

CHAPTER - 2PROCEDURES RELATING TO THE EXERCISE OF LENDING POWERS IN BANKS

In this chapter, an attempt has been made to discuss the procedures that are generally prescribed by the banks in India for the exercise of Delegated Powers by functionaries operating at different decision centres in the bank. The need for a uniform policy and common operating procedures and their standardisation is all the more necessary in a banking system having wide geographical coverage and functional diversification. Further, in an analytical study of the delegation of powers, especially in the area of credit disbursement and monitoring, involving a number of decision centres at the top management level located at one and the same place, middle level management decision centres, responsible for monitoring the grass root level decision centres, located in different geographical zones of the country and the grass root level decision centres located all over the country from metropolitan areas to the remote rural, desert and hilly centres, it is all the more essential to get a clear idea about rules and procedures which the decision centres are required to follow while exercising the powers delegated to them. In view of this, the procedures relating to the exercise of lending powers, as generally prescribed by the banks and followed by the decision centres, have been briefly discussed here. Section I of the chapter provides the main observations and recommendations of the 'Study Group on Bank Procedures' and the 'PEP Committee on Banking' in the context of the changing functional profile of

banks in India, especially after the nationalisation of major commercial banks. The subject matter of section I provides a background for Section II, in which the procedures followed by different decision centres in exercising the powers delegated to them have been generalised and presented.

### SECTION - I BACKGROUND

Prior to the nationalisation of major commercial banks in 1969, most of the banks owed allegiance to some industrial/business houses and catered mainly to their credit requirements.

Traditionally, they were confined to a selective and narrow scale of operations which is commonly described as 'class banking'. With the scope and area of operation being very much specified and limited, the whole gamut of decision making was centralised in Head Office. Indian Banks were organised as monolithic structures with the Head Office reserving the right to decide in almost all matters and the branches being directly under the supervision and control of the Head Office.

The post-nationalisation period, however, has witnessed revolutionary changes in the banking industry. There has been a spurt in the network of the branches, spread in remote and far-flung areas. The public sector banks have now undertaken the role of a catalytic agent for ushering in new socio-economic order in rural areas and removing the regional imbalances through the media of credit dispensation for activities and sectors which hitherto remained neglected. This new activity

profile of the banks involved qualitative and quantitative changes in their operations entailing restructuring of their organisational setup to facilitate smoother and better supervision and control over the operations. A number of study groups and committees appointed by the government of India and the Reserve Bank of India have also examined the problem of improving the organisational efficiency of banks especially, during the period of their transformation. Important amongst these committees and study Groups have been the study Group on Banking Procedures (1971) and the PEP Committee on Banking (1977) which have gone into the details of organisational efficiency of banks in the context of their changing role profile and have also opined on the issue of Delegation of Powers in the banks. The observations and recommendations of these two committees may provide a useful background for this study. Hence their observations and main recommendations relevant to our study have been given below very briefly.

#### Study Group on Bank Procedures

The study group on Bank Procedures, appointed by the Banking Commission, examined the problem of organisational decentralisation in banks with a view to ensure procedural simplification and effective delegation of powers for enabling the banks to improve their efficiency in the field of non-traditional business, especially lending to the priority sector.

Study Group observed that decentralisation of organisational structure and liberalisation of delegation of powers have an important place in the simplification of procedures for the grant and supervision of credit. As far as the procedures relating to traditional type of advances were concerned, the situation was satisfactory. However, there was need for improving the procedures for grant of non-traditional advances, especially the advances belonging to the 'priority sector'. It therefore offered a number of suggestions relating to 'Bank Organisation and Management' and 'Delegation of Discretionary Powers to Sanction Advances'. While considering the extent to which the powers to sanction advances should be delegated to different officials, a number of factors such as the size of the branch, the type of business handled, the experience of the concerned officials etc., have to be kept in view. These factors differ from bank to bank widely. The Group, therefore, recommended certain general principles which could serve the banks as useful guidelines in that regard, as given below :

- (i) Powers delegated to branch agents should be adequate to enable them to sanction working capital advances to small borrowers without reference either to the regional offices or the head office. While vesting such powers the head office should, however, prescribe overall ceiling on the total amount of credit that could be advanced at each of the branches to various

categories of borrowers, i.e., agriculturists, small scale industries, other small borrowers, etc. This provision is necessary to ensure equitable distribution of credit in relation to the bank's total available resources and in the context of liquidity requirements. Regional offices should have authority to sanction the bulk of the advance proposals emanating from the branches; only proposals for working capital advances to large scale industries and those for medium-term and long-term advances for sizeable amounts should be referred to the Head Office.

- (ii) Delegation of authority should be reviewed at least once in two to three years and discretionary powers should be varied, if necessary, according to requirements.
- (iii) While senior agents are normally posted at important branches, occasions may arise when the powers to sanction advances delegated to agents on the basis of their seniority and/or grade may not be adequate considering the type of business required to be handled by a branch. In such cases, necessary adjustments should be made.
- (iv) Branches should be required to maintain a register recording the receipt of loan applications (whether made orally or in writing) and their disposal. The reviewing officers should examine this register in

order to find out whether there has been any undue delay or wrongful refusal of credit facilities.

- (v) While exemplary punishment should be awarded to the agents who are found guilty of deliberate misuse of powers, gross negligence, dishonesty or favouritism in order to curb any tendency to abuse the powers vested in them, the agents should be protected even though an advance becomes difficult of recovery<sup>but</sup> it was granted in the normal course without malafide intent.

These recommendations of the study group were taken into consideration by the banks in designing their power structure for sanctioning of credit. The functionaries at different levels of hierarchy constituting different decision centres were thus given powers to sanction different types of advances and other credit facilities. Still, after a lapse of about six years, when the PEP committee examined the problem, it found a number of weaknesses in the system of delegation of authority in banks and, had to offer remedial action. The observations and suggestions of the PEP Committee, are briefly given below.

#### PEP Committee on Banking

The committee,<sup>1</sup> while dealing with the issue of 'Delegation of Authority in Banks' pointed out that the management of a bank

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1. Reserve Bank of India: Report of the PEP Committee on Banking, Bombay, 1977. pp. VIII-35.

is vested in its Board of Directors. The decisions and intentions of the Board have to be translated into action and this is done through the Chief Executive and various other functionaries by means of a system of delegation of authority. It is observed that there is either undue concentration of power at certain levels leading to avoidable delay in taking decisions or unfettered freedom of operation exposing the wielder of such authority to the temptation for misuse of power. A sound system of delegation of authority should aim at :

- (a) quick and efficient discharge of work at all levels.
- (b) overall reduction in cost of administration.
- (c) development of the human resources from the point of sharpening the decision-making capabilities of the managerial personnel.
- (d) widening the scope for participative management, and
- (e) providing encouragement for the innovative spirit among all the employees.

It is necessary to lay down certain principles and norms for the evolution of a system of delegation of authority in banks. This involves identification of decision centres on a uniform basis for different categories of banks and categories of branches as well as roles specification and assessment of expectations of both the management and the public about the performances of decision centres.

Adequate discretionary powers to the operating personnel in banks are essential in order to speed up the process of decision-making. The scheme of delegation of powers in banks must be under constant vigil in order to ensure that delays do not occur due to not being equipped with adequate powers. The extent of delegation will depend on the size of the organisation, the quality of the man-power, etc. However, as a guiding principle banks must ensure that at least 80 percent of the decisions are taken at the primary levels and only 20 per cent are passed on to the next higher authority.

Delay in decision making due to the temporary absence of the authorised officer can be obviated by an arrangement by which two officials next below the rank of the authorised officer can jointly exercise the power. It should be possible to give effect to this proposal by incorporating suitable provisions in the scheme of delegation of powers to the concerned officers. Any scheme of delegation should be supported by an effective control system. In the banking industry today, the control systems designed for conventional banking are on the verge of a breakdown with the emergence of mass banking. Banks must redesign the control system so as to ensure that control reports are timely and meaningful.

Thus, both the study group on Bank Procedures and the PEP Committee on Banking had a unanimity in opinion about the urgency of organisational decentralisation and effective and adequate delegation of lending powers in banks, especially in



the context of their new role. A number of other studies conducted by banks and academicians<sup>an</sup> also felt about the inevitability of effective delegation of lending powers, especially, at the grass root level. It can therefore be concluded that delegation of lending powers in a banking institution is inevitable and unavoidable on account of the role and responsibility assigned to it and also because of its organisational structure which has three/four tiers. In the organisation set up of the banks, branch constitutes the operating unit at the grass root level. A number of branches are grouped together and are put under the operational control of an administrative tier called Region/Division. In some Banks, Regions/Divisions report directly to the top tier called Head Office/Central Office. The top tier constitutes policy formulation, planning and corporate control tier of the bank. In large sized banks, one more tier is introduced and is called a Zone/Circle. This tier acts as an extended arm of the Head Office/Central Office. It is a management control tier controlling a number of Regions/Divisions. In such multi-tier structure of the banks, delegation and decentralisation become an organisational necessity.

Banks in India have also realised it and have made sincere efforts in the direction of delegation of powers - both lending and non-lending. However, as our study is concerned with the delegation of lending powers only, we shall analyse

such powers at length for each bank identified for the purpose and then attempt an inter-bank analyses also. But before we take up that exercise, it will be desirable to have an idea of the procedures that are followed in most of the banks in regard to the exercise of delegated lending powers.

## SECTION - II

### The Prescribed Procedures

The procedures relating to the exercise of lending powers by different functionaries at different decision centres have been prescribed by different banks differently. However, all the banks have prepared power charts deputing the Maximum Delegated Lending Powers to the functionaries belonging to the top level management, the middle level management and the grass root level management. These procedures as pointed out earlier, differ from bank to bank on the basis of their organisational set-up and the prevailing practices. The range of the magnitude of delegated powers is very high and the procedures followed by different banks in the exercise of the delegated lending powers are also different. Still, some important practices and procedures, common to all the banks, can be generalised for the purpose of our understanding. The methodology followed for the purpose was to pick out the common points of procedures from the banks identified for the purpose of inter-bank analysis and leave aside the provisions which were typically based on the distinction of organisational profile of a particular bank. The procedures, so generalised are briefly described below.

### Implementation of Prescribed Policy & Norms

The delegated lending powers in practically all the banks are exercised by the delegates subject to the observance of lending policy of the concerned bank and the credit restraint measures imposed by the RBI and the concerned bank from time to time, the prescribed norms of scrutiny and assessment; various terms and conditions pertaining to margin/rate of interest-/ security norms, etc.; authorisation under the Credit Authorisation Scheme of the RBI, where applicable; guidelines and norms by prescribed by the RBI based on the Tandon study Group<sup>1</sup> recommendations and the recommendations of the Ghore committee<sup>2</sup> where applicable, selective credit control directives as prescribed by RBI and such other directives and policy guidelines that may be issued by the Reserve Bank of India/Government of India from time to time and the administrative<sup>instructions</sup> issued by the concerned banks in that regard. All the banks have the legal obligation to adhere to the RBI directives, each bank has prescribed it in the guidelines for the exercise of powers related to the sanction, disbursement and monitoring of credit.

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1. Reserve Bank of India: Report of the Study Group to Frame Guidelines for Follow-up of bank credit-1975.
  2. Reserve Bank of India, Report of the Working Group to review System of Cash Credit, Bombay, 1979.

### Powers related to specific schemes

So far as the utilisation of delegated lending powers related to different types of lending schemes are concerned, the loans and advances coming within the purview of any scheme evolved by the concerned banks are sanctioned by the concerned authorities of the banks, as provided in the scheme and to the extent permissible therein. In case, specific powers have not been delegated under some scheme, the delegates are supposed to exercise the general delegated powers. In any case, the branch officials in any bank are not supposed to exceed the 'over all limits', wherever prescribed.

### Secured Loans, Partly Secured Loans and Unsecured Loans

According to the law and practice of banking in India, for the purpose of exercising the delegated lending powers, secured loans and advances means such loans and advances that are fully secured by some approved tangible securities, such as, LIC policies, approved shares, convertible debentures, Units under Unit Scheme 1964 of Unit Trust of India, Government Securities, National Saving Certificates, Government Promissory Notes, Specified Post Office Time Deposits, inventory and book-debts, documents of title to goods, vehicles, durable utility articles, land, building, plant and machinery, agricultural crops, agricultural implements like pump sets, power tillers, tractors, livestock, poultry, etc., gold jewellery, term deposits of the concerned bank, and guarantees of scheduled commercial banks and bills of exchange co-accepted by the banks.

participating under the IDBI Bills Rediscounting Scheme. It may be relevant to note here that prime gold, silver and bullion are not accepted as security under the existing system and special Bearer Bonds are accepted only as a collateral security. Loans and advances against supply bills, cash incentives, duty drawback, EPC, BE, FBE (DA basis) CDB are treated as unsecured advances. In the case of partly secured loans, advances, guarantees and LCs, that portion of loan, advance, guarantee or LC which is fully secured, i.e., the value of the security minus margin is treated as secured and only the balance portion of such loan, etc., is treated as unsecured. For the purpose of determining as to whether the limits sanctioned to be sanctioned are secured or unsecured, the prime security alone is taken into consideration. Where, an unsecured limit is granted by obtaining any collateral security, such advances are treated as unsecured for the purpose of lending powers.

#### Sanctioning Authority and the concept of a single Borrower

In all the banks, as a matter of general policy and procedures, the powers of lower officer do not derogate the powers of any higher officer. The banks' power charts indicate the powers to be exercised by different functionaries in the hierarchy on the basis of the maximum amount of loans, advances and other facilities that can be sanctioned to a single borrower. For instances if a person is the sole proprietor of more than one proprietorship concerned, then all such concerns are treated as only one entity for the purpose of exercising the delegated

lending powers. The same principle applies, where partners are the same in more than one firm.

In order to determine as to who has to exercise the delegated powers in any given case, the power permitted under the category for which the facility is sought for (limit or the sub-limit as the case may be) is generally taken into consideration, if the party has no other limits except the limits sought for. If out of the several limits permitted or proposed to be sanctioned to a borrower, any of the limits or sub limits, excluding those granted against security of the Banks' term deposits, exceed the power delegated to a particular sanctioning authority, or if the aggregate of the several limits permitted or recommended exceed the ceiling prescribed for the category of a group of advances, for that particular authority, then all the limits, excluding those to be granted against the security of the bank's term deposits, are sanctioned by the appropriate higher authority. For the purpose of aggregating the permitted limits:

- (i) the loans, guarantees, LCs granted on the full security of deposits or a 100 per cent cash margin;
- (ii) the limits granted to clearing agents, ginning factories, cold storage plants for clearing forwarding and storing of goods; and
- (iii) the loans granted for acquiring bank's premises, are excluded.

However, where single transaction limits are permitted,

- (i) the outstanding liability, if the sanctioned limit is fully utilised;
- (ii) the permitted limit not availed, but still not cancelled and
- (iii) the unavailed portion of the limit plus the outstanding liability in case of partly availed limits; are taken into consideration for determining the amount of limits that can be sanctioned.

#### Credit Reports

For permitting any credit facility to any party, except in the case of loans or advances against bank's term deposits and gold jewellery, irrespective of the fact as to whether the requirement is for a single transaction or a series of transactions or for a specified period or as a regular credit facility, the branches are required to prepare credit reports in the prescribed format applicable to the party except where the facility is granted under the emergency powers delegated to various authorities.

In the case of branch sanctions, the copies of the credit reports prepared by the branch are endorsed to RO/DO/CO as per the procedure laid down from time to time. Branches/RO/DOS/COs are required to maintain a separate Register for noting down all the credit proposals received for their sanction and

incorporate therein all the relevant particulars such as the sanctions/rejections/reductions, etc.. However, where telephonic permission has been given for a credit facility, proper record of such sanction is maintained both by the sanctioning authority as well as by the concerned branches, explaining the circumstances under which the oral/telephonic sanction was conveyed/obtained.

For this purpose, a separate note book/register is kept in which the date of sanction, the name of the borrower, the limits sought for, the limits sanctioned, the conditions specified by sanctioning authority and the reasons for obtaining such sanction are recorded. Later on, written sanction of the competent sanctioning authority is obtained by submission of a credit report within a week of obtaining the telephonic/oral sanction.

#### Re-constitution of firms

Where same borrower partnership firm is reconstituted with addition or deletion of partners, branches are empowered to make available such limits to the reconstituted firm on the same terms and conditions that existed before the reconstitution of the firm, provided there are no adverse changes in the financial or other matters and subject to such procedural guidelines as may be in force from time to time.



### Recommending Authority

In practically all the banks, the recommending authorities at the branch level are different for the proposals falling within the sanctioning powers of different authority. For example the proposals falling within the powers of the Board/CSC/<sup>CMD</sup>~~MD~~/ED/GM/DGM/AGM, the recommending authority at branch level is Sr. Manager, through DM, in case of ELB and First Line Manager in the case of other branches. The proposals falling within powers of DM (Admn.) at circle office are recommended by Sr. Manager through the DM in the case of ELBs and Sr. Manager/Manager in charge of branch in other cases. Whereas Sr. Manager/Manager-in-Charge of branch recommends the proposals falling within the powers of DM(operations) and Sr.Manager/Accountant at DO/CO.

### Validity Period and Renewal

As far as the time limit for availing the sanctioned limits are concerned, all credit limits sanctioned generally are required to be availed of, fully or partially, by the party within a maximum period of six months from the date of the sanction. Availament of credit facilities beyond the stipulated time are authorised by the concerned sanctioning authority, excepting in the case of facilities sanctioned by the Board, where the clearance of GM,(Credit Wing) shall be obtained.

The proposals coming within the powers of DM and above are valid for a maximum period of one year from the date of sanction

or fifteen months from the date of credit report whichever is earlier. All other cases are valid for a maximum period of two years from the date of sanction or twenty seven months from the date of credit report, whichever is earlier. These limits apply to only running/operative limits.

If the party is not able to furnish the required particulars and the renewal is not effected by the due date on account of genuine reasons or unavoidable circumstances, the sanctioning authority, depending on the merits of each case, generally permits extension of limit for a period not exceeding three months from the date of expiry, provided no adverse features are noticed. In the case of limits falling within the powers of GM, ED, MD, CSC, and the Board, Circle Office permits such extension and report to the Credit Wing. Where limits are not renewed within three months from the date of expiry, such limits are not made available to the party unless the credit report is submitted and there are no adverse features. So also, no requests for additional or temporary limit are entertained from such parties.

#### Transfer of Limit

The entire limit or a portion thereof of a borrower can be transferred from one branch to another provided it is authorised by the RM/DM in the case of limits coming upto RM's/DM's powers and those beyond the powers of RM/DM, with the consent of the DGM.

#### Absence of Sanctioning Authority

Where any of the sanctioning authorities like AGM, RM/DM (Admn.) exercise the powers of their higher authority due to their absence, a copy of the note wherein the relevant orders have been passed are placed for information, before such higher authority. The MD and in his absence the ED, and in the absence of both the GM (Credit Wing) is empowered to consider and accord sanction on urgent proposals in respect of credit limits sanctioned by or falling within the powers of Board of Directors. The Circle/Regional Office immediately thereafter gets the action ratified by the Board.

#### Suspension and Restoration of Powers

The Deputy General Manager of the concerned Circle Office may, taking into account the recovery performance, the proper utilisation or otherwise of the delegated powers, the credit requirements at the concerned place, etc., suspend the powers delegated to any official in full or in part depending upon the circumstances in each case. The reasons for such suspension is recorded and communicated to the concerned official and the case is reviewed as early as practicable as to the necessity of restoration of the suspended powers. In case an official whose powers have been so suspended is transferred from one branch to the other, the Deputy General Manager in most of the banks, examines if the powers of the new incumbent should also stand suspended and whether the powers of the official whose powers were earlier suspended stand restored.

### Reduction and Rejection of Proposals

Any rejection or reduction in, proposals by Accountant/Manager/Senior Manager in administrative units and officers of various ranks in branches require the concurrence of the next higher authority. Proposals rejected by DMs and above and upto DGM are informed to the next higher authority. In the case of proposals rejected by DGM of the Circle, such information is submitted to GM(Credit Wing). The DO/COs enter all the rejected proposals in a serial order in a separate Register providing a separate number. For each rejection, a copy of the note superscribed with the serial number given in the register is endorsed to such higher authority for their information, as and when such proposals are rejected.

Credit refusals and reduction effected by any authority below Divisional Manager are reviewed by the next higher authority. If a proposal, coming within the powers of any authority below the level of Deputy General Manager once rejected is represented, subsequent rejection is made only in consultation with the next higher authority. Branch sanctions are reviewed by Divisional Office. In the case of ELB's, sanctions upto Senior Manager are reviewed by DM of ELB and the sanctions of DM (ELB) are reviewed by the Circle Office. In the case of DOs, the sanctions of Manager/Senior Manager at DO are reviewed by DM (Operations) and the sanctions of DM (O) are reviewed by the Circle Officer.

Where the limits sanctioned by a higher authority are kept in abeyance or are not made available to the borrower, such fact

are reported to the sanctioning authority. In the case of sanctions by the Board, Credit Sanctioning Committee, MD, ED and GM (Credit Wing) such reporting is made to Credit Wing of Head Office.

#### Emergency Powers

Emergency powers are exercised in case of proposals for granting additional/single transaction limits in situations where due to urgency the branches (D.O./C.O. are not in a position to prepare a regular Credit Report to place it before the appropriate sanctioning authority for obtaining the prior sanction. In the case of those parties who do not enjoy any credit facility with the bank, such powers can be used for short term credit accomodation in specified categories where the branches have been empowered to grant such facility. The credit limits permitted under the emergency powers shall not outstand for a period longer than the period stipulated for the relative category of advance/guarantee/LC (as the case may be) in the manuals of instruction/relative circulars issued by the concerned banks from time to time.

However, where no such express stipulation has been made in the instruction/circulars, the facility does not outstand beyond 15 days in the case of unsecured loans and 30 days in the case of secured loans.

While permitting the credit facility, in every case under this Head, the concerned authority has to specify the period for which

the facility granted shall outstand. The branch notes the period so specified in the Emergency Advances Register for the purpose of follow-up and clearance of such loans.

Emergency powers are supposed to be exercised sparingly. However, it shall not be exercised as a substitute for the general sanctioning powers, where the borrower requires the credit facility regularly. The branches shall exercise the emergency powers (for parties with or without credit limits) not exceeding 12 times per party in a calendar year, under all heads, including casual overdrawings in current account. If in the case of any party (with or without credit limits) such occasions become frequent, suitable limits/additional limits are fixed under general sanctioning powers. The overdrawings in current account should not exceed 25 per cent of the net worth of the party.

After understanding the general provision's relating to the procedures for exercising the delegated lending powers in the Indian banks, an attempt has been made in Part II of this work to analyse the delegated lending powers in the identified banks. Analysis in respect of each bank has been done in a separate chapter, so that the profile of delegation of powers in the bank can be understood in the background of its structural - functional profile.