BANKING AND INSURANCE

COURSE CODE: SGB24CM101MD
Multi-Disciplinary Course
For Four Year Undergraduate Programmes
Self Learning Material

SREENARAYANAGURU
OPEN UNIVERSITY

SREENARAYANAGURU OPEN UNIVERSITY

The State University for Education, Training and Research in Blended Format, Kerala

Vision

To increase access of potential learners of all categories to higher education, research and training, and ensure equity through delivery of high quality processes and outcomes fostering inclusive educational empowerment for social advancement.

Mission

To be benchmarked as a model for conservation and dissemination of knowledge and skill on blended and virtual mode in education, training and research for normal, continuing, and adult learners.

Pathway

Access and Quality define Equity.

Banking and Insurance

Course Code: SGB24CM101MD

Semester - III

Multi Disciplinary Course
For FYUG Programmes (Honours)
Self Learning Material

BANKING AND INSURANCE

Course Code: SGB24CM101MD
Semester- III
Multi Disciplinary Course
For FYUG Programmes (Honours)

SREENARAYANAGURU OPEN UNIVERSITY

വിദ്യകൊണ്ട് സ്വതന്ത്രരാവുക

Academic Committee

Dr. Biju .T
Dr. Sreedhar P. Nair
Dr. Binu R.
Dr. Shehnaz S. R.
Dr. Vinod A. S.
Dr. Chithra P.
Dr. Anzer R.N.
Kevin Thomas Villoth
Savitha M.A.
Dr. Jayaprakasan P.P.
Dr. Baijumon P.

Development of the Content

Dr. Muhammed Abdul Rasheed K.P.

Review and Edit

Abdul Latheef K.T.

Linguistics

Sujith Mohan

Scrutiny

Dr. Midhun V.
Dr. Athena Prince
Dr. Kavitha S.
Dr. Dany Thomas
Dr. Gopika C.G.
Mahesan K.P.

Design Control

Azeem Babu T.A.

Cover Design

Jobin J.

Co-ordination

Director, MDDC :
Dr. I.G. Shibi
Asst. Director, MDDC :
Dr. Sajeevkumar G.
Coordinator, Development:
Dr. Anfal M.
Coordinator, Distribution:
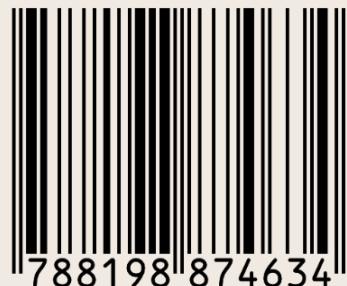Dr. Sanitha K.K.

Scan this QR Code for reading the SLM on a digital device.

Edition
August 2025

Copyright
© Sreenarayanaguru Open University

ISBN 978-81-988746-3-4

9 788198 874634

www.sgou.ac.in

Visit and Subscribe our Social Media Platforms

Message from Vice Chancellor

Dear Learner,

It is with great pleasure that I welcome you to the Four Year UG Programme offered by Sreenarayanaguru Open University.

Established in September 2020, our university aims to provide high-quality higher education through open and distance learning. Our guiding principle, 'access and quality define equity', shapes our approach to education. We are committed to maintaining the highest standards in our academic offerings.

Our university proudly bears the name of Sreenarayanaguru, a prominent Renaissance thinker of modern India. His philosophy of social reform and educational empowerment serves as a constant reminder of our dedication to excellence in all our academic pursuits.

The University is dedicated to offering forward-looking, skill-based learning experiences that prepare learners for the evolving demands of the modern world. As part of the FYUG programme, the Multidisciplinary Course "Banking and Insurance" is an introductory course designed to make the basics of financial services accessible to learners from diverse backgrounds. It covers fundamental concepts, key practices, and simple real-world applications in banking operations and insurance management, enabling you to develop a foundational understanding of how these sectors function. The course aims to demystify complex financial ideas and equip you with essential skills to make informed decisions in matters of money, savings, credit, and risk management. By exploring related disciplines, you gain a more comprehensive education, preparing you for diverse career opportunities and fostering well-rounded intellectual growth throughout your academic journey.

Our teaching methodology combines three key elements: Self Learning Material, Classroom Counselling, and Virtual modes. This blended approach aims to provide a rich and engaging learning experience, overcoming the limitations often associated with distance education. We are confident that this programme will enhance your understanding of statistical methods in business contexts, preparing you for various career paths and further academic pursuits.

Our learner support services are always available to address any concerns you may have during your time with us. We encourage you to reach out with any questions or feedback regarding the programme.

We wish you success in your academic journey with Sreenarayanaguru Open University.
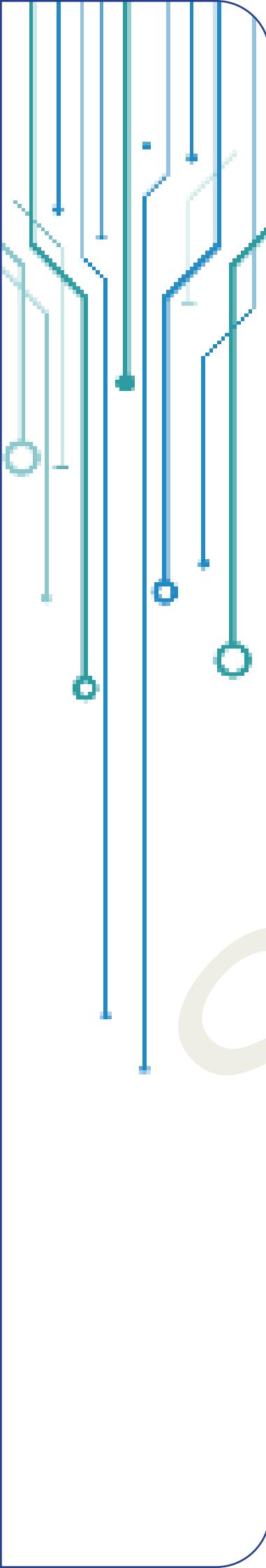
Best regards,

Dr. Jagathy Raj V.P.
Vice Chancellor

01-08-2025

Contents

1

BLOCK

Banking

Unit ①

Basics of Banking

Learning Outcomes

After completing this unit, the learner will be able to:

◊ explain the fundamental concepts of banking and the role banks play in the economy

◊ comprehend various types of banks such as commercial, cooperative, and development banks

◊ analyse core banking operations, including accepting deposits and granting loans

◊ describes the process of credit creation and assess the impact of mergers on banking efficiency

Prerequisites

A small village where people grow crops and rear animals. One farmer, Raju, harvests a lot of rice but has no place to store his extra earnings safely. Another villager, Meena, wants to start a small tailoring business but doesn't have the money to buy a sewing machine. Here, a wise elder in the village suggests creating a system where people like Raju can keep their money safely and people like Meena can borrow money to start businesses. This system becomes a basic "bank." Raju deposits his extra money in the bank, and the bank lends some of it to Meena. Meena uses the loan to start her work, earns money, and repays the loan with a little extra, called interest. The bank gives Raju a small portion of this interest as a reward for keeping his money. This way, both Raju and Meena benefit, and the bank acts as a trusted middleman. In real life, banks work in a very similar way, helping people save, borrow, invest, and grow economically.

Keywords

Credit Creation, Core Banking Solutions (CBS), Retail Banking Commercial Banks, Central Bank

Discussion

1.1.1 Banking

Banking is the lifeline of the modern economic system. A bank is a financial institution licensed to receive deposits and make loans. Banks also provide various financial services such as wealth management, currency exchange, and safe deposit boxes. They act as intermediaries between savers and borrowers and facilitate capital formation and economic development.

According to the Banking Regulation Act, 1949, "Banking means accepting, for the purpose of lending or investment, of deposits of money from the public, repayable on demand or otherwise, and withdrawable by cheque, draft, order or otherwise."

Horace White opines, "a bank is manufacturer of credit and a machine for facilitating exchanges".

In the words of Crowther, "A bank collects money from those who have it to spare or who are saving it out of their income and lend this money to those who require it".

Features of a Bank

1. Dealing in money: Bank is a financial institution which deals with other people's money.

2. Individual or Firm or Company: A bank may be a person, firm or a company. A banking company means a company which is doing the business of banking.

3. Acceptance of Deposit: A bank accepts money from the people in the form of deposits which are usually repayable on demand or after the expiry of a fixed period.

4. Giving Advances: A bank lends out money in the form of loans to those who require it for different purpose.

5. Payment and withdrawal: A bank provide easy payment and withdrawal facility to its customers in the form of cheques and drafts. It also brings money in circulation.

6. Connecting Link: A bank acts as a connecting link between borrowers and lenders of money. Banks collect money from those who have surplus money and give the same to those who are in need of money.

7. Agency and Utility Services: A Bank provides various banking facilities to its customers. They include general utility services and agency services.

1.1.1.1 Functions of a Bank

According to M.N. Mishra, banks perform a variety of functions that are broadly classified into primary and secondary functions. These functions ensure the smooth operation of financial systems and serve both individual customers and the economy as a whole.

A. Primary Functions

These are the essential functions that form the foundation of banking operations.

1. Accepting Deposits

The core function of a bank is to accept deposits from the public. People keep their money in banks for safety and convenience, and banks use these funds for lending and investment purposes. Different types of deposit accounts cater to different needs:

i.   *Savings Deposits*: These accounts encourage small savings from individuals. Depositors earn a modest interest and can withdraw money when needed *Example*: SBI's *Savings Plus Account* offers interest on daily balances and auto-sweep facilities.

ii. *Current Deposits*: Designed mainly for businesses, these accounts allow unlimited transactions but usually offer no interest.
Example: Traders and firms use ICICI's *Current Account Services* to manage their daily business operations.

iii. *Fixed Deposits (FDs):* These are time-bound deposits where money is locked in for a specific period and earns higher interest.
Example: HDFC Bank offers attractive FD rates for 1-year and 5-year deposits, popular among senior citizens.

iv. *Recurring Deposits (RDs):* Customers deposit a fixed amount every month and receive a lump sum with interest at maturity. This promotes regular savings among salaried individuals.
Example: Post Office Recurring Deposit Scheme is widely used in rural India for disciplined savings.

2. Granting Loans and Advances

Banks provide loans and advances to individuals and businesses to help them meet personal needs and fund economic activities. These credit facilities are of different types:

i.   *Overdraft*: This facility allows account holders to withdraw more money than they have in their accounts, up to a sanctioned limit.*Example*: Banks offer overdraft facilities to salaried customers against their salary account, useful during short-term cash crunches.

ii. *Cash Credit*: A short-term credit facility provided against security such as inventory or receivables. The borrower can withdraw funds as needed within the sanctioned limit.
Example: Small manufacturing units use cash credit from banks to manage working capital needs.

iii. **Term Loans**: These are loans granted for a specific period and are repaid in instalments. Typically used for purchasing machinery, vehicles, or building infrastructure.
Example: SBI's *Flexi Pay Home Loan* is a term loan product for young professionals buying a house.

iv. **Demand Loans**: These loans are repayable on demand by the bank, often granted against tangible security.
Example: Banks may provide demand loans to farmers against gold or agricultural produce stored in warehouses.

B. Secondary Functions

Apart from their core roles, banks also perform several additional services that support customers in their day-to-day financial dealings.

1. Agency Functions

Banks act as agents on behalf of customers for handling financial transactions and other related services.

i. **Collection of Cheques and Bills:** Banks collect cheques, drafts, and bills of exchange from other banks on behalf of customers and credit the proceeds. Example: A salaried person can deposit a cheque from another city in their local bank branch, which handles collection and credit.

ii. **Periodic Payments:** Banks offer standing instructions to make periodic payments such as house rent, electricity bills, or insurance premiums. Example: Customers can instruct HDFC Bank to auto-pay their LIC insurance premium every year.

iii. **Sale and Purchase of Securities:** Banks help clients in buying and selling government bonds, mutual funds, or shares by acting as intermediaries. Example: Through SBI's Demat and Trading Account, investors can directly invest in stock markets.

2. Utility Functions

These are modern services provided by banks for customer convenience and financial empowerment.

i. **Safe Deposit Lockers :** Banks offer secure lockers for storing valuable items like jewellery, property documents, and certificates.

Example: Bank of Baroda offers locker facilities in small, medium, and large sizes with annual rental charges.

ii. **Issue of Credit/Debit Cards :** Banks issue cards that allow customers to withdraw cash, make purchases, and pay bills conveniently.

Example: Axis Bank provides VISA debit and credit cards linked to customers' accounts, enabling both online and offline payments.

iii. **Online Banking, Fund Transfer, Mobile Banking :** Modern banks offer 24/7 digital services that let customers transfer funds, pay bills, and check balances via websites or apps.

Example: With YONO SBI App, customers can access all banking services from their mobile phones, including UPI transfers, FD booking, and shopping.Example: State Bank of India (SBI)

SBI, India's largest bank, offers all the above services to a wide range of customers. It has deposit products like *Savings Plus*, loan products like *SBI Education Loan*, utility services such as *YONO mobile banking*, and agency functions like *auto-debit insurance payments*. With over 40 crore customers, SBI is a practical example of how a bank performs both primary and secondary functions effectively.

1.1.2 Types of Banks

In the modern financial system, banks play specialised roles depending on the economic segment they serve. Based on their nature and function, banks in India can be classified into various types, each contributing uniquely to national development and financial inclusion.

1.1.2.1 Commercial Banks

Commercial banks are financial institutions that accept deposits from the public and provide loans for personal and business needs. They offer services like savings and current accounts, personal and business loans, credit cards, and fund transfers. Their primary aim is profit-making through interest income and service charges. *Example*: HDFC Bank and ICICI Bank are leading commercial banks in India offering home loans, business loans, and digital banking facilities.

1.1.2.2 Cooperative Banks

Cooperative banks are small, community-based institutions that operate under cooperative principles, focusing on mutual benefit rather than profit. They mainly serve farmers, small-scale industries, and low-income groups by offering affordable credit. Cooperative banks are registered under the Cooperative Societies Act and regulated by both the RBI and state governments. *Example*: Kerala State Cooperative Bank provides agricultural and rural loans to farmers at concessional interest rates.

1.1.2.3 Regional Rural Banks (RRBs)

RRBs were established in 1975 with the objective of providing credit and other banking services to rural areas, especially to small farmers, artisans, and rural entrepreneurs. These banks are jointly owned by the Central Government, State Government, and a sponsoring public sector bank. RRBs play a critical role in rural financial inclusion by offering crop loans, savings accounts, and rural development schemes. *Example:* Aryavart Bank in Uttar Pradesh offers rural housing loans and supports government schemes like PM Kisan.

1.1.2.4 Development Banks

Development banks provide long-term capital to industries and infrastructure projects that require significant investment and extended repayment periods. They focus on sectors like manufacturing, transport, energy, and housing, which are vital for economic development. Unlike commercial banks, they do not accept public deposits but raise funds from the government and capital markets. *Example*: The Industrial Development Bank of India (IDBI) was originally a development bank established to finance large-scale industries.

1.1.2.5 Investment Banks

Investment banks assist companies and governments in raising capital by underwriting and issuing securities. They provide financial advisory services, manage mergers and acquisitions, and help clients invest in the stock market. These banks operate more in the corporate and financial markets domain than in retail banking. *Example*: JM Financial and Goldman Sachs India are major investment banks helping Indian firms raise funds via IPOs and debt issues.

1.1.2.6 Central Bank

The central bank is the apex monetary authority in a country that regulates the entire banking system. In India, the Reserve Bank of India (RBI) performs this role by issuing currency, controlling inflation, managing foreign exchange reserves, and regulating the credit supply. It also acts as a banker to the government and other banks. *Example*: The RBI sets the repo rate and cash reserve ratio (CRR), which influence interest rates and liquidity in the economy.

1.1.3 Core Banking Solutions (CBS)

Core Banking Solutions (CBS) refer to a centralised software system that connects all branches of a bank through a common platform. This system allows customers to access their accounts and perform banking transactions from any branch, ATM, or online channel, regardless of where the account was originally opened. CBS has revolutionised traditional banking by making it faster, more efficient, and more customer-centric. It acts as the backbone of modern banking, supporting services such as fund transfers, loan processing, account management, and customer verification in real-time.

Some of the key features of CBS include:

i. 24x7 banking services through online platforms and mobile apps.

ii. Real-time transaction processing that updates customer balances instantly.

iii. Centralised customer information, making account details accessible from any branch.

iv. Integration of digital services such as ATMs, internet banking, UPI, and mobile banking apps.

For instance, ICICI Bank uses the Flexcube Core Banking System, developed by Oracle, which enables customers to deposit, withdraw, or transfer money from any ICICI branch or ATM in India. They can also access their accounts through the iMobile Pay app or internet banking, thanks to the seamless integration provided by CBS. CBS has not only improved convenience for customers but has also helped banks reduce operational costs and improve service quality.

1.1.4 Retail Banking Products and Services

Retail banking, also known as consumer banking, refers to the banking services provided by financial institutions to individual customers and small businesses. It focuses on meeting the day-to-day financial needs of the general public through a wide range of deposit, loan, and financial advisory products. Retail banking plays a key role in financial inclusion by providing convenient access to savings, credit, and investment services. This type of banking is typically delivered through branches, ATMs, mobile banking, and online platforms.

Retail banking services are mainly categorised into three segments: liability products, asset products, and other financial services.

A. Liability Products (Deposits)

These are products where banks accept money from customers and are liable to repay it on demand or after a fixed term. The bank pays interest on these deposits depending on the type and tenure.

i. **Savings Account**: This is the most common deposit product for individuals, encouraging the habit of saving. Customers earn interest (typically between 2.5% and 4% annually), and funds can be withdrawn anytime.

   Example: SBI's *Savings Plus Account* links savings with fixed deposit features for better returns.

ii. **Current Account**: Mostly used by businesses and professionals, this account facilitates unlimited transactions but usually earns no interest. It is ideal for high-frequency banking needs like payments and receipts. *Example*: ICICI Bank's *Smart Business Account* offers overdraft and payment features for small enterprises.

iii. **Fixed Deposit (FD)**: A time deposit where money is kept for a fixed tenure at a higher interest rate. Customers cannot withdraw before maturity without penalty. *Example*: HDFC Bank offers *Senior Citizen FDs* with interest rates up to 7.75%.

iv. **Recurring Deposit (RD)**: This is a savings scheme where a fixed amount is deposited every month for a specific period, and interest is paid at maturity. It encourages regular saving habits.

   Example: Axis Bank's *RD Plus* allows flexibility in monthly deposit amounts and tenure.

B. Asset Products (Loans and Advances)

These are credit products that allow individuals to borrow money from the bank to meet personal or business needs. Banks earn interest on these loans, which forms a major part of their income.

i. **Home Loans:** Offered to individuals for buying or constructing a house. These are long-term loans with tenures of 15–30 years.

Example: SBI's Home Loan Advantage Scheme offers lower interest rates linked to the borrower's savings account balance.

ii. **Auto Loans:** Loans to purchase two-wheelers or four-wheelers. Offered for both new and used vehicles with flexible repayment terms.

Example: HDFC Bank's Car Loan includes 100% on-road financing with minimal paperwork.

iii. **Personal Loans:** Unsecured loans provided for purposes like weddings, travel, or emergencies. Since these are riskier, they have higher interest rates.

Example: ICICI Bank offers personal loans with instant disbursal for salaried individuals.

iv. **Education Loans:** Financial support provided to students to pursue higher education in India or abroad. They often come with a moratorium period during the course of study.

Example: Bank of Baroda's Vidyarthi Loan Scheme supports students studying in reputed institutions like IITs and IIMs.

v. **Credit Cards:** A revolving credit facility that allows customers to make purchases and pay later. Banks charge interest on outstanding amounts and also offer reward points.

Example: Axis Bank's ACE Credit Card offers cashback and discounts on online spending.

C. Other Services

In addition to traditional deposit and credit services, retail banks also offer a variety of financial and digital services to meet the evolving needs of customers.

i. **Internet and Mobile Banking:** Customers can access banking services such as fund transfers, bill payments, and account statements anytime using their phones or computers.

Example : The YONO SBI app allows customers to open accounts, invest in FDs, shop online, and transfer funds.

ii. **Insurance Services:** Banks tie up with insurance companies to offer life, health, and general insurance products as part of their bancassurance strategy. Example: ICICI Bank partners with ICICI Lombard and ICICI Prudential to sell insurance products through its branches.

iii. **Mutual Funds and Investment Advisory:** Banks help customers invest in mutual funds, bonds, and government schemes, and provide financial planning advice. Example: HDFC Bank's Investment Services Account allows retail customers to invest in SIPs, mutual funds, and ETFs.

Example: HDFC Bank offers a comprehensive retail product called *Smart EMI*, where customers can convert high-value purchases like smartphones or appliances into easy monthly instalments using their debit or credit cards. This service combines retail lending with technology and provides affordable finance to middle-class consumers. Such products demonstrate how retail banking helps customers manage finances and meet lifestyle needs conveniently.

1.1.5 Mergers in Banking

Bank mergers involve the consolidation of two or more banks into a single larger entity. In India, bank mergers have been implemented as part of the government's strategy to improve the strength, efficiency, and global competitiveness of the banking sector, especially among public sector banks. These mergers are overseen by the Reserve Bank of India (RBI) and the Ministry of Finance and are generally aimed at creating fewer but stronger banks with better capital adequacy, enhanced service delivery, and a larger customer base. Mergers also help in managing non-performing assets (NPAs) more efficiently and bringing technological upgrades across all merged entities.

1.1.5.1 Objectives of Bank Mergers

Bank mergers are usually undertaken with specific financial and operational goals in mind:

i. **Improve Capital Base**: A merged bank has a stronger balance sheet and can meet international capital requirements such as those prescribed by the Basel III norms. *Example*: After the merger, Punjab National Bank (PNB) became the second-largest public sector bank with a stronger capital base.

ii. **Reduce Operational Costs**: By consolidating overlapping branches, staff, and resources, banks can reduce redundant expenses and operate more efficiently. *Example*: Merged entities share common back-end systems, reducing infrastructure duplication.

iii. **Enhance Technology and Service Efficiency**: Unified technological platforms help in better customer experience and smoother digital services. *Example*: Post-merger, Canara Bank implemented a single Core Banking System (CBS) across its network.

iv. **Create Globally Competitive Banks**: Bigger banks are better equipped to handle international trade, large-scale corporate financing, and cross-border transactions. *Example*: The merger of Bank of Baroda with Vijaya Bank and Dena Bank gave it a wider international presence.

1.1.5.2 Recent Major Bank Mergers in India

In recent years, India has witnessed several large-scale public sector bank mergers to achieve these objectives.

Merged Banks	Merged Into
Allahabad Bank	Indian Bank
Andhra Bank, Corporation Bank	Union Bank of India
Oriental Bank of Commerce, United Bank of India	Punjab National Bank (PNB)
Syndicate Bank	Canara Bank

These mergers reduced the number of public sector banks from 27 in 2017 to 12 in 2020, streamlining the banking structure.

Case Study: 2020 Mega Merger of 10 Public Sector Banks

In April 2020, the Indian government carried out one of the largest banking consolidation initiatives. A total of 10 public sector banks were merged into 4 major banks. One significant example was the merger of Syndicate Bank into Canara Bank. This created the fourth-largest public sector bank in India, both in terms of branch network and business volume. Post-merger, Canara Bank had over 10,000 branches, enhanced capital strength, and improved access to advanced digital banking platforms. The merger aimed at reducing fragmentation in the banking sector and enabling the consolidated entity to support larger credit needs and adopt better risk management practices.

1.1.5.3 Impact of Bank Mergers

i. Improved financial strength and lending capacity.

ii. Expanded customer reach across rural and urban areas.

iii. Harmonisation of products, interest rates, and customer service.

iv. Challenges during the transition included system integration, cultural adjustment, and harmonising employee benefits.

Bank mergers in India reflect a structural reform aimed at modernising the banking sector and preparing it for global competition. While mergers bring several long-term advantages, careful execution is necessary to manage challenges like customer confusion, system downtime, and employee reallocation. Overall, the mergers are expected to create a more stable, digital, and future-ready banking system in India.

1.1.6 Central Bank System

A Central Bank is the apex financial institution of a country that manages and regulates the entire banking and monetary system. It plays a crucial role in ensuring financial stability, controlling inflation, regulating the money supply, and guiding the economy through its monetary policy. Unlike commercial banks, a central bank does not deal with the public directly but works to maintain the economic health of the nation by supervising other banks and acting as the government's banker. In India, this role is performed by the Reserve Bank of India (RBI), established on April 1, 1935, under the RBI Act of 1934, and nationalised in 1949.

1.1.6.1 Functions of a Central Bank

Central bank is an institution that fulfils the credit needs of banks and other credit institution, which works as banker to the banks and the government and which work for the economic interest of the country. The following are the major functions of a central bank:

1. Issuer of Currency

The central bank has the sole authority to issue the national currency, making it the monopoly issuer of legal tender in the country. In India, the Reserve Bank of India issues currency notes of all denominations except the one-rupee note (which is issued by the Ministry of Finance). This helps maintain uniformity, control over inflation, and prevents counterfeiting. Example: Every Indian currency note carries the signature of the RBI Governor, ensuring its authenticity and legal backing.

2. Custodian of Foreign Reserves

The central bank manages the country's foreign exchange reserves, including foreign currencies, gold, and special drawing rights (SDRs). It intervenes in the foreign exchange market to stabilise the currency and maintain a favourable balance of payments. Example: The RBI actively monitors and adjusts India's foreign exchange reserves to protect the rupee from excessive volatility in the global market.

3. Regulator of Credit

The central bank controls the availability, cost, and direction of credit in the economy using various monetary policy tools such as the repo rate, reverse repo rate, CRR, and SLR. This helps manage inflation, encourage investment, and ensure adequate liquidity in the system. Example: If inflation is rising, the RBI may increase the repo rate to make borrowing costlier, thereby reducing the money supply.

4. Banker to the Government

The central bank acts as a banker, agent, and financial advisor to the central and state governments. It manages government accounts, facilitates the borrowing needs of the government through bond and treasury bill issues, and advises on fiscal matters. Example: The RBI manages the issue and redemption of government securities and conducts auctions for raising public debt.

5. Lender of Last Resort

In times of financial crisis or liquidity shortages, the central bank provides emergency funding to commercial banks to prevent their collapse. This function protects public confidence in the banking system and maintains financial stability. Example: During the 2008 global financial crisis, central banks across the world, including the RBI, infused liquidity to support stressed financial institutions.

6. Maintains Financial Stability

One of the most critical roles of a central bank is to ensure financial stability by monitoring systemic risks and acting promptly to prevent banking failures. It regulates banking operations through licensing, supervision, and inspection. It also issues guidelines and imposes penalties to maintain public trust in the banking sector. Example: The RBI conducts regular stress testing of banks and issues regulatory frameworks such as the Prompt Corrective Action (PCA) norms to identify and rectify weak banks.

7. Custodian of Cash Reserve of Commercial Bank

Central bank is the bank of banks. This signifies that it has the same relationship with the commercial banks. In the country that they gave with their customers. It provide security to their cash reserves, gives then loan at the time of need, give them advice on financial and economic matter and work as clearing house among various members bank.

8. Clearing House Function

All commercial bank has their accounts with the central bank. Therefore, central bank settle the mutual transactions of banks and thus saves all banks controlling each other individually for setting their individual transaction.

Thus the Central Bank, particularly the Reserve Bank of India, plays a vital role in India's financial system. It ensures that the economy remains on a stable path by controlling inflation, guiding interest rates, regulating credit, and protecting the value of the currency. Its unique position as the lender, regulator, and currency issuer makes it central to economic governance in any modern nation.

1.1.7 Role of the Reserve Bank of India (RBI)

The Reserve Bank of India (RBI), established in 1935 under the RBI Act of 1934, is the central bank of India and the primary authority responsible for regulating the country's monetary and financial system. Headquartered in Mumbai, the RBI was originally a private institution but was nationalised in 1949 after India's independence. Since then, the RBI has played a pivotal role in ensuring the stability of the Indian economy by formulating and implementing policies related to currency issuance, monetary control, and financial regulation. Its mission extends beyond traditional banking functions and includes developmental initiatives to promote economic growth and financial inclusion.

1.1.7.1 Key Roles of the RBI

1. Monetary Authority

As the monetary authority, the RBI formulates and implements the Monetary Policy to control inflation, maintain price stability, and support economic growth. It uses tools such as the repo rate (the rate at which it lends money to commercial banks) and the reverse

repo rate (the rate at which it borrows from banks) to manage liquidity in the market. Example: During the COVID-19 pandemic, the RBI cut the repo rate multiple times to encourage banks to lend more and support businesses and consumers during economic slowdown.

2. Issuer of Currency

The RBI is the sole authority for issuing currency notes in India, except for the one-rupee note, which is issued by the Government of India. All notes issued by the RBI are legal tender and bear the signature of the Governor. This role ensures uniformity, control over currency supply, and prevention of counterfeiting. Example: In 2016, after the demonetisation of ₹500 and ₹1000 notes, the RBI introduced new ₹500 and ₹2000 notes as part of its currency issuance function.

3. Regulator of the Financial System

The RBI regulates and supervises all commercial banks, cooperative banks, NBFCs, and other financial institutions in India. It sets capital adequacy norms, licensing requirements, and issues regulatory guidelines to maintain public confidence and stability in the banking system. The RBI also monitors non-performing assets (NPAs) and implements corrective measures. Example: Through the Prompt Corrective Action (PCA) framework, the RBI places restrictions on weak banks to restore their financial health.

4. Foreign Exchange Manager

The RBI manages the country's foreign exchange reserves and oversees the implementation of the Foreign Exchange Management Act (FEMA), 1999. It ensures the orderly functioning of the forex market and maintains the external value of the Indian Rupee. The RBI also authorises banks to deal in foreign exchange and monitors cross-border transactions. Example: The RBI intervenes in the forex market to stabilise the rupee when it experiences excessive volatility against the US dollar.

5. Developmental Role

The RBI also performs a developmental role by supporting initiatives that enhance financial inclusion, promote digital payments, and develop rural banking. It introduces policies and schemes aimed at expanding banking services to the unbanked and underbanked sections of society. Example: The Pradhan Mantri Jan Dhan Yojana (PMJDY) was implemented with RBI support, resulting in the opening of over 40 crore basic savings accounts across India. The RBI also launched the Unified Payments Interface (UPI) system to promote real-time digital transactions.

Additional Functions

◊ Acts as banker to the government, managing its accounts, payments, and borrowings.

◊ Maintains public debt and conducts auctions for government securities.

◊ Publishes key reports and statistics such as the Monetary Policy Report, Financial Stability Report, and Annual Report to guide policy makers and investors.

The Reserve Bank of India serves as the nerve centre of India's financial and monetary system. Its actions have far-reaching implications on inflation control, banking sector stability, exchange rate management, and economic development. By balancing its roles as a regulator, policymaker, currency issuer, and developmental institution, the RBI plays a fundamental role in shaping the economic future of India.

1.1.8 Commercial Banks

Commercial banks are financial institutions that provide a wide range of banking services to individuals, businesses, and institutions. Their primary objective is to accept deposits from the public and provide loans and advances to borrowers, thereby earning profits through interest income and service fees. These banks play a vital role in the economy by mobilising savings, providing credit for consumption and investment, and facilitating trade and commerce. Unlike central banks, commercial banks operate directly with the public and businesses.

1.1.8.1 Key Functions of Commercial Banks

1. Accepting Deposits

Commercial banks offer various types of deposit accounts such as savings accounts, current accounts, fixed deposits, and recurring deposits. These deposits form the primary source of funds for banks. Banks pay interest on certain types of deposits, encouraging the public to save and invest their idle money. Example: HDFC Bank offers multiple deposit options including Senior Citizen FDs, which attract higher interest rates.

2. Providing Loans and Advances

Banks lend money to individuals, businesses, and industries in the form of personal loans, home loans, business loans, and overdrafts. They charge interest on these loans, which is their main source of revenue. Example: SBI offers the SBI MaxGain Home Loan, which helps borrowers reduce interest payments by linking loans to savings.

3. Payment and Remittance Services

Commercial banks facilitate domestic and international money transfers through services like NEFT, RTGS, IMPS, and SWIFT. They

also issue cheques, demand drafts, and enable electronic transactions. Example: ICICI Bank allows its customers to transfer funds instantly through IMPS using its iMobile Pay app.

4. Providing Safe Deposit Lockers and Other Services

Banks offer locker facilities for the safe custody of valuable items such as jewellery, documents, and bonds. They also provide ATM services, debit/credit cards, internet and mobile banking, bill payments, and insurance sales through bancassurance. Example: Axis Bank provides lockers in multiple sizes and digital access to locker availability in branches.

1.1.8.2 Types of Commercial Banks in India

Commercial banks in India are broadly classified into the following categories:

1. Public Sector Banks (PSBs)

These are government-owned banks where the majority stake (more than 50%) is held by the Government of India. They are known for their wide branch network and social banking initiatives. Examples:

◊ State Bank of India (SBI) – India's largest public sector bank.

◊ Bank of Baroda (BoB) – A major PSB known for international operations.

2. Private Sector Banks

In these banks, the majority stake is held by private individuals or institutions. They are often more technology-driven and customer-focused. Examples:

◊ HDFC Bank – Known for retail banking and digital innovation.

◊ ICICI Bank – Offers a wide range of personal, corporate, and digital banking services.

3. Foreign Banks

These are banks headquartered outside India but operating in the country through branches or subsidiaries. They typically focus on corporate banking, wealth management, and international transactions. Examples:

◊ Citi Bank – Offers investment and corporate banking services.

◊ HSBC – Provides global banking services to individuals and companies.

Commercial banks are the backbone of India's financial system. By accepting deposits and providing credit, they bridge the gap between savers and borrowers and stimulate economic activity. With technological advancements and policy reforms, commercial banks in India have evolved to offer a wide range of digital and financial services that support both personal and business growth.

1.1.9 Credit Creation by Commercial Banks

Credit creation is the most significant function of commercial banks. Credit creation is the process by which banks increase the money supply by lending out a portion of the deposits they receive, rather than holding all deposits in reserve. This process relies on the fractional reserve system, where banks keep only a fraction of deposits as reserves and lend out the rest. This creates a "multiplier effect," where the initial deposit can lead to a larger increase in the total money supply. Thus they multiply the initial deposits by creating loans, thereby increasing the money supply in the economy.

Process of Credit Creation with example:

1. A person deposits ₹1,000 in the bank.
2. The bank keeps 10% (₹100) as reserve.
3. It lends ₹900 to another customer.
4. The new borrower deposits ₹900 in the bank.
5. The process continues, multiplying the money in the economy.

Formula:

$$\text{Total Credit Creation} = \frac{1}{\text{Cash Reserve Ratio (CRR)}} \times \text{Initial Deposit}$$

- If CRR = 10% or 0.10, then the credit multiplier is $\frac{1}{0.10} = 10$.
- Initial deposit = ₹1,000
- So, Total Credit Creation = 10 × ₹1,000 = ₹10,000

Example : If CRR is 10%, then ₹1,000 can lead to total deposits of ₹10,000 in the banking system.

Case Study - Credit Creation by Commercial Banks:

After the Government of India merged Syndicate Bank into Canara Bank in April 2020, customers experienced both transitional challenges and long-term improvements, particularly in the area of credit creation. The merger significantly strengthened Canara Bank's capital base, branch network, and digital infrastructure, enabling it to expand its credit offerings more efficiently. As a result, the bank could extend more loans across sectors like MSMEs, agriculture, and housing. The unified credit products, streamlined loan approval processes, and enhanced risk assessment mechanisms supported faster and broader lending. Additionally, the creation of centralised loan processing hubs and the implementation of integrated IT systems allowed the bank to disburse credit with reduced turnaround time, thereby increasing the overall credit-deposit ratio post-merger.

However, the transition initially caused service disruptions for former Syndicate Bank customers. Changes in account numbers, IFSC codes, and unfamiliarity with Canara Bank's banking systems led to confusion, especially for those dependent on auto-debits or mobile banking. Customers also faced delays in loan processing due to

system integration. Despite these issues, the bank's post-merger consolidation efforts paid off, as it gradually restored smooth operations and improved customer access to credit. Ultimately, the merger enhanced Canara Bank's ability to perform its fundamental function as a commercial bank i.e., credit creation by enabling it to multiply deposits more effectively and support broader economic activity.

Credit Control

Credit control refers to the process of regulating and managing the extension of credit by financial institutions to borrowers. It aims to balance the need for providing credit to stimulate economic growth while minimising the risk of default and financial instability. Effective credit control involves assessing the creditworthiness of borrowers, setting credit limits, monitoring credit utilisation, and implementing measures to mitigate potential risks.

Why is Credit Control Important?

The following points highlight the importance of credit control for your lender:

◊ With credit control, financial institutions can meet their monetary requirements by collecting timely payments from customers, resulting in healthy cash flow.

◊ It helps financial institutions identify risky borrowers and take immediate actions to set off the risks.

◊ Customer trust and business relationships can be strengthened with the help of consistent and clear credit control practices.

◊ An effective credit control system can minimise the cost of recovering loan amounts, enhancing business profitability.

◊ Streamlined processes and automation can help employees to focus on more important tasks.

1.1.9.1 Different Methods of Credit Control

Credit control methods can be qualitative or quantitative. They aim to regulate the availability and cost of credit in an economy.

1. Qualitative Methods

Qualitative methods focus on influencing the quality of credit. The methods include the following measures:

a. **Credit Rationing:** In this method, credit is rationed by limiting the availability of credit to each applicant. RBI sets a maximum limit for loans that lenders can provide to a particular sector. This method is used to divert credit flow to desirable sectors and restrict the flow in undesirable sectors.

b. **Margin Requirements:** It refers to the difference between the value of loan security offered for a loan (collateral) and the value of the loan granted. This method is adopted for stabilising the economy during inflation or deflation.

c. **Moral Persuasion:**In this method, RBI may advise, suggest, or persuade lending institutions to cooperate in controlling price stability by limiting credit lending.

d. **Method of Publicity:** RBI publishes various reports in a public forum to educate and influence lending institutions about the good and bad systems. This helps the lending institutions direct the credit supply in desired sectors and attain monetary policy goals.

e. **Regulation of Consumer Credit:** Consumers are given limited credit. As a result, the number of EMIs is reduced. Consumer credit is regulated for certain products affected by inflation or deflation.

f. **Direct Action:** In this method, if the lending institutions do not follow the policy laid by RBI. It only has a recourse to the direct action. This method is usually used to supplement other credit control methods.

2. Quantitative Methods

Quantitative methods target the quantity of credit. These include the following measures:

a. **Bank Rate Policies:** It is the rate at which RBI provides loans to lending institutions without any security or collateral. The bank rate policy is increased to control credit and inflation.

b. **Open Market Operations:** RBI conducts the buying or selling of Government securities in the open market to increase or decrease the money supply, affecting interest rates and credit availability.

c. **Cash Reserve Ratio:** RBI mandates commercial banks to hold a certain percentage of their deposits as reserves, controlling the amount of funds available for lending.

Recap

◊ Definition of Banking: Banking is accepting deposits and lending for investment and personal needs.

◊ Primary Functions: Accepting deposits and granting loans are core banking functions.

◊ Secondary Functions: Includes agency services, utility services, and investment facilitation.

◊ Types of Banks: Includes commercial, cooperative, rural, development, and investment banks.

◊ Core Banking Solutions: Provides integrated, efficient, and real-time banking services.

◊ Retail Banking Services: Includes savings, loans, credit cards, and insurance.

◊ Central Bank Role: Issues currency, controls inflation, and acts as banker to the government.

◊ Credit Creation Process: Banks lend more than the reserve, multiplying money supply.

◊ Merger Case Study: Canara Bank's merger with Syndicate Bank improved credit capacity.

◊ Impact of Mergers: Leads to improved capital base, better technology, and operational challenges.

◊ Credit Control: Process of regulating and managing the extension of credit by financial institutions to borrowers

Objective Questions

1. What is the full form of CBS?
2. Which Act defines banking in India?
3. What is the percentage of CRR in the credit creation example?
4. Which app is used by SBI for mobile banking?
5. What type of deposit offers the highest interest?
6. Name one public sector bank in India.
7. Which bank merged with Canara Bank in 2020?
8. Who regulates cooperative banks?
9. What is the main function of the RBI as a monetary authority?
10. What is the purpose of cash credit?
11. What are recurring deposits ideal for?
12. Name one function of a central bank.

Answers

1. Core Banking Solution
2. Banking Regulation Act
3. Ten percent
4. YONO SBI
5. Fixed Deposit
6. Bank of Baroda
7. Syndicate Bank
8. RBI and State
9. Control inflation
10. Working capital
11. Regular savings
12. Issue currency

Self-Assessment Questions

1. Define banking
2. Explain the functions of a bank
3. Describe the types of banks with examples
4. Explain the types of commercial banks in India
5. What is core banking solutions?
6. What are the different methods of credit creation?
7. Describe the functions of RBI
8. Explain the role of central bank in banking sector

Assignments

1. Explain the process of credit creation by commercial banks with a suitable example.

2. Describe the primary and secondary functions of banks with examples.

3. Differentiate between commercial banks and cooperative banks.

4. What are Core Banking Solutions (CBS)? How have they changed modern banking?

5. Discuss the impact of the Syndicate–Canara Bank merger on credit creation and customer service.

6. Prepare a chart comparing the functions of different types of banks (Commercial, Cooperative, Central).

7. Interview a local banker to understand how CBS is implemented in their branch.

8. Track a fixed deposit scheme from three banks and compare interest rates and features.

9. Create a poster explaining how the Reserve Bank of India regulates inflation using the repo rate.

10. Write a report on the impact of bank mergers on employee morale using real-world examples.

Reference

1. Mishra, M. N., & Mishra, S. B. (2020). *Insurance: Principles and Practice*. S. Chand Publishing.

2. Bhole, L. M., & Mahakud, J. (2011). *Financial Institutions and Markets in India*. Tata McGraw-Hill.

3. Khan, M. Y. (2020). *Indian Financial System*. McGraw-Hill Education.

4. Reserve Bank of India. (2020). *RBI Annual Report 2019-20*. Retrieved from https://www.rbi.org.in

5. Canara Bank. (2021). *Annual Report 2020-21*. Retrieved from https://www.canarabank.com

6. Indian Bank Association. (2019). *Basics of Banking*. IBA Publications.

7. Sengupta, R., & Vardhan, H. (2017). *Banking Sector Reforms in India*. IGIDR.

8. Basu, A. (2022). *Retail Banking in India: Trends and Practices*. Sage Publications.

9. RBI Circulars. (2020). *Guidelines on Amalgamation of Public Sector Banks*. Retrieved from https://www.rbi.org.in

10. Sundaram, K. P. M., & Varshney, P. N. (2018). *Banking Theory, Law and Practice*. Sultan Chand & Sons.

Suggested Reading

1. Mishra, M. N., & Mishra, S. B. (2020). *Insurance: Principles and Practice*. S. Chand Publishing.

2. Bhole, L. M., & Mahakud, J. (2011). *Financial Institutions and Markets in India*. Tata McGraw-Hill.

3. Khan, M. Y. (2020). *Indian Financial System*. McGraw-Hill Education.

4. Reserve Bank of India. (2020). *RBI Annual Report 2019-20.* Retrieved from https://www.rbi.org.in

Unit ②

Banker and Customer

Learning Outcomes

After completing this unit, the learner will be able to:

◊ define the legal concepts of banker and customer and explain their mutual relationship

◊ identify and differentiate various types of accounts offered by banks and their features

◊ interpret the legal meaning and essential characteristics of cheques and their operational guidelines

◊ comprehend legal provisions related to cheque dishonour, payment in due course, crossing, and endorsement

Prerequisites

Ravi, a school teacher, wants a safe place to keep his salary and also needs help managing his monthly bills. He walks into a nearby bank, opens a savings account, and deposits his money. At the same time, Priya, a young entrepreneur from the same town, approaches the same bank to get a loan for starting her bakery. The bank accepts Ravi's deposit and lends a portion of it to Priya. In this simple interaction, the bank plays the role of a banker, an institution that accepts deposits and lends money, while Ravi and Priya are customers, using the bank's services to save and borrow, respectively.

According to banking law, the relationship between a banker and a customer begins when the bank agrees to open an account in the name of a person and that person starts making transactions. The banker is obligated to honour the customer's cheques, safeguard deposits, provide financial advice, and extend credit facilities, while the customer is expected to maintain honesty, repay loans, and use services responsibly. This mutual relationship is built on trust, legality, and financial interest, forming the foundation of the banking system.

Keywords

Banker, Customer, Cheque, Crossing, Endorsement

Discussion

1.2.1 Banker and Customer

A banker is typically a bank or financial institution licensed and regulated under the relevant national banking laws to perform core financial services such as accepting deposits, granting loans, facilitating fund transfers, and managing investment services. In the Indian context, the definition of banking is clearly articulated in Section 5(b) of the Banking Regulation Act, 1949, which states:

"Banking means accepting, for the purpose of lending or investment, deposits of money from the public, repayable on demand or otherwise, and withdrawable by cheque, draft, order, or otherwise."

This definition emphasises two essential aspects:

1. Accepting public deposits, and
2. Utilising those funds for lending or investment while allowing depositors to withdraw their money.

Thus, a banker refers not only to a commercial bank like the State Bank of India, HDFC Bank, or ICICI Bank, but also to licensed cooperative banks, development banks, and other financial institutions authorised by the Reserve Bank of India (RBI). These institutions perform a dual function such as protecting savings and enabling credit expansion, which is vital for economic growth.

For example, Punjab National Bank, one of the largest public sector banks in India, performs all essential functions of a banker. It offers savings and current accounts to individuals, provides loans to farmers, businesses, and students, and facilitates payments through cheque, NEFT, UPI, and debit cards. Moreover, it also acts as an agent for government-related services such as pension disbursement and subsidy payments under schemes like the Pradhan Mantri Jan Dhan Yojana (PMJDY).

Who is a Customer?

Unlike the well-defined term "banker," the Indian legal system does not offer a precise statutory definition of a customer in banking laws. However, it is generally accepted by courts, banks, and scholars that a customer is any person or legal entity who has a bank account or maintains a banking relationship with a bank and regularly uses banking services.

The most widely acknowledged interpretation is that:

◊ A person becomes a customer the moment they open an account (such as a savings, current, or fixed deposit account), and

◊ They engage in regular banking transactions or avail services such as loans, cheques, fund transfers, or ATM withdrawals.

This understanding was notably clarified in the landmark British case Tournier v. National Provincial and Union Bank of England (1924). The case emphasised the contractual and fiduciary relationship between the banker and the customer. One of the key takeaways from the judgment was the duty of the bank to maintain customer confidentiality, unless disclosure is legally required or justified by public interest.

In the Indian context, courts and regulatory authorities have adopted this broad interpretation. For instance, the Reserve Bank of India (RBI) in its guidelines on Know Your Customer (KYC) norms insists that banks must verify the identity of every person intending to open an account, thereby recognising them formally as customers.

An example would be a college student opening a zero-balance savings account under PMJDY. From the moment the account is opened and the student receives a RuPay debit card, they become a customer of the bank. Even if the account balance is minimal, the student is entitled to banking facilities like mobile banking, ATM services, and government subsidy transfers.

In conclusion, the relationship between a banker and a customer is foundational to the financial system. It is rooted in legal definitions, practical engagement, and mutual responsibilities. The banker offers a range of services under legal and regulatory frameworks, while the customer participates by maintaining accounts and using services in good faith. Together, they contribute to the smooth operation and growth of the economy.

1.2.2 Relationship Between Banker and Customer

The relationship between a banker and a customer is both legal and fiduciary. It can be classified into two types:

1.2.2.1 General Relationship

1. Debtor and Creditor

When a customer deposits money in a bank, the bank becomes a debtor, and the customer is a creditor. The bank is not a trustee of the money and is only obliged to repay it on demand, not automatically. In Joachimson v. Swiss Bank Corporation (1921), it was held that the debt is repayable only upon proper demand by the customer.

2. Agent and Principal

When a bank undertakes tasks such as collecting cheques, paying utility bills, or purchasing securities, it does so as an agent on behalf of the customer. In this relationship,

the customer gives instructions and the bank acts on their behalf. The bank is bound to follow lawful directions and act in the customer's best interest.

3. Trustee and Beneficiary

If a customer deposits funds for a specific purpose (e.g., payment to a third party), the bank becomes a trustee and must hold and use the money solely for that purpose. The customer, in this case, is the beneficiary. The bank must not use the funds for any other purpose, or it will breach its fiduciary duty.

4. Bailee and Bailor

When a customer stores valuables like jewellery or documents in a bank locker, the bank assumes the role of a bailee, and the customer becomes the bailor. This relationship is governed by the Indian Contract Act, 1872, which mandates the bailee to take reasonable care of the items. The bank must return the valuables in the same condition upon demand.

1.2.2.2 Special Relationship

1. Obligation to Honour Cheques

If a customer has a sufficient balance and presents a valid cheque, the bank is legally bound to honour it. Wrongful dishonour can lead to a loss of reputation and legal liability for the bank. However, the bank may refuse to pay if the cheque is irregular, post-dated, or exceeds the available balance.

2. Duty of Secrecy

Banks are legally required to maintain confidentiality about a customer's account details and transactions. Disclosure is only permitted in specific situations: with the customer's consent, under legal compulsion, or when public interest demands it. In Tournier v. National Provincial Bank of England (1924), the court defined these exceptions to the duty of secrecy.

3. Right to Lien

A banker has a general lien over the securities, goods, or instruments of the customer in its possession, allowing it to retain them until the debt is repaid. This right arises in the ordinary course of business and does not require a specific agreement. However, it does not apply to items held in safe custody or for a specific purpose.

4. Right to Set-off

If a customer has multiple accounts in the same bank, the bank can combine the balances and adjust a debit in one account against a credit in another. This is known as the right of set-off and is exercised after giving due notice to the customer. It is particularly useful in loan recoveries and insolvency situations.

1.2.3 Types of Accounts in Banks

Banks offer various types of accounts tailored to suit the diverse needs of individuals, businesses, and non-resident Indians. Each account differs in terms of purpose, interest rate, liquidity, and transaction limits. Understanding these account types helps customers choose the most appropriate option for saving, investing, or transacting.

1. Savings Account

A savings account is designed for individuals to deposit their income and earn interest on the balance while retaining easy access to funds. It encourages the habit of saving, typically offering interest rates ranging from 2.5% to 4% annually, and allows a limited number of withdrawals per month. Many banks now offer zero-balance savings accounts, along with facilities like internet banking, ATM cards, and mobile apps. Example: HDFC Bank offers savings accounts with features such as digital banking, auto-sweep fixed deposit links, and interest payouts on a quarterly basis.

2. Current Account

A current account is primarily meant for businesses, firms, and professionals who require frequent and large-scale transactions. These accounts do not earn interest and usually come with overdraft facilities, allowing withdrawals beyond the available balance up to a limit. Current accounts offer unlimited transactions, cheque book usage, and payment gateway facilities to suit commercial needs. *Example:* ICICI Bank's Smart Business Account provides value-added services such as bulk payment options and inward/outward remittance services.

3. Fixed Deposit (FD)

Fixed Deposits are time-bound deposit accounts where money is locked in for a fixed tenure (ranging from 7 days to 10 years), earning higher interest than savings accounts. The interest rates can go as high as 7% to 7.5% per annum depending on the bank and tenure, with special rates for senior citizens. Premature withdrawal is allowed, but may incur a penalty. *Example:* As of 2024, HDFC Bank offers FDs with interest up to 7.25%, and flexible options like tax-saving FDs under Section 80C of the Income Tax Act.

4. Recurring Deposit (RD)

A recurring deposit is suitable for individuals who wish to invest small amounts regularly and earn interest like a fixed deposit. Customers deposit a fixed amount every month for a chosen period, usually ranging from 6 months to 10 years, and receive a lump sum on maturity. It promotes disciplined savings and is ideal for salaried individuals or students. *Example:* Post Office RD Scheme is popular in rural and semi-urban areas due to its simplicity and assured returns, with an interest rate of around 6.7% per annum (as revised quarterly by the government).

5. NRI Accounts

Non-Resident Indians (NRIs) can open specialised accounts in India such as:

i.   NRE (Non-Resident External) – Repatriable and tax-free, used to park foreign income.

ii. NRO (Non-Resident Ordinary) – Non-repatriable beyond a limit, used to manage income earned in India.

iii. FCNR (Foreign Currency Non-Resident) – Maintained in foreign currencies, protects against currency risk.

These accounts cater to the banking needs of Indians living abroad, allowing them to send money home, pay bills, and invest in India. *Example:* SBI and Axis Bank offer all three types of NRI accounts with facilities like online access, repatriation services, and multi-currency options.

1.2.4 Cheque

A cheque is a widely used financial instrument that facilitates the non-cash transfer of funds between bank accounts. It is considered a negotiable instrument, which means it can be transferred from one person to another by endorsement or delivery, ensuring the transfer of the right to receive the amount specified.

As per Section 6 of the Negotiable Instruments Act, 1881, a cheque is defined as:

"A cheque is a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand."

This means that a cheque:

◊   Is essentially a type of bill of exchange,

◊   Is drawn upon a specific banker (i.e., a bank),

◊   Must be payable on demand, without delay or a future date.

Thus, a cheque is a written directive from the drawer (account holder) instructing their bank (the drawee) to pay a specific sum of money to the payee (recipient), either to the bearer or to the order of a specific individual or organisation.

1.2.4.1 Essential Characteristics of a Cheque

For a cheque to be considered valid and enforceable under Indian law and banking practice, it must possess certain essential characteristics:

1. Must Be in Writing

A cheque must be written or printed on a paper instrument. Oral cheques or verbal instructions are not valid. Cheques can be handwritten, typed, or printed, and with technological advancement, electronic cheques (e-cheques) are also recognised under the Negotiable Instruments (Amendment and Miscellaneous Provisions) Act, 2002.

Example: If Mr. Raj writes a cheque to pay ₹5,000 to Ms. Priya for services rendered, the instrument must be written, signed, and submitted to the bank.

2. Contains an Unconditional Order

A cheque must contain an unconditional instruction to the bank to pay a certain amount of money. Conditional instructions (e.g., "pay only if the goods are delivered") are not acceptable. The bank does not question the purpose or condition behind the payment.

Example: "Pay Ms. Priya ₹5,000 only if she delivers the parcel" – such a conditional statement renders the cheque invalid.

3. Must Be Signed by the Drawer

The person who issues the cheque (drawer) must sign it to validate the instruction. Unsigned cheques are not considered legally binding.

Example: If a business owner issues a cheque from the company account without signing it, the bank will not process the payment, and the cheque will be returned as "signature missing" or "signature differs".

4. Payable on Demand

A cheque must be payable on demand, meaning the bank is required to pay the amount when the cheque is presented for payment. It cannot specify a future payment date (which would make it a bill of exchange instead).

Example: If a cheque is dated 17th July 2025 and presented on or after that date, the bank is bound to honour it immediately, subject to fund availability and validity.

5. Specific Banker and Amount

A cheque must be drawn upon a specific bank branch where the drawer holds an account. It must also state the exact amount of money to be paid, both in words and figures, to avoid ambiguity.

Example: "Pay Rupees Ten Thousand Only – ₹10,000" clearly indicates the payable amount. If there's a mismatch between the amount in figures and words, the cheque may be dishonoured.

6. Payee Must Be Certain

The person or entity to whom the cheque is to be paid (the payee) must be clearly identified. It can be:

◊   A specific person ("Pay to Ms. Priya")

◊   To the bearer ("Pay to Bearer")

◊   To the order of a person ("Pay to the order of Mr. Arun")

Example: In the cheque "Pay to ABC Enterprises", ABC Enterprises is the payee. If the cheque is lost or stolen and made payable to bearer, it could be misused, which is why 'order' cheques are considered safer.

7. Date

A cheque must be dated. Post-dated cheques (i.e., dated in the future) are valid but can be presented only on or after the specified date. If the date is missing or invalid, the cheque becomes void.

Example: A cheque dated 01-01-2025 can be presented any time after that date within three months (i.e., before 01-04-2025) as per the current validity rules.

8. Amount Specified in Words and Figures

To avoid ambiguity or tampering, cheques require the amount to be written in both words and figures. If there's a discrepancy, the amount written in words is considered final.

Example: If a cheque states ₹5,000 in figures but "Five Hundred Rupees only" in words, the bank will treat the amount as ₹500.

1.2.4.2 Types of Cheques

Cheques come in various forms to serve different purposes and provide varying levels of security. Understanding the types of cheques helps individuals and businesses choose the appropriate mode for payments and avoid potential risks such as fraud or rejection. Below are the commonly used types of cheques in real-world transactions:

1. Bearer Cheque

A bearer cheque is a cheque that is payable to the person who presents it at the bank, regardless of identity. It does not require endorsement and can be transferred simply by handing it over to another person. While convenient, bearer cheques pose a security risk if lost or stolen, as anyone can encash it.

2. Order Cheque

An order cheque is one that is payable only to the specific person whose name appears on the cheque. The bank verifies the identity of the person before releasing the payment, making it more secure than a bearer cheque. To convert a bearer cheque into an order cheque, the drawer simply adds the words "or order" or strikes out the word "bearer".

3. Crossed Cheque

A crossed cheque has two parallel lines on the top left corner or bears the words "A/C Payee" or "Not Negotiable", which directs the bank to credit the amount only to the bank account of the payee. It cannot be encashed over the counter and must be

deposited into a bank account. This type of cheque offers enhanced security and is widely used in business transactions and salary payments.

4. Post-Dated Cheque

A post-dated cheque is one that is issued with a future date, and it becomes valid only on or after that date. Banks are not allowed to process such cheques before the mentioned date, even if they are presented early. Post-dated cheques are commonly used for instalment payments, loan repayments, or scheduled financial commitments.

5. Stale Cheque

A stale cheque is one that is presented for payment after three months from its date of issue. As per RBI guidelines, banks are not allowed to honour such cheques to avoid fraud or misuse. To make the payment, the drawer would need to issue a new cheque with an updated date.

Example 1 : Payment of Salary by Cheque

A small enterprise issues monthly salary cheques to employees. Each cheque includes the employee's name, the amount, and the current date. If the employee deposits it within three months, the cheque will be honoured.

Example 2 : Cheque Dishonour Case

In 2020, a prominent real estate developer was taken to court for issuing a cheque that was dishonoured due to insufficient funds. Under Section 138 of the Negotiable Instruments Act, this is a punishable offence, and the drawer can face imprisonment up to two years or a fine or both.

1.2.4.3 Legal and Banking Perspective

To strengthen the security, reliability, and efficiency of cheque transactions, the Reserve Bank of India (RBI) and the Indian Banks' Association (IBA) have implemented several regulatory frameworks and technological advancements. These measures aim to reduce the risks of cheque fraud, ensure faster clearance, and protect both customers and banks from financial loss. Two of the most important developments in this area are the CTS-2010 Cheque Standards and the Positive Pay System.

1. CTS-2010 Cheque Standards (Cheque Truncation System)

The Cheque Truncation System (CTS) is an image-based cheque clearing system introduced by the RBI to improve the speed and safety of cheque processing. Under CTS-2010 standards, physical cheques are scanned and transmitted electronically to the paying bank, eliminating the need to physically move the cheque from one bank to another. This system reduces cheque clearance time, enhances security against fraud, and improves efficiency in banking operations by using features like watermarking, standardised fonts, MICR (Magnetic Ink Character Recognition) codes, and embedded bank logos.

Example: Before CTS, a cheque deposited in Mumbai but payable in Delhi would take 3–5 days to clear. With CTS, it is now processed within 24 hours, greatly reducing delays.

2. Positive Pay System

Introduced by the RBI in January 2021, the Positive Pay System is a fraud detection tool that enhances the security of high-value cheques. Under this system, the issuer of the cheque must provide key cheque details (like date, payee name, amount, and cheque number) to the bank before the cheque is presented. The bank then cross-verifies the details during clearing, and any mismatch results in the cheque being flagged for further verification or rejection.

This system is mandatory for cheques of ₹50,000 and above in many banks and is particularly useful in preventing forgery, alterations, and duplicate presentations of high-value cheques.

Example: If Mr. Suresh issues a cheque of ₹1 lakh and provides the cheque details to the bank via internet banking or mobile app, the bank will use these details to validate the cheque when it is presented for clearing, ensuring enhanced protection for both the issuer and the payee.

These initiatives reflect the evolving role of the RBI and IBA in promoting digital innovation, risk mitigation, and customer trust in cheque-based payments. They align with global banking best practices and are crucial for maintaining confidence in India's banking infrastructure, especially at a time when financial fraud is increasingly sophisticated.

Cheques remain a significant mode of payment, especially in business and government transactions, despite the rise of digital transfers. Understanding their legal definition and essential characteristics helps prevent fraud, ensures compliance with banking procedures, and facilitates smooth financial transactions. Properly drafted and issued cheques serve as secure, verifiable, and traceable instruments for payments in both personal and institutional contexts.

1.2.4.4 Dishonour of Cheque

A cheque is said to be dishonoured when a bank refuses to process the payment written on the cheque. Dishonour occurs when the bank does not fulfil the instruction of the drawer to pay the cheque amount to the payee, and the cheque is returned unpaid. This situation can arise due to various technical or financial reasons and often leads to legal consequences under Indian law, particularly if the cheque was issued for a legally enforceable debt.

Common Reasons for Dishonour of Cheque

1. **Insufficient Funds** : If the drawer's account does not have enough money to cover the cheque amount, the bank will reject the payment. This is the most frequent reason for cheque dishonour in India. It also forms the primary basis for legal action under Section 138 of the Negotiable Instruments Act, 1881.

2. **Mismatch of Signature :** If the signature on the cheque does not match the specimen signature maintained by the bank, the cheque will be returned. Signature mismatches can happen due to changes in handwriting style, oversight, or forgery concerns. Banks follow strict verification protocols to prevent fraudulent transactions.

3. **Stale or Post-Dated Cheque :** A stale cheque is one that is presented for payment after three months from the date mentioned on it, and it is not honoured as per RBI guidelines. A post-dated cheque is issued with a future date and cannot be cleared before that date. Presenting a cheque outside of the valid date range leads to automatic dishonour.

4. **Stop Payment Instructions :** If the drawer instructs the bank to stop payment of a particular cheque before it is presented, the bank will not process it. While stopping payment is within the drawer's rights, if done with an intention to avoid repayment, it may still lead to legal action under Section 138. This can happen in cases where a dispute arises after the cheque is issued.

5. **Account Closure :** When the drawer's bank account has been closed before the cheque is presented, the cheque cannot be honoured. This is viewed seriously under the law, as it indicates an intentional act of issuing a cheque without a valid account. It is treated as fraudulent behaviour under the Negotiable Instruments Act.

Legal Consequences: Section 138 of the Negotiable Instruments Act, 1881

Section 138 of the Negotiable Instruments Act, 1881 provides for criminal liability in the event of cheque dishonour due to insufficient funds or if the drawer has stopped payment to avoid a legally owed obligation. This section was introduced to enhance trust in commercial dealings and discourage people from issuing cheques irresponsibly.

Key Legal Provisions

i. The cheque must be issued for the discharge of a legal debt or liability.

ii. The cheque must be presented within 3 months from the date mentioned on it.

iii. If dishonoured, the payee must issue a written demand notice to the drawer within 30 days of receiving the return memo from the bank.

iv. The drawer has 15 days to pay the cheque amount after receiving the notice.

v. If payment is not made, the payee can file a criminal complaint within 1 month after the 15-day period.

Punishment Under Section 138:

◊   Imprisonment for a term up to 2 years, or

◊   Fine up to twice the amount of the cheque, or

◊   Both imprisonment and fine

This law treats cheque dishonour as a criminal offence to instill financial discipline, particularly in business and credit transactions.

Case Study: M/s Meters and Instruments Pvt. Ltd. vs. Kanchan Mehta (2017)

In this landmark case, the Supreme Court of India adopted a progressive and reformative approach towards cheque dishonour matters. The Court recognised that a large number of cases under Section 138 were burdening the criminal justice system and delaying justice.

Key Observations of the Court

◊ The objective of Section 138 is compensation rather than punishment.

◊ Courts should encourage compounding of offences (i.e., settling disputes between parties) at all stages of legal proceedings.

◊ The use of mediation and summary trial mechanisms should be promoted to ensure speedy resolution.

Significance

The judgment encouraged a compromise-based approach in cheque bounce cases, promoting reconciliation between parties and reducing the pressure on Indian courts. It also reinforced the idea that not all dishonour cases deserve criminal prosecution if the matter can be resolved amicably.

Cheque dishonour is a serious financial and legal issue governed strictly under Indian law. While there may be various reasons for a cheque being dishonoured, the most severe consequences arise when it is due to insufficient funds or deliberate avoidance of payment. The legal framework under Section 138 of the Negotiable Instruments Act ensures accountability, while recent judicial trends are focusing on decriminalisation and settlement, especially in cases involving small businesses and individuals. Understanding these provisions helps ensure compliance, promotes responsible financial behaviour, and protects the interests of both drawers and payees in commercial transactions.

1.2.4.5 Payment in Due Course

Payment in Due Course is a crucial legal concept under the Negotiable Instruments Act, 1881, particularly significant for banks and financial institutions involved in cheque transactions. It refers to a payment made in accordance with the law and banking norms, which protects the paying party, usually a bank, from liability, even if the cheque has a defective title or was obtained improperly.

According to Section 10 of the Negotiable Instruments Act, 1881,

"Payment in due course means payment made in accordance with the apparent tenor of the instrument, in good faith and without negligence, to any person in possession thereof under circumstances which do not afford a reasonable ground for believing that he is not entitled to receive payment of the amount therein mentioned."

This definition outlines three key conditions that must be satisfied for a payment to qualify as being made "in due course."

1. Payment in Accordance with the Apparent Tenor of the Instrument

The payment must be made as per the face value and conditions of the instrument (in this case, the cheque). This includes checking that:

◊ The date is valid and the cheque is not stale or post-dated.

◊ The amount is clearly stated.

◊ The document appears authentic and has not been altered.

Example: If a bank receives a cheque dated today with no signs of tampering and all fields properly filled, paying it as presented is consistent with the apparent tenor of the instrument.

2. Payment Made in Good Faith and Without Negligence

The bank or person making the payment must do so honestly, without any intention to deceive or facilitate fraud. Furthermore, due diligence must be exercised to ensure that the cheque has not been forged, altered, or suspicious in nature.

Example: If a bank notices an erasure or overwriting on the amount field but still proceeds with payment, it may not be considered payment in due course due to negligence.

3. Payment to the Person in Possession of the Cheque

The cheque must be paid to the current lawful holder or bearer of the cheque. This person must be in actual possession, and there should be no apparent reason to suspect that he or she is not entitled to receive the money.

Example: If a cheque marked "Pay to Rakesh or bearer" is presented by a third party holding it legally, and the bank pays the amount after verifying all details, the payment is considered to be made to the rightful possessor.

Legal Protection to the Banker

If a banker makes a payment fulfilling all the above three conditions, he is protected from liability even if it is later discovered that the cheque was stolen or the person who presented it had a defective title. This protection encourages the smooth functioning of financial transactions and reassures banks that they will not be held responsible for unintended errors, provided they act in accordance with the law and with due diligence.

Example : Suppose Mr. A issues a bearer cheque to Mr. B, who loses it. Mr. C, an unknown third party, finds it and presents it to the bank. If the cheque appears genuine and untampered, and the bank pays Mr. C without negligence, the bank will be protected under Section 10, even though Mr. C had no rightful claim.

Payment in Due Course is a vital concept that ensures fairness and operational confidence in banking transactions involving cheques and other negotiable instruments. It balances the rights of cheque holders with the duties and liabilities of banks. By following the proper procedure including verifying the instrument, acting in good faith, and ensuring payment to the correct possessor, banks can avoid legal repercussions and contribute to a secure financial environment.

1.2.4.6 Crossing of Cheques

Crossing of a cheque is a method used to instruct the paying bank that the cheque should not be encashed directly at the counter. Instead, it must be deposited into a bank account, thereby increasing the security of the transaction. This is typically done by drawing two parallel lines on the top-left corner of the cheque and may include additional instructions such as the name of a bank or the phrase "Account Payee."

Crossing acts as a protective mechanism to reduce the risk of misuse, theft, or fraud, especially when cheques are sent by post or handled by third parties.

1.2.4.6.1 Types of Cheque Crossing

Cheque crossings are classified into three main types, each offering a different level of security and restriction on the method of encashment.

1. General Crossing

A cheque is said to be generally crossed when two parallel transverse lines are drawn across its top-left corner. These lines may or may not include the words "& Co." or "Not Negotiable." The cheque cannot be encashed over the counter and must be deposited into a bank account. This provides a basic level of security by ensuring that only someone with a bank account can receive the funds.

Example: If Mr. Ravi issues a cheque to Ms. Anita with general crossing, Ms. Anita must deposit it in her bank account. She cannot go to the bank counter and demand cash payment directly.

2. Special Crossing

A cheque is specially crossed when the name of a specific bank is written between the two parallel lines. This directs the paying bank to honour the cheque only when it is presented through the specified bank. The cheque becomes more restrictive, as it must be deposited through the mentioned bank only. Even if the payee has accounts in multiple banks, the payment will be routed only through the named one. It adds an extra layer of safety, especially in business transactions where routing through a specific bank is desired.

Example: A cheque crossed with "HDFC Bank Ltd." between the lines can be cleared only if presented through HDFC Bank or its clearing branch. This ensures that even if the cheque falls into the wrong hands, it cannot be deposited elsewhere.

3. Account Payee Crossing (Restrictive Crossing)

A cheque is crossed as Account Payee when the words "A/c Payee" or "Account Payee Only" are written between the two parallel lines. This is the most restrictive form of crossing. The cheque amount can be credited only to the bank account of the payee whose name is written on the cheque. It cannot be endorsed or transferred to any third party. This ensures maximum protection against fraud and unauthorised negotiation of the cheque.

Example: If a cheque is issued in favour of "XYZ Traders" with "A/c Payee" written between the lines, the cheque can be deposited only into XYZ Traders' bank account, not even into a partner's personal account.

Purpose of Crossing a Cheque

The primary objective of crossing is to enhance the safety and traceability of the cheque transaction. Here's how:

i.   Prevents misuse: A crossed cheque cannot be stolen and cashed easily at the counter.

ii.   Ensures accountability: Payments can be traced back to the receiver through bank account records.

iii. Reduces fraud: Particularly in the case of lost or stolen cheques, unauthorised encashment is avoided.

iv.   Legal safeguard: Banks are protected if they follow the crossing instructions correctly.

Crossing of cheques is a simple but effective mechanism to make cheque payments more secure and controlled. Whether it is a general crossing, special crossing, or account payee crossing, each type serves a unique purpose in protecting the drawer and ensuring the funds reach the intended recipient. In the modern banking system, especially with the prevalence of remote cheque clearing and online transactions, crossing continues to be a critical safeguard against financial fraud and mismanagement.

1.2.4.7 Endorsement of Cheques

Endorsement refers to the act of the payee or holder signing on the back of a negotiable instrument, such as a cheque, with the intention of transferring the rights or title of that cheque to another person. It is governed under Section 15 of the Negotiable Instruments Act, 1881.

When a cheque is endorsed, it becomes negotiable, i.e., the right to receive the payment can pass from one person to another. The person who signs and transfers the cheque is called the endorser, and the person to whom it is transferred is called the endorsee.

Essentials of a Valid Endorsement

For an endorsement to be legally valid:

i.   It must be written on the instrument itself (or on an attached slip called an **allonge**).
ii.   It must be signed by the endorser.
iii.   The signature must match the name of the payee or previous endorser.
iv.   Endorsement must be made with the intention of transferring ownership.

1.2.4.7.1 Types of Endorsements

There are several types of endorsements, each serving a different purpose in the negotiability and security of the instrument.

1. Blank Endorsement

An endorsement in which the endorser simply signs his or her name without specifying the name of the endorsee. The cheque becomes payable to bearer, and any person in possession of the cheque can claim the amount. It offers maximum negotiability but less security, as possession of the cheque is enough to claim payment.

Example: If Ms. A receives a cheque and signs her name on the back without writing anything else, it becomes a blank endorsement. Anyone holding the cheque can now present it for payment.

2. Full Endorsement (Special Endorsement)

The endorser writes "Pay to [Name of Endorsee]" and then signs underneath. The cheque becomes payable only to the person named (endorsee), and the cheque cannot be encashed by any other person unless further endorsed. Offers better security than blank endorsement.

Example: Mr. A writes on the back of a cheque: "Pay to Mr. B or order" and signs below. This is a full endorsement, and only Mr. B can negotiate or deposit the cheque further.

3. Restrictive Endorsement

. This type of endorsement restricts the further negotiation of the cheque. The cheque can be deposited only into the account of the named endorsee and cannot be further endorsed or transferred. Ensures that the amount reaches the intended person or account, often used for greater financial control.

Example: "Pay to Mr. Ramesh only" — signed by Mr. Suresh. In this case, Mr. Ramesh cannot transfer the cheque to anyone else

4. Conditional Endorsement

An endorsement that places a condition on the payment of the cheque. The endorsement becomes valid only if the specified condition is fulfilled. The bank may

disregard the condition and still honour the cheque, but in disputes between endorser and endorsee, the condition becomes important. Used when the payment is dependent on an event or action.

Example : Mr. A writes: "Pay to Mr. B if he delivers the documents" and signs below. This is a conditional endorsement.

Table 2.1.1. Comparison of Types of Endorsements

Types of Endorsement	Description	Negotiability	Security Level	Example
Blank Endorsement	Signature only, no name of endorsee	High	Low	"(Signature)"
Full Endorsement	Endorsee's name mentioned with signature	Medium	Medium	"Pay to Mr. B or order – (Signature)"
Restrictive Endorsement	Restricts further transfer	Low	High	"Pay to Mr. B only – (Signature)"
Conditional Endorsement	Payment subject to condition	Medium	Medium	"Pay to Mr. B if goods received – (Sign)"

1.2.4.7.2 Legal Importance of Endorsement

i.   Transfer of Title: Enables legal transfer of the right to receive payment.

ii. Tracing Ownership: Signatures on endorsements help identify the path of ownership.

iii. Holder in Due Course: A person who receives a properly endorsed cheque in good faith becomes a holder in due course and gains legal protection under the law.

Endorsement is a fundamental concept in the handling of negotiable instruments like cheques. Understanding the types of endorsements—blank, full, restrictive, and conditional—helps in choosing the right level of negotiability and security. While blank endorsements allow easy transferability, full and restrictive endorsements provide better control and protection over the transaction. In business and banking, correct endorsement practices are crucial to ensure legal validity, prevent fraud, and facilitate smooth financial dealings.

◊ Banker and Customer Relationship: Based on mutual trust, legality, and defined roles like debtor–creditor, agent–principal, and trustee–beneficiary.

◊ Types of Bank Accounts: Savings, current, fixed deposit, recurring deposit, and NRI accounts cater to various customer needs and financial goals.

◊ Cheque Essentials: A cheque must be written, signed, payable on demand, and addressed to a specific banker and payee.

◊ Cheque Dishonour: Commonly due to insufficient funds or mismatched signatures; punishable under Section 138 of the NI Act.

◊ Crossing and Endorsement: Enhance cheque security and negotiability; types include general, special, account payee crossing, and various endorsements like blank, full, restrictive, and conditional.

Objective Questions

1. Who is considered a customer in banking law?
2. Under which Act is the definition of banking given?
3. Which case highlighted the duty of a bank to maintain secrecy?
4. What is the validity period of a cheque in India?
5. What type of account is suitable for businesses?
6. What type of cheque can be encashed by anyone holding it?
7. Which form of cheque crossing allows deposit only into the payee's account?
8. What section of the Negotiable Instruments Act deals with cheque dishonour?
9. What is the maximum imprisonment for cheque bounce under Section 138?
10. What system electronically clears cheques using scanned images?
11. What is the name of the fraud-prevention tool introduced by RBI in 2021?
12. What type of endorsement limits further negotiation of a cheque?

Answers

1. Account holder
2. Banking Regulation Act
3. Tournier case
4. Three months
5. Current account
6. Bearer cheque
7. Account payee
8. Section 138
9. Two years
10. Cheque Truncation System
11. Positive Pay System
12. Restrictive endorsement

Self-Assessment Questions

1. Explain the relationship between banker and customer
2. What are the different types of bank accounts?
3. Discuss the types of endorsement
4. Explain the types of cheque crossing
5. Explain the types of cheques with examples
6. Banker act as an agent of the customer. Justify answer with examples?

Assignments

1. Explain the general and special legal relationships between a banker and a customer with examples.
2. Discuss the different types of bank accounts and their uses in personal and business finance.
3. Describe the essential features of a valid cheque as per the Negotiable Instruments Act.

4. Examine the reasons for dishonour of cheques and the legal consequences under Section 138.

5. Explain the meaning and types of cheque endorsements with examples.

6. Visit a nearby bank or its website and collect brochures or online information about savings, current, and FD accounts. Compare their features.

7. Design a sample cheque with general, special, and account payee crossings using blank formats.

8. Write a case analysis of M/s Meters and Instruments vs. Kanchan Mehta (2017) explaining the Supreme Court's observations on cheque dishonour cases.

9. Draft a sample legal notice under Section 138 of the NI Act for a dishonoured cheque.

10. Interview a bank official (in person or virtually) to understand how endorsements and cheque clearing are handled in practice.

Reference

1. Indian Parliament. (1881). *Negotiable Instruments Act, 1881*. Government of India.

2. Reserve Bank of India. (2021). *RBI guidelines on Positive Pay System*. https://www.rbi.org.in

3. Indian Parliament. (1949). *Banking Regulation Act, 1949*. Government of India.

4. Tannan, M. L. (2021). *Banking Law and Practice in India* (28th ed.). LexisNexis.

5. Gopalakrishnan, R. (2019). *Banking Theory and Practice*. Himalaya Publishing House.

6. Shekhar, K. C., & Shekhar, L. (2018). *Banking Theory and Practice* (22nd ed.). Vikas Publishing.

7. Jain, R. K., & Jain, S. C. (2022). *Modern Banking and Insurance*. Kalyani Publishers.

8. Muralidharan, S. (2020). *Modern Banking: Theory and Practice*. PHI Learning.

9. Kapoor, N. D. (2019). *Elements of Mercantile Law*. Sultan Chand & Sons.

10. Supreme Court of India. (2017). *M/s Meters and Instruments Pvt. Ltd. vs. Kanchan Mehta*, Civil Appeal No. 17360 of 2017.
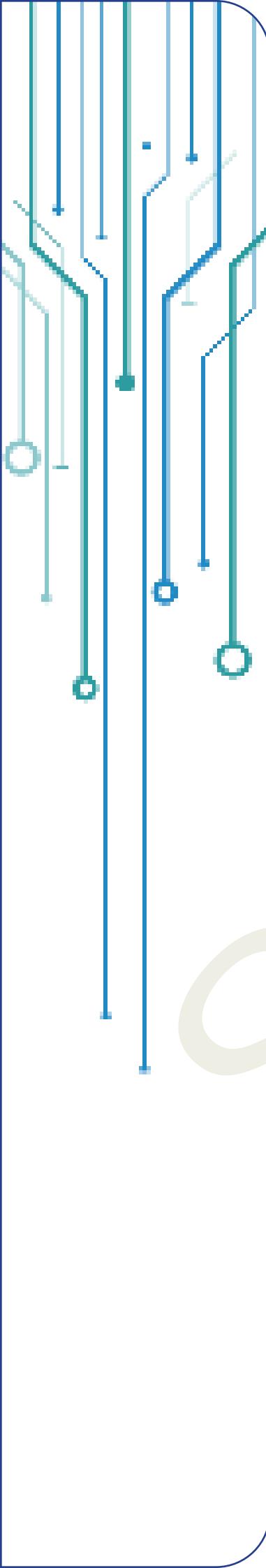
Suggested Reading

1. Tannan, M. L. (2021). *Banking Law and Practice in India* (28th ed.). LexisNexis.

2. Gopalakrishnan, R. (2019). *Banking Theory and Practice*. Himalaya Publishing House.

2

BLOCK

Banking Regulation

Unit ①

Banking Practice

Learning Outcomes

After completing this unit, the learner will be able to;

◊ explain the legal and institutional framework governing debt recovery through the DRT Act and SARFAESI Act

◊ familiarise the evolution, features, and significance of Basel Reforms in the Indian banking sector

◊ interpret capital adequacy norms and calculate CRAR using Tier 1 and Tier 2 capital components

◊ assess causes and implications of Non-Performing Assets (NPAs) and suggest appropriate management strategies

Prerequisites

A small business owner named Ramesh who borrows ₹15 lakhs from a public sector bank to expand his garment shop. Due to unforeseen events like a market slowdown and supply chain issues, he struggles to repay the loan. As months pass and payments are delayed, the bank must act quickly to recover the money. But going through regular civil courts takes years. This is where laws like the Debt Recovery Tribunal (DRT) Act and the SARFAESI Act come in. They allow banks to recover such loans faster, either by approaching special tribunals or by directly selling the borrower's assets without court delays.

Just as it is important for banks to recover money, it's equally vital that they remain strong and prepared for financial stress. That's why there are international standards like the Basel norms, which require banks to keep enough capital aside to face risks. In this unit, you will explore the major practices and legal tools used by banks to manage risk, recover loans, handle bad debts (called NPAs), and follow guidelines to stay financially stable. Understanding these topics will help you see how India's banking system works to protect depositors, support businesses, and maintain economic growth.

Keywords

CRAR (Capital to Risk-Weighted Assets Ratio), Non-Performing Assets (NPA), SARFAESI Act, Debt Recovery Tribunal (DRT), Basel Reforms

Discussion

2.1.1 Recovery of Debts Due to Banks and Financial Institutions Act, 1993 (DRT Act)

The Recovery of Debts Due to Banks and Financial Institutions Act, 1993, commonly referred to as the DRT Act, was enacted by the Parliament of India to streamline and accelerate the process of recovering debts owed to banks and financial institutions. Prior to the enactment of this legislation, recovery proceedings were carried out through regular civil courts, which were overburdened and led to substantial delays, adversely impacting the financial health and liquidity of banks and financial institutions.

This Act came into force on 24th June 1993, and its primary goal was to establish a special judicial mechanism to handle cases relating to the recovery of large loan amounts efficiently and effectively.

2.1.1.1 Key Objectives

The main objective of the Recovery of Debts and Bankruptcy Act (RDB Act), 1993, is to provide for the expeditious adjudication and recovery of debts due to banks and financial institutions. It establishes Debts Recovery Tribunals (DRTs) and Debts Recovery Appellate Tribunals (DRATs) to handle these matters, streamlining the process and aiming to reduce the burden on traditional civil courts. The following are the important objectives :

1. Speedy Recovery of Loans

One of the primary objectives of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 (commonly known as the DRT Act), is to enable the expeditious recovery of loans advanced by banks and financial institutions. Before the enactment of this legislation, debt recovery suits were filed in regular civil courts, often resulting in significant delays sometimes stretching for years due to the procedural rigour and pendency of cases. The DRT Act addresses this concern by establishing a time-bound legal framework that facilitates the quick adjudication of cases involving defaulted loans. This in turn enhances the credit recovery ratio and helps maintain the liquidity and financial health of lending institutions.

Under Section 17 of the Act, Debt Recovery Tribunals (DRTs) are empowered to adjudicate applications made by banks and financial institutions for the recovery of debts that amount to ₹10 lakh or more. This threshold ensures that only substantial claims are

brought before the DRTs, thereby allowing for focused and efficient resolution of high-value non-performing assets (NPAs). This mechanism also encourages greater financial discipline among borrowers, as the repercussions for default are swifter and more direct under the DRT framework.

2. Establishment of Debt Recovery Tribunals (DRTs)

To support the objective of fast-track debt recovery, the Act provides for the creation of Debt Recovery Tribunals (DRTs) and Debt Recovery Appellate Tribunals (DRATs). These quasi-judicial bodies are exclusively dedicated to resolving loan recovery cases, which allows them to build expertise in handling complex financial disputes. DRTs are presided over by a Presiding Officer, who is typically qualified to be a District Judge, while DRATs are headed by a Chairperson, usually a former High Court judge.

The procedures followed by these tribunals are less formal than those of traditional civil courts, enabling quicker processing of applications. The DRTs possess powers equivalent to civil courts under the Code of Civil Procedure, 1908, including summoning witnesses, examining evidence, and ordering the attachment and sale of properties. As of 2023, 39 DRTs and 5 DRATs are operational across India, ensuring regional access and timely resolution of loan default cases. These tribunals have played a crucial role in reducing the volume of pending debt-related litigations and improving the overall debt recovery climate in the country.

3. Reduction of Burden on Civil Courts

Another significant aim of the DRT Act is to reduce the burden on conventional civil courts, which were historically overloaded with commercial and financial litigation. By vesting the jurisdiction for recovery of loans with specialised tribunals, the Act relieves civil courts from adjudicating such cases. This allows the regular judicial system to focus more on general civil disputes, criminal trials, and other non-financial matters, thereby enhancing the overall efficiency of the Indian judiciary.

According to Section 18 of the Act, civil courts have no jurisdiction over matters that fall within the purview of DRTs. This exclusivity ensures that there is no duplication of proceedings and that recovery-related disputes are addressed by a competent and focused judicial forum. The specialised knowledge and procedures followed by DRTs have led to a more consistent and uniform approach to debt recovery jurisprudence, promoting legal certainty and investor confidence in the financial system.

4. Strengthening Financial Stability

While not expressly stated in the original Act, a broader implication of the DRT framework is the strengthening of financial discipline and systemic stability. When banks and financial institutions are assured of an efficient mechanism to recover dues, they are more confident in extending credit, which boosts investment and economic growth. Furthermore, the functioning of DRTs contributes to reducing the incidence of non-performing assets (NPAs) by serving as a deterrent to willful defaulters.

2.1.1.2 Salient Features

1. Applicability

The DRT Act, 1993, applies specifically to cases involving the recovery of debts owed to banks and public financial institutions, provided the amount involved is ₹10 lakhs or more. This monetary threshold ensures that the Debt Recovery Tribunals (DRTs) deal with high-value defaults, thereby maximising the use of their specialised infrastructure and judicial expertise. Smaller debt recovery cases continue to be handled by civil courts or under other legal mechanisms such as Lok Adalats. The inclusion of both public and private sector banks, as well as notified financial institutions under the Act, reflects its broad scope in the Indian financial system. Over time, through amendments, the Act also expanded to accommodate recovery applications from asset reconstruction companies (ARCs) and in some instances, non-banking financial companies (NBFCs), when permitted.

2. Exclusive Jurisdiction

Under Section 18 of the Act, the jurisdiction of civil courts is explicitly barred in matters that fall within the purview of DRTs. This means that once a case qualifies for adjudication under the DRT Act, no civil court has the authority to entertain or try such matters. The objective of granting exclusive jurisdiction to DRTs is to avoid duplication of proceedings, eliminate delays associated with civil litigation, and ensure consistency in decision-making related to debt recovery. This provision has helped banks avoid prolonged litigation cycles and has brought greater certainty to enforcement processes. The DRTs also have jurisdiction to decide counterclaims and set-offs filed by the borrowers, thereby giving a holistic platform for resolution.

3. Tribunal Composition

The DRT Act provides for a two-tier tribunal structure comprising Debt Recovery Tribunals (DRTs) at the primary level and Debt Recovery Appellate Tribunals (DRATs) at the appellate level. A DRT is headed by a Presiding Officer, who is appointed by the Central Government and is typically a judicial officer qualified to be a District Judge. These Presiding Officers bring legal expertise and are entrusted with ensuring fair and speedy disposal of cases.

At the appellate level, the DRAT is headed by a Chairperson, usually someone qualified to be a Judge of a High Court. The DRAT serves as a forum for appeals against the orders passed by the DRT. Both tribunals function under the administrative control of the Department of Financial Services, Ministry of Finance. Their appointments, qualifications, and terms of service are governed by the rules framed under the DRT Act.

4. Appeals and Procedure

The DRT Act lays down a simple and efficient procedure for filing and adjudicating claims. Any party aggrieved by a decision of the DRT has the right to appeal before

the DRAT within 30 days from the date of the order. The appellate tribunal has the discretion to condone delays if sufficient cause is shown. However, as a precondition for filing an appeal, the borrower must deposit 75% of the debt amount as determined by the DRT, although the DRAT has the authority to waive or reduce this amount for reasons recorded in writing.

Unlike civil courts, the tribunals are not bound by the Code of Civil Procedure (CPC). Instead, they are guided by principles of natural justice, allowing them to adopt a more flexible and case-specific approach. This helps streamline the litigation process, reducing procedural bottlenecks and ensuring speedier resolution.

5. Powers Similar to Civil Courts

Despite the simplified procedure, DRTs are vested with powers similar to those of a civil court under the Civil Procedure Code, 1908 for the purpose of conducting hearings and enforcement. These powers include:

◊   Summoning and enforcing the attendance of witnesses.

◊   Requiring the discovery and production of documents.

◊   Receiving evidence on affidavits.

◊   Issuing commissions for examination of witnesses or documents.

◊   Ordering attachment and sale of movable and immovable property of the defaulter to recover dues.

These quasi-judicial powers ensure that DRTs are not merely advisory forums but have the legal teeth necessary to enforce decisions and secure compliance. In fact, the Recovery Officers attached to the DRTs have powers equivalent to those of an Income Tax Recovery Officer to carry out coercive recovery measures such as arrest, detention, and attachment of property.

6. Electronic Filing and Digitisation

Recent reforms have promoted e-filing of applications, video conferencing of hearings, and digital access to case status to make the process more transparent and accessible.

7. Time-Bound Disposal

While the Act does not prescribe rigid timelines, several judicial pronouncements and government circulars emphasise that DRTs must endeavour to dispose of applications within 180 days to ensure expeditious recovery.

8. Integration with SARFAESI and IBC

The DRT mechanism complements other major legislations like the SARFAESI Act, 2002 and the Insolvency and Bankruptcy Code (IBC), 2016, particularly in cases where borrowers challenge enforcement proceedings initiated under those laws.

Amendments and Updates

◊ The Act was amended several times to strengthen its enforcement mechanisms.

◊ In 2016, the Act was renamed as the Recovery of Debts and Bankruptcy Act, 1993, and incorporated certain provisions in line with the Insolvency and Bankruptcy Code (IBC), 2016.

◊ The 2016 amendment also brought about several reforms to digitise tribunal processes, tighten timelines, and improve the efficiency of debt recovery.

2.1.1.3 Functions of DRT Act

The DRT Act typically refers to the Recovery of Debts and Bankruptcy Act, 1993 (formerly known as the Recovery of Debts Due to Banks and Financial Institutions Act, 1993) in India. The act primarily deals with the establishment and functions of Debt Recovery Tribunals (DRTs) to expedite the recovery of debts owed to banks and financial institutions.

Here are the main functions of DRTs under the DRT Act:

1. Adjudication of Debt Recovery Cases

DRTs are empowered to adjudicate applications from banks and financial institutions for the **recovery of debts exceeding Rs 20 lakh**. They ensure speedy resolution of such cases, avoiding delays in civil courts.

2. Issuance of Recovery Certificates

After hearing both parties, if the tribunal finds the debt to be recoverable, it issues a Recovery Certificate to the Recovery Officer, specifying the amount due. This certificate acts like a decree and is executable by the Recovery Officer.

3. Execution of Recovery

DRTs can direct the Recovery Officer to:

1. Attach and sell the property of the debtor.
2. Arrest and detain the debtor (in specific cases).
3. Appoint receivers for management of debtor's properties.

4. Hearing Appeals

Appeals against the orders of DRTs can be made to the Debt Recovery Appellate Tribunal (DRAT).

5. Power of Civil Court

DRTs have powers equivalent to a civil court under the Code of Civil Procedure (CPC), such as:

1. Summoning witnesses,
2. Requiring document production,
3. Taking evidence on oath,
4. Issuing commissions, etc.

6. Handling of Counterclaims and Set-offs

Defendants (borrowers) can file counterclaims or set-offs in response to claims filed by banks.

7. Support in Insolvency Proceedings

Post-amendments, DRTs also handle **individual insolvency and bankruptcy** matters under the **Insolvency and Bankruptcy Code (IBC),** 2016, for personal guarantors to corporate debtors.

Case Studies

Case Study 1: Kingfisher Airlines Case (Vijay Mallya Loan Default)

The Kingfisher Airlines case is among the most well-known examples of large-scale corporate loan default in India. The airline, promoted by liquor baron Vijay Mallya, accumulated massive debts to a consortium of 17 Indian banks, led by the State Bank of India (SBI). The total outstanding loan amount ballooned to over ₹9,000 crore, much of which turned into Non-Performing Assets (NPAs) due to prolonged defaults.

In 2013, the banks filed a recovery application with the Debt Recovery Tribunal (DRT) Bengaluru under the provisions of the DRT Act. After lengthy legal proceedings, in January 2017, the DRT issued a landmark order in favour of the banks, allowing them to recover dues by attaching and selling Mallya's properties. This included both domestic assets and foreign holdings. The tribunal declared Vijay Mallya a "willful defaulter" and directed him to repay the loans.

The case, though prolonged due to cross-border legal complications (including Mallya's departure to the UK and extradition battles), highlighted the vital role of DRTs in handling complex, high-value corporate debt recovery. It also led to further institutional strengthening, such as the introduction of more stringent rules under the Fugitive Economic Offenders Act, 2018 and increased synergy between DRTs, the Enforcement Directorate, and other recovery mechanisms like SARFAESI and IBC.

Case Study 2: PNB vs. Rotomac Global Pvt. Ltd.

Another notable case that demonstrates the use of the DRT mechanism is the Punjab National Bank (PNB) vs. Rotomac Global Pvt. Ltd. case. Rotomac, a well-known pen manufacturer owned by the Kothari family, was accused of defaulting on loans worth over ₹3,695 crore from a consortium of banks, including PNB, Bank of India, and Bank of Baroda.

In 2018, following allegations of willful default and loan fraud, Punjab National Bank filed a petition with the Debt Recovery Tribunal, Kanpur, seeking legal recourse for the recovery of outstanding dues. The DRT admitted the case and allowed proceedings for the attachment and auction of Rotomac's properties and bank accounts. Additionally, enforcement agencies like the Central Bureau of Investigation (CBI) and the Enforcement Directorate (ED) conducted investigations alongside the DRT proceedings, resulting in the seizure of various assets and subsequent arrests.

This case underscored the usefulness of the DRT framework in coordinating with other regulatory and enforcement bodies to ensure asset recovery. It also brought attention to the role of internal banking controls and due diligence failures, which were later addressed through reforms in bank auditing and risk assessment protocols.

Case Study 3: Deccan Chronicle Holdings Ltd.

Another illustrative case is that of Deccan Chronicle Holdings Ltd. (DCHL), a media house that defaulted on loans from several banks, including Canara Bank, Axis Bank, and IDBI Bank, amounting to over ₹4,000 crore. The banks approached the DRT in Hyderabad to initiate proceedings for debt recovery.

The DRT, after reviewing the application, ordered the attachment of DCHL's assets, including properties and business holdings. This case illustrated the scope of DRT jurisdiction over corporate borrowers in diverse sectors, including media and publishing. It also showed how DRT orders could be used in conjunction with proceedings under the SARFAESI Act, wherein secured creditors can take possession of and sell collateral assets independently of DRT verdicts.

Key Takeaways from the Case Studies

These cases demonstrate that DRTs play a crucial role in high-stakes loan recovery, especially where large sums are involved and corporate borrowers are either untraceable, non-cooperative, or under investigation.

1. DRT proceedings are instrumental in enabling banks to recover dues through judicial enforcement, especially when borrowers challenge SARFAESI actions or when the recovery requires legal adjudication of complex issues.

2. Despite procedural delays and appeals, DRT orders form a strong legal basis for seizing, attaching, and liquidating assets, thereby contributing to the resolution of bad loans and reduction of NPAs.

3. These real-life cases not only validate the relevance and necessity of the DRT Act but also underscore the need for continuous reforms to strengthen tribunal infrastructure, increase efficiency, and ensure faster resolution of debt recovery proceedings in India's evolving financial environment.

2.1.2 SARFAESI Act, 2002

The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI Act) is a landmark legislation enacted by

the Government of India to empower banks and financial institutions to recover non-performing assets (NPAs) efficiently, without requiring court intervention. Before the SARFAESI Act came into effect, lenders had to approach civil courts or Debt Recovery Tribunals (DRTs) for the enforcement of security interests, which caused significant delays in the recovery of bad loans.

This Act came into force on 21st June 2002, following the recommendations of the Narasimham Committee II and the Andhyarujina Committee, which identified the need for faster asset recovery and legal enforcement in banking.

2.1.2.1 Objectives of the SARFAESI Act

1. **Allow Banks to Take Possession of Secured Assets:** One of the core objectives of the SARFAESI Act is to empower banks and financial institutions to take physical possession of the mortgaged or hypothecated assets of a defaulting borrower and sell them to recover dues. This skips the long-winded litigation process and enables lenders to act directly and quickly.

2. **Enforce Security Interest Without Court Involvement:** The Act authorises banks to enforce security interests without the need to approach civil courts or DRTs in most cases. This legal provision significantly reduces delays and improves the recovery rate of NPAs, thereby strengthening the financial sector.

3. **Facilitate Asset Reconstruction by Asset Reconstruction Companies (ARCs):** The Act also provides a regulatory framework for the formation and operation of Asset Reconstruction Companies (ARCs), which can buy bad loans from banks and undertake reconstruction or recovery on their behalf. This mechanism helps clean bank balance sheets and support financial restructuring of distressed assets.

2.1.2.2 Key Features

1. **Securitization and Reconstruction:** The act facilitates the securitization and reconstruction of financial assets, allowing for the transfer of NPAs to asset reconstruction companies.

2. **Enforcement of Security Interest:** It provides a framework for lenders to enforce their security interest (collateral) when borrowers default on secured loans.

3. **No Court Intervention (in many cases):** The SARFAESI Act allows lenders to initiate recovery proceedings without going to court, streamlining the process.

4. **Auction of Assets:** Lenders can seize and auction off the secured assets (like property) to recover the outstanding loan amount.

5. **Focus on NPAs:** The act specifically targets non-performing assets, which are loans where the borrower has defaulted on payments.

6. **Applicability:** It applies primarily to secured loans where the borrower has pledged assets as collateral.

2.1.2.3 Key Provisions of the SARFAESI Act

1. Applicability

The SARFAESI Act, 2002 is applicable only to secured loans, meaning loans that are backed by tangible collateral such as immovable property (e.g., land or buildings), movable assets (e.g., vehicles or machinery), or financial assets (e.g., receivables). This ensures that banks or financial institutions have a charge over a specific asset, which can be enforced in case of default. However, the Act does not apply to unsecured loans, where no collateral has been provided. It also excludes debts involving amounts less than ₹1 lakh, or where the outstanding due is less than 20% of the principal loan amount, in order to prevent the misuse of stringent enforcement provisions for small defaults. Importantly, the Act excludes agricultural land from its scope, in line with the constitutional protection of farmers' rights and to prevent displacement of agriculturists from their livelihood sources.

2. Section 13 – Enforcement of Security Interest

One of the most powerful aspects of the SARFAESI Act lies in Section 13, which provides a legal procedure for enforcing the security interest. Under Section 13(2), when a borrower defaults on a secured loan, the lender can issue a notice of demand, asking for repayment of the dues within 60 days. If the borrower fails to comply, the lender may proceed under Section 13(4), which empowers the bank or financial institution to take direct action without court intervention. Under this section, the lender can take possession of the secured asset, such as a house, land, or industrial unit; sell or lease the asset to recover dues through public auction or private sale; and even appoint a manager or take over the borrower's business operations if it aids in preserving or realising the asset's value. This provision significantly reduces the time and cost of recovery, allowing banks to address rising non-performing assets (NPAs) in a more proactive and structured way.

3. Role of Asset Reconstruction Companies (ARCs)

A distinctive feature of the SARFAESI Act is its provision for the establishment and functioning of Asset Reconstruction Companies (ARCs). As per Section 3 of the Act, ARCs must be registered with the Reserve Bank of India (RBI) to operate. These companies are authorised to purchase bad loans or NPAs from banks and financial institutions, often at a discounted rate, and then take steps to restructure the debt, recover dues, or enforce security under the provisions of the Act. The existence of ARCs enables banks to clean up their balance sheets and transfer the task of recovery to specialised entities. Prominent ARCs in India include Asset Reconstruction Company (India) Ltd (ARCIL) - India's first ARC and Edelweiss ARC, among others. These organisations play a vital role in the financial ecosystem by recycling distressed assets and promoting credit discipline in the economy.

These key provisions demonstrate how the SARFAESI Act, 2002 functions as a powerful legal tool to expedite loan recovery, reduce bad debts, and ensure stability in

the banking and financial sectors while also incorporating safeguards for borrowers and maintaining alignment with constitutional protections.

Case 1: United Bank of India vs. Satyawati Tandon (2010)

The United Bank of India vs. Satyawati Tandon (2010) case is widely regarded as a landmark judgment that shaped the judicial approach to the SARFAESI Act and clarified the hierarchy of legal remedies. In this case, United Bank of India had granted a loan to Satyawati Tandon and her guarantors. Upon default, the bank issued a demand notice under Section 13(2) of the SARFAESI Act, initiating the process to recover the outstanding amount by enforcing its security interest. In response, the borrower filed a writ petition before the Allahabad High Court, challenging the bank's actions and seeking protection from coercive recovery measures.

The High Court granted an interim injunction, restraining the bank from proceeding further. However, the matter escalated to the Supreme Court of India, which delivered a significant verdict. The apex court held that borrowers must first exhaust all alternative statutory remedies, such as approaching the Debt Recovery Tribunal (DRT) under Section 17 of the Act, before invoking the writ jurisdiction of High Courts under Article 226 of the Constitution. The Supreme Court emphasized that High Courts should not ordinarily interfere in matters where effective remedies are available under special statutes, unless exceptional circumstances exist.

This judgment significantly strengthened the SARFAESI framework, reaffirming the autonomy of banks and financial institutions in enforcing their rights under the Act and discouraging unnecessary judicial intervention that could delay recovery. It also laid down a precedent on the principle of judicial restraint, especially in matters related to specialised financial legislations. The verdict has since been frequently cited in similar cases, reinforcing the efficacy and purpose of SARFAESI.

Case 2: Jet Airways (India) Ltd.

The financial collapse of Jet Airways (India) Ltd., one of India's leading private airlines, offers a compelling illustration of how the SARFAESI Act operates in conjunction with other recovery and insolvency mechanisms. When Jet Airways defaulted on substantial loans taken from a consortium of banks, including the State Bank of India (SBI) and Punjab National Bank (PNB), lenders initially invoked the SARFAESI Act to recover dues. The banks issued notices under Section 13(2) and subsequently took possession of secured assets such as office premises, aircraft equipment, and other movable and immovable properties of the airline under Section 13(4).

These enforcement actions represented the first step in the recovery process. However, due to the magnitude of the debt, the case was later admitted before the National Company Law Tribunal (NCLT) under the Insolvency and Bankruptcy Code (IBC), 2016, marking a shift from asset recovery to full-fledged corporate insolvency resolution. The SARFAESI proceedings, in this context, acted as a precursor to insolvency resolution and enabled banks to secure control over key assets before the IBC process commenced.

This case highlights the complementary nature of SARFAESI and IBC, especially in handling high-value non-performing assets (NPAs). It shows how the SARFAESI Act provides an immediate remedy for secured creditors to take control of and preserve the value of assets, even while larger restructuring or liquidation proceedings are undertaken under the IBC framework. It also reflects how institutional lenders strategically use multiple laws to safeguard their financial interests in complex loan default cases.

The SARFAESI Act, 2002 is regarded as one of the most effective legal mechanisms for the recovery of bad loans in India. By empowering lenders to bypass traditional court procedures and directly enforce security interests, it has significantly improved the resolution of NPAs. However, the Act also includes safeguards, such as allowing the borrower to appeal to DRT and DRAT, ensuring that recovery actions remain just and fair. In combination with complementary laws like the DRT Act and the Insolvency and Bankruptcy Code (IBC), SARFAESI forms a critical pillar in India's legal framework for financial recovery and asset reconstruction.

2.1.3 The Payment and Settlement Systems Act, 2007 (PSS Act)

The Payment and Settlement Systems Act, 2007 (PSS Act) is a landmark legislation that provides the statutory and institutional framework for the regulation, supervision, and orderly development of payment systems in India. It plays a pivotal role in shaping India's modern financial ecosystem by ensuring secure, efficient, and reliable digital and traditional modes of payment.

The Act was promulgated on December 20, 2007 and came into force on August 12, 2008. It marked a significant step in India's journey towards a cashless economy, enabling the Reserve Bank of India (RBI) to function as the principal regulator and supervisor of payment systems in the country.

2.1.3.1 Objectives of the Payment and Settlement Systems Act, 2007

The PSS Act was enacted to provide a sound legal framework for the regulation, supervision, and development of payment systems in India. It aims to establish a secure, efficient, and inclusive payments ecosystem while also enabling innovation in the digital finance space. Below are the key objectives of the Act, explained in detail:

1. Statutory Recognition of Payment Systems

One of the fundamental objectives of the PSS Act is to give legal recognition to various payment and settlement systems operating in India. This includes both conventional banking mechanisms and newly emerging digital platforms. Traditional systems such as NEFT (National Electronic Funds Transfer) and RTGS (Real-Time Gross Settlement) are critical for processing interbank electronic fund transfers. NEFT, typically used for small and medium-value payments, is now available 24x7, making it highly convenient for individual users and businesses. RTGS, on the other hand, caters to high-value transactions where funds are transferred in real time and on a gross basis, ensuring immediate settlement.

The Act also encompasses emerging digital systems that have transformed the financial landscape. Among them is UPI (Unified Payments Interface), introduced by NPCI (National Payment Corporation of India) in 2016, which allows instant money transfers between bank accounts using mobile phones. It has become a backbone for peer-to-peer (P2P) and peer-to-merchant (P2M) transactions, witnessing a phenomenal increase in adoption. Other systems such as mobile wallets (e.g., Paytm, PhonePe), prepaid instruments (PPIs), IMPS (Immediate Payment Service), and QR code-based payments have further broadened the spectrum of digital payment options.

By formally recognizing these systems, the PSS Act brings them under a uniform regulatory framework, ensuring that they operate safely, transparently, and in accordance with national standards. This statutory backing enhances public trust and stability in the payment infrastructure.

2. Empowering the Reserve Bank of India

Another core objective of the PSS Act is to designate the Reserve Bank of India (RBI) as the sole regulator and supervisor of all payment and settlement systems in India. The Act gives RBI extensive powers to authorize, regulate, monitor, and penalize payment system operators. As per Sections 4 and 7 of the Act, no entity can operate a payment system in India without obtaining prior authorization from the RBI. This ensures that only financially sound and technically capable entities are permitted to participate in the payment ecosystem.

The Act authorizes the RBI to frame detailed rules and guidelines related to the operation of payment systems, covering aspects such as transaction limits, settlement cycles, cybersecurity measures, risk management frameworks, data protection, and consumer protection mechanisms. It can inspect systems, request information, and intervene if systemic risks are identified, such as operational failures or breaches of regulatory norms.

In addition, the RBI can impose penalties or revoke licenses in cases of non-compliance, thus enforcing discipline and stability in the financial sector. The Board for Regulation and Supervision of Payment and Settlement Systems (BPSS), constituted under the Act, assists RBI in framing and executing policies related to payment infrastructure. Through this regulatory structure, the RBI ensures that India's payment systems remain safe, efficient, and aligned with international best practices.

3. Ensuring Safety, Soundness, and Efficiency

The PSS Act places strong emphasis on maintaining the security, soundness, and operational efficiency of payment systems in India. Given the increasing shift towards digital transactions, safeguarding the payment infrastructure from risks such as cyberattacks, data breaches, technical failures, and fraudulent activities is of paramount importance. The Act mandates that all payment systems operate under stringent regulatory standards that ensure protection against misuse and vulnerabilities.

Security is enforced through multi-layered authentication, encryption, fraud monitoring tools, and compliance with RBI's cyber security frameworks. For example, UPI transactions use two-factor authentication and are constantly monitored for unusual activities. Efficiency is achieved through real-time settlements (as in RTGS, UPI, and IMPS), low transaction costs, and ease of use, which enhance the user experience and reduce the burden on banking infrastructure.

Reliability is another critical component. Systems must ensure high uptime, rapid transaction processing, and robust disaster recovery plans. The legal provisions in the PSS Act help RBI to implement settlement finality norms, meaning once a transaction is processed, it cannot be reversed, thus preventing disputes and operational ambiguities.

Perhaps most importantly, the Act aims to maintain public confidence in digital payments. It does so by ensuring transparency, customer grievance redressal mechanisms, and regular audits of system providers. As a result, consumers are more willing to shift from cash to digital modes of payment, contributing to the growth of a formal, transparent economy.

2.1.3.2 Significance in the Indian Context

The PSS Act laid the groundwork for India's exponential growth in digital payments, particularly in the last decade. Its provisions have enabled:

i.   The rise of innovative digital platforms like UPI and Bharat Bill Payment System (BBPS).

ii. The introduction of interoperable mobile wallets and digital onboarding of small merchants.

iii. Financial inclusion through Aadhaar-enabled Payment Systems (AePS), especially in rural areas.

iv. Enhanced consumer protection through grievance redressal mechanisms, limits on transaction values, and transaction authentication.

Example:

One of the most notable impacts of the PSS Act is the rise of Unified Payments Interface (UPI), developed by the National Payments Corporation of India (NPCI). UPI, introduced in 2016, enables instant money transfers via mobile using Virtual Payment Addresses (VPAs), QR codes, and mobile numbers.

◊   As of April 2024, UPI transactions reached a record monthly value of ₹18.23 lakh crore, processing over 9.3 billion transactions in that month alone.

◊   UPI has enabled low-cost, real-time payments across rural and urban India, and has now been integrated for cross-border payments with countries like Singapore, Bhutan, and the UAE.

This phenomenal growth would not have been possible without the legal and regulatory foundation laid by the PSS Act.

2.1.3.3 Legal Framework & Administration of the Payment and Settlement Systems Act, 2007

The Payment and Settlement Systems Act, 2007 (PSS Act) lays down a robust and legally binding framework for the establishment, regulation, and supervision of payment and settlement systems in India. Its effective implementation hinges on clear administrative authority and well-defined regulatory mechanisms. The Act ensures that the legal and operational structure for payment systems remains resilient, inclusive, and forward-looking.

2.1.3.4 Authority of the Reserve Bank of India (RBI)

Under Section 4 of the PSS Act, 2007, the Reserve Bank of India (RBI) is designated as the sole regulator and supervisor of all payment and settlement systems in India. This provision empowers the RBI to exercise comprehensive oversight and control over both traditional and digital payment infrastructure in the country.

To operationalize its mandate, the RBI constituted the Board for Regulation and Supervision of Payment and Settlement Systems (BPSS) in March 2005, even before the Act was formally enforced. The BPSS functions as a sub-committee of the RBI's Central Board of Directors and is responsible for laying down policies related to the regulation and supervision of payment and settlement systems, including both domestic and cross-border arrangements.

The BPSS plays a pivotal role in:

1. Granting authorization to system operators.
2. Framing policies related to new technologies and innovations (e.g., UPI, tokenisation).
3. Overseeing risk mitigation, cyber-security, and operational continuity in payment systems.
4. Conducting periodic reviews and issuing regulatory directions.

Example: The RBI, under the authority of the PSS Act and through the BPSS, facilitated the introduction and scaling of Unified Payments Interface (UPI) in 2016. The BPSS set standards for data security, interoperability, and user authentication, allowing UPI to become the most widely used retail payment system in India.

2.1.3.5 Key Regulations Under the Act

Two key sets of regulations were notified by the RBI to give effect to the provisions of the PSS Act. Both regulations came into force on August 12, 2008, the same date the Act was enforced.

a. BPSS Regulations, 2008

The Board for Regulation and Supervision of Payment and Settlement Systems Regulations, 2008 govern:

i. The composition of the BPSS, including representatives from RBI and external experts.

ii. The powers, functions, and procedures of the BPSS in dealing with payment and settlement system matters.

iii. The decision-making process, including quorum, frequency of meetings, and reporting mechanisms to the Central Board of RBI.

The BPSS acts as a policy-formulating body that ensures RBI's oversight role is exercised uniformly and strategically across all payment platforms, including emerging fintech models.

b. Payment and Settlement Systems Regulations, 2008

These regulations provide a detailed procedural and compliance framework for:

i. Authorization of payment system operators (banks, NBFCs, fintech companies, etc.).

ii. Application process and conditions for grant, renewal, and revocation of licenses.

iii. Operational standards regarding system design, security protocols, settlement timelines, and participant obligations.

iv. Reporting requirements, including regular submission of operational and audit reports to the RBI.

v. Inspections and compliance audits conducted by RBI or its authorized agencies.

These regulations ensure that all payment systems function in a safe, efficient, and legally compliant manner, minimizing systemic risks and protecting consumer interests.

Example: In October 2020, the RBI issued a directive to HDFC Bank to temporarily halt the issuance of new credit cards and the launch of digital services due to repeated outages in its online payment infrastructure. This action was taken under the RBI's supervisory powers derived from the PSS Act and the 2008 regulations, demonstrating the Act's utility in enforcing service continuity and customer protection.

2.1.3.6 Institutional Oversight and Global Alignment

The RBI's regulatory framework under the PSS Act is aligned with global best practices such as:

vi. The Principles for Financial Market Infrastructures (PFMI) by the Bank for International Settlements (BIS).

vii. The G20 Financial Inclusion Action Plan, which promotes the use of technology to enhance financial access.

India's regulatory structure is now seen as a global model, particularly due to its success in:

i.   Launching and regulating UPI.

ii.   Creating an interoperable system of wallets, banks, and Aadhaar-linked payments.

iii. Ensuring uninterrupted digital services during national emergencies such as the COVID-19 pandemic.

The legal framework and administrative structure under the PSS Act, 2007, ensure that India's payment and settlement ecosystem is governed by a comprehensive, transparent, and secure regulatory regime. With the RBI at the helm and the BPSS guiding policy and oversight, the system has enabled India to transition into a predominantly digital economy while ensuring public trust, innovation, and international credibility. The two core regulations issued in 2008 remain foundational pillars that support continuous evolution in the payment space, from NEFT to UPI and beyond.

2.1.3.7 Key Provisions

1. Authorization of System Operators (Section 7)

Under Section 7 of the PSS Act, no individual or organization is allowed to initiate or operate a payment system in India without first obtaining explicit authorization from the Reserve Bank of India (RBI). This provision is designed to ensure that only reliable and financially sound entities with robust technological infrastructure are entrusted with managing payment systems. Applicants are required to submit comprehensive details including technical standards of the system, risk management frameworks, consumer protection mechanisms, integrity of the management team, and evidence of financial stability. The RBI holds the power to impose processing fees or demand security deposits as part of the application process. Additionally, it has the authority to refuse, suspend, or revoke authorization if it deems necessary, provided that due notice is given. Entities affected by such decisions have the right to appeal to the Central Government within a stipulated period of 30 days, ensuring a fair redressal mechanism.

2. Rule-Making and Standards (Section 10)

Section 10 empowers the Reserve Bank of India to frame comprehensive rules and operational standards to govern the functioning of payment systems in the country. These include prescribing the exact format of payment instructions, determining the settlement cycles, establishing eligibility and membership criteria for system participants, and setting stringent security protocols. RBI can also specify the permissible business hours for conducting payment-related operations. This regulatory authority ensures uniformity, reliability, and security across all payment service providers, thereby safeguarding the integrity of the national financial infrastructure. By exercising this mandate, the RBI plays a crucial role in promoting efficient, secure, and inclusive payment systems.

3. Information, Inspection & Penalties (Sections 12–18)

Sections 12 to 18 of the PSS Act deal with the regulatory oversight and compliance enforcement mechanisms available to the RBI. System providers are legally obligated

to submit periodic returns, financial and operational statements, and allow on-site inspections by RBI officials. These inspections are essential for monitoring ongoing compliance with legal, financial, and technical norms. If the RBI identifies any violations or non-compliance, it can issue binding directions requiring the entity to cease such activities immediately. Additionally, under the amended framework introduced in 2025, the RBI is empowered to impose stricter monetary penalties and even compound offences in cases of repeated or serious breaches. These enhanced enforcement tools serve as a strong deterrent against negligence and malpractice in the rapidly growing digital payments ecosystem.

4. Netting & Settlement Finality (Section 18)

Section 18 of the Act addresses the critical concepts of netting and settlement finality, which are foundational for ensuring stability in payment systems. Netting refers to the consolidation of multiple payment obligations into a single net amount payable between parties, which reduces systemic risk. The law grants legal sanctity to such netting arrangements, ensuring that once a payment cycle is closed, the resulting obligations are final and irrevocable. This protection remains in effect even if one of the participants subsequently defaults or enters insolvency. By providing legal certainty, this provision promotes trust among participants and reinforces the robustness of payment and settlement systems in India's financial markets.

2.1.3.8 Payment Systems Covered

The Payment and Settlement Systems Act, 2007 is deliberately crafted to be technology-neutral, enabling it to accommodate both existing and emerging payment technologies without the need for constant legislative amendments. Its coverage extends to a wide array of both large-value and retail payment systems operating in India. Among the large-value systems, the Real Time Gross Settlement (RTGS) system is a prominent example, used primarily for high-value and time-sensitive fund transfers between banks. RTGS processes each transaction individually in real time, ensuring immediate settlement and reducing settlement risk.

In the domain of retail payment systems, several widely-used platforms fall under the Act's ambit. The National Electronic Funds Transfer (NEFT) system facilitates one-to-one fund transfers between banks in batch mode and has been operating 24×7 since December 16, 2019, significantly enhancing convenience for customers. Immediate Payment Service (IMPS) offers real-time interbank fund transfers using mobile phones and is available round-the-clock, even on holidays, catering to the need for instant fund movement. One of the most transformative innovations is the Unified Payments Interface (UPI), which allows users to perform seamless, mobile-based, interoperable transactions using Virtual Payment Addresses (VPAs). UPI has revolutionized India's digital payments landscape through its ease of use, instant confirmation, and integration with multiple banks and applications.

Additionally, the Act encompasses systems such as the Bharat Bill Payment System (BBPS) a unified, interoperable platform for bill payments across utility services and

Prepaid Payment Instruments (PPIs) like mobile wallets and gift cards, which store monetary value for future payments. Other covered instruments include QR-based payments, debit and credit card transactions, Aadhaar-enabled Payment Systems (AePS) that leverage biometric authentication, and the Cheque Truncation System (CTS), which digitizes cheque processing by replacing physical movement with image-based clearing. Together, these systems form a comprehensive and inclusive framework under the Act, promoting efficiency, transparency, and trust in India's rapidly evolving digital economy.

2.1.3.9 Impact on Digital Transactions

1. Post-Demonetisation Surge (2016 – 17)

The Government of India's demonetisation drive on November 8, 2016, which rendered ₹500 and ₹1,000 currency notes invalid overnight, triggered a significant behavioural shift towards digital payments. As cash circulation was abruptly curtailed, businesses and individuals were compelled to explore electronic payment alternatives. This led to a sharp rise in digital transactions, particularly through established systems like NEFT (National Electronic Funds Transfer). According to data from that period, the total transaction value through NEFT increased by approximately 44% in 2016–17 compared to the previous financial year, demonstrating a strong push towards non-cash methods. The demonetisation period served as a catalyst that familiarised a wide cross-section of the population with digital payment tools, laying the groundwork for deeper adoption in subsequent years.

2. Launch of UPI & BHIM (2016 – 17)

In the wake of demonetisation, India witnessed the launch of two transformative digital payment solutions Unified Payments Interface (UPI) in January 2016, and the BHIM (Bharat Interface for Money) app in December 2016. Both initiatives were developed by the National Payments Corporation of India (NPCI) and built upon the regulatory and infrastructural provisions enabled by the Payment and Settlement Systems (PSS) Act. UPI enabled seamless real-time interbank transfers using mobile phones and Virtual Payment Addresses (VPAs), while BHIM offered a simple interface for users to send and receive money without relying on internet banking. Together, these innovations made instant, interoperable, and secure transactions accessible to a large population, including those with limited digital literacy. Their success marked the beginning of a mobile-centric, cashless revolution in India's payment landscape.

3. Rapid Scale-up (2020 – 25)

Between 2020 and 2025, the adoption of UPI accelerated dramatically, establishing it as India's leading retail payment system. The convenience, speed, and zero-cost structure of UPI transactions appealed to both consumers and merchants, leading to explosive growth in usage. As of April 2025, over 668 banks were integrated with UPI, and the platform processed nearly 17,893 million transactions valued at approximately ₹23.95 lakh crore in just one month. This momentum continued unabated, with June

2025 witnessing a record 18,395 million UPI transactions worth ₹24.04 lakh crore, according to data from NPCI. These figures underscore UPI's central role in reshaping the digital economy and reducing reliance on cash. The scalability and interoperability of UPI have enabled its integration with various apps, including Google Pay, PhonePe, Paytm, and WhatsApp Pay, further driving its ubiquity across demographic segments.

4. Enhanced Financial Inclusion & Innovation

The growth in digital payments has also significantly contributed to financial inclusion, especially in rural and semi-urban regions. Services like mobile wallets, Aadhaar-enabled Payment Systems (AePS), Bharat Bill Payment System (BBPS), and QR-based payments have made digital transactions accessible to those without traditional banking infrastructure. These systems allow users to make payments using biometric authentication, scan-and-pay features, and integrated bill payment networks—tools that have bridged the digital divide. Furthermore, the regulatory sandbox mechanism introduced under the PSS Act has facilitated a safe space for fintech companies to test new products like e-mandates, card tokenisation, and cross-border remittance platforms without immediately risking consumer harm. This controlled environment has led to rapid innovation, supporting the development of secure and user-friendly financial technologies tailored to the Indian market.

Use Case 1: Market Share Dynamics

One of the key regulatory interventions under the PSS Act has been the enforcement of competitive neutrality in the fast-growing digital payments ecosystem. To prevent market concentration and ensure a level playing field among UPI (Unified Payments Interface) participants, the National Payments Corporation of India (NPCI) introduced a rule capping the market share of any single UPI app at 30% of total transaction volumes. This rule, introduced in 2020, was meant to reduce systemic risks and promote diversity in service providers. However, to avoid disrupting user experience during the period of rapid digital adoption, the implementation of this cap has been postponed multiple times. Despite this, the market has remained highly competitive under the PSS Act's regulatory framework. For instance, as of April 2024, PhonePe held the largest market share, commanding 48.3% of UPI transaction volumes, followed by Google Pay at 37.4%, as reported by Reuters. This competitive environment, though dominated by a few large players, is continually shaped and balanced by RBI's oversight and intervention powers under the Act.

Use Case 2 : Disaster Resilience

The COVID-19 pandemic served as a critical stress test for India's digital payment infrastructure. During the nationwide lockdowns in 2020, physical access to cash and banking services was severely restricted. In this crisis, systems such as NEFT (National Electronic Funds Transfer) and UPI became indispensable tools for individuals, businesses, and governments to conduct daily financial operations. The surge in usage volumes for these systems during the lockdown highlighted not only their operational scalability but also the effectiveness of the RBI's regulatory safeguards under the PSS

Act. Both platforms functioned without major disruptions, managing massive increases in transaction loads. For example, UPI experienced record-breaking growth as people turned to mobile-based, contactless payment methods for essentials like groceries, utilities, and medical services. This real-life scenario affirmed the resilience of India's digital payment architecture and the role of prudent regulation in building robust and adaptable financial systems.

Use Case 3: Cross-Border Remittances Pilot

In 2024, the Reserve Bank of India took significant steps to internationalise India's digital payment systems by launching pilot projects for cross-border UPI-based remittances. These pilots were initiated with countries like Bhutan and the United Arab Emirates (UAE), marking a new chapter in digital financial connectivity. The initiative leveraged the provisions of the PSS Act that empower the RBI to regulate not just domestic, but also international payment interfaces. Through these pilots, Indian users gained the ability to make real-time remittances directly to recipients in partner countries using UPI, thereby reducing the costs and complexities associated with traditional remittance channels. For instance, Indian tourists in Bhutan could pay merchants using UPI QR codes, while workers in the UAE could send money to Indian bank accounts via UPI-linked platforms. These developments illustrate how the Act provides the legal and operational flexibility for India to extend its digital financial ecosystem beyond its borders, supporting the vision of "Digital India, Global Impact."

By providing a clear, flexible and forward-looking legal scaffold, the Payment and Settlement Systems Act, 2007 has underpinned India's transformation into one of the world's largest and fastest-growing digital payment markets. Through robust authorisation processes, comprehensive oversight powers and support for innovation, the RBI has ensured that safety, efficiency and public trust remain at the heart of India's payment revolution.

2.1.4 Banking Ombudsman Scheme

The Banking Ombudsman Scheme is a vital mechanism established by the Reserve Bank of India (RBI) to provide a cost-effective, speedy, and impartial redressal system for resolving grievances raised by bank customers. The scheme ensures that customers do not have to navigate complicated legal procedures to address banking-related disputes. It plays a crucial role in reinforcing transparency, accountability, and trust in the banking sector.

2.1.4.1 Legal Foundation and Latest Update

The scheme was originally introduced under the powers conferred by Section 35A of the Banking Regulation Act, 1949, which allows the RBI to issue directions to banks in the public interest. The first Banking Ombudsman Scheme was launched in 1995, and since then, it has undergone several revisions to broaden its scope and improve efficiency.

The most recent development came with the launch of the Integrated Ombudsman Scheme, 2021, which merged three separate ombudsman schemes—Banking Ombudsman Scheme (2006), Ombudsman Scheme for Non-Banking Financial Companies (2018), and Ombudsman Scheme for Digital Transactions (2019) into a single, unified platform. This integrated approach simplifies the complaint process for customers and brings uniformity in redressal mechanisms across financial service providers.

The Integrated Scheme is administered through the RBI's Complaint Management System (CMS) portal (https://cms.rbi.org.in), which allows customers to file complaints online with tracking facilities.

2.1.4.2 Scope of Complaints

The scheme covers a wide range of services offered by both Scheduled Commercial Banks, Regional Rural Banks (RRBs), and selected Non-Banking Financial Companies (NBFCs). The complaints that can be lodged under the scheme include:

i. Delay in cheque clearance or fund transfers, including those conducted through NEFT or RTGS.

ii. Refusal by banks to open deposit accounts, grant loans, or issue credit/debit cards without valid reasons.

iii. Non-disbursement or undue delay in disbursing loans, despite completing formalities.

iv. Failure to update passbooks, provide account statements, or reflect transactions correctly.

v. Problems related to ATM transactions, such as cash not dispensed but account debited.

vi. Issues with internet or mobile banking, such as transaction failures or unauthorized debits.

vii. Overcharging or non-transparency in service charges and fees.

viii. Refusal to accept small denomination notes or coins, or insisting on minimum balance requirements.

The scheme also covers grievances related to digital transactions, reflecting the shift towards a more digitally inclusive economy.

2.1.4.3 Procedure for Lodging a Complaint

The scheme lays down a simple, transparent, and time-bound procedure for resolving complaints:

1. **Initial Complaint to Bank :** The customer must first lodge a complaint with the concerned bank. If the bank fails to respond within 30 days, or if the customer is unsatisfied with the reply, they may approach the ombudsman.

2. **Filing with the Ombudsman :** The complaint can be filed online via the RBI's CMS Portal, via email, post, or in person. The application must include relevant

details such as the complainant's name, bank details, nature of the complaint, and previous correspondence.

3. **No Fee :** The process is free of cost for customers, making it accessible to all, especially those from rural and semi-urban areas.

4. **Redressal and Appeal :** The Ombudsman can pass binding decisions known as awards. If the customer or the bank is dissatisfied with the decision, an appeal can be made to the Appellate Authority at the RBI, generally a Deputy Governor.

5. **Resolution Timeline :** The RBI Ombudsman aims to dispose of complaints within 90 days, ensuring swift redressal.

The effectiveness of the scheme can be illustrated through recent data and specific examples:

◊   According to the Annual Report on the Integrated Ombudsman Scheme 2022–23 published by the RBI, over 1.9 lakh complaints were resolved during the year. The majority of these complaints were related to digital transactions, unauthorized debits, ATM failures, and account management issues.

◊   One notable case involved a customer who lodged a complaint after failing to receive ₹10,000 dispensed from an ATM, though the amount was debited from their account. Upon investigation, the Ombudsman ruled in favour of the customer, and the bank was instructed to refund the amount along with interest.

◊   In another case, a senior citizen was denied a home loan top-up by a public sector bank despite eligibility. After the Ombudsman's intervention, the bank reconsidered its decision, sanctioned the loan, and issued a written apology for the delay and procedural lapses.

Such instances demonstrate the scheme's role in empowering consumers, improving bank accountability, and promoting responsible banking practices.

The Banking Ombudsman Scheme, now integrated into a comprehensive grievance redressal mechanism, is a cornerstone of consumer protection in India's banking and financial ecosystem. It simplifies the complaint process, ensures free and fair resolution, and contributes to building public confidence in the formal financial sector. With the advent of digital banking and fintech services, the scheme continues to evolve, backed by the legal authority and technological infrastructure of the Reserve Bank of India.

2.1.5 Basel Reforms

The Basel Accords are a set of international banking regulations developed by the Basel Committee on Banking Supervision (BCBS), under the Bank for International Settlements (BIS). These accords aim to ensure that financial institutions maintain adequate capital to absorb unexpected losses and manage risks effectively, thereby promoting global financial stability. The Basel norms provide a global standard for capital adequacy, stress testing, and market liquidity risk, and are voluntarily adopted by member countries.

The BCBS was established in 1974 by the Group of Ten (G10) countries in response to financial disruptions caused by the failure of major banks like Herstatt Bank in Germany. Since then, three major Basel Accords such as Basel I, Basel II, and Basel III have been issued to address evolving challenges in the global banking sector.

Basel I (1988)

Basel I was the first international regulatory framework introduced by the Basel Committee on Banking Supervision (BCBS) with the primary focus on managing credit risk in the banking sector. It aimed to standardize capital adequacy regulations across countries to ensure a level playing field and to strengthen the stability of the global financial system. One of the key provisions of Basel I was the introduction of the Capital to Risk-Weighted Assets Ratio (CRAR), also known as the Capital Adequacy Ratio (CAR). According to this norm, banks were required to maintain a minimum capital of 8% of their risk-weighted assets to protect themselves against potential credit losses. Assets were assigned different risk weights depending on their nature and risk profile—for instance, government securities were assigned a 0% risk weight, while loans to private entities could carry a 100% risk weight, reflecting their higher risk.

The primary objective of Basel I was to ensure that banks held sufficient capital to absorb losses, thereby safeguarding depositors' interests and protecting the overall financial system from systemic shocks. However, Basel I had several limitations. It did not account for market risk or operational risk, and it failed to differentiate between loans of varying credit quality, treating all corporate loans equally regardless of the borrower's creditworthiness. This lack of risk sensitivity limited its effectiveness in capturing the actual exposure of banks.

In the Indian context, banks such as the State Bank of India (SBI) began implementing Basel I norms in the 1990s under the guidance of the Reserve Bank of India (RBI) as part of broader financial sector reforms. This marked a significant step in aligning India's banking regulations with international standards and laid the groundwork for future reforms under Basel II and III.

Basel II (2004)

Basel II was introduced as an advancement over Basel I, expanding the regulatory framework to address not only credit risk, but also market risk and operational risk. The main objective of Basel II was to enhance the risk management capabilities of banks and ensure a stronger link between a bank's capital requirement and the actual level of risk it faces. It aimed to create a more comprehensive and risk-sensitive approach to capital adequacy by encouraging banks to develop better internal risk assessment models and align their capital more closely with their risk profiles.

Three Pillars of Basel II:

1. Minimum Capital Requirements: Enhanced risk sensitivity by refining the way credit risk is calculated, including external credit assessments (ratings).

2. Supervisory Review Process: Enabled regulators to evaluate and ensure that banks have adequate internal processes to assess capital adequacy relative to their risk profile.

3. Market Discipline: Required banks to publicly disclose information regarding risk exposures and capital adequacy to promote transparency and allow market participants to assess banks' soundness.

In India, banks like ICICI Bank and HDFC Bank began adopting the IRB approaches under Basel II, using advanced risk models for credit risk assessment and more accurate capital allocation. These practices helped larger banks gain deeper insights into their risk exposure and optimize their capital usage. However, Basel II posed several challenges, particularly in its implementation. The framework required sophisticated internal systems, skilled human resources, and advanced data collection and analysis tools, which made the compliance process complex and costly, especially for smaller and mid-sized banks that lacked the necessary infrastructure and expertise.

Despite these difficulties, Basel II marked a significant step toward building a more resilient banking system by encouraging banks to strengthen their risk management frameworks and aligning their regulatory capital more closely with the actual risks they undertake.

Basel III (2010 onwards)

Basel III was introduced in response to the 2008 Global Financial Crisis, which exposed critical weaknesses in the global banking sector's capital adequacy, liquidity, and risk management practices. The collapse of major financial institutions such as Lehman Brothers, which failed due to excessive leverage and poor liquidity management, highlighted the need for more robust regulatory safeguards. In this context, Basel III was designed to strengthen the resilience of banks, ensuring they could better withstand financial and economic shocks without triggering broader systemic crises.

The main objectives of Basel III were to enhance the quality and quantity of banks' capital base, particularly Tier 1 capital, and to improve their liquidity positions. It introduced several new regulatory measures, such as the Capital Conservation Buffer, Countercyclical Capital Buffer, Leverage Ratio, and Liquidity Coverage Ratio (LCR), to provide a more comprehensive and risk-sensitive framework. These measures aimed to reduce the risk of bank failures and limit the impact of financial turmoil on the broader economy by ensuring that banks maintain adequate capital and liquid assets even under stressed conditions. Overall, Basel III represents a significant shift towards a more resilient and transparent banking system, reinforcing global financial stability.

2.1.5.1 Key Features of Basel III

1. **Capital Conservation Buffer :** The Capital Conservation Buffer is an additional capital requirement of 2.5% of risk-weighted assets, imposed above the minimum regulatory capital. It is designed to ensure that banks accumulate capital in normal times, which can be drawn down when losses are incurred

during periods of stress. This helps banks avoid breaching minimum capital requirements during economic downturns.

2. **Countercyclical Capital Buffer** : The Countercyclical Capital Buffer ranges from 0 to 2.5% and is imposed during periods of excessive credit growth. Its purpose is to protect the banking sector from systemic risk that arises from cyclical economic trends. Regulators activate this buffer to ensure banks build up capital during booms to cushion potential losses during busts.

3. **Leverage Ratio:** The Leverage Ratio is a non-risk-based measure that compares Tier 1 capital to total exposure, with a minimum threshold of 3%. It is intended to prevent banks from becoming excessively leveraged, regardless of the perceived riskiness of their assets. This acts as a backstop to the risk-based capital framework and enhances overall financial stability.

4. **Liquidity Coverage Ratio (LCR):** The LCR requires banks to maintain High-Quality Liquid Assets (HQLA) sufficient to meet their net cash outflows over a 30-day stress scenario. It ensures that banks have enough liquidity to survive short-term funding disruptions. In India, the LCR was phased in gradually and became fully implemented by January 2019, as mandated by the Reserve Bank of India.

5. **Net Stable Funding Ratio (NSFR):** The NSFR promotes long-term funding stability by requiring banks to maintain a stable funding profile in relation to their asset composition. It compares a bank's available stable funding to its required stable funding over a one-year time horizon. This ensures that banks do not rely excessively on short-term wholesale funding to finance long-term assets.

2.1.5.2 Current Status and Implementation in India

India has made significant progress in adopting and implementing the Basel III regulatory framework, under the supervision of the Reserve Bank of India (RBI). As of now, Basel III norms have been fully implemented for all Scheduled Commercial Banks operating in the country. This includes both public and private sector banks, but excludes Regional Rural Banks (RRBs) and cooperative banks, which are governed by a different set of regulatory guidelines due to their unique structures and operational scopes. The phased implementation of Basel III in India began in April 2013 and was completed by March 2019, in line with the RBI's roadmap.

In addition to Basel III adoption, the RBI has developed and enforced a structured Prompt Corrective Action (PCA) framework, which is aligned with key indicators such as capital adequacy, asset quality, and leverage ratios core elements of the Basel principles. Under this framework, banks that breach certain thresholds are subjected to mandatory corrective measures and restrictions, including limitations on lending, dividend payments, branch expansion, and managerial compensation. This system is designed to act as an early warning mechanism to prevent financial deterioration and to promote the timely rehabilitation of stressed banks. The PCA framework has been instrumental in guiding troubled banks like IDBI Bank and UCO Bank back to financial stability by enforcing strict regulatory oversight and capital restoration plans.

Overall, India's implementation of Basel III and related supervisory mechanisms like PCA reflects a strong commitment to international banking standards and contributes to the long-term soundness and resilience of the Indian banking system.

2.1.5.3 Significance of Basel Norms

1. **Enhance the resilience of the banking sector :** The Basel norms require banks to maintain adequate levels of capital and liquidity, enabling them to absorb financial shocks and continue operations during times of economic stress. This improves the overall robustness and health of the banking sector. As a result, banks become better equipped to deal with credit defaults, market volatility, and operational disruptions.

2. **Promote global financial stability :** By setting uniform regulatory standards for banks across countries, the Basel norms create a consistent framework that reduces the risk of financial contagion. This harmonization helps maintain confidence among international investors and stakeholders. It also facilitates smoother cross-border banking operations and coordination among financial regulators.

3. **Improve risk management practices:** Basel norms encourage banks to adopt advanced risk assessment models and internal control systems to evaluate and manage various types of risks, including credit, market, and operational risks. This leads to more informed decision-making and efficient capital allocation. Over time, it fosters a culture of accountability and prudence within financial institutions.

4. **Prevent bank failures and systemic collapses:** By mandating minimum capital requirements and robust liquidity provisions, Basel norms help prevent excessive risk-taking by banks. These safeguards act as a buffer against insolvency, reducing the likelihood of individual bank failures. In turn, this prevents broader systemic crises that could disrupt the entire financial system and economy.

The Basel Accords such as Basel I, II, and III reflect the global banking sector's evolving understanding of risk and resilience. While Basel I laid the foundation by introducing capital adequacy, Basel II introduced comprehensive risk management principles, and Basel III responded to the vulnerabilities exposed during the 2008 crisis by emphasizing capital quality, liquidity, and systemic risk buffers. Their implementation, especially in a growing economy like India, remains central to maintaining a robust and sound banking system.

2.1.6 Capital Adequacy Norms

Capital Adequacy Norms are a set of regulatory standards that ensure banks maintain enough capital reserves to absorb potential losses arising from their lending and investment activities. These norms are critical for maintaining the financial health and stability of banks, protecting depositors, and safeguarding the overall banking system from insolvency risks. The most widely used measure of capital adequacy is the Capital to Risk-Weighted Assets Ratio (CRAR), also known as the Capital Adequacy Ratio (CAR).

The formula for calculating CRAR is:CRAR = (Tier 1 Capital + Tier 2 Capital) / Risk Weighted Assets × 100

◊ Tier 1 Capital represents a bank's core capital, which includes equity capital and disclosed reserves. It is the primary funding source of a bank and is capable of absorbing losses without the bank being required to cease operations.

◊ Tier 2 Capital is supplementary capital, which includes items like revaluation reserves, hybrid capital instruments, and subordinated debt. While Tier 2 can absorb losses in the event of winding up, it is considered less secure than Tier 1 capital.

In India, the Reserve Bank of India (RBI) mandates that all scheduled commercial banks maintain a minimum CRAR of 9% under the Basel III framework, which is stricter than the global Basel III requirement of 8%. This higher standard reflects the RBI's conservative regulatory approach and aims to provide a stronger buffer against potential risks in a developing economy. Maintaining an adequate CRAR not only improves a bank's resilience during financial stress but also boosts investor and depositor confidence, contributing to a more stable and efficient banking sector.

2.1.6.1 Capital Adequacy Ratio (CAR) in India

Capital Adequacy Ratio (CAR) also known as The Capital to Risk-Weighted Assets Ratio (CRAR) is a crucial measure used to assess a bank's financial strength and its ability to absorb potential losses. Under Basel III norms, the global minimum CRAR requirement is 8%, but the Reserve Bank of India (RBI) has mandated a stricter requirement of 9% for Indian banks. This higher threshold reflects the RBI's more conservative regulatory approach, aimed at strengthening the resilience of the Indian banking system.

By requiring banks to maintain higher levels of capital, the RBI ensures that they have a stronger buffer to absorb unexpected losses, manage credit risks, and maintain confidence among depositors and investors. This is particularly important in a country like India, where economic and financial market volatility, exposure to stressed assets, and the need to support financial inclusion demand a stable and well-capitalized banking sector. The 9% CRAR requirement applies to Scheduled Commercial Banks and is often supplemented with additional buffers such as the Capital Conservation Buffer (CCB) and, where applicable, the Countercyclical Capital Buffer (CCyB), further enhancing the sector's ability to withstand economic shocks.

Example: YES Bank Crisis

◊ YES Bank, once a high-performing private lender in India, came under regulatory scrutiny post-2008 and especially during the late 2010s.

◊ Due to poor corporate governance, over exposure to risky loans, and inadequate capital buffers, it struggled to meet the Basel III norms.

◊ In March 2020, RBI imposed a moratorium and orchestrated a restructuring plan with the backing of banks like SBI to infuse capital.

◊ YES Bank was required to strengthen its capital adequacy ratio and improve liquidity coverage, as per Basel III standards.

2.1.7 NPA Management

A Non-Performing Asset (NPA) refers to a loan or advance for which the principal or interest payment has remained overdue for more than 90 days. When a borrower defaults on repayment obligations, the asset ceases to generate income for the bank, turning it into a financial liability. The classification of NPAs is based on the period for which the asset remains overdue: if the default persists for up to 12 months, it is categorized as a Substandard Asset; if it exceeds 12 months, it becomes a Doubtful Asset; and when the asset is considered irrecoverable, it is classified as a Loss Asset, though it may not be written off immediately.

The causes of NPAs are multifaceted. They include macroeconomic issues like economic slowdowns, sectoral downturns, and currency fluctuations, which impact the repayment ability of borrowers. Other contributing factors include poor credit appraisal, willful defaults by borrowers, and external shocks such as natural calamities, especially affecting sectors like agriculture. Structural issues within banks, such as lax due diligence, and corruption in loan disbursement, also aggravate the NPA problem.

The impact of NPAs on the banking sector is profound. A high level of NPAs erodes bank profitability, as defaulted loans fail to generate interest income and require provisioning a process by which banks set aside funds to cover potential losses. This, in turn, reduces the bank's lending capacity, restricting its ability to support economic growth and finance new business ventures.

To manage and reduce NPAs, banks and regulators have adopted several strategic measures:

1. **Early Recognition**: Banks are now using Early Warning Signals (EWS) and risk-based supervision to identify stressed accounts at the pre-default stage. This allows timely intervention and restructuring of loans before they become NPAs.

2. **Asset Reconstruction**: Banks transfer bad loans to Asset Reconstruction Companies (ARCs), which specialize in recovering dues through restructuring or sale of assets. This helps clean up the banks' balance sheets and recover partial value from non-performing loans.

3. **SARFAESI Act (2002)**: Under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, banks can seize and sell secured assets of defaulting borrowers without the intervention of courts, expediting recovery.

4. **One-Time Settlement (OTS)**: Banks may offer borrowers the option of settling outstanding dues at a discounted amount. This pragmatic approach facilitates quicker recovery while reducing legal costs and time delays.

5. **Insolvency and Bankruptcy Code (IBC)**: Introduced in 2016, the IBC offers a comprehensive legal framework for resolving insolvencies in a time-bound

manner (typically within 180-270 days). It enables creditors to take control of defaulting companies, initiate resolution plans, or proceed with liquidation if recovery is not feasible.

A notable example is the IL&FS crisis in 2018, where the Infrastructure Leasing & Financial Services group defaulted on massive debt obligations, resulting in a surge of NPAs across the banking and NBFC sectors. The RBI, along with commercial banks, responded using a mix of tools including the IBC, regulatory intervention, and recapitalisation efforts to mitigate the systemic risk and stabilise the financial ecosystem.

Overall, effective NPA management is critical for the sustainability of the banking system. It requires a combination of regulatory oversight, financial discipline, institutional reforms, and improved credit monitoring to ensure healthy asset quality and restore trust in the financial sector.

Recap

◊ DRT Act, 1993: Established special tribunals (DRTs) for faster resolution of large-value loan recovery cases.

◊ SARFAESI Act, 2002: Allows banks to enforce security interests without court intervention to recover bad loans.

◊ PSS Act aims to provide a sound legal framework for the development of payment systems in the country

◊ Banking ombudsman scheme provides efficient grievance redressal mechanism to bank customers

◊ Basel Reforms: Basel I, II, and III established global risk and capital adequacy frameworks to enhance banking stability.

◊ Capital Adequacy Norms: CRAR ensures banks hold sufficient capital; RBI mandates 9% minimum in India.

◊ NPA Management: Combines early recognition, asset reconstruction, SARFAESI, OTS, and IBC for effective recovery.

Objective Questions

1. What does CRAR stand for?
2. What is the minimum capital adequacy ratio under Basel III?
3. Which Act enables banks to take possession of assets without court intervention?

4. What is the full form of NPA?

5. Under which section can banks enforce security under SARFAESI?

6. What is the threshold debt amount for approaching DRT?

7. What does Tier 1 capital include?

8. What is the maximum Capital Conservation Buffer under Basel III?

9. Which institution supervises Basel norms in India?

10. What is the full form of ARC?

11. In which year was the SARFAESI Act enacted?

12. What is the purpose of the Liquidity Coverage Ratio?

Answers

1. Capital to Risk-weighted Assets Ratio

2. 8 percent

3. SARFAESI Act

4. Non-Performing Asset

5. Section 13

6. ₹10 lakh

7. Equity and reserves

8. 2.5 percent

9. Reserve Bank of India

10. Asset Reconstruction Company

11. 2002

12. Ensure short-term liquidity

Self-Assessment Questions

1. What are the key objectives of RDB Act ?

2. Explain the salient features of DRT Act ?

3. Explain the crucial role of DRT in high stakes loan recovery with the help of practical cases ?

4.	What are the objectives of SARFAESI Act ?

5.	Explain PSS Act ?

6.	Write a shortnote on Sec.13 of SARFAESI Act ?

7.	Explain the impact of PSS Act on difital payment trasactions in India ?

8.	Briefly explain Banking ombudsman scheme

9.	Describe Basel norms?

10.	What is NPA management?

Assignments

1.	Explain the key objectives and features of the DRT Act, 1993.

2.	Discuss the differences between Basel I, Basel II, and Basel III reforms.

3.	Describe the mechanism and importance of the SARFAESI Act in NPA recovery.

4.	What is Capital Adequacy Ratio (CRAR)? Explain how it is calculated with examples.

5.	Evaluate the causes and impacts of NPAs on the Indian banking system and outline the major management strategies.

6.	Visit a bank branch and prepare a report on how they monitor and classify NPAs.

7.	Prepare a comparative chart of Basel I, II, and III including key features and timelines.

8.	Analyse a real-life case of debt recovery under the SARFAESI Act and summarise the outcomes.

9.	Create a sample CRAR calculation using hypothetical balance sheet figures.

10.	Conduct a role-play or interview with a bank manager on how they handle defaulted loan cases.

Reference

1. Reserve Bank of India. (2023). *Report on Trends and Progress of Banking in India*. RBI.

2. Bank for International Settlements. (2011). *Basel III: A global regulatory framework*. BIS.

3. Pathak, B. V. (2014). *Indian Financial System* (5th ed.). Pearson Education.

4. Khan, M. Y. (2020). *Indian Financial System* (10th ed.). McGraw-Hill Education.

5. Machiraju, H. R. (2010). *Modern Commercial Banking*. Vikas Publishing.

6. Bhole, L. M., & Mahakud, J. (2019). *Financial Institutions and Markets* (6th ed.). McGraw-Hill.

7. Reserve Bank of India. (2021). *Master Circular - Basel III Capital Regulations*. RBI.

8. NITI Aayog. (2018). *Report on Bad Bank and NPA Resolution Strategies*. Government of India.

9. Narasimham Committee II Report. (1998). *Recommendations on Banking Sector Reforms*. Government of India.

10. Ghosh, S. (2015). *Managing Non-Performing Assets in Indian Banks*. Economic and Political Weekly, 50(12), 65-72.

Suggested Reading

1. Narasimham Committee II Report. (1998). *Recommendations on Banking Sector Reforms*. Government of India.

2. Ghosh, S. (2015). *Managing Non-Performing Assets in Indian Banks*. Economic and Political Weekly, 50(12), 65-72.

3. Machiraju, H. R. (2010). *Modern Commercial Banking*. Vikas Publishing.

4. Bhole, L. M., & Mahakud, J. (2019). *Financial Institutions and Markets* (6th ed.). McGraw-Hill.
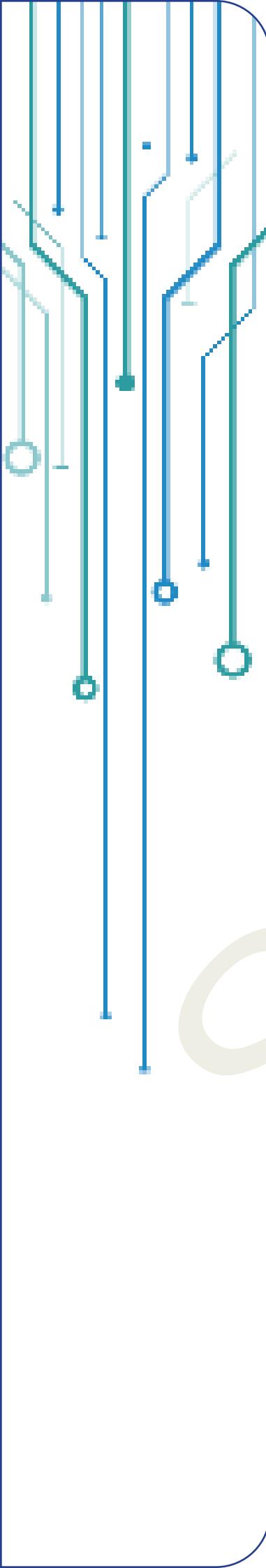
Unit 2
Account Opening Process in Banks

Prerequisites

A young college student named Asha who just got her first part-time job. She wants to save her earnings safely and also pay for things like books, mobile bills, and online purchases. Her parents advise her to open a bank account. She walks into a nearby bank, but soon realises it's not just about filling a form. She is asked to choose the right type of account, submit documents like Aadhaar and PAN, fill in personal details, and even complete something called KYC. She's also offered a debit card, internet banking, and help with mobile banking.

This real-life situation shows how important it is to understand the account opening process. It's not just paperwork it's the first step in becoming part of the formal financial system. This unit will walk you through every step Asha takes: from choosing the account to submitting documents, understanding digital banking, and even applying for loans. Whether you're a student like Asha or a future entrepreneur, knowing this process is essential in today's banking world.

Discussion

2.2.1 Introduction

Opening a bank account is the foundational step in forming a formal and regulated relationship between a bank and a customer. It allows individuals and businesses to access essential financial services such as depositing and withdrawing money, applying for loans and credit facilities, using debit or credit cards, and availing digital banking features like mobile apps and internet banking. Having a bank account not only enables safe and secure money management, but also serves as a gateway to financial inclusion, especially in developing countries like India, where millions were previously outside the formal banking system.

In India, the account opening process is governed by guidelines laid down by the Reserve Bank of India (RBI) and reinforced through the Prevention of Money Laundering Act (PMLA), 2002. These regulations make it mandatory for banks to implement a KYC (Know Your Customer) process before opening an account. KYC involves verifying the identity and address of the customer using officially valid documents such as Aadhaar, PAN card, passport, voter ID, or driving license. This helps prevent financial crimes like money laundering, fraud, and financing of terrorism by ensuring that only legitimate individuals and entities can access the banking system.

To make banking more inclusive, RBI has also promoted Basic Savings Bank Deposit Accounts (BSBDAs) and Jan Dhan Yojana accounts, which allow even low-income individuals to open zero-balance accounts with simplified KYC norms. For example, under the Pradhan Mantri Jan Dhan Yojana (PMJDY) launched in 2014, over 50 crore bank accounts have been opened as of 2023, many with Aadhaar-based e-KYC. These initiatives have significantly improved access to financial services for rural and underprivileged populations while maintaining compliance with anti-money laundering regulations. Thus, opening a bank account today involves not only initiating a financial relationship but also complying with national and global standards for customer verification and financial integrity.

2.2.2 Steps in Account Opening

Opening a bank account involves a series of structured steps that help banks identify and verify the customer while ensuring the account meets the customer's financial needs. Each step serves a specific purpose in aligning regulatory compliance with customer convenience. Below is a detailed explanation of each step involved in the account opening process:

Step 1: Selection of Account Type

The first step is for the customer to determine the type of account they want to open, depending on their financial goals and transaction needs. Banks offer different types of accounts such as Savings Account, Current Account, Fixed Deposit, Recurring Deposit, and NRI Accounts, each with unique features and benefits. For instance, a college student may open a savings account to manage personal finances, while a trader may opt for a current account to facilitate frequent and large transactions. The following are the different types of accounts.

Savings Account

A Savings Account is designed for individuals who want to save money securely while earning interest on their deposits. It generally has limitations on the number of withdrawals per month and offers basic services like debit cards, internet banking, and cheque books. For example, a salaried employee might open a savings account with banks to receive salary credits and manage monthly expenses.

Current Account

A Current Account caters primarily to business professionals, companies, and traders who need to make multiple or high-volume transactions daily. These accounts typically do not earn interest but offer overdraft facilities and allow unlimited transactions. For example, a retail shop owner may open a current account make frequent supplier payments and deposit daily sales collections.

Fixed Deposit

A Fixed Deposit (FD) account allows customers to deposit a lump sum of money for a fixed period, ranging from 7 days to 10 years, at higher interest rates compared to savings accounts. The amount is locked in, and premature withdrawal usually incurs a penalty. For example, a retiree may choose to deposit ₹5 lakhs in an FD Bank for five years to earn stable interest income.

Recurring Deposit

A Recurring Deposit (RD) account is suitable for individuals who want to save a fixed amount every month over a predetermined tenure, encouraging disciplined savings. It is especially popular among middle-income earners or students saving for short-term goals. For instance, a young professional may start an RD of ₹2,000 per month for 2 years with Canara Bank to fund a vacation or gadget purchase.

NRI Accounts

NRI accounts are designed for Non-Resident Indians (NRIs) to manage their income earned abroad or in India. These accounts come in different forms like NRE (Non-Resident External), NRO (Non-Resident Ordinary), and FCNR (Foreign Currency Non-Resident) accounts, depending on whether the income is repatriable and the currency

in which it is held. For example, an Indian working in the UAE might open an NRE account to send remittances to India in rupees while earning tax-free interest.

Step 2: Collecting the Application Form

Once the customer has selected the type of account, the next step is to collect and fill out the account opening form, which is available in both physical and digital formats. Most public and private sector banks in India have standardised application forms that gather essential information and ensure compliance with regulatory requirements. The form typically includes sections for personal details (such as name, address, date of birth), nominee information (in case of the account holder's death), a declaration and consent clause, and a KYC checklist listing documents to be submitted.

Customers can access these forms by visiting the branch in person, downloading the form from the bank's official website, or completing the process through online banking portals or mobile apps. For example, State Bank of India (SBI) and HDFC Bank allow customers to either download a PDF form or use their digital onboarding platforms to fill and submit the application online. This step helps banks initiate the account opening workflow while collecting preliminary customer data in a secure and regulated manner.

Step 3: Filling the Account Opening Form

After collecting the form, the applicant must carefully fill in all the required details, ensuring accuracy and consistency with official identity documents. The information typically includes the full name (as per Aadhaar or PAN), date of birth, gender, marital status, occupation, annual income, and both residential and permanent addresses. It is also mandatory to provide the PAN number or Form 60 (if the applicant does not have a PAN), and although the Aadhaar number is optional, most banks request it for seamless verification.

The form also includes space to nominate a person who will receive the account proceeds in case of the account holder's death. The final step in the form involves the applicant's declaration, agreeing to the bank's terms and conditions, followed by signing or digitally verifying the form. Many banks, such as Kotak Mahindra Bank and ICICI Bank, offer digital account opening through eKYC, where Aadhaar-linked mobile numbers can be used for OTP-based identity verification via mobile apps eliminating the need for branch visits and physical paperwork.

2.2.3 KYC Formalities

Know Your Customer (KYC) is a mandatory verification process introduced by the Reserve Bank of India (RBI) to prevent identity fraud, money laundering, and other financial crimes. During this step, banks are required to verify the identity and residential address of the customer using officially valid documents (OVDs). The purpose is to ensure that the person opening the account is genuine and traceable, creating a secure and transparent banking system.

According to RBI guidelines, the customer must provide:

◊ Proof of Identity such as Aadhaar card, PAN card, passport, or voter ID.

◊ Proof of Address, which can be a utility bill, Aadhaar, or driving license.

◊ PAN card or Form 60 is also required for conducting financial transactions and for compliance with the Income Tax Act.

◊ A recent passport-size colour photograph is necessary to complete the documentation.

For accounts opened on behalf of minors, the KYC documents of the parent or legal guardian must be submitted instead. In efforts to promote financial inclusion, simplified KYC norms are allowed for low-income individuals. For example, under the Pradhan Mantri Jan Dhan Yojana (PMJDY), people can open Basic Savings Bank Deposit Accounts (BSBDAs) using just Aadhaar and a self-declaration, making banking accessible to even those with limited documentation.

2.2.4 Loan Application Forms – Necessary Documents

Applying for a loan is a formal process through which individuals or businesses approach a bank or financial institution for credit. To evaluate the borrower's credibility and repayment capacity, banks require a loan application form to be filled and supporting documents to be submitted. This step is essential in ensuring that the bank assesses the loan request in a transparent, efficient, and risk-mitigated manner.

1. Loan Application Form: Meaning and Purpose

A loan application form is a standardised document provided by the bank or lender that collects the applicant's personal, financial, and employment details. It serves as the primary basis for credit assessment. The form varies depending on the type of loan (personal, home, vehicle, education, etc.) and the lending institution but typically seeks detailed information regarding:

◊ Personal identification

◊ Employment or business profile

◊ Income and assets

◊ Existing liabilities

◊ Loan requirement and purpose

The application form helps the bank conduct credit appraisal, risk analysis, and comply with regulatory guidelines such as KYC and AML (Anti-Money Laundering) norms.

2. Key Sections in a Typical Loan Application Form

A comprehensive loan application form usually includes:

Section	Details
Personal Information	Name, DOB, Gender, Marital Status, Nationality, Contact Details
Identity and Address Proof	Aadhaar, PAN, Passport, Voter ID, Driving License
Employment/Business Details	Employer Name, Designation, Type of Business, Work Address
Financial Information	Monthly/Annual Income, Bank Account Details, Tax Returns
Loan Details	Type of Loan, Loan Amount, Tenure, Repayment Source
Asset & Liability Declaration	Immovable assets, investments, existing loans/credit cards
Co-applicant Details (if any)	Joint applicant's personal and financial information
Declaration & Signature	Consent to terms, data verification, legal declaration

3. Necessary Documents to be Submitted Along With Loan Application

Banks mandate the submission of supporting documents to verify identity, address, income, and purpose of the loan. Below are the commonly required documents grouped by category:

A. Identity Proof (Any one)

i.   PAN Card *(mandatory for financial transactions above a threshold)*
ii. Aadhaar Card
iii. Passport
iv. Voter ID
v.   Driving License

B. Address Proof (Any one)

i.   Utility Bills (Electricity/Water/Telephone)
ii. Passport
iii. Aadhaar Card
iv. Rental Agreement (with utility bill)
v.   Ration Card

C. Income Proof

For Salaried Individuals:

i.   Latest Salary Slips (last 3 months)

ii. Form 16 or Income Tax Return (last 2 years)

iii. Bank statements (last 6 months)

For Self-employed/Business Owners:

i.   Income Tax Returns (last 2–3 years)

ii. Profit & Loss Account and Balance Sheet

iii. Business registration documents

iv. GST returns

D. Employment/Business Proof

i.   Employment ID card / Offer letter / Appointment letter (for salaried)

ii. Registration certificate / Shop Act license / GST certificate (for business)

E. Loan-specific Documents

Type of Loan	Additional Documents
Home Loan	Property documents, Sale deed, Agreement to sell, Title deed, Approved building plan
Education Loan	Admission letter, Fee structure, Academic records, Co-borrower income proof
Vehicle Loan	Proforma invoice from dealer, Driving license
Personal Loan	Proof of need (if applicable)
Business Loan	Business profile, MSME registration, Project report, Collateral documents

Example: SBI Home Loan Application

State Bank of India (SBI) requires the following documents for a home loan:

i.   Duly filled loan application form with photographs

ii. KYC documents (Aadhaar, PAN)

iii. Salary slips (3 months), Form 16

iv. Bank account statement (6 months)

v.   Sanctioned plan and title documents of the property

SBI evaluates the application based on the applicant's income, credit score (usually CIBIL score), and property value. The processing time ranges from 7–15 working days.

Case Study: HDFC Personal Loan Digital Application

HDFC Bank, a leader in retail lending, introduced a paperless loan application system for salaried customers. By linking Aadhaar and PAN, the system fetches KYC automatically. The customer only needs to Latest salary slips, Bank statement and Employment details

In 2022, HDFC Bank reported that over 65% of personal loan disbursals were processed through their digital channel in less than 24 hours, showing the importance of streamlined documentation.

Importance of Accurate Documentation

Proper documentation helps:

i. Ensure smooth processing and timely loan approval

ii. Build borrower credibility

iii. Reduce fraud and risk for banks

iv. Comply with RBI and PMLA regulations

v. Determine eligibility and repayment capacity

Banks may reject applications if documents are missing, invalid, or inconsistent.

2.2.5 Submission of Documents

After filling the form, the applicant must:

1. Attach self-attested photocopies of KYC documents

After filling out the account opening form, the applicant must attach self-attested photocopies of all KYC documents required by the bank. These include copies of identity proof, such as Aadhaar, PAN card, passport, or voter ID, and address proof like a recent utility bill, Aadhaar, or driving license. Self-attestation—where the applicant signs on the photocopy—serves as a declaration that the copy matches the original document, helping the bank verify authenticity while maintaining a clear record for compliance with regulatory guidelines.

2. Submit passport-size photographs

A recent passport-size colour photograph is a mandatory part of the account opening documentation, as it helps the bank maintain a visual record of the customer. The photo is typically affixed to the account opening form in the designated space and is also stored in the bank's internal system to verify identity during future transactions. This step is important because it adds another layer of identification, reducing the risk of impersonation or fraud, especially when a customer visits a branch in person.

3. Carry originals for in-person verification

The applicant must also carry the original documents corresponding to the submitted photocopies when visiting the bank branch. A bank official will inspect these originals to confirm that the self-attested copies match the authentic documents. This in-person verification process is essential under RBI and PMLA norms because it ensures that the person opening the account is indeed the rightful holder of the identity documents, adding an extra safeguard against identity theft or fraudulent account creation.

In case of joint accounts, documents of all account holders must be submitted When a joint account is being opened, every individual listed as an account holder must submit their own set of self-attested KYC documents and photographs. Each joint applicant must also visit the branch together (or separately, if allowed by the bank) to complete their in-person verification. For example, if a husband and wife open a joint savings account with Bank of Baroda, both must submit documents proving their identity and address, and both must be verified by the bank to ensure full compliance with KYC and anti-money laundering norms.

2.2.6 Verification by Bank Officials

Once the customer submits the account opening form along with the required documents, the next crucial step is verification by bank officials, which ensures the authenticity and compliance of all submitted information. This process helps protect both the bank and the customer from fraudulent activities and aligns with regulatory standards set by the Reserve Bank of India (RBI).

1. Bank officials verify the originals

The bank officials begin by cross-checking the original documents brought by the customer with the self-attested photocopies submitted earlier. This includes verifying proof of identity (such as Aadhaar, PAN card) and address documents to ensure that they are genuine, valid, and unaltered. This step serves as a key safeguard against identity theft and document forgery, helping banks maintain secure customer onboarding practices.

2. Conduct in-person verification (IPV) – as per RBI norms

As per RBI's KYC Master Direction, an in-person verification (IPV) must be conducted by a bank representative. In IPV, the customer's presence is recorded during the document submission, and the officer verifies that the person submitting the documents matches the details and photograph on the ID. This verification can take place at the bank branch or digitally via video KYC methods offered by many banks today, ensuring that onboarding is both compliant and convenient.

3. Validate PAN through the Income Tax database

To meet regulatory and tax compliance requirements, the Permanent Account Number (PAN) provided by the applicant is verified through the Income Tax Department's online

database. The bank inputs the PAN into the system, which confirms whether the number is valid and correctly linked to the applicant's name and date of birth. This prevents the use of fake or duplicate PANs and helps track financial transactions under the tax system, particularly for high-value accounts.

4. Aadhaar verification using UIDAI for e-KYC

If the customer opts for e-KYC, the Aadhaar number provided is verified online through the UIDAI (Unique Identification Authority of India) system. The bank sends an OTP (One-Time Password) to the Aadhaar-linked mobile number for real-time verification, ensuring instant and secure validation. This method has become popular in digital banking as it enables quick, paperless, and remote account opening, especially in rural areas or for tech-savvy users.

Post-verification and account activation

After all documents are verified and cross-checked successfully, the bank approves the account application, generates a Customer ID, and shares the account number, passbook, and welcome kit (which may include a debit card and cheque book). The bank may also provide login credentials for internet and mobile banking at this stage. The entire process usually takes between 1 to 3 working days, depending on the bank's internal processing time and whether the application was submitted online or in person.

2.2.7 Account Activation and Welcome Kit

Upon successful opening:

1. Account Number and Customer ID are issued

Once the bank has completed all verification processes, the Account Number and Customer ID are generated. The account number is a unique identification code for the customer's specific account (e.g., savings, current), while the Customer ID is used to manage the overall customer profile, especially when a customer has multiple accounts with the same bank. These details are communicated to the customer through an account opening confirmation slip, email, SMS, or welcome letter.

2. Cheque Book, Passbook, and Welcome Kit are handed over or couriered

After the account is activated, the bank provides a Welcome Kit containing basic account materials. This usually includes a cheque book for making payments, a passbook for tracking transactions (for savings accounts), and important documents such as the terms and conditions of the bank. Depending on the bank's policy and the method of account opening (online or branch), these items are either handed over in person at the branch or sent via registered courier to the customer's address.

3. Internet banking credentials

As part of the digital onboarding process, the bank issues internet banking login credentials, typically consisting of a User ID and a temporary password. These credentials allow customers to access and manage their account online, check balances, transfer funds, pay bills, and perform various transactions 24/7. Once logged in for the first time, customers are usually prompted to set a permanent password and may activate additional security features like OTP verification.

4. Mobile banking registration option

To make banking more convenient, customers are also offered the option to register for mobile banking services, either during the account opening or shortly after activation. Registration can be done through the bank's mobile app or by visiting the branch, and once complete, the customer can carry out key transactions directly from their smartphone. Mobile banking apps typically include features such as real-time fund transfers (IMPS/UPI), account statements, card blocking, and QR payments, enabling customers to bank anytime, anywhere.

5. Debit Card or Smart Card, if applicable

A debit card or smart card is also issued to the customer for use at ATMs, point-of-sale machines, and for online purchases. This card is either delivered with the welcome kit or separately by courier and is typically PIN-enabled for secure usage. The debit card is linked directly to the customer's bank account, making it easy to access funds instantly. For example, many banks now offer RuPay, Visa, or MasterCard debit cards with features like international usage, cashback, or rewards programs.

Example: ICICI Bank

For instance, ICICI Bank issues a fully activated welcome kit within 48 hours of account approval. This includes a PIN-enabled debit card, cheque book, internet banking login details, and instructions to activate mobile banking. Such quick turnaround and complete digital access help ensure that the customer can begin using their new account with minimal delay and maximum convenience.

2.2.8 Debit Cards and Smart Cards

2.2.8.1 Debit Card

A debit card is a plastic payment card issued by banks and linked directly to a customer's savings or current account. It enables the cardholder to withdraw cash from ATMs, make payments at point-of-sale (POS) terminals, and conduct online transactions such as shopping, utility bill payments, and fund transfers. Unlike credit cards, debit card transactions immediately deduct the amount from the customer's account balance, promoting disciplined spending and eliminating the risk of debt accumulation.

1. ATM Cash Withdrawals

All debit cards issued by banks allow customers to withdraw cash from ATMs across the country and even abroad (in the case of international cards). Most banks provide a limited number of free ATM withdrawals per month, after which a nominal fee is charged. For example, a SBI Classic Debit Card allows up to 5 free ATM withdrawals per month at SBI ATMs in metro cities, offering convenience and access to funds at any time.

2. Online Shopping and Bill Payments

Modern debit cards can be used for online shopping on e-commerce platforms such as Amazon or Flipkart, as well as for paying utility bills, booking tickets, or subscribing to digital services. These cards work through card networks like Visa, Mastercard, and RuPay, which provide global or domestic payment support. For instance, an HDFC Bank Visa Debit Card can be used on international websites, while a RuPay debit card is typically accepted only within India.

3. PIN-Enabled Security

To ensure secure transactions, debit cards are PIN-enabled, meaning that the cardholder must enter a Personal Identification Number (PIN) during ATM and POS transactions. This 4-digit PIN acts as a security layer to prevent unauthorized usage, especially in case the card is lost or stolen. Banks also allow customers to change their PIN through ATMs or online banking platforms, promoting safer card management.

4. Linked to Customer's Bank Account with Transaction Limits

Since debit cards are directly linked to the customer's bank account, the available balance determines the transaction limit. Banks also impose daily limits on ATM withdrawals and shopping, which can be adjusted on request for added safety. For example, Axis Bank's Titanium debit card may have a withdrawal limit of ₹50,000 and a POS transaction limit of ₹1,00,000 per day, depending on the customer's account type.

2.2.8.2 Smart Card

A smart card is an advanced payment or identification card that contains an embedded microprocessor chip instead of or in addition to a magnetic stripe. This chip stores and processes data securely, making smart cards more resistant to fraud and tampering compared to traditional cards. Smart cards are used in banking, identity verification, digital wallets, and even public transportation systems, offering multi-purpose functionality.

1. Higher Security than Magnetic Strip Cards

The chip in a smart card offers encryption and dynamic authentication, making it significantly harder to clone or skim compared to magnetic stripe cards, which store

static data. When used at ATMs or POS machines, the chip generates a unique code for each transaction, providing additional security against fraud. This enhanced safety feature has led to global adoption of chip-based cards under the EMV standard (Europay, Mastercard, and Visa).

2. Use in Banking, ID Authentication, and Digital Wallets

Apart from banking, smart cards are used in government identity programs (e.g., e-passports, driving licenses), corporate employee IDs, and transport cards (e.g., metro smart cards). They can also be integrated with digital wallets and contactless payments, making them versatile in everyday use. For example, educational institutions use smart cards to combine student ID, library access, and meal payments into a single secure card.

Example: SBI EMV Chip Debit Cards

A real-world example is the State Bank of India (SBI), which issues EMV chip-enabled debit cards with smart card functionality. These cards allow contactless payments, encrypted security, and global acceptance through Visa or Mastercard. With features like tap-and-pay, these cards enable users to make quick transactions for small purchases without entering a PIN, thus combining convenience with safety.

2.2.9. Online Account Opening (Digital Onboarding)

With the advancement of digital technology and the growing need for convenient banking, online account opening, also known as digital onboarding, has become increasingly popular among banks in India. This method allows customers to open a bank account remotely, without visiting a branch, using mobile apps or official bank websites. The process is secure, efficient, and aligned with the Reserve Bank of India's digital banking guidelines, making banking services more accessible especially in rural and semi-urban areas.

Step 1: Enter Aadhaar and PAN

The digital process begins with the customer entering their Aadhaar number and PAN on the bank's mobile application or website. These are essential documents for identity verification and tax compliance. The Aadhaar serves as a universal identity, while the PAN is mandatory for linking the account with financial and income tax transactions.

Step 2: OTP-Based Authentication from UIDAI

Once the Aadhaar number is entered, an OTP (One-Time Password) is sent to the mobile number linked with Aadhaar, enabling real-time verification via UIDAI (Unique Identification Authority of India). This step confirms the identity of the applicant and ensures that only legitimate users with a valid Aadhaar-linked phone number can proceed with account opening. The e-KYC data retrieved includes name, address, date of birth, and gender.

Step 3: Upload Scanned Photo and Signature

The applicant is then prompted to upload a scanned passport-size photograph and signature, which are used for documentation and banking operations such as cheque issuance. Some banks offer the option to take a photo directly through the app interface. This digital submission eliminates the need for physical documents and accelerates the onboarding process.

Step 4: Video KYC or Live Verification

To meet RBI's KYC norms, banks conduct a Video KYC, where a bank official interacts with the applicant over a video call. During this call, the applicant is asked to show their face and display their original PAN or Aadhaar card, which is recorded and stored for compliance purposes. This method replaces in-person branch visits and ensures safe, paperless verification.

Step 5: Account Gets Activated Within 24 – 48 Hours

After successful verification, the account is typically activated within 24 to 48 hours, and the customer receives their account number, customer ID, and internet banking credentials via SMS or email. Banks may also courier a welcome kit with a debit card and cheque book. This quick turnaround time enhances customer satisfaction and encourages more users to adopt digital banking.

Case Study: Kotak Mahindra Bank's "811" Initiative

A landmark example of successful digital onboarding in India is the "811" initiative by Kotak Mahindra Bank, launched in March 2017. This digital banking product was introduced shortly after the Indian government's demonetisation drive, with the aim of promoting cashless transactions and supporting the Digital India mission. Named after the date of demonetisation (8/11), the initiative sought to transform banking by making it more accessible, efficient, and paperless.

The "811" account was designed as a zero-balance digital savings account, which users could open entirely online within a few minutes, using just their Aadhaar and PAN numbers. The onboarding process included OTP-based e-KYC verification, making the account accessible even to first-time users who had no previous relationship with a bank. This simplified process removed the need for physical branch visits and paperwork, significantly reducing barriers to entry, especially for young users and people in remote areas.

By 2022, Kotak Mahindra Bank reported that 70% of all new savings accounts were being opened through digital channels, largely due to the widespread adoption of the "811" platform. This success demonstrated not only the increasing acceptance of digital banking among Indian consumers but also the importance of innovation and customer-centric design in driving financial inclusion. The "811" model has since inspired other banks to adopt similar paperless, app-based account opening processes, making it a benchmark in India's digital banking evolution.

Recap

◊ Opening a Bank Account is essential for accessing financial services like deposits, withdrawals, and credit.

◊ Types of Accounts include Savings, Current, FD, RD, and NRI accounts, each designed for specific user needs.

◊ KYC Norms are mandatory and involve identity and address verification through valid documents.

◊ Loan Application Forms require detailed personal, financial, and employment details along with supporting documents.

◊ Digital Onboarding enables users to open accounts remotely through Aadhaar and PAN-based verification.

◊ Verification by Bank Officials involves checking submitted documents and conducting In-Person Verification (IPV).

◊ Welcome Kits typically contain a cheque book, passbook, debit card, and internet banking credentials.

◊ Debit and Smart Cards allow ATM use, online shopping, and are linked directly to the customer's account.

◊ Video KYC is an RBI-approved method for digital verification of identity in real time.

◊ Case Studies like Kotak 811 and HDFC digital loans show successful implementation of paperless banking.

Objective Questions

1. What is the full form of KYC?
2. Which Act governs anti-money laundering compliance in India?
3. What type of account is meant for business transactions?
4. Which bank launched the "811" digital banking initiative?
5. What is the purpose of a Welcome Kit?
6. Name one document used as identity proof.
7. What type of card contains a microprocessor chip?
8. Which account requires monthly fixed deposits for savings?
9. What is the minimum KYC document for Jan Dhan account?

10. What does IPV stand for?
11. Which organisation handles Aadhaar authentication?
12. Name one bank that offers paperless personal loan processing.

Answers

1. Know Your Customer
2. PMLA
3. Current Account
4. Kotak Mahindra Bank
5. Provide account tools
6. PAN Card
7. Smart Card
8. Recurring Deposit
9. Aadhaar
10. In-Person Verification
11. UIDAI
12. HDFC Bank

Self-Assessment Questions

1. Describe the steps in Account Opening
2. Briefly explain Debit Cards and Smart Card
3. Explain the steps in online bank account opening
4. Describe the importance of accurate documentation
5. What is UIDAI ?

Assignments

1. Explain the step-by-step procedure involved in opening a bank account.
2. Describe the various types of bank accounts and their features with examples.
3. What is KYC? Discuss its importance and the documents required.
4. Discuss the significance of digital onboarding in modern banking.
5. Elaborate on the necessary documents and key sections in a typical loan application form.
6. Collect and review sample account opening forms from two different banks and compare the information required.
7. Simulate the process of e-KYC-based digital onboarding using a flowchart.
8. Prepare a checklist of documents needed to apply for a personal loan for a salaried individual.
9. Interview a bank official or customer who has recently opened a digital account and write a report on their experience.
10. Create a presentation highlighting the differences between debit cards and smart cards, including usage scenarios.

Reference

1. Reserve Bank of India. (2023). *Master Direction – Know Your Customer (KYC) Direction*. RBI. https://www.rbi.org.in
2. Kotak Mahindra Bank. (2022). *811 Digital Savings Account*. https://www.kotak.com
3. HDFC Bank. (2022). *Personal Loan Process*. https://www.hdfcbank.com
4. Indian Banks' Association. (2020). *Model Bank Account Opening Form*.
5. Reserve Bank of India. (2021). *Guidelines on Fair Practices Code for Lenders*.
6. PMLA. (2002). *Prevention of Money Laundering Act*. Ministry of Finance, India.
7. UIDAI. (2022). *Aadhaar Authentication and e-KYC Guidelines*. https://uidai.gov.in

8. ICICI Bank. (2023). *Account Services and Documentation*. https://www. icicibank.com

9. Sharma, R. (2020). *Banking and Financial System in India*. New Delhi: Atlantic Publishers.
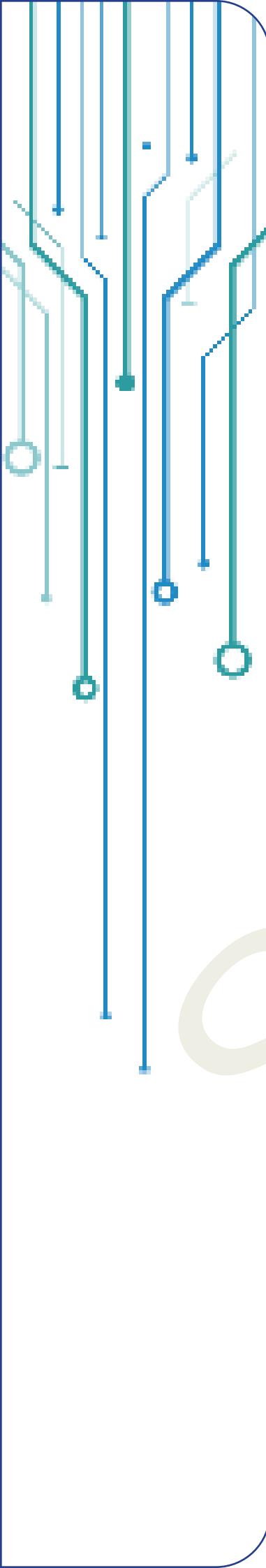
Suggested Reading

1. Kaur, H., & Bansal, A. (2021). *Digital Banking Trends in India*. International Journal of Finance and Banking Studies, 10(1), 45–56.

2. Sharma, R. (2020). *Banking and Financial System in India*. New Delhi: Atlantic Publishers.

3. Kaur, H., & Bansal, A. (2021). Digital Banking Trends in India. International Journal of Finance and Banking Studies, 10(1), 45–56.

Insurance

Unit ①

Introduction to Insurance

Learning Outcomes

After completing this unit, the learner will be able to:

◊ explain the concept, purpose, and importance of insurance in personal and economic contexts

◊ distinguish between different types of risks and their insurability

◊ identify the features of insurable risk and understand the key principles governing insurance contracts

◊ evaluate the primary and secondary functions of insurance and its role in national economic development

Prerequisites

Anita runs a small tailoring shop in a busy town. One night, a short circuit causes a fire that destroys her shop and sewing machines. With no savings or backup, Anita faces a major financial crisis. In contrast, her friend Leela, who owns a similar shop nearby, had an insurance policy that covered fire damage. After the incident, Leela filed a claim, received compensation, and was able to restart her business quickly. This real-life situation shows how insurance works as a shield against unexpected events. It helps people to avoid heavy financial burdens by offering support when losses occur. Whether it's protecting homes, businesses, vehicles, or lives, insurance provides confidence and stability. Understanding the basics of insurance including what it is, how it functions, and why it matters, is important for everyone. Therefore, this unit introduces the concept of insurance, explains different types of risks, and highlights how insurance benefits individuals, businesses, and the economy.

Keywords

Premium, Risk Pooling, Pure Risk, Insurable Interest, Utmost Good Faith

Discussion

3.1.1 Insurance

Ramesh, a shopkeeper in a small town, runs a grocery store that supports his entire family. One night during the monsoon season, a severe storm hits the town, damaging his shop and ruining most of his stock. Since Ramesh had no financial backup or support system, he had to borrow money at a high interest rate to restart his business, pushing him into debt.

Now consider another shopkeeper, Suresh, who runs a similar grocery store just a few streets away. Before the storm, Suresh had purchased an insurance policy that covered his shop and inventory. When the same storm damaged his shop, he informed the insurance company, which sent a surveyor to assess the loss. Within a few weeks, Suresh received a claim amount that helped him repair the damage and restock his goods, without needing to borrow money.

This illustration highlights the basic concept of insurance: it is a financial arrangement that protects against unforeseen risks. By paying a small amount regularly (called a premium), individuals or businesses can safeguard themselves from major financial losses due to accidents, natural disasters, theft, illness, or other unexpected events. Insurance offers peace of mind and financial security, helping people bounce back from setbacks with stability.

3.1.1.1 Definitions

"Insurance can be defined as a cooperative device to spread the loss caused by a particular risk over a number of persons who are exposed to it and who agree to ensure themselves against the risk". – Prof. R S Sharma

"Insurance is an arrangement by which a company or the state undertakes to provide a guarantee of compensation for specified loss, damage, illness, or death in return for payment of a specified premium." - Oxford Dictionary

"Insurance is a contract between two parties wherein one party agrees to compensate the other party for the loss or damage caused due to uncertain events in exchange for a regular premium." - IRDAI (Insurance Regulatory and Development Authority of India)

According to D.S. Hansell, *"Insurance is a social device for reducing or eliminating risk of loss to life and property."*

According to Reigel and Miller, "the function of insurance is primarily to decrease the uncertainty of events".

On the basis of the above definitions the following are the main features of insurance:

1. It is a cooperative device by which risks are distributed among large number of individuals.
2. It provides securities against losses or risks.
3. A common fund is raised among members to meet the losses.
4. It is a plan under which the losses of uncertain events are secured.

Legally insurance can be defined as " Insurance is a contact between two parties whereby one party agrees to undertake the risk of another in exchange for consideration known as premium and promises to pay a fixed sum of money to the other party on happening of an uncertain event (death) or after the expiry of a certain period in case of life insurance or to indemnify the other party on happening of an uncertain event in case of general insurance".

3.1.1.2 Key Elements of Insurance

i. Contract between insurer and insured: Insurance is based on a legally binding contract between the insurer (the company) and the insured (the policyholder). This contract, known as an insurance policy, outlines the terms, conditions, coverage details, exclusions, and responsibilities of both parties. Once agreed upon and signed, it ensures that the insurer will provide financial protection or compensation in exchange for a premium.

ii. Payment of premium: The insured must pay a fixed or periodic amount, known as the premium, to the insurer for the policy to remain active. This premium is determined based on the level of risk, coverage amount, duration of policy, and other underwriting factors. Timely payment of the premium is essential, as failure to do so may result in lapse or cancellation of the policy.

iii. Promise of compensation on the occurrence of a specified event: An insurance policy includes a promise from the insurer to compensate the insured in the event of a specified loss or incident, such as accident, illness, theft, or death. The compensation is provided as per the policy terms to help the insured recover financially from the loss. However, the claim is honoured only if the event is covered under the policy and all conditions are met.

3.1.1.3 Parties of Insurance

The following are the parties involved in an insurance contract:

1. Insured: The person seeking some surety against the possible loss is called insured.
2. Insurer: the person contracting to indemnify against the loss is the insurer.
3. Beneficiary: the person to whom the indemnity is paid is the beneficiary (who may or may not be the insured).
4. Insurance Policy: The written contract of insurance is the policy.

5. Premium: The price paid by the insured in fulfilment of his part of the contract is the premium.

6. Indemnity: The amount paid when a loss has been incurred is the indemnity.

3.1.2 Insurance and Risk

Risk refers to the uncertainty regarding the occurrence of an event that may lead to loss, damage, injury, or financial setback. It is inherent in nearly every aspect of human life such as personal, professional, social, and economic. Examples of Risks includes the following;

i. Loss of life due to accident or illness.

ii. Destruction of property due to fire or floods.

iii. Theft of assets.

iv. Liability for damages in a car accident.

Risk arises due to various factors such as natural disasters, human error, technical failure, health issues, or unforeseen circumstances. According to the Insurance Institute of India, risk is "the possibility of an unfortunate occurrence" that can be measured in terms of likelihood and impact.

In everyday life, people and businesses face multiple kinds of risks:

◊ **A businessman risks losing stock due to fire or theft**: For example, in 2019, a major fire broke out in a Mumbai textile market, destroying several shop owners' inventories. Those with fire insurance were compensated for the damage, while others suffered huge losses.

◊ **A family risks financial hardship if the earning member passes away unexpectedly**: For instance, during the COVID-19 pandemic, many families lost their sole breadwinners. Those with **life insurance** policies such as term plans were able to receive death benefits, helping them cope with sudden financial burdens.

◊ **A person driving a car risks accidents and damage**: In India, road accidents cause thousands of fatalities and injuries every year. As per the Ministry of Road Transport and Highways (2023 report), over 1.5 lakh people lost their lives in road accidents in 2022. Motor insurance helps cover repair costs, hospital bills, or legal liabilities resulting from such events.

Risk is not just a theoretical concept; it is real, measurable, and impactful. This is why understanding and managing risk is essential for financial security and long-term planning.

3.1.2.1 How Insurance and Risk Are Related

Insurance is a risk management mechanism that provides financial protection against unforeseen losses. It works on the principle of risk pooling, where individuals or businesses pay a small amount (premium) to an insurance provider in exchange for a promise of compensation if a specific risk occurs. In simple terms:

◊   Risk is the possibility of a loss.

◊   Insurance is the assurance that the loss will be financially covered.

According to the IRDAI (Insurance Regulatory and Development Authority of India), insurance is "a contract under which one party undertakes to compensate the other against a loss arising from specified events." This allows individuals and businesses to transfer the burden of risk to insurers, reducing uncertainty.

Example: Priya, who owns a bakery in Pune. She is aware that kitchen fires are a common risk in food businesses. She wisely purchases a fire insurance policy for her bakery premises and equipment. One day, due to an electrical short circuit, a fire breaks out, damaging expensive baking equipment and furniture. Since Priya was insured, the insurance company compensates her for the losses, allowing her to resume operations quickly without borrowing or losing savings. This example demonstrates the core function of insurance, not to eliminate risks, but to reduce the financial consequences of such risks.

3.1.3 Classification of Risk

Risks are a part of everyday life and are classified based on their characteristics, nature, and impact. Understanding the types of risks helps in determining which risks are insurable and how to manage them effectively. The major classifications include Pure and Speculative Risk, Financial and Non-Financial Risk, and Fundamental and Particular Risk. Each type has distinct features that influence decision-making in personal finance, business, and insurance.

3.1.3.2 Pure and Speculative Risk

Pure risks refer to situations where there is only the possibility of a loss or no loss, there is no chance of making a profit. These risks are beyond one's control and are usually accidental or unforeseen. Common examples include death, illness, fire, theft, or natural calamities. For instance, if a person's house is damaged in a flood, they face a pure risk. Since the outcome is either a loss (property damage) or no loss (if the flood misses their house), and never a gain, pure risks are considered insurable. This is why most insurance products such as life insurance, health insurance, and property insurance are designed to cover pure risks.

In contrast, speculative risks involve the possibility of either loss or gain. These risks are generally undertaken voluntarily in the hope of achieving a benefit. A classic example is investing in the stock market—the investor may make a profit or incur a loss. Similarly, starting a new business or gambling also falls under speculative risks. Because these are driven by personal decisions and involve an element of profit-making, speculative risks are not insurable. Insurance providers avoid covering speculative risks due to the difficulty in predicting and pricing them accurately.

3.1.3.2 Financial and Non-Financial Risk

Financial risks are those which can be expressed and measured in monetary terms.

These risks result in a direct financial loss and are quantifiable. For example, if a car is involved in an accident, the cost of repair is a financial risk. Likewise, hospital expenses following an illness or surgery also fall under this category. Since the extent of damage or loss can be calculated, these risks are often covered by insurance products such as motor insurance, health insurance, and property insurance. The insurability of financial risks makes them important in the field of personal and business risk management.

On the other hand, non-financial risks are those that cannot be measured in terms of money. These include emotional distress, mental trauma, social embarrassment, and reputational damage. For example, if someone faces public defamation or emotional suffering due to personal loss, it is considered a non-financial risk. Though such risks may have indirect economic consequences, they are difficult to quantify and insure. Insurance companies usually do not cover such risks because assigning a monetary value to emotional or psychological damage is highly subjective and lacks standard criteria.

3.1.3.3 Fundamental and Particular Risk

Fundamental risks are risks that affect large sections of society or entire populations. These are generally caused by broad external forces such as natural disasters (earthquakes, floods, droughts), wars, economic crises, or pandemics. They are usually beyond the control of individuals and require government intervention or public policy measures. For example, during the COVID-19 pandemic, millions of people around the world were affected by illness, job loss, and economic uncertainty. In India, the government introduced the PM Garib Kalyan Package insurance scheme for healthcare workers, reflecting the need for social insurance in managing fundamental risks.

In contrast, particular risks are personal in nature and affect specific individuals or small groups. These include theft, house fires, personal accidents, and vehicle damage. Such risks arise due to individual actions or localized events and are often within the control or influence of the person. For instance, if Ramesh's shop is burgled or his car meets with an accident, he experiences a particular risk. Because these risks are specific, measurable, and controllable, they are generally insurable. Insurance companies prefer such risks because they can evaluate the probability of occurrence and determine suitable premiums.

3.1.4 Features of Insurable Risk

For a risk to be insurable, it must meet certain specific criteria. These features help insurance companies to assess the probability and cost of the risk, allowing them to set fair premiums and ensure long-term sustainability of the insurance system. Below are the key characteristics that make a risk insurable:

1. Pure Risk

Only pure risks, which involve the possibility of loss or no loss (but never a gain), are considered insurable. These risks are generally beyond the control of the insured and occur unexpectedly, such as illness, fire, or death. Unlike speculative risks (which

can result in profit or loss), pure risks have outcomes that are either neutral or negative, making them suitable for insurance coverage.

2. Definite and Measurable

An insurable risk must be definite in time, place, and cause, and the potential loss should be measurable in financial terms. The insurer must be able to assess how much compensation to provide and under what conditions. For example, in a motor accident, the time of occurrence, the damage caused, and the repair cost can usually be clearly documented and quantified.

3. Accidental and Unexpected

The insured event must occur accidentally or unexpectedly, rather than by deliberate action. Insurance does not cover losses that are planned or intentional, as this would encourage fraud and moral hazard. For instance, life insurance covers death due to natural causes or accidents, but not suicide within the initial policy period, which is considered a non-accidental risk.

4. Large Number of Similar Exposure Units

The risk should apply to a large number of similar exposure units (e.g., people, homes, vehicles) to enable insurers to apply the law of large numbers. This principle allows insurers to predict overall losses more accurately and spread risk across a wide pool of policyholders. For example, by insuring thousands of vehicles, an insurer can estimate the probable number of accidents in a year and price premiums accordingly.

5. Not Catastrophic

The risk must not be catastrophic in nature—meaning it should not affect a large number of insured units simultaneously. Catastrophic events like wars, nuclear explosions, or major natural disasters (e.g., tsunamis) can lead to widespread losses, overwhelming insurance companies and threatening their solvency. That's why such events are typically excluded from standard insurance policies and may require separate coverage or government intervention.

6. Economically Feasible

The insurance premium must be affordable and economically viable for the insured, and the potential compensation should be meaningful relative to the cost. If the cost of coverage is too high, people will avoid buying insurance, defeating its purpose. At the same time, insurers must ensure that the premium collected is sufficient to cover claims and administrative expenses.

Example: Insuring Human Life

A person's life is an example of an insurable risk because it satisfies all the above features. Death is a pure, accidental, and unpredictable event that causes a financial loss, especially to dependents. Life insurance companies use actuarial data to calculate the likelihood of death based on age and health, making the risk measurable, affordable,

and spread across millions of policyholders, thus fulfilling the essential conditions of insurability.

3.1.5 Functions of Insurance

Insurance serves a vital function in modern society by offering financial protection and risk management to individuals, businesses, and the economy. It acts not only as a safety net against unexpected losses but also plays a broader role in economic development by mobilising savings, facilitating investments, and supporting trade and commerce. Through its primary and secondary functions, insurance contributes to financial stability and confidence across multiple sectors.

3.1.5.1 Primary Functions

1. Risk Transfer

One of the fundamental roles of insurance is to transfer risk from an individual or business to the insurance company. Instead of bearing the full burden of a potential financial loss, the insured pays a premium to the insurer, who assumes responsibility for certain defined risks. For instance, a car owner with motor insurance shifts the risk of vehicle damage or theft to the insurance provider, thereby avoiding unexpected out-of-pocket expenses.

2. Risk Pooling

Insurance operates on the principle of risk pooling, where premiums collected from a large number of policyholders are pooled together into a common fund. This fund is then used to compensate those who experience a covered loss, thus spreading the financial burden across many contributors. For example, health insurance companies use the pooled premiums to cover hospital expenses for policyholders who fall ill, even though only a fraction of them may claim during a given year.

3. Compensation

Insurance provides timely financial compensation to the insured in the event of an unforeseen and covered loss or damage. This compensation helps the individual or business to recover quickly and continue functioning without severe economic hardship. For example, if a house insured under a fire insurance policy is damaged due to fire, the insurer pays out the repair or rebuilding costs as per the policy terms, reducing the homeowner's financial burden.

3.1.5.2 Secondary Functions

1. Encourages Savings

Certain types of insurance, especially life insurance, serve a dual purpose by providing both protection and a mechanism for long-term savings. Policyholders pay

regular premiums, a portion of which is invested, and receive a lump sum or periodic benefits either on maturity or death. For example, an endowment life insurance plan not only provides a death benefit but also accumulates a corpus that the insured can receive at the end of the policy term, supporting future financial goals like children's education or retirement.

2. Promotes Financial Stability

Insurance offers peace of mind by covering unpredictable events such as accidents, illness, or natural disasters, thus reducing the financial uncertainty in individuals' and businesses' lives. This stability enables better planning, investment, and continuity of operations even in the face of adversities. For instance, a factory insured against machinery breakdown can resume operations promptly with the insurer's assistance, ensuring minimal disruption to its supply chain.

3. Credit Enhancement

Insurance acts as a form of collateral or risk mitigation, which enhances the creditworthiness of individuals and businesses in the eyes of lenders. Banks and financial institutions are more willing to extend credit to borrowers who are covered by insurance, as the risk of default is lowered. For example, home loan providers often require the borrower to purchase mortgage protection insurance, which ensures that the loan will be repaid in case of the borrower's death or disability.

4. Supports Business Operations

By covering various operational and business risks such as fire, theft, liability, or employee injuries insurance enables businesses to operate with greater confidence and security. It also allows firms to focus on growth and innovation without the constant fear of unpredictable losses. For example, a retail business with property and liability insurance can confidently open multiple branches, knowing that unforeseen events like customer injury or stock damage are covered.

3.1.6 Importance of Insurance

Insurance plays a critical role in safeguarding the financial well-being of individuals, ensuring business continuity, and supporting national economic development. It acts as a financial buffer against unexpected events, enabling stability and resilience across all sectors. From providing personal security to enhancing credit access and mobilising public savings, insurance is a cornerstone of a well-functioning society.

3.1.6.1 To Individuals

a. **Provides security against life and health risks :** Insurance offers financial protection against life's uncertainties such as illness, disability, accidents, and premature death. Health and life insurance ensure that individuals and their families are not left financially devastated by medical emergencies or the loss of a breadwinner. For example, a person diagnosed with a serious illness can

rely on their health insurance policy to cover costly hospital treatments and surgeries.

b. **Acts as an investment (especially life insurance) :** Certain types of life insurance not only provide coverage but also act as a long-term investment or savings plan. Policies such as endowment plans or unit-linked insurance plans (ULIPs) accumulate wealth over time, offering maturity benefits along with life cover. For instance, a parent may buy a child education plan through a life insurer, which helps them accumulate funds for future academic expenses.

c. **Offers peace of mind :** Knowing that one is protected from major financial shocks brings immense psychological comfort and reduces anxiety. Insurance allows individuals to live, work, and plan for the future without the constant fear of financial ruin due to unforeseen events. For example, a senior citizen with a comprehensive health insurance plan feels more secure about facing age-related medical issues.

3.1.6.2 To Businesses

a. **Reduces uncertainty :** Insurance protects businesses from various risks such as property damage, liability claims, employee injuries, and business interruptions. This protection reduces financial uncertainty and allows entrepreneurs to focus on growth and innovation. For example, a logistics company with transit insurance can continue its operations confidently even if goods are damaged during transport.

b. **Enables risk management :** Insurance forms a key component of a company's risk management strategy by transferring potential losses to the insurer. Businesses can assess risks and obtain appropriate coverage to mitigate the impact of operational disruptions. For instance, a manufacturing unit may take machinery breakdown insurance to avoid heavy repair costs that could affect productivity.

c. **Facilitates access to credit and funding :** Lenders are more willing to provide loans to insured businesses, as insurance minimises the risk of default due to unforeseen events. Insurance policies can serve as collateral or be mandated as part of loan conditions, making it easier to obtain financing. For example, a small enterprise may secure a business loan more easily if it has a fire and property insurance policy covering its premises and inventory.

3.1.6.3 To the Economy

a. **Mobilises national savings :** Insurance companies collect premiums and invest them in long-term financial instruments, contributing to the mobilisation of national savings. These funds are channelled into infrastructure, public sector projects, and other areas that stimulate economic growth. For instance, the Life Insurance Corporation (LIC) of India is one of the largest institutional investors in government securities and infrastructure bonds.

b. **Supports capital market development :** By investing in stocks, bonds, and mutual funds, insurance companies help deepen capital markets and provide liquidity. Their long-term investments offer stability to financial markets and

support the availability of capital for businesses and the government. For example, insurance funds often back initial public offerings (IPOs), enabling companies to raise funds for expansion.

c. **Helps reduce the fiscal burden on the government during disasters :** During natural calamities or large-scale accidents, insured individuals and businesses rely on insurance payouts rather than state aid, reducing the financial pressure on public resources. Insurance thus acts as a private safety net that complements government relief efforts. For example, after Cyclone Fani in Odisha, insured properties and crops received quicker financial support through insurance claims, easing the burden on disaster relief funds.

Example: The Pradhan Mantri Jeevan Jyoti Bima Yojana (PMJJBY), launched by the Government of India, offers life insurance coverage of ₹2 lakh for an annual premium of just ₹436. This scheme has significantly improved financial inclusion by making life insurance accessible to low-income and rural populations. It ensures that families of the deceased policyholders receive immediate support, reducing their vulnerability and strengthening the nation's social safety net.

3.1.7 Principles of Life Insurance

Life insurance is governed by fundamental legal and ethical principles that ensure fairness, transparency, and accountability in the relationship between the insurer and the insured. These principles form the backbone of life insurance contracts and help build trust in the system. Understanding these principles is essential for both policyholders and insurance providers to uphold contractual obligations and ensure the validity of claims.

3.1.7.1 Principle of Utmost Good Faith (Uberrimae Fidei) :

This principle requires both the insurer and the insured to disclose all relevant facts truthfully and completely at the time of entering into the insurance contract. The insured must inform the insurer about pre-existing medical conditions, lifestyle habits (such as smoking or alcohol use), and other material facts that may affect the risk assessment. Example: If an applicant hides a history of heart disease while purchasing a life insurance policy, the insurer can later deny the claim on grounds of misrepresentation.

3.1.7.2 Principle of Insurable Interest

The person buying the life insurance policy must have a legitimate financial or emotional interest in the life of the person being insured. This ensures that the policyholder would suffer a loss upon the insured's death, and discourages speculative insurance. Example: A husband can legally take a life insurance policy on his wife because he has an insurable interest, but he cannot insure the life of a colleague or neighbour unless he can prove a valid financial dependence.

3.1.7.3 Principle of Indemnity *(Not directly applicable to life insurance)*

Unlike general insurance, the principle of indemnity where compensation is based on the extent of loss does not apply to life insurance, because the value of human life is immeasurable. Life insurance pays a pre-decided fixed amount (sum assured) regardless of the actual financial loss suffered. Example: If a life insurance policy has a sum assured of ₹20 lakhs, the nominee will receive the full amount upon the insured's death, irrespective of any other financial circumstances.

3.1.7.4 Principle of Risk Management / Pooling of Risk :

This principle states that insurers collect premiums from a large group of policyholders to create a risk pool. The losses (claims) of a few are paid from this pool, making insurance affordable and sustainable for all. Example: In a group of 10,000 life insurance policyholders, only a few may die in a given year, and the insurer uses the combined premiums to pay the death benefits to those few claimants.

3.1.7.6 Principle of Proximate Cause (Causa Proxima)

This principle helps determine the actual, immediate cause of death to assess whether it falls within the policy coverage, especially in specialized policies. It is mainly applicable to life insurance riders such as accidental death or critical illness riders, where the cause of death must be proven to trigger the benefit. Example: If a policyholder dies due to a car accident and has an accidental death rider, the proximate cause is the accident, and the rider benefit will be paid.

3.1.7.7 Principle of Contribution *(Not applicable to life insurance)*

This principle is relevant in general insurance where the same subject matter is insured by multiple insurers; each contributes proportionally in case of a loss. In life insurance, however, this principle does not apply because multiple policies can pay out the full sum assured independently. Example: If a person has three life insurance policies, their nominees will receive the sum assured from all three insurers upon the insured's death without any contribution adjustment.

Case Study: LIC – Life Insurance Corporation of India

The Life Insurance Corporation of India (LIC) is not just the largest life insurance company in India, but also one of the most trusted financial institutions in the country. Established in 1956 following the nationalisation of over 245 private insurers, LIC has played a pivotal role in popularising life insurance as a tool for financial security among millions of Indians. Over the decades, it has expanded its reach to urban and rural areas alike, promoting insurance awareness, financial inclusion, and long-term savings.

1. **Offers a wide range of policies: endowment, term, money-back, and ULIPs** : LIC provides diverse life insurance products tailored to suit the varying needs of individuals at different life stages. These include endowment plans (which offer both insurance and savings), term plans (pure risk cover), money-back policies (which provide periodic survival benefits), and ULIPs (unit-linked insurance plans that combine market-linked returns with life cover). Example: LIC's Jeevan Anand is a popular endowment plan offering lifelong risk cover even after policy maturity, while LIC Tech Term is a pure protection term policy that offers high coverage at low premiums for tech-savvy customers purchasing online.

2. **As of March 2023, LIC held around 62% market share in individual life insurance policies** : LIC continues to dominate the Indian life insurance market despite the entry of numerous private sector players since the industry was liberalised in 2000. According to data from IRDAI (Insurance Regulatory and Development Authority of India), LIC accounted for approximately 62% of the market share in individual life insurance business in terms of new policies sold and premium collected. This dominance reflects LIC's brand credibility, extensive agency network, strong rural presence, and ability to offer competitive returns to policyholders.

3. **The company contributes significantly to infrastructure funding and national savings** : Beyond offering life insurance, LIC plays a vital role in India's economy by investing policyholder funds in long-term infrastructure and public sector projects. It is one of the largest institutional investors in India, with significant holdings in government securities, roads, railways, power, housing, and public sector bonds. As of 2023, LIC had invested over ₹39 lakh crore in various sectors, helping mobilise national savings and supporting government initiatives such as Bharat Mala (road development) and PMAY (housing). This investment activity boosts economic development and creates employment across sectors.

LIC stands as a benchmark in the Indian insurance industry, balancing its social responsibility with financial performance. Its wide range of products, market leadership, and contribution to national development make it a model public sector enterprise. As the insurance sector continues to grow with digital transformation and rising awareness, LIC remains a key player in ensuring financial security and long-term wealth creation for the Indian population.

Recap

◊   Insurance protects individuals and businesses from unforeseen financial losses due to events like illness, death, or accidents.

◊   Insurance addresses financial impacts of measurable and uncertain risks.

◊   Insurable risks are specific, only pure, measurable, accidental, and non-catastrophic risks are generally insurable.

- ◊ Insurance functions beyond compensation by promoting savings, credit access, and financial stability in society.
- ◊ Legal principles like utmost good faith, insurable interest, and proximate cause form the basis of life insurance contracts.

Objective Questions

1. What is the term for the amount paid periodically for insurance?
2. What type of risk is insurable: Pure or Speculative?
3. What principle requires full disclosure in insurance contracts?
4. Which principle relates to determining the actual cause of a loss?
5. What is the full form of IRDAI?
6. Name the largest life insurance company in India.
7. Which principle is not applicable to life insurance: Indemnity or Utmost Good Faith?
8. What type of risk involves both gain and loss?
9. What kind of risk affects the whole society or region?
10. Which principle ensures compensation only if there is a legitimate financial interest?
11. What is the term for grouping similar risks to predict losses?
12. Name one life insurance policy offered by LIC.

Answers

1. Premium
2. Pure
3. Utmost Good Faith
4. Proximate Cause
5. Insurance Regulatory and Development Authority of India
6. LIC
7. Indemnity
8. Speculative Risk

9. Fundamental Risk
10. Insurable Interest
11. Risk Pooling
12. Jeevan Anand

Self-Assessment Questions

1. Explain the features of Life Insurance?
2. Describe the Importance of Insurance
3. Illustrate different functions of Insurance
4. Explain the features of Insurable rule
5. Illustrate the different types of lists and there insurability

Assignments

1. Explain the concept of insurance and its significance in modern society.
2. Discuss the classifications of risk with suitable real-life examples.
3. Describe the key features that make a risk insurable.
4. Elaborate on the primary and secondary functions of insurance.
5. Analyze the principles of life insurance with examples for each principle.
6. Survey Assignment: Interview five individuals on their awareness and use of insurance products. Present the findings in a report.
7. Case Study Analysis: Compare the cases of Ramesh and Suresh mentioned in the unit to highlight the role of insurance in risk management.
8. Policy Review: Collect a sample insurance policy (e.g., motor or life insurance) and identify the key components and clauses.
9. Newspaper Analysis: Collect 3 recent news stories where insurance played a critical role and write a summary explaining its application.
10. Poster Presentation: Create an informative poster explaining the types of risks and insurable risks with visual illustrations.

Reference

1. Hansell, D. S. (2020). *Principles and Practices of Insurance*. New Delhi: Global Press.
2. IRDAI. (2023). *Annual Report 2022-23*. Insurance Regulatory and Development Authority of India. https://www.irdai.gov.in
3. Mishra, M. N., & Mishra, S. B. (2016). *Insurance: Principles and Practice*. S. Chand Publishing.
4. Black, K., & Skipper, H. D. (2014). *Life and Health Insurance*. Pearson Education.
5. Rejda, G. E., & McNamara, M. J. (2021). *Principles of Risk Management and Insurance* (14th ed.). Pearson.
6. Vaughan, E. J., & Vaughan, T. (2013). *Fundamentals of Risk and Insurance* (11th ed.). Wiley.
7. Kothari, C. R. (2018). *Research Methodology: Methods and Techniques* (4th ed.). New Age International Publishers.
8. National Insurance Academy. (2022). *Essentials of Insurance*. Pune: NIA Publications.
9. LIC India. (2023). *Performance Highlights*. https://www.licindia.in
10. Economic Survey of India. (2023). *Chapter on Financial Sector*. Ministry of Finance.

Suggested Reading

1. Hansell, D. S. (2020). *Principles and Practices of Insurance*. New Delhi: Global Press.
2. IRDAI. (2023). *Annual Report 2022-23*. Insurance Regulatory and Development Authority of India. https://www.irdai.gov.in
3. Mishra, M. N., & Mishra, S. B. (2016). *Insurance: Principles and Practice*. S. Chand Publishing.
4. Black, K., & Skipper, H. D. (2014). *Life and Health Insurance*. Pearson Education.
5. Rejda, G. E., & McNamara, M. J. (2021). *Principles of Risk Management and Insurance* (14th ed.). Pearson.
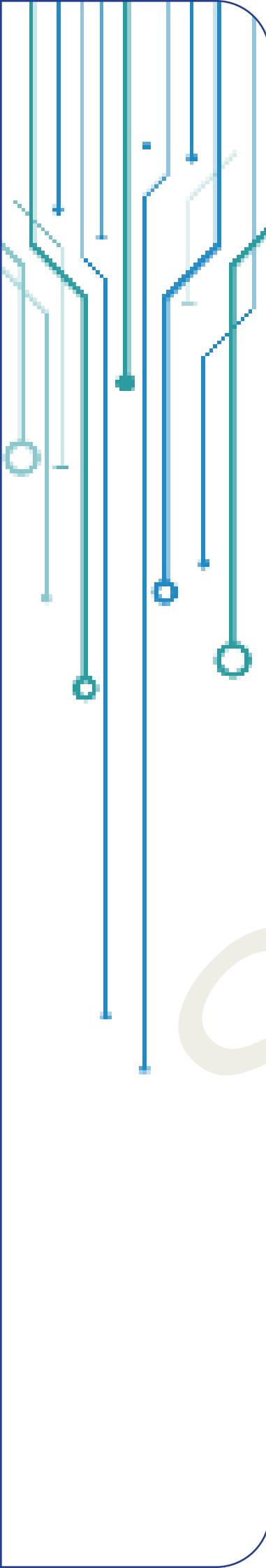
Unit ②
Types of Insurance

Learning Outcomes

After completing this unit, the learner will be able to;

◊ explain the major classifications and types of insurance products available in India

◊ analyse the principles, features, and benefits of various life and general insurance policies

◊ interpret the role and process of underwriting, premium calculation, and essential insurance documents

◊ apply knowledge of claim settlement procedures through practical and case study examples

Prerequisites

You are a shopkeeper in a small town. One night, a fire breaks out in the market and destroys several shops, including yours. While others worry about starting over from scratch, you are able to rebuild quickly because you had a fire insurance policy that covered your losses. Insurance works like this, providing a financial safety net when unexpected events threaten our health, property, livelihood, or life itself. It is essentially a promise from an insurance company to protect you from certain risks in exchange for a regular payment called a premium.

In India, the insurance sector is diverse and covers a wide range of needs, from securing a family's future through life insurance, to protecting vehicles, homes, crops, and businesses through general insurance. Understanding the different types of insurance helps individuals and organisations choose the right cover for their specific risks. This unit will take you through the main categories of insurance, their principles, features, and benefits, as well as the processes involved in underwriting, premium calculation, and claim settlement, ensuring you can make informed decisions about financial protection in real-life situations.

Keywords

Underwriting, Sum Assured, Cashless Facility, Rider Indemnity

Discussion

3.2.1 Classification of Insurance Business in India

Insurance in India is broadly classified into two major categories based on the nature of the risk covered: Life Insurance and General Insurance. Life insurance deals with the protection of human life, while general insurance covers non-life assets and liabilities such as property, health, vehicles, and businesses. Both categories play a crucial role in ensuring financial stability for individuals and organisations. This classification helps consumers to choose policies based on specific needs and risk profiles.

3.2.1.1 Life Insurance

Life insurance is a financial contract between an individual (the policyholder) and an insurance company, where the insurer promises to pay a specified sum of money to the nominee upon the death of the insured or on policy maturity. It serves as a protective financial tool, especially for dependents of the insured, providing income replacement, debt coverage, and peace of mind in case of unforeseen events. In some policies, the insured receives survival benefits if they live beyond the policy term, helping in long-term savings and planning for future goals like children's education, marriage, or retirement. Life insurance policies may also offer tax benefits under Indian income tax laws, making them a popular component of personal financial planning.

Life insurance can be defined as the contract, whereby the insurer in consideration of a premium undertakes to pay a certain sum of money either on death of the insured or on the expiry of a fixed period.

Features of Life Insurance :

1. Life insurance is an outcome of offer and acceptance. The offer is made by the insured and acceptance is done by the insurer.

2. The insurance company agrees to pay a certain sum of money either on the death of the insured or on the maturity of the policy whichever is earlier.

3. Life insurance is not a contract of indemnity. Because we can not calculate the value of life in terms of money.

4. Insurable interest must be present at the time of taking policy and which may may not be present at the time of death of the insured.

Various Life Insurance Plans:

1. Term Plan

A term insurance plan is the simplest and most affordable form of life insurance. It provides pure life cover for a specified period and pays the sum assured only if the insured dies during the policy term. If the policyholder survives the term, there is no maturity benefit. This type of policy is ideal for individuals seeking high coverage at low premiums, particularly young earners or families with dependents.

Example: LIC's Tech Term plan is a popular term insurance product offering high sum assured with an online application process and affordable premiums.

Features of Term Plan

a. **Pure Protection :** Offers financial protection only in case of the death of the insured during the policy term.

b. **No Maturity Benefit :** If the insured survives the term, no money is paid (unless it is a return of premium plan).

c. **Affordable Premiums :** Provides high sum assured at relatively low premiums compared to other life insurance types.

d. **Flexible Terms :** Policyholders can choose the coverage period (e.g., 10, 20, 30 years).

e. **Tax Benefits :** Premiums paid qualify for tax deductions under Section 80C of the Income Tax Act.

2. Endowment Plan

An endowment plan is a combination of insurance protection and savings. It pays out the sum assured either upon death during the policy term or as a lump sum at maturity if the insured survives. This dual benefit makes it suitable for individuals who wish to secure their family's future while also building a financial corpus for personal goals. These policies often come with optional bonuses and riders that enhance returns.

Example: LIC's New Endowment Plan offers life cover along with a lump sum maturity amount, including reversionary bonuses and a final additional bonus.

Features of Endowment Plan

a. **Dual Benefit**: Offers both life cover and savings, with payout on death or maturity.

b. **Lump Sum Payout**: Sum assured (plus bonuses) is paid either on death during the term or on policy maturity.

c. **Encourages Savings**: Helps to build a financial corpus for future needs like education or marriage.

d. **Participating Options**: Many endowment plans participate in the insurer's profits and offer reversionary bonuses.

e.   **Loan Facility**: Policyholders can borrow against the policy after a few years of premium payment.

3. Whole Life Policy

A whole life policy provides coverage for the entire lifetime of the insured, typically up to 100 years of age. The policy pays out the sum assured to the nominee upon the insured's death, regardless of when it occurs. This type of insurance is designed to offer lifelong protection and may also accumulate a cash value over time. It is especially useful for creating a legacy or ensuring financial support for dependents far into the future.

Example: LIC's Jeevan Umang is a whole life cum income plan that offers annual survival benefits after the premium payment term and a lump sum to the nominee upon the insured's death.

Features of Whole Life Policy

a.   **Lifetime Coverage**: Provides coverage for the entire life of the insured, usually up to 100 years.

b.   **Death Benefit Guaranteed**: Sum assured is paid to the nominee upon the insured's death, whenever it occurs.

c.   **Wealth Transfer Tool**: Helps in estate planning and ensuring financial security for the next generation.

d.   **Bonus Additions**: Participating whole life policies may earn annual bonuses, increasing the final payout.

e.   **Limited Premium Option**: Some plans allow paying premiums for a limited time while coverage continues lifelong.

4. Unit Linked Insurance Plan (ULIP)

ULIPs are hybrid insurance products that combine life cover with market-linked investments. A portion of the premium is used to provide life insurance, while the remaining is invested in equity, debt, or balanced funds based on the policyholder's risk preference. ULIPs offer the potential for wealth creation along with financial protection but are subject to market risks. They are suitable for investors who seek life cover along with returns from capital markets.

Example: LIC's SIIP (Systematic Investment Insurance Plan) is a ULIP that allows policyholders to invest in multiple fund options while enjoying life insurance benefits.

Features of Unit Linked Insurance Plan (ULIP)

a.   **Insurance plus Investment**: Combines life insurance with investment in equity, debt, or balanced funds.

b.   **Market-Linked Returns**: Returns are based on market performance of the chosen funds.

c.   **Fund Switching Option**: Policyholders can switch between fund types (equity to debt, etc.) during the policy term.

d. **Lock-in Period**: Typically has a 5-year lock-in before withdrawal is allowed.

e. **Transparency & Flexibility**: Offers transparency on charges and fund performance, with optional top-ups and riders.

5. Money Back Policy

Money back policies provide periodic payments, known as survival benefits, during the policy term, in addition to the life cover. If the insured survives certain milestones of the policy term, they receive a portion of the sum assured, and the remaining is paid at maturity or to the nominee in case of death. This type of policy is ideal for individuals seeking liquidity along with protection. It is particularly popular among those who need regular payouts for planned expenses like education, vacations, or household needs.

Example: LIC's Bima Shree is a money-back policy that offers guaranteed survival benefits, final maturity benefits, and death cover, targeted toward high-net-worth individuals.

Features of Money Back Policy

a. **Periodic Returns**: Provides regular payouts (survival benefits) during the policy term.

b. **Life Cover**: Offers death benefit even after part of the sum assured is already paid out as survival benefits.

c. **Maturity Benefit**: Remaining sum assured plus bonuses (if applicable) is paid at the end of the term.

d. **Higher Premiums**: Premiums are usually higher due to regular payouts and maturity benefit.

e. **Ideal for Liquidity Needs**: Suitable for those who need funds at regular intervals, e.g., for children's education.

6. Pension and Annuity Plans

Pension and annuity plans are life insurance products designed to provide a steady income after retirement. These plans help individuals accumulate a retirement corpus during their working years and later convert it into regular payouts (annuities) to ensure financial independence in old age. There are two phases in such plans: the accumulation phase, where the policyholder pays premiums, and the annuity phase, where they receive periodic income. These plans are ideal for senior citizens who need guaranteed income for expenses like healthcare, living costs, or emergencies.

Example: LIC's Jeevan Akshay VII is a popular annuity plan that offers immediate lifelong income options to retirees, with choices like monthly or annual payouts.

Features of Pension and Annuity Plans

a. **Retirement Planning Tool**: Helps build a retirement corpus and ensures a steady income post-retirement.

b. **Two Phases – Accumulation & Annuity**: Premiums are paid during the accumulation phase; regular payouts begin in the annuity phase.

c. **Lifelong Income**: Many plans provide lifelong annuity to the policyholder or spouse.

d. **Tax Benefits**: Contributions qualify for deductions under Section 80CCC and 80C.

e. **Guaranteed Payout Options**: Various annuity options available, such as monthly, quarterly, or joint life annuity.

3.2.1.2 General Insurance

General insurance, also known as non-life insurance, provides financial protection against losses that do not involve human life. These policies cover tangible assets like vehicles, homes, health, travel, and business properties, offering compensation for damage, theft, liability, or unexpected emergencies. Unlike life insurance, general insurance policies are usually short-term contracts and need to be renewed periodically. These insurance products are essential for individuals, families, and businesses to manage risks and avoid severe financial disruptions caused by accidents, natural disasters, or liabilities.

3.2.1.2.1 Principles of General Insurance

1. **Principle of Utmost Good Faith (Uberrimae Fidei) :** Both the insurer and the insured are required to disclose all relevant facts honestly at the time of entering into the contract. Any misrepresentation or concealment can lead to claim rejection. Example: A policyholder must inform the insurer if they regularly engage in risky activities like mountaineering.

2. **Principle of Insurable Interest :** The policyholder must have a financial or emotional interest in the continued safety of the insured person. This ensures the insurance is taken to protect against genuine loss rather than for speculative gain. Example: A business owner can insure their key employee but cannot insure an unrelated celebrity.

3. **Principle of Indemnity :** The goal is to restore the insured to the same financial position they were in before the accident, without allowing profit. While this applies to medical reimbursements, lump-sum benefits for disability or death are fixed amounts agreed in advance. Example: If hospital expenses are ₹80,000, the insurer reimburses that amount, not more.

4. **Principle of Subrogation :** After paying the claim, the insurer can recover the amount from any third party responsible for the accident. This prevents double recovery by the insured.

   Example: If a bus company is liable for an accident, the insurer may sue them after settling the insured's hospital bills.

5. **Principle of Contribution :** If the insured has multiple accident policies covering the same risk, each insurer shares the claim proportionately. This prevents over-compensation.

6. Example: If two policies cover the same ₹1,00,000 loss, one may pay ₹60,000 and the other ₹40,000.

3.2.1.2.2 Types of General Insurance

Various Types of General Insurance are discussed below;

A. Fire Insurance

Fire insurance offers protection against losses caused by fire or related perils such as explosion, lightning, or smoke. It covers damage to buildings, stock, machinery, furniture, and other contents, providing compensation to help repair or rebuild after a fire-related event. This insurance is especially important for homeowners, shopkeepers, and manufacturers. Policies may also include add-on covers for earthquake, terrorism, and fire brigade charges.

Fire insurance is a contract between the insured and the insurer where the insurer agrees to compensate the insured for loss or damage caused by fire or related perils (like lightning, explosion, or smoke) to property. It provides financial protection against accidental fire outbreaks that damage buildings, stock, machinery, furniture, and other assets.

According to the Insurance Regulatory and Development Authority of India (IRDAI), fire insurance policies cover loss or damage caused by fire, lightning, explosion/implosion, aircraft damage, riots, strikes, storm, cyclone, floods, impact damage, landslide, and more under the Standard Fire and Special Perils Policy.

Example: A garment factory in Ludhiana insured under a fire policy received compensation after a short-circuit caused a major fire, damaging inventory and machines.

Principles of Fire Insurance

Fire insurance is governed by key insurance principles that ensure fairness and validity of the contract:

i.   **Insurable Interest:** The insured must have a financial interest in the property. This means they must suffer a financial loss if the property is damaged by fire. *Example: A shop owner has insurable interest in his inventory. A neighbour does not.*

ii. **Utmost Good Faith (Uberrimae Fidei):** Both parties must disclose all material facts honestly. The insured must declare the nature, location, and condition of the property, and the insurer must clearly state the terms. *Example: If an insured fails to declare that their property is in a fire-prone industrial area, the policy may become void.*

iii. **Indemnity:** Fire insurance aims to restore the insured to the financial position they were in before the loss. No profit can be made from a claim. *Example: If a factory worth ₹10 lakh is destroyed by fire, and the policy was for ₹10 lakh, the claim cannot exceed that even if market prices go up.*

iv. **Subrogation:** After compensating the loss, the insurer has the right to recover the loss from any third party responsible for the fire. *Example: If a neighbour's negligence caused the fire, the insurer can sue them after compensating the policyholder.*

v. **Contribution :** If the property is insured with multiple insurers, each insurer will contribute proportionately to the claim. *Example: If a property worth ₹10 lakh is insured with two companies (₹6 lakh and ₹4 lakh), and the loss is ₹5 lakh, they will pay in a 60:40 ratio.*

vi. **Proximate Cause :** The insurer will only pay if fire or related perils are the direct cause of the damage. *Example: If a short-circuit (proximate cause) causes a fire, which burns stock, the loss is covered.*

All fire insurance policies in India are governed under the IRDAI's Standard Fire and Special Perils Policy, which outlines inclusions, exclusions, and standard terms.

B. Accident Insurance

Accident insurance is a type of insurance policy that offers financial protection in the event of bodily injury, disability, or death caused by an accident. Unlike health insurance, which covers a range of illnesses, accident insurance specifically addresses injury-related events. Coverage often includes expenses for hospitalisation, ambulance charges, and lump-sum or periodic compensation for temporary or permanent disability. In the unfortunate event of the insured's death, the policy pays a predetermined benefit to the nominee. This type of insurance ensures income continuity for families and individuals during recovery or in the event of death. It is useful for workers in hazardous jobs, drivers, and even students.

Example: A two-wheeler rider injured in a road accident received compensation under a personal accident cover, including treatment expenses and a payout for temporary disability.

Features of Accident Insurance

1. **Accidental Death Benefit :** This feature provides a lump-sum payment to the nominee if the insured person dies solely and directly as a result of an accident. The benefit ensures that the family receives immediate financial assistance to cover living expenses, debts, or other urgent needs after the loss of the breadwinner. Example: If a construction worker falls from scaffolding and dies on-site, the policy pays the full insured sum to his dependents.

2. **Permanent Total Disability (PTD) Cover:** PTD cover offers a pre-decided payout when the insured suffers complete and irreversible loss of limbs, eyesight, or other critical functions, making them unable to engage in any gainful employment. This compensation helps cover medical costs and supports long-term financial stability. Example: A railway passenger who loses both legs in a derailment accident receives the full sum insured for permanent disability.

3. **Permanent Partial Disability (PPD) Cover :** This feature compensates the insured for partial but permanent loss of physical abilities, such as losing a hand, foot, or an eye, which reduces earning capacity. The payout is calculated as a percentage of the sum insured, depending on the severity of the disability. Example: A factory worker losing one hand in a machine accident receives 50% of the total insured amount.

4. **Temporary Total Disability (TTD) Cover :** TTD cover provides periodic payments (weekly or monthly) to replace lost income during the recovery period when the insured is completely unable to work due to accidental injuries. It helps meet daily household and medical expenses until the person resumes work. Example: A shop owner who fractures his leg in a road accident and cannot run his store for six weeks receives ₹10,000 weekly as per the policy terms.

5. **Medical Expense Reimbursement :** This covers hospitalisation charges, surgical expenses, medicines, and post-hospital rehabilitation directly related to the accident. The insured either gets cashless treatment in network hospitals or reimbursement after submitting bills. Example: A cyclist injured in a hit-and-run accident gets ₹75,000 reimbursed for surgery and physiotherapy.

6. **Ambulance Benefit :** This benefit pays for the cost of emergency transportation to the nearest hospital following an accident. It ensures that timely medical attention can be accessed without worrying about ambulance charges. Example: A policyholder who meets with a highway accident gets ₹3,000 reimbursed for ambulance service.

7. **Education Grant :** Certain policies provide an education grant for dependent children in case the insured dies or suffer permanent disability due to an accident. This helps to safeguard the child's schooling or higher education. Example: After a mining accident resulting in the insured's death, his child receives ₹50,000 annually for education until age 21.

Types of Accident Insurance Policies

1. **Personal Accident Insurance :** This covers an individual against accidental death, disability, and medical expenses. It can also extend to family members with additional premiums.

    Example: A software engineer buys personal accident cover for himself and his spouse, ensuring financial safety during road travel.

2. **Group Personal Accident Insurance :** Employers or associations provide this to cover all members under a single contract, often at a lower cost. It is commonly offered as an employee benefit.

    Example: A logistics company covers all its delivery staff under a group accident policy.

3. **Travel Accident Insurance :** This protects against accidents occurring while travelling, whether by road, rail, or air .It is often bundled with travel tickets or credit cards

Example: A passenger on a domestic flight is automatically covered for ₹50 lakh under the airline's travel accident policy.

4. **Student Accident Insurance :** Covers students for accidents occurring in school, during sports, or educational trips. It offers medical expense coverage and disability benefits.

Example: A student injured during a football match at school gets hospital bills reimbursed.

C. Health/Medical Insurance

Health insurance is a type of insurance policy that provides financial coverage for medical expenses incurred due to illness, injury, or surgery. It typically covers hospitalisation costs, doctor's consultation fees, diagnostic tests, medicines, and post-operative care. With the steep rise in healthcare expenses, health insurance is essential for individuals and families to protect savings and access quality medical care without financial strain.

Example: Under a Star Health Insurance policy, a policyholder diagnosed with dengue fever received treatment at a network hospital through the cashless facility, avoiding any upfront payment.

Features of Health/Medical Insurance

1. **Cashless Hospitalisation :** Health insurance companies tie up with a network of hospitals to provide cashless treatment, where the insurer directly settles the bill with the hospital. This benefit eliminates the need for patients to arrange funds during a medical emergency. Example: A patient undergoing an appendectomy at a network hospital had all bills settled by the insurer without paying from pocket.

2. **Reimbursement Facility :** If treatment is taken at a non-network hospital, the insured can pay the bills and later claim reimbursement from the insurer. This ensures coverage even outside the insurer's hospital network. Example: A patient receiving knee surgery in a small-town hospital not on the insurer's list received full reimbursement upon submitting bills.

3. **Coverage for Critical Illnesses :** Many policies offer a lump-sum payment upon diagnosis of serious illnesses such as cancer, heart attack, kidney failure, or stroke. This payout helps cover high-cost treatments and income loss during recovery. Example: A critical illness rider provided ₹5 lakh to a policyholder diagnosed with stage-2 breast cancer.

4. **Maternity and Newborn Cover :** Some health plans include expenses related to childbirth, pre- and post-natal care, and coverage for the newborn. These benefits usually have a waiting period before they can be claimed. Example: A couple claimed maternity expenses under their family floater plan after completing the two-year waiting period.

5. **Daily Hospital Cash Benefit :** A fixed daily amount is paid for each day of hospitalisation to cover non-medical expenses like transport, meals,

and attendant costs. This is paid in addition to hospital bill settlement. Example: A patient hospitalised for pneumonia received ₹1,000 per day for 10 days as hospital cash benefit.

6. **Pre - and Post - Hospitalisation Cover :** Policies reimburse medical expenses incurred a set number of days before and after hospitalisation, such as diagnostic tests, medicines, and follow-up visits. Example: A patient's pre-surgery MRI and post-surgery physiotherapy sessions were fully covered.

Types of Health/Medical Insurance Policies

1. **Individual Health Insurance :** Covers medical expenses for a single person under the policy. Premium is based on the individual's age, health status, and sum insured. Example: A 30-year-old purchasing a ₹5 lakh individual cover for personal protection.

2. **Family Floater Plan :** Provides a single sum insured shared among all family members covered. Premiums are lower than buying separate individual plans. Example: A ₹10 lakh cover for a family of four under one policy.

3. **Critical Illness Insurance :** Provides a lump-sum payout on diagnosis of specified critical illnesses, regardless of actual treatment cost. Example: ₹7 lakh paid upon diagnosis of a heart attack, even if treatment cost was ₹5 lakh.

4. **Group Health Insurance :** Offered by employers to employees, often covering their dependents as well. Example: An IT company providing health cover for staff and their spouses.

5. **Senior Citizen Health Insurance :** Tailored for individuals aged 60 and above, with higher sum insured for age-related ailments. Example: A 65-year-old purchasing a ₹10 lakh senior citizen plan with cataract surgery coverage.

Importance and Benefits

1. **Financial Protection Against High Medical Costs :** Covers hospitalisation and treatment costs that could otherwise deplete personal savings. Example: A ₹6 lakh bypass surgery bill covered entirely by the insurer.

2. **Access to Quality Healthcare :** Enables treatment in reputed hospitals without worrying about expenses. Example : A policyholder opting for a top-tier hospital for cancer treatment using cashless benefits.

3. **Tax Benefits :** Premiums paid for health insurance are eligible for deduction under Section 80D of the Income Tax Act in India. Example: An individual saving ₹5,000 in taxes on a ₹25,000 premium payment.

4. **Peace of Mind :** Removes financial stress during illness, allowing the patient and family to focus on recovery. Example: Parents concentrating on their child's surgery without worrying about bills.

D. Motor Insurance

Motor insurance is a contract between the vehicle owner and an insurer that provides financial protection against damage to the vehicle, theft, and liabilities arising from third-party injury, death, or property damage caused by the insured vehicle. In India, as per the Motor Vehicles Act, 1988, third-party insurance is mandatory for all motor vehicles before they can be legally driven on public roads. Comprehensive policies offer both third-party cover and own-damage protection, safeguarding the owner against repair costs, loss, and legal liabilities.

Example : After a collision, a car owner claimed repair and replacement costs under a comprehensive motor insurance policy issued by Bajaj Allianz.

Key Features of Motor Insurance

1. **Third-Party Liability Cover :** This is mandatory by law and covers injury or death of third parties and damage to third-party property caused by the insured vehicle. It ensures compliance with legal requirements while providing protection against substantial compensation claims. Example: A bike rider causing damage to another car's bumper had the repair cost paid by the insurer under third-party cover.

2. **Own-Damage Cover:** Covers damage to the insured's own vehicle due to accidents, fire, theft, natural calamities, or man-made disasters. This feature is available in comprehensive motor insurance policies. Example: A car damaged in a flood was repaired with the insurer covering all costs except the deductible.

3. **Personal Accident Cover for Owner-Driver :** Provides financial compensation in case of accidental injury, disability, or death of the owner-driver while using the insured vehicle. This cover is often built into both third-party and comprehensive policies. Example: A delivery van driver injured in an accident received ₹5 lakh compensation for disability.

4. **Add-on Covers :** Policyholders can enhance protection by purchasing optional riders such as zero depreciation cover, roadside assistance, engine protection, or no-claim bonus (NCB) protection. Example: A zero-depreciation add-on ensured full claim settlement for replacing car parts without depreciation deduction.

5. **No-Claim Bonus (NCB) :** Insurers offer a discount on the renewal premium for each claim-free year, encouraging safe driving habits. This bonus can accumulate over multiple years. Example: A car owner enjoyed a 35% premium discount after three consecutive claim-free years.

6. **Cashless Garage Network :** Insurers have tie-ups with authorised garages where repair bills are settled directly, reducing out-of-pocket expenses for the policyholder. Example: After an accident, a two-wheeler was repaired at a network garage without the owner paying upfront.

Types of Motor Insurance Policies

1. **Third-Party Liability Insurance :** Mandatory by law; covers third-party injury, death, or property damage but does not cover own vehicle damage. Example: A taxi owner met the legal requirement by purchasing third-party insurance.

2. **Comprehensive Motor Insurance :** Includes third-party cover along with own-damage cover for the insured vehicle. Recommended for better protection. Example: A car owner received compensation for both damage to his car and injury to another driver.

3. **Standalone Own-Damage Cover :** Available for vehicles with an active third-party policy, this covers only own-vehicle damage. Example: A scooter owner with mandatory third-party insurance added a standalone own-damage policy.

4. **Commercial Vehicle Insurance :** Designed for vehicles used for business purposes such as trucks, buses, and taxis. Covers both third-party and own-damage risks. Example: A transport company insured its fleet of trucks under commercial vehicle policies.

Importance and Benefits

1. **Legal Compliance :** Avoids penalties and legal consequences under the Motor Vehicles Act by maintaining mandatory third-party coverage. Example: A driver avoided a ₹2,000 fine during a traffic inspection by having valid third-party insurance.

2. **Financial Protection :** Shields against high repair costs, medical expenses, and compensation claims after accidents. Example: ₹1.5 lakh repair costs after a major accident were fully covered by the insurer.

3. **Customisable Coverage :** Add-ons allow tailoring the policy to suit specific needs such as protection against natural disasters or enhanced roadside assistance. Example: An engine protection add-on covered damage caused by heavy rain.

4. **Peace of Mind :** Ensures confidence while driving, knowing that financial risks are minimised.

   Example: A new car owner drove long distances without fear of accident repair costs.

E. Home Insurance

Home insurance is a policy designed to protect a residential property's structure and contents from financial losses caused by risks such as fire, theft, burglary, natural disasters (earthquakes, floods, storms), and man-made hazards (riots, vandalism). Policies can also include additional benefits such as personal liability protection and alternative accommodation coverage when the home becomes temporarily uninhabitable. This type of insurance ensures that homeowners can rebuild, repair, and replace valuable possessions without bearing the entire financial burden themselves.

Example: During the Kerala floods, homeowners with valid home insurance policies received compensation for structural damage and loss of furniture.

Features of Home Insurance

1. **Building (Structure) Cover :** Protects the physical structure of the house, including walls, roof, and permanent fixtures, from insured risks such as fire, storms, and earthquakes. This ensures financial support for rebuilding or repairing after damage.
   Example: After a lightning strike damaged a house roof, the insurer covered the repair costs.

2. **Contents Cover :** Provides coverage for household items such as furniture, electronics, appliances, and clothing against theft, fire, and accidental damage. It can apply whether the property is owned or rented.
   Example: A short-circuit that destroyed a television and washing machine was covered under the contents section.

3. **Burglary and Theft Cover :** Compensates for loss or damage to household items due to burglary, attempted burglary, or theft. This may include damage to the property during forced entry.
   Example: A break-in resulting in stolen jewellery and broken doors was fully compensated.

4. **Natural Calamity Protection :** Covers damages caused by floods, earthquakes, cyclones, landslides, and other natural disasters. Particularly valuable in high-risk geographic zones.
   Example: A house in Assam damaged by floods was restored with insurance payout.

5. **Personal Liability Cover :** Offers protection against legal liability if a guest or third party is injured within the insured premises.
   Example: A visitor slipping on wet flooring and sustaining injuries had their medical costs covered by the policy.

6. **Alternative Accommodation Benefit :** Pays for temporary housing expenses if the insured home becomes uninhabitable due to an insured event.
   Example: After a fire, a family's hotel stay was paid for under the policy's alternative accommodation clause.

Types of Home Insurance Policies

1. **Standard Fire and Special Perils Policy :** Covers damage due to fire, lightning, storms, floods, and similar risks.
   Example: A kitchen fire destroying cabinets was covered under this policy.

2. **Comprehensive Home Insurance :** Covers both the building and contents along with additional benefits like burglary cover and liability protection.
   Example: A fire and theft incident were both compensated under a comprehensive policy.

3. **Contents-Only Insurance :** Ideal for tenants; covers only household belongings against insured risks.

Example: A rented apartment's electronics and furniture were insured under contents-only cover.

4. **Building-Only Insurance :** Covers just the structure, often chosen by homeowners with minimal household contents.
Example: A homeowner insured only the walls, roof, and fixtures against earthquake damage.

Importance and Benefits

1. **Financial Security :** Prevents large out-of-pocket expenses for rebuilding or replacing household items after loss.
Example: A ₹10 lakh reconstruction cost after a cyclone was fully covered.

2. **Comprehensive Risk Coverage :** Protects against a wide range of natural and man-made risks in one policy.
Example: Both fire and burglary damages were settled under the same claim.

3. **Peace of Mind :** Assures homeowners they can recover quickly from unforeseen events without financial distress.
Example: A flood-affected family rebuilt their home without taking loans due to their insurance payout.

4. **Customisable Add-Ons :** Additional riders such as jewellery cover, art cover, or tenant liability can be added to tailor the policy.
Example: A high-value art collection was protected through an add-on rider.

F. Travel Insurance

Travel insurance is designed to protect travellers against unforeseen events during domestic or international trips, including medical emergencies, trip cancellations, baggage loss, or travel delays. It is particularly important for international travel where healthcare costs, emergency services, or repatriation can be prohibitively expensive. Policies may be customised for solo travellers, families, business trips, students studying abroad, or adventure travel.

Example: ICICI Lombard's Travel Insurance plan helped a traveller stranded in Europe with emergency hospitalisation and reimbursement for delayed baggage.

Features of Travel Insurance

1. **Medical Emergency Cover :** Pays for hospitalisation, surgery, medication, and sometimes dental care required during a trip due to illness or accidental injury. This often includes cashless treatment at network hospitals abroad.
Example: A traveller in the USA with severe appendicitis had surgery without upfront payment through the policy's cashless facility.

2. **Trip Cancellation and Interruption Cover :** Reimburses prepaid and non-refundable travel costs if a trip is cancelled or cut short due to covered reasons like illness, injury, or natural disasters. This prevents heavy financial losses from sudden plan changes.
Example: A family received full ticket refunds after cancelling their Europe tour due to a medical emergency.

3. **Baggage Loss or Delay Cover :** Compensates for lost, stolen, or delayed luggage and personal belongings during travel. Delay benefits often reimburse for essential purchases like clothes and toiletries.
   Example: A passenger whose baggage was delayed for two days in Singapore was reimbursed for clothing and toiletries expenses.

4. **Flight Delay and Missed Connection Cover :** Provides compensation for additional expenses caused by long delays or missed connecting flights due to reasons like bad weather or airline strikes. This can cover accommodation, meals, and rebooking costs.
   Example: A traveller stuck in Dubai for 12 hours received compensation for hotel and meal charges.

5. **Emergency Evacuation and Repatriation :** Covers the cost of transporting the insured to the nearest suitable medical facility or repatriating remains in the event of death. This is critical in countries with limited healthcare infrastructure
   Example: A trekker in Nepal was airlifted to a hospital in Kathmandu after a severe fall, covered entirely by insurance.

6. **Loss of Passport Cover :** Reimburses expenses for obtaining a duplicate passport or travel documents if the original is lost or stolen. This often includes help with embassy coordination.
   Example: A tourist in Paris had their stolen passport replaced with insurer-assisted embassy support.

Types of Travel Insurance Policies

1. **Single-Trip Travel Insurance :** Covers one specific trip, ideal for occasional travellers.
   Example: A solo traveller insured their 10-day holiday in Japan.

2. **Multi-Trip Travel Insurance :** Provides coverage for multiple trips within a year, suitable for frequent travellers.
   Example: A business executive used the same annual policy for five international trips.

3. **Student Travel Insurance :** Tailored for students studying abroad, covering medical expenses, study interruptions, and sponsor protection.
   Example: An Indian student in Canada received tuition fee reimbursement after returning home for a family emergency.

4. **Family Travel Insurance :** Covers an entire family under a single policy, offering convenience and cost savings.
   Example: A family trip to Europe was insured under one comprehensive plan.

5. **Senior Citizen Travel Insurance :** Specialised plans for older travellers, often with higher medical cover and fewer restrictions.
   Example: A 68-year-old couple travelling to Australia had coverage for pre-existing conditions.

Importance and Benefits

1. **Medical Security Abroad :** Covers expensive foreign medical treatment without draining personal savings.
   Example: Hospitalisation costs in the USA for pneumonia were fully paid by the insurer.

2. **Financial Protection Against Travel Disruptions :** Safeguards against losses from cancellations, delays, and lost baggage.
   Example: A weather-related flight cancellation led to full refund and accommodation reimbursement.

3. **Peace of Mind for Travellers :** Allows travellers to enjoy their journey without constant worry over potential risks.
   Example: A family exploring Europe felt secure knowing their insurance covered emergencies.

4. **Customisation for Destination and Purpose :** Plans can be adapted for adventure sports, business travel, or specific regional risks.
   Example: A mountaineer's policy included special cover for high-altitude rescue.

G. Commercial Insurance

Commercial insurance offers financial protection to businesses against various operational risks, property damage, legal liabilities, and employee-related claims. It helps ensure business continuity by covering unexpected events such as fires, theft, natural disasters, or lawsuits. Many industries—including manufacturing, retail, hospitality, healthcare, and IT—use commercial insurance to safeguard assets and maintain operations.

Example: A restaurant in Mumbai insured under a commercial fire and liability policy recovered losses after a kitchen fire caused extensive damage and a customer injury claim.

Features of Commercial Insurance

1. **Property Damage Cover :** Protects physical business assets such as buildings, machinery, inventory, and office equipment from risks like fire, flood, earthquake, or vandalism. Policies may also extend to leased or rented premises.
   Example: A textile factory received compensation for damaged machinery after a short-circuit fire.

2. **Liability Protection :** Covers legal costs and compensation if the business is held responsible for third-party injury, property damage, or negligence. This may include public liability, product liability, and professional indemnity.
   Example: A software company paid no legal costs when a client sued for a data breach, as their professional indemnity cover handled the claim.

3. **Business Interruption Cover :** Provides income replacement if the business is forced to halt operations due to insured events, ensuring ongoing expenses like salaries and rent are covered.

Example: A retail store closed for three months after flood damage, but insurance covered lost income and staff wages.

4. **Employee - Related Coverage :** Includes worker's compensation, group accident cover, and fidelity guarantee to protect against employee injuries or fraud.
Example: A warehouse owner received medical expense coverage for a staff member injured during lifting operations.

5. **Customisable Policy Options :** Allows businesses to choose coverage types and limits tailored to industry-specific risks, from cyber threats to supply chain disruptions.
Example: An e-commerce company added cyber liability protection to safeguard against hacking and data theft.

Types of Commercial Insurance Policies

1. **Fire Insurance :** Covers loss or damage to business property due to fire and related perils.
Example: A bakery rebuilt after a fire destroyed its premises using claim funds.

2. **Burglary and Theft Insurance :** Protects against loss of goods or cash due to theft or burglary.
Example: A jewellery shop recovered losses after a break-in.

3. **Fidelity Guarantee Insurance :** Covers financial loss from employee dishonesty or fraud.
Example: A bank claimed compensation after an employee embezzled funds.

4. **Business Interruption Insurance :** Compensates for lost income during downtime caused by insured events.
Example: A hotel received payouts during a six-month closure after cyclone damage.

5. **Liability Insurance :** Includes public, product, and professional liability to protect against third-party claims.
Example: A manufacturer's product defect injury claim was fully covered under liability insurance.

Importance and Benefits

1. **Business Continuity :** Ensures operations can resume quickly after disruptions without severe financial strain.
Example: A printing press restored operations within weeks after fire damage.

2. **Legal Compliance :** Some industries require certain commercial covers by law or contractual obligations.
Example: A construction company must carry liability insurance to win government contracts.

3. **Risk Management :** Transfers significant operational and financial risks to the insurer, safeguarding long-term stability.
Example: A hospital reduced exposure to malpractice lawsuits with adequate professional indemnity cover.

4. **Customisation and Flexibility :** Policies can be designed to suit the unique risk profile of each business.
    Example: A logistics company added marine cargo insurance to protect goods in transit.

H. Rural Insurance

Rural insurance is designed to meet the unique risk protection needs of rural populations, including farmers, artisans, and small entrepreneurs. It provides coverage for agricultural assets such as crops, livestock, farm equipment, huts, and even rural health care. By protecting against losses from natural disasters, disease outbreaks, or accidents, it safeguards rural livelihoods and supports economic stability.

Example: Under the Pradhan Mantri Fasal Bima Yojana (PMFBY), a farmer received compensation after unseasonal rains damaged his wheat crop.

Features of Rural Insurance

1. **Crop Insurance :** Protects farmers against loss of crops due to natural calamities, pests, or diseases. This ensures income stability and reduces debt dependency among farming families.
    Example: A paddy farmer claimed compensation under PMFBY after a flood destroyed his harvest.

2. **Livestock Insurance :** Covers the death or disability of animals such as cows, buffaloes, goats, or poultry, which are crucial to rural income. Policies often include veterinary care costs.
    Example: A dairy farmer was reimbursed for the loss of a high-yield cow due to disease.

3. **Farm Equipment and Asset Cover :** Provides coverage for tractors, irrigation pumps, and other essential farm tools against damage or theft.
    Example: A farmer replaced his stolen tractor using funds from his equipment insurance policy.

4. **Rural Health Insurance :** Offers affordable medical coverage to rural families, often supported by government subsidies.
    Example: Under Rashtriya Swasthya Bima Yojana, a rural labourer's family received cashless treatment for surgery.

5. **Affordable Premiums with Subsidies :** Many rural policies are supported by government funding, making premiums low for small farmers and artisans.
    Example: A weaver obtained property insurance for his hut and tools at a subsidised rate.

Types of Rural Insurance Policies

1. **Crop Insurance Schemes :** Government and private programs protect against yield loss due to weather, pests, or disease.
    Example: PMFBY covers various crops with seasonal premium rates.

2. **Livestock Insurance Schemes :** Compensates for the loss of farm animals due to illness, accident, or natural disasters.
   Example: A goat farmer claimed under the Livestock Insurance Scheme after a viral outbreak.

3. **Farm Equipment Insurance :** Protects machinery like tractors and harvesters against theft or accidental damage.
   Example: A sugarcane harvester damaged in a road accident was repaired under the policy.

4. **Rural Health and Life Insurance :** Covers medical expenses and provides life insurance for rural households.
   Example: Under Pradhan Mantri Jeevan Jyoti Bima Yojana (PMJJBY), a widow received the insured sum after her husband's accidental death.

Importance and Benefits

1. **Risk Mitigation for Vulnerable Communities :** Shields rural households from severe financial loss due to unpredictable natural or economic events.
   Example: A farmer avoided debt after drought destroyed his crops, thanks to insurance payout.

2. **Encourages Agricultural Investment :** Farmers are more willing to adopt modern farming techniques when financial risks are covered.
   Example: A horticulturist invested in high-value fruit crops knowing they were insured.

3. **Supports Poverty Reduction :** Prevents families from falling into poverty after disasters by providing financial recovery support.
   Example: A fisherman rebuilt his damaged boat with insurance funds instead of taking high-interest loans.

4. **Government Support and Accessibility :** Subsidised premiums and simplified claim procedures make rural insurance widely accessible.
   Example: Farmers registered at Common Service Centres (CSCs) can enrol for multiple schemes easily.

I. Marine Insurance

Marine insurance provides financial protection for goods, vessels, and related interests during transportation over sea, land, or air. It covers risks such as storms, piracy, theft, fire, collision, and handling damage. This type of insurance is vital for importers, exporters, and logistics providers to safeguard against losses in domestic and international trade.

Example: A Logistics company shipping electronics from Mumbai to Dubai claimed marine insurance after a container was damaged during rough sea conditions.

Features of Marine Insurance

1. **Cargo Insurance :** Covers loss or damage to goods during transit due to perils such as storms, theft, or accidental damage.

Example: A textile exporter claimed for fabric damage after seawater entered a container during a cyclone.

2. **Hull Insurance :** Protects the ship or vessel against physical damage caused by accidents, collisions, or natural disasters.
   Example: A shipping company repaired its vessel after a collision using hull insurance coverage.

3. **Freight Insurance :** Covers loss of freight revenue if goods are lost or damaged during transit.
   Example: An exporter received compensation for lost freight charges when cargo was destroyed in a fire at port.

4. **Comprehensive Coverage for All Modes :** Though called "marine" insurance, it often includes protection for goods transported by air, road, or rail as part of the overall shipping journey.
   Example: Electronics damaged during truck transport to the port were covered under the marine cargo policy.

Types of Marine Insurance Policies

1. **Voyage Policy :** Covers a shipment for a specific journey, regardless of time.
   Example: Machinery insured for transport from Chennai to Singapore.

2. **Time Policy :** Provides coverage for a vessel for a fixed period, usually 12 months.
   Example: A shipping company insured its fleet for one year under a time policy.

3. **Mixed Policy :** Combines elements of both voyage and time policies.
   Example: A cargo ship insured for a specific trip during a defined period.

4. **Open or Floating Policy :** Covers multiple shipments under one policy, suitable for regular shippers.
   Example: An importer insured all monthly consignments from China under an open policy.

Importance and Benefits

1. **Risk Protection for Traders and Logistics :** Shields businesses from significant financial losses caused by unpredictable maritime and transit hazards.
   Example: An exporter avoided heavy losses after cargo was lost at sea due to a storm.

2. **Facilitates International Trade :** Marine insurance builds trust between global buyers and sellers by ensuring goods are protected.
   Example: A foreign buyer agreed to a deal because the seller provided marine cargo insurance.

3. **Compliance with Legal and Contractual Requirements :** Many trade agreements and banking arrangements mandate marine insurance.
   Example: A letter of credit required full marine insurance coverage for exported goods.

4. **Covers Multi-Modal Transport Risks :** Protects goods across the full journey, including road, rail, and air links.

Example: Coffee beans damaged in a truck accident en route to the port were compensated under the marine policy.

General insurance plays a critical role in protecting individuals and organisations from financial losses due to unforeseen and often uncontrollable events. With a wide range of policy types tailored to various needs, it ensures stability, security, and business continuity. From a hospital bill to a house fire or a delayed flight, general insurance helps people recover quickly and confidently.

3.2.2 Underwriting in Insurance

Underwriting in insurance is the process through which an insurer evaluates the risk associated with an applicant (individual or business) seeking insurance coverage. It involves a careful analysis of the applicant's risk profile, which may include factors such as age, health status, occupation, financial history, lifestyle habits, and previous claim records. Based on this evaluation, the insurer decides:

1. **Whether to accept the risk** – The insurer determines if the risk falls within the company's acceptable risk appetite or underwriting guidelines.

2. **On what terms** – If the risk is accepted, the insurer specifies the coverage details, exclusions, deductibles, and any special conditions that apply.

3. **At what price (premium)** – The insurer calculates an appropriate premium that reflects the risk level while ensuring competitiveness and profitability.

The underwriting process ensures that the insurer balances offering protection to customers while safeguarding the financial stability of the insurance company.

Example: If a 55-year-old applicant applies for a health insurance policy and has a history of heart disease, the underwriter may either increase the premium, impose a waiting period for heart-related claims, or decline the application altogether.

3.2.2.1 Objectives of Underwriting

1. **Risk Assessment** : The primary goal of underwriting is to evaluate the likelihood of a claim being made. Insurers analyse applicant information and compare it to historical data, actuarial tables, and statistical models. Example: In motor insurance, factors such as the driver's age, driving record, location, and vehicle type are assessed to determine the probability of an accident.

2. **Pricing Accuracy** : Accurate premium setting is crucial for maintaining the insurer's profitability while offering fair prices to customers. Premiums are based on the assessed risk level – higher risks lead to higher premiums, while low-risk clients enjoy lower premiums.

   Example: A non-smoker applying for life insurance will usually pay a lower premium compared to a smoker of the same age and health profile.

3. **Preventing Adverse Selection**: Adverse selection occurs when high-risk individuals are more likely to purchase insurance, while low-risk

individuals opt out, leading to unbalanced risk pools and potential financial losses for the insurer. Underwriting helps identify and control these risks by setting appropriate terms, pricing, or declining certain applications. Example: Without proper underwriting, a travel insurance company might unintentionally sell high-risk policies to people already planning dangerous expeditions, increasing the chances of claims.

3.2.2.2 Types of Underwriting

1. **Life Insurance Underwriting** : This type of underwriting evaluates the applicant's health status, age, medical history, occupation, and lifestyle habits such as smoking or alcohol consumption. These factors help the insurer estimate the applicant's life expectancy and the probability of a claim during the policy term. For example, a younger, healthy non-smoker working in a low-risk job will typically receive lower premiums compared to an older applicant with chronic illnesses.

2. **Health Insurance Underwriting :** Here, the insurer examines pre-existing medical conditions, recent medical check-up reports, Body Mass Index (BMI), and family health history to assess the likelihood of future healthcare claims. The goal is to determine coverage eligibility, set suitable premiums, and impose necessary exclusions or waiting periods. For instance, an applicant with a history of diabetes may face a waiting period before claims for diabetes-related treatments are covered.

3. **General Insurance Underwriting :** This underwriting deals with non-life assets such as property, motor vehicles, marine cargo, and industrial equipment. It assesses factors like the asset's value, physical location, exposure to hazards, and patterns of use to estimate the risk of loss or damage. For example, a warehouse located in a flood-prone area may attract higher premiums than one in a safe, elevated location.

4. **Reinsurance Underwriting** : This process involves evaluating the risks that primary insurers want to transfer to a reinsurance company to protect themselves from large or catastrophic losses. The reinsurer assesses the type of policies, claim history, and concentration of risks before deciding on acceptance and pricing. For instance, a reinsurer may take on part of the risk for a portfolio of high-value industrial fire insurance policies to reduce the original insurer's exposure.

3.2.2.3 Underwriting Procedure

A. Underwriting Procedure for Life Insurance

1. Application Form and Personal Details : The process begins when the applicant submits a duly filled application form containing essential personal details such as name, age, gender, address, date of birth, and contact information. The proposal form also includes declarations regarding health status, existing insurance policies, and any past claims. Providing accurate and complete information at

this stage is crucial, as it forms the basis for the insurer's risk assessment and determines the suitability of the applicant for the requested cover.

2. **Medical Reports and Past History :** Medical evaluation is a critical component of life insurance underwriting, as it helps determine the applicant's current health status and any pre-existing conditions. The insurer may require a medical examination, blood tests, ECG, or other diagnostic procedures depending on the applicant's age and the sum assured. In addition, the applicant's past medical history, including hospitalisations, surgeries, and chronic illnesses, is reviewed to assess the likelihood of future claims.

3. **Occupation and Lifestyle (Smoking, Alcohol Use) :** The applicant's occupation plays a significant role in risk assessment, as certain jobs—such as mining, construction, or aviation—carry a higher risk of injury or death compared to office-based roles. Lifestyle habits such as smoking, alcohol consumption, or participation in high-risk hobbies (e.g., skydiving, scuba diving) are also considered, as they can significantly impact life expectancy. Applicants with hazardous occupations or risky lifestyles may face higher premiums or policy restrictions.

4. **Income Documents (for Large Sum Assured) :** For policies with a high sum assured, insurers require proof of income to ensure the requested coverage aligns with the applicant's financial capacity. Income verification also helps prevent over-insurance, which could lead to moral hazard. Documents such as salary slips, bank statements, or income tax returns are reviewed to confirm the applicant's ability to pay premiums consistently over the policy term.

5. **Risk Classification (Standard, Substandard) :** After reviewing all collected information, the underwriter classifies the applicant into a risk category. Standard risk applicants meet the insurer's normal underwriting criteria and are offered coverage at standard premium rates. Substandard risk applicants present higher risks due to health issues, hazardous occupations, or lifestyle habits and may be offered coverage at increased premiums, with exclusions, or in some cases, declined. This classification ensures that the insurer maintains a balanced portfolio and manages claims risk effectively.

B. Underwriting Procedure for Non-Life Insurance

1. **Nature and Location of Asset :** In general insurance underwriting, the first step is to assess the type of asset to be insured—such as a residential building, commercial property, motor vehicle, or industrial equipment—and its physical characteristics. The location of the asset is equally important, as it can influence the level of risk; for example, a property located in a flood-prone or earthquake-prone zone will attract higher premiums than one in a low-risk area. Understanding the asset's nature and location helps insurers evaluate exposure to hazards and set appropriate policy terms.

2. **2Usage and Safety Features (e.g., CCTV for Shops):** How the asset is used plays a critical role in determining the likelihood of loss or damage. Commercial premises such as shops, factories, or warehouses have different risk profiles

compared to residential properties. Safety and security measures—such as fire alarms, sprinkler systems, CCTV surveillance, or security guards—can significantly reduce risk and may qualify the policyholder for lower premiums. For instance, a retail store equipped with CCTV cameras and a burglar alarm system may be offered better terms than one without such protections.

3. **Claims History :** The applicant's past record of insurance claims provides valuable insight into their risk behaviour. A history of frequent or high-value claims may indicate a higher likelihood of future claims, leading to stricter policy terms or higher premiums. Conversely, a clean claims history can strengthen the applicant's profile and result in more favourable rates. For example, a fleet owner with no accident-related claims over five years might receive discounted motor fleet insurance premiums.

4. **Insured Value and Sum Insured :** The insured value refers to the declared worth of the asset, while the sum insured is the maximum liability the insurer will bear in the event of a claim. Underwriters ensure that these values are accurate and aligned with market prices to prevent underinsurance (inadequate cover) or overinsurance (excessive cover leading to moral hazard). Accurate valuation is essential for fair premium calculation and claim settlement.

Example: In life insurance, for a ₹50 lakh term insurance policy, the insurer may require the applicant to undergo a medical examination and provide income proof before approving coverage. Similarly, in general insurance, a ₹2 crore factory insurance proposal may involve an on-site inspection and verification of safety protocols before acceptance.

3.2.3 Insurance Premium

An insurance premium is the amount of money that the insured pays to the insurer in exchange for the promise of financial protection against specified risks. It represents the cost of transferring risk from the policyholder to the insurance company and is typically determined during the underwriting process. Payment of the premium is essential for the policy to remain active, and non-payment can result in policy lapse or cancellation. Premiums vary widely depending on the type of insurance, the coverage chosen, and the risk profile of the applicant.

3.2.3.1 Factors Affecting Premium

1. **Sum Assured :** The sum assured is the guaranteed amount the insurer will pay in the event of a claim. A higher sum assured generally leads to a higher premium because the insurer's potential liability increases.

2. **Age and Health (in Life Insurance) :** In life insurance, younger and healthier individuals are considered lower risk, resulting in lower premiums. Older applicants or those with health issues may have to pay more. For example, a 25-year-old non-smoker will usually pay significantly less than a 50-year-old smoker for the same coverage.

3. **Risk Level of Asset (in General Insurance)** :In general insurance, the nature and condition of the insured asset, as well as its exposure to risks, influence the premium. For instance, a house located in a cyclone-prone area may attract higher premiums than one in a safer location.

4. **Policy Duration** : Longer policy terms may result in higher overall premiums, but insurers often offer discounts for long-term commitments. In some cases, opting for a shorter-term policy may lead to higher per-year costs.

5. **Add-on Riders** : Riders are optional benefits that enhance the base policy, such as critical illness cover, accidental death benefit, or waiver of premium. Each rider adds to the cost of the premium because it increases the insurer's potential payout.

6. **Underwriting Decisions** : The insurer's underwriting process directly impacts the premium by adjusting rates based on the applicant's assessed risk. Factors like medical results, occupation, and lifestyle habits influence these decisions.

3.2.3.2 Modes of Premium Payment

Policyholders can choose from different payment frequencies depending on their convenience and budget:

i. Monthly – Smaller, regular payments spread across the year.

ii. Quarterly – Payments made every three months.

iii. Half-yearly – Payments made twice a year.

iv. Annually – A single payment for the entire year, often with a small discount.

v. Single Premium – One-time lump sum payment covering the entire policy duration, commonly used for certain investment-linked or short-term plans.

Example: A healthy 30-year-old male non-smoker may pay around ₹6,000 per year for a ₹50 lakh term life insurance plan with a 20-year duration. If he adds a critical illness rider, the premium might increase to ₹8,500 per year, reflecting the additional risk cover.

3.2.4 Insurance Documents

When purchasing an insurance policy, several important documents are involved at various stages of the process. These documents serve as a legal record of the agreement between the insurer and the insured, and they ensure that both parties are clear on the terms and obligations. Each plays a distinct role, from initiating coverage to receiving claim benefits.

1. **Proposal Form:** This is the application form that the proposer fills out to request insurance coverage. It captures personal, financial, and risk-related details, along with necessary declarations and disclosures. The insurer uses the information in this form to assess the risk and decide whether to issue the policy.

2. **Policy Document:** This is the formal legal contract issued by the insurer after the proposal is accepted and underwriting is completed. It contains all the terms,

conditions, coverage details, exclusions, and endorsements applicable to the insurance policy. The policy document serves as the primary reference for resolving disputes and processing claims.

3. **Premium Receipt:** This document is proof that the policy holder has paid the insurance premium to the insurer. It specifies the amount paid, the date of payment, and the mode of payment. Maintaining this receipt is important, as it confirms that the policy is active and in force.

4. **Rider/Add-on Document:** This is an additional agreement to the base policy, offering extra coverage or benefits for an additional premium. Riders may include benefits like accidental death cover, critical illness cover, or waiver of premium. The rider document outlines its specific terms, coverage limits, and conditions separate from the main policy.

5. **Nomination Form:** This document specifies the person or persons who will receive the policy benefits in the event of the policyholder's death. It ensures that claim proceeds are transferred directly to the nominated beneficiary without legal disputes. Updating the nomination form is important whenever there are changes in personal circumstances.

6. **Claim Form:** This form is used by the policyholder or beneficiary to request compensation after an insured event occurs. It collects essential information such as policy details, nature of the loss, and supporting evidence. The insurer processes the claim based on this form and the documents submitted with it.

Case Study: Health Insurance Claim Settlement

Mr. Ajay, a 38-year-old working professional, had purchased a comprehensive health insurance policy from Star Health Insurance with a sum insured of ₹5 lakh. One evening, he experienced severe abdominal pain and was admitted to a network hospital for an urgent surgery. The total hospital bill after the procedure amounted to ₹1.8 lakh, which could have been a major financial burden without health insurance coverage.

Procedure Followed

i. **Intimation to the Insurer:** Immediately after admission, Mr. Ajay informed the insurer about the hospitalisation through the hospital's helpdesk. Since the hospital was part of the insurer's cashless network, the claim process could be initiated directly without him paying the full bill upfront.

ii. **Submission of Required Documents:** The hospital staff helped him submit the necessary documents, including the admission note, medical reports, discharge summary, itemised hospital bills, and identification proof. These documents were sent electronically to the insurer's claims department for verification.

iii. **Claim Processing:** The insurer reviewed the medical records and bills, ensuring the treatment fell within the policy's coverage. Within 7 working days, the claim was processed and a cashless authorisation was granted to the hospital.

iv. **Settlement and Out-of-Pocket Expense:** Under the cashless arrangement, the insurer directly paid ₹1.76 lakh to the hospital, covering all eligible expenses. Mr. Ajay only had to pay ₹4,000 for non-covered items such as certain consumables and registration charges.

Key Learning

This case highlights how a well-chosen health insurance policy can provide substantial financial protection during medical emergencies, reducing out-of-pocket expenses and ensuring timely treatment. It also demonstrates the convenience of cashless claim settlement, where the insurer directly pays the hospital, allowing the patient to focus on recovery instead of financial arrangements.

Recap

◊ Life and general insurance provide financial protection for different risks.

◊ Underwriting evaluates the risk and sets terms, conditions, and premiums accordingly.

◊ The cost of transferring risk to the insurer is known as premium and it is determined by multiple factors.

◊ Insurance documents are essential for policy issuance, record keeping, and claim processing.

◊ Claim Settlement can be cashless or reimbursement-based, ensuring timely financial support.

Objective Questions

1. Which principle of insurance requires honest disclosure of material facts?

2. What is the main purpose of a term life insurance plan?

3. Which document serves as proof of premium payment?

4. Name the policy that provides both life cover and investment options in market funds.

5. Which insurance covers losses from fire-related perils to property?

6. What is the mandatory motor insurance required in India?

7. Which type of travel insurance covers multiple trips within a year?

8. Name one scheme that provides crop insurance in India.

9. In underwriting, what is the classification for low-risk applicants?

10. Which insurance add-on covers accidental death benefit?

11. What is the role of the nomination form?

12. In a health policy, which feature allows hospitalisation without upfront payment?

Answers

1. Utmost Good Faith
2. Pure life cover
3. Premium Receipt
4. ULIP (Unit Linked Insurance Plan)
5. Fire Insurance
6. Third-party liability
7. Multi-trip travel insurance
8. PMFBY (Pradhan Mantri Fasal Bima Yojana)
9. Standard risk
10. Rider
11. Names policy beneficiary
12. Cashless facility

Self-Assessment Questions

1. Explain the various life insurance plans
2. Illustrate the principles of General Insurance
3. Describe the features of accident insurance
4. Breefly explain the features of Motor Insurance
5. Illustrate importance of rural insurance policies
6. Explain the different types of undercircling

Assignments

1. Explain the classification of insurance business in India with suitable examples.

2. Discuss the features and benefits of any three types of life insurance policies.

3. Describe the underwriting process for life insurance and general insurance.

4. Analyse the role of premium calculation factors in insurance pricing.

5. Explain the claim settlement process with reference to the given case study of Mr. Ajay.

6. Collect and compare three life insurance products from different insurers, highlighting features and premiums.

7. Prepare a flowchart showing the underwriting process for a health insurance policy.

8. Visit an insurance company website and list available add-on riders with their benefits.

9. Draft a sample filled-in proposal form for a motor insurance policy.

10. Conduct a mock claim settlement process for a home insurance fire loss scenario.

Reference

1. Black, K., & Skipper, H. D. (2014). *Life and health insurance*. Pearson Education India.

2. Dorfman, M. S., & Cather, D. A. (2012). *Introduction to risk management and insurance* (10th ed.). Pearson.

3. Gupta, P. K. (2011). *Insurance and risk management*. Himalaya Publishing House.

4. IRDAI. (2023). *Annual report 2022–23*. Insurance Regulatory and Development Authority of India.

5. IRDAI. (2024). *Handbook on general insurance*. Insurance Regulatory and Development Authority of India.

6. Mishra, M. N., & Mishra, S. B. (2016). *Insurance: Principles and practice*. S. Chand Publishing.

7.	Outreville, J. F. (2013). *Theory and practice of insurance*. Springer.

8.	Rejda, G. E., & McNamara, M. J. (2020). *Principles of risk management and insurance* (14th ed.). Pearson.

9.	Skipper, H. D., & Kwon, W. J. (2007). *Risk management and insurance: Perspectives in a global economy*. Wiley-Blackwell.

10.	Vaughan, E. J., & Vaughan, T. M. (2014). *Fundamentals of risk and insurance* (11th ed.). Wiley.

Suggested Reading

1.	Black, K., & Skipper, H. D. (2014). *Life and health insurance*. Pearson Education India.

2.	IRDAI. (2023). *Annual report 2022–23*. Insurance Regulatory and Development Authority of India.

3.	Mishra, M. N., & Mishra, S. B. (2016). *Insurance: Principles and practice*. S. Chand Publishing.

4.	Rejda, G. E., & McNamara, M. J. (2020). *Principles of risk management and insurance* (14th ed.). Pearson.

5.	Vaughan, E. J., & Vaughan, T. M. (2014). *Fundamentals of risk and insurance* (11th ed.). Wiley.

4 BLOCK

Insurance Claims and Regulations
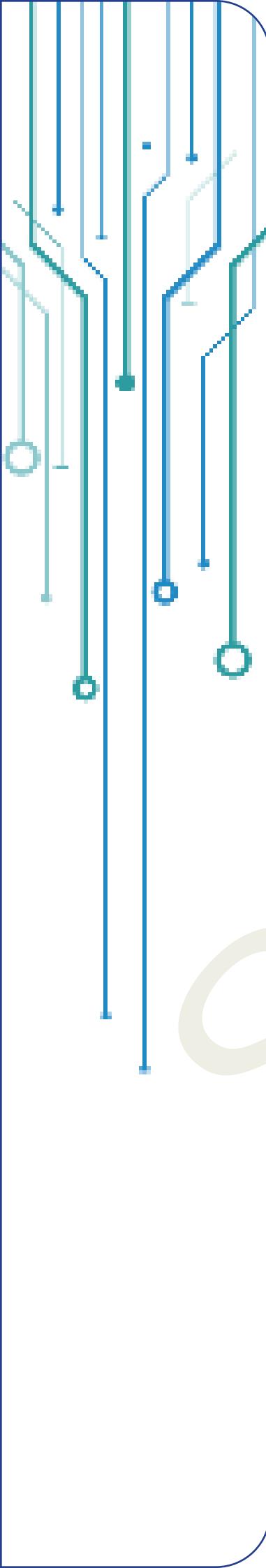
Unit ①
Insurance Claims

Learning Outcomes

After completing this unit, the learner will be able to;

◊ explain the meaning and importance of insurance claims in both life and non-life insurance sectors

◊ distinguish between various types of insurance claims and the procedures for their settlement

◊ identify the key documents and timelines required for efficient claim settlement

◊ comprehend IRDAI guidelines to evaluate and process different claim scenarios

Prerequisites

Mr. Sharma, a 45-year-old small business owner, had been diligently paying premiums for his life insurance policy for 15 years. One day, tragedy struck when he passed away unexpectedly due to a heart attack. His wife, Mrs. Sharma, suddenly found herself responsible for their children's education, household expenses, and an outstanding home loan. In this difficult moment, she remembered the life insurance policy. Within a week, she approached the insurance company, submitted the required documents, and within 20 days, the claim amount was credited to her account. This timely settlement not only gave her financial security but also reassured her faith in the value of insurance.

Just like Mr. Sharma's case, insurance claims play a vital role in protecting individuals, families, and businesses from financial distress after unforeseen events. Whether it is a life insurance payout to a grieving family, a motor insurance claim after a road accident, or a health insurance settlement covering surgery costs, the claim process is the mechanism through which the insurer fulfils its promise.

This unit will guide you through the meaning, importance, types, procedures, timelines, documentation, and regulations related to insurance claims, both life and non-life, supported by real-world examples and IRDAI guidelines. By the end, you will understand not just the technical process, but also the human impact of timely and fair claim settlement.

Keywords

Claim Settlement Ratio (CSR), Nominee, Third Party Administrator (TPA), Surveyor's Report, Early Death Claim

Discussion

4.1.1 Meaning of Insurance Claim

An insurance claim is a formal request made by the insured (policyholder) or their legal beneficiary to the insurance company, asking for compensation for a loss, damage, illness, or death that is covered under the terms and conditions of the insurance policy. When the insured event occurs whether it's a medical emergency, property damage, or the death of the life assured the policyholder (or nominee) becomes entitled to receive the agreed benefit from the insurer.

In simple terms, a claim is the legal right of the insured to demand payment or service from the insurer, once the specified insured risk materialises. The insurer is obligated to verify the claim and, if valid, to settle it in accordance with the policy provisions

Example:If a policyholder holding a ₹50 lakh term life insurance policy dies during the policy term, the nominee can file a claim under the policy to receive the sum assured. For instance, in 2023, an LIC nominee in Maharashtra successfully claimed ₹25 lakh after the policyholder's accidental death. The claim was settled within 15 days under IRDAI's prompt settlement guidelines.

4.1.2 Importance of Insurance Claims

Insurance claims form the core function of an insurance contract, because they represent the fulfilment of the insurer's promise to provide financial protection in case of loss. Without the ability to make and settle claims, an insurance policy would have no real value to the policyholder.The importance of insurance claims are as follows : -

i.   **Ensure Financial Security :** Claims provide critical financial relief to the insured or their nominees. For example, a health insurance claim can cover high hospitalisation bills, preventing financial distress for the family.

ii. **Reinforce Trust in the Insurance Industry :** Smooth and fair claim settlement boosts public confidence in insurers. The Claim Settlement Ratio (CSR), published annually by IRDAI, is one of the main indicators of an insurer's reliability on Life Insurance. In the FY 2022–23 reported a CSR of 98.52% for individual life insurance in FY 2022–23.

iii. **Help Mitigate Losses from Unexpected Events :** Whether it's a factory fire, a vehicle accident, or sudden illness, timely claims enable quick recovery, minimising the financial loss.

iv. **Maintain Social and Economic Stability :** By ensuring that individuals and businesses can recover from setbacks, insurance claims contribute to wider economic stability and social well-being.

4.1.3 Types of Insurance Claims

Insurance claims differ based on the type of insurance policy and the nature of the insured event. In the case of life insurance, claims can generally be classified into three major categories: maturity claims, death claims, and rider claims. Whereas Non-life insurance claims can be generally divided into Health insurance, Motor insurance, Fire insurance, Marine insurance and travel insurance. Below is the classification.
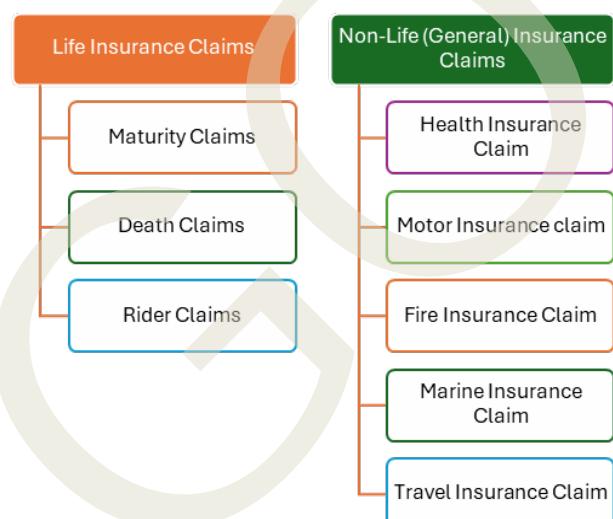

Figure 4.1.1: Types of Insurance Claims

A. Life Insurance Claims

Insurance claims in life insurance are broadly classified into maturity claims, death claims, and rider claims. Each type has its own eligibility conditions, required documentation, and settlement process. Understanding these categories helps policyholders and nominees know what to expect and how to ensure a smooth settlement experience.

i. **Maturity Claims :** A maturity claim arises when a life insurance policy completes its term and the life assured is alive on the maturity date. In such cases, the insurer is liable to pay the sum assured along with any applicable bonuses to the policyholder, as per the terms of the contract. The policyholder

is required to submit the original policy document, valid identity proof such as Aadhaar or PAN, and a duly signed discharge form. Maturity claims are generally straightforward because the payment is due under the contractual agreement without the need for further investigation into risk factors. For example, in 2023, a policyholder who had completed a 20-year endowment plan with the Life Insurance Corporation of India received ₹10 lakh in maturity benefits, which included both the basic sum assured and accrued bonuses. The claim was processed and paid within seven working days in line with IRDAI service standards, illustrating the efficiency of maturity claim settlements.

ii. **Death Claims :** Death claims occur when the insured person dies during the policy term, and the benefit is paid to the nominee or legal heir. These claims are categorised as early death claims when the death occurs within three years of policy issuance and non-early death claims, which occur after three years. Early death claims often undergo detailed investigation to verify the cause of death and ensure that there was no material misrepresentation at the time of policy issuance. For non-early death claims, Section 45 of the Insurance Act, 1938 provides that an insurer cannot repudiate the policy on the ground of misstatement except in cases of proven fraud. To process a death claim, the nominee must submit the death certificate issued by the municipal authority, the claim form, and their KYC documents. Additional evidence such as hospital records, post-mortem reports, or FIR copies may be required in cases of accidental death. For instance, in 2022, a nominee in Kerala received ₹50 lakh under a term insurance policy after the insured died in a road accident. As it was an early claim, the insurer conducted a 20-day investigation by reviewing police and medical reports before releasing the payment, ensuring compliance with IRDAI's fair claims settlement requirements.

iii. **Rider Claims :** Rider claims relate to additional benefits purchased along with the main life insurance policy to enhance coverage. Common riders include accidental death benefit riders, critical illness riders, and disability riders. Claims under these riders are payable when the specific conditions outlined in the rider terms are met, and the claimant provides supporting documentation. For critical illness riders, medical records and hospital discharge summaries are required to confirm the diagnosis, while accidental death or disability riders typically require police reports, post-mortem findings, and eyewitness statements. Rider payouts are made over and above the base sum assured. For example, in 2021, a policyholder with a base sum assured of ₹20 lakh and an accidental death benefit rider worth ₹10 lakh died in a car accident. The nominee received ₹30 lakh in total ₹20 lakh from the base policy and ₹10 lakh from the rider after submitting the FIR, post-mortem report, and hospital records. This demonstrates how riders can significantly increase the financial support available to beneficiaries in specific circumstances.

B. Non-Life (General) Insurance Claims

Non-life insurance claims cover a wide variety of risks beyond life coverage, protecting against losses related to health, property, vehicles, marine transit, and travel.

Each category has specific documentation and procedures to ensure that the claim is settled fairly and promptly.

i. **Health Insurance Claim :** A health insurance claim is made to cover hospitalisation or medical treatment expenses incurred by the insured. Claims can be settled in two ways: through a cashless facility, where the insurer directly settles bills with a network hospital, or through reimbursement, where the policyholder pays the expenses upfront and later claims repayment from the insurer. In both cases, the insured must submit the hospital discharge summary, medical bills, prescriptions, and identity proof. For example, in 2023, under the Ayushman Bharat scheme, thousands of beneficiaries availed cashless treatments in empanelled hospitals, with claim approvals often processed within 24 hours to facilitate immediate patient care.

ii. **Motor Insurance Claim :** A motor insurance claim is lodged when a vehicle suffers damage due to an accident, theft, or natural disaster, or when there is third-party liability for injury or property damage. The claimant is required to provide the First Information Report (FIR) in case of theft or serious accidents, vehicle registration and insurance papers, and repair estimates or bills from authorised workshops. In 2022, for instance, a Delhi motorist who suffered heavy damage to his car during a flood successfully claimed ₹3.5 lakh under his comprehensive motor insurance policy after submitting photographs of the damage, the repair invoice, and the necessary vehicle documents.

iii. **Fire Insurance Claim :** Fire insurance claims are made when insured property is damaged or destroyed by fire, explosion, or other perils covered in the policy. To process such claims, the insured must submit a fire brigade report confirming the incident, property ownership documents, and a detailed loss assessment report prepared by a surveyor. In 2021, a textile warehouse in Gujarat that suffered massive damage due to a short circuit fire recovered ₹1.2 crore from its insurer after the surveyor verified the extent of the loss and the cause was confirmed as accidental, in accordance with the policy's coverage terms.

iv. **Marine Insurance Claim :** Marine insurance claims cover loss or damage to cargo or ships during transit by sea, air, or land. The claimant needs to provide a bill of lading, shipping invoice, packing list, and a survey report that details the nature and extent of the damage. For example, in 2022, an exporter from Mumbai claimed compensation for water-damaged machinery shipped to Dubai after the cargo hold was flooded during a storm. The insurer settled the claim based on the marine surveyor's report, which confirmed that the loss occurred during the insured transit and was due to a covered peril.

v. **Travel Insurance Claim :** Travel insurance claims can arise for various reasons, including lost baggage, trip cancellations, flight delays, or medical emergencies during travel. The required documents vary depending on the claim type baggage loss claims need airline baggage irregularity reports, trip cancellations require proof of bookings and cancellations, and medical claims need treatment bills and reports from the destination country. In 2023, an Indian tourist in Singapore who suffered a sudden appendicitis attack filed a claim for emergency surgery costs amounting to ₹5 lakh. The insurer reimbursed the expenses within 15 days after verifying hospital records and the travel insurance policy coverage.

4.1.4 Life Insurance Claim Settlement Procedure

The Insurance Regulatory and Development Authority of India (IRDAI) mandates that insurers settle claims promptly, fairly, and transparently, especially for life and health insurance. Under the IRDAI (Protection of Policyholders' Interests) Regulations, 2017, life insurance claims must be settled within 30 days of receiving all necessary documents, and in no case later than 90 days if further investigation is required. Health insurance claims, especially in cashless mode, must be approved or rejected within a pre-specified turnaround time to avoid delays in treatment.

Example: In 2022, ICICI Lombard processed over 95% of its health claims in under 30 days, aligning with IRDAI's service benchmarks. Similarly, a private sector bank's term insurance claim for a cardiac death was approved in just 8 days, reinforcing customer trust.

Let's understand the step-by-step process for both maturity and death claims:

A. Maturity Claim Process:

i.   **Intimation by Insurer :** The maturity claim process begins when the insurance company sends an official intimation to the policyholder regarding the upcoming maturity date. As per industry practice and IRDAI guidelines for timely settlements, this notice is typically sent 30 to 90 days before the policy's maturity. The communication delivered via post, email, or SMS serves as a reminder for the policyholder to prepare the necessary documents in advance. This proactive approach helps ensure that the policyholder experiences no delay in receiving their maturity benefits and that all requirements are met before the due date. For instance, the Life Insurance Corporation of India (LIC) routinely dispatches maturity notices 90 days prior, enabling smooth claim processing for lakhs of policyholders annually.

ii. **Submission of Documents :** Once the maturity intimation is received, the policyholder must submit the required documents to the insurer. These generally include the original policy bond to confirm the validity of the contract, valid identity proof such as Aadhaar or PAN for KYC compliance, and bank account details often with a cancelled cheque or passbook copy to ensure accurate and secure fund transfer. The documents may be submitted physically at the insurer's branch or through authorised digital claim portals, depending on the insurer's facilities. Proper and complete documentation is critical; any missing information can delay claim settlement.

iii. **Claim Processing :** After receiving the documents, the insurer begins the claim processing stage. Here, the submitted details are verified against the insurer's records to confirm the policy's authenticity, ensure that all premiums have been paid up to date, and check for any pending requirements or encumbrances. This process may also involve internal checks for compliance with IRDAI regulations and anti-fraud measures. Efficient processing not only ensures prompt payment but also reinforces customer trust in the insurer's service standards.

iv. **Payment :** Once the claim is approved, the maturity amount comprising the sum assured and any accrued bonuses or loyalty additions is disbursed directly to the policyholder's registered bank account. Most insurers use electronic payment modes like NEFT or RTGS for speed, safety, and accuracy. Payment timelines are generally short; IRDAI requires life insurers to settle maturity claims within 30 days of receiving all necessary documents. For example, a 2023 LIC endowment policy maturity claim worth ₹8 lakh was credited to the policyholder's account in just seven working days after verification, showcasing the efficiency possible when both insurer and policyholder act promptly.

B. Death Claim Process

i. **Intimation of Death :** The first step in the death claim process is for the nominee or legal heir to inform the insurance company about the insured's death as soon as possible. Prompt intimation helps the insurer initiate the claim process without delay and prevents any procedural complications. The nominee should provide essential details such as the policy number, full name of the deceased, date of death, and the cause of death (whether natural or accidental). This information allows the insurer to locate the policy in its records and guide the nominee regarding the required documentation. Many insurers now offer multiple channels for death claim intimation, including branch visits, customer care hotlines, email, and online claim portals, ensuring accessibility and speed.

ii. **Claim Form Submission :** Once the death has been intimated, the nominee must submit the required documents to the insurer. This includes Form A (Claimant's Statement) duly filled and signed, the death certificate issued by the local municipal authority, valid identity proof of the nominee such as Aadhaar or voter ID, and bank account details for payment transfer. The original policy document must also be submitted as proof of the insurance contract. In cases of unnatural death such as accidents, suicide, or homicide an FIR (First Information Report) from the police and a post-mortem report are required to verify the circumstances of death. These requirements are in place to prevent fraudulent claims and ensure fair settlements.

iii. **Investigation (If Early Death) :** If the death occurs within three years from the date of policy issuance (known as an early claim), the insurer may conduct an investigation before approving the claim. This investigation can include verifying hospital and medical records, reviewing police reports, interviewing witnesses, and checking for possible non-disclosure of material facts at the time of policy purchase. The aim is to ensure that the claim is genuine and that there was no misrepresentation or fraud during the policy's inception.

iv. **Claim Decision :** According to IRDAI regulations, if no investigation is required, the insurer must make a claim decision and settle the payment within 30 days from the receipt of all necessary documents. However, if an investigation is needed, the process must be completed within 90 days, and the final claim decision must be communicated to the nominee within a maximum of 120 days from the date of claim intimation. This regulation ensures that nominees are not left waiting indefinitely and that insurers maintain transparency in claim handling.

v. **Claim Payment :** Once the claim is approved, the insurer releases the payment to the nominee or legal heir. This is typically done through NEFT (National Electronic Funds Transfer) to ensure secure and speedy transfer of funds, though cheque payments are also possible in certain cases. The claim amount usually equals the sum assured along with any applicable bonuses or riders, depending on the policy terms. For example, in 2022, a private life insurer in India settled a ₹50 lakh term insurance claim within 20 days of the nominee submitting complete documentation, demonstrating how efficient the process can be when both parties act promptly.
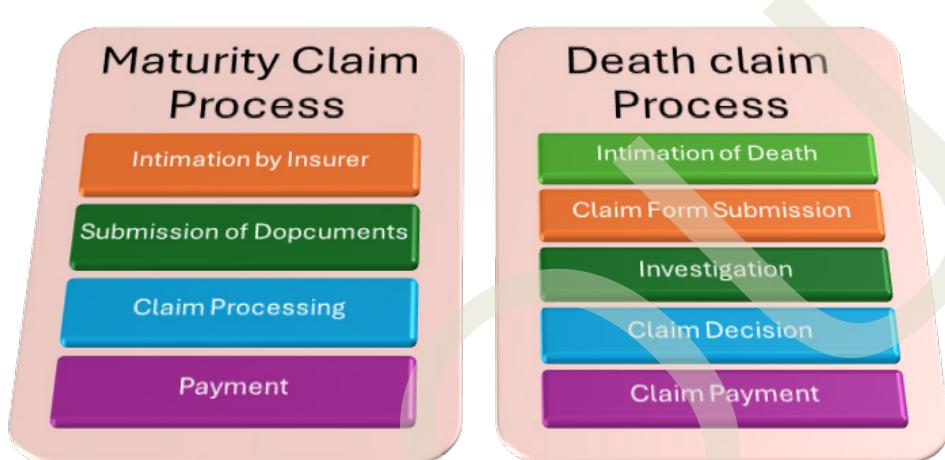

Figure 4.1.2 Life Insurance Claim Settlement Procedure

Case Study

In 2023, the Life Insurance Corporation of India (LIC), the country's largest life insurer, reported that it had successfully settled over 98% of death claims within the mandated 30-day period, as per IRDAI guidelines. This high settlement ratio reflected LIC's emphasis on efficient claim processing and its commitment to policyholders. The small percentage of remaining cases less than 2%, were delayed primarily due to disputes over policy terms, incomplete or incorrect documentation submitted by nominees, or the need for additional investigation in early-death claims (those filed within three years of policy issuance). For instance, some delays occurred when nominees failed to provide an original death certificate or bank account proof, requiring additional correspondence. This example underscores the importance of prompt and complete documentation by claimants, as well as the industry's focus on timely claim settlement to maintain trust in the insurance system.

4.1.5 Non-Life Insurance Claim Settlement Procedure

While specific requirements vary depending on the type of general (non-life) insurance, such as motor, health, fire, or marine, the overall claim settlement process broadly follows the same sequence of steps. Below is the general procedure explained in detail.
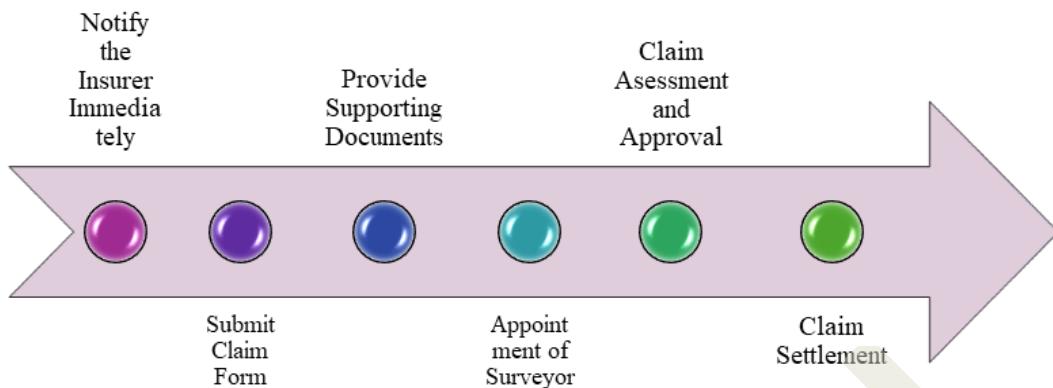
Figure 4.1.3 Non-Life Insurance Claim Settlement Procedure

1. **Notify the Insurer Immediately** : The first step is to inform the insurance company about the loss or damage as soon as possible, ideally within the time limit specified in the policy document. Timely intimation is critical because delays can make it difficult for the insurer to verify facts or assess the damage accurately. The notification should include the policy number, the type of loss (such as accident, theft, fire, or illness), and an estimate of the claim value. Most insurers now allow this step to be completed through toll-free numbers, mobile apps, or dedicated claim-reporting websites, in addition to physical branch visits. For example, in motor insurance, reporting an accident within 48 hours is a common requirement to ensure hassle-free processing.

2. **Submit Claim Form :** After the initial notification, the insured must fill out and submit a claim form, which can be downloaded from the insurer's website or collected from its branch office. This form captures detailed information about the incident, including the date, time, location, description of the event, and any other relevant circumstances. Accurate and truthful disclosure is essential, as any inconsistency can delay or even lead to the rejection of the claim. Some insurers also provide pre-filled digital claim forms to speed up the process for registered policyholders.

3. **Provide Supporting Documents :** To substantiate the claim, the insured must provide specific supporting documents depending on the nature of the insurance and the event. For example:

   i. FIR (First Information Report) in case of motor accidents, theft, or fire incidents involving criminal investigation.

   ii. Hospital bills, discharge summaries, and medical reports in case of health insurance claims.

   iii. Surveyor's report for large-scale property or marine cargo losses.

   iv. Repair estimates or invoices for vehicle or property damage claims. These documents help the insurer verify the validity of the claim and quantify the loss accurately. The list of required documents is usually outlined in the policy booklet.

5. **Appointment of Surveyor :** For significant claims especially in motor, fire, and marine insurance, the insurer appoints an IRDAI-approved surveyor to assess the extent of loss or damage. The surveyor's role is to conduct a site visit, inspect the damage, interview witnesses if necessary, and prepare a survey report with recommendations on claim validity and the quantum of loss. According to IRDAI regulations, surveyors must submit their reports within 30 days of appointment, ensuring the process moves forward without undue delay.

6. **Claim Assessment and Approval :** Once all documents, reports, and assessments are received, the insurer evaluates the claim in light of the policy terms, exclusions, and coverage limits. If the claim is valid and falls within the policy's scope, it is approved for settlement; otherwise, the insurer may issue a rejection letter with clear reasons. This step may also involve internal legal and compliance checks to ensure the decision aligns with regulatory standards and company policy.

7. **Claim Settlement** : The final step is the disbursement of the claim amount. In cashless claims such as health insurance at network hospitals or motor repairs at authorised garages the insurer directly pays the service provider, sparing the policyholder from making upfront payments. In reimbursement claims, the policyholder first pays the expenses out-of-pocket, submits all original bills and receipts, and then receives the payment from the insurer. IRDAI mandates that insurers must settle approved claims within 30 days of receiving the last required document to protect policyholders' interests.

4.1.5.1 Specific Claim Types

1. **Health Insurance (Cashless Claim Example)** : Cashless claims are one of the most convenient features of modern health insurance policies, as they allow the insured to receive medical treatment without having to make upfront payments, provided the hospital is part of the insurer's network hospital list. For example, Mrs. Rani was admitted to a network hospital for a planned surgery. On arrival, her son approached the hospital's insurance helpdesk, where a Third-Party Administrator (TPA) a specialised agency appointed by the insurer handled claim coordination. The TPA verified her health insurance policy details, hospital admission records, and medical diagnosis against the coverage terms. Once satisfied, the TPA granted pre-authorisation for the expenses covered under the policy. This meant that the hospital billed the insurer directly for all eligible costs, while Mrs. Rani was responsible only for charges not covered by the policy, such as certain consumables or non-medical items. This process eliminated the financial burden at the time of treatment and ensured a smooth hospital discharge.

2. **Motor Insurance (Accident Claim Example) :** Motor insurance claims, especially after accidents, follow a sequence designed to ensure proper documentation and accurate assessment of damage. In one instance, Mr. Ahmed's car was involved in a collision, causing significant damage to the front bumper and engine components. Immediately after the incident, he lodged a First Information Report (FIR) at the local police station an essential

requirement in many accident cases, especially when there is third-party involvement or injury. He then informed his motor insurance provider about the accident, providing details of the location, nature of damage, and FIR number. The insurer appointed a licensed surveyor to inspect the vehicle, photograph the damage, and prepare a repair estimate in line with policy coverage. Once Mr. Ahmed submitted the garage's final repair bill, the insurer either paid the amount directly to the authorised garage (in case of a cashless facility) or reimbursed Mr. Ahmed after he settled the bill himself. This process ensured transparency, proper documentation, and adherence to IRDAI's claims settlement norms.

4.1.6 Important Guidelines and Time Limits

1. **Intimate Insurer (Non-Life) :** In the case of non-life insurance policies such as motor, health, fire, or marine insurance, the insured must inform the insurer about the loss or event within 24–48 hours of its occurrence. This time frame may vary depending on the insurer's specific policy conditions, but prompt intimation is crucial for accurate assessment and speedy claim settlement. Delays in reporting can lead to complications in verifying the incident and, in some cases, denial of the claim. For example, in motor accident cases, quick notification allows the insurer to appoint a surveyor before the vehicle is repaired, ensuring that damage assessment is based on actual evidence.

2. **Submit Documents :** After notifying the insurer, the insured is required to submit all relevant claim documents such as claim forms, invoices, reports, and supporting evidence within 7 to 15 days of the event, depending on policy type and terms. Timely submission helps avoid claim processing delays and prevents the insurer from closing the claim due to incomplete information. For instance, in health reimbursement claims, hospital bills and discharge summaries must be provided within the stipulated period to be eligible for settlement.

3. **Life Insurance Claim Settlement (No Investigation) :** When a life insurance claim is filed and no investigation is necessary, the insurer is mandated by the Insurance Regulatory and Development Authority of India (IRDAI) to settle the claim within 30 days from the date of receiving all required documents. This ensures that nominees or beneficiaries receive financial support quickly after the death of the policyholder or maturity of the policy. This time limit is critical for dependents who may rely on the claim proceeds for immediate expenses such as education, daily living, or loan repayments.

4. **With Investigation (Life Insurance)** : If the life insurance claim involves suspicious circumstances such as an early claim (filed within three years of policy issuance) or conflicting evidence the insurer is allowed to conduct a detailed investigation. As per IRDAI rules, the entire process, including investigation and final decision, must be completed within 120 days from the date the claim was filed. This provision balances the insurer's need to prevent fraud with the policyholder's right to timely claim resolution.

5. **Health Reimbursement Settlement :** In health insurance reimbursement claims, where the insured pays the hospital expenses upfront and later seeks repayment, insurers are required to process and settle the claim within 15–30

working days after receiving all necessary documents. The variation in time depends on the complexity of the claim and the insurer's internal processes. For example, claims involving multiple hospitalisations or specialised treatments may require more verification, but must still adhere to IRDAI's maximum allowable timeframe.

4.1.7 Common Documents for Claim Settlement

A. Life Insurance

For life insurance claims, the documentation serves to verify the policyholder's death, establish the claimant's identity, and confirm the policy details. The claim form (also called the claimant's statement) must be duly filled with all required details such as policy number, cause of death, and nominee information. A death certificate, issued by the local municipal authority or relevant government department, is mandatory to officially confirm the demise. The original policy document is required as legal proof of the insurance contract, and helps the insurer confirm policy terms and status. The KYC documents of the nominee, such as Aadhaar card, PAN card, or voter ID, ensure proper identification and compliance with anti-money laundering (AML) norms. Finally, bank account proof (such as a cancelled cheque or bank passbook copy) is necessary to facilitate direct transfer of claim proceeds through NEFT or RTGS. For instance, in 2022, LIC reported that incomplete KYC and missing bank proof were among the top reasons for delayed life insurance claim settlements.

B. General Insurance

In general (non-life) insurance, the required documents depend largely on the nature of the claim, but certain essentials remain common. A duly filled claim form is the starting point, providing key details about the insured event. For claims involving theft or accidents, particularly in motor or property insurance an FIR (First Information Report) from the police is mandatory to establish the occurrence and investigate responsibility. A copy of the policy document is needed to verify coverage, limits, and exclusions. In health insurance claims, medical bills and discharge summaries support the reimbursement of hospitalisation expenses, while in motor claims, repair estimates from an authorised garage help determine the cost of restoration. For larger claims, particularly in fire, marine, or major accident cases, the insurer may appoint a licensed surveyor, and the surveyor's report becomes a critical document for assessment. For example, in a 2023 motor theft case in Delhi, the claim was settled swiftly within 15 days because the insured submitted the FIR, policy copy, and surveyor's report without delay.

Recap

◊ Insurance claim means a formal request made to the insurer for compensation when a covered event occurs.

◊ Claims are important because they ensure financial security, build trust, reduce losses, and promote stability.

◊ There are two main types of claims: life insurance claims (maturity, death, rider) and non-life insurance claims (health, motor, fire, marine, travel).

◊ The life insurance settlement process follows a step-by-step procedure for maturity and death claims as per IRDAI timelines.

◊ The non-life insurance settlement process generally includes notification, submission of documents, survey, and final settlement.

◊ IRDAI provides guidelines and timelines to ensure claims are settled within specific periods to protect policyholders.

◊ Common documents required include the claim form, proof of loss, a copy of the policy, KYC documents, and other supporting evidence depending on the type of claim.

Objective Questions

1. What does CSR stand for in insurance?
2. Who receives life insurance claim benefits if the insured dies?
3. Time limit to intimate insurer for non-life claim?
4. Document required for motor theft claim from police?
5. IRDAI settlement limit for life claims without investigation?
6. What is a TPA in health insurance?
7. Early death claim period in life insurance?
8. Payment mode for most claim settlements?
9. Document verifying ownership in fire claims?
10. Report prepared by IRDAI-approved loss assessor?
11. Time limit for health reimbursement claim settlement?
12. Law section protecting non-early death claims?

Answers

1. Claim Settlement Ratio
2. Nominee
3. 24–48 hours
4. FIR
5. 30 days
6. Third Party Administrator
7. 3 years
8. NEFT
9. Property documents
10. Surveyor's report
11. 15–30 working days
12. Section 45

Self-Assessment Questions

1. Briefly explain the life insurance claim settlement procedure
2. Essay on types of Insurance claims ?
3. Short note on significance of Insurance claims
4. List out the common documents required for insurance claims ?
5. What do you mean by Insurance claim ?
6. Short note on time limit for Insurance claim settlement ?

Assignments

1. Explain the significance of insurance claims in maintaining public trust in the insurance industry.
2. Describe the step-by-step maturity claim process for life insurance with an example.
3. Discuss the types of documents required for life and general insurance claim settlement.

4. Evaluate the role of IRDAI in ensuring timely and fair claim settlements.

5. Compare the procedures for cashless health claims and reimbursement claims.

6. Prepare a flowchart showing the death claim settlement process in life insurance.

7. Collect and review two real-life examples of motor insurance claim settlements from news or case reports.

8. Draft a sample claim intimation letter for a fire insurance claim.

9. Visit an insurance company website and download a health insurance claim form; identify required fields.

10. Create a comparative table of claim settlement ratios for five insurers over the last three years.

Reference

1. Bhole, L. M., & Mahakud, J. (2017). *Financial Institutions and Markets: Structure, Growth and Innovations* (6th ed.). McGraw Hill Education.

2. IRDAI. (2017). *Protection of Policyholders' Interests Regulations, 2017*. Insurance Regulatory and Development Authority of India.

3. Kothari, R. & Batra, S. (2019). *Principles of Insurance*. PHI Learning Pvt. Ltd.

4. LIC of India. (2023). *Annual Report 2022–23*. Life Insurance Corporation of India.

5. Mishra, M. N., & Mishra, S. B. (2016). *Insurance: Principles and Practice*. S. Chand Publishing.

6. Rejda, G. E., & McNamara, M. J. (2020). *Principles of Risk Management and Insurance* (14th ed.). Pearson.

7. ICICI Lombard. (2023). *Claim Process and Service Standards*. ICICI Lombard General Insurance Co. Ltd.

8. Tripathi, K. P. (2018). *Insurance Theory and Practice*. Himalaya Publishing House.

9. Yadav, S. S., & Singh, R. (2021). *Insurance and Risk Management*. Sage Publications.

10. IRDAI. (2023). *Annual Report 2022–23*. Insurance Regulatory and Development Authority of India.

Suggested Reading

1. IRDAI. (2017). *Protection of Policyholders' Interests Regulations, 2017*. Insurance Regulatory and Development Authority of India.

2. Kothari, R. & Batra, S. (2019). *Principles of Insurance*. PHI Learning Pvt. Ltd.

3. LIC of India. (2023). *Annual Report 2022–23*. Life Insurance Corporation of India.

4. Mishra, M. N., & Mishra, S. B. (2016). *Insurance: Principles and Practice*. S. Chand Publishing.

5. Rejda, G. E., & McNamara, M. J. (2020). *Principles of Risk Management and Insurance* (14th ed.). Pearson.

6. ICICI Lombard. (2023). *Claim Process and Service Standards*. ICICI Lombard General Insurance Co. Ltd.
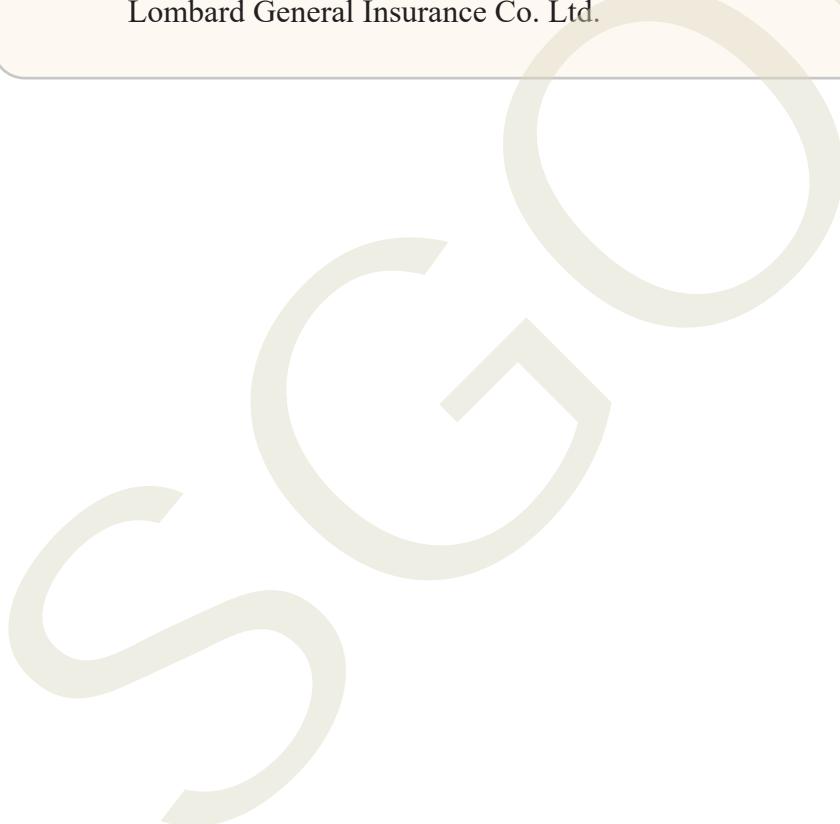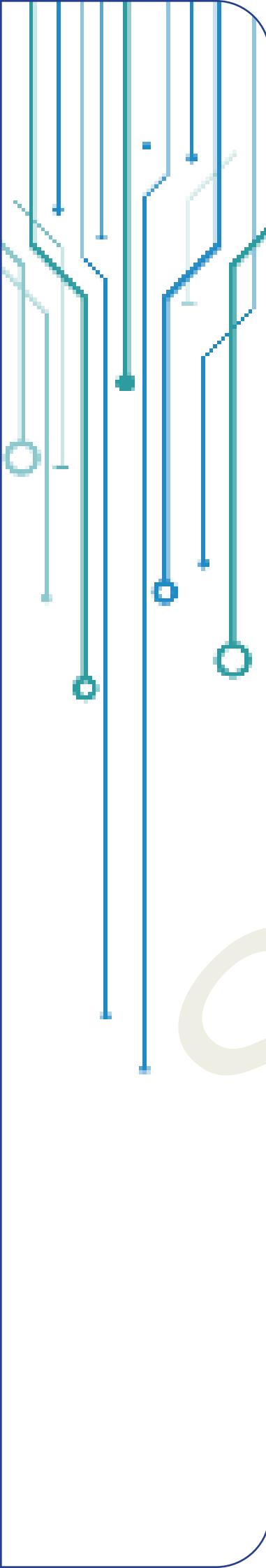
Unit 2

Insurance Regulations

Learning Outcomes

After completing this unit, the learner will be able to;

◊ comprehend the history and impact of the privatisation of the Indian insurance industry

◊ explain the role and implications of Foreign Direct Investment (FDI) in insurance

◊ define bancassurance and its benefits for banks and insurers

◊ realise key IRDAI regulations governing insurance operations in India

Prerequisites

In 2000, when India opened its insurance sector to private participation, Mr. Sharma, a middle-class shop owner, found himself with more options than ever before. Until then, his choices were limited to the government-owned LIC for life insurance and a few state-owned general insurers for his shop's coverage. With the arrival of private and foreign-backed insurers, he could now compare policies, premiums, and services, something unimaginable a decade earlier. This change was not accidental; it was the result of deliberate reforms, regulatory oversight, and global investment.

The transformation of India's insurance industry has been shaped by privatisation, foreign direct investment (FDI), bancassurance partnerships, and the proactive role of the Insurance Regulatory and Development Authority of India (IRDAI). These developments not only brought innovation in product offerings but also expanded coverage to rural and underserved populations. Initiatives like micro-insurance,

standardised health policies, and digital claim settlements are now part of everyday insurance operations.

By studying this unit, learners will explore how these regulatory changes, market innovations, and strategic collaborations have created a more competitive, transparent, and customer-friendly insurance landscape. The journey from a closed, state-controlled sector to a dynamic, tech-enabled marketplace offers valuable lessons in policy reform, financial inclusion, and sustainable industry growth.

Keywords

Privatisation, Foreign Direct Investment (FDI), Bancassurance, IRDAI Regulations, Insurance Penetration

Discussion

4.2.1 Insurance Regulation in India

For decades, insurance in India was dominated by state-owned entities such as the Life Insurance Corporation of India (LIC) in the life segment and the General Insurance Corporation of India (GIC) along with its subsidiaries in the non-life segment. This monopoly meant that products, services, and processes were largely standardised, but innovation and customer choice were limited.

The wave of economic reforms in the 1990s brought a significant shift. Based on the recommendations of the Malhotra Committee (1993), the Government of India opened the insurance sector to private companies in 2000, allowing both domestic and foreign players to participate. This liberalisation led to increased competition, the introduction of innovative insurance products, improved customer service, and more efficient claim settlement practices. The sector also attracted foreign investment, which helped strengthen the capital base and technological capabilities of insurers.

Today, the Insurance Regulatory and Development Authority of India (IRDAI), established in 1999 under the IRDA Act, serves as the apex body overseeing the industry. IRDAI's mandate includes protecting policyholders' interests, ensuring fair market conduct, promoting healthy competition, regulating premium rates where necessary, and fostering the orderly growth of the insurance sector. Through its regulations, guidelines, and periodic monitoring, IRDAI has transformed insurance into a more transparent, competitive, and customer-centric industry, aligning it with global standards while addressing India's unique socio-economic needs.

4.2.2 Privatisation of the Insurance Industry - Historical Background

4.2.2.1 Pre-Nationalisation Era

Before 1956, the Indian insurance sector consisted of numerous private insurers, both domestic and foreign, operating in a largely unregulated environment. This led to inconsistent service quality, financial instability among some insurers, and limited consumer protection. While some companies maintained ethical practices, others faced solvency issues, which sometimes left policyholders without payouts.

◊ **1956 – Nationalisation of Life Insurance**

To safeguard policyholder interests and consolidate the fragmented industry, the Government of India nationalised the life insurance business in 1956. All 245 private life insurance companies were merged to form the Life Insurance Corporation of India (LIC). This move ensured stability and uniform service standards, though it also removed competition from the market.

◊ **1972 – Nationalisation of General Insurance**

Following the success of LIC's consolidation, the General Insurance Business (Nationalisation) Act, 1972 brought over 100 general insurers together under the umbrella of the General Insurance Corporation of India (GIC) and its four subsidiaries National Insurance, New India Assurance, Oriental Insurance, and United India Insurance. This gave the government complete control over both life and general insurance sectors.

◊ **1991 – Economic Reforms**

In 1991, India's broader economic liberalisation policies began to reshape several sectors, including insurance. The focus shifted towards deregulation, improving efficiency, and attracting private and foreign investments. This reform agenda set the stage for opening up the insurance sector.

◊ **1999 – Formation of IRDAI and Opening to Private Companies**

The Insurance Regulatory and Development Authority of India (IRDAI) was established in 1999 as an autonomous body to regulate and promote the orderly growth of the insurance industry. In the same year, the government allowed private companies—both Indian and foreign joint ventures to enter the insurance market, breaking the state monopoly and introducing competition.

4.2.2.2 Malhotra Committee Recommendations (1994)

The Malhotra Committee, set up in 1993 and reporting in 1994, was tasked with reviewing the structure of the insurance sector and suggesting reforms. Its recommendations were pivotal in shaping the privatisation process. Key proposals included:

i. Liberalisation of the insurance sector to encourage competition and efficiency.

ii. Creation of a strong and independent regulator to protect policyholders' interests and oversee the market.

iii. Encouragement of competition among both public and private players to enhance product quality, customer service, and outreach.

iv. Diversification of distribution channels, including brokers and bancassurance, to expand penetration.

These recommendations laid the groundwork for legislative and policy changes that materialised by the end of the decade.

4.2.2.3 Post-Privatisation Developments

Entry of Private and Foreign Insurers

The year 2000 marked the entry of private players such as ICICI Prudential Life (the first private life insurer), HDFC Life, Bajaj Allianz, and Max Life. Many of these companies partnered with established international insurers, bringing in global expertise, advanced underwriting systems, and customer service innovations.

Enhanced Product Innovation and Customer Choice

Privatisation led to the introduction of products tailored to different customer segments, including term plans, unit-linked insurance plans (ULIPs), micro-insurance for rural markets, and critical illness covers. This variety provided consumers with choices beyond the traditional endowment or money-back policies that dominated the pre-2000 market.

Technology-Driven Servicing and Competitive Pricing

Private insurers leveraged technology to improve policy issuance, premium payment, and claim settlement processes. Online platforms, mobile apps, and AI-based customer support became common, making insurance more accessible and user-friendly. Increased competition also led to more competitive premium rates, benefiting customers.

Example: In 2000, ICICI Prudential Life became the first private sector life insurer in India. It introduced flexible term insurance plans and ULIPs with investment-linked benefits, setting new benchmarks in transparency and service standards. Its rapid market growth highlighted the positive impact of private participation in the insurance sector.

4.2.3 Foreign Direct Investment (FDI) in Insurance

Foreign Direct Investment (FDI) in insurance refers to the capital invested by overseas companies or investors into Indian insurance firms. Such investment not only brings much-needed funds to strengthen the capital base of insurers but also introduces advanced technology, global best practices in risk assessment, product design, and customer service. FDI has been a critical driver in expanding the scale, efficiency, and competitiveness of India's insurance sector, especially after privatisation in 2000.

4.2.3.1 FDI Limit Changes

◊ **2000 – Initial 26% Cap**

When the insurance sector was opened to private players in 2000, the Government of India allowed foreign companies to hold up to 26% equity in Indian insurance firms. This cautious approach was meant to encourage foreign participation while ensuring majority Indian ownership and control.

◊ **2015 – Increased to 49%**

Under the Insurance Laws (Amendment) Act, 2015, the FDI cap was raised to 49%, allowing greater foreign involvement in joint ventures. This change was aimed at improving the capital adequacy of insurers, expanding product offerings, and enhancing operational efficiencies without relinquishing Indian majority control.

◊ **2021 – Latest Hike to 74%**

In 2021, the Government further increased the FDI limit to 74% to attract more foreign capital and deepen market penetration. This move was especially significant in the wake of the COVID-19 pandemic, as insurers required substantial funds to meet solvency norms and expand coverage to underinsured segments.

4.2.3.2 Conditions under the 74% FDI Cap

While the 74% limit permits foreign investors to hold majority stakes, certain conditions ensure regulatory oversight and safeguard policyholders' interests:

i. Board Majority and Control – Foreign partners are allowed to have majority representation and control in the company's board.

ii. Data Protection – Ownership and storage of policyholder data must remain within India to safeguard privacy and comply with local laws.

iii. Enhanced Solvency and Reporting – Insurers with majority foreign ownership are subject to stricter solvency margins, disclosure norms, and regulatory compliance to maintain financial stability and transparency.

4.2.3.3 Impact of FDI in the Indian Insurance Sector

i. **More Joint Ventures :** One of the most visible impacts of higher FDI limits in insurance has been the increase in joint ventures between Indian and foreign companies. Collaborations such as HDFC Life with Standard Life (UK) and Max Life with Axis Bank and Mitsui Sumitomo (Japan) have brought together domestic market expertise and global insurance know-how. These partnerships have enabled Indian insurers to access international capital, risk management practices, and global product design strategies, helping them compete effectively in a liberalised market.

ii. **Improved Customer Services, Innovation, and Competitiveness :** FDI has encouraged insurers to adopt advanced technology, data analytics, and customer engagement tools from global markets. This has led to more personalised insurance products, faster policy issuance, and quicker claim settlements. The

competition from foreign-backed insurers has also prompted domestic players to enhance service quality and introduce innovative offerings such as wellness-linked health plans and flexible premium options.

iii. **Strengthening of Insurance Infrastructure :** The inflow of foreign capital has helped insurers improve their operational infrastructure, including digital platforms, distribution networks, and training facilities. Many foreign partners have introduced robust underwriting systems, fraud detection mechanisms, and online service portals that have transformed the way insurance is sold and serviced in India. This has significantly contributed to increasing insurance penetration in both urban and rural areas.

Case Study – HDFC ERGO

A prime example of FDI-driven collaboration is HDFC ERGO General Insurance Company, a joint venture between HDFC Ltd. (India) and ERGO International AG (Germany), part of the Munich Re Group. The partnership combines HDFC's strong distribution reach in India with ERGO's international expertise in product innovation and risk assessment. As a result, HDFC ERGO has become one of the leading private general insurers in India, offering a wide range of motor, health, travel, and home insurance products with efficient digital claim settlement systems.

4.2.4 Bancassurance

Bancassurance refers to a distribution model where banks sell insurance products. both life and general through their branch network to their existing and potential customers. It is essentially a partnership between a bank and an insurance company in which the bank acts as a distribution channel for the insurer. The arrangement leverages the bank's extensive customer base, physical presence, and trust to promote insurance products, making it a win-win for all stakeholders.

4.2.4.1 Benefits of Bancassurance

Bancassurance delivers significant advantages for all parties involved banks, insurance companies, and customers. By blending banking and insurance services, it creates an integrated financial service model that enhances efficiency, accessibility, and profitability.

1. Benefits for Banks

a. **Diversification of Income Sources :** Through bancassurance, banks can supplement their traditional interest income with commission or fee-based revenue from selling insurance policies. This additional non-interest income helps reduce dependency on lending activities and strengthens financial stability. *Example:* HDFC Bank's partnership with HDFC Life has generated substantial fee-based income over the years, making it a consistent contributor to the bank's overall profits.

b. **Enhanced Customer Loyalty :** By positioning themselves as one-stop financial service providers, banks can deepen their relationships

with clients. Customers who purchase multiple products from the same bank are more likely to remain loyal and maintain long-term accounts. *Example:* ICICI Bank offers integrated wealth, loan, and insurance solutions, increasing customer retention rates.

c. **Opportunities for Cross-Selling :** Banks can use existing customer interactions to offer relevant insurance products. For instance, while granting a car loan, the bank can also propose motor insurance; while approving a mortgage, it can suggest home loan protection plans. This not only meets customer needs but also boosts bank revenues. *Example:* State Bank of India (SBI) offers life insurance alongside education loans, helping parents secure repayment assurance.

2. Benefits for Insurers

a. **Wider Market Reach :** Bancassurance allows insurance companies to tap into the bank's extensive branch network, including rural and semi-urban regions with historically low insurance penetration. This helps insurers expand their footprint without creating new sales infrastructure. *Example:* LIC's partnerships with several PSU banks have enabled it to access millions of rural customers.

b. **Reduced Customer Acquisition Costs :** Instead of building an independent network of agents, insurers can leverage the bank's facilities, trained staff, and trusted brand name. This drastically cuts marketing, training, and operational expenses. *Example:* Max Life Insurance's bancassurance alliances have reduced its distribution costs compared to traditional agency models.

c. **Access to Customer Data for Tailored Products :** Banks hold rich customer data on income levels, spending habits, and investment preferences. Insurers can use this information to design customised policies that match specific customer needs, leading to higher acceptance rates. *Example:* Some insurers design single-premium policies for fixed deposit customers who prefer one-time investments.

3. Benefits for Customers

a. **Convenience of a Single Service Point :** Customers can handle both their banking and insurance needs in one location. This saves time and eliminates the need to visit multiple offices. *Example:* While opening a savings account, customers can simultaneously buy life or health insurance at the same branch.

b. **Faster Service and Easy Premium Payments :** Bancassurance enables quicker policy issuance, premium collection, and claim assistance through bank counters or digital platforms. Premiums can often be paid via automatic deductions from bank accounts, reducing missed payments. *Example:* Many banks integrate insurance premium payment options into their net banking portals.

c. **Comprehensive Financial Planning :** By accessing savings, loans, investments, and insurance under one roof, customers

can plan their finances more holistically. This ensures they have both wealth-building tools and risk-protection measures in place. *Example:* Customers can bundle their mutual fund investments with life insurance to balance growth and protection.

4.2.4.2 Models of Bancassurance

Bancassurance is implemented through different models, each varying in the level of integration between the bank and the insurance company. The choice of model depends on the strategic goals, regulatory permissions, investment capacity, and operational readiness of the bank and insurer.

1. Referral Model

In the Referral Model, the bank plays a very limited role in the insurance sales process. Its main function is to identify potential customers and refer them to the insurance company. The insurer then handles all aspects of the transaction from explaining the policy to the customer, to underwriting, issuing the policy, and providing after-sales service. This model requires minimal training for bank staff and involves low compliance responsibility, making it attractive for smaller banks or those new to bancassurance. However, revenue potential is lower compared to other models since the bank only earns a small referral fee or incentive for each successful policy sale.

For example, a regional rural bank may refer its customers to the Life Insurance Corporation of India (LIC) for life policies without getting involved in selling or servicing the product, simply earning a fixed fee per referral.

2. Corporate Agency Model

The Corporate Agency Model involves a higher level of engagement, as the bank becomes a licensed corporate agent for one or more insurance companies. In this model, the bank markets and sells insurance products directly to customers through its branch network, while the insurer handles underwriting and claims. Bank staff receive product training and can explain policy features, assist with documentation, and collect premiums. The bank earns a commission on every sale, which often makes this model financially rewarding compared to referrals.

For instance, the State Bank of India operates as a corporate agent for SBI Life Insurance, allowing its branch staff to sell term insurance, endowment plans, and health insurance directly to customers. This model deepens customer relationships while generating significant non-interest income for the bank.

3. Joint Venture Model

In the Joint Venture Model, the bank and the insurance company form a separate legal entity to jointly develop, market, and service insurance products. This model enables both partners to share resources, infrastructure, expertise, and profits. It also allows for the creation of customised products tailored to the bank's customer base. Such joint ventures typically require significant investment and a long-term strategic commitment

but can deliver high returns through brand strength and dedicated product development.

A well-known example is ICICI Bank's joint venture with Prudential Corporation Holdings, which created ICICI Prudential Life Insurance. This partnership combines ICICI Bank's strong customer reach with Prudential's global insurance expertise, resulting in a comprehensive range of life insurance solutions for Indian customers.

4. Full Integration Model

The Full Integration Model represents the most advanced form of bancassurance, where insurance products are seamlessly integrated into the bank's overall suite of services. Here, customers perceive insurance as a natural extension of the bank's offerings, similar to savings accounts or investment products. Bank staff are thoroughly trained to sell, service, and advise on insurance, and IT systems are integrated so that customers can purchase and manage insurance policies through bank branches, ATMs, mobile apps, or online banking platforms. This high level of integration enables quick processing, strong cross-selling opportunities, and improved customer loyalty.

For example, HSBC integrates its insurance products into its global banking services, allowing customers to open an account, apply for a loan, and buy life or travel insurance during the same visit or via its online banking portal.

4.2.5 IRDAI: Insurance Regulatory and Development Authority of India (IRDAI)

The Insurance Regulatory and Development Authority of India (IRDAI) was established under the IRDA Act, 1999 as an autonomous statutory body to regulate, promote, and ensure the orderly growth of the insurance industry in India. Headquartered in Hyderabad, IRDAI operates under the jurisdiction of the Ministry of Finance, Government of India. Its creation marked a major milestone in the liberalisation of India's insurance sector, ensuring that both private and public insurers operate under a uniform and transparent regulatory framework.

Vision:

IRDAI's vision is *"to protect the interests of policyholders and ensure orderly growth of the insurance industry."* This vision underlines its dual mandate safeguarding policyholders from unfair practices while fostering a competitive and innovative insurance market that supports financial inclusion and economic stability.

4.2.5.1 Functions of IRDAI

1. Licensing and Registration

IRDAI is responsible for issuing licenses to insurers, agents, brokers, and other intermediaries in the insurance sector. It also regulates Third-Party Administrators (TPAs), who play a key role in health insurance claims processing. Licensing ensures that only qualified and financially sound entities are allowed to operate, thereby protecting consumers from fraudulent operators.

2. Policyholder Protection

One of IRDAI's core functions is to ensure transparency in policy terms and conditions so that policyholders fully understand the benefits and limitations of their coverage. The authority enforces strict guidelines for fair treatment of policyholders, including timely claim settlement and clear disclosure of charges. It has also set up grievance redressal mechanisms such as the Insurance Ombudsman to resolve disputes quickly and fairly.

3. Framing Regulations

IRDAI frames and enforces regulations related to product design, commissions paid to agents, solvency requirements, and investment norms for insurers. It sets rules for various types of insurance products such as Unit Linked Insurance Plans (ULIPs), term plans, health insurance, and crop insurance to ensure they meet minimum service standards and provide fair value to customers.

4. Monitoring and Supervision

The authority regularly audits the operations of insurers to ensure compliance with laws and regulations. This includes monitoring claim settlement ratios, fund management practices, and the financial health of companies. IRDAI's supervision helps maintain public trust in the insurance system by ensuring companies remain solvent and capable of meeting their obligations.

5. Promoting Competition and Innovation

By encouraging the entry of new players and fostering competition, IRDAI helps improve customer choice and service quality. It supports innovation in product design, distribution channels, and digital services, enabling insurers to adapt to changing customer needs and market conditions.

6. Financial Inclusion

IRDAI plays a vital role in extending insurance coverage to underserved populations. It promotes micro-insurance products and mandates that insurers maintain a certain level of rural and social sector coverage. The authority also oversees government-backed schemes such as the Pradhan Mantri Jeevan Jyoti Bima Yojana (PMJJBY) for life cover and the Pradhan Mantri Fasal Bima Yojana (PMFBY) for crop insurance, ensuring that benefits reach the intended beneficiaries.

4.2.5.2 Major IRDAI Regulations

1. Protection of Policyholders' Interests Regulations (2017)

These regulations are designed to safeguard the rights of policyholders by ensuring transparency in policy documents, clear disclosure of terms and conditions, and fair marketing practices. They also mandate prompt settlement of claims and impose

penalties on insurers for undue delays. For example, insurers must communicate claim decisions within 30 days of receiving all necessary documents, reinforcing trust in the industry.

2. IRDAI Regulations on Registration of companies

This regulation lays down the eligibility criteria, capital requirements, and solvency norms for companies seeking to enter the insurance business. It ensures that only financially sound entities with adequate resources and governance standards are granted licenses. The solvency margin requirement, maintaining a minimum surplus of assets over liabilities, ensures that insurers remain capable of meeting their obligations to policyholders.

3. Health Insurance Regulations (2016)

These rules govern various aspects of health insurance products, including renewability, portability, and standardisation. Renewability provisions ensure that insurers cannot arbitrarily refuse policy renewal except under specific circumstances such as fraud or non-disclosure. Portability allows policyholders to switch insurers without losing accrued benefits, and standardisation ensures uniform definitions of critical terms, reducing confusion for customers.

4. Micro Insurance Regulations

Framed to promote small-ticket insurance products targeted at low-income groups and rural populations, these regulations aim to improve financial inclusion. They define the scope, distribution methods, and benefit limits for micro-insurance products, making insurance more accessible to marginalised communities. For instance, products with low premiums and simplified claim procedures are encouraged under these rules.

5. Corporate Governance Guidelines

These guidelines ensure that insurers maintain high standards of compliance, risk management, and ethical conduct. They require a clear division of responsibilities between the board of directors and management, periodic risk assessments, and internal audits. By strengthening governance, IRDAI ensures the stability and credibility of insurance companies, which is vital for maintaining public confidence.

6. IRDAI (Expenses of Management) Regulations, 2023

This recent regulation imposes limits on the commissions paid to intermediaries and the operating expenses of insurers. The aim is to improve operational efficiency and ensure that more funds are available for claim payouts and policyholder benefits rather than administrative costs. It also promotes cost discipline in the industry, which can contribute to lower premiums for customers.

Case Study of Regulatory Action – Standardised Health Policies

In 2022, the Insurance Regulatory and Development Authority of India (IRDAI) took a significant step towards improving accessibility and transparency in the health insurance market by directing all general and health insurers to offer standardised health insurance products, such as the Arogya Sanjeevani Policy.

The objective was to ensure that every insurer in India provided a common minimum health coverage with clearly defined benefits, exclusions, and premium structures. This policy includes features like hospitalisation cover, pre- and post-hospitalisation expenses, AYUSH treatment, and room rent limits, all under uniform terms across insurers.

The introduction of such standard products benefits consumers in multiple ways:

◊ Transparency – Customers can easily understand what is covered without navigating through complex and varied policy wordings.

◊ Comparability – Since all insurers offer the same basic product, buyers can compare premiums and service quality without worrying about hidden differences in coverage.

◊ Affordability – By setting a common minimum standard, IRDAI ensured that basic health coverage is available at reasonable rates to a wider section of the population.

This action also reduced mis-selling in the market, as agents could no longer pitch drastically different basic plans under confusing terms. For example, a family looking for a starter health insurance plan could now choose Arogya Sanjeevani from different insurers—such as New India Assurance, ICICI Lombard, or Star Health—confident that the core benefits would remain the same, with variations only in pricing and service delivery.

4.2.6 Regulatory Reforms and Future Directions

1. Simplification of Products and Claims

IRDAI is actively working to make insurance products easier to understand by introducing clear and standardised policy wordings. This helps eliminate jargon and ensures that customers know exactly what is covered and excluded. Similarly, claim processes are being simplified through reduced documentation requirements, online claim submission options, and faster settlement timelines. For example, the regulator has promoted "quick claim settlement protocols" in health insurance where pre-authorisation decisions are made within hours.

2. Greater Focus on Digital Insurance Platforms

Recognising the growing role of technology in financial services, IRDAI is encouraging insurers to expand their presence on digital platforms. This includes online policy purchase, digital KYC verification, AI-based underwriting, and app-based claim

tracking. The aim is to reach customers in remote locations, reduce operational costs, and improve transparency. For instance, insurers like HDFC ERGO and ICICI Lombard now offer end-to-end policy issuance and claim settlement through mobile apps.

3. Push Towards 100% Insurance Penetration

One of IRDAI's long-term goals is to achieve universal insurance coverage in India, ensuring that every individual has access to some form of life, health, or general insurance. This aligns with national financial inclusion objectives and involves targeted outreach to rural areas, low-income groups, and informal sector workers. Government-backed schemes like PMJJBY (life cover) and PMFBY (crop insurance) are central to this mission, with IRDAI ensuring efficient rollout and monitoring.

4. Introduction of Sandbox Regulations

To foster innovation, IRDAI has introduced regulatory sandbox guidelines allowing insurers, intermediaries, and tech startups to test new products, distribution channels, or service models in a controlled environment. This framework enables market experimentation while managing risk, encouraging the development of micro-insurance products, wearable-linked health plans, and blockchain-based claims settlement systems. For example, some insurers have used sandbox approvals to pilot telematics-based motor insurance, where premiums are linked to driving behaviour.

Recap

◊ Privatisation of insurance refers to the shift from a state monopoly to a competitive market in 2000, which increased innovation and customer choice.

◊ Foreign Direct Investment (FDI) in insurance brought capital, technology, and global practices, with limits rising from 26% in 2000 to 74% in 2021.

◊ Bancassurance means a partnership between banks and insurers that improves reach, revenue, and customer convenience.

◊ The Insurance Regulatory and Development Authority of India (IRDAI) performs functions such as licensing, protecting policyholders, framing regulations, monitoring companies, encouraging innovation, and promoting financial inclusion.

◊ Major regulations cover areas such as policyholder protection, health insurance norms, micro-insurance, corporate governance guidelines, and expense management rules.

◊ The future of insurance includes digital platforms, simplified products, universal coverage, and sandbox models for testing innovation.

Objective Questions

1. Year when insurance privatisation began?
2. What is the FDI cap in insurance as of 2021?
3. First private life insurer in India?
4. Full form of IRDAI?
5. Headquarters of IRDAI?
6. Example of a standardised health policy mandated by IRDAI?
7. Year FDI limit increased to 49%?
8. Which model involves bank acting as an insurance agent?
9. Vision of IRDAI?
10. What does PMJJBY stand for?
11. Regulation promoting rural small-ticket insurance?
12. Tool introduced by IRDAI to test innovative products?

Answers

1. 2000
2. 74%
3. ICICI Prudential Life
4. Insurance Regulatory and Development Authority of India
5. Hyderabad
6. Arogya Sanjeevani
7. 2015
8. Corporate Agency Model
9. Protect interests of policyholders and ensure orderly industry growth
10. Pradhan Mantri Jeevan Jyoti Bima Yojana
11. Micro Insurance Regulations
12. Regulatory Sandbox

Self-Assessment Questions

1. Discuss the insurance regulations in India
2. Describe the post privatisation development in insurance industry in India
3. Role of FDI in Indian Insurance Sector
4. Short note on Sand box regulations by IRDAI ?
5. Essay on IRDAI Regulations
6. Briefly explain the functions of IRDAI ?

Assignments

1. Trace the historical background of the privatisation of the Indian insurance industry.
2. Discuss the changes in FDI limits in insurance and their impact.
3. Explain the concept, benefits, and models of bancassurance with examples.
4. Describe the key functions and major regulations of IRDAI.
5. Evaluate the regulatory reforms and future directions of the Indian insurance sector.
6. Prepare a comparative table of insurance sector structure before and after privatisation.
7. Analyse two recent FDI-backed insurance joint ventures and their market impact.
8. Conduct a survey of customers at a local bank to assess awareness of bancassurance products.
9. Draft a sample complaint to the Insurance Ombudsman regarding claim settlement delay.
10. Propose a new micro-insurance product suitable for rural markets and outline its regulatory compliance requirements.

Reference

1. IRDAI. (2021). *Annual Report 2020–21*. Insurance Regulatory and Development Authority of India.

2. Government of India. (2015). *Insurance Laws (Amendment) Act, 2015*. Ministry of Law and Justice.

3. Malhotra Committee. (1994). *Report on Reforms in the Insurance Sector*. Government of India.

4. Outreville, J. F. (2013). *The relationship between insurance and economic development: 85 empirical papers for a review of the literature*. Risk Management and Insurance Review, 16(1), 71-122.

5. Swiss Re Institute. (2022). *World Insurance: The recovery gains pace*. Sigma No. 4/2022.

6. Reserve Bank of India. (2020). *Report on Trend and Progress of Banking in India 2019–20*.

7. KPMG India. (2020). *Insurance industry: Challenges, reforms and realignment*.

8. PwC India. (2018). *Future of India's Insurance Sector*.

9. Ernst & Young. (2019). *Reimagining the Insurance Sector in India*.

10. Deloitte India. (2021). *Digital Transformation in Insurance*.

Suggested Reading

1. Skipper, H. D., & Kwon, W. J. (2007). *Risk management and insurance: Perspectives in a global economy*. Blackwell Publishing.

2. Rejda, G. E., & McNamara, M. J. (2017). *Principles of risk management and insurance*. Pearson.

3. Vaughan, E. J., & Vaughan, T. M. (2014). *Fundamentals of risk and insurance*. Wiley.

4. Outreville, J. F. (2013). *Theory and practice of insurance*. Springer.

5. Mishra, M. N., & Mishra, S. B. (2016). *Insurance: Principles and practice*. S. Chand Publishing.

SREENARAYANAGURU OPEN UNIVERSITY

QP CODE: ………

Reg. No   : ....

Name   : ……...........

THIRD SEMESTER BACHELOR OF COMMERCE (B.Com) EXAMINATION

MULTI-DISCIPLINARY COURSES- SGB24CM101MD
- BANKING AND INSURANCE (FYUGP - B.Com)

MODEL QUESTION PAPER- SET- A

2023-24 - Admission Onwards

Time: 2 Hours   Max Marks: 45

SECTION A

Answer any five questions in a word or sentence. Each question carries one mark

(5×1 = 5 Marks)

1. What do you mean by core banking solutions?
2. Write formula for calculating total credit creation
3. Short note on NRI account.
4. List out the classification of risk.
5. Write the full form of IRDAI.
6. List out any two bancassurance models.
7. Name one life insurance policy offered by LIC.
8. State any 2 private sector banks.

SECTION B

Answer any five questions in two or three sentences each.

Each question carries two marks.

(5×2 =10 Marks)

9. List out the 4 types of endorsement.
10. Define insurance.
11. what is FDI.
12. Explain claim settlement ratio.

13. Discuss the principle of proximate cause.

14. State any 4 features of term plan under various life insurance plans.

15. List out any 4 non-life insurance claims.

16. List out the key elements of insurance.

SECTION C

Answer any four questions. Each question carries five marks.

(4×5 = 20 Marks)

17. Short note on types of accounts in banks

18. Briefly explain the essential characteristics of a cheque.

19. Discuss the SARFAESI Act ,2002

20. Briefly explain the functions of insurance

21. Princiles of life insurance.

22. Explain the procedure for opening a bank account.

SECTION D

Answer any one questions. Each question carries 10 marks.

(1×10 =10 Marks)

23. Discuss the relationship between banker and customers

24. Explain in detail the life insurance claims settlement procedure of both maturity and death claims.

SREENARAYANAGURU OPEN UNIVERSITY

QP CODE: ………

Reg. No   : ....

Name   : …….............

THIRD SEMESTER BACHELOR OF COMMERCE (B.Com) EXAMINATION
MULTI-DISCIPLINARY COURSES- SGB24CM101MD
- BANKING AND INSURANCE (FYUGP - B.Com)
MODEL QUESTION PAPER- SET- B
2023-24 - Admission Onwards

Time: 2 Hours   Max Marks: 45

SECTION A

Answer any five questions in a word or sentence. Each question carries one mark

(5×1 = 5 Marks)

1. What do you mean by a bank?

2. What is NPA?

3. Explain KYC?

4. What is risk?

5. What is fire insurance claim?

6. What is bancassurance?

7. What is retail banking?

8. What are capital adequacy norms?

SECTION B

Answer any five questions in two or three sentences each.

Each question carries two marks.

(5×2 =10 Marks)

9. What is speculative risk?

10. Explain principle of indemnity?

11. Describe recurring deposits?

12. Explain credit control?

13. What is credit rationing?

14. What are the differences between financial and non-financial risk?

15. What is endowment plan?

16. State any two utility services offered by a commercial bank?

SECTION C

Answer any four questions. Each question carries five marks.

(4×5 = 20 Marks)

17. Explain the secondary function of a commercial bank?

18. Discuss functions of IRDAI Act?

19. Briefly explain the different types of risks?

20. Explain the function of DRT Act?

21. Describe the types of Rural Insurance Policies?

22. Write a note on recent mergers in banking?

SECTION D

Answer any one questions. Each question carries 10 marks.

(1×10 =10 Marks)

23. Discuss the various functions of commercial banks and their importance in economic development.

24. Discuss the main principles of insurance with suitable examples

സർവ്വകലാശാലാഗീതം

വിദ്യയാൽ സ്വതന്ത്രരാകണം
വിശ്വപൗരരായി മാറണം
ഗ്രഹപ്രസാദമായ് വിളങ്ങണം
ഗുരുപ്രകാശമേ നയിക്കണേ

കൂരിരുട്ടിൽ നിന്നു ഞങ്ങളെ
സൂര്യവീഥിയിൽ തെളിക്കണം
സ്നേഹദീപ്തിയായ് വിളങ്ങണം
നീതിവൈജയന്തി പാറണം

ശാസ്ത്രവ്യാപ്തിയെന്നുമേകണം
ജാതിഭേദമാകെ മാറണം
ബോധരശ്മിയിൽ തിളങ്ങുവാൻ
ജ്ഞാനകേന്ദ്രമേ ജ്വലിക്കണേ

കുരീപ്പുഴ ശ്രീകുമാർ

SREENARAYANAGURU OPEN UNIVERSITY

Regional Centres

Kozhikode
Govt. Arts and Science College
Meenchantha, Kozhikode,
Kerala, Pin: 673002
Ph: 04952920228
email: rckdirector@sgou.ac.in

Thalassery
Govt. Brennen College
Dharmadam, Thalassery,
Kannur, Pin: 670106
Ph: 04902990494
email: rctdirector@sgou.ac.in

Tripunithura
Govt. College
Tripunithura, Ernakulam,
Kerala, Pin: 682301
Ph: 04842927436
email: rcedirector@sgou.ac.in

Pattambi
Sree Neelakanta Govt. Sanskrit College
Pattambi, Palakkad,
Kerala, Pin: 679303
Ph: 04662912009
email: rcpdirector@sgou.ac.in

Banking and Insurance

COURSE CODE: SGB24CM101MD

SGOU

Sreenarayanaguru Open University

Kollam, Kerala Pin- 691601, email: info@sgou.ac.in, www.sgou.ac.in Ph: +91 474 2966841