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Internal Assessment Test - II

Sub:	Principles and Practices of Banking					Code:	16MBA FM301		
Date:		Duration:	90 mins	Max Marks:	40	Sem:	III	Branch:	MBA

		Marks	OBE	
			CO	RBT
<b>Part A - Answer Any Two Full Questions (16*02=32 Marks)</b>				
1	(a) Explain cheque truncation	[02]	CO2	L1
	(b) What are the essential characteristics of a “Promissory Note”?	[06]	CO2	L2
	(c) Explain duties and responsibilities of a paying banker? When a banker must refuse payment?	[08]	CO2	L5
2	(a) What are Hundis? List any 3 kinds of Hundis	[02]	CO2	L1
	(b) Differentiate cheque and Bill of Exchange.	[06]	CO2	L2
	(c) Summarize the Banker and Customer relationship.	[08]	CO2	L3
3	(a) What is “No Frill” in Banking?	[02]	CO2	L1
	(b) Under what circumstances does the relationship between a banker and customer gets terminated?	[06]	CO2	L3
	(c) Analyze the responsibilities(functions) of a collecting banker and list down the parties involved to a Bill of Exchange and Promissory Note	[08]	CO2	L5
<b>Part B - Compulsory (01*08=08 marks)</b>				
4	(a) Explain briefly i) Duties of a banker ii) Rights of a banker	[08]	CO2	L4

Course Outcomes		PO1	PO2	PO3	PO4	PO5	PO6	PO7
CO1:								
CO2:	To discuss the features of Negotiable Instrument Act of 1881		3a, 1a	3c		3b		1c

CO3:										
CO4:										
CO5:										
CO6:										

Cognitive level	KEYWORDS
L1	List, define, tell, describe, identify, show, label, collect, examine, tabulate, quote, name, who, when, where, etc.
L2	summarize, describe, interpret, contrast, predict, associate, distinguish, estimate, differentiate, discuss, extend
L3	Apply, demonstrate, calculate, complete, illustrate, show, solve, examine, modify, relate, change, classify, experiment, discover.
L4	Analyze, separate, order, explain, connect, classify, arrange, divide, compare, select, explain, infer.
L5	Assess, decide, rank, grade, test, measure, recommend, convince, select, judge, explain, discriminate, support, conclude, compare, summarize.

## 2nd Internal Assessment Test – Key Answers – PPB - 16MBA FM301

1) a) A "**truncated Cheque**" means a Cheque which is truncated during the course of a clearing cycle, either by the clearing house or by the Bank whether paying or receiving payment, immediately on generation of an electronic image for transmission, substituting the further physical movement of the cheque in writing.

b) the essential characteristics of a "Promissory Note" are

(1) In writing - A promissory note must be in writing. Writing includes print and typewriting.

(2) Promise to pay - It must contain an undertaking or promise to pay. Thus, a mere acknowledgement of indebtedness is not sufficient.

Notice that the use of the word 'promise' is not essential to constitute an instrument as promissory note.

(3) Unconditional - The promise to pay must not be conditional. Thus, instruments payable on performance or non-performance of a particular act or on the happening or non-happening of an event are not promissory notes.

(4) Signed by the Maker – The promissory note must be signed by the maker, otherwise it is of no effect.

(5) Certain Parties - The instrument must point out with certainty the maker and the payee of the promissory note.

(6) Certain sum of money - The sum payable must be certain or capable of being made certain.

(7) Promise to pay money only - If the instrument contains a promise to pay something in addition money, it cannot be a promissory note.

(8) Number, place, date etc - These are usually found in a promissory note but are not essential in law. If a promissory note does not bear a date, it is deemed to have been made when it was delivered.

(9) It may be payable in installments

(10) It may be payable on demand or after a definite period - Payable 'on demand' means payable immediately or any time till it becomes time-barred. A demand promissory note becomes time barred on expiry of 3 years from the date it bears.

(11) It cannot be made payable to bearer on demand or even payable to bearer after a certain period

(12) It must be duly stamped under the Indian Stamp Act - It means that the stamps of the requisite amount must have been affixed on the instrument and duly cancelled either before or at the time of its execution. A promissory note, which is not so stamped, is a nullity.

c) The 'paying banker' is a term used to denote the position and duties of the drawee-banks in paying cheques of their customers. Thus, 'paying banker' is a banker upon whom a cheque is drawn

## DUTIES AND RESPONSIBILITIES OF A 'PAYING-BANKER'

The drawee of a cheque having sufficient funds of the drawer in his hands must pay the cheque when duly required so to do. In default of such payment, the paying bank must compensate the drawer for any loss or damage caused by such default Protection in case of crossed cheques

A banker paying the cheques crossed generally to a banker or to the specified banker, is protected even if it turns out to be a payment to a wrong payee.

Payment in due course [Section 10]

Payment in due course means payment in accordance with the apparent tenor of the instrument made in good faith and without negligence. They are as follows: -

1. Payment must be in accordance with the apparent tenor of the instrument
2. Payment must be made in good faith and without negligence
3. Payment must be made to the person in possession of the instrument
4. Payment must be made to the person entitled to receive.
5. Payment must be made in money only.

When banker **must refuse** payment

A paying banker must refuse payment on cheques if any of the following circumstances exist:

1. Where the customer countermands the payment (stopped by the drawer)
  2. On receipt of a notice of customer's death
  3. On customer's becoming insolvent
  4. On receipt of a notice of the customer's insanity
  5. On receipt of Garnishee order
  5. On assignment of Credit balance
  7. On suspicious misuse by trustee
- 2) a)** Hundis are instruments written in an oriental language. The word 'hundi' appears to have been derived, from the Sanskrit work 'hund' which means 'to collect'. These hundis were, therefore, originally used for the collection of debts. Hundis have been in circulation in India from very early times, long before the Negotiable Instrument Act, 1881. Shah-Jog Hundi, Darshni Hundi, Muddati Hundi or Miadi Hundi.

**b)**

<b>Cheque</b>	<b>Bill of Exchange</b>
<ol style="list-style-type: none"><li>1) It must be drawn only on a banker.</li><li>2) The amount is always payable on demand.</li><li>3) The cheque is not entitled to days of grace.</li><li>4) Acceptance is not needed.</li><li>5) A cheque can be crossed</li><li>6) Notice of dishonour is not necessary. The parties thereon remain liable, even if no notice of dishonour is given.</li><li>7) A cheque is not to be noted or protested in case of dishonour.</li><li>8) The protection given to the paying banker in respect of crossed cheques is peculiar to this instrument.</li></ol>	<ol style="list-style-type: none"><li>1) It can be drawn on any person including a banker.</li><li>2) The amount may be payable on demand or after a specified time.</li><li>3) A usance (time) bill is entitled to three days of grace.</li><li>4) A bill payable after sight must be accepted.</li><li>5) Crossing of a bill of exchange is not possible.</li><li>6) Notice of dishonour is necessary to hold the parties liable thereon. A party who does not receive a notice of dishonour can generally escape its liability thereon.</li><li>7) A bill is noted or protested to establish dishonour.</li><li>8) No such protection is available in the case of bills.</li></ol>

**c)** Banking is a trust-based relationship, relationship is based on contract, and on certain terms and conditions. These relationships confer certain rights and obligations both on the part of the banker and on the customer.

Classification of Relationship: General Relationship and Special Relationship.

**General Relationship – debtor – creditor** - When a 'customer' opens an account with a bank, he fills in and signs the account opening form. By signing the form he enters into an agreement/contract with the bank. When customer deposits money in his account the bank becomes a debtor of the customer and customer a creditor. The money so deposited by customer becomes bank's property and bank has a right to use the money as it likes. The bank is not bound to inform the depositor the manner of utilization of funds deposited by him. Bank does not give any security to the depositor i.e. debtor. The bank has borrowed money and it is only when the depositor demands, banker pays. Bank's position is quite different from normal debtors.

Banker does not pay money on its own, as banker is not required to repay the debt voluntarily. The demand is to be made at the branch where the account exists and in a proper manner and during working days and working hours.

**creditor – debtor** - The resources mobilized by banks are utilized for lending operations. Customer who borrows money from bank owns money to the bank. In the case of any loan/advances account, the banker is the creditor and the customer is the debtor. The relationship in the first case when a person deposits money with the bank reverses when he borrows money from the bank. Borrower executes documents and offer security to the bank before utilizing the credit facility.

In addition to opening of a deposit/loan account banks provide variety of services, which makes the relationship more wide and complex. Depending upon the type of services rendered and the nature of transaction, the banker acts as a bailee, trustee, principal, agent, lessor, custodian etc.

Special Relationship - Bank as a Trustee

Bailee – Bailor

Lessor and Lessee - The transferor is the lessor, transferee is lessee

Agent and Principal

As a Custodian

As a Guarantor

**3) a)** The practice followed by banks in the past was that for opening account there has to be an initial deposit in cash. However the condition of initial cash deposit for opening the account appears to have been dispensed with the opening of '**No Frill**' account by banks as per directives of Reserve Bank of India. '**No Frill**' accounts are opened with 'Nil' or with meager balance.

**b)** The relationship between a bank and a customer ceases on:

- The death, insolvency, lunacy of the customer.
- The customer closing the account i.e. Voluntary termination
- Liquidation of the company
- The closing of the account by the bank after giving due notice.
- The completion of the contract or the specific transaction

**c)** One of the principal functions of a banker is to receive instruments from his customer in order to collect the proceeds and credit them to his customer's account. When acting in this capacity he is called a "collecting banker".

- While collecting his customer's cheques, a banker acts either:
- (i) Banker as Holder for value - When, to oblige a customer, a bank pays the proceeds of a cheque drawn upon another banker, before collection, he is treated as a holder for value. Similarly, where, a customer pays in a cheque and the banker expressly or impliedly permits him to draw against it before it is cleared, the banker will be regarded as a holder for value.
- (ii) Banker as Agent - A collecting banker acts, as an agent of the customer if he credits the customer's account with the amount of the cheque after it is actually realised.

#### **Duties and responsibilities of a collecting banker**

- Due Care and Diligence in Collection of Cheques
- Presentation for payment by the next working day after the receipt of the cheques.
- Notice of Dishonour
- **Parties to a Bill of Exchange**

1. The Drawer - the person who draws or makes the bill.
2. The Drawee - the person on whom the bill is drawn.
3. The Payee - the person to whom the amount of the bill is payable.
4. The Holder - is the original payee but where the bill has been endorsed, the endorsee.
5. The endorser - is the person who endorses a bill.
6. The endorsee - is the person to whom the bill is negotiated by endorsement.

#### **Parties to A Promissory Note**

1. The Maker - the person who makes the note promising 'to pay the amount stated therein.
2. The Payee - the person to whom the amount of the note is payable.
3. The Holder - is either the original payee or any other person in whose favour the note been endorsed.
4. The Endorser - the person who indorses the note in favour of another person.
5. The Endorsee - the person in whose favour the note is negotiated by indorsement.

#### **4) a) Duties of a banker**

A 'Banker' has certain duties vis-à-vis his customer. These are:

Duty to maintain secrecy/confidentiality of customers' accounts.

Duty to honour cheques drawn by customers on their accounts and collect cheque, bills on his behalf.

Duty to pay bills etc., as per standing instructions of the customer. Duty to provide proper services.

Duty to act as per the directions given by the customer. If directions are not given the banker has to act according to how he is expected to act.

Duty to submit periodical statements i.e. informing customers of the state of the account

Articles/items kept should not be released to a third party without due authorization by the customer

#### **Rights of a banker**

Right of General Lien

Right of Set-Off

Right of Appropriation

Act as per the mandate of customer

Right to Charge Interest, Commission, Incidental Charges etc. Lien: