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PART VI

Bills introduced into the Council of the Governor General of India and Bills published before introduction in that Council

COMMERCE AND LABOUR DEPARTMENT.

NOTIFICATION

The 2nd January 1945

No. 1-Com.—The following Notes on Clauses of the Banking Companies Bill is republished for general information.

By order of the Governor
J. E. MAHER
Secretary to Government

THE BANKING COMPANIES BILL

(Published in the Gazette of India, Part V, dated the 18th November 1944, and in the Orissa Gazette, Part VI, dated the 15th December 1944

NOTES ON CLAUSES

Clause 1(1)—The Bill is confined to companies carrying on the business of banking. It would be impracticable to include within its scope all institutions and individuals dealing in credit in view of the complex credit structure of the country and the fact that moneylending is an item of provincial legislation.

Clause 2—Except in matters pertaining to banking it is desirable that the Indian Companies Act should continue to be applicable to banking companies.

Clause 3—It is unnecessary to include co-operative banks, which are governed by special legislation.

Clause 4—The object underlying this clause is that in cases of genuine emergency, e.g., a general run on all banks or a run on some bank in a particular area, Government should have power to suspend the operation of the Act after considering the recommendations of the Reserve Bank. The suspension of clause 18 will, for instance, enable the Reserve Bank to give an advance to tide over a banking crisis against liquid assets maintained by banks under that clause.

Clause 5(b)—The present definition of banking in section 277F of the Indian Companies Act gives rise to administrative difficulties, particularly in respect of the words "principal business" in determining whether a company comes within its scope. The new definition is intended to connect banking definitely with the acceptance of demand deposits and to confine the scope of the legislation to those institutions in which funds are deposited primarily to ensure their safety and ready withdrawability. It has the further advantage that it automatically excludes non-banking companies which accept only time deposits or borrow money at call.

Clause 6—Based on sections 277F and 277G(2) of the Indian Companies Act, 1913.

Clause 7—Sub-clause (1) is considered necessary for the protection of the interests of the depositors while sub-clause (2) merely follows the existing proviso to section 277F of the Indian Companies Act, 1913.

Clause 8—This is intended to prohibit a bank from engaging directly or indirectly in trading activities and undertaking trading risks in addition to ordinary banking risks. Certain banks have been found to engage in such activities under the guise of agency business.

Clause 9—It is not intended to prohibit a bank from conducting the management of industrial concerns which it may have acquired in satisfaction of its claims or from taking any other steps necessary in the interests of the bank. The period prescribed should be sufficient for the disposal of such non-banking assets.

Clause 10—This embodies the new section 277HH added to the Indian Companies Act, 1913, by the Indian Companies (Amendment) Act, 1944, supplemented by a provision disallowing the employment of managing agents under some other name, or on a salary disproportionate to the resources of the bank.

Clause 11—One of the chief defects of the Indian banking system is the weak and vulnerable capital structure of the vast majority of banks, as evidenced by the fact that during the years 1934—43, no less than 669 banking companies were liquidated or wound up, most of which possessed very poor capital resources. Even the minimum of Rs. 50,000 prescribed by the Indian Companies Act for banks incorporated after the 15th January 1937 is low as compared with many other countries, notwithstanding the lower standard of wealth in India. Another defect in the present banking system is the undue concentration of banking offices in a few cities and towns whereas a very large number of small towns have no banking facilities. Small banks with low capital have also a tendency to open branches in larger towns which have already sufficient banking facilities. Clause 11(1) seeks to remedy these defects.

In the case of banking companies incorporated outside British India, the provisions as regards capital do not afford any real protection; hence the safeguarding provisions of sub-clause (2).

Sub-clause (3) follows the recently enacted section 277I(2) of the Indian Companies Act.

Clause 12—This reproduces section 277J of the Indian Companies Act.

Clause 13—This embodies sub-sections (1) and (2) of section 277K of the Indian Companies Act. Sub-section (3) of that section has been omitted in view of clause 18 of the Bill which provides for a general reserve.

Clause 14—This follows section 277L(1) of the Indian Companies Act except that the prescribed returns are to be filled with the Reserve Bank and not the Registrar.

Sub-section (2) of section 277L, which defines the terms "demand liabilities" and "time liabilities", has been removed to clause 5 of the Bill.

Clause 15—The clause is more or less identical with section 277M of the Indian Companies Act. The words "issued and subscribed share capital" however have been substituted for the words "issued share capital" as the latter term is somewhat confusing and is used indiscriminately.

Clause 16—Past failures of several banks in India have been due mostly to indiscriminate advances to directors or their concerns. An absolute and unqualified ban on such transactions would, however, result in depriving the banks of the advantage of having on their directorate important and experienced industrial magnates. A check is therefore prescribed on advances to directors and their concerns.

Clause 17—When the Reserve Bank's original "Proposals for an Indian Bank Act" were circulated by Government in 1940, suggestions were received that a system of licensing foreign banks doing business in British India should be introduced. The Banking Enquiry Committee had also recommended that banks should be required to take out licenses from the Reserve Bank, such licenses being granted freely to the existing banks. Clause 17 provides for the licensing of foreign banks intending to open branches in India on the basis of reciprocal treatment of Indian nationals and companies in the foreign countries concerned.

Clause 18—This clause is an attempt to prescribe by law what has already been recognised as some banking practice, viz., that a bank should keep a reserve of cash and liquid assets to meet its demand liabilities. One of the worst defects of Indian banking is the propensity of the smaller banks to overtrade at the expense of liquidity and it seems best to insist on all banks maintaining a reasonably large proportion of their cover in the form of cash or trustee securities as defined in the Indian Trusts Act, excluding immovable property. The proportion of 25 per cent is in accordance with the actual practice followed by smaller banks.

Clause 19—The failure of a bank incorporated in an Indian State, which had the bulk of its deposits from British India but the greater part of its assets in Indian States, has brought out the necessity of protecting the interests of British Indian depositors by requiring such banks to maintain a reasonable proportion of their British India liability in the form of assets in British India. Export bills are included in such assets with a view to helping Indian exports.

Clause 20—The existing return under section 42 of the Reserve Bank Act applies only to scheduled banks and also omits important details like investments. For an adequate control of banking development, it is necessary that the Reserve Bank should have a full picture of the banking situation of the country through periodical returns of assets and liabilities.

Clause 21—The intention in prescribing an annual return of deposits which remain unclaimed for 10 years is to enable the Reserve Bank to have the necessary data for consideration of the question whether deposits remaining unclaimed for a prescribed period should be transferred to Government making it responsible for meeting any claim which may be established in future. Similar returns are called for, in the banking legislation of Canada, and it is provided there that after the lapse of a certain period of years the deposits will be paid over to Government.

Clause 22—The Form F laid down by the Companies Act is meant for companies in general and is not suited to the special requirements of banking companies. Many of the smaller banks publish their balance-sheets in different forms and there is no uniformity of presentation. The banks also colse their books on different dates making it difficult to have a picture of the banking situation of the country as on a particular date. The Central Banking Inquiry Committee, which considered this question in detail, recommended a separate form for banking companies. As regards banks incorporated outside British India, there is no provision in the Companies Act for the publication of separate balance-sheets of their Indian business. In Forms A and B of the Schedule to the Banking Companies Bill, an attempt has been made to provide a form of balance-sheet and profit and loss account specially suitable for banking companies.

Clause 23—This provides for the audit of the statements prescribed under clause 22.

Clause 24—At present, some of the banks publish their balance-sheets after a considerable period from the date to which they relate so that the position of the banks remains unknown for an unduly long period. The clause remedies this defect.

Clause 25—This follows section 17 of the Insurance Act, 1938.

Clause 26—There is no provision in the Indian Companies Act for the publication of balance-sheets by banking companies incorporated outside British India similar to that contained in section 136 applicable to companies incorporated in British India. This clause provides for uniformity of treatment as regards the publication of balance-sheets.

Clause 27—This provides for the period of transition and follows section 17A of the Insurance Act, 1938.

Clause 28—The opinions received on the Reserve Bank's "Proposals for an Indian Bank Act" circulated in 1940 revealed that public opinion was generally in favour of the inspection of banks by Government or the Reserve Bank. In view of this and in the light of the experience gained by the Reserve Bank in connection with the inspection of banks for the purposes of section 42(6) of the Reserve Bank Act, and in view of possible post-war developments, provisions have been made for the inspection, in certain circumstances, of a bank's book by the Reserve Bank at the instance of the Central Government. A regular system of inspection of all banks does not seem practicable and provision has therefore been made for inspection only where necessary in the interests of depositors. Sub-clause (1) generally follows the lines of section 33(1) of the Insurance Act, and sub-clauses (2) and (3) enumerate the various corrective measures which the Central Government may take.

Clause 30—This clause is a modification of section 277N of the Indian Companies Act, the period of moratorium having been limited to three months. It is the intention that the report under sub-clause (2) should be submitted by the Reserve Bank.

Clause 31—The provisions of the Indian Companies Act in respect of liquidation do not seem to be suitable for banking companies. A bank's business is conducted on an over-the-counter basis and it is important that current accounts should be withdrawable at any time and drafts, etc., should be honoured on presentation; otherwise great business dislocation is likely to result. A provision has, therefore, been made under this clause for the winding up of a banking company if it refuses to meet a lawful demand for payment at one of its offices or branches within two working days, if such demand is made at a place where there is an office or branch or agency of the Reserve Bank, or within four working days, elsewhere. The clause also authorises the Reserve Bank to apply for the liquidation of a banking company if it appears from the results of an inspection made under clause 28 that its affairs are being conducted to the detriment of the interests of its depositors.

Clause 32—Experience has shown that the cost of liquidation proceedings under the Indian Companies Act is high. It has, therefore, been provided in this clause that the Reserve Bank should be empowered to carry out liquidations so that unnecessary expense and delay in liquidation proceedings may be avoided, and that the assets may be realised as speedily and cheaply as possible in the interests of the creditors.

Clause 33—This limits the power of the Court to stay proceedings to cases in which it is satisfied that the depositors can be paid in full.

Clause 34—The period prescribed under section 177B of the Indian Companies Act for the submission of a preliminary report by the official liquidator is too long in the case of a banking company and the clause is intended to remedy this defect.

Clause 35—In the case of a banking company, rapidity in liquidation is essential if the assets are not to grow cold or to be dissipated. The provisions for calling meetings of creditors to discuss arrangements or to appoint an advisory committee to work with the official liquidator should, therefore, be rescinded in the case of banking companies unless the Court considers that this should be done.

Clause 36—This simplifies the formalities for depositors proving their debts.

Clause 37—It has been found that banking companies in a shaky condition take advantage of the voluntary winding up proceedings under the cover of a merger, or manipulate such proceedings to the disadvantage of the depositors who are a scattered body and are unlikely to take concerted action. The clause is intended to prevent such abuses.

Clause 38—This empowers the Central Government to make regulations under the Act after consultation with the Reserve Bank.

Clause 39—This is a consequential amendment.

Clause 40—Repeals.

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