

GLOSSARY OF TERMS USED IN BANKS

1. Acceleration - A standard clause in a mortgage instrument permitting the lender to demand full payment of principal from the borrower upon default of the obligation
2. Account History - The payment history of an account over a specified period of time, including the number of times the account was past due or over limit.
3. Bank Guarantee - Bank Guarantee could be a finance guarantee or a performance guarantee. Under finance guarantee, the bank guarantees the beneficiaries (The person named in the guarantee to receive the guaranteed sum under stated circumstances), certain amount on behalf of its customers who has commercial relationship with the beneficiary. Under performance guarantee, the bank guarantees performance of a contract or goods/ services supplied under a contract by its customers. However, even in the later case, if its customers fail to deliver, it settles the claim of the beneficiary in money terms only; the bank does not fulfill the contract, obligation of its customer.
4. Bank Statement - A periodic record of a customer's account that is issued at regular intervals, showing all transactions recorded for the period in question.
5. Bill - Usually mistaken for commercial invoice. Actually bill in the banking parlance means a bill of exchange drawn by a seller on the buyer whenever he sells goods or services on "payment later" basis. Such a transaction is also referred to as a credit transaction. The bill is routed through the bank for collection of amount from the buyer. Commercial invoice is a part of the document submitted to the bank by the seller. A bill of exchange is an order made to the buyer by the seller that in exchange for the goods or services sold by him on credit, the buyer is required to pay on a specific date a certain amount with or without interest to him or to any other directed party.
6. Cash Credit - A credit facility under which a customer draws up to the preset limit, subject to availability of sufficient security with the bank. The difference between an overdraft and cash credit account is that while the former is extended more to individuals, and less for business, the latter is extended only to business bodies. The cash credit facility is unique to India, as in most of the countries it is called overdraft.

Further the cash credit facility is more or less on a permanent basis so long as the business is going on. Internationally at the end of specific period the overdraft facility is withdrawn and the customer is required to pay back the amount lent by the bank. The purpose of cash credit is for working capital. The operations are similar to overdraft.

7. Cash Reserve Ratio - Called in short CRR. Suppose a bank has total deposits of Rs.100 Bn and is required to maintain a CRR of say 5%. This means that the bank should maintain in current accounts with the central bank or any other approved bank balances, not less than Rs. 5 Bn. This much amount is impounded and kept in the free form. And the bank cannot lend this money. This acts as a buffer to the bank. In India, RBI decides from time to time and at

present it is 5.5 % of the deposits, held by the bank.

8. Credit Report - It is called by different names. At times it is referred to as credit information report. At other times it is also called customer's confidential report. Bankers report also means the same. With the growth of commerce within a country and abroad, most of the times, trade is done with the organizations about which you are in the dark. The banker provides good platform for knowing something about the business enterprise with which you are likely to deal. There are accepted abbreviations internationally for denoting the soundness or the lack of it of a business enterprise. These abbreviations are commonly used in such reports. You can seek confidential information about your prospective customers about whom you do not have sufficient knowledge. The banker provides this information for a fee which includes the fees that they have to remit to international credit agencies.

9. Daily Product Basis - This is the basis on which interest is usually determined on credit facilities, like loan, overdraft, cash credit etc. for this; the basis is 365 days in a year. Some banks do take 360 days in a year also. There is no hard and fast rule in this behalf. E.g. A bank has given a customer an overdraft facility to the extent of Rs.10, 000/- for 45 days at 6% p.a. on a daily product basis the interest is determined as under.

Step No 1. $10000 \times 45 \text{ days} = \text{known as product} = 450000$

Step No 2. Determination of annual average as rate of Interest is on annual basis i.e. $450000/365 = \text{Rs. } 1233/-$.

This means that on a 365 days per year basis, drawing Rs. 10000/- for 45 days is equivalent to drawing Rs. 1233/- through out the year, i.e. on annual basis.

Step No 3. Calculation of interest at 6% p.a. is equal to $1233 \times 0.06 = \text{Rs. } 73.98$.

This means that by adopting daily product basis we are converting the amount drawn for a period less than a year to its annual equivalent so that the rate of Interest, which is universally on annual basis can be applied to determine the quantum of interest.

10. Discount - Less than face value. If the value of the bill is Rs. 100/- and in case the bank gives the finance against the same, the amount of finance will be less than Rs. 100/-, say Rs. 98/-. Rs 98 is the discounted value of the bill for Rs. 100/-, while the difference of Rs. 2/- is known as "discount". Discount is the interest recovered upfront, especially in the case of those bills for which payment will be forthcoming after a specific or extended period.

11. Letter of Credit - Seller "A" enters into contract with Buyer "B". One of the terms of supply is that buyer will establish a letter of credit in favor of the seller through his bank. The buyer approaches his bank, which, on certain conditions, agrees to extend this facility. Under this facility, the buyer's bank gives commitment of payment to the seller through his bank. The commitment is dependent upon the seller fulfilling specific conditions as per the L/C. The conditions are:

The seller should furnish proof of dispatch of goods or services and submit all the documents required under the L/C.

Then, the buyer's bank will pay the amount of bill drawn by the seller on the buyer under this agreement. International letter of credit are by and large, "irrevocable" (cannot be cancelled by the buyer without the consent from the seller).

12. Loan - A lump-sum amount given to the customers, either in one installment or in two or three installments, and repayment over a period of time in monthly or quarterly, or half yearly or annual (very rarely) installments. Interest may be recovered separately from the customer who is called borrower or combined with the installment. In case it is combined with the installment it is called equated installment. If interest is recovered separately it is usually on a quarterly basis. Loans against property and for the purpose of owning flats/ apartments/ houses are known as mortgage loans.

13. Margin Money - Margin money is like a security deposit retained by the bank till the loan is fully settled. The banks sanction the credit limit after retaining a margin on the value of the security offered. The percentage of margin requirements varies as per RBI guidelines.

14. Monthly Product Basis - In India, in the savings account, the product is taken on a monthly basis; the rule is interest is paid on the minimum balance in the account between the 10th and the last day of every month. This means that any credit to the account after the tenth of the month is ignored for the particular month, while debit is taken into account. Accordingly let us say for example. The following minimum credit balances in the savings account earning 3.5 % pa interest in India

January, 2005	1000
February, 2005	800
March, 2005	150
April, 2005	250
May, 2005	300
June, 2005	300

Suppose the Interest is payable every half-year and accordingly this customer will be entitled to 1.75 % for the half year ending June 2005. In order to determine the correct half yearly interest, you need to find out the annual equivalent of the deposit that the customer has kept in his savings account. Then divide the sum of the monthly products by 12. The annual equivalent amount is RS 233.33 and the interest at 3.5% p.a. for the half year on this work out to be Rs 8.17. This is the way the interest is found out on a monthly product basis.

15. Overdraft - An extension of current account in which the customer is allowed to withdraw more than the credit balance lying in the account. This may be a temporary accommodation to tide over temporary cash crunch or on a regular basis. If permitted on a regular basis, withdrawals are allowed up to a ceiling (called "a limit"), subject to availability of sufficient security with the

bank. In case the overdraft is given to the business enterprises and it is for day-to-day operations, it is known as “working capital”.

16. Remittance – A facility, by which its customers at one place makes funds available to the bank and the bank in exchange, makes the funds available to the customer or any other specified party at the required place, within the same country or abroad.

Remittance can be in the form of Demand Draft (DD), mail Transfer (MT), Telegraphic Transfer (TT), Electronic mail transfer (EMT) through computer networking (or satellite channel), International Money Order (IMO) etc.

17. Repayment Holiday - Whenever a loan is taken especially for acquiring fixed assets, the repayment does not start immediately. It starts after the fixed assets starts giving a return especially in the case of business enterprises. This is not so in the case of personal loans. The period during which there is no repayment is known as repayment holiday period. This is also known as moratorium period. The period is longer in the case of industrial loans and minimum or absent in case of personal loans. It should be noted that during this period, Interest is charged and there is no period on non-levy of interest. Although there may be a period of non-recovery of Interest. That is interest although levied, not recovered for a specific period. Again if this is the case interest on interest is recovered.

18. RTGS - refers to the settlement system where, settlement of payments on an individual order basis is done on continuous basis, without netting debits with credits across the books of a central bank. RTGS system is also defined as a gross settlement system, in which both processing and final settlement of funds transfer instructions take place continuously (i.e. on real time basis). Thus we can say that RTGS system reduces settlement risk because inter-bank settlements are done throughout the day, rather than just at the end of the day. One of the main attractions of the RTGS systems is that payee banks and their customers receive funds with certainty, or so-called finality, during the day, enabling them to use the funds immediately without exposing themselves to risk. RTGS is a system where both the processing and final settlement takes place on real time basis. RTGS is regarded as the centerpiece of an integrated payments system. Settlement risk refers to the risk when a settlement (in a transfer system) does not take place as expected. This can happen due to various reasons, e.g. one party may default on its clearing obligations to one or more counter parties. Thus, settlement risk consists of two components namely credit and liquidity risks. Credit risk arises when a counter party fails to meet an obligation for full value on due date and thereafter

19. Statutory Reserve Ratio – Called in short SLR. In the above example, suppose the bank is supposed to maintain SLR of 24%, this means that over and above CRR the bank is expected to keep aside an amount of Rs. 25 Bn. This will be kept in easy-to-encash securities like, treasury bills of the government and any other approved securities. In India at present it is 25%. This again acts as buffer to the bank and prevents the bank from lending the entire amounts of deposits kept with it by various customers.

20. Stock & Receivables Audit is one of the most important aspects of the overall exercise of audit of any organization. In stock and receivable audit, auditor ensures himself about the quantity, quality, composition and actual

value of the stock and the debtors.

21. Syndication – Making arrangement for loans for borrowers. Should not be confused for granting of loans. The bank may or may not participate in the loan process, but would assume responsibility for getting “in principle” sanction from all participating banks and financial institutions. Syndication fees are part of non-interest income as no funds are involved in the activity. For example. An Indian company wants a foreign currency loan of 100 mn Rs. Making arrangement for this is known as syndication. Even if the arranging bank participates in the loan, by granting a portion of it, syndication is different from it. It gets paid separately for this activity.