Shyamala Gopinath: Banks' relationship with customers – evolving perspectives

Address by Ms Shyamala Gopinath, Deputy Governor of the Reserve Bank of India, at the 4th M R Pai Memorial Award Function, organised by the All India Depositors' Association, Mumbai, 8 April 2008.

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I feel it a privilege to be associated with today's function as a tribute to the late Mr. M.R.Pai, the doyen of consumer activism in India. He successfully championed the cause of consumers, particularly bank depositors, during a different economic setting when the institutional dynamics were different, particularly for the public sector, and customer as a generic entity had not acquired the high pedestal in public discourses and management meetings. Times have changed. But as a Sanskrit saying goes…*kadachit anidrishyam jagat*. The world has always been the same and consumer issues in the new economic order remain as pressing as ever, even more so. Even in developed countries issues relating to customer protection and financial inclusion are finding increasing focus. There is as much need for a Mr. Pai today, as it was then in putting across consumer issues to the fore in an effective manner.

In my address today, I intend to share my perspective on the evolving nature of banks' relationship with its individual customers and the new challenges in this regard. The role of banks in intermediation of financial needs of different classes of customers has undergone significant changes. For the sake of convenience, banks' various roles vis-à-vis their customers can be broadly categorized as (i) acceptors of deposits (ii) credit providers (ii) providers of payments and remittances services (iv) provider of foreign exchange services (v) facilitators in circulation of currency notes/coins; and (vi) providers of financial instruments.

One of the defining features of the process of reforms initiated in the early nineties was the deregulation of interest rates. On the deposit side, interest rates on all deposits, except savings accounts, have been de-regulated. Similarly, on the bank lending, rates to be charged by the banks on most of the credit facilities have been deregulated except a small component for lending related to certain segments. Simultaneously, in 1993, as per the new licensing policy, fresh licenses were issued to a few private sector banks with the objective of enhancing the level of competition in the sector. One of the expected outcomes of this policy was expanding the reach of banking services, both in qualitative and quantitative terms. Technology emerged as the backbone of banking operations, revolutionizing service delivery through new platforms and channels. But it became evident gradually, these developments created more challenges for the customer in terms of service quality, non-human interface, unsolicited marketing of products, ever-increasing fine-prints on documents etc. all of which got compounded on account of basic financial unawareness on part of the ordinary customer.

Self regulation by the banking industry would have been the ideal redressal for the emerging challenges. But due to heterogeneous and complex nature of the problems coming to light, some regulatory initiative had become necessary. In the mid term review of the Monetary and Credit Policy 2003-2004, it was decided to review the level of public service provided by the Reserve Bank and banks, and to evolve appropriate incentives to facilitate change on an ongoing basis. Accordingly, the Committee on Procedures and Performance Audit on Public Services was set up. The Committee focused on the inadequacy in banking services available to common person and looked into the need to (i) benchmark the current level of service, (ii) review the progress periodically, (iii) enhance the timeliness and quality, (iv) rationalize the processes taking into account technological developments, and (v) suggest appropriate incentives to facilitate change on an ongoing basis. Following the Committee's recommendations, various important customer service regulations were issued, notable among them being the guidelines on facilitating the payment to survivor/nominee of a deceased depositor, simplifying the KYC requirements, collection of cheques and facilitating operations in bank accounts.

Simultaneously, a series of measures was taken to improve the institutional mechanism within as well as outside the banks to improve the quality of customer service.

- All the banks were advised to constitute a Customer Service Committee of the Board with a view to strengthening the corporate governance structure in the banking system and also to bring about ongoing improvements in the quality of customer service provided by the banks.
- In order to encourage a formal channel of communication between the customers and the bank at the branch level, banks were advised to take necessary steps for strengthening the branch level customer service committees with greater involvement of customers. Further as senior citizens usually form an important constituency in banks, banks were advised to preferably include a senior citizen in the branch level committees.
- The Banking Ombudsman Scheme was revised to enlarge the scope of the Scheme to include customer complaints on certain new areas, such as, credit card complaints, deficiencies in providing the promised services even by banks' sales agents, levying service charges without prior notice to the customer and non-adherence to the fair practices code as adopted by individual banks. The Scheme therefore provides a forum to bank customers to seek redressal of their most common complaints against banks, including those relating to credit cards, service charges, promises given by the sales agents of banks, but not kept by banks, as also, delays in delivery of bank services. The bank customers would be able to complain about non-payment or any inordinate delay in payments or collection of cheques towards bills or remittances by banks, as also non-acceptance of small denomination notes and coins or charging of commission for acceptance of small denomination notes and coins by banks. The present Scheme also allows appeals from both banks and complainants against the decisions of Banking Ombudsmen.
- Recognising an institutional gap in measuring the performance of the banks against codes and standards based on established best practices, Reserve Bank of India has taken the initiative in setting up the Banking Codes and Standards Board of India (BCSBI). It is an autonomous and independent body, adopting the stance of a self-regulatory organisation in the larger interest of improving the quality of customer services by the Indian banking system. Banks register themselves with the Board as its members and provide services as per the agreed standards and codes. The Board in turn, monitors and assesses the compliance with codes and standards which the banks have agreed to. The registration of banks with the BCSBI, as members, enables the Reserve Bank of India to derive greater supervisory comfort, so also the customers of the member banks. This would also enable the BCSBI to accommodate the bank-specific differences in the customer service related benchmarks set by the banks for themselves. As on date, around 71 banks have joined the BCSBI as members.

I. Deposit accounts

With regard to account holders, it would be useful, to recollect some of the important incremental measures taken by RBI, which over a period have made significant impact:

- Banks are required to inform customers upfront about the requirement of minimum balances and the charges if such balances are not maintained. They are also required to inform customers one month in advance any changes in such minimum balances and charges.

- It has been clarified to banks that NRO accounts can be held jointly with residents
- In case of collection of cheques, banks are required to formulate and disclose their policy for affording immediate credit, time frame for collection and interest payment for delayed collection, taking care to ensure that the interests of the small depositors are fully protected. The policy should clearly lay down the liability of the banks by way of interest payments due to delays for non-compliance with the standards set by the banks themselves. Compensation by way of interest payment, where necessary, should be made without any claim from the customer.
- Banks are required to provide both the drop box facility and the facility for acknowledgement of the cheques at the regular collection counters and no branch should refuse to give an acknowledgement if the customer tenders the cheques at the counters.
- Banks have been advised to ensure that brief, intelligible particulars are invariably entered in passbooks/statements of account and they adhere to the prescribed monthly periodicity while sending statement of accounts.
- It has been clarified to banks that payment to the survivor/nominee of a deceased depositor where there is a valid nomination or where the account has been opened with a survivorship clause is a valid discharge of liability provided inter alia it has been made clear to the survivor(s)/nominee that he would be receiving the payment from the bank as a trustee of the legal heirs of the deceased depositor, i.e., such payment to him shall not affect the right or claim which any person may have against the survivor(s)/nominee to whom the payment is made. In such cases insistence on production of legal representation is unwarranted and would, invite serious supervisory disapproval. In such case, therefore, while making payment to the survivor(s)/nominee of the deceased depositor, the banks have to desist from insisting on production of succession certificate, letter of administration or probate, etc., or obtain any bond of indemnity or surety from the survivor(s)/nominee, irrespective of the amount standing to the credit of the deceased account holder.
- In case where the deceased depositor had not made any nomination or for the accounts other than those styled as “either or survivor” (such as single or jointly operated accounts), banks have been told to adopt a simplified procedure for repayment to legal heir(s) of the depositor keeping in view the imperative need to avoid inconvenience and undue hardship to the common person. In this context, banks may, keeping in view their risk management systems, fix a minimum threshold limit, for the balance in the account of the deceased depositors, up to which claims in respect of the deceased depositors could be settled without insisting on production of any documentation other than a letter of indemnity.
- In the case of term deposits, banks are advised to incorporate a clause in the account opening form itself to the effect that in the event of the death of the depositor, premature termination of term deposits would be allowed. The conditions subject to which such premature withdrawal would be permitted may also be specified in the account opening form. Such premature withdrawal would not attract any penal charge.
- In order to avoid hardship to the survivor(s)/nominee of a deposit account, banks are advised to obtain appropriate agreement/authorization from the survivor(s)/nominee with regard to the treatment of pipeline flows in the name of the deceased account holder.

- Banks are advised to settle the claims in respect of deceased depositors and release payments to survivor(s)/nominee(s) within a period not exceeding 15 days from the date of receipt of the claim subject to the production of proof of death of the depositor and suitable identification of the claim(s), to the bank's satisfaction.
- Information should not be gathered in the name of KYC with the intention of using it for cross-selling of services. The banks should obtain the information required for opening an account independent of any other information that they may seek for cross-selling purposes with the consent of the customer. The forms containing this information must not be a part of the account opening form.
- The KYC procedure for opening accounts for those persons who intend to keep balances not exceeding rupees fifty thousand (Rs. 50,000/-) in all their accounts taken together and the total credit in all the accounts taken together is not expected to exceed rupees one lakh (Rs. 1,00,000/-) in a year has been simplified to enable those belonging to low income groups without documents of identity and proof of residence to open banks accounts. In such cases banks can take introduction from an account holder on whom full KYC procedure has been completed and has had satisfactory transactions with the bank for at least six months. Photograph of the customer who proposes to open the account and his address need to be certified by the introducer. Recently, clarification had also been issued to facilitate account opening by close relatives, e.g. wife, son, daughter and parents etc. who live with their husband, father/mother and son, as the case may be, who may not have the utility bills required for address verification in their name.

II. Bank lending

On the lending side, guidelines were issued on Fair Practices Code for Lenders, including comprehensive details in loan applications and conveying reasons for rejection of loans.

In terms of the guidelines banks/FIs are required to ensure that loan application forms in respect of priority sector advances up to Rs.2.00 lakhs contains comprehensive information about the fees/charges and any other matter which affects the interest of the borrower. The Guidelines were further revised to ensure that all loan applications in respect of all categories of loans irrespective of the amount of loan sought by the borrower contains comprehensive information about fees/charges etc.

Banks/FIs are also required to convey in writing, the main reason/reasons which have led to rejection of the loan applications in case of all categories of loans irrespective of any threshold limits, including credit card applications.

RBI has issued comprehensive Credit Card Guidelines relating to credit card operations of banks/NBFCs in November 2005. These guidelines have been issued aimed at encouraging growth of credit cards in a safe, secure and efficient manner as well as to ensure that the rules, regulations, standards and practices of the card issuing banks are in alignment with the best customer practices. These guidelines address issues relating to billing, use of Direct Selling Agents (DSAs) and other agents, protection of customer rights, customer confidentiality, fair practices in debt collection, redressal of grievances, etc. Master Circular on the issue has since been issued.

Measures for ensuring reasonableness of service charges

Reserve Bank has made it obligatory for banks to display and update, in their offices/branches as also on their websites, the details of various service charges in a prescribed format. The banks are also required to display the service charges and fees on the homepage of their website at a prominent place under the title of “Service Charges and Fees” so as to facilitate easy access to the bank customers. Reserve Bank has also placed a web-link to these web pages of banks in its website to facilitate comparison of service charges and thereby enabling the customer to take an informed decision. A Working Group was also set up to look into the issue of reasonableness of bank charges, which submitted its Report in August 2006. The Working Group indicated broad principles of reasonableness that banks should adopt in fixing and notifying the service charges for providing basic services to individuals. Guidelines have been issued to the banks based on the recommendations of the Working Group and steps taken by the banks in this regard are being examined.

Instructions to guard against incidence of excessive interest rates & charges

Based on feedback that excessive interest and charges were being levied on certain loans and advances, banks were advised to lay out appropriate internal principles and procedures so that usurious interest, including processing and other charges, are not levied by them on small value loans, particularly personal loans and such other loans of similar nature. Banks are also required to fix appropriate ceiling on the interest, including processing and other charges that could be levied on such loans, which may be suitably publicised.

III. Foreign exchange

Over the last two decades, there has been a paradigm shift in the foreign exchange regime in India. The approach of conservation and preservation of foreign exchange has been replaced with a liberal framework aimed at facilitation of external trade and payments and orderly development of foreign exchange markets. In the process, the RBI has moved beyond the role of a regulator to that of a facilitator of foreign exchange transactions.

Several measures have been taken to expand the delivery channels of foreign exchange services for reducing transaction costs and to undertake external transactions in a hassle free manner. These measures include – licensing of a new category of entities as AD category-II to handle non-trade related current account transactions and licensing of select Urban Cooperative Banks and RRBs as well to operate as AD Cat-II. In addition, the norms for the Full Fledged Money Changers have been reviewed and the ADs have been permitted to enter into franchisee arrangements for provision of money changing facilities. Further, measures have been taken to simplify procedures in respect of cross-border flows through Exchange Houses (Rupee Drawing Arrangements).

Resident individuals have been permitted to make remittances overseas up to USD 200,000 per financial year for undertaking any of the permitted current or capital account transactions or a combination of both. Only requirements are a designated bank account, PAN number and a simple declaration.

The critical issue at this juncture is for the banks to ensure efficient customer service by equipping the frontline staff with up-dated instructions and bring about an attitudinal change in their approach towards foreign exchange business. It is disconcerting to note that the incognito visits to various banks have revealed that the services delivered at various banks are deficient and insistence on unwarranted or complex documents continues for individuals. Another issue is the reluctance of the banks to extend service to walk-in customers for handling their small value transactions. We have been sensitizing banks to these issues.

The steps taken by the RBI in liberalizing the forex regulations, delegating authority to the ADs and simplify the procedures is basically designed to extend the forex services to the residents and non-residents in a simple and hassle free manner with minimal documentation.

IV. Payment systems

The traditional role of banks as providers of various payment and settlement services to customers is getting redefined. Until recently, requirements of customers, be it corporate or retail, were determined and extended by banks based on their perception and understanding of customer necessities. This to a large extent was also dictated by the banks' ability to offer such products. The scenario is fast changing and changing for the better. Now, the banks are encouraged to innovate and tailor products to suit various segments of customers, apart from being more sensitive to their demands. Competition between banks for market share and the emergence of other service providers are other reasons for this push.

It is also necessary to put into context the magnitude of challenges that are ahead of us. The paper clearing volumes we handle is the sixth largest in the world with a volume of 1.44 billion cheques cleared during the year 2007. The RBI has launched the Cheque Truncation System in the National Capital Region of New Delhi on February 1, 2008 with the participation of 10 banks in the pilot run. Once fully operational, the system will be the largest in the world and leapfrog the country into migrating the paper based instruments to the electronic mode. The electronic suite of products is continuously expanding in terms of coverage of branches, volume of transactions and number of users availing the facility. The Reserve Bank has intervened and mandated (a) reasonability in pricing of transactions effected through ATMs, (b) compulsory use of electronic mode of initiating transactions above a specified cut-off limit, (c) strengthening the payment systems infrastructure, etc.

Whilst the clearing cycle operating across the country on a T+1 basis for cheques payable locally, favourably compares with the best in the world, it is necessary to look into the entire cycle from the time a customer deposits a cheque at a branch till the point of realisation of credit in his account. There is scope for continuous improvement in overall cycle. Going by the number of complaints, it is felt that customer-service in this area is not customer-centric. Albeit the fact that electronic payment products are improving their share in the overall retail portfolio, the volume of paper instruments would continue to be significant in the near future as well.

The share of electronic payment products like RTGS, NEFT and ECS is rising by the day and the number of branches which are offering this facility is also increasing. Notwithstanding this, the share of public sector banks in the electronic product usage is very less. It is necessary to make available these products across all bank branches. While the build-up should continue, banks need to also concentrate on reaching geographical areas and segments of populace that have not been embraced by this expansion. It is difficult to achieve financial inclusion without involving rural-India in the payment system out-reach and those banks who do so first, will reap the benefits of increase in volumes and increase in market-share, leading to concomitant increase in revenues, and of-course increase in other businesses as well. And as we all know, the electronic medium is location independent, can leave a better audit-trail and will surely improve customer involvement and service expectations. It is our vision that electronic products reach 50% of volume and 95% of value by the end of March 2009.

Banks need to adopt a "**STOCK**" approach while conceiving and bringing out products. Products that are "**S**ecure and scalable", **T**ransparent in terms and conditions of usage, **O**perationally resilient and efficient, **C**ost-effective and reasonably priced, and **K**nowledgeable to staff and customers. The customers have an equal if not higher responsibility to ensure banks adopt this approach while innovating products for them.

V. Currency management

As per the provisions of Reserve Bank of India Act 1934, RBI is statutorily required to undertake certain activities in the area of currency management. In view of the fact that RBI has its Offices only at state capitals or at large centres, the services of commercial banks are used to store banknotes on behalf of the Reserve Bank in the currency chests held at designated branches. These bank branches may operate on the balances of the currency chests as per their requirements with correct and timely reporting being their responsibility. A decision has also been taken to provide the currency chest facility to private sector and foreign banks with 99 currency chests being held by these banks. Further, now the Urban Cooperative Bank and RRBs are also allowed to hold the facility. These steps would improve the availability of banknotes and coins across the country.

The channel of currency chests is used not only for distributing banknotes and coins but also for collecting back the soiled notes. While the banks are under instructions to sort the banknotes before depositing them into the currency chest, it was observed that meaningful sorting was not done as evident from a number of reissuable notes being retrieved at the level of the Reserve Bank regional offices. To overcome this, all the banks were advised to install Note Sorting Machines at their currency chests, a task that has been completed. To carry the Clean Note Policy further, banks have been instructed to process all of their daily receipts over Note Sorting Machines and keep a daily record thereof. It may be mentioned here that banks are already under instructions by way of a Directive under Section 35A of the Banking Regulation Act 1949 on non-stapling of banknotes, issue only good quality of banknotes and not to write anything on the watermark portion. This would be evident from the general improvement in the quality of notes in circulation.

Further, to extend the reach of channels for distribution of coins, the services of Post Offices, Urban Cooperative Banks and Regional Rural Banks are being used in view of their wide reach to the members of general public.

VI. Financial education and inclusion

Lastly, let me come to the very significant aspect of financial inclusion which has been pursued with a missionary purpose by the Reserve Bank of India during the last four years. Given the socio-demographic complexities in India, the endeavour has been towards a multi-institutional and multi-instrumental approach to comprehensively address the issue of financial inclusion in all its entirety, going beyond mere availability of credit. By financial inclusion we mean the provision of affordable financial services, viz., access to payments and remittance facilities, savings, loans and insurance services by the formal financial system to those who tend to be excluded.

Globally the issue of financial inclusion has now assumed significance not merely in developing countries but also in developed countries. RBI started a focused drive in this regard in 2004.

In the Annual Policy of the Reserve Bank for 2004-05, the Governor, Dr. Reddy observed and I quote -

"There has been expansion, greater competition and diversification of ownership of banks leading to both enhanced efficiency and systemic resilience in the banking sector. However, there are legitimate concerns in regard to the banking practices that tend to exclude rather than attract vast sections of population, in particular pensioners, self-employed and those employed in unorganised sector. While commercial considerations are no doubt important, the banks have been bestowed with several privileges, especially of seeking public deposits on a highly leveraged basis, and consequently they should be obliged to provide banking services to all segments of the population, on equitable basis."

Pursuant to this, the Reserve Bank has undertaken a number of measures with the objective of attracting the financially excluded population into the structured financial system going beyond credit to a whole range of financial services.

- In November 2005, banks were advised to make available a basic banking "no-frills" account with low or nil minimum balances as well as charges to expand the outreach of such accounts to vast sections of the population. Banks are required to make available all printed material used by retail customers in the concerned regional language.

- In order to ensure that persons belonging to low income group, both in urban and rural areas do not encounter difficulties in opening bank accounts, the know your customer (KYC) procedures for opening accounts has been simplified for those persons with balances not exceeding Rs 50000/- (about GBP 600) and credits in the accounts not exceeding Rs.100000/- (about GBP 1200) in a year. The simplified procedure allows introduction by a customer on whom full KYC drill has been followed.
- Banks have been asked to consider introduction of a General purpose Credit Card (GCC) facility up to Rs. 25000/- at their rural and semi urban braches. The credit facility is in the nature of revolving credit entitling the holder to withdraw upto the limit sanctioned. Based on assessment of household cash flows, the limits are sanctioned without insistence on security or purpose. Interest rate on the facility is completely deregulated.
- In January 2006, banks were permitted to utilise the services of non-governmental organisations (NGOs/SHGs), micro-finance institutions and other civil society organisations as intermediaries in providing financial and banking services through the use of business facilitator and business correspondent (BC) models. The BC model allows banks to do “cash in – cash out” transactions at the location of the BC and allows branchless banking.
- Other measures include setting up pilots for credit counselling and financial education. A multilingual website in 13 Indian languages on all matters concerning banking and the common person has been launched by the Reserve Bank on 18 June 2007.

The key driver in the success of these initiatives would undoubtedly be technology. Technology today provides a lever which can enable multilevel leapfrogging in pursuit of financial inclusion. Andhra Pradesh has started a project that aims to improve the mechanism for paying pensions and unemployment benefits to around half a million people in villages in the Karimnagar and Warangal regions of the state. It is a tiny start – so far some 40,000 cards have been issued – but the potential is clear. The initiative is to have a bank tie up and extend this model to other places and states.

The role of financial literacy in this regard can't be over-emphasised. As noted by the *Economist* in a recent issue, a global crusade is under way to teach personal finance to the masses. Governments from USA to Britain to Russia are declaring their commitment to financial education. This month the World Savings Banks Institute, which represents retail and savings banks from 92 countries, will hold a summit in Brussels about financial education in the light of the sub-prime crisis. There is also an exhortation to the policy makers to simplify the choices available to people in financial matters, quoting the Swedish savings plan for old age, which offers a choice of funds to invest in but also includes a low-cost default option, chosen by 90% of the people.

Financial education has an ever more critical role to play in the changed financial landscape of India which, while on one hand has presented with newer opportunities for future collective growth, on the other, it has also heightened fears of uncertainty in certain quarters mainly because of increasing multi-faceted choices and options in the management of personal finances and exposure to a gamut of risks. Financial education could ideally supplement the financial inclusion initiatives for long term efficacy. RBI has recently put out a concept paper on setting up Financial Literacy and Counseling Centres with the objective of providing free financial literacy/education and credit counselling. The specific objectives of the proposed FLCCs would be:

- To educate the people in rural and urban areas with regard to various financial products and services available from the formal financial sector;
- To make the people aware of the advantages of being connected with the formal financial sector;
- To provide face-to-face financial counselling services, including education on responsible borrowing and offering debt counselling to individuals who are indebted to formal and/or informal financial sectors;
- To formulate debt restructuring plans for borrowers in distress and recommend the same to formal financial institutions, including cooperatives, for consideration;
- To take up any such activity that promotes financial literacy, awareness of the banking products, financial planning and amelioration of debt-related distress of an individual; and
- To take up any other activity that facilitates the above.

Once feedback is received, the initiative could be carried forward in consultation with all stakeholders.

Conclusion

I would like to conclude by quoting from one of Governor Dr. Reddy's speech:

"Banking is a trust-based relationship and the banking licence from the regulator provides an assurance of trust to the public at large. To the banks, the banking licence provides the privilege of accepting uncollateralised deposits from the public. However, the acts of stealth banking, negative option marketing, misleading advertisements, information gathering from customers for cross selling of products and services, and tie-up arrangements are inconsistent with the concept of a trust-based relationship. The lack of transparency, coupled with the difficulty of consumers in identifying key information from the large volume of material and communication in fine print, leads to an information asymmetry, which renders the banker-customer relationship one of unequals."

The broad approach of RBI is to empower the common person where banking services are concerned and strengthen customer-service delivery in banks by adopting a consultative process with banks, through the IBA. Specifically, the focus is on:

a) Sensitising banks to customer service and encouraging the involvement of the Boards of the banks, especially to strengthen the banks own grievance redressal machinery.

b) Insisting on transparency in all the dealings with the customers, and ensuring reasonableness in pricing.

c) Promoting adherence to self imposed codes by banks on commitments to bank customers and monitoring compliance by an independent agency, viz. BCSBI.

d) Strengthening the mechanism for dispute resolution.

e) Using regulation/prescription only when essential, while encouraging the industry association (IBA) to take initiatives.

f) Rationalising RBI's own systems and procedures.

It is a constant endeavour to meet the above objectives and collectively, I am sure we can build a customer-oriented banking culture and, through the initiatives on financial inclusion, achieve democratization of the financial sector.