**Asian Journal of Research in Business Economics and Management**
ISSN: 2249-7307 Vol. 11, Issue 12, December 2021 SJIF 2021 = 8.075
A peer reviewed journal

# REVIEW OF BANKING SYSTEM IN INDIA

**Vipin Jain***

*Professor,
Department of Finance & Marketing,
Faculty of Commerce, Management & Law,
Teerthanker Mahaveer Institute of Management and Technology,
Teerthanker Mahaveer University, Moradabad, Uttar Pradesh, INDIA
Email Id-vipin555@rediffmail.com

**DOI: 10.5958/2249-7307.2021.00072.4**

**ABSTRACT**

*Banking is not a new idea; it has been steadily evolving over many decades. A bank is a financial institution that provides banking and other financial services to its clients in general. The terms "banks" and "banking" are divided into various categories in India. Each group has its own set of advantages and disadvantages. With the advancement of technology, a revolution in the area of banking has occurred. As we all know, India's banking idea has been developing since before independence. A bank named The General Bank of India was founded in 1786, and it was believed to be the first bank ever established in India. The classifications established with regard to banking in India are scheduled and Non-Scheduled. Non-Scheduled banks include development, local area banks, and others, while Scheduled banks include public sector, private sector, and other banks. The following two acts were established by Indian law to protect the interests of consumers. The Banking Regulation Act and the Federal Reserve Bank of India Act. In addition, the RBI established the Banking Ombudsman system to protect customers. This study article enlightens us on the Indian banking idea. It also focuses on the different kinds of banks and the goal of consumer protection in the banking industry. Finally, it is necessary to comprehend the laws and regulations pertaining to consumer protection.*

**KEYWORDS:** *Banking, Customers, RBI Act 1934, Banking Regulation Act 1949, Banking Ombudsman*

## 1. INTRODUCTION

The idea of banking has been developing in some form or another since the dawn of human civilization. The current banking system provides credit and financial services to meet the needs of our Indian economy. Multiple levels are included in such a banking system in order to meet the requirements of different clients and borrowers. It contributes significantly to the economic growth of our nation. Furthermore, it varies from place to place depending on their economic circumstances and economic structure. Essentially, banks are categorized based on the volume and scope of their activities. They will not be mistreated or mislead in their enterprises as a result of this categorization[1].

The banking system plays an important role in promoting economic growth not only by channeling savings into investments but also by improving al locative efficiency of resources. The recent empirical evidence, in fact, suggests that banking system contributes to economic growth more by improving the al locative efficiency of resources than by channeling of resources from savers to investors. An efficient banking system is now regarded as a necessary pre-condition for growth.

The banking system of India consists of the central bank (Reserve Bank of India - RBI), commercial banks, cooperative banks and development banks (development finance institutions). These institutions, which provide a meeting ground for the savers and the investors, form the core of India's financial sector. Through mobilization of resources and their better allocation, banks play an important role in the development process of underdeveloped countries.

Banking development in India has been, by and large, a state-induced activity. The Reserve Bank of India was nationalized in 1949 followed by the nationalization of Imperial Bank of India (now the State Bank of India - SBI) in 1955. In 1969, 14 major commercial banks were nationalized and the exercise was repeated when 6 more commercial banks were nationalized in 1980. Thus, prior to economic reforms initiated in early 1990s, banking business in India was a near-monopoly of the Government of India[2].

The underlying philosophy of this approach was to encourage growth, via availability of adequate credit at reasonable/concessional rates of interest, in areas where commercial considerations did not allow for disbursal of credit. Along with the rest of the economy and perhaps even more than the rest, financial markets in India have witnessed a fundamental transformation in the years since liberalization. The going has not been smooth all along but the overall effects have been largely positive.

Nationalization of commercial banks was a mixed blessing. After nationalization there was a shift of emphasis from industry to agriculture. The country witnessed rapid expansion in bank branches, even in rural areas. However, bank nationalization created its own problems like excessive bureaucratization, red-tapism and disruptive tactics of trade unions of bank employees. It was in this backdrop that wide-ranging banking sector reforms were introduced as an integral part of the economic reforms program me started in early 1990s and which is still under way.

The Indian banking sector has witnessed wide ranging changes under the influence of the financial sector reforms initiated during the early 1990s[3]. The approach to such reforms in India has been one of gradual and non-disruptive progress through a consultative process. The emphasis has been on deregulation and opening up the banking sector to market forces. The Reserve Bank has been consistently working towards the establishment of an enabling regulatory framework with prompt and effective supervision as well as the development of technological and institutional infrastructure[4].Persistent efforts have been made towards adoption of international benchmarks as appropriate to Indian conditions. While certain changes in the legal infrastructure are yet to be effected, the developments so far have brought the Indian financial system closer to global standards.

Meanwhile, when it comes to the banking industry, the idea of consumer protection is critical. Within the Indian banking industry, the need for and significance of such a notion is quickly growing. Simply put, consumer protection is the process of safeguarding the general public and purchasers of goods and services against unfair business practices. The banks' responsibility includes not only making adequate disclosures about all elements of their functioning and operations, but also teaching consumers about the goods available, operating methods, and, ultimately, the dangers involved. This research paper discusses different topics such as banking, kinds of banking, and finally the importance of consumer protection in the banking industry in India[5].

## 2. REVIEW OF LITERATURE

1. According to Abhijit V Banerjee and Shawn Cole's India Policy Forum, 83 percent of India's banking operations are controlled by state or nationalized banks. Furthermore, the availability of bank branches in rural regions has been harmed as a consequence of nationalization, according to the report.
2. Principles of Banking Law by Ross Cranston and Emilios Avgoulea - states that banks are an essential component of the financial system, and that they are a part of the financial system that fulfills economic tasks such as saving mobilization and managing liquidity risks.
3. Consumer Protection in Indian Banking with Special Reference to Branchless Banking by Vilakshan – discusses how customers have brought the fast growing consumer protection problems under the scrutiny of legal forums.

## 3. DISCUSSION

In India, banking is the foundation for the country's economic growth. With the development of technology and the consideration of individual needs, major changes in the banking sector and management have occurred throughout the years. Indian banking may be divided into three stages based on its history.

### Period Prior to Independence

In 1770, the Bank of Hindustan, which was considered India's main bank, was founded. During this time, over 600 banks were established, but only a handful lasted. Only a few banks were founded in India during this time, including the General Bank of India and the Oudh Commercial Bank. Three presidential banks were created during the British period: the Bank of Bengal, the Bank of Madras, and the Bank of Bombay. These presidential banks were amalgamated into the Imperial Bank of India, which is now the largest bank in India. This bank was renamed State Bank of India after nationalization, and it is currently regarded India's largest public sector bank[6].

### Period Following Independence

Because residents in rural areas still relied on money lenders for financial assistance, the government was worried about allowing all of the major banks to operate independently. They intended to nationalize banks under the Banking Regulation Act to solve the issue. The government chose to nationalize banks under the Banking Regulation Act of 1949 in order to solve this issue. 14 banks were nationalized in addition to the Reserve Bank of India. Allahabad Bank, Bank of India, Bank of Baroda, Bank of Maharashtra, and the Central Bank of India were among them. In 1980, six banks were nationalized once again. Apart from these banks, SBI has seven subsidiaries, five of which merged with the company in 2017. This period saw significant changes and advancements in the banking industry.

### Period of Liberalization

The present stage of the banking sector's growth is critical. The government established a commission to oversee the numerous changes in the banking sector in order to ensure that all nationalized banks achieve stability and profit. The creation of private sector banks was a significant development during this time period. The RBI granted these banks permission to establish themselves in India. HDFC bank, ICICI bank, and Axis bank are just a few among them. Aside from that, a few additional changes were made, such as enabling all international banks to form joint ventures with Indian banks, allowing these banks to have branches in

India, and ultimately bringing the banking system online. As a result of this banking history, we can see that progress in this area has been achieved in accordance with the needs of the people. The provisions of the Banking Companies Legislation, 1969 relating to the payment of compensation to banks following nationalization had not been followed in Rustom Cavasjee Cooper v. UOI (Nationalization case), and therefore the act was likely to be thrown down. This lawsuit ushered in a sea shift in the banking industry's regulation[7].

**Banks In India Are Divided Into Four Categories.**

When it comes to banking in India, there are two types of banks. The Scheduled banks are one, while the Non–scheduled banks are the other. Scheduled banks are those that are included in the second schedule of the RBI Act. Nationalized banks, the State Bank of India and its seven subsidiary banks, international banks, and regional rural banks are only a handful of the banks included in the schedule. These banks are eligible for RBI loans and are classified as scheduled banks if their paid-up capital and bank collected funds do not exceed Rs. 5 lakh. Non-scheduled banks are defined as those having a reserve capital of less than 5 lakhs and those that are not included on the schedule.

**Banks that are scheduled**

**i. Co-Operative Banks**

Co-operative banks are those that are registered under the Cooperative Societies Act of 1912 and run by elected members of the management committee. These banks may be found in both rural and urban settings. This bank's primary goal is to offer low-interest loans. Furthermore, with these types of institutions, the agricultural sector is offered a fast loan. It was ruled in Pandurang Gandpati Choogle Vs. Vishwasrao Patil Murgud Sahakari Bank Limited that cooperative banks engaged in banking operations fall under the definition of a "Banking Company" as specified under Section 5(c) read with Section 56(a) of the Banking Regulation Act, 1949[8].

**ii. Regional Rural Banks**

Basic financial services are given to the agricultural industry and rural communities in this kind of bank. Prathama bank, a rural bank in India, was founded in 1975. It was thought to be India's first RRB bank. These banks are typically held by 15% of the state government, 50% of the federal government, and 35% of the sponsoring bank, such as Syndicate Bank. These banks were established under the Regional Rural Banks Act of 1976 with the goal of removing money lenders from the market.

**iii. Commercial Banks**

Under the Banking Regulation Act of 1949, they are profit-making banks that are regulated and governed. These banks provide loans to both the public and the government, and serve all segments from rural to urban. There are four different kinds of banks.

- Public Sector Banks — Also known as nationalized banks, these are banks that are owned by the government. The government or the central bank, the RBI, owns the vast majority of the shares. The State Bank of India (SBI) is India's biggest public sector bank. Some of the banks in this category are Allahabad Bank, SBI, Andhra Bank, and Indian Bank.
- Private Sector Banks - Private owners own the bulk of the shares in these institutions. The Reserve Bank of India regulates these institutions. Private sector banks in India include Yes Bank, Axis Bank, HDFC Bank, and ICICI Bank.

- Foreign Banks - This category includes banks with branches in other nations. These banks are governed by both their home nation and the country where they have set up branches. They are expected to obey both country's laws and regulations. There are about 40 international banks in India, including HSBC and CITI[8].

### iv. Bank of Payments

This financial idea has just recently been introduced. This bank allows customers to deposit up to Rs 1 lakh. This bank also offers ATM and debit card banking services. Payments banks in India include Jio and Airtel, to name a few.

### v. The Bank of England

This bank was founded with the goal of regulating all other banking organizations in the country. The Reserve Bank of India (RBI) is the country's central bank. This bank was established for the purpose of issuing currencies, regulating the financial system, and implementing monetary policies.

## The Importance of Consumer Protection in the Banking Industry

RBI must create effective authority over all banks in our nation in order to ensure a transparent financial system in our country. As long as all banks collaborate and coordinate with RBI via banking ombudsman and consumer protection divisions, a transparent system may be achieved.

When it comes to consumer protection, one of the RBI's responsibilities is to build effective customer trust by ensuring the banking system's safety. Consumers are individuals who use the products and services that manufacturers create. In India, a consumer protection legislation was enacted to safeguard consumers from fraud and unfair business practices[3].

After a massive change in the consumer protection sector, this legislation was enacted in 1986. Banking is one of the services listed in the scope of this legislation. It is widely known that the banking industry has undergone many changes up to this point. As technology advances, the bank's operating system evolves as well. This legislation also covers failure to provide appropriate services or any flaws in financial services. The Consumer Protection Act of 1986 essentially safeguards the rights of consumers, including the right to consumer education, the right to be heard, and the freedom to choose, to name a few[9].

## Banks' Function

When it comes to consumers, banks must be transparent about their roles and educate them on the operating methods, products, and dangers involved. Banking penalties, fees, and service costs must all be clear. It is the banker's responsibility to raise knowledge about the banking ombudsman in rural and semi-urban regions, as well as to oversee the execution of the customer rights charter. Only in this way can a safe atmosphere for consumers be created. RBI created the Consumer Education and Protection Department in India to handle consumer complaints[3].

Consumers who have been treated unfairly are dealt with by this department. The implementation of a banking ombudsman system is one of the primary goals of the Consumer Protection Act. This plan is based on 27 distinct banking-related reasons. The phrase "banking ombudsman" refers to a person designated by the RBI to resolve complaints about the bank's services that aren't up to par. The process of submitting a complaint is straightforward. It may be sent or written on a simple piece of paper.

## Under The Consumer Protection Act, How Should Banking Issues Be Handled?

When a client and a bank have a disagreement, the Consumer Protection Act kicks in. If the customer's disputed issue is worth less than $2 million, he or she may file a complaint with the district forum. The customer may contact the State Commission if the value is between 2 and 10 million rupees. The client may contact the national commission if the value surpasses ten million dollars. Consumers may even take their case to the Supreme Court. The RBI also selects a quasi-judicial entity known as the banking ombudsman to handle complaints about the bank's services. A complaint must be filed with the banking ombudsman program within one year of the cause of action[2].

The National Commission ruled in the case of Unit Trust of India v Ms. Kavita Gupta that customers often try to benefit from the situation by presenting hypothetical scenarios in which there was no deficit in service and they might have gained from a market increase. Surendra Kumar Bara established an account with UCO Bank under the Laghu Bachat Yojana program. The bank agent collects the deposits at regular intervals and records his entry in the passbook provided by the bank. The money had been stolen by the agency, it was discovered. The Orissa state commission ordered the bank to repay the stolen funds, plus interest and legal costs, as well as compensate the customer for his mental anguish.

The bank did not modify the loan returned in its records or provide a correct receipt to the complaint in Jila Sahakari Kendriya Bank vs. Sarda Ram Nayak, and the District Forum's award of compensation for deficiency in service was affirmed by the Chhattisgarh State Commission.

### Present-Day Developments

The Indian Constitution's Article 21 (Right to Privacy) has had a major impact on the creation of consumer protection legislation in India. The Kerala High Court ruled in District Registrar and Collector v. Canara Bank that requesting information regarding bank accounts without legislative support breaches the right to privacy. This has instilled optimism in banking consumers that banks would now be held accountable for preserving their customers' privacy and upholding the validity of the Indian Constitution's Right to Privacy[10].

## 4. CONCLUSION

It is critical that people recognize their rights and fight for them without remorse. Meanwhile, they should be aware of the law in order to avoid wasting time and money by bringing a case in a venue that lacks the necessary geographical jurisdiction. The development of banking in India was examined in depth in this article. We also looked at the different types of banks that have been formed in India up to this point. The role of the Consumer Protection Act in the banking industry was also highlighted in this study. Finally, individuals must be informed about the processes for submitting complaints, particularly the reasons for filing complaints under different ombudsman systems.

## REFERENCES

**1.** "Bank Crisis: the Current Scenario of Merger and Acquisition in India," Int. J. Recent Technol. Eng., 2020.

**2.** S. K. Sethy, "Developing a Financial Inclusion Index and Inclusive Growth in India," Indian Econ. J., 2015.

**3.** A. Ponnam, D. Sahoo, A. Sarkar, and S. N. Mohapatra, "An exploratory study of factors affecting credit card brand and category selection in India," J. Financ. Serv. Mark., 2014.

**4.** H. G. Krishna and N. Maithreyi, "Recruitment and selection in banking industry," Int.

J. Appl. Bus. Econ. Res., 2017.

**5.** R. Gupta, R. P. Kumar, and A. Bharadwaj, “Mobile Banking System in India: Practices,Challenges and Security Issues,” Int. J. Comput. Trends Technol., 2017.

**6.** P. S. Aithal, P. Kumar, and M. Dillon, “How to Improve the Employee Productivity of Banking System in India – a Theory of Accountability Based Analysis,” Int. J. Manag. Technol. Soc. Sci., 2018.

**7.** U. Dhanda and M. Sehrawat, “ISLAMIC BANKING IN INDIA: AN ALTERNATIVE BANKING SYSTEM,” Int. J. Res. -GRANTHAALAYAH, 2015.

**8.** J. Jayaram and P. N. Prasad, “Insights of modernized banking system of India from research perspective,” J. Chem. Pharm. Sci., 2016.

**9.** C. Cai, “Banking structure and financial stability: A comparison of Chinese and German banking systems,” Front. Econ. China, 2006.

**10.** A. Mohanty and A. Saini, “A Comparison of Islamic Banking and Conventional Banking System in India: A Conceptual Approach,” Al Barkaat J. Manag. Stud., 2014.