

Unit – III

Chapter - IV

Opening & Closing of Bank Accounts

Objectives

- To understand the procedure for opening of various bank accounts
- To know about the formalities to be complied for opening a bank account
- To know the circumstances under which a bank account is to be closed

1. Opening of a Bank Account

1.1 *Opening Savings Bank Account*- Normally, a banker will not open an account in favour of a stranger. Any person who wishes to open a savings account has to be introduced by another savings account holder of the same branch. Even a minor is allowed to open a saving account.

1.2 *Opening Current Account* - In the case of current account, it cannot be opened by any person unless he is introduced by another current account holder of the branch. The current account holder has to give a letter of introduction in favour of the person intending to open the current account.

Current account can also be opened when the employee of the bank gives a letter of introduction about the person intending to open the current account. A third type of letter of introduction can be given by a well reputed person known to the banker.

The contents of letter of introduction must spell out the conduct and character of the person intending to open the current account. It is more of a fidelity guarantee vouchsafing the character of the person, willing to open the current account. The banker requires such a letter as the current account holder is not only providing with overdraft and cash credit facility but also acceptance of third party cheques through endorsement.

At present the bank insists not only the introduction but also the photographs in duplicate of persons intending to open an account; one photograph is affixed in the pass book and the other in the ledger.

1.3 Opening Fixed Deposit Account and Recurring Deposit – For opening a fixed deposit account, the banker does not impose any condition. But he normally accepts fixed deposits from known persons and the fixed deposit account is opened only by deposit cash or in case of cheques only after realization of cheques. The same rule applies for recurring deposit also.

2. STEPS IN OPENING ACCOUNTS

Following are the steps involved in the opening of an account for customer, by a banker:

2.1 Obtaining Letter of Introduction

The first and the foremost step in opening an account for a new customer is to obtain a letter of introduction from the person who wants to open an account. A letter obtained by a banker from a prospective customer before a banker can open an account in the name of the prospective customer is known as 'letter of introduction'. The purpose of obtaining this type of a letter enables the banker to ascertain the genuineness of applicant. The letter serves as a letter of guarantee of conduct and genuineness of the applicant obtaining a letter of introduction is an important duty of a modern banker. The information obtained so helps the banker in confidently providing various services of banking and financial services. The information is also need to obtain protection from the provisions of the various legislations that are in force from time to time as part of carrying out the banking business.

2.1.1 Benefits/purposes:

Obtaining a proper letter of introduction is beneficial for the banker to know more about the new customer in the following manner:

- Protecting against issuing cheque books to unscrupulous persons.
- Facilitating the claiming of overdraft inadvertently granted by the banker.
- Protecting against undischarged insolvent.
- Helping to provide correct financial information about the customer.
- Obtaining statutory protection.

2.2 Application Form

After obtaining a letter of introduction, the banker supplies an application form according to the type of account, which the customer wants to open. The application form contains the rules and regulations of the bank with the terms and conditions of deposit. The application form is to be filled in and handed over to the banker. The applicant furnishes all details about himself including the name, nomination, address, etc.,.

2.3 Specimen Signature

After the application form duly filled in, the banker obtains the specimen signature of the new customer in a separate card called 'specimen signature' card. Every customer is expected to have read the rules of business of the bank to confirm in writing his willingness to comply with and bound by them before his account is opened. He is required to supply his bankers with one or more specimens of his signature and the bank usually enters these in a signature card maintained for the purpose. The cards are filed and arranged in an alphabetical order. Each customer's name must be written in bold characters above his account in the ledger. His address and occupation are also noted.

2.4 First Transaction

After obtaining the specimen signature of the new customer, the banker opens the new account by obtaining cash from the new customer. This marks the first transaction between the new customer and the banker. The relationship between the banker and customer begins after this transaction.

2.5 Issue of Cheque, Pay-in –slip, and Passbook

The banker issues pay-in-slips, cheque book, and passbook immediately after successfully completing the first transaction with the customer. The cheque book supplied to the customer usually contains ten or twenty blank forms. These leaves are used for making payments. A cheque book contains a requisition slip which helps to get a new cheque book.

Pay-in-slip or credit voucher are forms used to pay coins, notes, bills, and cheques to the credit of customer's account. Each slip should be signed by the customer or the person who has

prepared it on his behalf. For correct accounting, name, account number, date, and the amount of the customer should be clearly mentioned. Customer will receive a duplicate slip or counterfoil with a signature and the rubber stamp of the banker. It is an acknowledgement to the customer that cash, etc., have been duly received. The initials of the cashier in counterfoil do not in any way mean that the cheques, etc., are in order.

2.6 PAY-IN-SLIP BOOK

The pay-in-slip book is a book that contains printed slips with perforated counterfoils to be filled in by the depositor or his agent at the time of depositing cash, cheques, drafts, etc., to the credit of his account. Usually every bank prescribes and supplies free of cost separate pay-in-slips for depositing cash and cheques and drafts. The contents of pay-in-slips include the information regarding the date of deposit, name and account number of the customer, amount to be deposited, etc.

2.7 'DONATIO MORTIS CAUSA'

'Donatio mortis causa' means a gift made in contemplation of death. The gift is said to be made by a person who owns any movable property and who is very ill and believes that he is going to die. This is a peculiar gift as it has a condition that it will come into operation if only the donor actually dies of the illness. But if he recovers from the illness, the gift is to be returned.

2.8 PRINTED CHEQUE FORMS- MERITS

A cheque drawn on any paper is legally valid. In England, banks honor cheques even if they are not drawn on forms supplied by them. However, when the customer draws a cheque on ordinary slip of paper, the banker must be careful to see that it is an unconditional order. Otherwise the banker would lose the statutory protection. But it is to be noted that using plain papers to write cheques will prove risky for the paying banker. Hence, bankers always insist on using printed cheque forms to enable customers to derive the following advantages:

1. Easy and convenience of writing a cheque, only the relevant columns need to be filled in.
2. Avoidance of forgery and hence safety to banker and customer too.
3. Easy detection of fraud in a printed form is possible.
4. Ensure that the signature is drawn only according to the requirements of law.

5. Facility of verifying the customer's name by referring to chequebook issue record.
6. Easy countermanding of cheques by the customer; it is enough if the customer instructs to countermand the cheque number to the banker in case of fraud.
7. Counterfoils kept by the customer can be used as a record of payment made.
8. Popularity of name of the company or the individual where the names are printed on the cheque.

3. CUSTOMER IDENTIFICATION AND KYC NORMS

3.1 Meaning

The term KYC for 'Know Your Customer'. KYC is used for identifying a customer of banking and a financial service company such as a Mutual Fund, Pension Fund, etc. KYC essentially involves making reasonable efforts to determine true identity and beneficial ownership of accounts, source of funds, the nature of customer's business etc.

The objective of KYC is to help the banks and financial institutions to manage their risks prudently. KYC is made available by the RBI by way of guidelines designed to prevent banks from being used, intentionally or unintentionally by criminal elements for money laundering. There are two important components of KYC, viz., Identity and Address. While identity remains the same, the address may change and hence the banks are required to periodically update their records.

3.2 Legal Compliance

KYC norms have legal backing of the RBI. RBI has issued guidelines to banks under Section Regulation Act, 1949 and Rule 7 of Prevention of Money – Laundering (Maintenance of Records of the Nature and Value of Transactions, Time for Furnishing Information and Verification and Maintenance of records of the Identity of the Clients of Banking Companies, Financial Institutions and Intermediaries) Rules, 2005. Any contravention thereof non-compliance will attract penalties under Banking Regulation Act.

3.3 Applicability

KYC norms are applicable to a bank customer. For this purpose, a customer includes the following:

- A person or entity that maintains an account and/ or has a business relationship with the bank.
- One on whose behalf the account is maintained i.e., the beneficial owner.
- Beneficiaries of transactions conducted by professional intermediaries such as Stock Brokers, Chartered Accountants, Solicitors etc as permitted under the law.
- Any person or entity connected with a financial transaction which can pose significant reputational or other risks to the bank, say, wire transfer or issue of a high value demand draft as a single transactions.

In certain cases such as ‘ no frill accounts’, which are meant providing basic banking facilities to poor and promote financial inclusion, KYC norms are rather relaxed by banks.

3.4 Customer Identification

Customer identification involves identifying the customer and verifying the identity by using reliable, independent source documents, data or information. Banks have been advised by the RBI to lay down Customer Identification Procedure to be carried out different stages i.e., while establishing a banking relationship; carrying out a financial transaction or when the bank has a doubt about the authenticity/veracity or the adequacy of the previously obtained customers, KYC details about a customer are required to be updated periodically by the banker.

Banks create a customer profile with details on social/ financial status, nature of business activity, information about his clients’ business and their location, the purpose and reason for opening the account, the expected origin of the funds to be used within the relationship and details of occupation/employment, sources of wealth or income, expected monthly withdrawals etc. In the event of the transactions in the account are bring consistent with the customer profile already created, bank may ask for is any additional details/ documents as required. The ultimate objectives is to ensure that the account is not being used for any Money Laundering / Terrorist/ Criminal activities.

3.5 KYC Documents for Normal Customers

There are two aspects of Customer Identification- One is establishing identity and the other is establishing present residential address. For establishing identity, the bank requires any authentic document carrying photo of the customer such as driving license/ passport/pan card/ voter' card etc. Though these documents carry the residential address of the customer, it may not be the present address. Therefore, in order to establish the present address of the customer , in addition to passport/driving license/voter's card / pan card; the bank may ask for utility bills such as Telephone/Electricity bill etc.

A Banker would ask for the following list of documents to establish the proof of identity and residence of a customer.

3.5.1 For Individuals

The Banker will ask for copies of any the documents such as Aadhar card, Passport, Pan Card, Voter's Identity Card, Driving License, Identity Card and a letter from a recognized public authority or public servant verifying the identity and residence of the customer to the satisfaction of the bank. This would help the bank to establish the genuineness of the legal name or any other used by customer. To verify the documents such as Telephone bills, bank account statement, letter from any recognized public authority, electricity bill, ration card and letter from employer (Subject to satisfaction of the bank).

3.5.2 For Companies

In the case of companies, the banker will ask for documents such as Certificate of Incorporation and the Memorandum of Association and the Articles of Association to verify the name of the company. Similarly, banks will look into the resolution of the Board of Directors to open an account and identification of those who have authority to operate the account to determine the principal place of business.

4. CLOSING OF BANK ACCOUNTS

4.1 INTRODUCTION

Similar to the opening of account, banker has to adopt certain procedures while closing of account of a customer. At the time of closing an account, the banker should ask the customer to surrender the unused cheque along with the passbook.

When a customer expresses his willingness to close the account in writing, the banker should settle his account. Before doing so, the banker has to arrive at the closing balance which maybe to the credit or debit of the customer. When the balance is to the credit of the customer, the banker to pay the amount either in person or send the same by a cheque to the address of customer.

In case of undesirable customer, banker will give notice to the customer for closing the account. If the customer evades the request of the banker, a date will be fixed by the banker to close the account. This will be informed to the customer. On that particular day, the bank will close the account of the undesirable customer and send the credit balance to the address of the customer.

A bank will close the account of the customer under the following conditions

- (1) Death of customer
- (2) Insolvency of the customer
- (3) When customer becomes insane
- (4) Garnishee order
- (5) With drawl of power attorney
- (6) When the partnership firm is dissolved
- (7) In case of company, on winding up
- (8) When the customer assigns his entire credit balance
- (9) In the case of associations and institutions, on the passing of resolution as per the Bye-laws.

4.1.1 DEATH OF A CUSTOMER

When a customer dies, the contractual relationship stands terminated and operations in the account should be stopped as soon as the banker receives the notice of death. The banker should also obtain a copy of the death certificate.

If the customer has left a will, the will has to be probated by a court and the amount should be paid to the executor, or administrator of the will. In the absence of a will, the legal heirs have to obtain a Succession Certificate. In that case, he should be satisfied through discreet enquiries that the customer died in state and that the legal heirs are not required to obtain a Succession Certificate for the disposal of other assets left by him. However, the legal heirs would have to execute a stamped indemnity form along with two sureties each good for the amount involved. The legal heirs are also required to submit affidavit from an independent person, indicating their heir-ship or submit an heir-ship certificates.

4.1.2 Insolvency of Customer

When a customer is adjusted insolvent by the court, an assignee will be appointed by the court. The account of the customer in the bank will not be operated by the official assignee appointed by the court. Thus, the account of the customer stands closed and the customer cannot operate the same.

4.1.3 When the customer becomes insane:

When the customer is of unsound mind, the account cannot be operated. As soon as the banker comes to know that the customer is of unsound mind, a doctor will be asked to judge the nature of unsound mind. If it is of permanent nature, the bank will have to close the account of the customer. But if the unsound mind is of a temporary nature, the account will be suspended till such time the customer becomes normal. It is on the basis of medical report, the banker will take a decision.

4.1.4 Garnishee Order:

On the receipt of order from the court, the banker has to close the account of the customer. Such an order is called **Garnishee Order**. This order is of two parts. First, the court

will ask the banker about the status of the account which is called Order Nisi. After receiving the explanation from the bank when court sends an absolute order, it is called Order Absolute. Thereupon, the account will be closed. The court orders the closure of the account when creditors of the customer convince the court that in spite of sufficient funds at his disposal, the customer is unwilling to settle their claims.

4.1.5 Withdrawal of Power of Attorney:

When the customer gives permission to another person to operate his account during the absence of the customer, such an account is called Power of attorney account. When the customer withdraws such a power, the agent who was allowed to operate can no longer operate the account.

4.1.6 Dissolution of Firm:

When a partnership firm has an account in a bank, it is operated as long as the firm remains in operation. A firm gets dissolved due to the death, insolvency, insane, etc., of any partner or all the partners. The partners may also agree to dissolve the firm. In all the above cases, the account of the firm stands closed.

4.1.7 Winding up of Company:

A company's account will be operated as long as it is in operation. Once the company's winding up process commences, the account will be operated by liquidator. The company's account stands closed.

4.1.8 Assignment of credit balance:

When a customer informs the banker to assign his entire credit balance to third party, the account of the customer gets closed.

5. Closing of Account of Associations and Institution:

The accounts of association, institutions with the bank are operated as per their bye-laws. When they pass a resolution to close the account with the bank, it will be closed as per the provisions provided in their bylaws.

CONCLUSION

The latest legal formalities and practices followed by a modern banker and the other guidelines necessary for opening various bank accounts have been enumerated. The details of KYC norms to be followed for opening bank accounts are given. We have also studied the circumstances for closure of a bank account.

EXERCISES

Short Answers Questions

1. What is letter of introduction?
2. What do you mean by specimen signature?
3. Explain Donatio Mortis Causa.
4. What is KYC?
5. What is garnishee order?

Big Answers Questions

1. Give the procedure for opening a bank account.
2. Bring out the significance of KYC (Know Your Customer) norms to a banker.
3. What are the merits of printed cheques forms?
4. Explain the circumstances under which a bank account is to closed.