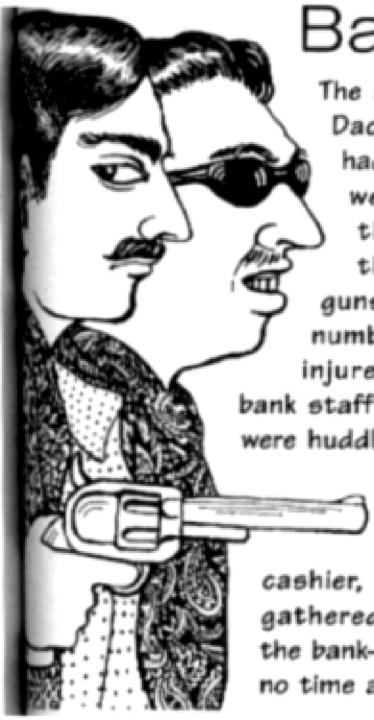
CHAPTER 6

BANKS

> *You must already know something about banks. Write a paragraph on how people use banks.*

A Robbery at the Bank



The bank had been robbed! Dacoits armed with guns had raided the bank. There were six or seven of them, so even though the guards also had guns, they were outnumbered. One guard was injured in the attack. The bank staff and some customers were huddled into a room with a pistol pointed at them. Meanwhile, threatening to kill the cashier, the dacoits hurriedly gathered all the money from the bank-safe. It was all over in no time and they fled in a jeep.

Hearing news of this daylight robbery at the bank, many people grew worried and distraught. After all, so much of their money was deposited in the bank! One had fifty thousand rupees - another, two lakh. Many others had savings of four to five thousand rupees.

Some of them thought that they would never get their money back now. They were under the impression that all the money they had deposited was stored in the bank's safe, and now it was gone. As news of the robbery spread in the small town, people started gathering at the bank. They were discussing how they had lost all their money.

Others disagreed, saying it was the bank's responsibility. They demanded their money back. They wanted to meet the manager but she was busy with the police officials who had come there to investigate. Mohan Kumar was one of the people in the crowd. He had Rs. 50,000 in his bank account.

He *overheard* the manager asking the cashier, "How much cash (notes and coins) was taken?"

The cashier said that the safe had Rs. 1,00,000 in it. Mohan was puzzled. His account alone had Rs. 50,000, so how could the safe have only Rs. 1,00,000 in it? If the amounts in all the depositors' accounts were added up, it would be a huge sum. Yet there was only this much money in the bank-safe? What had happened to the rest?

What do banks do with people's money? How do banks function? This is what we'll discuss in this chapter.

Money Transactions

Anytime money changes hands from one person to another we say a **transaction** has occurred. Now we'll find out about different kinds of transactions that occur when people use banks: **deposits** (putting money in banks), **withdrawals** (taking money out of banks) etc.

Depositing Money in a Bank – Types of Bank Accounts

Teachers, shopkeepers, farmers, traders, officers, doctors, lawyers, schools, companies - all kinds of people and organisations open accounts in banks and deposit their money in them. People have different reasons for keeping their money in a bank.

Saving Accounts

Some people want to deposit money in a bank to safely save it for future needs. They do not need to withdraw money daily, only once in a while. For such people, banks have **Saving Accounts**.

People's money remains safe when it is deposited in a Saving Account. In addition, the bank pays them **interest** on their money – after a specified time, the bank will add a small percentage of money to the account. There are, however, some restrictions in this type of account. For instance, there is a rule that in a Saving Account, money cannot be withdrawn more than 50 times in half a year.

Current Accounts

Other people, like shopkeepers and traders, have daily earnings that they like to deposit in a bank to keep the money safe. They also frequently withdraw money according to their needs. This could be to buy goods, pay labourers, or whatever. Similarly, large business offices have a daily inflow of money from customers who purchase their goods and services, as well as a daily outflow of money to people who have supplied them with various things or who have done some work for them. For these kinds of commercial needs, banks have a type of account called a **Current Account**. Many organisations and business people use this kind of account. There are no restrictions on the number of times you can deposit or withdraw money from a Current Account. However, the bank does not pay any interest on money deposited in a Current Account. The bank may even charge some fees for using a Current Account.

Fixed Deposit Accounts

Sometimes people may decide that they do not need to use a certain amount of their money for many months or years. They just want to save it, without withdrawing any of it for a long time. They can deposit this money in a **Fixed Deposit Account** (also called a **Term Deposit Account**) for a specified period of time. After the specified number of months or years has passed, the bank pays them their original money plus a fixed amount of interest. For this type of account, the rate of interest paid is greater than for a Saving Account. The interest rate is higher for accounts that specify longer fixed periods of time for the deposit.

The interest paid by banks does change from time to time. There may also be some differences in the interest rates among different banks. Go to a bank and find out:

a) What is the rate of interest on a Saving Account?

b) What is the rate of interest for a 5 year Fixed Deposit?

c) If someone needs money urgently, how can they withdraw money from a Fixed Deposit Account?

What kind of account can be opened for the purpose of trade and business? What are the differences between this account and a Fixed Deposit Account?

Give three reasons why people may want to deposit their money in banks.

Withdrawals and Other Transactions

People can withdraw the money they have deposited in a bank on demand, i.e. whenever they choose to do so. This is because it is their money, which the banks are keeping as a deposit, so the banks must pay them whenever they want to withdraw it. However, there are certain rules and procedures to be followed. There are three common ways of withdrawing money from an account - through a withdrawal form, through a cheque, or (in some places) through an ATM (Automatic Teller Machine).

Using Withdrawal Forms and Passbooks

One day some money was needed at Rajinder's home. She thought, "I'll go and get some money from my Saving Account."

Her account was in the State Bank of India. On reaching the bank, she asked for a withdrawal form. She filled it up, as shown below:

अपराक्राम्य / Not Negotiable

भारतीय स्टेट बैंक
STATE BANK OF INDIA

________ शाखा / Branch

खाता धारक का (के) नाम
Name of the Account Holder(s) Rajinder Kaur

बचत खाते से पैसा निकालने का फॉर्म
SAVINGS BANK WITHDRAWAL FORM

तारीख / DATE 8/5 2003

सावधानी : यह बचत बैंक निकासी आदेश फार्म चेक नहीं है, इस फार्म के साथ पास-बुक रहना अनिवार्य है, अन्यथा भुगतान प्राप्त नहीं होगा ।
CARE : This form is not a cheque. Payment will be refused if the pass book is not produced with this form.

बही / खाता क्रमांक
Ledger/Account Number 523368481

आद्याक्षर / Initials

कृपया केवल मुझे / हमें अदा करें / PLEASE PAY SELF/OURSELVES ONLY

रुपये / Rupees one thousand and five hundred only

तथा राशि को मेरे / हमारे उपर्युक्त खाते में नाम करें /
AND DEBIT THE AMOUNT TO MY/OUR ABOVE SAVINGS BANK ACCOUNT

₹ / Rs. 1500/-

टोकन क्र. / Token No.

सारणी क्र. / Scroll No.

रोकड़ अदा करें / Pay Cash

पासकर्ता अधिकारी / Passing Officer

Rajinder Kaur

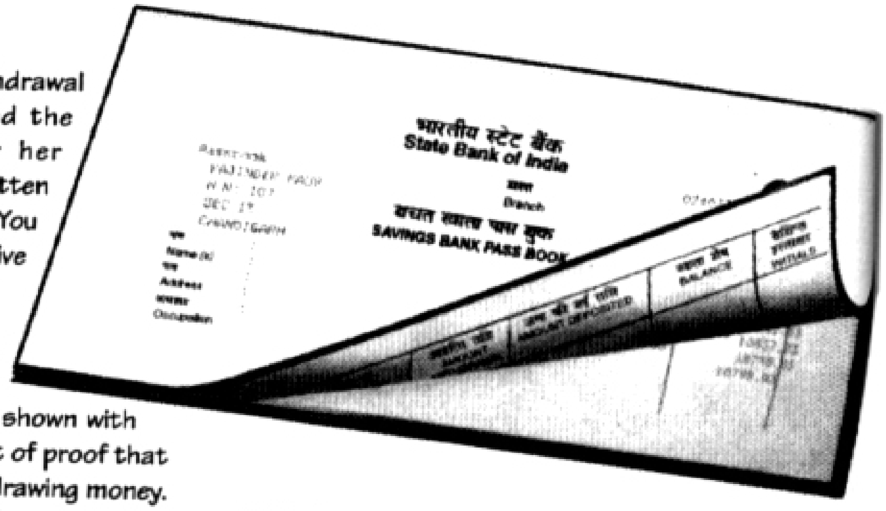
खाता धारक का (के) हस्ताक्षर
Signature(s) of the Account Holder(s)

लेजर / खाता क्रमांक / Ledger/Account No.

आर० एफ० 10/R.F. 10

Item Code No. 3010139

Y.P.20799/4½"x8¾"/20,000 Pads of 100 Lvs.



Rajinder handed the filled up withdrawal form to the clerk sitting behind the counter. The clerk asked for her passbook, but Rajinder had forgotten it at home. She said to the clerk, "You know me quite well. Why don't you give me the money?"

To which the clerk replied, "Oh, that is impossible. It is a rule of the bank that the passbook must be shown with the withdrawal form." This is a sort of proof that the genuine deposit-holder is withdrawing money. Even if you know someone personally, you have to follow the rules. You can read the rules on the withdrawal form.

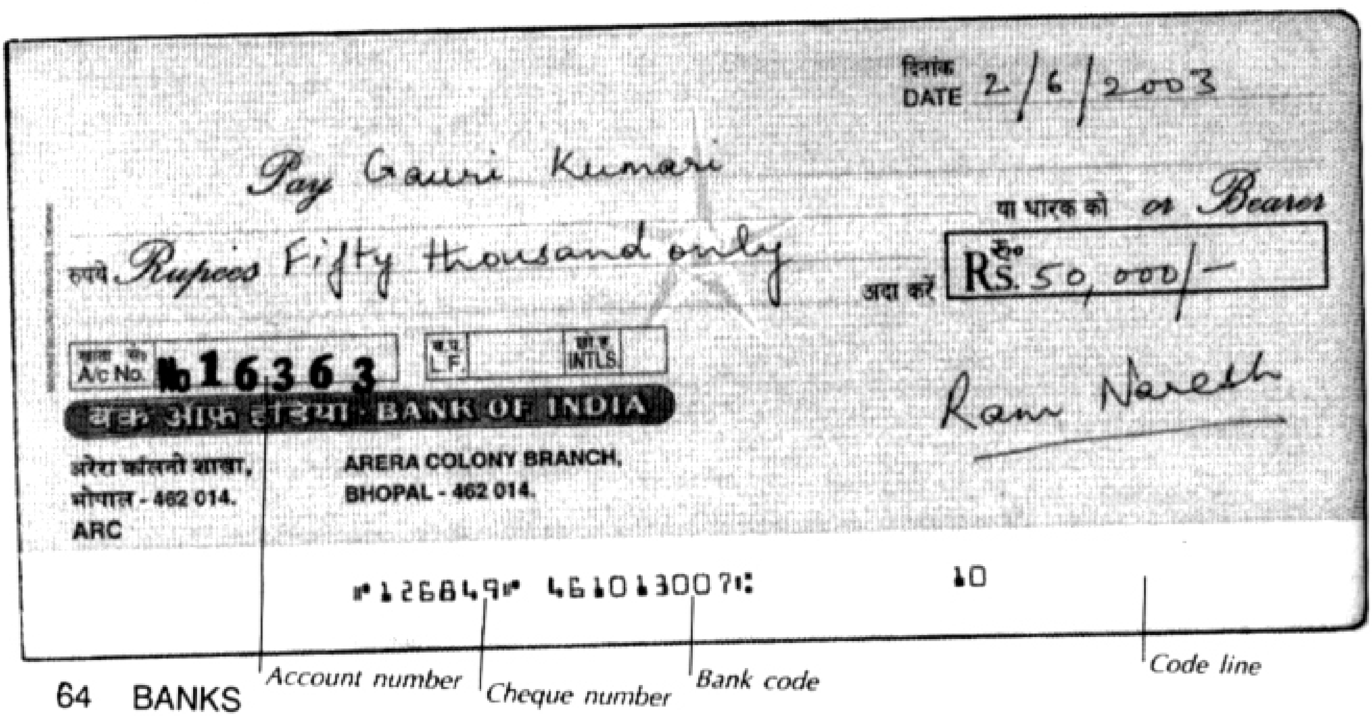
> *Discuss this incident with your classmates. Do you think the clerk was right to insist on following the rules? Why did the bank have this rule? Is it for the good of the bank or for the good of the account holder?*
>
> *What is a passbook and what is its use?*

Rajinder went home and came back with her passbook and was able to withdraw money. But standing next to her was a woman who was withdrawing her money without a passbook. Rajinder asked her, "How did you withdraw money without a passbook?"

Rajinder noticed that the woman was using a different kind of form. The woman said, "This is a cheque. With my kind of Saving Account, I get cheques. It isn't necessary to have the passbook with you if you use a cheque."

Cheques - a convenient way to exchange money

These days cheques are widely used for both making payments and receiving money. Not only can you withdraw money from your account with cheques, you can also give cheques to others. When you want to give money to someone, you can write a cheque with that person's name on it. When you want to send money to someone who lives in a different place, you can write a cheque and send



it by post. For business purposes, where money is frequently received and paid, the cheque is a very important medium for money transactions.

Look at this example of a transaction by cheque. Ram Naresh is a major trader of Bhopal and Gauri Kumari is the owner of a factory there. Ram Naresh has an account in the Bank of India, while Gauri Kumari's account is in the Punjab National Bank. Ram Naresh had to give Gauri Kumari Rs. 50,000. So he wrote out a cheque in her name.

On the cheque is written: "Pay Gauri Kumari or Bearer Rupees Fifty Thousand Only". The cheque reaches Gauri Kumari. She has two options.

If she wants the money in cash, she can go and encash the cheque by presenting it at Ram Naresh's bank (Bank of India, Arera Colony, Bhopal). The bank staff will check to be sure Ram Naresh's signature on the cheque matches the one they have in their record. They will also check to be sure there is enough money in Ram Naresh's account for the payment to be made. Then they will give Gauri Kumari the money in cash and will subtract Rs. 50,000 from Ram Naresh's account.

Gauri Kumari could do another thing instead. She could deposit the cheque in her own bank account. Then, her bank (that is, Punjab National Bank) will send the cheque to Ram Naresh's bank. His bank (Bank of India, Bhopal) will match the signature and check the account and then pay ('settle accounts with') Gauri Kumari's bank. Ram Naresh's bank will subtract Rs. 50,000 from his account while Gauri Kumari's bank will add Rs. 50,000 to her account.

Different people give cheques which each bank needs to collect from other banks. Now how do you think each bank will get money from the other banks? In many towns and cities, representatives of all the banks meet on each working day to settle what each bank has to pay and receive from all the others Each bank has an account in the Clearing Bank where they meet. All the banks then give or receive payments from each other (in the form of cheques from their accounts with the Clearing Bank). This is how banks clear cheques between themselves.

Thus, money transactions between people can take place without cash being exchanged.

In the beginning, there was Rs. 65,000 in Ram Naresh's account and Rs. 60,000 in Gauri Kumari's. After the cheque is deposited in the bank, how much money will there be in each account?

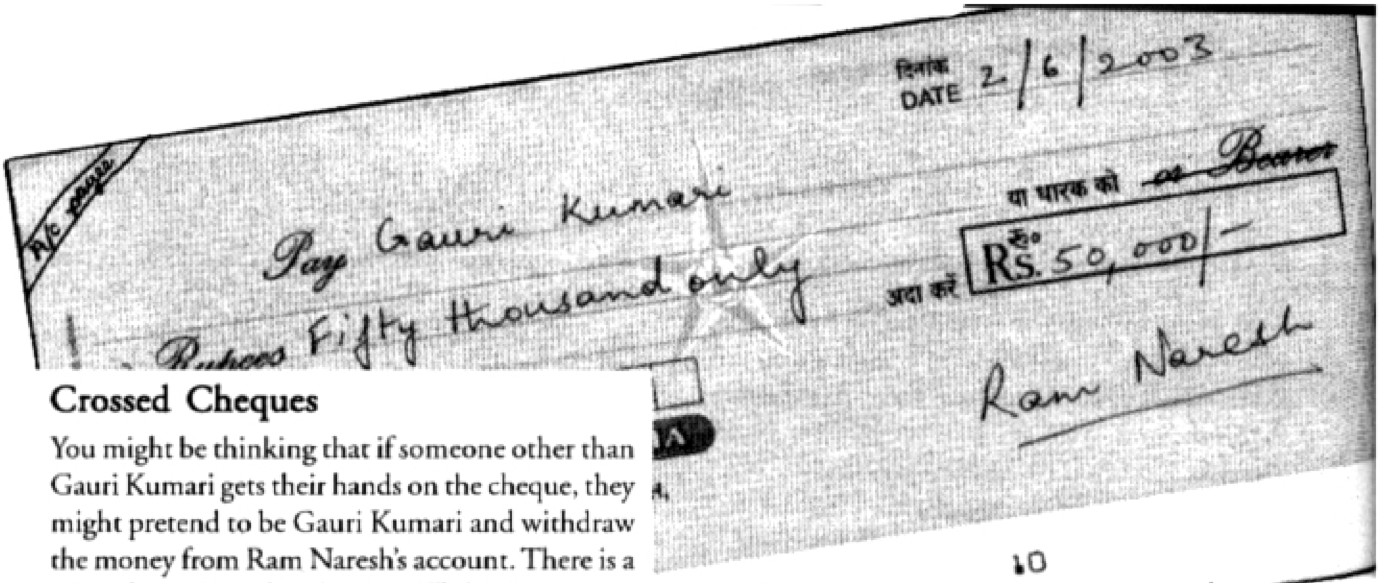
Explain how this transaction was done without actually handling cash.

Who checked Ram Naresh's signature on the cheque, and why did they check it?

Make a skit with your classmates to show how a Clearing Bank works.

Why is a passbook not necessary when you use a cheque to withdraw money?

If Gauri Kumari was in Dewas and not in Bhopal, she would adopt the second option. That is, she would deposit the cheque in her own bank account. In such a situation both the banks would have to correspond with each other to verify if the cheque should be accepted. After that, the same procedure is followed as above. However, the correspondence between two banks at different places takes place through post and therefore one has to wait for a number of days for the cheque to be cleared.



Crossed Cheques

You might be thinking that if someone other than Gauri Kumari gets their hands on the cheque, they might pretend to be Gauri Kumari and withdraw the money from Ram Naresh's account. There is a way of avoiding this danger. While writing out the cheque, Ram Naresh can delete the words 'or Bearer' and draw two lines in the top, left hand corner, as shown above. Such a cheque is called a **crossed cheque** or an **account payee cheque**. When a cheque is crossed, it cannot be directly exchanged for cash – it must be deposited in the account of the person in whose name it is written. Gauri Kumari can receive the money only by depositing the cheque in her own account.

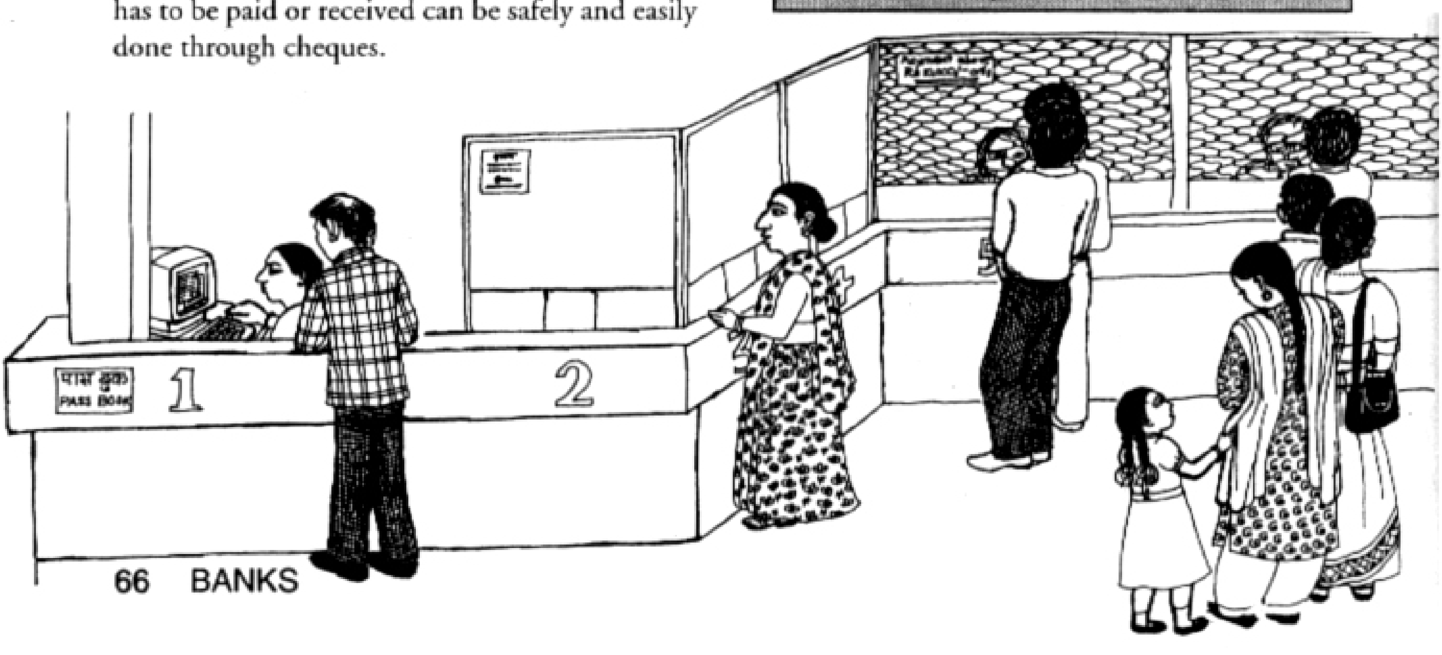
A crossed or account payee cheque is a good way to exchange money. By and large, transactions involving large sums of money take place only through crossed cheques. This way people can avoid the difficulty and danger involved in keeping or carrying bundles of notes.

This is one reason why it has become common for people to use banks. It is not necessary for people to keep their money in cash. It can remain as deposits in a bank account and whatever money has to be paid or received can be safely and easily done through cheques.

If someone stole the crossed cheque from Gauri Kumari, can they get the Rs. 50,000?

You have now heard about several ways of making payments and receiving money. Compare the convenience, safety and other advantages and disadvantages of making transactions with (1) cash, (2) bearer cheques, and (3) crossed cheques. For each of these three methods, give an example of a case where it would be the best way of making or receiving a payment.

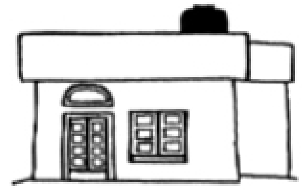
In last year's textbook, there was a skit about how money, in the form of coins, helped in a situation where barter deals were not possible. Do you remember it? Look at pages 139-141 of Social Studies, Class 7. *Suppose, in that situation, instead of coins there was a bank and all transactions took place through cheques. How would the problem be solved? Write a new ending to the skit in which transactions are done through a bank.*



Noting Transactions in an Account

Phool Singh's account is in the Timarni Branch of the State Bank of India. He is a farmer. He has sold soyabean to Chhagan Lal. Chhagan Lal has given him a cheque for Rs. 5,000. There was Rs. 7,000 in Phool Singh's account. After depositing Chhagan Lal's cheque there will be a balance of Rs. 12,000 in his account.

Given below is the table from Phool Singh's passbook. Copy it in your notebook. Fill the details in the table till the point where Chhagan Lal's cheque has been deposited.



Phool Singh's Passbook:

Sr. No.	Description	Money withdrawn	Money deposited	Balance
1	Money in Phool Singh's account			7,000
2	Cheque received from Chhagan Lal			
3				
4				
5				

Phool Singh was building a house. He needed to buy cement for the house. The cost of cement was Rs.8,000. He gave the cement stockist, Komal Gupta, a cheque for Rs.8,000. She deposited the cheque in her account.

There were labourers working on Phool Singh's house. He needed Rs.2,000 in cash to pay them. He withdrew this amount from the bank.

Fill in the details of the money paid by Phool Singh to Komal Gupta by cheque and the money withdrawn to pay the labourers, in the appropriate places in the passbook.

After each of these payments, how much money was there in Phool Singh's account? Fill the balance in the appropriate places in the table.

A BANK'S PROMISE

If a person has a deposit in a bank, then it is the duty of the bank to accept any demand for withdrawal of money in cash, or payments made by cheque. However there are many rules and procedures to be followed, especially to ensure that fraudulent methods are not used. At the same time, it is the account holder's responsibility to ensure that there is enough money in their account to cover the amount of whatever withdrawal is requested. For example, suppose you write a cheque for an amount that is more than the balance in your account. The cheque will **bounce** – it will be returned to you, and you may even be punished according to the rules agreed upon when you opened your account with the bank.

Electronic Banking

With the use of computers and electronic communication, many new ways of conducting money transactions are being devised. Some banks are fully computerised and do not use passbooks anymore. Instead, the bank gives a computer printout of the transactions and balance in the account whenever the account holder requests it.

Nowadays most cities and even some small towns have **Automatic Teller Machines (ATMs)**. These are machines that people can use to withdraw cash from their bank accounts, find out their balance, and, in some cases, also make deposits.

How do you withdraw money using an ATM? What advantages and disadvantages does it have compared to other ways of withdrawing money?

Instead of paying in cash or by cheque, some employers pay their workers by depositing money directly into their employees' bank accounts. Assuming that the employer and employee have accounts in the same bank, the employer has to just instruct the bank to transfer the correct amount to the employee's account.

Find out whether banks in your area are using computers, and if so, how computers have changed the way they operate. Are there any other recent changes besides the ones we have already mentioned?

You read about Clearing Banks, where representatives of different banks clear the cheques issued against each other. In the newer systems, representatives do not even have to meet. Transactions between one bank and another can be done through the banks' interconnected computers. This makes the whole system operate at a much faster speed than ever before. In our country this modernisation process has started and most banks are now computerised. We will witness rapid changes in banking in the years to come.

How do Banks Work?

You read about the bank robbery in the beginning of the chapter and how Mohan Kumar was puzzled that there was very little cash in the safe, compared to the total money of all the depositors. Like many people, he thought that all this money must be kept in the bank's safe. But it wasn't. So how do banks work?

Banks promise to pay cash to depositors on demand. But there are numerous account holders in a bank. It never happens that all the depositors turn up at the same time to withdraw all their money. Suppose there are 2000 account holders in a bank. On any given day 25 to 50 people might come to withdraw cash. Many people will withdraw money at the beginning of the month. If many of the depositors are farmers, then there will be a greater demand for cash during certain seasons. Every day only a limited number of people come to withdraw cash, and some also make deposits. With some experience, banks are able to estimate how much cash people will withdraw and how much they will deposit each day. The bank arranges to have the necessary amount of cash available.

Banks can fulfil their promises by keeping only a small fraction of their total deposits as cash. They can use the rest of the money that is deposited in their accounts for other purposes.

There is another reason why banks do not need to keep a large amount of money in cash. As you saw in this chapter, a great number of transactions take place through cheques. For these, cash may not be required at all. Each such transaction is simply recorded (as a deposit or withdrawal) in the written or electronic record of the account. Thus, the bank needs to keep very little money in the form of cash.

Why was there only Rs. 100,000 in the safe of the bank when Mohan Kumar went there?

Discuss: In case of a theft or robbery at a bank, it is the bank's responsibility to bear the loss. However, what would happen if all the people who had deposits in a bank felt insecure and decided to withdraw their money in cash all at the same time?

The banking system works on the assurance to the depositors that they can withdraw their money at any time, and that their money will not be lost. The following story illustrates how this principle might have begun in India.

How did Banking Begin?

Hundreds of years ago, people who wanted to borrow money (which was then usually in the form of gold or silver coins) would go to moneylenders, or shroffs. By lending, the shroffs could make a profit because they charged interest (i.e. the borrowers would have to pay back slightly more than what they had borrowed).

Some people started trusting the shroffs and giving them their gold for safekeeping. The shroffs gave them receipts that stated how much of their gold was lying with them. People found that this was a convenient system, and whenever they wanted they could get their gold from the shroff. They found that their gold was always safe and available on demand. The shroffs also gave the depositors some interest. The people's trust in the shroffs grew. So more and more people kept their gold with them.

The shroffs found that after some time they had accumulated lots of gold. This was because the amount of gold that people withdrew at any given time was relatively small. The shroffs found that they could easily lend some of this gold without risking a shortage. They would still be able to meet the demand of the depositors who wanted to withdraw their gold.

Suppose a trader had a receipt for a certain amount of his gold that was lying with a shroff. When he purchased goods from someone, rather than paying in gold, he might just give the receipt. The receipt would be accepted only if the shroff was trusted. Maybe this is how the system of paper bank notes began.

A shroff accepting a deposit from a customer (painted around 1760).

Why did people keep their gold with the shroffs?

How could the shroffs make use of these deposits, without getting into problems?

Would this system work if people had kept their special gold ornaments with the shroffs instead of bars or lumps of gold?

Loans

Many people save their money in bank accounts and in this way banks accumulate a lot of money. Banks then use this money to give loans. For some special lending schemes, the government also gives extra money to banks.

Some loans are given for trade and commerce. For example, loans may be given to someone who needs to buy machines, run a factory, set up a business, buy a truck or construct a building. Banks fulfil the needs for such loans and take interest according to their rules. One such example is as follows:

Narmada Soyabean Company wanted to set up one more factory to extract oil from soyabeans. Its manager drew up a loan plan for Rs.200 lakh (two crore) and submitted a proposal to the bank. The bank officials studied the loan plan and held discussions. They were convinced that the factory would be able to run successfully. The loan was sanctioned. The company had also invested Rs. 50 lakh from its own money. For its

security the bank mortgaged the machinery that was bought. This means that if for some reason the factory fails to run and the company doesn't get enough money to repay the loan, the bank can then sell the mortgaged machinery and recover the loan. An interest rate was fixed and a scheme was worked out as to how the loan would be repaid. It was decided that after the company's production of oil takes place, it will keep returning the loan in instalments.

Banks also give another kind of loan that is related to government schemes. The government wants agricultural production to be increased. Thus, banks give many kinds of loans for agriculture - for the purchase of fertilisers and seeds, for digging wells, buying an electric motor, purchasing cattle, tractors and threshers, for the improvement of agricultural land etc.

For example, Dhanna Lal and Badri Prasad had each given applications for loans. Dhanna Lal had 8 acres of land. He needed money for fertilisers and seeds at the time of sowing. So he took a loan of Rs. 10,000. He mortgaged his harvest as security. After selling the harvest Dhanna Lal will return the loan to the bank, along with interest.

Badri Prasad had 20 acres of land. He applied for a loan for a tube well. He had Rs. 10,000 and wanted a loan of Rs.45,000 from the bank. In this case, he mortgaged his land as security with the bank. He will return the money, plus interest in instalments, within 5 years. If he does not return the loan, the bank can sell his land and recover its money.

Both the applications were accepted and sanctioned. Thus, Badri Prasad was able to get his tube well dug and Dhanna Lal was able to sow his crop.

What types of loans do banks give?

Moneylenders also lend money. So what are the differences between moneylenders and banks?

Find out an actual example of a loan given by a bank. Discuss the following:

a) The purpose and amount of the loan

b) The kind of security kept, if any

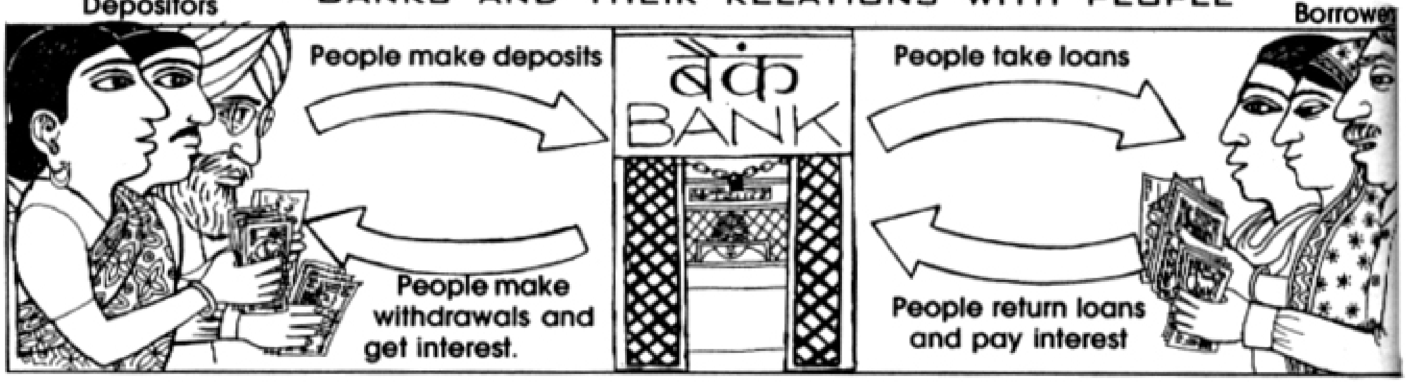
c) The manner in which the borrower has to repay the loan

d) How much the borrower will have to pay back in all

Functions of Banks

A bank has two major functions - to accept deposits into different types of accounts and to give loans to people who need them. This flow of money is shown in the diagram below. The borrowers return loans along with the interest. It is from this interest that the bank earns money needed for its work. The bank keeps depositors' money safe and pays cash whenever the depositors want. It also pays interest on saving / fixed deposit accounts. Besides this, there is a special feature of banks. Money transactions can be done from bank deposits without actually exchanging cash. This exchange of money is mainly done through cheques.

BANKS AND THEIR RELATIONS WITH PEOPLE



Exercises

1. Fill in the following table with as many examples of money transactions as you can:

Transactions involving Rupee notes and coins	Transactions that don't involve Rupee notes and coins

2. Can there be any difficulties or disadvantages in keeping money in a bank? Think and write.

3. Suppose you need Rs. 2000. You draw a cheque, give it to your sister and send her to get the money in cash. Draw the cheque in your note book. (Make it for an imaginary sister if you like.)

4. In what ways have cheques made exchange of money more convenient?

5. How is a crossed cheque safer than an ordinary cheque?

6. Only a part of the total deposits is kept as cash in the bank-safe. Why is this so and how does this benefit the bank?

7. If a very large number of account-holders do not wish to keep their money in the bank, how will it affect the bank's working?

8. If a great many loans are written off (that is, borrowers are not required to pay back the money), how will this affect the working of the bank?

9. People have to pay a higher interest on a loan than the interest they receive on a fixed deposit for the same time-period. Why do you think this is so?

10. Read the example of loans for agriculture again and answer the questions given below:
(a) If Dhanna Lal or Badri Prasad do not return the money they have borrowed, what can the bank do?
(b) The time periods given to Dhanna Lal and Badri Prasad to return the money are different. Why?
(c) Why does the government give loans like those given to Dhanna Lal and Badri Prasad?
(d) Suppose this year the rains are poor and the crop yield is only half as much as was originally expected. Some people say that if this happens the farmers should be asked to pay back only half the amount they have taken as loans. However, other people say that the full amount should be repaid, keeping in view the next year's crop. In your opinion what should the bank do, and why?

12. Apart from cheques, people can also exchange money through Bank Drafts. Find out:
(a) How do you send a Bank Draft?
(b) For the person receiving the money what advantage does a Draft have compared to a cheque?

13. Suppose a moneylender charges 2.5% interest per month (which is 30%/year). Compare this with the rate charged by banks. So why do a large number of people go to moneylenders?

14. Look at the table and answer the following questions:
(a) Calculate the percentage of each type of money and fill in the table.
(b) What does this table show? In which form is most of the money kept and why?

Total money in India (Financial year 2000-2001)

Form of money	Amount	Percentage
Notes and coins	Rs. 209,000 Crores	
Bank deposits (Saving, Current and Fixed Deposits)	Rs. 1097,000 Crores	
Total	Rs. 1306,000 Crores	