BANKE₹'S EDGE

JAIIB

A Comprehensive Guide to

Retail Banking and Wealth Management

Feature:

- Master All Concepts
- Revise Swiftly with Mind Maps
- Tackle 300+ Questions with Case Studies
- Your Winning Formula

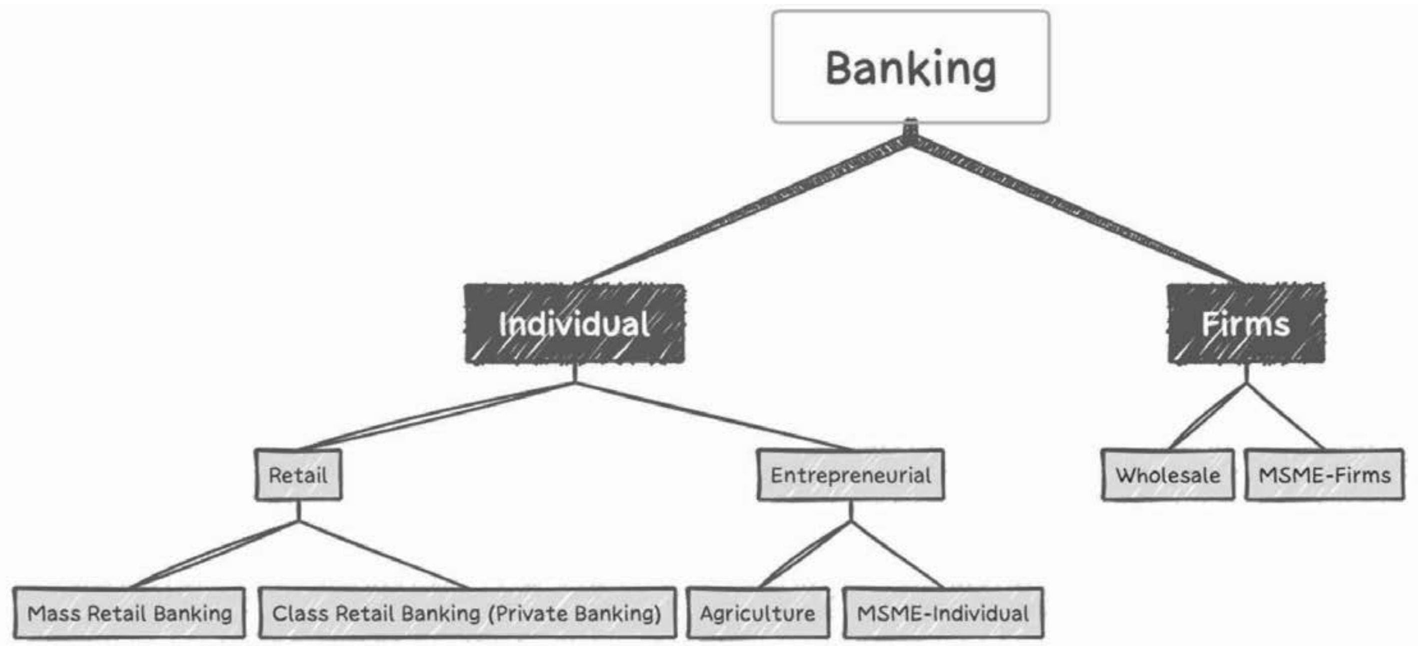
Contents

Topic 1

Retail Banking : Introduction

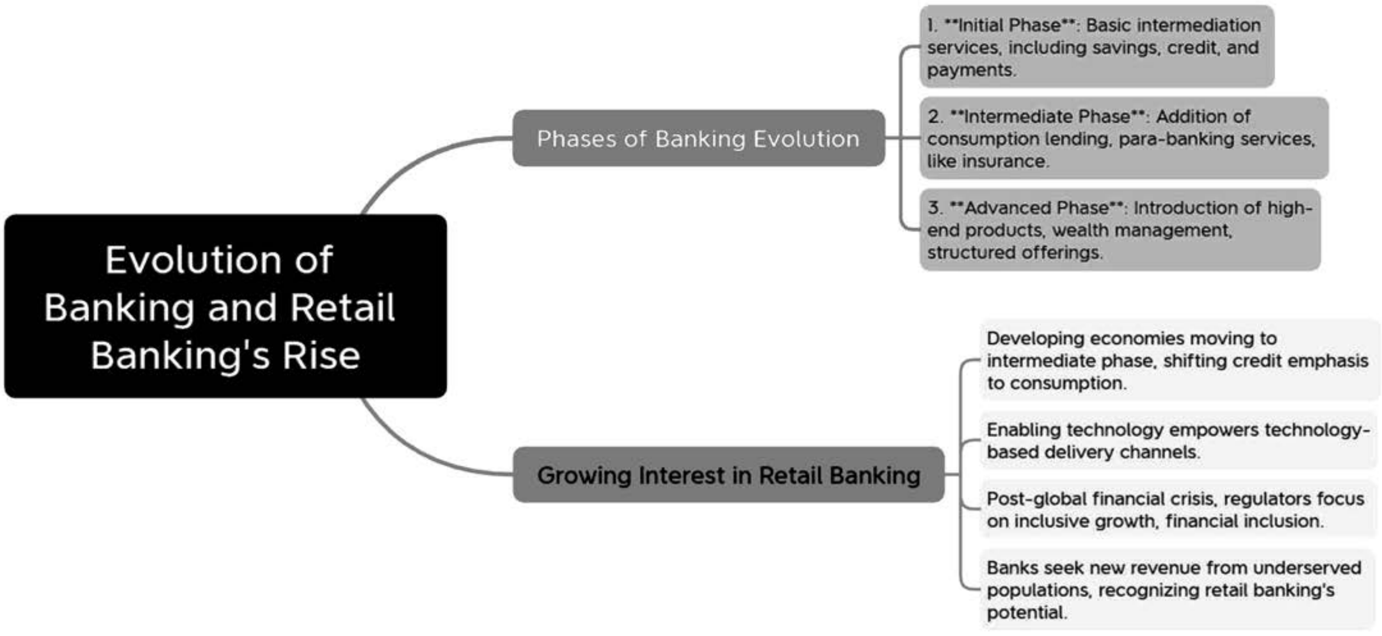
RETAIL BANKING OVERVIEW

- Retail banking offers banking products and services to individual customers.
- Banks raise resources primarily from retail depositors and focus on lending to a large number of customers with low ticket sizes.
- Products include fixed deposits, current/savings accounts, mortgages, loans (personal, housing, auto, educational), credit cards, insurance, and capital market products.



GROWING INTEREST IN RETAIL BANKING

To comprehend the increasing attraction of banks towards retail banking, it is essential to first understand the evolution of banking. In developed markets, banking has gone through three distinct phases, closely aligning with the development level of the real economy in respective jurisdictions.



Phases of Retail Banking

- Retail banking starts with a target clientele and progresses through "mass retail banking" and "class retail banking."
- Mass retail banking involves standardized products for a broad customer base.
- Class retail banking offers customized products for niche customer segments, like high net worth individuals.

Definitions of Retail Banking

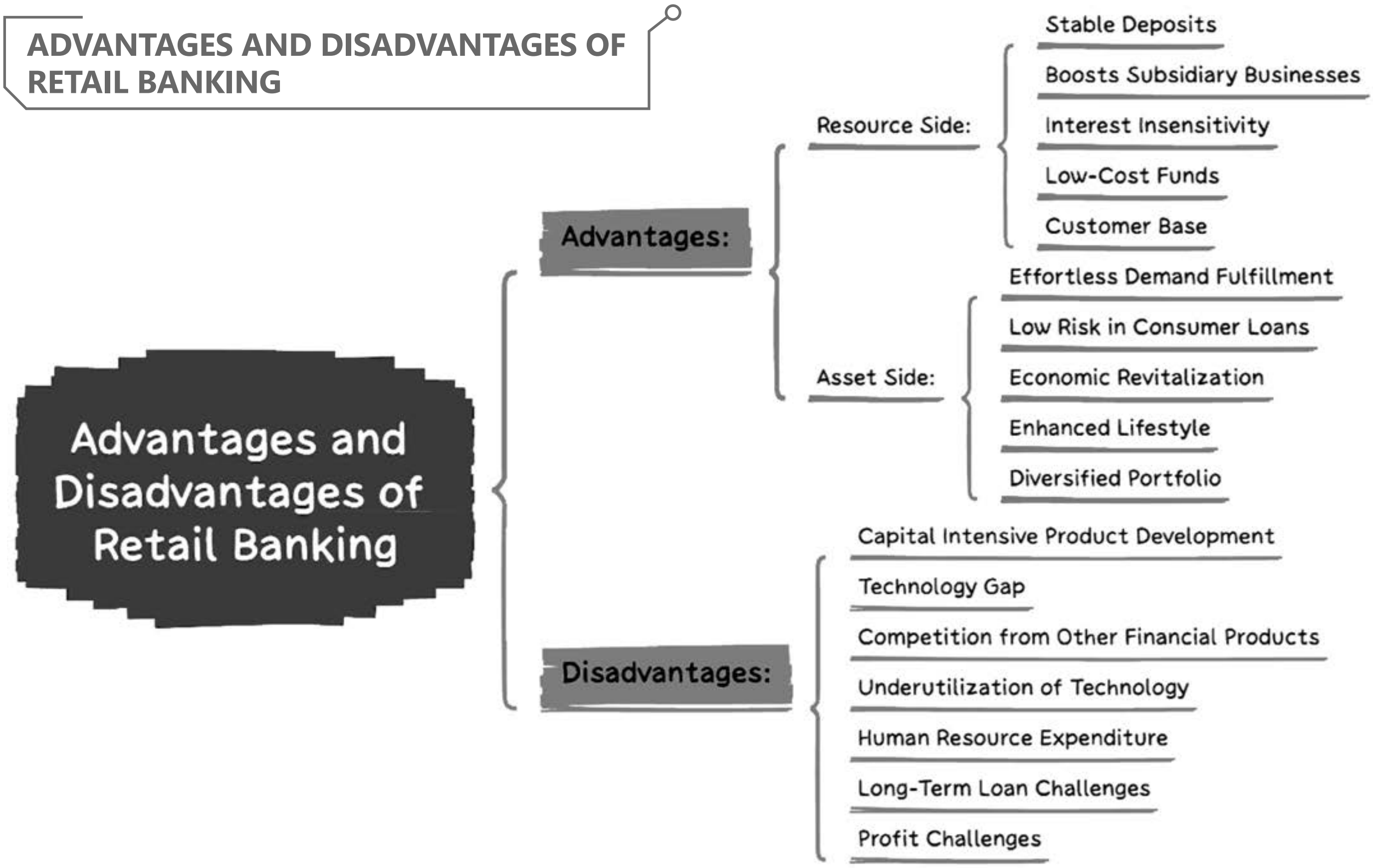
- Retail banking serves individual consumers, managing money, providing credit, and ensuring secure deposits.
- Focuses on consumer markets, offers various personal banking services, mortgages, loans, and credit cards.
- Lending money to consumers, covering a range of loans including credit cards, mortgages, and auto loans.

Characteristics of Retail Banking:

Retail Banking, also known as consumer banking or personal banking, caters to individual consumers, providing financial services that enable them to manage money, access credit, and securely deposit funds.

- **Consumer-Centric Services:** Retail banking focuses on serving individual consumers rather than businesses. It offers a range of personal banking services, including savings and operative accounts, bill payments, debit and credit cards, mortgages, and personal loans.
- **Commercial Banks' Role:** Typically offered by commercial banks, retail banking is distinct from wholesale banking, which targets consumer markets exclusively. While mainly aimed at the mass market, some services extend to small and medium-sized businesses.
- **Electronic Convenience:** Much of retail banking is facilitated electronically, either through Automated Teller Machines (ATMs) or online banking platforms.
- **Lending Aspect:** Retail banking involves lending money to consumers through various loans such as credit cards, mortgage loans, and auto loans. It covers loans at both prime and sub prime rates.
- **Direct Consumer Transactions:** Retail banking entails banking institutions engaging in transactions directly with consumers, rather than with corporations or other entities.
- **Branch-Centric Services:** It encompasses services offered at bank branches, primarily for small account holders, and includes offerings like savings accounts, retail loans, and remittance services.
- **Focus on Mass Market:** Pure retail banking primarily delivers mass market banking services to private individuals. Over time, its scope has expanded to include services for small- to medium-sized businesses. Some banks also incorporate their "private banking" services for high net worth individuals within the retail banking framework.

ADVANTAGES AND DISADVANTAGES OF RETAIL BANKING



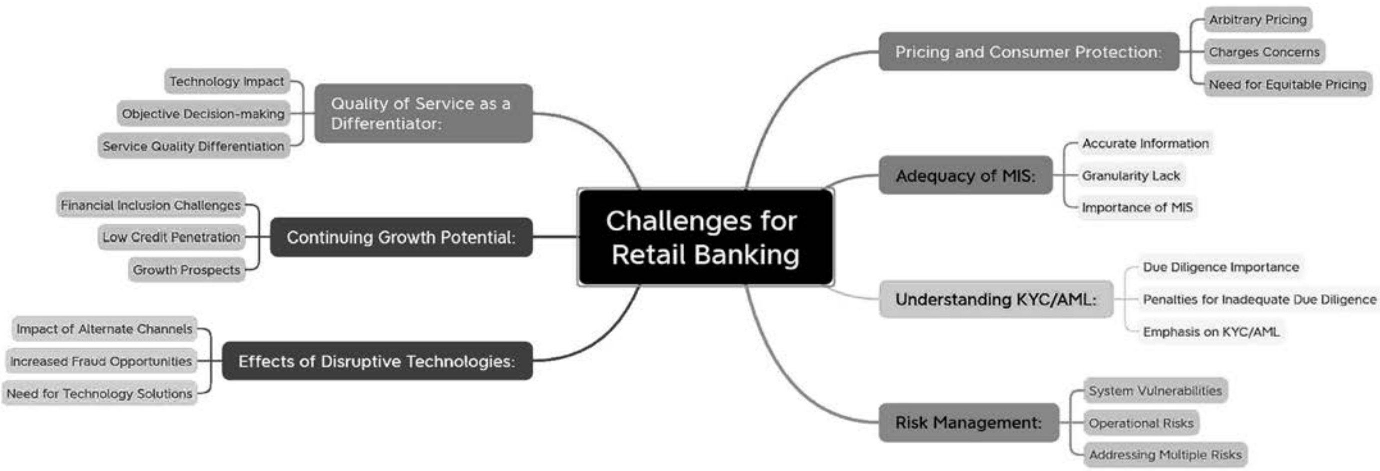
EVOLUTION OF RETAIL BANKING: A HISTORICAL PERSPECTIVE

- The concept of retail banking has evolved over time, transforming from traditional banking practices to meet the changing needs and demands of customers. Here is an overview of its evolution and key developments:
- Historical Banking in India (Before 1960s): Banking in India was predominantly focused on lending to business and corporate clients for working capital and project financing. Traditional banking was tailored towards serving class clients and their banking requirements, offering financing for raw materials, work in progress, finished goods, and bills receivables.
- Product and Service Paradigm Shift: As customer needs expanded and became more diverse, banks had to redesign their product and service offerings. The initial architecture of banking services was insufficient to accommodate these varied requirements.
- Emergence of Specialized Banks: In response to the changing landscape, specialized banks emerged, focusing on specific functional areas. Investment banks and merchant banks came into existence to handle investment-related functions, capital raising, and debt structuring activities.
- Evolution of Business Models: Banks continued to evolve their business models to keep up with the ever-changing needs of customers. With a broadening customer base that shifted from homogeneous to heterogeneous, banks had to adapt to fulfill the diverse needs of these customers.
- Corporate Banking and Retail Banking: With the changing customer base, banks introduced corporate banking and retail banking. Retail banking, also known as consumer banking, focused on serving individual consumers' financial needs.
- Capgemini's World Retail Banking Reports: Capgemini's reports on retail banking shed light on industry trends and challenges. The reports highlight various key findings:
- Customer Expectations and Behavior: Customer expectations are rising faster than banks can handle. Younger generations show declining positive customer behavior, impacting loyalty, referrals, and product adoption.
- Competition from Non-Bank Players: Non-bank players, like fintech firms, are becoming significant competitors to traditional banks, posing potential threats to their core business.

Impact of retail banking on profitability

PREREQUISITE FOR SUCCESS OF RETAIL BANKING

CHALLENGES FOR RETAIL BANKING



REASONS FOR THE GROWTH OF THE RETAIL BANKING SEGMENT

Rise of Young Indian Professionals

- Growing middle-class with rising purchasing power.
- Younger population comfortable with personal debt.
- Improving consumer purchasing power, contributing to India's retail banking segment.

Economic Growth Catalyst

- Retail banking plays a role in India's economic growth.
- India was identified as the 'second most attractive retail destination' among emerging markets.
- Retail banking's expansion aligns with India's emergence as an economic superpower.

Middle-Class Empowerment

- Growing percentage of middle to high-income households.
- Young population embraces personal debt.
- Rising consumer purchasing power fuels retail banking's growth.

Financial Market Reforms

- Retail lending's growth is linked to IT advancements, macroeconomic changes, demand-supply dynamics, and financial market reforms.
- Retail banking expansion driven by favorable market conditions and reforms.

Economic Engine

- Retail banks critical to economic growth.
- Retail credit functions drive economic activity.
- Banking sector's health influences overall economic circumstances.

Mass-Market Services:

- Retail banks offer essential services to consumers.
- Savings, loans, cards, and mortgages meet diverse customer needs.

Volume-Driven Business

- Retail credit diversifies risk across a broad customer base.
- High volume and diversification contribute to retail banking's success.

Automation Enhancements

- Retail banking growth facilitated by technological advances.
- ATM, internet, mobile, and QR code solutions expand reach and lower costs.
- Technology-driven accessibility accelerates retail banking adoption.

Accessibility and Affordability

- Banks offer flexible loan options with value-added services.
- Affordable and accessible products attract a wider customer base.

Financial Liquidity Advantages

- Banks attract customers with additional services and incentives.
- Low-cost deposits contribute to lower loan interest rates.
- Higher liquidity enables competitive pricing in retail loans.

Economic Prosperity Enabler

- Retail banking contributes to India's economic growth story.
- Increasing demand for retail credit accompanies economic expansion.

Demographic Dynamics

- Large, youthful population drives consumption growth.
- Demographic advantage positions India favorably for retail banking growth.

Technological Innovations:

- Technology reshapes the retail banking landscape.
- Convenience of online banking, cards, mobile apps, and QR codes boosts adoption.
- New delivery channels cater to changing customer preferences.

Enhanced Liquid Cash:

- Retail business diversifies bank income streams.
- Retail loans minimize provisioning burden, bolstering profitability.

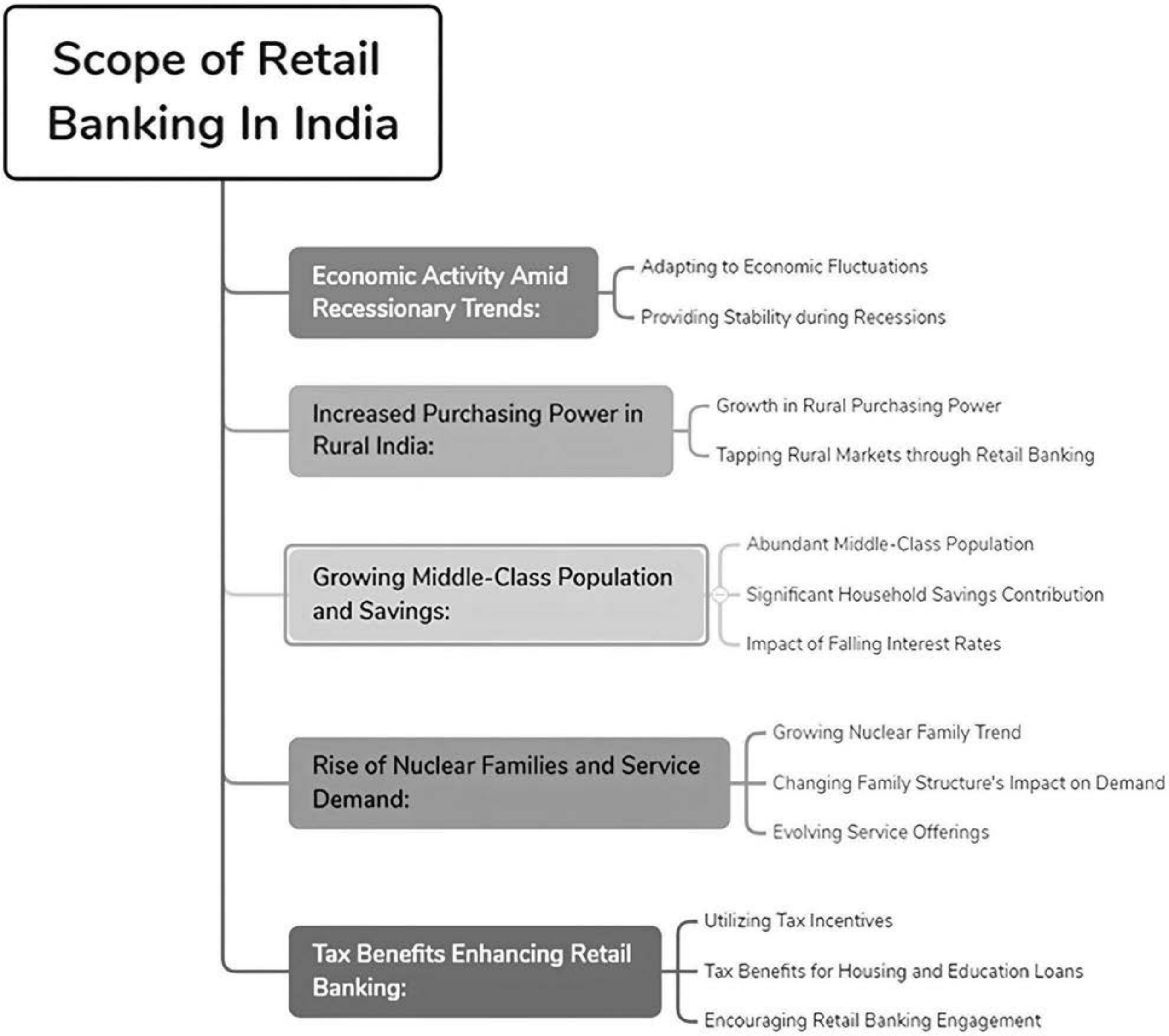
Interest Rate Impact

- Decline in interest rates fuels retail credit demand.
- Lower interest rates enhance affordability and attract borrowers.

Flexible Loan Terms

- Retail loans offered with diverse repayment options.
- Extended loan terms empower borrowers with financial leverage.

SCOPE OF RETAIL BANKING IN INDIA



FUTURE TRENDS IN RETAIL BANKING:

Growth in Digital Banking

- Pandemic accelerated adoption of digital banking.
- Fintechs driving digital payments and financial inclusion.
- Increased convenience, instant transactions, personalized advice.
- Strengthened security features against fraud.

Rapid Adaptation of Blockchain:

- Blockchain offers faster, transparent, and cost-effective transactions.
- Solving challenges in money transfers and record-keeping.
- Enhanced security and reduced reliance on intermediaries.

Artificial Intelligence (AI) and Data Science:

- AI and data science revolutionize banking operations.
- Predictive analytics for fraud prevention, customer behavior analysis, and risk management.
- Significant cost reduction and operational efficiency expected.

Cyber Security Priority

- Banks at the forefront of enterprise cyber security.
- Stringent security policies, monitoring, and compliance required.
- Continuous training and awareness to combat human errors.

Payment Innovations:

- Instant payments are gaining prominence for both consumers and B2B transactions.
- Technology advancements by NPCI, RBI, SEPA, and others.
- Streamlined accounts payable/receivable, simplified B2B payments.

Rise of Big Tech in Banking:

- Tech giants like Apple, Google, and Samsung entering financial services.
- Open Banking tools and partnerships driving tech companies' role in banking.
- Collaboration between banks and tech firms for enhanced customer experiences.

QUESTIONS

1. Which type of banking is most likely to offer the customer a savings account, a checking account, or a credit card?

(*a*) Corporate banking (*b*) Investment banking
(*c*) Retail banking (*d*) Private banking

2. Which of the following is/are the advantages of retail banking?

1. Client base will be large and therefore the risk is spread across the customer base
2. Customer loyalty will be strong with a good scope for cross-selling and customers tend to change from one bank to another very often
3. Attractive and wide interest spreads since customers are too fragmented to bargain effectively
4. Large numbers of clients can facilitate marketing, mass selling and the ability to categorize/select clients using scoring systems/data mining

(*a*) 1, 2 and 4
(*b*) 1, 3 and 4
(*c*) 2, 3 and 4
(*d*) 1 and 4

3. In the case of retail banking, the ticket size of the loan will be _______ while the customer base will be _______ and the interest spread here will be _______.

(*a*) Small, huge, high (*b*) High, small, huge
(*c*) Low, small, less (*d*) Small, huge, less

4. Which of the following can be categorized as third- party products in retail banking?

(*a*) Selling of Gold coins through branches
(*b*) Assets products
(*c*) Liability products
(*d*) None of these

5. What is a disquieting feature in the pricing of products and services by banks?

(*a*) Pricing that is risk-based and competitive
(*b*) Charges for non-maintenance of minimum balance
(*c*) Charges for cheque return only
(*d*) Charges for services that have been provided

6. What does direct banking encompass in terms of customer service and sales approaches?

(*a*) Only online banking services.
(*b*) In-person branch services.
(*c*) Various channel approaches including ATMs,mobile banking, and more.
(*d*) Exclusively physical mail-based services.

HINTS & SOLUTION

1. (*c*) **2**. (*b*) **3**. (*a*) **4**. (*a*) **5**. (*b*) **6**. (*c*)

1. (*c*) Retail banking is the type of banking that deals directly with individual consumers, and it offers a wide range of products and services to meet their financial needs. These products and services typically include savings accounts, checking accounts, credit cards, loans, and mortgages.

Corporate banking, on the other hand, deals with businesses of all sizes. Investment banking provides advisory services to businesses and governments, and it helps them raise capital. Private banking is a specialized type of banking that caters to high-net-worth individuals.

2. (*b*) **Advantages of Retail Banking**

- ❖ The client base will be large and therefore risk is spread across the customer base.
- ❖ Customer loyalty will be strong with a good scope for cross-selling and customers tend not to change from one bank to another very often.
- ❖ Attractive and wide interest spreads since customers are too fragmented to bargain effectively;
- ❖ Credit risk tends to be well diversified, as loan amounts are relatively small. There is less volatility in demand and credit cycle than in large corporates.

Large numbers of clients can facilitate marketing, mass selling and the ability to categorize/select clients using scoring systems/data mining.

3. (*a*)
- ❖ **Retail banking typically involves providing financial services to individual customers rather than businesses or organizations.**
- ❖ **The ticket size of the loan refers to the amount of money being borrowed. In retail banking, the loan amounts are generally smaller compared to corporate or investment banking.**
- ❖ **The customer base in retail banking is usually large as it caters to individual customers.**
- ❖ **The interest spread refers to the difference between the interest rate at which the bank borrows money and the interest rate at which it lends money. In retail banking, the interest spread is generally higher compared to other types of banking due to the higher risk associated with lending to individual customers.**

4. (*a*) The third-party products in retail banking include:
- ❖ Insurance products
- ❖ Mutual funds
- ❖ Government bonds
- ❖ Gold coins

Therefore, option A, selling of Gold coins through branches, can be categorized as a third-party product in retail banking. Options B and C, assets products and liability products, are not third-party products.

Option D, none of these, is incorrect as option A is a valid answer.

5. (*b*) One of the disquieting features in the pricing of products and services by banks is the increasing number of charges for non-usage of services or for non-maintenance of minimum balance. These charges can be seen as unfair to customers, as they are often levied even when the customer has not used the service or has only maintained a small balance in their account. Options A, C, and D are not disquieting features in the pricing of products and services by banks. Option A refers to pricing that is risk-based and competitive, which is a fair and transparent way to price products and services. Option C refers to charges for cheque return only, which is a legitimate charge that is incurred when a cheque is returned unpaid. Option D refers to charges for services that have been provided, which is also a legitimate charge.

6. (*c*) Direct banking encompasses a wide range of channel approaches to sell and service customers' needs. These approaches include ATMs, call and email centers, mobile banking devices, direct mail, and a variety of web-based models. Direct banking has evolved to provide services beyond just online banking, incorporating multiple methods to meet customer needs.

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Principles & Practices of Banking

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Topic

1 Banker-Customer Relationship

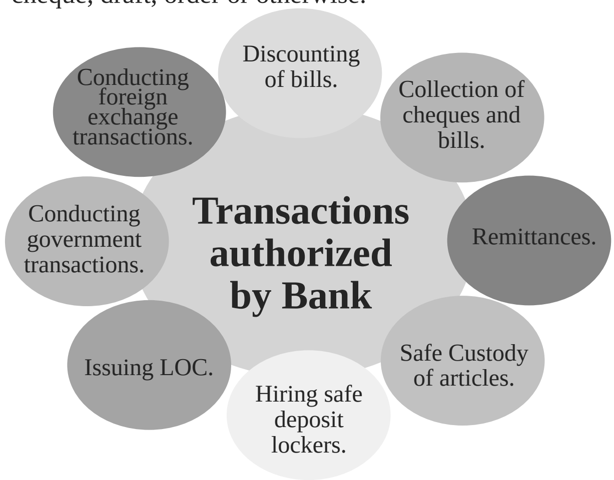
Different types of relationships are created between the banker and the customers, depending upon the nature of service rendered.

REQUIREMENTS TO BE CALLED A BANK

- Section 5 (b) of the Banking Regulation Act, 1949, defines the term banking.
- As per Section 5, the essentials to satisfy the requirements of the definition are:
  - Deposits should be only for lending and investment.
  - The deposit should be from the public.
  - Acceptance of deposit should be in the form of money.

Note: Companies accepting deposits for trading or manufacturing are not considered as a bank.
'Nidhis' multi-benefit societies, co-operative societies that accept deposit from their members are not covered as a bank.

- Under section 5 (c) of the Banking Regulation Act, 1949, 'Banking Company' means any company that transacts the business of banking in India.
- Sec. 7 of the Banking Regulation Act, 1949, prohibits use of the words 'banker' or 'banking' or 'banking company' by a company other than a banking company, individual, a group of individuals or a firm.
- **Moneylenders are not bankers:** In the case of Kadiresan Chettiar vs. Ramanathan Chettiar (AIR 1927, Madras 438), it was held that while a moneylender lends his own money, a banker lends money of his customers/depositors.
- **Accepting deposits of money from the public:** In Mahalaxmi Bank Limited vs. Registrar of Companies, it was decided that if a company gave loan to the public but did not accept deposits from the public, it could not be considered as a banking company.
- Deposit repayable to depositors on demand or otherwise.
- The deposits may be withdrawable by the customers by cheque, draft, order or otherwise.



BANKER-CUSTOMER RELATIONSHIP

Who is a customer?

- Not defined by law.
- Ordinarily, a person who has an account in a bank.
- Kerala High Court observed in the case of Central Bank of India Ltd. Bombay vs. V.Gopinathan Nair and others: "Broadly speaking, a customer is a person who has the habit of resorting to the same place or person to do business. So far as banking transactions are concerned, he is a person whose money has been accepted on the footing that banker will honour up to the amount standing to his credit, irrespective of his connection being of short or long standing."

For the purpose of KYC requirements, a 'Customer' is defined as:

- A person or entity that maintains an account and/or has a business relationship with the bank or conducts a transaction with the bank.

DIFFERENT DEPOSIT PRODUCTS OR SERVICES

Deposits are normally classified as demand deposits and time deposits.

Demand Deposits	Time Deposits
1. Payable on Demand.	1. Repaid after expiry of the Deposit Period.
2. Low interest rates or no interest.	2. High interest rates, which vary according to period.
3. It includes current, savings, overdue deposits and unclaimed deposits.	3. Time deposits are for a period ranging from 7 days to 120 months period with or without reinvestment plans.

Demand Deposits: Demand deposits are classified into current accounts and savings accounts.

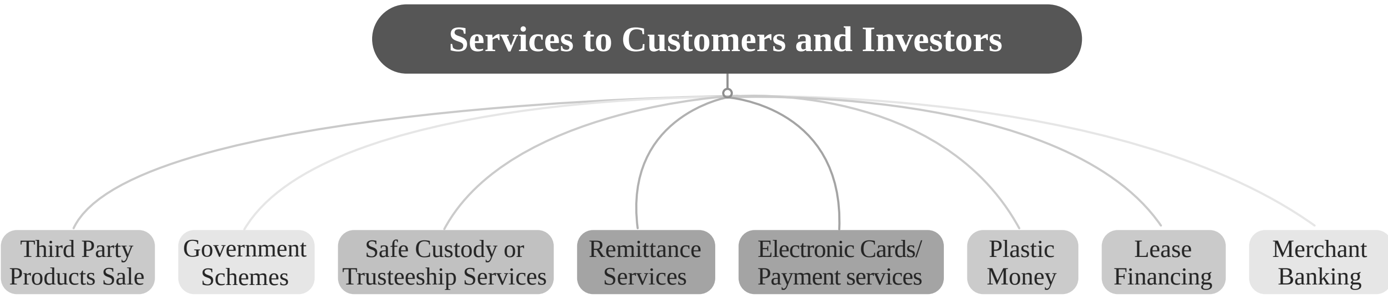
Time Deposits: TDs are of several types namely, Fixed Deposits (periodical interest payment); Short-term Deposits (of less than a year); Reinvestment Deposit Scheme (cumulative interest paid on maturity); Recurring Deposit Scheme (periodical deposits made); and Flexi Recurring Deposit (special type of recurring deposit).

Deposit Products for Non-Resident Indians

Banks also offer special deposit accounts/ schemes for Non Resident Indians, Persons of Indian Origins, and Overseas Citizens of India.

- Non-Resident Ordinary Rupee Account (NRO Account)
- Non-Resident (External) Rupee Account (NRE Account)
- Foreign Currency Non-Resident (Bank) Account – FCNR (B) Account

SERVICES TO CUSTOMERS AND INVESTORS



Merchant Banking

Merchant bankers are financial intermediaries facilitating transfer of capital from those who own it (Investor or Bond Subscriber) to those who use it (Corporates or Governments). They help a corporate in Initial Public Offering (IPO) or a Follow-up Public Offer (FPO), popularly called a public issue or Private Placement of Debt or Equity.

Lease Financing

This means leasing out the capital assets owned by an institution to another company against payment of monthly rents for asset's consumption or use.

Plastic Money

Plastic money in the form of credit cards and other types of cards has become a preferred mode of payments. Increasing use of the plastic money, has reduced the need of cash to a significant extent. E.g., Charge Cards, Credit Cards, Debit Cards, ATM Cards, Prepaid Cards, Co-branded Cards.

Electronic Cards/Payment services

These instruments can be loaded on the smartphones of the customers, like mobile wallet, etc. Various cards are now issued in electronic form also.

Remittance Services

For facilitating funds transfers between two persons, banks were providing services remittances services. E.g., NEFT, RTGS, IMPS, UPI, AePS, NACH.

Government Schemes

Banks also serve as the distribution points for several Government Schemes that are aimed at financial inclusion and also providing safe avenues of investment to the common man. Some of the prominent schemes are PPF, NPS, RBI bonds, SGB, CGAS, SGAS, Pradhan Mantri Jan Dhan Yojana, Stand up India Scheme, etc.

Third Party Products Sale

With a view to providing one-stop-services to their customers, banks have tapped the opportunity made available through regulatory relaxations for banks to sell third party financial products pertaining mainly to the capital market and insurance sectors.

Some of the major third-party products are: Demat Accounts, Trading Account, Three-in-One Account, Mutal Funds, Life Insurance Policy, Health Insurance Policy, Vehicle Insurance, House Insurance, etc.

Safe Custody or Trusteeship Services

Banks and bankers enjoy tremendous public trust. Banks have therefore offered certain services like Safe Custody of articles, documents; Hiring out safe deposit lockers; Escrow account; Escrow services for document; Trusteeship; Executorship.

QUESTIONS

1. Which one of the following cannot categorized as a Time Deposit?
(*a*) Overdue deposits
(*b*) Short-term Deposits
(*c*) Recurring Deposit Scheme
(*d*) Both (*a*) and (*b*)

2. In the context of the agent-principal relationship,which of the following statements is INCORRECT?
(*a*) The agent has a fiduciary responsibility to act in the best interest of the principal.
(*b*) The principal is generally responsible for the actions of the agent performed within the scope of the agency.
(*c*) The agent is entitled to act on his own benefit while representing the principal's interest.
(*d*) The principal can terminate the agency relationship at will, provided there is no contractual term specifying otherwise.

3. Shivam remitted money to purchase the shares of X&Y Public Limited Company. The bank bought shares in parts but failed before completing the rest of the purchase. What role did the bank assume in the given situation?
(*a*) Debtor (*b*) Trustee (*c*) Agent (*d*) Lessor

4. When a customer deposits certain documents for their safe custody with the bank the relationship between them is of:
(*a*) Principal and Agent (*b*) Trustee and Beneficiary
(*c*) Bailor and Bailee (*d*) Debtor and Creditor

5. When a bank renders ancillary services like remittance on behalf of the customers, the relationship between them is of:
(*a*) Agent and Principal (*b*) Creditor and Debtor
(*c*) Bailee and Bailor (*d*) Trustee and Beneficiary

HINTS & SOLUTION

1. (*a*) **2.** (*c*) **3.** (*b*) **4.** (*c*) **5.** (*a*)

1. (*a*)
❖ Time deposits are for investing surplus funds for short to long term.
❖ Type of Time Deposits includes Fixed Deposits (periodical interest payment), Short-term Deposits, Reinvestment Deposit Scheme, Recurring Deposit Scheme, and Flexi Recurring Deposit.
❖ Demand Deposits includes current, savings,overdue deposits and unclaimed deposits.

2. (*c*)
❖ The agent indeed has a fiduciary responsibility to act in the best interest of the principal. This is a basic tenet of the agent-principal relationship.
❖ The principal is generally responsible for the actions of the agent, provided those actions are performed within the scope of the agency.
❖ The principal can usually terminate the agency relationship at will unless there is a specific contractual term that dictates otherwise.
❖ is incorrect because an agent, owing to his fiduciary relationship with the principal, is not entitled to act in his own benefit while representing the principal. Doing so would constitute a breach of fiduciary duty.

3. (*b*) A trustee is a person or firm that holds and administers property or assets for the benefit of a third party. Trustees are required to make decisions in the beneficiary's best interests and have a fiduciary responsibility to them, meaning they act in the best interests of the beneficiaries to manage their assets. If a customer keeps certain valuables or securities with the bank for safekeeping or deposits a certain amount of money for a specific purpose, the banker, besides becoming a bailee, is also a trustee.
In one case, a customer remitted money to purchase a company's shares. The bank bought shares in parts,but it failed before completing the rest of the purchase. It was held that the bank stood in the position of a trustee, and the remitter was entitled to the refund of the unspent amount.

4. (*c*) When a customer deposits certain valuables, bonds, securities, or other documents with the bank, for their safe custody, the bank becomes a bailee and the customer is the bailor.

Transaction	Bank	Customer
Safe Custody	Bailee	Bailor
Collection of Cheque	Agent	Principal
Articles left by mistake	Trustee	Beneficiary
Loan from Bank	Creditor	Debtor

5. (*a*) When Bank renders the ancillary services like remittance collection of cheques, bills, paid regularly,electricity bills, telephone bills, insurance premiums, club fees, etc. on behalf of the customers, in the secases, the bank acts as an agent, his principal being the customer.

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Topic

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Indian Banking Structure

FUNCTIONS OF BANKING

The banking system plays a critical role in the economy by performing various functions. Here's an overview of the main functions of banking:

Accepting Deposits

- Savings Accounts
- Fixed Deposits
- Current Accounts
- Recurring Deposits

Providing Loans and Advances

- Personal Loans
- Home Loans
- Educational Loans
- Overdraft Facilities

Facilitating Payments

- Cheque Clearing
- Electronic Funds Transfer (EFT)
- NEFT, RTGS
- Credit/Debit Card Transactions

Investment Services

- Mutual Funds
- Fixed Income Securities
- Wealth Management Services

Foreign Exchange Services

- Currency Exchange
- Foreign Currency Accounts
- Letters of Credit for International Trade

Safe Custody of Valuables

- Safe Deposit Lockers
- Dematerialized (Demat) Accounts for Securities

Credit Creation

- Expansion of Money Supply through the Multiplication of Deposits

Agency Services

- Acting as an Agent for Collection and Payment
- Performing Functions like Bill Payments, Pension Disbursements, etc.

Risk Management

- Providing Insurance Products
- Hedging Services for Foreign Exchange and Commodity Risks

Promoting Financial Inclusion

- Extending Banking Services to Unbanked and Underbanked Areas
- Offering Tailored Products for Low-Income Groups

Social and Developmental Roles

- Support for Priority Sector Lending
- Microfinance and Self-Help Group (SHG) Lending
- Participation in Government Schemes and Initiatives

DEVELOPMENT OF BANKING IN INDIA

The development of banking in India can be traced through various phases, each marked by key events, reforms, and trends that shaped the sector. Here's a comprehensive look:

Phase I: Pre-Independence (Before 1947)

1. **Early Beginnings (18th Century):** The Bank of Hindustan established in 1770 in Calcutta.
2. **Establishment of Major Banks:** The State Bank of India, originally founded as the Bank of Calcutta in 1806.
3. **Swadeshi Movement (1906-1907):** Establishment of banks with Indian capital like the Bank of India, Punjab National Bank.

4. **Regulatory Framework:** The RBI Act, 1934, and the formation of the Reserve Bank of India (RBI) in 1935.

Phase II: Post-Independence (1947 - Mid-eighties)

1. **Nationalization of the Reserve Bank (1949):** The RBI was nationalized.
2. **Banking Regulation Act (1949):** Introduced to regulate and control banks in India.
3. **Nationalization of Major Banks (1969 & 1980):** Major banks were nationalized to promote financial inclusion and direct credit towards priority sectors.
4. **Formation of Regional Rural Banks (1975):** Established to cater to the rural population.

Phase III: Liberalization and Reforms (1991 Onwards)

1. **Narasimham Committee (1991 & 1998):** Recommendations for financial sector reforms, leading to a roadmap for banking sector liberalization.
2. **Liberalization and Entry of New Banks:** Licenses granted to new private-sector banks.
3. **Prudential Norms and Basel Accords:** Introduction of international banking standards.
4. **Technological Advancements:** Emergence of internet banking, ATMs, mobile banking.
5. **Focus on Financial Inclusion:** Launch of Pradhan Mantri Jan Dhan Yojana, Small Finance Banks, Payment Banks.
6. **Insolvency and Bankruptcy Code (2016):** Framework for resolving insolvency.
7. **Consolidation in Public Sector Banks:** Merging of various PSBs to create larger and more efficient entities.

Present Status

- **Digital Revolution:** Further expansion in digital banking and fintech innovation.
- **Asset Quality Challenges:** NPA management and resolution.
- **Global Integration:** Participation in global financial markets.
- **COVID-19 Pandemic Impact:** Emergency measures to support the economy and financial stability.

SCHEDULED COMMERCIAL BANKS- TYPES AND FUNCTIONS

Types of Scheduled Commercial Banks

Public Sector Banks (PSBs)

- State Bank of India and its Associates
- **Nationalized Banks:** Majority ownership by the Government of India.
- **Regional Rural Banks (RRBs):** Focus on rural areas and agriculture.

Private Sector Banks

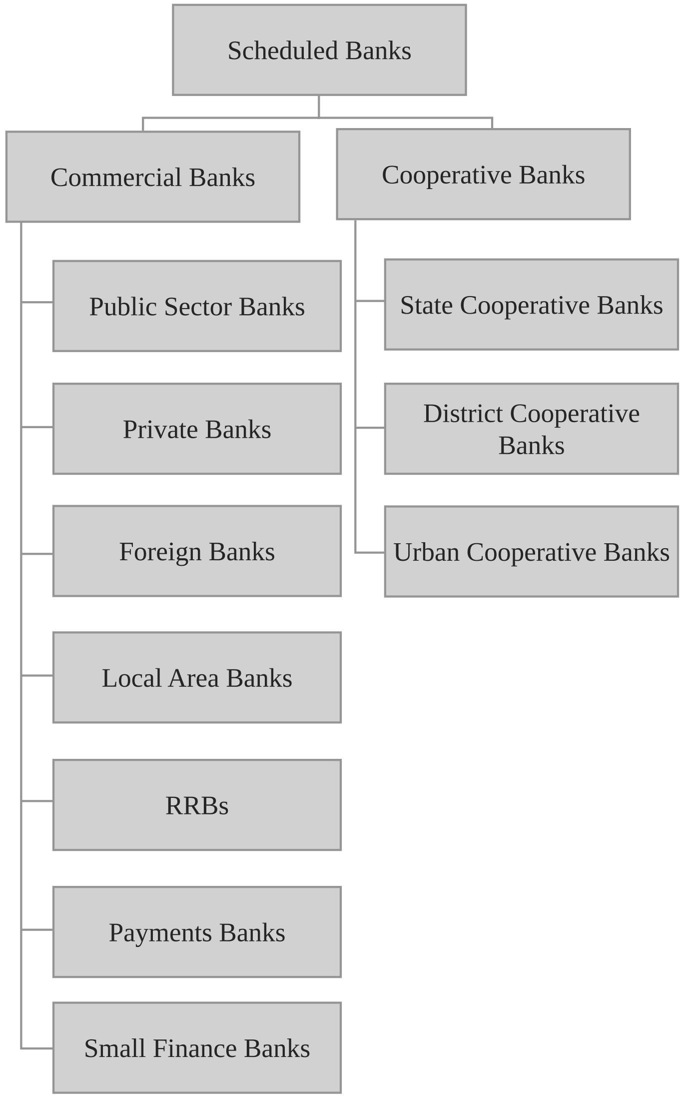
- **Old Generation Private Banks:** Established before the economic reforms of 1991.
- **New Generation Private Banks:** Established post-1991 economic liberalization.

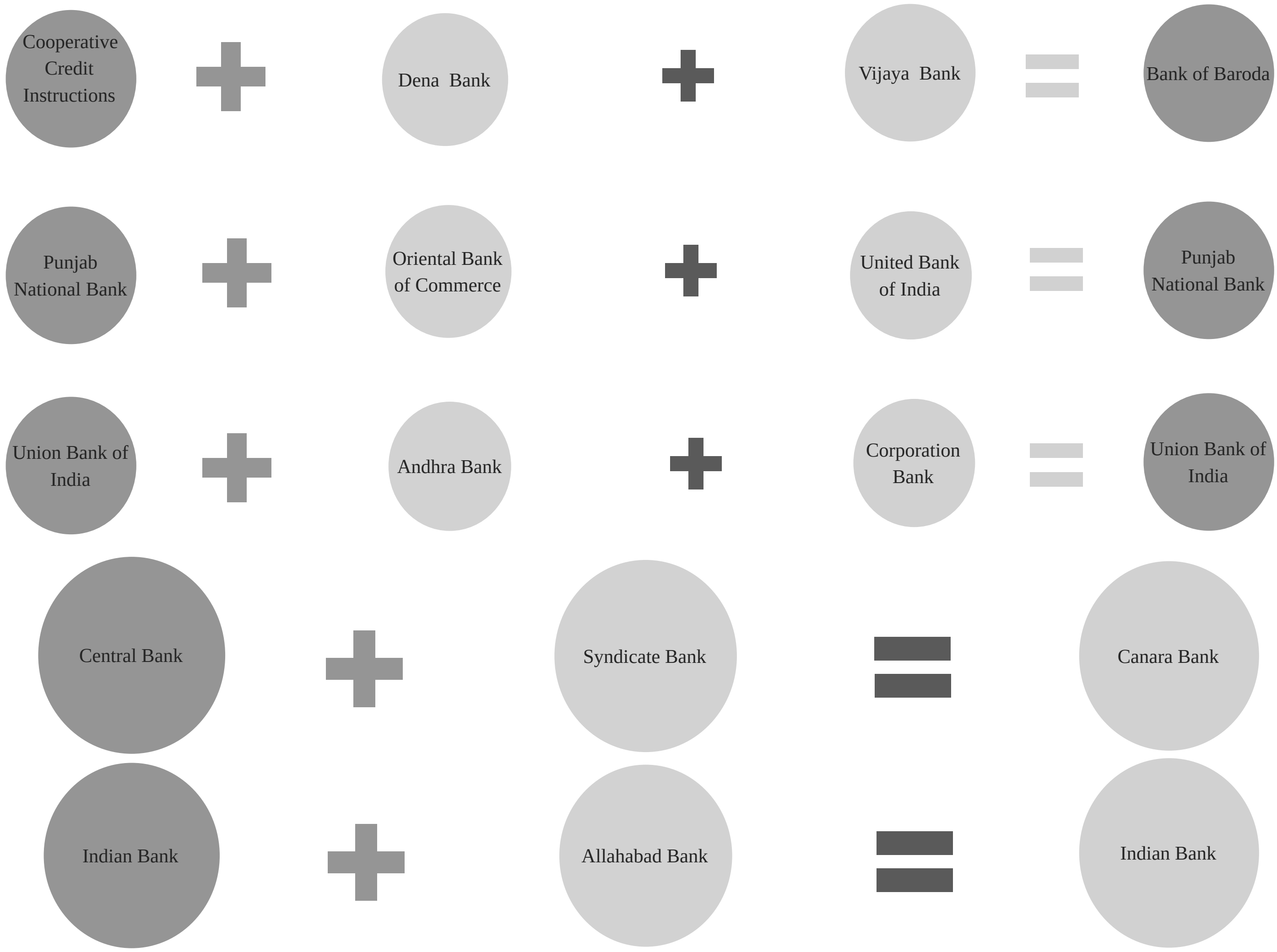
Foreign Banks

- Banks incorporated outside India but operating branches in India.

Small Finance Banks

- Focus on financial inclusion by providing services to unserved and underserved sections.





Functions of Scheduled Commercial Banks

Acceptance of Deposits

- **Savings Accounts:** Encourage small savings.
- **Current Accounts:** For businesses and frequent transactions.
- **Fixed Deposits:** Deposits for a fixed tenure with higher interest rates.

Providing Loans

- Personal Loans, Home Loans, Education Loans, etc.
- Business and Industrial Loans.
- Overdraft and Cash Credit Facilities.

Investment Functions

- Investment in Government and Corporate Securities.
- Wealth Management Services.

Agency Functions

- Collection of Cheques, Bills, Dividends, etc.
- Acting as a Trustee or Executor.

Foreign Exchange Transactions

- Buying and Selling of Foreign Currency.
- Providing Letters of Credit for International Trade.

Digital Banking Services

- Internet Banking, Mobile Banking, ATMs.

Other Miscellaneous Services

- Safe Deposit Lockers, Credit Cards, Merchant Banking, etc.

COOPERATIVE BANKS: TYPES

Cooperative Banks are financial institutions that are owned and operated by their members to provide financial services primarily within a specific community or group. They play a vital role in promoting financial inclusion, particularly in rural areas.

Types of Cooperative Banks

Urban Cooperative Banks (UCBs)

- **Scheduled Urban Cooperative Banks:** Included in the Second Schedule of the RBI Act, 1934.
- **Non-Scheduled Urban Cooperative Banks:** Not part of the Second Schedule.
- Operate in urban and semi-urban areas and cater to the needs of small borrowers.

Rural Cooperative Banks

- Focus on the agricultural and rural sector.

A. State Cooperative Banks (StCBs)

- **Apex Cooperative Banks:** Operate at the state level.
- Provide funds to other cooperative banks within the state.

B. District Central Cooperative Banks (DCCBs)

- Operate at the district level.
- Act as a link between the StCBs and Primary Agricultural Credit Societies.

C. Primary Agricultural Credit Societies (PACS)

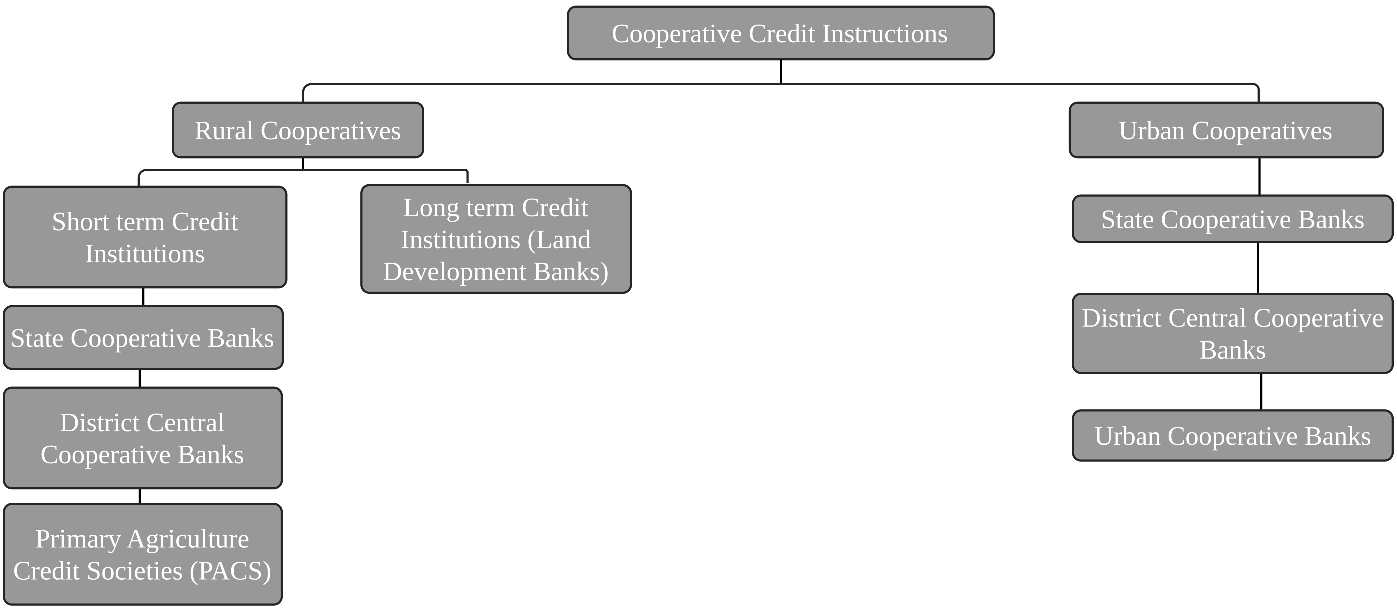
- Operate at the grassroots level, usually a village or a group of villages.
- Provide agricultural credit and other related services to farmers.

Multi-State Cooperative Banks

- Operate in more than one state.
- Require registration under the Multi-State Cooperative Societies Act.

Cooperative Credit Institutions

- **Land Development Banks (LDBs):** Provide long-term loans for agricultural purposes.
- **State Cooperative Agriculture and Rural Development Banks (SCARDBs):** Provide long-term credit for agricultural and rural development.



NBFCs

Non-Banking Financial Companies (NBFCs) are critical components of the Indian financial system. They complement banks by providing financial services and products that meet the diverse needs of businesses, industries, and individuals. Unlike banks, NBFCs cannot accept demand deposits and are not part of the payment and settlement system. Here's an overview of NBFCs:

Types of NBFCs

1. **Asset Finance Company (AFC):** Financing physical assets that correspond to productive or economic activity.
2. **Investment Company (IC):** Dealing mainly with the acquisition of securities.
3. **Loan Company (LC):** Providing finance by making loans and advances.
4. **Microfinance Institution (NBFC-MFI):** Providing microloans to the economically weaker sections.

QUESTIONS

1. The reform of the banking sector in India between 1992-2008 was a critical phase in transforming the banking landscape in the country. This period saw significant changes like the introduction of prudential norms, improvement in technology, and efforts to increase transparency and competition. One of the pivotal reforms during this period was the implementation of the Basel Accords, which primarily aimed to __________.
   (*a*) increase the gold reserves of the central bank
   (*b*) encourage the merger of small banks
   (*c*) enhance the quality and stability of the financial system
   (*d*) regulate the foreign exchange market

2. The financial system is a network of financial institutions, financial markets, financial instruments and financial services to facilitate the transfer of funds. The constituents of a financial system create, trade, and settle in financial assets and also deal with the creation and transfer of money. One key component of the financial system, this institution facilitates the flow of funds from the areas of surplus to the areas of deficit and is primarily responsible for financial intermediation in the economy, is also known as __________.
   (*a*) Financial Market (*b*) Financial Services
   (*c*) Financial Instruments (*d*) Financial Institutions

3. Which of the following measures was NOT part of the Banking Sector Reforms in India between 1992-2008?
   (*a*) Implementation of prudential norms
   (*b*) Deregulation of interest rates
   (*c*) Introduction of Universal Banking
   (*d*) Complete privatisation of public sector banks

HINTS & SOLUTION

1. (*c*) **2.** (*d*) **3.** (*d*)

1. (*c*)
- ❖ The implementation of the Basel Accords during the reform of the banking sector in India between 1992-2008 aimed to enhance the quality and stability of the financial system.
- ❖ The Basel Accords are international regulatory frameworks developed by the Basel Committee on Banking Supervision to ensure that financial institutions maintain enough capital reserves to absorb unexpected losses.
- ❖ By implementing these standards, the goal was to strengthen the resilience and stability of the banking system, thereby fostering a more robust and transparent financial environment.

2. (*d*)
- ❖ Financial Institutions are crucial components of the financial system, and they play a key role in the financial intermediation process by facilitating the flow of funds from areas of surplus to areas of deficit. They match the description provided in the question.
- ❖ Financial Markets are the venues where buyers and sellers interact to trade financial instruments, such as shares, bonds, or derivatives.
- ❖ Financial Services refer to services provided by the finance industry, which encompasses a broad range of businesses that manage money, such as banks, credit card companies, insurance companies, accountancy companies, consumer finance companies, stock brokerages, investment funds, and some government-sponsored enterprises.
- ❖ Financial Instruments represent a claim to the payment of a sum of money in the future and/or periodic payment in the form of interest or dividend. They do not directly facilitate the flow of funds from areas of surplus to areas of deficit.

3. (*d*)
(*a*) Implementation of prudential norms: Prudential norms related to capital adequacy, income recognition, asset classification, and provisioning were implemented as part of the banking sector reforms.
(*b*) Deregulation of interest rates: Before the reforms, interest rates in India were regulated by the government. One of the significant reforms was the deregulation of interest rates to provide banks with the freedom to set their interest rates.
(*c*) Introduction of Universal Banking: The concept of Universal Banking was introduced where banks were allowed to undertake any form of financial services and not just confined to traditional banking.
(*d*) Complete privatisation of public sector banks: This measure was NOT part of the reforms. Although the government did reduce its holdings in public sector banks and allowed private banks to operate, it did not completely privatise public sector banks.

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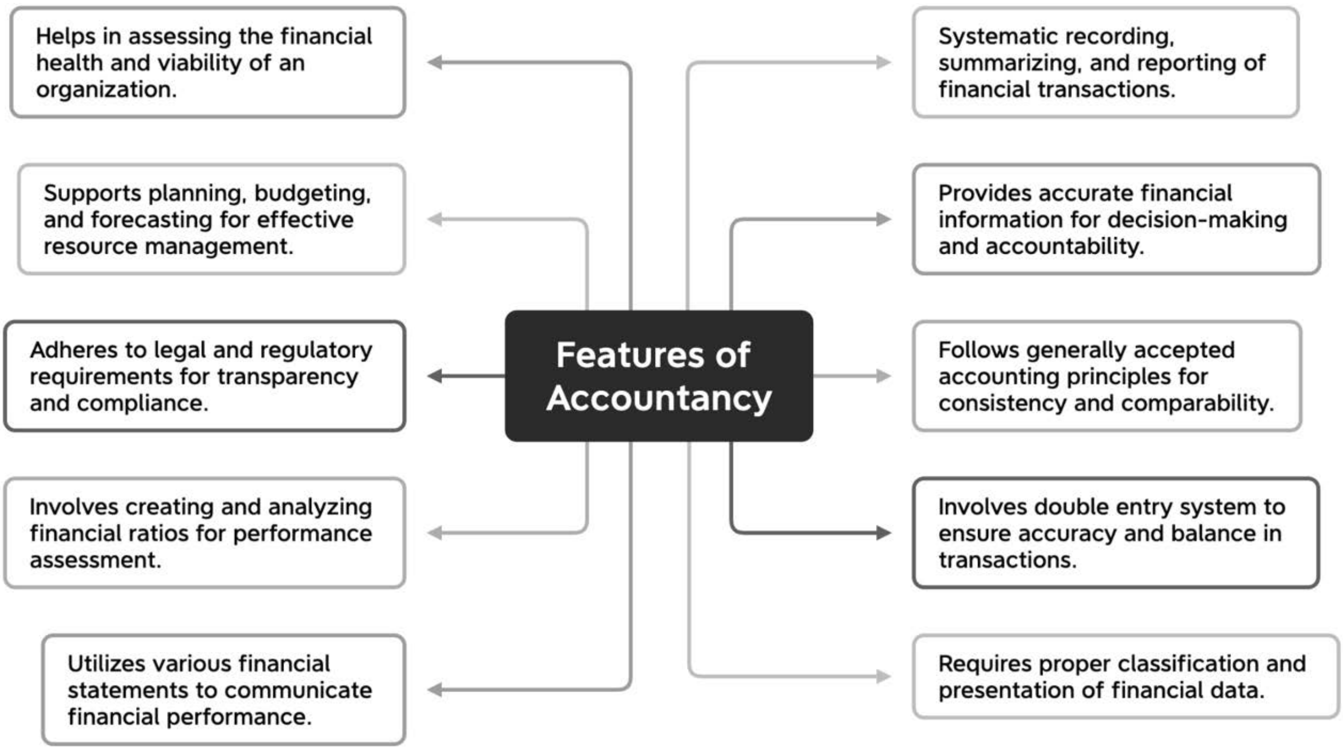
Contents

Topic 1

Definition, Scope and Accounting Standards

ACCOUNTANCY

- Accountancy is the systematic process of recording, summarizing, analyzing, and reporting financial transactions and information of an individual, business, or organization.
- It involves the preparation of financial statements, such as balance sheets, income statements, and cash flow statements, to provide a clear and accurate picture of the financial performance and position.



"Branches of accounting" refer to the various specialized areas or disciplines within the field of accounting that focus on specific aspects of financial information, reporting, analysis, and management. These branches help cater to the diverse needs of businesses, organizations, and individuals by providing in-depth knowledge and expertise in different areas of accounting.

Other Branches of Accounting

- Financial Accounting records and communicates financial information to external stakeholders for decision-making, regulatory compliance, and accountability.
- Cost Accounting involves tracking and analysing the costs associated with producing goods or services within an organisation, aiding in cost control, pricing decisions, and budgeting.
- Management Accounting provides internal financial information to aid managerial decision-making, strategic planning, performance evaluation, and resource allocation.
- Inflation Accounting adjusts financial statements to reflect the impact of inflation, ensuring that the effects of rising prices on assets and liabilities are properly accounted for.
- Human Resource Accounting quantifies the value of human resources within an organisation, recognising employees as valuable assets and incorporating their contribution into financial statements.

ACCOUNTING STANDARDS

- In response to the necessity for aligning varying accounting policies and methods, the Institute of Chartered Accountants of India (ICAI) established the 'Accounting Standards Board' (ASB) on April 21st, 1977. The central role of the ASB involves creating accounting standards, which can be subsequently mandated by the ICAI council.
- Under Section 129(5) of the Companies Act 2013, companies not adhering to accounting standards must disclose: (a) deviations, (b) reasons for deviations, and (c) resulting financial effects.
- The 'National Advisory Committee on Accounting Standards', established on June 15, 2001, advised the government on accounting policies. Replaced by the 'National Financial Reporting Authority' (NFRA) since October 1, 2018, it's an independent regulatory body overseeing accounting and auditing legislation.
- NFRA's role involves collaboration with the ICAI and its recommendations on Accounting Standards, potentially impacting the ICAI's powers.

A BRIEF OVERVIEW OF ACCOUNTING STANDARDS

- AS 1: Disclosure of Accounting Policies: This standard provides guidance on the disclosure of significant accounting policies in the financial statements of an entity.
- AS 2: Valuation of Inventories: It emphasizes valuing inventories at the lower of cost or net realizable value. Methods like weighted average cost or FIFO are allowed for interchangeable goods, while specific identification is allowed for non-interchangeable goods. Alternative techniques like standard cost or retail method are permitted if they closely match actual costs. Exclusions from this standard include work in progress under construction contracts, service providers' work in progress, shares and debentures as stock-in-trade, and certain types of inventories like livestock, agricultural products, and minerals.

Number	Name
Ind AS 101	First time adoption of Ind AS
Ind AS 102	Share Based Payment
Ind AS 103	Business Combination
Ind AS 104	Insurance Contracts
Ind AS 105	Non-Current Assets Held for Sale and Discontinued Operations
Ind AS 106	Exploration for and Evaluation of Mineral Resources
Ind AS 107	Financial Instruments: Disclosures
Ind AS 108	Operating Segments
Ind AS 109	Financial Instruments
Ind AS 110	Consolidated Financial Statements
Ind AS 111	Joint Arrangements
Ind AS 112	Disclosure of Interests in Other Entities
Ind AS 113	Fair Value Measurement
Ind AS 114	Regulatory Deferral Accounts
Ind AS 115	Revenue from Contracts with Customers (Applicable from April 2018)
Ind AS 116	Leases (Applicable from April 2019)
Ind AS 1	Presentation of Financial Statements
Ind AS 2	Inventories
Ind AS 7	Statement of Cash Flows
Ind AS 8	Accounting Policies, Changes in Accounting Estimates and Errors
Ind AS 10	Events occurring after Reporting Period
Ind AS 11	Construction Contracts (Omitted by the Companies (Indian Accounting Standards) Amendment Rules, 2018)
Ind AS 12	Income Taxes
Ind AS 16	Property, Plant and Equipment
Ind AS 19	Employee Benefits
Ind AS 20	Accounting for Government Grants and Disclosure of Government Assistance
Ind AS 21	The Effects of Changes in Foreign Exchange Rates
Ind AS 23	Borrowing Costs
Ind AS 24	Related Party Disclosures
Ind AS 27	Separate Financial Statements
Ind AS 28	Investments in Associates and Joint Ventures
Ind AS 29	Financial Reporting in Hyper inflationary Economies
Ind AS 32	Financial Instruments: Presentation
Ind AS 33	Earnings per Share
Ind AS 34	Interim Financial Reporting
Ind AS 36	Impairment of Assets
Ind AS 37	Provisions, Contingent Liabilities and Contingent Assets
Ind AS 38	Intangible Assets
Ind AS 40	Investment Property
Ind AS 41	Agriculture

GAAP AND IFRS

- Generally Accepted Accounting Principles (GAAP), used in the United States for financial reporting by publicly traded and many private companies, encompass a set of standardized rules and standards.
- Though not government-regulated, they have been adopted by the U.S. Securities and Exchange Commission (SEC) to enhance financial reporting uniformity.
- While the SEC aims to transition to International Financial Reporting Standards (IFRS), the process has been gradual due to significant differences between IFRS and GAAP.
- Despite not being mandated for all businesses, publicly traded companies must adhere to GAAP in financial reporting as required by the SEC.
- Key organizations shaping the development of Generally Accepted Accounting Principles (GAAP) in the United States include: United States Securities and Exchange Commission (SEC), American Institute of Certified Public Accountants (AICPA), Financial Accounting Standards Board (FASB), and Governmental Accounting Standards Board (GASB).
- IFRS stands for International Financial Reporting Standards. These are a set of global accounting standards developed and maintained by the International Accounting Standards Board (IASB).
- IFRS provides a common framework for preparing financial statements and reporting financial performance across different countries and industries.
- It aims to enhance transparency, comparability, and consistency in financial reporting worldwide, making it easier for investors, analysts, and stakeholders to understand and assess the financial performance of companies operating in different regions.
- IFRS is widely adopted by many countries and organizations around the world, particularly in regions where it is mandated for use in preparing financial statements of publicly traded companies.
- Despite being adopted by over 100 countries, some nations have not yet implemented IFRS due to certain criticisms.
- Ind AS, a convergence of Indian Accounting Standards and IFRS, offers an opportunity to thoroughly reevaluate financial reporting and revamp financial policies and processes. This transition is expected to benefit the overall economy, industries, and investors.

GAAP	IFRS
Framework based on legal authority	Based on a principles-based approach
More detailed and prescriptive	More high-level and flexible
Requires more disclosures	Requires fewer disclosures
More focused on the historical cost of assets	More flexibility in the valuation of assets
Only adopted in the US	Globally accepted
Developed by Financial Accounting Standard Board (FASB)	Developed by International Accounting Standard Board (IASB)
Uses FIFO, LIFO and weighted average cost method of inventory valuation	Allows FIFO and weighted average cost method for valuation of inventories
Uses a cost model for fixed asset valuation	Uses a revaluation model for valuation of fixed assets
Fixed assets are valued using the cost model, or the historical value of the asset less any accumulated depreciation	Allows another model - the revaluation model - which is based on fair value on the date of evaluation, less any subsequent accumulated depreciation and impairment losses

TRANSFER PRICING

Transfer pricing involves setting the prices for goods and services within a multi-divisional organization, especially for cross-border transactions.

Transfer pricing is established in Indian banks but is applied differently across institutions for various goals. It's commonly used to assess branch performance and has gained importance with the adoption of prudential accounting norms. Banks aim to enhance branch profitability and overall performance using the Transfer Price Mechanism (TPM), which involves interest rates for fund transfers between branches. The interest rate must align with the arm's length price concept for fairness and compliance.

Arm's length price refers to the price that unrelated parties would agree upon. Though country-specific laws may vary, they are generally based on OECD guidelines. Despite taxation risks, using global transfer pricing policies can effectively determine an appropriate arm's length price range for transactions across an enterprise.

Traditional Transfer Pricing Methods:	Non-traditional Transfer Pricing Methods:
Comparable Uncontrolled Price (CUP) Method: Compares the price of a controlled transaction to that of a comparable uncontrolled transaction. However, finding truly comparable transactions is challenging due to minor trade circumstance variations.	Profit Split (PS) Method: Applied when integrated businesses make separate evaluation impossible. Profits are split based on contributions, often measurable by factors like compensation and expenses.
Cost Plus Method (CP): Adds an appropriate mark-up to costs incurred in manufacturing/purchasing goods. The mark-up is based on comparable companies' profits.	Transactional Net Margin Method (TNMM): Examines a company to determine the net profit margin relative to a base of costs. It unifies RP and CP methods using comparable companies to apply an appropriate margin.
Resale Price Method (RP): Works backward from transactions in the supply chain, subtracting a gross margin from the sale price to an unrelated third party. Appropriate gross margin is determined by comparing transactions.	

QUESTIONS

1. Accounting Standard 7 (AS 7) deals with the accounting for construction contracts. Its main objective is to provide guidelines for recognizing and measuring revenue and costs related to construction contracts. Construction contracts typically span multiple accounting periods, as they involve activities that are initiated at one point in time and completed at a later date.

One type of contract is a cost-plus contract. Which of the following statements is true regarding a cost-plus contract?

(*a*) The buyer agrees to pay the seller a fixed price for the project, regardless of the actual costs incurred.

(*b*) The seller is only reimbursed for the direct costs incurred without any additional profit or fee.

(*c*) The contract price is determined based on the estimated costs of the project, without considering any changes or variations.

(*d*) The seller is entitled to recover the actual costs incurred along with an agreed-upon profit margin or fee.

2. A Small and Medium Sized Company (SMC) is a company?

(*a*) whose debt securities or equities are not listed on any stock exchange.

(*b*) whose revenue in the immediately prior accounting year was not more than 250 crores (excluding other income).

(*c*) which at no time during the immediately prior accounting year had borrowings (including public deposits in excess of 50 crores.

(*d*) All of the above

3. Match the Number of Accounting Standards with their correct title.

Number of Accounting Standard		Title of the Accounting Standard	
A.	AS 28	(*i*)	Intangible Assets
B.	AS 22	(*ii*)	Impairment of Assets
C.	AS 24	(*iii*)	Accounting for taxes on income
D.	AS 26	(*iv*)	Discontinuing of operations

(*a*) A-(*i*), B-(*iii*), C-(*iv*), D-(*ii*)

(*b*) A-(*iii*), B-(*ii*), C-(*iv*), D-(*i*)

(*c*) A-(*ii*), B-(*iii*), C-(*iv*), D-(*i*)

(*d*) A-(*ii*), B-(*iv*), C-(*i*), D-(*ii*)

4. Match the following Accounting Standards with their title

Accounting Standards		Title	
A.	AS - 1	(*i*)	Disclosure of Accounting Policies
B.	AS - 2	(*ii*)	Cash flow statements
C.	AS - 3	(*iii*)	Valuation of inventories
D.	AS - 19	(*iv*)	Leases

(*a*) A - (*i*); B - (*ii*); C - (*iii*); D - (*iv*)
(*b*) A - (*i*); B - (*iii*); C - (*ii*); D - (*iv*)
(*c*) A - (*iv*); B - (*iii*); C - (*ii*); D - (*i*)
(*d*) A - (*iii*); B - (*i*); C - (*ii*); D - (*iv*)

5. In accounting, amalgamation refers to the process of combining two or more companies into a single entity. It is a type of corporate restructuring in which the assets liabilities, and operations of multiple companies are merged to form a new or existing company. The main purpose of amalgamation is to consolidate resources, increase operational efficiency,and create synergies among the merging entities.
Which of the following accounting standards deal with accounting for amalgamation of companies?
(*a*) AS - 05 (*b*) AS - 14 (*c*) AS - 21 (*d*) AS - 25

6. Which of the following accounting standards is related to consolidated financial statements?
(*a*) AS 01 (*b*) AS 21 (*c*) AS 26 (*d*) AS 16

7. Who notifies the IND AS in India?
(*a*) Ministry of Finance
(*b*) Securities and Exchange Board of India (SEBI)
(*c*) Ministry of Corporate Affairs
(*d*) Reserve Bank of India (RBI)

8. GAAP refers to a set of accounting standards,principles, and procedures that are widely recognized and followed in the preparation and presentation of financial statements. What does GAAP stand for?
(*a*) Generally Accepted Accounting Policies
(*b*) General Accounting and Auditing Practices
(*c*) Generally Applied Accounting Procedures
(*d*) Generally Accepted Accounting Principles

9. The business entities which follow Accounting Standards are required to prepare a cash flow statement as a part of their financial statements. Which of the following Accounting Standards provide guidelines for preparing this cash flow statement?
(*a*) AS - 3 (*b*) AS - 7
(*c*) AS - 10 (*d*) AS - 3 and Ind AS - 7

10. A three-stage approach is used to measure ECL on financial instruments accounted for at amortised cost. Which of the following is NOT one of three stages that financial assets will migrate through based on changes in credit quality?
(*a*) 6 months ECL
(*b*) 12 months ECL
(*c*) Lifetime ECL - Credit Impaired
(*d*) Lifetime ECL - Non-Credit Impaired

HINTS & SOLUTION

1. (*d*) **2**. (*d*) **3**. (*c*) **4**. (*b*) **5**. (*b*) **6**. (*b*) **7**. (*c*) **8**. (*d*) **9**. (*d*) **10**. (*a*)

1. (*d*) In a cost-plus contract, the seller is reimbursed for the actual costs incurred in the project, including direct costs and sometimes indirect costs or overheads. Additionally the seller is entitled to a profit margin or fee which is typically agreed upon in advance. This allows the seller to recover their costs and earn a reasonable profit for their services.
This type of contract is commonly used in situations where the scope of work or project requirements are uncertain making it difficult to determine a fixed price upfront. The cost-plus contract provides flexibility by allowing for adjustments to the contract price based on the actual costs incurred during the project.

2. (*d*) A Small and Medium Sized Company (SMC) is a company
1. whose debt securities or equities are not listed on any stock exchange.
2. whose revenue in the immediately prior accounting year was not more than 250 crores (excluding other income).
3. which at no time during the immediately prior accounting year had borrowings (including public deposits) in excess of 50 crores.
4. which is not a holding or subsidiary company of a company which is not a small and medium-sized company.

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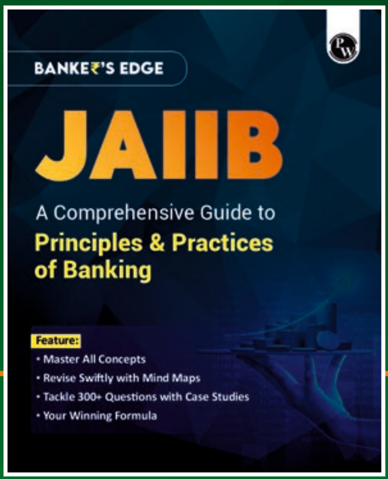

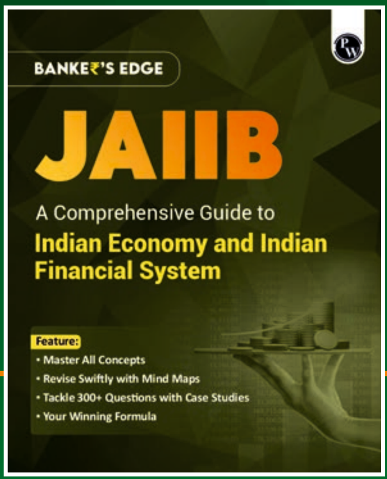

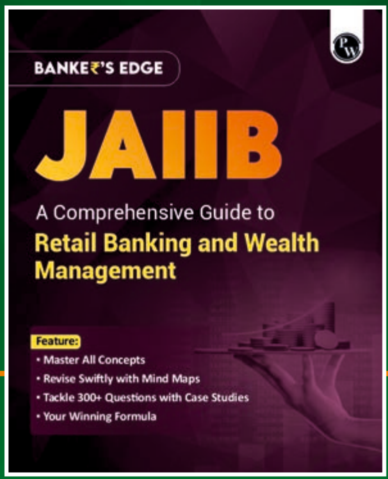

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