Chaper-1: Introduction

Origin of the word "BANK": Generally it is assumed that the word "BANK" was probably derived from the word "BENCH". Because during the ancient time people used to do money-lending business sitting on long bench. There are at least three schools of thought who give their separate opinion about the origin of word "Bank". Some of the economists believe that the word bank originates from the German word BANC meaning a joint stock firm. The second school of thought believes that the word bank has been derived from the Italian word 'BANCO' which means heap or mound. There are another group of people who traces the origin of the word bank to the Greek word "BENQUE" meaning a bench.

According to prof. chamber the word BANK came from the Italian word 'Banco' and French word 'Banque.

Finally we can say that with the passage of time the word Banco, Banc or Banque becomes Bank.

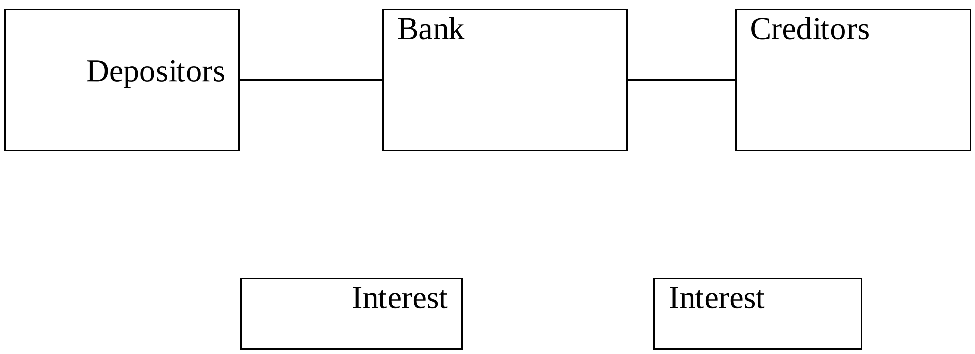
Definition of Bank: Bank is a financial institution that collects surplus cash from society and gives a part of that as a loan to investors for earning profit. More precisely bank is a financial intermediary that accepts deposits and channels those deposits into lending activities, either directly through by loaning or indirectly through capital market. That is, a bank established relationship between the customer that have capital surplus and the customer that have capital deficit.

According to American Institution of Bankers- "A bank provides service activity and acts as an intermediary between creditor and lender."

According to Dictionary of Banking and Finance "Bank is an institution that is registered by central bank and mainly performs the following activities:

- Receives current deposits and give the withdrawal facilities to clients through cheque.
- Receive term deposits and pay interest on them.

- Discounting notes, approving loans, and invest in government and other credit instrument.
- Collect cheque, draft and note etc.
- Notification of depositor's cheque.
- Acts as a trustee in accordance with government permission.



So at last we say that bank is a business/financial institution that receives surplus funds of individual, trading or non-trading institution, government or private institution as deposits and supply money with assurance of repayment against security in exchange of profit or interest to trading or non-trading institution who has deficit fund and demand for money.

<u>Origin and Historical Evaluation of Bank:</u> Really it is very difficult to say about the origin and historical evaluation of Bank. But it is sure that the development of bank is performed step by step. Historical evaluations of bank are discussed below:

As early as 2000 B.C. Babylonians had developed a system for depositing their extra money which was known as Bank. That is, the history of banking begins with the first proto type banks of merchants of the ancient world which made grain loans to farmers and traders who carried goods between two cities. This began around 2000B.C. in Babylonian.

In 1157 the bank of Venice was established which was the first public banking institution. Originally it was not a bank in modern sense, rather an office for transferring public debt.

History shows the existence of a 'Monte' in Florence in 1336. The meaning of 'Monte' is given in Italian dictionary as- a standing bank or mount of money, as they have in diverse cities of Italy.

As early as 1349 the business of the banking was carried on by the drapers of Barcelona. During 1401 a public bank was established in Barcelona. It used to exchange money, receive deposits and discount bills of exchange both for citizens and foreigners.

In 1407 the bank of Genoa was established. It accepted all kinds of deposits which could be drawn on demand or transferred from the account of one person to another. It is one of the greatest banks of the century at that time.

The bank of England was established in 1694 in England but the development of modern commercial banking institution was started only when banking act of 1833 was passed.

However it was only in 19th century when the modern joint stock commercial banking system developed in most of the lending countries of the world.

In ancient India, the joint stock companies' act 1850 was the first legislative enactment which permitted the corporate sector to come into the banking business as per provisions of the act. The first bank to be established under this act was the Oudh commercial bank in 1881 followed by Punjab national bank in 1895 and People's bank in 1901.

Banking History in Bangladesh: Banking in Bangladesh is as old as banking in other parts of the world. Today's banking system has evolved primarily from British banking through it has undergone substantial changes in post-liberation period.

After the emergence of Bangladesh in 1971 Bangladesh Bank was established in 1972 which is the successor bank of state bank of Pakistan. It is wholly government- owned bank managed by a board appointed by the government.

Again after the achievement of victory against pak-occupation forces on 16th December 1971, there were 12 scheduled banks operating in Bangladesh. All these banks were established by west Pakistanis and their head offices were in West Pakistan.

Nationalized Commercial Banks (NCBs) were established in Bangladesh in 1972 through amalgamation of twelve commercial banks that were operating in pre-independent Bangladesh.

The Bangladesh government initially nationalized the entire domestic banking system and proceeded to reorganize and rename the various banks. Foreign-owned banks were permitted to continue doing business in Bangladesh.

The policy of the government regarding economic management has changed since 1976 from which year private sector has been entrusted to play a bigger role in the economy than before. Accordingly, to encourage private sector and to create competition in the banking sector, government decided to allow setting-up of local private commercial banks in addition to nationalized commercial banks operating in the country. Few private commercial banks were allowed to operate in the country in 1981.

In Bangladesh first private bank was incorporated in 1983. On that time govt. approved some commercial bank to operate their activities which are IIBL, ABBL, NBL and IFIC bank.

After enactment of Banking Company act-1991, banking business becomes popular in Bangladesh. In 1991 govt. again approved some commercial and specialized banks such as DBL, NCCBL etc. In this way various political govt. in our country approved different banks in different time. Now there are 66 banks in our country which have various natures.

- 1981-1990, 9 private commercial banks
- 1991-1996, 8 private commercial banks
- 1996-2001, 13 private commercial banks
- 2009 till today 14 private commercial banks

Nationalization of Bank: Immediately after the govt. of Bangladesh consolidated its authority, it decided to adopt a socialistic pattern of society. This means a society with wealth distributed as possible was adopted as the state policy of the government for newly created state of Bangladesh. In order to implement the above mentioned state policy, the govt. of Bangladesh decided to nationalize all the banks of the country. Accordingly on the 26th March, 1972, the Bangladesh Bank (Nationalization) order 1972, (president's order no.26 of 1972) was promulgated. All the existing 12 banks were nationalized and were taken over by the government under the president's order.

Under Article 4 of the nationalizing law, six new banks have been constituted with all the legal characteristics of body corporate. Each of the new banks has common seal and perpetual succession and subject to the prevision of the law each new bank is empowered to acquire, hold, and dispose of the property, to contract and to sue and be sued in its own name. the undertakings of existing banks specified below stand transferred to and vested in, the new banks mentioned against them.

Nationalized Banks	Amalgamated and rename after nationalization
• National Bank of Pakistan • Bank of Bahawalpur Limited • Premier Bank Limited	Sonali Bank

• United Bank Limited • Union Bank Limited	Janata Bank
• Habib Bank Limited • Commerce Bank Limited	Agrani Bank
• Muslim commercial Bank Limited • Standard Bank Limited • Australasia Bank Limited	Rupali Bank
Eastern Mercantile Bank Limited	Pubali Bank
Eastern Banking corporation Limited	Uttara Bank

Objectives of Nationalization: Objectives of nationalizing commercial banks are outline below:

- To ensure that banking system serves a much wider section of the community by dispensing credit to the poorest and weaker sections of the society.
- Remove the regional disparities.
- Help in development of backward areas.
- Serve better the needs of development of the economy in conformity with national policy and objectives formulated by govt.
- Improving our rural economy for socio-economic upliftment by boosting up production activities in the rural sectors so as to raise the income level and living standard of the rural inhabitants.

Bangladesh Bank: Bangladesh Bank is the central bank of Bangladesh. It was established on 16th December 1971 under the Bangladesh Bank (temporary) order1971n (Subsequently substituted by the presidential order no. 127 of 1972). The powers and functions of Bangladesh Bank are governed by Bangladesh Bank order 1972 and Banking companies' act 1991.
The bank is run according to the direction of the government. The chief executive, the governor and his deputies as well as the bank's policy making body board of directors are all appointed by the government. Bangladesh Bank has 10 branches. 2 branch office in Dhaka (one in Motijheel and another is in Sadarghat) and other branches in Barishal, Chittagong, Rangpur, Sylhet, Bogra, Khulna, Rajshahi and Mymnsynha.
With the recommendation of World Bank /IMF, govt. in 2003 provided some degree of autonomy to the bank to carry out its responsibilities without undue interference of the government and a new body called co-ordination council headed by ministry for finance with ministry of commerce , governor of Bangladesh Bank, secretary of finance divisions, secretary of international resource division, member of planning commission as the member has been set up to oversee the Bangladesh Bank's fiscal, monetary and exchange rate policies.

<u>Functions of Bangladesh Bank:</u> The Bank which builds up banking system and money market is a central bank. Bangladesh bank is the central bank in our country which functions are briefly outlined below:

Issuance of notes & coins: Bangladesh Bank is the sole authority for issuance of bank notes in the country. This power enables the bank to regulate and control money supply in the country. With the exception of one and two taka notes & coins remaining notes and coins are issued by Bangladesh Bank.

Government Bank: The bank acts as the banker to the government and manages the public debt, custodian and management of the country's internal value of taka and acts as a adviser to government in economic matters in general and financial problems in particular. Bangladesh Bank conducts and maintains government accounts for all government receipts and payments.

Baker's Bank: The Banks also functions as the banker's bank. All commercial banks maintain their accounts with Bangladesh Bank. They borrow money from Bangladesh Bank when necessary. In case of difficulties, Bangladesh Bank acts as lender of the last resort to commercial banks. At the same time, schedule banks are allowed rediscounting facilities from Bangladesh Bank against govt. securities to meet their temporary requirements of fund.

Reservoir of foreign currency: Bangladesh Bank maintains foreign currency reserve.

Clearing house:

Credit control:

Others:

- To formulate and implement monetary policy.
- To formulate and implement intervention policies in the foreign exchange market.
- To give advice to the govt. on the interaction of monetary policy with fiscal and exchange rate policy.
- To promote, regulate and ensure a secure and efficient payment system including the issuance of bank notes.
- To regulate and supervise banking companies and financial institutions.

<u>Controlling Volume of Credit:</u>

Bangladesh bank formulates and conducts its monetary and credit policies in a manner consistent with the government's targets for growth and inflation and the recommendation of co-ordination council for attaining macro-economic objectives. These monetary and credit policies are primarily implemented through banking channel. The main instrument of selective credit control are (a) minimum margins for lending against selected commodities, (b) ceiling on the levels of credit and (c) charging of minimum rate of interest on advances against specific commodities.

Credit control mechanism: Bangladesh Bank also controls volume of credit in a quantitative way so as to influence the total volume of bank credit in the following ways:

Bank rate**:** Bank rate is the rate of interest at which Bangladesh Bank gives loan to the commercial banks. That is bank rate is that rate at which Bangladesh Bank re-discounts the first class bills of exchange from commercial banks. Whenever Bangladesh Bank wants to reduce credit, the bank rate is raised and whenever the volume of bank credits is to be expended the bank rate is lowered. This is because by changes in the bank rate, Bangladesh Bank seeks to influence the cost of bank credit.

Open Market Operations**:** Bangladesh Bank can influence resources of commercial banks by buying or selling government securities in open market. If Bangladesh Bank buys government securities in the market from commercial banks, there is a transfer of cash from Bangladesh Bank to commercial banks and this increases the cash base of the commercial banks enabling them to expand credit and conversely, if Bangladesh Bank sells govt. securities to the commercial banks, the commercial banks transfer cash to Bangladesh Bank and therefore, their cash base is reduced, thus adversely affecting the commercial banks to expand credit.

Variables Reserve Requirement: The commercial bank is under obligation to keep cash reserve with Bangladesh Bank. Bangladesh Bank is legally authorized to raise or lower the minimum reserves that the commercial banks must maintain against their deposit. Present minimum cash reserve ratio is 5.5 per cent (14 April, 2018) of total demand and time liabilities. If there be a shortfall in the maintenance of CRR, penal interest is charged on shortfall. It has got the power to use the variable reserve requirements as an instrument of monetary Control.

Exchange Control: Being responsible for maintaining the external value of taka, Bangladesh Bank also administers exchange control in the country. This task is two-fold. On the one hand, it ensures that all foreign exchange receipts are accounted for and surrender to the authorized dealers; on the other, it allocates and rations foreign exchange in line with set priorities.

Chapter-2: Commercial Bank

<u>Commercial Bank:</u> Generally the bank which collects deposits according to the nature of accounts & gives loan from the deposits and gain profit or interest is called commercial bank. That is, commercial bank is a financial institution which is authorized by law to receive money from business & individuals and lend money to them. Commercial banks are open to the public and serve individuals, institutions and business. The inception of modern banking is the outcome commercial bank. The main element of commercial bank is money and its main objective is to earn profit. Commercial bank is called "The mother of modern bank".

According to prof. Roger, "The bank which deals with money and money's worth with a view to earn profit is known as commercial bank".

According to prof. Ashutoshnath, "commercial bank is an intermediary profit making institution."

So at last we say that Commercial bank

- Is an intermediary institution of capital and money market
- By various accounts it collects deposits on small rate of interest.
- Gives short-term loan to others on higher rate of interest.
- Main objective is to earn profit.

<u>Inflow and Outflow of Commercial Bank's Funds:</u>

<u>Inflows of bank funds:</u>

- Increase in deposits
- Increase in borrowing
- Undistributed profit
- Loan recovery
- Return of invested funds on maturity
- Sales proceeds of other assets: if any.

<u>Outflows of bank funds:</u>

- Increase in loans and advances

- Increase in investment
- Increase in the cash in hand
- Withdrawal of deposits
- Repayment of borrowing
- Payment of dividends
- Increase in other assets

Comparison of different sources of bank funds: Deposits is the principal source of fund for bank. In addition to deposits, a bank has many other sources of funds. The major sources of bank funds are discussed below:

***Paid-up-capital**:*

Reserve and retained earnings: Reserves and retained earnings are created out of profits earned by banks. Unless profits can be increased by maximizing business, rising of reserve base is particularly impossible.

Call money: Usually this source is utilized by banks to meet emergency needs. Banks which have excess liquidity usually lend in call money market and banks having shortage of liquidity borrow. As a source it is neither stable nor desirable from the view point of liquidity and profitability. Continuous borrowing from call money market gives a wrong signal to other banks about the bank borrowing such fund. On the other hand, rate of interest in call money market also many times tend to be very higher.

Inter-bank deposits: Banks do not keep their funds idle for long time. But some banks might have excess liquidity for the time being. It is possible that they may, under the circumstances, keep fund with other banks for a shorter period. However, this is not a dependable source of fund since it may be withdrawn at the will of the depositing bank.

Loan from central bank: This is another ground window of getting funds. Central bank sometimes provides finance to commercial banks through rediscounting of bills of commercial banks and counter-finance for specified items. But this source is subject to many limitations and restrictions. This is not always a welcome method of generating fund.

Deposits: Deposit is the most important and major source of funds of a bank. There is no limit up to which a bank may raise its deposit level. Sometimes because of operation of restrictive measures pursued by the central bank, deposit rising may be subject to limits.

Functions of Commercial Bank:

Principle functions:

Accepting deposits: The first and foremost function of commercial bank is to receive or collect deposit from the individuals, business houses, public authorities. Generally deposits are collected through various accounts e.g. current, savings, term deposits accounts. No interest is charged in the current accounts, lower rate of interest charged in the savings account and comparatively higher interest rates given in fixed deposits. In this way commercial banks are able to collect fund and thereby developing customers' network.

Lending of money: A major portion of the deposits received by a bank is lent by it. This is the main source of income of a bank. The business of lending is usually done in the form of loans, overdraft, cash credit, purchase and discounting bill of exchange, financing foreign trade etc.

- **Loan**: When an advance is made in a lump sum repayable either in fixed monthly installments' or in lump sum by way of interest, incidental charges etc. it is called a loan.
- **Overdraft:** When a customer requires temporary accommodation, he may be allowed to overdraw on his current account, usually against collateral security and pay interest on the amount actually used by him.
- **Cash credit**: A cash credit is an arrangement by which a banker allows his customer to borrow money against pledge of goods, either in bank's go down under effective control. This type of facility is more freely grand by banks than any other advances.
- **Purchase and discounting of bill of exchange:** Purchase and discounting of bill of exchange is another way employing the bank's funds. These bills of exchange are classified into demand bills and usance bills. Where a bill is payable on demand then it is called demand bill. If the bill matures for payment after a certain period of time it is called usance bill.
- **Financing of foreign trade:** Commercial banks have been playing an important role in providing adequate financing facilities to both exporters and importers in order to place our economy in sound footing. Besides commercial banks also undertake to issue guarantees of various types on behalf of their customers to support trading transactions both in inland and foreign trade.

Subsidiary Services by Commercial Bank: Besides performing the two essential functions of accepting deposits and lending & investing its funds modern commercial banks cover a wide range of financial and non-financial services to their customers and general public. The services and facilities provided by modern banker may be classified as:

- Agency services.
- General utility or miscellaneous services.

Agency services: Following are the agency services provided by commercial banks to their customer:

- ✓ **Collection and payment:** Commercial bank collects and pays values of cheque, bill of exchange, promissory notes, pension, dividends, insurance premium, and interest on behalf of the clients.

- ✓ **<u>Purchase and sale of share & securities:</u>** Banks undertake to purchase and sell of shares and debentures of joint stock Company on behalf of its customer only whenever the customers delegate the work, the bankers should get clear and precisely instruction for this purpose. In executing the sale or purchase, the bankers act as an agent of the customer.
- ✓ **<u>Execution of standing instructions:</u>** A customer may leave standing instructions with his banker for the payments of sums to various persons or institutions against his account. Such orders may usually be given in respect of payment of insurance premium, subscription of club/ society, payment of rent and salaries and similar payments of a regular recurring nature. The bank may charge small fee for rendering such services.
- ✓ **<u>Maintenance of secrecy</u>**: Maintenance of secrecy is one of the most important functions of commercial bank. That is, commercial banks do not disclose information about customer without his consent.
- ✓ **<u>Act as a trustee:</u>** Commercial banks act as a trustee on behalf of the customers.
- ✓ **<u>As executor and administrator:</u>**
- ✓ **<u>Remittance of funds:</u>** In this competitive world all commercial banks have a network of branches thought the country. With this facility banks can conveniently provide the service of transferring funds from one place to another. Important methods of transferring funds are:
- ❖ ***Mail Transfer (M T):*** Banks provide the facility of sending money through mail transfer to any at any place where the bank has a branch and the person has an account in any other branch of the same bank.
- ❖ ***Telegraphic Transfers (T T):*** if the money is to be sent urgently, the bank may be requested for telegraphic transfer on payment of a nominal charge and telegraphic charges. Such facility is available at selected branches.
- ❖ ***Demand draft (D D):*** Demand draft is an order from one branch to another branch of the same bank to pay a specified sum of money to a person named therein or his order. The draft is payable on demand.

<u>General utility or miscellaneous services:</u> Commercial banks also provide a variety of general utility services which are briefly discussed below:

Letter of credit: This is a non-fund facility provided by banks to its customers. It is generally used in international trade.

Traveler's cheques: Traveler's cheques, a sort of cash substitute, are universally accepted method of payment for overseas travelers. It is very useful to persons who frequently travel abroad. It can be purchased by any one. He needs not be a customer of the bank.

Safe custody of valuables: A bank undertakes the safe custody of a client's valuables and important documents against theft and fire. There are two ways through which a banker ensures safety of its customers' valuables:

- Safe custody
- Safe deposits vaults (lockers)

When a bank takes care of important documents or other valuable possessions for someone, in return for a regular charge then it is called safe custody.

An area, usually found in a bank or other financial institution, which is a safe and secure place for storing items of value. Vaults are usually used to store cash, as well as customers' safe deposit boxes.

Bank giro: A method of transferring money by instructing a bank to directly transfer funds from one bank account to another without the use of checks. Giro transfers have become a more accepted payment method than checks because they provide security when lost or stolen, and they can be processed more quickly than a standard check.

Credit card: Credit cards are issued by the banks to good customers having current and savings accounts, free of charge. The cards enable a customer to purchase goods or services from certain retail and service establishments up to a certain limit without making immediate payment

Debit card:

Acting as a referee*:* A bank sometimes acts as a referee as to the responsibility and financial standing of his customers. This is very valuable service to businessmen.

Information and other services: As a part of their comprehensive banking services, many banks act as a major source of information on overseas trade in all aspects. Some banks produce regular bulletin on trade and economic conditions at home and abroad, their special reports on commodities and markets.

Consultancy service*:*

<u>Sound Banking Principles:</u> A successful and ideal commercial bank follows some principles in order to ensure smooth running of banking business. To cope with the prevailing competition, to provide better services to the clients and to gain competitive advantages commercial banks have to be careful about their services. The important sound principles of commercial bank are as follows-

- ***Principles of liquidity:*** Deposits are the life blood of the commercial bank. Deposits are repayable of demand or after expiry of a certain period. Everyday depositors either deposits or withdraw cash. To meet the demand for cash all commercial banks have to keep certain amount of cash in their custody.
- ***Principles of profitability***: The driving force of commercial enterprise is to generate profit. So it is true in case of commercial banks.
- ***Principles of solvency***: Commercial banks should have financially sound and maintain a required capital for running the business.
- ***Principles of safety***: While investing the fund, banks are to be cautious because bank’s money is the depositor’s money. Unless the money lent out is safe, the banks can’t pay

depositors money back. So banks must greatest care and vigilance in the matter of investing the funds received from public in the form of deposits.

- ***Loan and investment policy***: The main earning sources of commercial banks are lending and investing money to the viable projects. So commercial bank always tries to earn profit through sound investment.
- ***Principles of Economy***: Commercial banks never go for any unnecessary expenditure. They always try to maintain their functions with economy that increase their yearly profit.
- ***Principles of Secrecy***: Commercial bank maintains and keeps the clients accounts secretly. Nobody except the legitimized person is allowed to see the accounts of the clients.
- ***Principles of Modernization:*** It is the age of science and technology. So to cope up with the advance world the commercial bank has to adopt modern technical services like online banking, credit card etc.
- ***Principles of Specialization***:
- ***Principles of Publicity***: If commercial banks would like to earn more money, they have to give more advertisement through various media. In that case, commercial banks follow this kind of principle to increase their customer.

<u>Factors and trends influencing determination of cash balances</u>: Some of the important factors and trends which influence the determination of the amount of cash balances maintained by a banker are as follows:

- ***Banking habits:*** The need to maintain large amount of liquid cash will not be there if the customers are highly banking mined. In advance countries where people have cheque habit, the use of cash is very much reduced. All transactions are settled through cheques.

- ***Local business and economic conditions***:
- ***Nature of the account:*** Average size of deposits also determine amount of cash reserve. If the accounts are of a fluctuating nature, a higher cash reserve may be required.
- ***Nature of advances***: The nature of different types of advances made by the banker and the refinancing facilities provided by Bangladesh Bank also affect the cash reserve. The Bangladesh Bank provides advances and rediscounting facilities to banks. A banker may employ more funds in discounting of bills and rediscounting the same bills from Bangladesh Bank and thereby keep less cash reserve.
- ***Statutory cash reserve with Bangladesh Bank***:
- ***Level of operation***:
- ***Efficiency of clearing house***
- ***Location of the bank***

<u>Clearing House System:</u> Generally clearing house is an establishment maintained by banks for settling mutual claims and accounts. More especially clearing house a bankers' establishment where cheques and bills from member banks are exchanged, so that only the balances need be paid in cash. That is, clearing house is an arrangement for the banks to mutually settle their claim over each other arising out of deposit transfer from one bank to another by their respective customers. For the purpose of collection of cheques and drafts bank have devised a system called clearing house where all banks have their accounts. That is, clearing house is an organization of banks which settles inter-bank liabilities due to transfer of deposits by customers from one bank to another. In Bangladesh, BB performs the functions of clearing house wherever is has its offices. At places where the BB does not have its offices, the Sonali bank manages the business of clearing houses.

The mechanisms of clearing house are as follows:

- Each member bank of the clearing house prepares a bank wise list of cheques and drafts received from its customers and drawn on different banks.
- Representative of each bank visits the clearing house with the cheques and their list in the morning and delivers the cheques and drafts to the representatives of the respective banks. Similarly he also receives the same things from others.
- The representative returns to their respective banks to meet again in the afternoon.
- The representative of each bank computes the final balance payable or receivable his bank from other banks after taking into account the various amounts of receipts and payments.
- The final settlement is affected by the supervisor of the clearing house by debiting or crediting the accounts of the respective banks.

RTGS: The term real-time gross settlement (RTGS) refers to a funds transfer system that allows for the instantaneous transfer of money and/or securities. RTGS is the continuous process of settling payments on an individual order basis without netting debits with credits across the books of a central bank. Once completed, real-time gross settlement payments are final and irrevocable. In most countries, the systems are managed and run by their central banks. RTGS is one of the fund transfer systems which facilitate the real-time transfer of funds. RTGS is considered to be the fastest fund transfer method offered by the banks. RTGS system is an electronic way of transferring funds and does not need any exchange of money physically. The RTGS is suited for high-value transactions that require immediate clearing. It is an instant transfer and the bank that is supposed to receive the funds from the remitting bank, has it remitted in seconds. It is expected of the bank to deposit the funds within 30 minutes of the transfer message. RTGS also allows setting up the transfer at a later point in time. The value date of the transaction shall be analysed and the transfer is made from the queue.

Electronic Fund transfer system (EFTN/S): Transferring money from one bank account to another in an electronic mode is called Electronic Fund Transfer. The bank accounts may belong to the same or different banks. It is a computer-based transaction that is done in an electronic fashion. Electronic banking is the other name for EFT transactions. EFT creates a paper-free environment and also most sought by the people for its ease and convenience. Electronic Fund Transfer is also done through the ACH network. Electronic Funds Transfer is considered secured because of the usage of PIN (Personal Identification Number) and the login details which are known only to the customer. The money is transferred faster through EFT and the cost involved also is less. Ideally, this method helps save cost and effort in printing cheque leaves. Normally, cannot stop an EFT payment after initiating it, in case need to stop payment or refund amount then it’s between you and the person paid. However, we might able to stop scheduled payment such utility bills, recurring by notifying the financial institution to before 3 business working days.

<u>RTGS VS Electronic Fund transfer system (EFTS):</u>

- The main difference between EFT and RTGS is that EFT is based on net-settlement, meaning that the transactions are completed in batches at specific times; all transfers will be held up until a specific time. While RTGS is real-time and happens individually.
- EFT usually involves smaller value transactions and the maximum amount can be 2 Lakhs INR for the transactions. Whereas RTGS’ minimum value for transaction starts from 2 Lakhs INR.
- The process of EFTN is one working day, while RTGS processes in real-time (‘push’ transfer) EFT is slower, fewer transaction charges compared to RTGS.
- EFT is best for small value transactions and RTGS which is appropriate for a large amount of transactions.
- EFT takes time to transfer funds and it depends on the bank’s transaction timelines, but RTGS is an instant fund transfer mechanism.

<u>Non-Performing Assets:</u> Generally, non-performing assets refers to an asset which is not producing income. That is, non-performing assets means an assets which has ceased to generated income for the bank. Assets become non-performing when the interest or installment of principal is delayed and not received before the stipulated time. Banks usually classify as nonperforming assets any commercial loans which are more than 90 days overdue and any consumer loans which are more than 180 days overdue. Non-performing assets are problematic for financial institutions since they depend on interest payments for income as well as inevitable burden on the banking industry. Accumulation of non-performing assets is the direct result of deterioration in the quality of loan portfolio. Today the success of the bank depends upon the method of managing NPAs and keeping them within a tolerable level.

Factors contributed to non-performing assets: Following are the factors which contribute to non-performing assets:

Internal factors: Internal factors may be

- Diversion of funds for other purposes like expansion/modernization or for taking up new projects rather than the purpose for which it was borrowed.
- Diversion of funds for assisting or promoting other associate concerns.
- Time or cost overrun during the project implementation stage.
- Defective lending process.
- Improper SWOT analysis.
- Inadequate credit appraisal system.
- Absence of regular industry visit and monitoring.
- Business failures due to product failure, failure in marketing etc.
- Inefficiency in management.
- Alleged corruption.
- Inadequate network and linkage.
- Deficiency in re-loaning process.

External factors:

- Recession in the economy as a whole.
- Input or power shortage.
- Price escalation of inputs.
- Exchange rate fluctuation.
- Accidents and natural calamities.
- Changes in the govt. policies relating to excise and imports duties, pollution control orders etc.
- Govt. loan waiver scheme.
- Alleged political interference.
- Ineffective legal framework and weak recovery tribunal.

Others:

- Liberalization of economy like reduction of tariff, removal of restriction etc.
- Sudden crashing of capital markets and failure to raise adequate funds.
- Granting of loan to certain sectors on the basis of govt.'s directives rather than commercial imperatives.
- Mismatch of funding i.e. using loans granted for short terms for long term transactions.
- High leverage and high cost of borrowing.
- Willful defaults sensing that the legal recourse available to collect debts is very slow.

Roles of Commercial Bank in the economy of Bangladesh:

1. ***Mobilizing Saving for Capital Formation:*** The commercial banks help in mobilizing savings through network of branch banking. People in developing countries have low incomes but the banks induce them to save by introducing variety of deposit schemes to suit the needs of individual depositors. By mobilizing savings, the banks channelize them into productive investments. Thus they help in the capital formation of a developing country.
2. ***Financing Industry:*** Commercial banks finance the industrial sector in a number of ways. They provide short-term, medium-term and long-term loans to industry. In Bangladesh, the commercial banks undertake short-term and medium-term financing of small scale industries, and also provide hire- purchase finance. Besides, they underwrite the shares and debentures of large scale industries.
3. ***Financing Trade:*** Commercial banks help to finance both internal and external trades. The banks provide loans to retailers and wholesalers to stock goods in which they deal. They also help in the movement of goods from one place to another by providing all types of facilities such as discounting and accepting bills of exchange, providing overdraft facilities, issuing drafts, etc. Moreover, they finance both exports and imports of developing countries by providing foreign exchange facilities to importers and exporters of goods.
4. ***Financing Employment Generating Activities:*** Commercial banks provide financing facilities to employment generating activities in developing countries like Bangladesh. They provide loans for the education of young person's studying in engineering, medical and other vocational institutes of higher learning. They advance loans to young entrepreneurs, medical and engineering graduates, and other technically trained persons in establishing their own business. Such loan facilities are being provided by a number of commercial banks in Bangladesh. Thus the banks not only help inhuman capital formation but also in increasing entrepreneurial activities in developing countries.
5. ***Help in Monetary Policy**:* The commercial banks help the economic development of a country by faithfully following the monetary policy of the central bank. In fact, the central bank depends upon the commercial banks for the success of its policy of monetary management in keeping with requirements of a developing economy.
6. ***Assistance in transfer of money:*** Commercial bank transfers money from one place to another. It reduces the risk of carrying money & makes the transaction easy and comfortable that expands the business.
7. ***Maintaining economic stability*:** To maintain the economic stability commercial bank follows the credit control method of central bank.

Chapter-3: Relationship between Banker and Customer

Meaning of Banker: Generally banker is a dealer in money and capital money market. That is, the term 'banker' refers to a person or company carrying on the business of receiving moneys, and collecting drafts, for customers subject to the obligation of honoring cheques drawn upon them from time to time by the customers to the extent of the amounts available on their current accounts. Banker is an intermediary party between the borrower and lender. He borrows of one party and lends to another party.

G. Crowther: "A banker is a dealer in debt, his own and other people."

Prof. Hart "A banker is one who in the ordinary course of his business, receives money which he repays by honoring checks of person from whom or on whose account he receives it."

Sir John Paget: "No person or body corporate or otherwise can be a banker who does not take deposit accounts, take current accounts, issue and pay cheques and collect cheques crossed and uncrossed for his customers."

Meaning of Customer: A person who has an account in a bank is considered its customer. In broader sense a person who has a bank account in his name and for whom the banker undertakes to provide facilities as a banker, is considered to be a customer. A customer of a bank need not be a person. A firm, joint stock Company a society or any separate legal entity may be a customer.

Prof. Hart "A customer is one who has an account with a banker or for whom a banker habitually undertakes to act as such."

Thus to constitute a customer the following essential requisites must be fulfilled:

- A bank account- savings, current, fixed deposits must be opened in his name by making necessary deposit of money.
- The dealing between the banker and the customer must be of the nature of banking business.

General relationship between banker and customer:

Debtor-creditor relationship: When a customer deposits money with his bank, the customer becomes a lender and the bank becomes borrowers. The money handed over to the bank is a debt. The relationship is that of a debtor and creditor.

Creditor and debtor relationship: when the bank lends money to the customer, the customer is the borrower and the bank is the lender. The relationship therefore is that of a creditor and debtor.

Banker as Agent & principal: A banker acts as an agent of his customer and performs a number of agency functions for the convenience of his customers. These are as follows:

- Purchasing or selling of securities
- Collection of income
- Making periodical payments as instructed by his customers.
- Collecting interest and dividend on securities lodged by his customers.
- Receiving safe custody valuables and securities lodged by his customers.
- Collecting cheques, drafts of the customers

Banker as Trustee: Ordinarily, a banker is a debtor of his customer in respect of the deposits made by the latter, but in certain circumstances he acts as a trustee also. The customer may request the banker to keep his valuables in safe vaults or one may deposit some amount and can request the bank to manage that fund for a specific purpose, which the bank does, or in case of corporate debentures, the bank can become trustee for debenture holders or the bank collects the cheques hundies of the customers in the capacity of trustee. Thus, there are wide varieties of trustee functions discharged by the banker.

Banker as Bailee: As a bailee, the banker should protect the valuables in his custody with reasonable care. If the customer suffered any loss due to the negligence of the banker in protecting the valuables, banker is liable to pay such loss. If any loss is incurred due to the situation beyond the control of the banker, he is not liable for penalty.

Adviser of customer: Bankers also advise customers on their investments in shares and debentures of joint stock companies and other securities. In performing this function, they act as advisers to customers.

<u>Obligations of Banker:</u>

Bankers are under the obligations to fulfill certain duties while dealing with customers. Such obligations are as under:

- Obligation to honor the customer's cheques
- Obligation to maintain secrecy of customer's account
- Obligation to receive the cheques and other instruments for collection
- Obligation to honour the cheques of customers across the counter
- Obligation to give reasonable notice before closing the customer's accounts
- Obligation to provide information with respect to running the account.

Obligation to honor the customer's cheques: A banker must honour customers' cheque drawn on him provided:(a) The banker has sufficient funds of the customer,(b)The funds are properly applicable to the payment of such cheque, (c)The banker has been duly required to pay.(d)The cheque has been presented within a reasonable time after the apparent date of its issue;(e)No prohibitory order of the court or any other competent authority e.g. tax authority, is standing against the accounts of the customer.

Obligation to maintain secrecy of customer's account: When a person opens an account in a bank he/she is entitled to a reasonable assurance that information regarding the account remains a matter of knowledge only between the banker and the account holder. This is because; it is one of the principal duties of the banker to maintain complete secrecy of the status of the customer's account. This obligation of the Bank to maintain secrecy continues even after the customer's account is closed. If the banker makes an unwarranted disclosure of the status of account of the bank's customer, the banker becomes liable to compensate the customer. There are certain circumstances in which the banker is entitled or required to make disclosures about a customer's account:

- Under law
- Under express or implied consent of the customer
- Common courtesy among bankers
- Disclosure in the bank's interest
- Disclosure in Public/National interest

Obligation to receive the cheques and other instruments for collection: Basically, the business of banking, as it is known today, comprises acceptance of money on deposit account and payment of cheques. It also includes collection of cheques. It may rightly be contended that rightly be contended that services is not a banker. Whenever a banker is entrusted with the job of collection of cheques, they must be collected as speedily as possible through the accepted channels. Failure to exercise proper care and employ the recognised route for collection may make the bank liable for any loss which the customer may sustain.

Obligation to give reasonable Notice before Closing the Account: According to law, a debtor and a creditor may terminate the relationship without notice by the debtor paying off the balance or the creditor recalling the debt. It is not so simple between a banker and a customer for the obvious reason that the banker is under an obligation to honour his customer’s cheques. If this obligation could be terminated by the banker without notice, the customer might be faced with an embarrassing situation. Reasonable time must be granted to enable him to make alternative arrangements. Where any customer becomes a nuisance through overdrawing without arrangement or issuing post-dated cheques etc, it is advisable to close his account. But reasonable time has to be given to enable him to make alternative arrangements if he so desires. If a bank abruptly closes the customer’s account, it might affect his credit, giving cause for an action against the bank for damages.

Garnishee order: Generally a court order, making a garnishee pay money not to the debtor, but to a third party is called garnishee order. More especially garnishee order is a court order instructing a garnishee (a bank) that funds held on behalf of a debtor (the judgment debtor) should not be released until directed by the court. The order may also instruct the bank to pay a given sum to the judgment creditor (the person to whom a debt is owed by the judgment debtor) from these funds. Garnishments are typically used for debts. Garnishments can have a negative impact on one's credit rating.

The garnishee order is issued by court in two parts:

Order Nisi**:** By the order of the court:

- Directs the banker to freeze the debtor’s account.
- Seeks the banker to explain why the funds in the account, so freeze should not be used for payment to the judgment creditor.

On receipts of such an order the banker should immediately inform the customer (judgment debtor) so that he may make the necessary arrangements for payment of the debts due by him. No fund is payable by the banker on receipts of order nisi from the court until the order is made absolute by the court.

Order absolute: This order directs the banker to pay either the whole or a part of the funds lying in the account against which “order nisi” has been issued to the judgment creditor.

In the following circumstances the Garnishee order would not be applicable:

- Where the account of the judgement debtor is a joint account holder with another person;
- Where the identity of the judgement debtor is doubtful;
- Where the account of the judgement debtor is held by him in the capacity of a trustee;
- Where the judgement debtor has previously made an official assignment of his balance in favor of a third party and the banker is informed about it in writing;
- Where the account of the judgement debtor reveals a debit balance.

Rights of a Banker to customer:

- Right of general lien
- Right of set-off
- Right to appropriate payments
- Right to charge interest, incidental charges
- Right not to produce books of accounts
- Right to close accounts

***Right of general lien**:* A banker has the right of general lien in respect of the dues to him by the customer. Lien is the right to retain property belonging to another until a debt due from the latter is paid. In other words, it is the right of the creditor to retain the goods and securities in his possession, belonging to the debtor, until his debt due is paid. Lien, however, does not give right to sell unless such right is expressly conferred by statue or by custom or usage. The right of lien may be Particular and General.

***Right of Set-off*:** The right of set-off is a statutory right which enables a debtor to take into account a debt owed to him by a creditor, before the latter could recover the debt due to him from the debtor. In other words, the mutual claims of debtor and creditor are adjusted together and only the remainder amount is payable by the debtor. A banker, like other debtors, possesses this right of set-off which enables him to combine two accounts in the name of the same customer and to adjust the debit balance in one account with the credit balance in the other. This right of set-off can be exercised by the banker if there is no agreement - express or implied contrary to this right and after a notice is served on the customer intimating the latter about the former's intention to exercise the right of set-off. To be on the safer side the banker takes a letter of set-off from the customer authorizing the banker to exercise the right of set-off without giving him any notice.
Saving A/C = 250,000
Cash credit = -300,000

Conditions Necessary for Exercising the Right of Set-off:

- The accounts must be in the same name and in the same right.
- By giving notice to customer of banker's intention to combine accounts.
- The right can be exercised in respect of debts due and not in respect of future debts or contingent debts.
- The amount of debts must be certain.
- If there is letter of set-off given by customer.
- The right may be exercised in the absence of an agreement to the contrary.

- The banker has the right to exercise this right before the Garnishee order is made effective.

Conditions under which the Right cannot be exercised:

- If the accounts are not in the same right.
- The right of set off cannot be extended to a future contingent debt e.g. a bill which will mature in future.
- If the amounts of debts are uncertain.
- Trust account in which personal account of the customer cannot be combined.
- The account balance of an individual cannot be set-off against a joint account balance in which he is one of the account holders.

***Right of Appropriation*:** In case of several debts outstanding by the debtor (customer) to the bank, question arises as to which of the debts is to be discharged when payment is made by the debtor and the amount is not sufficient to discharge all the debts. The general rule in such a case is that the debtor has first choice and can appropriate the payment to any debt he likes. If the debtor makes no instructions about appropriation the banker may make the appropriation of payment to any debt according to his discretion. Where, however the right of appropriation is not exercised either by the debtors or creditors, rules laid down in Claytons' case is applicable:

- Where the account goes into credit, the first credit into the account is extinguished by the first debit and so on and so forth.

- Where the account goes into debit, the first debit into the account is repaid by the first credit and so on and so forth.

Right to charge interest, incidental charges: As a creditor, a banker has the implied right to charge interest on the credit provide to the customer. The rate of interest is nowadays levied as per the directions of Bangladesh Bank. It is charged on half yearly or quarterly basis and generally compound interest is used. The interest is directly debited, i.e., charged to the customer's account and then the interest is calculated on the principal with interest. Interest may also be fixed by the banker and customer by mutual consent. It may not however be beyond he prescribed limits of Bangladesh Bank. Banks also charge incidental charges on the current accounts to meet the incidental expenses on such accounts.

Right not to produce books of accounts: According to the provisions of the Bankers Book Evidence Act, the banker need not produce the original books of accounts as evidence in the cases in which the banker is not a party. He can issue only an attested copy of the required portion of the account which can be utilized as evidence before the court. When the court is not satisfied with the certified copy, the court can summon the original books. But when a banker is a party to the suit, the court can force the banker to produce the original records in support of his claim.

Right to Close Accounts: Banker also enjoys the right to close his customer's account and discontinue operations. This process terminates the relationship between banker and customer.

This is done only in situations where the continuation of relationship seems unprofitable to the banker.

<u>Lien:</u> Generally lien refers an official order that allows someone to keep the property of a person who owes them money until it has been paid. More specifically, Lien means the right of the creditor to retain the goods and securities owned by the debtor until the debt due is paid. That is, a lien is an encumbrance on one person's property to secure a debt the property owner owes to another person.

It confers upon the creditor the right to retain the security of the debtor and not the right to sell it. Such right can be exercised by the creditor in respect of goods and securities entrusted to him by the debtor with the intention to be retained by him as security for a debt due from him (debtor).

According law "*A right given to another by the owner of property to secure a debt, or one created by law in favor of certain creditors.*"

So we say that a lien is a right of one person to retain property or goods which are in his possession, belonging to another person until the promise or the liability is discharged.

<u>Type of lien:</u> Lien may be either (a) a general lien or (b) a particular lien

General lien: A general lien is a right of one person to retain any property or goods which are in his possession belonging to another person until the promise or liability is discharged. It is a right to retain the property belonging to another for a general balance of account. General lien is applicable in respect of all amounts due from the debtor to the creditor. That is, general lien will entitle a person in possession of the goods to retain them until all claims of account arising out of the general dealing between the two parties are satisfied. A banker has a general lien on all securities deposited with him by a customer unless there is an express contract, or unless there are circumstances showing an implied contract inconsistent with the lien. General lien gives right to retain any goods belonging to another person for any amount due from him. For example, A has two accounts in a bank. In savings bank account, he has a credit balance of Rs. 500. In current account, he has an overdraft of Rs. 1,000. Bank can exercise right of lien on the savings account for the amount due on the current account. It should be noted that right of lien will not apply to properties deposited for safe custody or for a specific purpose.

Particular lien: A particular lien confers a right to retain the goods in respect of a particular debt involved in connection with a particular transaction. A particular lien is attached to some specific goods. That is, particular lien gives right to retain only such goods in respect of which charges due remain unpaid. Particular lien is enjoyed by craftsmen like tailors, goldsmiths and bailees like repairers and public carriers. For example, a tailor has the right to retain the clothes made by him for his customer until his tailoring charges are paid by the customer or goldsmith can retain the jewelry till the making charges are paid.

Following condition must be fulfilled for applying the right of general lien:

- The property has come into the procession of the banker in his capacity as banker.
- The property has not been entrusted for a special purpose which is inconsistent with the lien.
- The banker should have lawfully obtained the possession of the property.
- There is no agreement contrary to the lien.