possibility of introducing an All India Banking Service on the lines of other All India Civil services to attract the best talent for the banking sector.

CHAPTER V

CUSTOMER SERVICE IN NATIONALISED BANKS

5.1 The Banks were nationalised in 1969 to ensure timely and adequate credit support for viable productive endeavour. Nationalisation was also aimed to subserve broader economic objectives. In the two decades since banks were nationalised, the number of commercial bank branches have increased over seven-fold. At the end of March, 1992 there were 60,528 branches of Commercial Banks (including RRBs) in the country of which 58.3 per cent. were in rural areas as compared to 27.3 per cent. at the time of nationalisation. Today, the top ten banks have a market share of more than 50 per cent. As a result of rapid expansion, the average population catered by a bank branch came down from 65,000 in 1969, to a figure of 11,000 by the end of March, 1992. Branch expansion has also led to more balanced spatial distribution of banking facilities. Today there is a bank office in almost all the 5000 development blocks of the country. With nationalisation, the inter-state disparities in banking have also been reduced. In 1969, 5 States (Maharashtra, Gujarat, Tamil Nadu, West Bengal and Punjab) accounted for a little under half of the total number of offices. By 1990, the share of other States had risen to nearly 80 per cent. which reflects the greater emphasis laid on opening offices in hitherto under-banked regions of the country.

5.2 The deposits with the Indian Commercial Banks which stood at Rs. 6,000 crores in 1969, zoomed to Rs. 2,25,000 crores in the Ninetees. The aggregate deposits of scheduled Commercial Banks have grown by Rs. 30,907 crores during the period from 20.8.1992 to 25.12.1992 representing a growth rate of 18.4% as against the growth rate of 14.7% during the corresponding period in 1991-92.

5.3 Along with expansion of business of nationalised banks, there is also a significant growth of customers complaints in regard to service offered by the banks. There is a widespread feeling that all is not well with the Banking Sector after nationalisation as far as Customer Service is concerned. Customer Service is an aspect of great importance in Banking. In the area of Customer Service, expectations and demands of the customers tend to rise at a much faster pace then banks are equipped to deal with. Even in the technologically advanced countries, Customer Service is an issue that constantly engages the attention of the bankers. In India, the issue of Customer Service is influenced by several factors that are peculiar to our Banking Industry. Among the specific areas of irritation to bank customers are delay in encashment of cheques, delay in issue of drafts, non-issue of advice of debit/credit and other advices, non-issue of statement of accounts and delay in updating passbooks, delay in collection of cheques, refusal to open accounts, refusal to issue cheque book/drafts, refusal to give safe deposit vaults, lack of response to enquiries, unhelpful attitude and lack of proper customer amenities. After nationalisation, there is a tremendous increase in the number of accounts served by banks. The banks are heavily loaded with small loan accounts and scheme based lending accounts. The small loans involve a lot of time and paper work in pre-sanction and post-sanction formalities. Apart from this, there are a number of extra banking activities such as collection of school fees, water charges/electricity charges municipal and other government taxes etc. Another reason for poor Customer Service is inadequate training and growing indiscipline amongst the staff. To mitigate the hardship faced by the customers, many working groups were formed to make recommendations for improved Customer Service. The Banking Commission (1972) made important recommendations on customer service. In 1975, Government appointed a working group on Customer Service in banks under the Chairmanship of Shri R.K. Talwar. The working group made several important recommendations covering many areas like deposit accounts, remittance and collections of loans and advances, discipline and attitude. The Standing Committee on Customer Services in Banks with representatives from the Ministry of Finance and Reserve Bank of India and Indian Bank Association was constituted to identify the areas of relative importance and to monitor the implementation of these recommendations. This Committee has been meeting periodically to assess the progress and to give direction to ensure effective implementation of the recommendations. In 1980s, several steps were taken by Government and Reserve Bank of India to redress the grievances of customers. These include (i) Setting up of Customer Service Committee in all branches and offices of public sector banks (ii) observing "customer meet day" which provides customers direct access to higher officials (iii) setting up of Customer Services Centres in State Capitals and major cities where a public sector bank is given the lead responsibility to coordinate grievances and redressal machinery and (iv) setting up of "Directorate of Public Grievances" under the Cabinet Secretariat which entertains the grievances from the public.

5.4 In spite of these measures a wide gap in customers' satisfaction still persists. The Government of india appointed another Committee under the Chairmanship of Shri M.N. Goiporia the then Chairman, State Bank of India in September, 1990, to study the causes for the persistance of below-par customer service in banks and to make recommendations for improvement of bank service.

5.5 The Committee submitted its report in December, 1991 and made 97 recommendations for improving the customer services in banks. The wide ranging recommendations relate to following aspects:—

(i) Improving customer service by enlarging scope of teller services, extending banking hours for non-cash transactions, devising appropriate procedure to render uninterrupted service during business hours, extending facilities for exchange of mutilated and soiled notes, and ensuring nomination in all deposit accounts;

(ii) Opening of specialised branches, focussing on international banking, industrial finance and small scale industries.

(iii) Making bank employees more responsive and customers friendly by job enrichment, proper training, reward system and more constructive role by employees' organisations;

(iv) Technology upgradation and continuous review of systems and procedures in tune with changing needs of customers to support effective and efficient services;

(v) Making bank deposits more attractive by raising interest rate on savings bank accounts, permitting tax benefit on deposits, etc.;

(vi) Compensating customers for delay in collection of cheques, payment of mail transfer, telegraphic transfer, etc.; and

(vii) Implementing the Talwar Committee recommendations on Customer Service both in letter and spirit.

5.6 The Ministry in a written reply furnished on 15.7.1993, informed the Committee that RBI issued its first set of instructions on 28th January, 1992 in which they had categorised the recommendations of the Goiporia Committee into four groups:

Group 'A'	Recommendations that can be implemented by banks immediately (66 recommendations).
Group 'B'	Recommendations which require approval/ examination by the RBI (32 recommendations).
Group 'C'	Recommendations requiring consultation and approval of the Government of India (10 recommendations).
Group 'D'	Recommendations requiring examination by banks and/or their dialogue with employees organisations either singly or collectively through Indian Bank Association (9 recommendations).

5.7 The Ministry further informed the Committee that some of the recommendations figure in more than one group. RBI has advised banks to implement straightaway the recommendations under Group 'A'. The

Banks have also been advised to initiate suitable action for implementing recommendations in Group 'D'. Out of 321 recommendations, under Group 'B', which are required to be examined by RBI, the decision has been taken in respect of 22 recommendations. Of the 10 recommendations, under Group 'C', action has been taken in respect of 5 recommendations. Implementation of the accepted recommendations of the Committee and in respect of which instructions have already been issued by the bank are being monitored by RBI on a continuing basis.

5.8 When asked during evidence the status of the recommendations of the Committee, the witness stated:—

> "Majority of the recommendations are in Group 'A'. These form almost 2/3rd of the total number of recommendations which cover a very wide area of banking service primarily aimed at providing satisfaction to the larger clientale of average and small means. In fact, as many as 66 out of 97 recommendations are contained in Category A and banks are in the process of implementing these recommendations. The Reserve Bank of India has in fact called for a report from various banks on the various stages of implementation of these recommendations."

5.9 Highlighting the salient features of main recommendations of the Goiporia Committee, the witness informed this Committee during evidence that the facility for nomination at the time of opening accounts has been made compulsory. For speedier collection of outstation instruments, the Committee have recommended that bank should pay on their own without being asked to pay 2% extra above the prevailing saving bank rate of interest for the period beyond the normal period prescribed for realisation of outstation instrumenets. The Government have viewed this and have decided to raise the penalty further particularly in the case of instruments deposited into a borrower accounts by clients. Now the banks the required to pay at the interest rate applicable at the minimum of commercial rate applicable to advances on delayed credit of outstation instruments to overdraft accounts and other borrower accounts. The Goiporia Committee has also recommended that telegraphic transfers payable at area I centres including State Capitals may be value dated on 3rd day. Other remittances may be credited on receipt of telegram or confirmation advance whichever is earlier. The externsion of banking hours, for noncash transactions has also been recommended by that Committee. Now the banks will render various services which do not involve cash transactions till one hour before the close of business hours. Another far reaching recommendation of the Committee is on instrument drawn on local clearance centres where there is total automation. These instruments would now be credited on the same day if the amount is above Rs. 5000/- provided the customer is willing to pay a service charge of Rs. 5 for this facility.

5.10 When asked what further steps the Government have undertaken for appraisal of customer services, the witness informed the Committee that Indian Banks' Association has commissioned a survey to determine customer satisfaction. These surveys have been undertaken in metropolitan cities and in rural areas of the country as well. The banks have also been advised to sponsor such surveys and take corrective steps, based on feedback received from the customers/clientele.

5.11 The Committee notes that in spite of Constitution of several Committees such as Customer Service Committee functioning at branch level, Customer Service Centres in State Capitals and major cities etc., the grievances of customers are yet to be satisfactorily redressed. Though banks have made several improvements in customer service, the requirements and demands of customers have also witnessed a steep rise.

5.12 The Committee further notes that Goiporia Committee made 97 useful recommendations and these have been categorised into four groups for the purpose of implementation. The Committee is distressed to note that in spite of clear cut instructions to implement recommendations under Group 'A' straightway, the progress made by the banks in implementing these recommendations is far from satisfactory. This Committee desires that the process of implementation of the recommendations of Goiporia Committee should be expedited and the Committee may be kept informed about the stage of each recommendation implemented by each nationalised bank.

5.13 As after nationalisation most of the branch expansion has occurred in the rural and semi-urban areas, the Committee recommends that special cells be created in each bank to oversee the provision of Customer Services in branches in those areas. Even though the Customer Services have improved in cities in some respects there has not been any appreciable improvement in rural areas. As the literacy rates in those areas are low, they are not able to make use of various fora available to oversee the Customer Services. Hence, it should be made the responsibility of Branch Manager to oversee the availability of various Customer Services in his branch. He should encourage the formation and working of Customer Services Committees, under his Chairmanship consisting of account holders in his branch. The norms for frequency of these meetings should also be prescribed and quarterly Reports with controlling office should be filed. It should be examined whether the Auditor can be entrusted to specifically oversee the provision of customer services in rural and semi-urban areas. Special surveys be made in these areas on the lines of the surveys done by Indian Banks Association and the conclusion/outcome of these surveys should be implemented in a given time frame.

5.14 With the rapid expansion of banking sector, the system is new finding it difficult to cope up with the load of servicing more branches manually. Keeping in view the need to improve customer service and house-keeping, the Committee recommend that banks should upgrade their

technology to bring mechanism, automation and computerisation in their operations. The banks should introduce Advanced Ledger Posting Machines (ALPMs) at the branch level, mini computers at Zone/Regional Office Level and mainframe computers at Central/Head Offices. However, the Commitee feel that the introduction of these machines should not be indiscriminate but should be need based. A detailed programme should be chalked out by the Banking Division, Ministry of Finance and it should be implemented by all the banks in a given time. The Committee also finds that banks have made little efforts to dispel the fear of staff unions towards automation and computerisation of work in banks. This should be given top priority and cooperation of staff unions should be sought in the matter. In some cases even after agreements with the Staff, little progress has been made by the banks in automation and computerisation. The Committee, therefore, recommends that banks should earmark sufficient funds for computerisation etc. every year to meet the competition from private and foreign banks in providing best customer services.

5.15 The Committee notes that, in spite of Constitution of several committees, the grievances redressal mechanism is not yet satisfactory. The Customers still have to more Civil Courts for settlement of their claims. There is thus a need to overhaul the grievance redressal machinery. The Committee, therefore, recommends the institution of Lok Pal on the pattern of Bank Ombudsman of United Kingdom for each nationalised bank. The Bank's Lok Pal should be a person of repute, preferably a retired Supreme/High Court Judge or a retired Comptroller and Auditor General of India with a fixed tenure, to deal with complaint matters and pertaining to deficiency of service by the banks. He should also be authorised to grant relief to bank customers including monetary relief wherever he think it necessary. The decision of the Lok Pal should be binding on the banks.

CHAPTER VI

CAPITAL ADEQUACY NORMS AND OTHER RELATED MATTERS

6.1 The strength and stability of a bank is measurable in terms of the ratio of capital funds to a bank's deposits and assets. The capital ratios of the Indian banks have, however, been low as compared to the international standards of capital adequacy. Many banks have been seriously under-capitalised during the past two decades. Serious problems have also been faced in the Banking Sector in the form of decline in profitability of the banks. Based upon the observation of Basle Convention on Banking Regulation and Supervisory Practices held under the auspices of the Bank of International Settlements, the Committee on Financial System (Narasimham Committee) prescribed the capital adequacy norms for the Banks in India. The BIS norm for capital adequacy is 8 per cent of the risk weighted assets. In accordance with the recommendations of the Narasimham Committee, the banks with no branches abroad are required to achieve a capital adequacy of 4% of risk weighted assets by 31.3.1993 and 8% of risk weighted assets by 31.3.1996. The banks with branches abroad are required to achieve capital adequacy of 8% of risk weighted assets by 31.3.1994.

6.2 When the Committee on Finance took evidence of the representatives of the Department of Economic Affairs on 16 July, 1993, the Secretary stated that the fundamental nature of the weaknesses in the banking system led the Government to appoint the Narasimham Committee. He further explained that till the new norms were introduced in 1992, the banks were not even following a uniform practice of accounting. Different banks followed different accounting practices. He stated that it was, therefore, absolutely essential as a first condition to set right the financial accounting pattern on which the performance of the banks could be judged. He also stated that with the introduction of the new norms, the banks have to make adequate provisions for assets which are non-performing.

R.B.I. GUIDELINES

6.3 Keeping in view the need for uniform accounting practices by the banks, the Committee enquired from the Department of Economic Affairs about the steps taken in this direction. The Department of Economic Affairs in a written note explained that with the RBI guidelines in 1992 on income recognition, assets classification and provisioning, attempts have been made to introduce a uniform practice of accounting.

6.4 RBI has now prescribed that all advances of a bank should be classified under eight health codes *viz.* satisfactory irregular, sick viable/under-nursing, sick, non-viable/sticky, advances recalled, suit filled accounts, decreed debts and debts classified by banks as bad/doubtful. The banks and financial institutions could also compress the health codes into broad groups i.e. standard, sub-standard, doubtful and loss to classify their assets.

6.5 This Committee examined the application of the RBI norms relating to assets classification, income recognition and provisioning, etc., introduced with a view to bring the accounts in line with International Accounting practices for the accounting year ended 31.3.1993. The points examined and the findings of the Committee in this regard are discussed below.

6.6 This Committee observes that though the objective of the new norms was laudable, monitoring by RBI, of the actual application of these norms by the banks was poor inasmuch as the accounts of various banks as audited and published disclosed continuance of varying accounting practices adopted by individual banks to suit their needs. It seems that in their anxiety to show higher profits or lower losses certain banks not only flouted the Reserve Bank of India's circulars but also adopted accounting policies which were devoid of financial prudence. The Punjab National Bank accounted for a large income on scam hit securities, the ownership of which is not known. Financial conservatism and propriety demanded that no uncertain income be booked on this account till the issue of ownership was settled. Similarly, some banks treated interest suspense as a provision and reduced the requirement of current year's provisions substantially. Varying treatment has also been given in respect of provisioning for loans below Rs.25,000/- and the Reserve Bank of India stipulation for an additional 2.5% provision has not been strictly adhered to by all banks. This has resulted in substantial under-provisioning.

What is surprising is that the RBI/Ministry nominees on the Boards of various Banks allowed the flouting of RBI's Circulars without raising their voice when they should have forcefully dissented on such matters. It is thus clear that the application of new RBI norms is not yet uniform and consistent and the Committee strongly recommends continuous and active supervision by RBI in this regard.

6.7 On the aspect of unreconciled amounts in

— Inter Branch Suspense Accounts;

— Drafts Paid without advice; and

— Interest accrued and payable, etc.

the Committee is constrained to note that many banks have a huge amount of reconciliation to be carried out and satisfactory progress in this regard is not being made. The Committee are at a loss to understand how financial statements can be expected to present a true and fair picture of huge

amounts are pending for reconciliation. As these are major fraud prone areas, this Committee recommends the accomplishment of this task at the earliest. The Committee notes that some banks are giving due priority to these areas of work but regrets to note that what has been touched is only the tip of the ice-berg and much more progress remains to be made. The Committee was not able to get all the information regarding unreconciled amounts for many banks and concluded that the position was absolutely unsatisfactory.

6.8 The Committee is also constrained to note that many bank managements in their enthusiam, to show higher deposits and advances have been window-dressing their results. This has been achieved by:—

(a) Putting in certain entries in bank reconciliation;

(b) Purchasing certain cheques sent in collection on last date and shown as advances and deposits. No discounting charges are levied in such cases;

(c) Under-provisioning of employees expenses though advances have been taken by employees for travelling, LTA, medical etc.; and

(d) Under provisioning of interest payment on large number of fixed deposits on the plea that the same have matured. In certain cases FDRs held as margins against guarantees, etc., have been overdue for a number of years. Neither these have been transferred to overdue fixed deposits nor any interest is provided thereon. Prudence demands that a provision be created for interest in such cases.

In addition to the above methods, the banks used several methods, technical in nature, to show exaggerated performance. The Committee suggests that RBI should do a strict monitoring to check such malpractices.

6.9 The Committee notes that a sum as large as Rs.5700 crores has been provided for capital adequacy in 1993-94 for various banks. This steady erosion of Equity has not taken place over-night but over the years due to poor accountability of those in-charge. In this regard, it is pertinent to point out that major losses have been due to mounting bad debts. The Committee addressed itself to this problem and in faot called for the names of top defaulting parties and industrial houses. In reply, the Government stated that in accordance with the statute and practice customary among the banks, these names could not be disclosed, as also the quantum of bad debts and doubtful debts incurred cumulatively.

6.10 This Committee appreciates fully the inherent risk in the nature of landing by banks. However, it cannot but observe that while the judgement and discretion of the bank authorities cannot be questionned, the results of this evaluation should certainly be reflected in the assessment of individuals. In other words, a bad judgement should be visited by some loss for the person who made the judgement. The Committee feels that over the years,

banking business, especially lending, has been carried out in such a flippant and casual manner that today it is the entire nation which is bearing the loss in the form of compensation by Government towards eroded capital basis of banks. In this regard, the Committee recommends that banks evolve a methodology of working whereby there is a relationship between the number of good decisions taken by a manager and the assessment of his performance. The Committee cannot but note with regret that precious resources of the State have been frittered away in the nature of bad debts in the form of ventures which were either unviable or fraudulent. The Committee recommends that Government should also examine the total elimination of secracy laws, so far as these prohibit the disclosure of the names of defaulters in refund of bank loans.

CHAPTER VII

PRIORITY SECTOR LENDING

7.1 One of the major aims of nationalisation of banks two decades ago was to build up a financial infrastructure geograpically wide and functionally diverse to help in the process of resource mobilisation to meet the expanding and emerging needs of a developing economy. It was also felt that timely and adequate credit support should be available for the sectors which were hitherto neglected so that the system reached out to the small man and the rural and semi urban areas. It was expected of the banking system to provide for expansion of credit to agriculture and small industry in place of what was regarded as a oligopolistic situation where the system served mainly the rich in the urban and industrial sectors.

7.2 For this, the extension of the geographical spread of banking was given prime importance because it acted as an instrument of deposit mobilisation on the one hand and the provision of credit to the rural hinterland of the economy on the other. The growth of deposits through a wide network of branches provided the banking system with an increasing volume of resources, yet the growth of these resources has not kept pace with the increasing demands made on them. The claims of the Government and the public sector on banking system's resources have been steadily increasing through the mechanism of Statutory Liquidity Ratio (SLR) and Cash Reserve Ratio (CRR). The resources remaining after meeting such statutory requirement had to be apportioned between competing users in the economy. It was this reconciliation of need with availability that was the rationale for diverting an increasing proportion of credit to the sectors important for the national economy in terms of their contribution to growth, employment generation and broadening the base of income distribution which were neglected until that time by the banking system.

7.3 Agriculture, small-scale industry and small enterprise generally represented what came to be regarded as the priority sector. These sectors accounted for no more than 14 per cent of aggregate bank credit at the time of nationalisation and in respect of agriculture sector the figure was 5 per cent only. The Committee notes that this figure for priority sector lending has now reached the level of around 40 per cent of aggregate bank credit.

7.4 During evidence of the Banking Division, the Committee was informed that in the priority sector, the credit allocation was 40 per cent of the advances and the two main areas of stress were agriculture and small industries. So far as the recovery of advances is concerned, in agricultural sector the overdues have been about 22 per cent which is a matter of concern. The Committee was also informed that a target of 22 per cent credit coverage of priority sector had been imposed on foreign banks also and that the same was proposed to be increased to 40 per cent by introducing export credit as a special area of responsibility of the foreign banks.

7.5 The Committee is of the view that the real problem in priority sector lending is the lack of availability of timely credit. All out efforts should be made to ensure timely availability of credit by strengthening the resource position of the banks in rural areas. The Committee is of the view that the question of Statutory Liquidity Ratio (SLR) and Cash Reserve Ratio (CRR) should be thoroughly gone into to enable the banks to plough more funds in the priority sectors. The Committee also feels that overhead costs in running the rural branches should be checked so that more funds are available for lending purposes. The Committee feels that deregulation of rate of interest should be undertaken in a phased manner and the lending rates for tiny sector should not be changed. The rate of interest for tiny sector borrowing upto Rs. 25,000 in rural areas used to be 5 to 6 per cent. Which has been increased recently. The Committee recommends that tiny sector borrowings should continue to get some preferential treatment as before. The banks should also give high priority to the recovery of loans and overdues. Lending to the priority sector does not mean that assets should not well performing. The banking system should be able to identify good quality small scale industries that have potential for profit. For this the banks can tie up with the District Industries Centres in their area of operation and publicise schemes for which they can provide credit to the people in rural areas. The Committee further recommends that the norms of 40% lending to the priority sectors should be strictly adhered to and the banks should deposit the shortfall in the prescribed percentage with NABARD. All these steps, the Committee feels, would go a long way in generating adequate funds for priority sector lending.

CREDIT DEPOSIT RATIO

7.6 During evidence of the representatives of RBI and Ministry of Finance, held by the Committee, the RBI informed that it was very difficult to strait-jacket the banks for state-wise limits for allocation of credit to certain individual sectors. However, efforts are being made that the banks should move towards achieving a CD ratio of 60 per cent in semi-urban and semi-metropolitan areas and in rural areas it should be 50 per cent. However, there are certain inhabiting factors like absence of infrastructure facilities due to which banks are not able to achieve the targets. Credit Deposit Ratio targets have been issued as an instruction to the banks in every State. It is not issued in the form of a directive under the provision of the Banking (Regulation) Act which indicates the purpose for and the circumstances under which the directives can be issued. Hence it is not mandatory.

7.7 Regarding State-wise variation in achievement of Credit Deposit Ratio, the Committee observed that in respect of Jammu Kashmir, North-Eastern States and Lakshadweep, Daman & Diu, the Credit Deposit Ratios have been very low. The Credit Deposit Ratio has been almost 80% in the southern regions, 59% in the northern region, 49 per cent in the North-Eastern region and 55% in the eastern regions.

The CD ratio has been also variant in respect of semi-urban, urban and rural areas. The CD ratio has been higher for semi-urban and urban areas.

7.8 The Committee notes from the information submitted and the evidence tendered by RBI that there are big variations in CD ratio of the banks in the various States. The Committee desires that effective steps be undertaken at the State-level to rectify persistence of low level of CD ratios. The Committee feels that lack of productive opportunities has led to the existence of low levels of CD ratios in certain States and regions. The Committee, also stresses that the Banking Sector should identify more productive opportunities in the States. The Committee feels that there is a need to strengthen the existing banks in the semi-urban and rural areas.

7.9 Reserve Bank of India have stated during evidence that it may not be possible to have a target CD ratio as a mandate for all banks to follow. However, the Committee recommends that earnest efforts be made to ensure the achieving of the uniform All-India average of CD ratio. The regional imbalances and variations in State-wise CD ratios should be removed in the interest of balanced growth and development of the economy of the country.

STATEMENT OF CONCLUSIONS/RECOMMENDATIONS OF THE STANDING COMMITTEE ON FINANCE CONTAINED IN THE REPORT

Sl. No.	Reference of Para No. of Report	Conclusions/Recommendations
1	2	3
1	1.8	The Committee note with concern the frauds and irregularities that have taken place in the banking system in the recent past. There appears to be a total failure of audit in banks. The Committee feels that the audit of accounts in Banks needs to be improved so as to avoid system failures and financial scandals. The Committee, therefore, recommends that the frequency of audit of banks should be increased from the present once in three years to atleast once in two years. It should be ensured that efforts are made to cover maximum number of branches. The norm regarding annual audit of large branches should be followed scrupulously. The RBI should take initiative to see that audit reports are properly scrutinised and are complied with by the bank management. The system of follow up and corrective action on these reports should be strengthened. A time limit should be fixed for compliance of audit objections. In the context of rising frauds and irregularities, the Committee is of the view that a detailed audit which operates simultaneously with the transactions will be very useful. The Committee, therefore, recommend that the concurrent audit of large branches should be introduced immediately. The Committee further recommends that the Standing Advisory Committee of RBI should also evaluate the performance of audit firms and any acts of ommissions and commissions on their part should be strictly dealt with.
2	1.9	The Committee strongly recommends that Parliamentary accountability of Banks should be enforced through audit of Banks by Comptroller & Auditor General of India for which the modalities should be worked out at the earliest.

1	2	3
		In this context, the Committee are at a loss to understand as to why the entire banking and financial sector of the economy has been kept outside the purview of C&AG audit. The Committee is not happy to note that the entire nationalised banking sector alongwith financial institutions, like IFC, IDBI, ICICI and the LIC are not at present covered by CAG audit though these institutions account for a major portion of the country's economic and financial infrastructure and are important agencies to carry out Government policies for development and public welfare. This Committee does not feel that there is any merit in the Ministry's argument that the banking sector should not be brought under CAG audit because CAG audit was primarily rule bound and banking activity necessarily involved a measure of discretion. There is also no weight in the argument that the nationalised banks and financial institutions would be discriminated against vis-a-vis the foreign banks, since the letter would be outside the purview of CAG audit. This Committe, therefore, recommends that the audit of the nationalised banks and other financial institutions which are Government owned or Government controlled should be brought under the control of C&AG who should select and appoint Statutory Auditors and carry out a supplementary audit through its own officers just as is done in the case of Government companies and other public sector undertakings. Bringing the banks under the CAG audit would ensure that a vital component of the economy is not left outside the purview of CAG's jurisdiction. This would also go a long way in restoring public confidence and credibility of the banks and other financial institution.
3	2.9	The Committee, therefore, recommends that there should be a separate independent authority for Vigilance in Banks, the staff for which should be from outside the banks. The Chief Vigilance Officers should be appointed by RBI or CVC from outside, having a separate channel of promotion. The Chief Vigilance Officer should send regular reports on quarterly basis to Central Vigilance

1	2	3
		Commission and to the Department of Banking, Ministry of Finance. The Reports should name the delinquent officers. The Ministry should ensure proper follow up action on vigilance reports within the prescribed time frame.
4	2.10	The Committee also recommends that the Ministry of Finance should frame certain rules governing the re-employment of retired senior executives in the private companies. The rules should prescribe penal action in case of violation as it has been seen that Senior Executives are very liberal in granting loans to the private companies when they are on the verge of retirement, after which they manipulate their re-employment in these companies. The Committee recommends that the provision of no employment within 2 years of retirement should be strictly followed. The Committee further recommends that the preventive vigilance should also be encouraged in the banks. For this the help of staff unions and the Customers' Committees etc. should be taken.
5	2.11	With regard to the security aspect of the banks the Committee notes with concern the previaling security environment in various states affecting the banking operations and the money which the government have to spend on the protection of the bank properties as well as bank employees. The Committee recommends that state Government should be entrusted with the responsibility of beefing up security for the banks. The question of providing suitable type of weapons to the bank security guards should be taken up in the Ministry of Home Affairs and examined in the light of prevailing security environment in each state.
6	3.8	The Committee note with concern that the cases of defaults in RRBs are on the high side though their performance in achieving the objectives of providing credit to economically weaker sections and channelising their savings is laudable. In the matter of deposits, the rural banks are placed on better footing than the nationalised banks. The Committee express their unhappiness over the sad plight of RRBs. The financial position of these banks is

1	2	3
		deteriorating and the Government appears to be complacent in improving viability of these banks. The Committee recommends that the Government should examine the question of reducing the number of RRBs by way of merger etc. to make them viable. More facilities should be extended to those banks like drawal of refinance from NABARD. The relaxation in eligibility criteria for refinance allowed to RRBs in North-Eastern region should be extended to RRBs in other states also. RRBs can also consider lending funds to industries being set-up in backward areas.
7	3.9	The Committee also express their resentment over the fact that rural banks are operating only as agencies of commer cial banks to collect funds from rural people and siphon them off to the cities. The Committee, therefore, feels that some C.D. ratio should be fixed for these banks to ensure that funds collected from the rural people are available to them for the economic development of that area.
8	3.10	The main objective of the Rural Banks is to meet credit needs of the Weaker Sections of Society in rural areas. The Committee therefore, recommend that a 'National Rural Bank of India' should be set up and all RRBs should be broguht under its control. This step would go a long way in improving the viability of Rural Banks. The Government should allocate sufficient capital to it to ensure its expansion and development. The National Bank should guide RRBs and monitor their activities. The Government may consider whether the National Rural Bank of India should be a single Central Bank or their should be several Zonal Rural Banks with independent headquarters and functioning.
9	3.11	The Committee was informed by the Govt. that out of 196 RRBs there are 173 RRBs which are loss-making and 23 RRBs which are making profit. In this connection the Committee feels that the factors contributing to the success of some RRBs should be identified so that the working of loss making RRBs could also be improved.
10	4.11	The Committee is distressed to note that out of twenty nationalised banks, three banks are without full fledged Managing Director/Chairman. It is surprising to note that the post of Chairman and Managing Director of Andhra

1	2	3
		Bank is vacant for more than one year. The Committee further notes that posts of Executive Director are lying vacant in four nationalised banks, ranging from one and half year to one month. The Committee considers this situation as most unfortunate and cannot but deplore the lackadisical manner in which Government have handled the matter. The Committee is of the view that for effective functioning of any organisation and particularly nationalised banks, which cater to the needs of people at large, there ought not to be any vaccum in top management. The delay in appointments to such high posts not only hampers the smooth functioning of banks, but also has a cascading negative effect on corporate goals and implementation of financial policies. The Committee also finds that in terms of Nationalised Banks (Miscellaneous Provision) Scheme 1970-1980, while the Government has assumed unbridled powers to appoint or remove at will both whole time and other Directors, the non-appointment of Chairman/Managing Directors and Executive Directors leads to the irresistible conclusion of usurping powers of the Board of Directors by the Ministry through over-centralisation.
11	4.12	The Committee is informed that non-official Directors represent the interests of varied field such as of staff and non-workmen staff, depositors, farmers, workers, artisans, small-scale industries etc. The Committee further observes that in none of the nationalised banks, the vacancies of non-official Directors, as stipulated in the statute, have been filled up. The Committee are perturbed to note that the tenures of these Directors have already expired and they are continuing in their positions pending appointment of their successors. Even in the RBI, which is the nodal bank and is the Banker of banks, there exist a large number of vacancies both at Central and Local Boards. The Committee is at a complete loss to understand the manner in which the interest of artisans, farmers, depositors, whose interest these non-official Directors represent, would be served, in the absence of their representatives on the Board of Directors. The Committee desires that the Government should explain to it the reasons for not filling up the vacancies of non-official directors on the Board of Directors of the Banks.

1	2	3
12	4.13	The Committee, therefore, recommends that in future no vacancy should remain unfilled for any length of time including the post of both Chairman-cum-Managing Director and Executive Director. Under no circumstances should both these posts remain vacant simultaneously. The Government should do some advance planning in the matter of filling up the vacancies on the Boards of Directors of various Banks. The Appointment Board should prepare bank-wise, a list of Directors, official as well as non-official, who are due to retire in the calander year and should take immediate steps to fill up those vacancies. The Committee desires that the Government should ensure with certainity that non-official directors automatically cease to be in office after the date of expiry of their term and not remain in office till the appointment of new directors. The Committee recommends that quarterly reports be sent to this Committee regarding vacancy position on the Board of Directors and the action taken by the Government to fill up those vacancies.
13	4.14	The Committee further recommends that the Appointment Board should also be restructured to include a group of eminent presons such as retired Governors of RBI, Judges of Supreme Court and High Courts, former C&AG and other widely respected persons in the financial field. The Board should also be empowered to make recommendations regarding removal of Directors from the Boards of Banks.
14	4.15	The Committee also note that there is limited availability of persons for filling up the posts of Chairman-cum-Managing Directors and the Executive Directors. The Committee recommends that the area of consideration for such posts should be further enlarged by including persons from the private sector and the universities, non-banking financial institutions and state financial institutions etc. so that the wider choice is available.
15	4.16	The Committee also observes that there is shortage of manpower in banking sector as the banking career has not remained that attractive as it once used to be. There are frequent instances of people leaving Bank Service to join the All India Civil Services. The Committee, therefore, recommends that immediate steps be taken to make the

1	2	3
		banking career more attractive and purposeful. The Government should also examine the possibility of introducing an All India Banking Service on the lines of other All India Civil Services to attract the best talent for the banking sector.
16	5.11	The Committee note that inspite of constitution of several Committees such as Customer Service Committee function ing at branch level, Customer, Service Centres in State, Capitals and major cities etc., the grievances of customers are yet to be satisfactorily redressed. Though banks have made several improvements in customer service, the requirements and demands of customers have also witnessed a steep rise.
17	5.12	The Committee further notes that Goiporia Committee made 97 useful recommendations and these have been categorised into four groups for the purpose of implementation. The Committee is distressed to note that inspite of clear cut instructions to implement recommendations under Group 'A' straightway, the progress made by the banks in implementing these recommendations is far from satisfactory. This Committee desires that the process of implemention of the recommendations of Goiporia Committee should be expedited and the Committee may be kept informed about the stage of each recommendation implemented by each nationalised bank.
18	5.13	As after nationalisation most of the branch expansion has occurred in the rural and semi-urban areas, the Committee recommends that special cells be created in each bank to oversee the provision of Customer Services in branches in those areas. Even though the Customers Services have improved in cities in some respects there has not been any appreciable improvement in rural areas. As the literacy rates in those areas are low, they are not able to make use of various fora available to oversee the Customer Services. Hence, it should be made the responsibility of Branch Managers to oversco the availability of various Customer Services in his branch. He should encourage the formation and working of Customer Services Committees, under his Chairmanship consisting of account holders in his branch. The norms for frequency of those meetings should also be prescribed and quarterly reports with controlling office

1	2	3
		should be filed. It should be examined whether the auditor can be entrusted to specifically oversee the provision of customer services in rural and semi-urban areas. Special Surveys be made in these areas on the lines of the surveys done by Indian Banks' Association and the conclusion/outcome of these surveys should be implemented in a given time frame.
19	5.14	With the rapid expansion of banking sector, the system is now finding it difficult to cope up with the load of servicing more branches manually. Keeping in view the need to improve customers service and house-keeping, the Committee recommend that banks should urgrade their technology to bring mechanism, automation and computerisation in their operations. The banks should introduce Advanced Ledger Posting Mechines (ALPMs) at the branch level, mini computers at Zone/Regional Office level and mainframe computers at Central/Head Offices. However, the Committee feel that the introduction of these machines should not be indiscriminate but should be need based. A detailed programme should be chalked out by the Banking Division, Ministry of Finance and it should be implemented by all the banks in a given time. The Committee also finds that banks have made little efforts to dispel the fear of staff unions towards automation and computerisation of work in banks. This should be given top priority and cooperation of staff unions should be sought in the matter. In some cases even after agreements with the staff, little progress has been made by the banks in automation and computerisation. The Committee, therefore, recommends that banks should earmark sufficient funds for computerisation etc. every year to meet the competition from private and foreign banks in providing best customer services.
20	5.15	The Committee notes that in spite of Constitution of several committees, the grievances redressal mechanism is not yet satisfactory. The Customers still have to move Civil Courts for settlement of their claims. There is thus a need to overhaul the grievance redressal machinery. The Committee, therefore, recommends the institutions of Lok Pal on the pattern of Bank Ombudsman of United Kingdom for each nationalised bank. The Bank's Lok Pal should be a person of repute, preferably a retired

1	2	3
		Supreme/High Court Judge or a retired Comptroller and Auditor General of India with a fixed tenure to deal with complaint and matters and pertaining to deficiency of service by the banks. He should also be authorised to grant relief to bank customers including monetary relief wherever he thinks it necessary. The decision of the Lok Pal should be binding on the banks.
21.	6.6	This Committee observes that though the objective of the new norms was laudable, monitoring by RBI, of the actual application of these norms by the banks was poor in as much as the accounts of various banks as audited and published, disclosed continuance of varying accounting practices adopted by individual banks to suit their needs. It seems that in their anxiety to show higher profits or lower losses certain banks not only flouted the Reserve Bank of India's Circulars but also adopted accounting policies which were devoid of financial prudence. The Punjab National Bank accounted for a large income on scam hit securities, the ownership of which is not known. Financial conservatism and propriety demanded that no uncertain income be looked on this account till the issue of ownership was settled. Similarly, some banks treated interest suspense as a provision and reduced the requirement of current year's provisions substantially. Varying treatment has also been given in respect of provisioning for loans below Rs. 25,000/- and the Reserve Bank of India stipulation for an additional 2.5% provision has not been strictly adhered to by all banks. This has resulted in substantial under-provisioning. What is surprising is that RBI/Ministry nominees on the Boards of various Banks allowed the flouting of RBI's Circulars without raising their voice when they should have forcefully dissented on such matters. It is thus clear that the application of new RBI norms is not yet uniform and consistent and the Committee strongly recommends continuous and active supervision by the RBI in this regard.
22.	6.7	On the aspect of unreconciled amounts in — Inter Branch Suspense Accounts; — Drafts Paid without advice; and — Interest accrued and payable etc. the Committee is constrained to note that many banks have huge amount of reconciliation to be carrried out and

1	2	3
		satisfactory progress in this regard is not being made. The Committee are at a loss to understand how financial statements can be expected to present a true and fair picture if huge amounts are pending for reconciliation. As these are major fraud prone areas, this Committee recommend the accomplishment of this task at the earliest. The Committee note that some banks are giving due priority to these areas of work but regret to note that what has been touched is only the tip of the ice-berg and much more progress remains to be made. The committee was not able to get all the information regarding unreconciled amounts for many banks and concluded that the position was absolutely unsatisfactory.
23.	6.8	The Committee is also constrained to note that many bank managements in their enthusiasm, to show higher deposits and advances have been window-dressing their results. This has been achieved by:— (a) Putting in certain entries in bank reconciliation; (b) Purchasing certain cheques sent in collection on last date and shown as advances and deposits. No discounting charges are levied in such cases; (c) Under-provisioning of employees expenses though advances have been taken by employees for travelling, LTA, medical etc.; and (d) Under provisioning of interest payment on large number of fixed deposits on the plea that the same have matured. In certain cases FDR's held as margins against guarantees, etc., have been overdue for number of years. Neither these have been transferred to overdue fixed deposits nor any interest is provided thereon. Prudence demands that a provision be created for interest in such cases. In addition to the above methods, the banks used several methods, technical in nature, to show exaggerated performance. The Committee suggest that the RBI does a strict monitoring to check such malpractices.
24	6.9	The Committee notes that a sum as large as Rs. 5700 crores has been provided for capital adequacy in 1993-94 for various banks. This steady erosion of Equity has not

1	2	3
		taken place over-night but over the years due to poor accountability of those in-charge. In this regard, it is pertinent to point out that major losses have been due to mounting bad debts. The Committee addressed itself to this problem and in fact called for the names of top defaulting parties and industrial houses. In reply, however, the Government stated that in accordance with the statute and practice customary among the banks, these names could not be disclosed, as also the quantum of bad debt and doubtful debts incurred cumulatively.
25	6.10	This Committee appreciates fully the inherent risk in the nature of lending by banks. However, it cannot but observe that while the judgement and discretion of the bank authorities cannot be questioned, the results of this evaluation should certainly be reflected in the assessment of individuals. In other words, a bad judgement should be visited by some loss for the person who made the judgement. The Committee feels that over the years, banking business, especially lending, has been carried out in such a flippant and casual manner that today it is the entire nation which is bearing the loss in the form of compensation by Government towards eroded capital bases of banks. In this regard, the Committee recommends that banks evolve a methodology of working whereby there is a relationship between the number of good decisions taken by a Manager and the assessment of his performace. The Committee cannot but note with regret that precious resources of the State have been frittered away in the nature of bad debts in the form of ventures which were either unviable or fraudulent. The Committee recommends that Government should also examine the total elimination of secracy laws, so far as these prohibit the disclosure of the names of defaulters in refund of bank loans.
26	7.5	The Committee is of the view that the real problem in priority sector lending is the lack of availability of timely credit. All out efforts should be made to ensure time availability of credit by strengthening the resources position of the banks in rural areas. The Committee is of the view that the question of Statutory Liquidity Ratio (SLR) and Cash Reserve Ratios (CRR) should be thoroughly gone into to enable the banks to plough more funds in the priority sectors. The Committee also feel that

1	2	3
		overhead costs in running the rural branches should be checked so that more funds are available for lending purposes. The Committee feel that deregulation of rate of interest should be undertaken in a phased manner and the lending rates for tiny sector should not be changed. The rate of interest for tiny sector borrowings upto Rs. 25,000 in rural areas used to be 5 to 6 percent which has been increased to 12 per cent recently. The Committee recommends that tiny sector borrowings should continue to get some preferential treatment as before. The bank should also give high priority to the recovery of loans and overdues. Lending to the priority sector does not mean that assets should not be well performing. The banking system should be able to identify good quality small scale industries that have potential for profit. For this the banks can tie up with the District Industries Centres in their area of operation and publicise schemes for which they can provide credit to the people in rural areas. The Committee further recommends that the norms of 40% lending to the priority sectors should be strictly adhered to and the banks should deposit the shortfall in the prescribed percentage with NABARD. All these steps, the Committee feel, would go a long way in generating adequate funds for priority sector lending.
27	7.8	The Committee notes from the information submitted and the evidence tendered by RBI that there are big variations in CD ratio of the banks in the various States. The Committee desires that effective steps be undertaken at the State-level to rectify persistence of low level of CD ratios. The Committee feels that lack of productive opportunities has led to the existence of low levels of CD ratios in certain States and regions. The Committee also stresses that the Banking Sector should identify more productive opportunities in the States. The Committee also feels that there is a need to strengthen the existing banks in the semi-urban and rural areas.
28	7.9	Reserve Bank of India have stated during evidence that it may not be possible to have a target CD ratio as a mandate for all banks to follow. However, the Committee

1	2	3
		recommends that earnest efforts be made to ensure the achieving of the uniform All-India average of CD ratio. The regional imbalances and variations in State-wise CD ratios should be removed in the interest of balanced growth and development of the economy of the country.

MINUTES

STANDING COMMITTEE ON FINANCE

Seventh Sitting

2.7.93

The Committee sat from 1030 hrs. to 1300 hrs. and 1500 hrs. to 1740 hrs.

PRESENT

Dr. Debiprosad Pal—*Chairman*

MEMBERS

Lok Sabha

2. Shri Chandulal Chandrakar
3. Dr. K. V. R. Chowdary
4. Shri Prithviraj D. Chavan
5. Smt. Maragatham Chandrasekhar
6. Shri P. C. Chacko
7. Shri Mahendra Kumar Singh Thakur
8. Shri Sushil Chandra Varma
9. Shri Jeewan Sharma
10. Shri Chetan P. S. Chauhan
11. Shri Dileepbhai Sanghani
12. Shri Manabendra Shah
13. Shri Sartaj Singh Chhatwal
14. Shri Harin Pathak
15. Shri George Fernandes
16. Shri Abdul Ghafoor
17. Shri Nirmal Kanti Chatterjee
18. Prof. Susanta Chakraborty
19. Shri T. J. Anjalose
20. Shri Bhogendra Jha

Rajya Sabha

21. Shri Jitendrabhai Labhshanker Bhatt
22. Shri Triloki Nath Chaturvedi
23. Shri K. R. Jayadevappa
24. Shri Chimanbhai Mehta
25. Shri Rajubhai A. Parmar
26. Shri Ashis Sen
27. Shri Surinder Kumar Singla
28. Shri Arangil Sreedharan
29. Shri S. Vidhuthalai Virumbi

SECRETARIAT

1. Shri Satish Loomba — *Deputy Secretary*
2. Shri Ram Autar Ram — *Under Secretary*

REPRESENTATIVES OF THE DEPARTMENT OF ECONOMIC AFFAIRS, MINISTRY OF FINANCE AND RESERVE BANK OF INDIA

1.	Smt. J. Kathpalia	—Additional Secretary, Deptt. of Economic Affairs.
2.	Shri R. V. Gupta	—Additional Secretary, Banking Division, Deptt. of Economic Affairs.
3.	Shri Dinesh Chandra	—Joint Secretary, Banking Division, Deptt. of Economic Affairs.
4.	Shri N. Mookerjee	—Joint Secretary, Banking Division, Deptt. of Economic Affairs.
5.	Shri V. B. Srinivasan	—Joint Secretary, Deptt. of Revenue.
6.	Shri P. J. Nayak	—Joint Secretary, Deptt. of Economic Affairs.
7.	Shri K. Srinivasan	—Joint Secretary, Banking, Deptt. of Economic Affairs.
8.	Km. V. Visvanathan	—Executive Director, Reserve Bank of India.
9.	Shri J. R. Prabhu	—Chief Officer, Reserve Bank of India.
10.	Shri R. K. Jalan	—Chief Officer, Reserve Bank of India.
11.	Shri N. T. Hariramani	—Chief Officer, Reserve Bank of India.
12.	Shri M. D. Patra	—Director, Reserve Bank of India.

2. At the outset, the Chairman welcomed the representatives of the Department of Economic Affairs and RBI and invited their attention to the provisions of Direction 58 of the Directions by the Speaker. The Committee then undertook evidence of the representatives on the Banking system in the country. The Chairman requested the Members to make enquiries and hold discussion on the list containing 16 selected points circulated to the Members and made available to the Ministry facilitating them to resolve the queries.

3. The Members then asked the representatives to explain the position of auditing of the Banks; security in banks; formation of National Rural Development Bank; Customer service in the nationalised banks; promotion policy in the banks; inter-bank reconciliation of accounts; capital adequacy norms; the role of public sector banks in the liberalised scenario; international financing and privatisation of public sector banks.

4. The representatives of the Department of Economic Affairs (Banking Division) and RBI explained the queries of the members raised at the meeting. The points raised and the replies given thereto were as under:—

5. The representatives of the Banking Division informed the Committee that the audit of the annual accounts of the banks is governed by the respective status applicable to the category to which the banks belong. In terms of Banking Regulation Act provisions, the appointment of statutory auditors for auditing their annual accounts in the case of private sector banks and foreign banks needs the prior approval of the Reserve Bank of India. The private sector banks every year approve the appointment of auditors in their annual general meetings and then send to Govt. for approval. But in the case of foreign banks, the names of audit firms are sent by them to Government for approval. The appointment of auditors for auditing the accounts of 20 nationalised banks is subject to the approval of the Government of India. The appointment of auditors in the case of State Bank of India is subject to Reserve Banks' approval. In the case of 7 associate banks of the State Bank, the appointment has to be done with the applroval of the State Bank. There is a Standing Advisory Committee set-up by Reserve Bank of India for the nationalised banks. This Committee has officials from the RBI, Banking Department of the Government, C&AG and the NABARD. The Committee meets twice in a year and draw up the criteria for empanelment of auditors for auditing the accounts of the nationalised banks. After the approval of the criteria by RBI, the C&AG gives the names of all the Audit firms who satisfy these criteria. The entire list is scanned by Government with reference to the audit experience of those persons, the number of partners, the period for which the partners have been with the firm and several other criteria. Thereafter, the lists of the auditors is sent by Government to different banks depending on the size of each bank. It could be 4, 5, 6 or 7. In the case of State Bank of India, each local circle has statutory auditor. Therefore, there are 13 statutory auditors for the State Bank but a complete list is sent to the Banking Department for approval. Once they clear the names, it is communicated to the banks. But the auditors are appointed by the Board of Directors. The Standing Advisory Committee also looks at the terms of remuneration. The haulting allowance is to be paid. The hotel accommodation to be entitled and cash fees for audit. These reviewed over 3-4 years. The tenure of each approved firm which is appointed for statutory audit is normally 4 years.

6. The statutory auditors who do the audit at the head office of the banks do not look into the individual accounts and how they have been disbursed. This is generally looked at by the branch auditors which are about 30,000 in number. The Chartered Accountants, who audit accounts, are required to comment on the advance portfolio of the banks. Here large-scale irregularities have taken place. They are not obliged to look into every single account. The Bank auditors do test check of some of the banks. They do not look into the end-use of funds in each and every account. Even the branches are selected on a random basis once in 3 years and the branches are not audited. If the RBI has any ground to believe

that there has been misuse of credit facilities extended by the bank in a big way and there are reasons also to consider that an external auditor should look into credit facilites, then the Government has been appointing special auditors under another provision of the (Banking Regulation Act) which empowers the Government to prepare detailed reports on those areas.

7. The witness also informed that in accordance with the recommendations of the Ghosh Committee on frauds, the question of concurrent audit for very large branches is also being considered. The concurrent audit will be a more detailed audit and it will be operating simultaneously with the transactions. As and when the transaction takes place audit also takes place. Large branches which have the business turn over of Rs. 1 crore are audited by branch auditors every year. Residuary Banks of lesser turn over annually are audited once in 3 years by rotation. The branch is audited by external auditors but there is a continuing system of auditing by the banks internal audit, the periodicity of which is about 12 to 18 months. On being suggested to have the audit of banks done through C&AG, it was told that the Government is not in favour of bringing the audit of banks under C&AG because there would be some element of difference in all the banks. There are some local banks also. The banks which are under the control of Government, can be put under C&AG. But there is no right to audit all private companies by C&AG. The Government can, however, have a separate body for auditing to improve the system and this is under Government's consideration. If one looks at any audit which is done by the C&AG, it is to see whether the expenditure is made in the correct way. Loans will go bad to some extent. The question is whether there was malafide in loans. There is an element of discretion in lending money. Lending itself will become very difficult. Here is also the problem of customer satisfaction. So, all these factors will have to be kept in mind. The witness further told that the complaints are received from some branch managers in the past that the auditors intended to be extended loans for giving good audit report. In such cases, the audit firms are disqualified.

8. The witness admitted that there are large number of bad debts and expressed their inability to declare them because of secrecy provision of the Act. This could be made possible if the Act is suitably amended and recommendation to this effect was made by the Committee.

The witness then informed the Committee that 25% of auditors are changed and 75% continue. There is no obligation for the Government to continue the remaining auditors who continue to be eligible and who are to complete the 4 year term and if an information is received that they, are not doing the audit properly, they are immediately withdrawn for the rest of the period. Such firms are not even included for the ensuing audit for the subsequent year.

The Committee suggested that the audit of banks should be put under the control of C&AG. The Committee also suggested that the auditing of accounts of all the banks should be done every year by the auditors and to achieve this goal, if need be, the Act may suitably be amended.

The Committee noted that there are large number of bad debts. The Ministry was not in a position to disolve the names of top defaulters in view of the secrecy provision of the Act. The Committee felt the need of amending this Act.

9. The witness informed the Committee that in 1991, the Government of India ordered that a high level Committee might be set-up by RBI to go into all the aspects of the matter and come out with recommendations. This Committee was appointed under the Chairmanship of Deputy Governor Mr. Ghosh. CBI and all other professionals were represented in this Committee. After a detailed examination, the report of the Committee has been accepted and the RBI has made an implementation schedule in the meeting. All the recommendations have been divided into 3 categories:—

(i) Which the banks can implement by themselves;

(ii) Where RBI has to direct the initiative and take the action to implement; and

(iii) Where the approval of the Government is necessary and the recommendations have been divided into 3 groups and each bank has been asked to go by them.

10. The witness also informed the Committee that the instructions have been issued from December onwards and the implementation has started. 53 recommendations have been completed and the remaining 5 are yet to be completed. The Committees recommendations are preventive vigilance. They have identified the vigilance prone areas. The Chief Vigilance Officer has suggested that a Vigilance officer be appointed from outside and not from the bank. Either RBI or some other banks provide the officer who is selected from the panel of officers. He is directly reporting to the CMD and his performance is being watched by the Chief Vigilance Commissioner. A new CR format for him has been advised. Even regarding the CMD, the Chief Vigilance Officer has a right to give his complaint or give factual information to the Chief Vigilance Commissioner by a special D.O. letter. If there are failure and malpractices commited by him, the Chief Vigilance Officer need not to sleep over it. He has authority to give his verbal or written complaint. Based on that the CVC will take an urgent action to go into this. Vigilance Officer is necessarily to be a banker, otherwise it will not be possible for him to pass his judgement. Hence Vigilance Officers are from the banks in which they are already serving.

11. The witness further informed the Committee that the Government was seriously concerned about security aspect of the banks as well as the banking operation mainly in Jammu & Kashmir area. In the valley, it was

not possible for any bank to function. All the officials are kept in hotel and paid virtually without any work. The Minister in-charge of Kashmir Affairs recently convened a meeting and he was briefed about it. The Chief Secretary had been asked to find a method by which a bank which is taking up a small enterpreneur, passes an employment schemes are given complete protection so that the different schemes of the Government of India were implemented in the State also. In the North-East, the Nagaland Chief Minister had given an assurance to the Reserve Bank that the full protection would be given if the Branches are opened. The bank employees had their own problems. They have made representations. The Home Ministry has seized the matter. The matter was being worked out in such a way that the State Government's security arrangements are ensured before the banks are able to operate. In the case of Punjab State, ITBP Batallions are raised and Government was spending Rs. 6 crores to see that the branches are protected. The position in the Punjab has improved to a great extent. Government is thinking of withdrawing slowly the extra forces to the extent possible. In Nagaland for instance, 43 State Banks of India branches are closed, for want of security.

12. There is a State-level Security Committee set-up by RBI for each State. This Committee holds meetings regularly and give information to the R.B.I. about the Security position. When a bank has not been able to function due to security reasons they have to report to the RBI as well as to the Government of India, if it is a nationalised bank. There is a Security Cell in the RBI to monitor the incidents and issue suitable instructions. Each public sector bank has a Chief Security Officer and there is a meeting of CSO's held regularly to find out what are the problems. They are connected with special telephones. They have been divided into 3 areas, namely high risk, medium risk and low risk areas. As per security instructions security arrangements are given to them. Where there is difficulty of communication, the Government is in touch with the Communication Department to sort out the problem.

After hearing the above views of the representatives of the Ministry, the Committee felt that the Government should think of some other system of having vigilance officers who do not belong to the banks. One alternative is that we might have officers from other banks who have some knowledge of banking. He might be imparted training and then posted as a vigilance officer. Another alternative that could be thought of to have the state cadre of IPS and IAS officers and Indian Audit and Accounts officers to be appointed as vigilance officers of the banks with a view to have an effective system in detecting the malpractices prevailing in the banks.

13. The witness explained the matter in detail and stated that there is a feeder cadre for Chairman of banks and Executive Directors of banks for filling up the vacancies. A person who has experience in financial services and banks is required. So the feeder cadre is from the 20 Nationalised Banks, State Bank of India, the 7 Subsidiary Banks, the banking financial

institutions and beyond that there are a few private banks in the country and few foreign banks. The salary structure of the foreign banks as well as the private banks is somewhat out of tune with our salary structure. Even if they are reconsidered, the assessment is that they will perhaps be not very keen to come as far as zone of consideration is concerned for Executive Directors or at the level of General Manager. There is a limited availability of persons who fulfil the criteria having put in 20—25 years as General Manager. The Governor, Reserve Bank presides over the appointments Board which consists, amongst others, the Secretary (Banking) and Deputy Governor of the RBI. They can make recommendations. The Committee felt that the problem was not in the selection, but in the feeder cadre which needed to the improved. The quality of people coming into the banking services was to be improved.

The Committee was told that the people joining the SBI leave it for another Central service which consider to be better. Better incentives are needed to be improved within the banking system. Within the system, the training orientation needs improvement for managing the higher posts. The quality of people had been deteriorating over a long period.

14. After 13 years of implementation of Pillai Committee Report, there had been no standardisation of promotion policy or transfer policy in the banks. Each nationalised bank follows a separate system. There are two kinds of persons; one who are very enthusiastic to do the work and others who just do their daily prescribed quota, and for that two track system is required to be built.

15. In branches, the staff is much less compared to the regional offices. In most of the banks, the regional office is doing nothing but a job of post office but a maximum staff is found in the regional office. Two years bank instructions were issued that there should be drastic reduction of staff in the administrative offices and this reduction should be passed on to the branches but it has not happened. There is no proper monitoring or supervision. It is easy to give advances but very difficult to control and monitor units. This is because of the lack of staff. Staff is needed to man the counter. It is a need which is really neglected. People were working hard and who want to rise their needs to have a separate system for them so that they may work sincerely. These are the people who will take the banks to a certain hight. There are certain banks where the posts of Chairman are lying vacant for more than a year. People have been identified for filling up those posts and recommendation to this effect has already been made. There are people who have got 2-3 promotions but they have not gone out of the city. These people are making a nexus. There should be a transfer policy whereby no officer should remain in one station for more than three years. This policy should apply to special officers, specialised officers and professional officers of the banks. This has to been seen as to how effectively it can be applied because there is a tremendous pressure for transfers and entries are being recorded in the

service books of the officers who apply this pressure which he should not use. The Committee suggested that the vacant posts of the Chairman might be filled up and transfer policy should be made more effective. The Committee also suggested that proper staffing might be done in the branch offices of the banks to have better customer service.

16. The witness informed the Committe that there had been some steps taken for opening more branches in the hill areas and the population covered by the hill areas have successfully come down over a period of time. There are some pockets which are under banks. Right upto 1992, the policy was to have one branch for 17 thousands population normally, but for a hill area, it was 13 thousand. The same has been reached but within that region, there may be some intra-regional variations also. The present policy is that the lead bank of the district is fully competent to apprise the Reserve Bank of India to open new branches. The Reserve Bank is also quite liberal in giving branches. But as far as North Eastern Areas are concerned, there is security problem where the branches are opened but they become unmanageable.

The Committee were of the opinion to have the branches of banks opened in the hill areas where they have not been opened so far.

17. The Committee took the view that large transactions, computerisation, customer statisfaction etc. were the most important aspects. There was not much problem regarding large transactions. The problem was about the ordinary man. Deposits in the banks had gone down as compared to the foreign banks. It is the common people who are going to deposit the money and it is the handful of people who are taking away the money. People to whom they owe their bread and butter, they deal with them in a different way. The recommendation which fall in category 'A' of the report of RBI which call for implementation by the banks straightway without any further examination either in the Government or in the Reserve Bank, form almost two-thirds of the total number of recommendations which cover a very wide area of banking service primarily aimed at providing satisfaction to the larger clientele of average and small means. Another area of the stress laid by the Committee was on speedy collection of outstation instruments. The witness told the Committee that the recommendation was that banks should pay on their own, without being asked to pay, two per cent above the prevailing savings bank rate of interest for the period beyond the normal period prescribed for realisation of outstation instruments. The matter has recently been reviewed and it is decided to raise the penalty further, particularly in the case of instruments deposited into borrowal accounts by clients. The circular is under issue. The banks should be required to pay at the interest rate applicable at the minimum of the commercial rate applicable to advances on delayed credit of outstation instruments to overdraft acccounts and other borrowal accounts. In the case of mail transfers, we have a system that within 7 days the transfer should be

credited and in the case of T.Ts., the amount of the Telegram Transfer should be credited on the third working day after remittal. In the case of the North-Eastern centres where T.Ts. do not reach within three days, it should be three days from the date of receipt of the telegram or the date of receipt of the postal advice, whichever is earlier. On the bill collection, the responsibility is to be fixed not only on the collecting bank but also on the bank which is the banker of the drawee of the bill. Two days have been specified for scrutiny of the bill, two days for transmission, two days for the drawee's banker to scrutinise the bill and two days for payment. If within the total framework of eight days the bill is not paid, the bank will have to pay at the rate of two percent above the saving bank rate of interest.

18. The witness further stated that another major recommendation which had been devised for implementation was extension of the banking hours of the branches till one hour before close of business hours for all non-cash transactions. Now it is just four hours and thereafter no customer can enter the bank. But now the bank will render various kinds of services which do not involve cash transactions, that is receipt of cash of paying out of cash, till one hour before the close of the business hours. They will accept cheques for collected they will collect, passbooks for updated and so on.

19. In case of instruments drawn on local clearance centres where there is total automation, it should be credited on the same day if the amount is upto Rs. 5,000 provided the customer is willing to pay a service charge of Rs. 5/- for this facility. This has become effective from Ist of April, 1993. Banks have been advised and one or two have already introduced this facility. Then bank orders upto a ceiling of Rs. 10,000 will be issued without the name of the beneficiary being written on it. One has the freedom to fill in the name of the beneficiary to whom he wants to pay the money and the deliver it to the payee. This provides for enormous saving in the use of cash for making payments and it also provides for safety of the payment mechanism whereby the need to use cash for large payments to totally obviated.

20. The capital adequacy norms were laid down in 1970. Excepting for a few banks, by and large, most banks are over staffed and there might be a difficulty in few branches who need to be looked at. It is found that when the branch opens in the morning, the previous day's accounts are reconciled instead of doing the same day's work and in a way not doing customer work. In some branches, the productivity norms are high and it needs extra staff. Then 0.7% norms of recruitment is relaxed.

21. As regards the unclaimed deposits, the instruction is that once there are no options in the accounts beyond a period of 10 years such accounts should be segregated and kept in a separate ledger even though it is transferred to a separate ledger, it still continues to be a liability of the

bank. If the customer approaches and asks for the amount, the bank is bound to return the amount.

22. The witness explained to the Committee that the new income and provisioning norms were introduced in the year 1992. Regarding to it, the provisioning had to be made in respect of all past non-performing assets also. This resulted in some banks having position where their assets went below the expected norms. The expected norms are 4% by 1994, 8% by 1986 etc. The need for this has arisen because the balance sheet of banks were to revealing the true position. They were taking note of income which not really come. The non-performing accounts and also provision which had to be made against what was considered as sticky, this was not made adequately. Where the income is not actually being released of their actual accounts, the rule is that the interest could be on quarterly basis. But the banks did generally debit the advance accounts by the amount of interest recovered from the parties and taking to interest account where the borrowers really paid the interest on those accounts and, therefore, it happened that the income which was shown in the profit and loss accounts did not reflect the actual interest on the borrower's accounts. The world over the advances are treated as non-performing if interest is realised within a period of 90 days. The rule laid down for banks is that for the year 1992, if income has not been released for the period of 4 quarters from the date on which interest fell due for payment plus a gross period of 30 days, the account would be treated as non-performing. On that asset, income will not be taken to profit and loss accounts. For the year 1993-94, the norm would be tightened to quarters. If it is not released, it would be recognised as non-performing asset. For 1994-95, it would go to tighten up. It will be 180 days as against international norms of 90 days.

23. Normally, security is not enforced for non-realisation of income. On the NPA, once the asset is treated as a non-performing asset, then it has to be classified. All the assets which are servicing the interest on due date are classified as standard assets.

24. The assets remain as assets of the bank. Nothing is there to make good theft. They had to be utilised. The Government is contributing the money to reach the capital adequacy norm. The money is to be recovered. There is a recovery tribunal which has been constituted. This will reduce the time in recovering the dues. The procedure is very slow. By this system, the delay will be reduced half of the normal time *i.e.* required.

25. The deficit is neutral. It has no impact on the deficit. The sum of Rs. 5700 crores will be given to the banks. Simultaneously, they will invest on the Government securities. There is no cash payment at all. This is not something new. Over the last 5 years, the Government has been making this provision at the rate of 700 crores every year. It has no impact on deficit. There is no cash out go. It is essentially a kind of book entry. This is just a transaction which is only on paper. The point is that this is an

additional money which the Government is keeping into its budget for making a paper allocation. It is adjusted in the profit and loss account of the bank. The interest on the sticky loan would be the income of the bank. If the banks are not allowed to add to the profit and loss account, then the unaccounted income is reduced because the banks never get final income. Secondly, the banks have been maintaining the mercentile method of accounting. The law has also been amended in the year 1992. Loans are not releasable for a certain period of time, then the banks need not show it in the income by way of interest on the sticky loan. Even after the amount is going for, the bank continues its efforts to recover the money and as and when the money is recovered, it is mentioned in the books of accounts. There is no such thing as final writing off till such time as the bank is continuing its efforts to recover this money. Therefore, it can not be said in terms of completely or finally writing off.

26. The majority of 196 regional rural banks are not doing well. There are many options available. Firstly, it has to be seen whether they can be merged with the sponsored banks or whether we can set-up rural subsidiaries banks or whether there should be a National rural bank of India. There have been committees which have gone into these questions. The Kothari Committee of 1989 suggested that this should be merged with the sponsored banks. The Narasimham Committee suggested that there should be rural subsidiaries. There was another suggestion made by some employees of the RRB that there should be a National Rural Bank of India. They have a detailed set of these recommendatins. The RBI thought that the best option would be to merge the regional rural banks with the sponsored banks. This is in line with the recommendation of the Kothari Committee. This is a matter which is currently under examination in the Government at the higher level.

The Committee were of the view that the Regional Rural Banks should not be merged with the sponsored banks. Instead there should be a National Regional Rural Bank of India so that the money of the rural areas is invested in rural areas for the benefit of the rural people.

The Committee then adjourned.

MINUTES

STANDING COMMITTEE ON FINANCE (1993-94)

Eighth Sitting

16-7-93

The Committee sat from 10.30 hrs. to 12.30 hrs. and 1500 hrs. to 17.30 hrs

PRESENT

Dr. Debiprosad Pal—*Chairman*

MEMBERS

Lok Sabha

2. Shri Chandulal Chandrakar
3. Shri Chittubhai Gamit
4. Dr. K.V.R. Chowdary
5. Shri Prithviraj D. Chavan
6. Shri S.B. Sidnal
7. Smt. Margatham Chandrasekhar
8. Shri P.C. Chacko
9. Shri B. Akbar Pasha
10. Shri Jeewan Sharma
11. Shri Manebendra Shah
12. Shri George Fernandes
13. Shri Abdul Ghafoor
14. Shri Srikanta Jena
15. Shri Nirmal Kanti Chatterjee
16. Shri T.J. Anjalose
17. Shri Bhogendra Jha
18. Shri Kadambur M. R. Janardhanan

Rajya Sabha

19. Shri Jitendrabhai Labhshanker Bhatt
20. Shri Triloki Nath Chaturvedi
21. Shri Gurudas Gupta
22. Shri Ghulam Rasool Matto

23. Shri Chimanbhai Mehta
24. Shri Rajubhai A. Parmar
25. Shri Surinder Kumar Singla
26. Shri S. Vidhuthalai Virumbi

SECRETARIAT

1. Shri Satish Loomba — *Deputy Secretary*
2. Shri Ram Autar Ram — *Under Secretary*

REPRESENTATIVES OF THE DEPTT. OF ECONOMIC AFFAIRS, MINISTRY OF FINANCE AND RESERVE BANK OF INDIA.

1. Shri Montek Singh Ahluwalia— Finance Secretary
2. Shri R.V. Gupta — Additional Secretary (Banking)
3. Smt. Janki Kathpalia — Additional Secretary (Budget)
4. Dr. S.N. Acharya — Chief Economic Adviser
5. Shri V.B. Srinivasan — Joint Secretary (BD)
6. Shri N.M. Mookerjee — Joint Secretary (Banking)
7. Shri A. Virmani — Adviser (P&P) DEA
8. Mr. V. Viswanathan — Executive Director, Reserve Bank of India
9. Shri S.P. Kazal — Director, Deptt. of Expenditure, M/o Finance
10. Shri J.R. Prabhu — Chief Officer, DBOD Reserve Bank of India
11. Shri R.K. Jalan — Chief Officer (RPCD) Reserve Bank of India.
12. Shri N.T. Hari Ramani — Chief Officer (Urban Bank) Reserve Bank of India
13. Shri M.D. Patra — Director, Deptt. of Economic Analysis & Planning, Reserve Bank of India.

2. At the outset, the Chairman welcomed the representatives of the Department of Economic Affairs and Reserve Bank of India and invited their attention to the provision of Dir. 58 of the Direction by the speaker. The Committee then undertook evidence of the representatives of the Ministry. The Chairman informed that the Committee had considered eight points, out of sixteen selected points during their sitting held on July 2, 1992. The Chairman requested the members to make further enquiries on the remaining 8 points of the List of Points.

3. The Members asked the representatives to explain the position regarding role of public sector banks in liberalised scenario, international

financing & privatisation of public sector banks, Priority Sector Credit policy of Banks, state-wise Credit Deposit ratio and regional imbalances. Monitoring use of loans and Small Scale lending, Balance of payment position including Balance of trade, Import/Export position and composition of foreign exchange reserves.

4. The representatives of the Ministry & Reserve Bank of India replied to the queries of the members raised at the meeting. The witness informed the Committee that with the new policy decisions taken, the Government expected that the public sector banks would operate in an environment in which there had to be much greater competition within the Banking system without which it would not be possible for the banking system to perform the role which it should perform in mobilising savings of the community and be able to allocate them in all productive areas of the economy. The performance of bank would therefore have to be evaluated in terms of the new criteria that had been laid down by RBI in the form of new prudential norms and capital adequacy norms. The rules governing working of Banking Sector were being changed in order to make the system more prudent. At the same time, the Government were of the view that banks would have to be given more freedom in regard to the decision making powers so that they could truely act as banker, take risk and in taking risks, if they make mistake they should be penalised as in the commerical world. The portfolio allocation in respect of SLR was proposed to be raised to the tune of 40%. If this was done, the banks would have much greater freedom and they could lend money to commerical sector. The Govt. is also asking the banks to make certain provisions for income recognition, profit, capital adequacy norms and expected that Banks would lend prudently.

5. The Committee learnt that Government would ensure that the banking system recapitalise itself not only to Government budgetary support but through raising capital from the market. The Government advocated the dilution in the equity of Banks. However, The Government would retain control over all the banks. More capital will be brought into the banks that would be done by way of broad basing the Board of Directors. Along with that, there would be a major change in the non-banking sector. There were many developments which aimed at stronger regulation taking place all of which would create a much more competitive environment by way of which, it would be possible to mobilise a large percentage of saving of the public to be deployed in the productive purposes. The policy of the Government was that to the extent to which capital of the banks had been impaired because of loan assets quality, there was a need to provide some resources from the budget to make for the impairment of capital in the banking system in order to ensure that banks were put on a sound footing. Provisions of Rs. 5700 crores had already been made in the current year budget,

which would contribute to the capital of bank and help to ameliorate the problems accumulated over the past.

6. The witness told the committee that the Basle Committee had prescribed capital adequacy norms for banks. According to this Committee, the capital of the banks should be equal to 8% of the risk weighted assets of the banks. Internationally these norms were being enforced. If Indian banks do not come to internationally recognised capital adequacy norms, they would beign to be treated as unacceptable and unsound and garantees given by them might not be accepted. The government expected that banks would meet the Basle Committee norms for the commerical part of the loan portfolio and not the Government part. The Government expected that all the banks would reach 4% of the risk weighted assets by March, 31, 1993. 8% norm had to be achieved two years later. For that at least a lot of capital would have to be injected into the banks.

7. The Committee were informed that until new norms were introduced in 1992, the banks were not following a uniform practice. Where interest was not being paid, it was shown as it was paid and added to the loan portfolio. There was no uniform accounting practices laid down by the RBI for the banks to comply with. In mid 80's a need was felt to classify the accounting system according to the health of the banks.

A very detailed code for classification was laid down whereby advances were put into 8 different categories starting from regular advances right down to the bad advances. It was expected of the bank management that they would not take the income of such advances where the interest was not being serviced by the borrowers. But this was not being done uniformally by all the banks even where they did comply income on accrural basis. They were taking it in the interest suspense account. Now the new norms have been coded. The RBI had tightened up its supervisory role. It is setting up a new supervisory Board. The Government would ensure that banks would not be able to misperform without not surfacing in future. They would surface in the annual reports and inspection reports of RBI and then corrective action taken.

8. The Committee come to learn from the witness that the Narasimham Committee had made certain recommendations in regard to merger/ privatisation of public sector banks. The Committe had recommended restructuring of banks where three banks would be operating at Inter national level, 8 to 10 banks at national level and 8 other banks as local banks. The Government were of the view that for top 4 or 5 Banks there would not be any difficulty in adopting new capital adequacy norms. With some cleanup operation they would be able to raise the capital from the public. In the middle category, there would be banks which could be revived and the provision of Rs. 5700 crores made in the budget will take care of their problems. There were banks low down whose performance

under the new norms would be very poor. These banks would have to be merged with stronger banks. On this, no final decision has been taken.

9. The Committee were informed that there were certain banks whose sticky advances were as high as 35%. Ordinarily, these sticky advances should not exceed 7 to 8. Sticky advances of 10% to 12% are manageable. But anything which goes above 10% to 12% is an indication of serious problem. Government expected that with the introduction of new norms the banks would be judged by the proportion of sticky advances. There were situation where bank's advances position and management culture was so bad that it was not worth simply resusciating the banks. There might be case for merging them with another stronger bank. In case of a merger, the capital of the larger was used for the capital of smaller banks. The management of the richer bank prevailed. Merger is a form of closure because the depositors were protected and the stronger banks takes over the operations. The workers are absorbed in the stronger bank.

10. The witness informed the committee that in the priority sector, the credit allocation is 40% of the advances and the 2 main areas were agriculture and small-scale industries. Out of this, 18% was earmarked for agriculture and 16% towards small-scale industries. The recovery of advance in agriculture was about 22% whereas under IRDP sector, it was around 30%.

11. The witnesses informed the Committee that an effort was made in 1988-89 to start imposing priority secotor requirement on foreign banks and they were asked to go up to 10%. Most recently, it was felt that since the Govt. are restricting the expansion of foreign bank branches they will not be able to bring in advances for agriculture. As they are international banks, they should pay a special role in promoting exports. In the area of priority sector credit, the Government was trying to narrow the difference in the treatment between foreign banks and domestic banks by introducing export credit and a social responsibility of the foreign banks because of their particular advantages.

The witness further informed the Committee that in regard to priority sector lending as a whole as far as Indian banks and Banking system were concerned, the general policy was that as far as quality of assets was concerned, there were no reasons why banks should compromise on the quality of assets with the priority sector lending. Lending to priority sector did not mean that the assets should not be well performing.

12. On the question of profitability, the representatives of the Ministry stated that priority sector lending was not of low profitability. It was related to the size of the loan. In the present system, upto 25,000 the interest rate charged was 12%. On 25,000 to 2 lakhs, the interest rate charged was 16% and above 2 lakhs, 16% or above.

13. The witnesses also informed the Committee that there was no policy of the Government to change the differential interest rates (DRI) which

carries an interest of 4%. At the same time, efforts should be made to avoid priority sector from getting locked into low interest rate. In the case of cooperative societies, only 7% of the advances of the banks go into less than Rs. 30,000 category. In the case of rest of lending, the interest rate was 16%. The cooperatives which gave small loan were badly hurt by regulated ceilings on their advances. Because they were not able to earn a productive interest rate. Therefore, they were not able to offer a viable interest rate.

14. The witnesses also informed the Committee that rural credit system depends on cooperative banking system. The deposit mobilisation in rural areas was not what it was expected of. As such, there was a need to restructure the interest rates in the rural sector. Since commercial banks had an interest rate of 11%, they had a wide scope for expanding. The rate of interest in cooperative sectors was 6-7% only. It was not possible for the cooperative banks to part with the margin of less than 4 per cent. If the cooperatives were to mobilise funds and use them in productive ventures, the only way they can do was to help them in regulating interest rate.

15. The witnesses admitted that only a small proportion of the credit needs of the people was made by the organised Banking system. 70% of people financed their needs from the money lenders at a very much higher interest rate. If the system was able to get rid of this interest rate regulation in rural areas, same resources which were today deriving within the banking system into the bands of money lenders, would come back into the banking system and cooperative systems and would flow through them to the rural society with an advantage to both. Only the loser would be the money lender. The real reason was no organised banking system credit could be provided if the interest rate regulations made the provisions of that credit fundamentally unviable. It would go on doing so to the extent to which the State was willing to subsidise the difference. The policy of the State to subsidise that difference had evaporated. It was possible in the early stages of nationalisation because the proportion of credit going to rural areas from the banking system was very small the financial viability of doing this with the present regulation of interest rate become impossible. This called for deregulation of interest rate which the Government were trying for.

16. The witness then informed the Committee that percentage of debts in large and medium industries was 13.7% for small-scale industries 22.7%, agriculture 22%, the other priority sector 32% and others 12%. While all industries in agriculture had practically the same level of outstandings, large and medium scale industries had a lessor level as a percentage.

17. In regard to the credit deposit ratio and regional imbalances, the witnesses stated that the ratio vary from one State to another and particularly in respect of States like Jammu & Kashmir, North

Eastern States, some of the UTs like Lakshdweep and Daman and Diu. There were factors which were responsible for the CD ratio being low. One such factor could be the absence of infrastructural facilities which prevented the banks from deploying the deposits mobilised in that State locally. There were also situations where the funds that were mobilised in that State were being utilised for industrial or other activities within the State. The accounts were maintained elsewhere.

18. A Task Force had been set-up in the States of Bihar Uttar Pradesh, Rajasthan, Pondicherry, Kerala and West Bengal to look into low level of CD ratio in these States.

19. When asked whether the Government proposed to fix up the percentage of deposit which should be deployed in the State, the representatives of the Ministry stated that it would be very difficult for the banks to limit state-wise allocation of credit to certain sectors. It was informed to the Committee that banks had been directed to achieve a CD ratio of 60%, state-wise. There were certain factors which inhibited to reach the 60% mark.

20. The Committee were informed that the balance of payments position in 1993-94 had been better as compared to 1992-93. But there was an unfilled gap in the balance of payments position, this year of two and a half billion dollars, after allowing for a normal external assistance in flow. The Government estimated that the actual balance of payments gap this year for which the country would have to find special exceptional financing would be only around 1.8 billion dollars. The current account deficit would be around 4.5 billion dollars. Out of this, approximately, 2.7 billion dollars would be through our normal capital in flow of about 1.8 billion dollars. This had to be made up through fast disbursing loans which were available from various multilateral organisations such as World Bank and ADB. Next year, the balance of payment would be under more pressure because IMF loan already taken some years ago would begin to be repaid. The exceptional financial needs would arise in 1994-95 and possibly in 1995-96. To meet this exceptional financial needs, the Government propose to negotiate with the IMF for extending fund facility arrangement.

21. The Committee were informed that the important factor in determining the balance of payment position was behaviour of exports. Saving depends on whether the economic developments will need to strong export growth. It is hoped that this year Government would be able to achieve 15% dollar growth of export. One of the very important factors in the balance of payments was that in spite of liberalisation of export and import and the removal of import licensing, the country had not been flooded with imports. In fact, the level of non-oil imports was lower than 4 years ago.

22. The Committee were also informed that on foreign trade in terms of import and export, the Government had anticipated that there would be a

trade deficit though the first 2 months have actually shown much better position. Imports for the year just passed away was 12.7 billion dollars and exports 18.4 billion dollars. When asked about how foreign exchange reserves were growing when the country had overall deficit in the balance of payment position, the witness stated that basically the foreign exchange reserves had been more or less stationary with marginal increases. The reserves stood at over 6.4 billion dollars. The external debt went up from 68.9 billion dollars in March 31, 1992 to 73.4 billion dollars as on March 31, 1993. The Committee were informed that whenever there was a current account deficit in the balance of payments, it could be by finances or by creating or non-debt creating flows. At the present moment, the non-debt creating flows were negligible. It did not indicate that the external position had been deteriorated. The external account position was more stable and manageable.

23. The Committee were told that the GDP was $5\frac{1}{2}$% in 1992-93, the non-oil imports were lower than in 1991. The Committee were informed that the country was one of the largest debtors but this did not reflect the seriousness of the problem. It overstated because most of our debt problems related to long-term debt problems. Brazil and Maxico had service ratio of 72% whereas India's debt service ratio was 30%. The endeavour of the Government was to bring it down to around 25% which was fairly comfortable and cannot be termed as debt trap.

The Committee then adjourned.

MINUTES

STANDING COMMITTEE ON FINANCE (1993-94)

Thirteenth Sitting
9-11-1993

The Committee met from 1500 hrs. to 1700 hrs. in Committee Room 'C', Parliament House Annexe.

PRESENT

Dr. Debiprosad Pal—*Chairman*

MEMBERS

Lok Sabha

2. Prof. K.V. Thomas
3. Sh. Chandulal Chandrakar
4. Dr. K.V.R. Chowdary
5. Sh. Prithviraj D. Chavan
6. Sh. S.B. Sidnal
7. Smt. Maragatham Chandrasekhar
8. Sh. P.C. Chacko
9. Sh. B. Akbar Pasha
10. Sh. Dileepbhai Sanghani
11. Sh. Sartaj Singh Chhatwal
12. Sh. George Fernandes
13. Sh. Nirmal Kanti Chatterjee
14. Prof. Susanta Chakraborty
15. Sh. T.J. Anjalose
16. Sh. Bhogendra Jha
17. Sh. Kadambur M.R. Janardhanan

Rajya Sabha

18. Sh. Triloki Nath Chaturvedi
19. Sh. Gurudas Das Gupta
20. Sh. Ghulam Rasool Matto
21. Sh. Chimanbhai Mehta

22. Sh. Kamal Morarka
23. Sh. Rajubhai A. Parmar
24. Sh. Ashis Sen

SECRETARIAT

1. Sh. Satish Loomba —*Deputy Secretary*
2. Sh. P.K. Bhandari —*Under Secretary*

2. At the outset, the Chairman welcomed the members and referred to the Draft Reports under consideration of the Committee relating to "Working of the Public Sector Banks" and Action Taken on the Ist Report on Demands for Grants (1993-94), Ministry of Finance.

3. The members then submitted their suggestions in respect of privatisation and merger of nationalised banks and grant of licences for opening up of new banks. The members also discussed the suitability of Audit of Banks to be carried out by *C&AG* of India. The Committee decided to call for imformation from the Ministry of Finance on the following points:

(i) Policy of Government on merger of nationalised banks in view of the deteriorating performance of many of these banks.

(ii) Criteria of Government to select organisation/institution for grant of licences for opening of new banks.

4. As the discussion on the draft report could not be completed, it was decided that the next sitting of the Committee would be held on 26th November, 1993 at 1030 hrs. to consider the Draft Report on the Working of the Public Sector Banks.

5. Pending a policy decision, the Action Taken Report was not taken up for discussion.

The Committee then adjourned.

MINUTES

STANDING COMMITTEE ON FINANCE (1993-94)

Fourteenth Sitting
26-11-1993

The Committee met from 1030 hrs. to 1300 hrs. and from 1530 hrs. to 1715 hrs. in Committee Room No. 50, Parliament House, New Delhi.

PRESENT

Dr. Debiprosad Pal—*Chairman*

MEMBERS

Lok Sabha

2. Dr. K.V.R. Chowdary
3. Sh. Prithviraj D. Chavan
4. Smt. Maragatham Chandrasekhar
5. Sh. P.C. Chacko
6. Sh. B. Akbar Pasha
7. Sh. Jeewan Sharma
8. Sh. Chetan P.S. Chauhan
9. Sh. Dileepbhai Sanghani
10. Sh. Manabendra Shah
11. Sh. George Fernandes
12. Sh. Abdul Ghafoor
13. Sh. Nirmal Kanti Chatterjee
14. Sh. Kadambur M.R. Janardhanan

Rajya Sabha

15. Sh. Triloki Nath Chaturvedi
16. Sh. Gurudas Das Gupta
17. Sh. K.R. Jayadevappa
18. Sh. Ghulam Rasool Matto
19. Sh. Chimanbhai Mehta
20. Sh. Rajubhai A. Parmar
21. Sh. Ashis Sen

22. Sh. Surinder Kumar Singla

SECRETARIAT

1. Sh. Satish Loomba —*Deputy Secretary*
2. Sh. P.K. Bhandari —*Under Secretary*

2. At the outset, the Chairman welcomed the members and placed the draft report on 'Working of the Public Sector Bank' for consideration of the Committee.

3. The Chapter-wise discussion on the draft report was then taken up. Members submitted their suggestions/amendments in the draft report.

4. Then the Chairman proposed that a Drafting Committee should be appointed to make necessary changes/amendments in the draft report. The proposal was agreed to. A Drafting Committee of the following members was nominated:—

1. Shri Nirmal Kanti Chatterjee
2. Shri P.C. Chacko
3. Shri Prithviraj D. Chavan
4. Shri Triloki Nath Chaturvedi

5. It was decided that the next sitting of the Committee would be held on 6th December, 1993 at 1500 hrs. to consider the draft report, as finalised by the Drafting Committee.

The Committee then adjourned.

MINUTES

STANDING COMMITTEE ON FINANCE (1993-94)

Fifteenth Sitting

9.12.1993

The Committee met from 1500 hrs. to 1045 hrs. in Committee Room 'A' Parliament House Annexe.

PRESENT

Dr. Debiprosad Pal — *Chairman*

MEMBERS

Lok Sabha

2. Shr S.B. Sidnal
3. Shri P.C. Chacko
4. Shri Sushil Chandra Verma
5. Shri Dileepbhai Sanghani
6. Shri Harin Pathak
7. Shri Nirmal Kanti Chatterjee

Rajya Sabha

8. Shri Ghulam Rasool Matto
9. Shri Chimanbhai Mehta
10. Shri Ashis Sen

SECRETARIAT

1. Shri Satish Loomba — *Deputy Secretary*
2. Shri P.K. Bhandari — *Under Secretary*

2. The Committee could not transact any business for want of quorum. The Chairman requested the members to send their suggestion on the revised draft Report in writing by Saturday, the 11th December 1993. It was also decided that the Drafting Committee may finalise the report on Monday, the 13th December, 1993 and the next sitting of the Committee would be held on Tuesday 14th December, 1993. Shri Ghulam Rasool Matto was also associated with the Drafting Committee.

The Committee then adjourned.

MINUTES

STANDING COMMITTEE ON FINANCE (1993-94)

Sixteenth Sitting

14.12.1993

The Committee met from 1500 hrs. to 1545 hrs. in Committee Room Parliament House Annexe.

PRESENT

Dr. Debiprosad Pal — *Chairman*

MEMBERS

Lok Sabha

2. Shri Chandula Chandrakar
3. Shri S.B. Sidnal
4. Shri B. Akbar Pasha
5. Shri Sushil Chandra Verma
6. Shri Chetan P.S. Chauhan
7. Shri Dileepbhai Sanghani
8. Shri Harin Pathak
9. Shri Nirmal Kanti Chatterjee
10. Shri Bhogendra Jha

Rajya Sabha

11. Shri Krishna Kumar Birla
12. Shri Triloki Nath Chaturvedi
13. Dr. Shrikant Ramchandra Jichkar
14. Shri Ghulam Rasool Matto
15. Shri Chimanbhai Mehta
16. Shri Kamal Morarka
17. Shri Rajubhai A. Parmar

SECRETARIAT

1. Shri Satish Loomba — *Deputy Secretary*
2. Shri P.K. Bhandari — *Under Secretary*

2. The Report on the 'Working of the Public Sector Banks' as revised by the Drafting Committee was placed for consideration of the Committee. The Report, as revised was adopted. However, the Committee decided not to include the Chapter on 'Proposals for Privatisation and merger of Banks' in the Report as it could not be finalised due to paucity of time.

3. Member of the Committee desired that they should have pre-budget discussion with the Hon'ble Finance Minister. The Chairman has agreed to it.

The Committee then adjourned.