

LAW RELATING TO E-BANKING IN INDIA – AN OUTREACH CHALLENGE

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ABSTRACT

Technology has entered into every sphere of the life and financial sector is no exception to them. Electronic banking is the talk of the day. Every transactions carried out by banks are computerized which has made working easier. Number of staff is reduced; most functions carried by man are now carried by machines. Moreover, globalization and liberalization of services has encouraged bankers to adopt new technology which even customer prefers. The risk associated with technology has complicated the story of introduction of e-banking. Numerous legislations deal with electronic banking and have tried to do away or minimize the risk associated with it. Apart from this there are also certain traditional obligations which the banker has to carry out even after introduction of electronic banking. To cope with all these issues Reserve Bank of India (RBI) has from time to time issued circulars and notification for the smooth functioning of banking. Yet there is much to do in this regard where the banker and the customer can talk about electronic banking without risk.

I INTRODUCTION

There is a saying that Rome was not built in a day, so is banking system of the World. Monetary policy of any country is directly related to economic development of the country where banks play major role. Information technology and communication networking systems have revolutionalised the working of banks and financial institutions all over the world. Banking has become more complex with the introduction of electronic banking. The convenience of e-banking has attracted the public at large all over the world. Banking services has reached rural people of India and has its working wing globalized. Thus is the complicatory story of e-banking; where there are advantages of

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numerous facilities offered due to digitalization, there are also plenty of obligations to be meted out by the banks. Banker has to act like a king and servant at the same time. He has to vigil and also be loyal to his customers. This dual play makes his job tough. E-banking has brought banking 24 hours and 7 days, where there is no need for the customer to visit banks personally.

E-banking is a product of the last century due to research conducted in the field of banking and financial services. The concept of e-banking has been simultaneously evolving with the development of the World Wide Web programmers working databases came up with the idea of online banking transactions sometime during the 1980s in Europe. They called this home banking. In 1983, the Nottingham building society commonly abbreviated and referred to as the Non Banking Service launched the first internet banking service in United Kingdom. The first online banking service in United States was introduced in 1994.

There are advantages and disadvantages of introduction of technology in banking system. The work of the law starts where there are disadvantages to the public in general and individual in particular. There are certain challenges banking is facing which are due to obligations imposed by law on the one hand and the invention of new technology and its adoption at the other. This necessitates introduction of new guidelines by the RBI. The theme of the paper rests on this matter.

II MEANING AND DEFINITION OF E-BANKING

E-banking is being used in India for some time now in the form of digital data in computers, credit and debit cards, Automated Teller Machines, Mobile Banking, net banking and internet banking.¹ Internet or e-banking means any user with a personal computer and a browser can get connected to his bank's website to perform any of the virtual banking functions.

E-banking has been defined in law lexicon as banking activities accessed by using a computer, employing modems and telephones.²

In e-banking, 'e' stands for electronic and the banking has been defined as 'an acceptance of money from the public, for purpose of lending or investment of money, which is withdrawable by cheque, draft or otherwise'³ and banking by using electronic devices is e-banking.

III FEATURES OF E-BANKING

The main features of e-banking are-

- In e-banking, banking functions are carried by using internet facility.

¹ B.R.Sharma, *Bank Frauds Prevention & Detection*, (3rd Ed.) (New Delhi: Universal Law Publishing Co. 2009), p 281

² P. Aiyar Ramnath , *Advanced Law Lexicon*, (4th Ed.) (Nagpur; Wadhwa and Co; 2013), p.1561

³ Section 6 of *Banking Regulation Act, 1949*

- It removes the traditional geographical barriers as it could reach customers at different counters/jurisdictions.
- E-banking facilitates banking transactions at all time and on the days including holidays and Sundays.
- It provides several additional delivery channels which are more convenient and cost effective to both customer and the banker.
- It is based on science and technology i.e. use of electronic devices which saves time and energy of banker and customer.
- Its special features lie in ensuring security of the transaction, customer's privacy and transparency of transaction.

IV SERVICES THROUGH E-BANKING

E-banking services are delivered to customers through the internet and web using Hypertext Markup Language (HTML). In order to avail e-banking facility, customer must have internet access and web browser software. Multimedia information in HTML format can be displayed through online web browsers. The heart of the e-banking application is the computer system, which includes web servers, database management systems and web application programmes that can generate dynamic html pages.

Bank customers' account and transaction information is stored in a database which is a specialized software that can store and process large amounts of data in high speed. The function of the web server is to interact with online customers and deliver information to users through internet. When web server receives a request such as an account inquiry from an online customer, it requires an external web application programme to process the request. C, Visual basic, VBS script and Java are some of the languages which are used to develop web application programmes to process customer requests interact with the database and generate dynamic responses. Then the web server will forward the response to HTML files to e-banking customers. Several banks also use state of the art imaging systems allowing customers to view images of cheques and invoices over the internet.

Services of e-banking includes-

1. **Information System-** General Information like interest rates, branch location, bank products and their features, loan and deposit features are provided in the bank website. There exist facilities for downloading various types of application forms like deposit application form, loan application form, etc. The communication is carried through e-mail, otherwise the person seeking information need not disclose his identity. Also there is no possibility of any unauthorized person getting into production systems of the bank through internet.⁴
2. **Electronic Information Transfer System-** The system provides customer with specific information in the form of account balances, transaction details and statement of accounts. The information is still largely of the 'read only' format.

⁴ Shekar K.C., *Banking Theory and Practice*, (20th Ed), (Mumbai; Vikas Publishing House Pvt Ltd, 2007), p.45

- Identification and authentication of the customer is through password. The information is fetched from the bank's application system either in batch mode or off-line. The application systems cannot directly access through the internet.⁵
3. **Fully Electronic Transactional System-** This system allows bi-directional capabilities. Transactions can be submitted by the customer for online update. This system requires high degree of security and control. In this environment, web server and application systems are linked to secure infrastructure. It comprises technology covering computerization, networking and security, interbank payment gateway and legal infrastructure.⁶
 4. E-banking services can be availed for payment of bill, fund transfer, credit card, railway and air ticket booking, investment, recharging phones and mobiles and shopping. Generally banks do not charge customers for providing certain services.⁷

V LEGAL PROVISIONS ON E-BANKING IN INDIA

India is a signatory of WTO. The basic principles of WTO are Liberalization, Globalization and Privatization. Therefore, trade and commerce in India has been liberalized. Incidentally, the financial sector has also undergone major changes. With the advent of e-banking, India is facing unprecedented competition from the World at large. If technology is not updated in financial sector, international trade would be a distant dream. The deregulation of the banking industry coupled with the emergence of new technologies has enabled new competitors to enter the financial services market quickly and efficiently. Various provisions of law, which are applicable to traditional banking activity, are also applicable to internet banking. This does not overcome the problems, and therefore there is a need for introduction of more stringent rules and laws specifically to meet the problems of e-banking.

The legal framework for banking in India is provided by a set of enactments, viz. *The Banking Regulation Act, 1949*, *the Reserve Bank of India Act, 1934* and *Foreign Exchange Management Act, 1999* are few among many such legislations. It is mandatory on the part of all entities to obtain a license from Reserve Bank of India under *Banking Regulations Act, 1949* to function as bank. Different types of activities which a bank may undertake and other prudential requirements are provided under this Act. Reserve Bank of India has regulated acceptance of deposit by Non Banking Institutions also. Under the *Foreign Exchange Management Act, 1999*, Non Residential Indians can lend, open a foreign currency account or borrow from a bank in India including from a Non-Resident bank, except under certain circumstances provided under the law. Besides, banking activities are also influenced by various enactments governing trade and commerce, such

⁵ *Ibid* at.46

⁶ http://www.iajet.org/iajet_files/vol.2/no.1/internet%20banking%20adoption%20in%20an%20emerging%20economy%20indian%20perspective.pdf retrieved on 5 May, 2011

⁷ Joga Rao s, *Computer Contracts and Information Technology Law*, (2nd Ed.), (Wadwa & Co; Nagpur, 2005), p.123

as, *Indian Contract Act, 1872*, the *Negotiable Instruments Act, 1881*, *Indian Evidence Act, 1872*, etc.⁸.

VI OBLIGATION OF BANKS AND THE ONLINE BANKING

There are certain obligations which the banker is supposed to fulfill. They are-

1. **Banks have to maintain secrecy of customers account**⁹. This obligation dates back to 1924 where in a case popularly known as *Tournier case*¹⁰, in which it was held that banker should not disclose customers financial position and the nature and the details of his account to anybody, since it may effect his reputation, credit worthiness and business. Now with the advent of new technology, this obligation has become a difficult task for there are hackers who can operate others account. Bankers are not in a position to trace them. They come to know only when the customer informs them of some irregularity in their transaction. Hence, to meet out this obligation, banks have to update their technology to the requirement.
2. **Banks are also under obligation (public duty), to produce documents to the court whenever called for.**¹¹ In earlier days this was easy as the documents were either in printed or in written form and readily available with the banks. Banks keep these information's in electronic form as it is easier and cheaper to store and retrieve and also ensures speedier communication/transmission. *Information Technology Act, 2000* was drafted to facilitate users of electronic communication similar to other paper based or oral testimony means. Records can be kept in electronic form. Electronic form means information generated, sent, received or stored in media, magnetic, optical, computer memory, micro film, etc. Now in the eyes of law written records means electronic records which can be produced before the court like it was produced previously.¹² But banks have to reproduce the documents and store them properly. If the software is attacked with virus it washes of all the documents. Hence, banks have to carefully handle the electronic documents or else they will be accountable to the law.
3. **Obligation to verify forgery of signatures**¹³. Banks have to verify the signature of the customer before paying their cheques. This obligation is on the paying banker. The law is very strict; and in case of forgery the banker is liable. This is limited to traditional banking. Introduction of new technology has helped banker in storage and retrieval of signature of customers. Each signature card is scanned using a scanner that takes images of the signature and converts it into digital form which are then stored in the hard disk. When

⁸ M.L.Tannan, Tannan's, *Banking Law and Practice in India*, (20th Ed.), (New Delhi: India Law House, 2003), p.157

⁹ Section 13 of *Banking Companies (Acquisition and Transfer of Undertaking) Act, 1970*.

¹⁰ *Tournier v. National Provincial & Union Bank of England*, (1924), K.B., 461.

¹¹ Section 4 of *Bankers Books Evidence Act, 1891*.

¹² R.N.Chaudhary, *Banking Laws*, (1st Ed.), (New Delhi: Central Law Publications, 2009). p.377.

¹³ Section 89 of the *Negotiable Instruments Act, 1881*.

a cheque (traditional) is received for payment, the signature can be retrieved by the user. What when the funds are transferred electronically? In case of electronic fund transfer, digital signatures are used which are in the form of code. These signatures are in electronic form attached to electronic record. The obligation of the banker to verify the signature is continuing here for digital signature. Hence, the banker should adopt technology which can identify the sender by recognizing message originator, authentication and non-reputable that affixes a coded message to the document. It is used to sign the record. Banker has to maintain records of the digital signature and also educate the customer in this regard.

4. **The other obligation on the banker is to provide proper service to the customer.** Otherwise the bank is answerable. Not providing proper service attracts Consumer Law which amounts to deficiency in providing service. It has been held in *Vimal Chandra Grover v. Bank of India*,¹⁴ that banking is a business transaction of a bank and customers of a bank are consumers within the meaning of Section 2(1) (d) (ii) of the Act. This obligation extends to electronic banking also.

VII RBI CIRCULAR TO CONTROL RISK DUE TO INTERNET BANKING

The Reserve Bank of India has issued New Circular to Internet Banking. The Reserve Bank of India as a supervisor, will cover the entire risks associated with electronic banking as a part of its regular duty. It is the statutory duty on every bank that they should develop a clear Customer Acceptance Policy laying down explicit criteria for acceptance of customers. The Customer Acceptance Policy must ensure that explicit guidelines are in place on the following aspects of customer relationship in the bank.¹⁵

- ❖ No account should be opened in anonymous or fictitious/benami name¹⁶. Banks should not allow the opening of or keep any anonymous account or accounts in fictitious name or account on behalf of other persons whose identity has not been disclosed or cannot be verified.
- ❖ Parameters of risk perception are clearly defined in terms of the nature of business activity, location of customer and his clients, mode of payments, volume of turnover, social and financial status etc., to enable categorization of customers into low, medium and high risk¹⁷. Customers requiring very high level of monitoring, may, if considered necessary, be categorized even higher;
- ❖ Banks can effectively control and reduce their risk only if they have an understanding of the normal and reasonable activity of the customer so that they have the means of identifying transactions that fall outside the regular pattern of activity. However, the extent of monitoring will depend on the risk sensitivity of

¹⁴ AIR. 2000 SC 2181.

¹⁵ RBI Vide Circular DBOD. AML. BC. No. 11/14.01.001/2012-13

¹⁶ Government of India Notification dated June 16, 2010 Rule 9, sub-rule (1C)

¹⁷ Banks may choose any suitable nomenclature viz. level I, level II and level III

the account. Banks should pay special attention to all complex, unusually large transactions and all unusual patterns which have no apparent economic or visible lawful purpose. Banks may prescribe threshold limits for a particular category of accounts and pay particular focus on these transactions which exceed the stated limits. A transaction that involves large amounts of cash inconsistent with the normal and expected activity of the customer should particularly attract the attention of the bank. Very high account turnover inconsistent with the size of the balance maintained may indicate that funds are being 'washed' through the account. High-risk accounts have to be subjected to intensified monitoring. Every bank should set key indicators for such accounts, taking note of the background of the customer, such as the country of origin, sources of funds, the type of transactions involved and other risk factors. High risk associated with accounts of bullion dealers (including sub-dealers) & jewelers should be taken into account by banks to identify suspicious transactions for filing Suspicious Transaction Reports (STRs) to Financial Intelligence Unit- India (FIU-IND) Banks should put in place a system of periodical review of risk categorization of accounts and the need for applying enhanced due diligence measures. Such review of risk categorization of customers should be carried out at a periodicity of not less than once in six months.

- ❖ The banks have to monitor the accounts of Multi-Level Marketing (MLM) Company's accounts which lure public money on a promise of high returns. They issue post dated cheques for interest and principal money. Once deposits from public stop the chain breaks and the cheques are dishonoured. Hence, banks should carefully analyse in cases where they find unusual operations in accounts when large number of cheques are issued bearing similar dates/amounts. The banks should intimate the matter to the RBI and the Financial Intelligence Unit India.
- ❖ Banks' internal audit and compliance functions have an important role in evaluating and ensuring adherence to the KYC policies and procedures. As a general rule, the compliance function should provide an independent evaluation of the bank's own policies and procedures, including legal and regulatory requirements. Banks should ensure that their audit machinery is staffed adequately with individuals who are well-versed in such policies and procedures. Concurrent/ Internal Auditors should specifically check and verify the application of KYC procedures at the branches and comment on the lapses observed in this regard. The compliance in this regard should be put up before the Audit Committee of the Board on quarterly intervals.
- ❖ Banks should pay special attention to any money laundering threats that may arise from new or developing technologies including internet banking that might favour anonymity, and take measures, if needed, to prevent their use in money laundering schemes. Many banks are engaged in the business of issuing a variety of Electronic Cards that are used by customers for buying goods and services, drawing cash from ATMs, and can be used for electronic transfer of funds. Banks are required to ensure full compliance with all KYC/AML/CFT guidelines issued from time to time, in respect of add-on/ supplementary cardholders also. Further, marketing of credit cards is generally done through the services of agents. Banks

should ensure that appropriate KYC procedures are duly applied before issuing the cards to the customers. It is also desirable that agents are also subjected to KYC measures.

❖ Wire transfer is an instantaneous and most preferred route for transfer of funds across the Globe. Hence, there is a need for preventing terrorists and other criminals from having unfettered access to wire transfers for moving their funds and further for detecting their misuse. This can be achieved if basic information on the originator of wire transfers is immediately available to appropriate law enforcement and/or prosecutorial authorities in order to assist them in detecting, investigating, prosecuting terrorists or other criminals and tracing their assets. The information can be used by Financial Intelligence Unit - India (FIU-IND) for analyzing suspicious or unusual activity and disseminating it. The originator information can also be put to use by the beneficiary bank to facilitate identification and reporting of suspicious transactions to FIU-IND. Owing to the potential terrorist financing threat posed by small wire transfers, the objective is to be in a position to trace all wire transfers with minimum threshold limits. Accordingly, banks must ensure that all wire transfers are accompanied by the following information:-

- All cross-border wire transfers must be accompanied by accurate and meaningful originator information.
 - Information accompanying cross-border wire transfers must contain the name and address of the originator and where an account exists, the number of that account.
 - Where several individual transfers from a single originator are bundled in a batch file for transmission to beneficiaries in another country, they may be exempted from including full originator information, provided they include the originator's account number or unique reference number as at (ii) above.
- ❖ The banks are required to maintain records of transaction and whenever a suspicion arises inform it to Financial Intelligence Unit India.¹⁸ There is an obligation on the banking companies to preserve and report customer account information to Financial Intelligence Unit India and the banks should take all steps to ensure the compliance.¹⁹
- ❖ Banks are required to maintain and preserve all necessary information in respect of transactions referred to and permit reconstruction of individual transaction, including the following information:
- the nature of the transactions;
 - the amount of the transaction and the currency in which it was denominated;
 - the date on which the transaction was conducted; and
 - the parties to the transaction

¹⁸ Government of India, Vide notification dated July, 2005 under *Prevention of Money Laundering Act, 2002*.

¹⁹ Section 12 of *Prevention of Money Laundering Act, 2002*

- ❖ Report all suspicion transactions to RBI.

The RBI has instructed all banks to adopt the circular in spirit and words and if they are unable to adopt send a 'nil' report.

VIII CONCLUSION & SUGGESTIONS

E-banking is changing the banking industry and is causing major effects on banking relationships and its working nature. E-banking involves use of internet for delivery of banking products and services.

Advantages previously held by large financial institutions have shrunk considerably. The internet has leveled the playing field and afforded open access to customers in the global marketplace. E-banking is a cost effective delivery channel for financial institutions. Consumers are embracing many benefits of E-banking. Access to one's account at anytime and from anywhere via World Wide Web is a convenient style. Thus, a bank's internet presence transforms from 'broucherware' status to 'E-banking' status once the bank goes through a technology integration plan which enables the customer to access information about his or her specific account relationship. The six primary drivers of e-banking includes, in order of primacy are:²⁰

1. Improve customer access.
2. Facilitate the offering of more services.
3. Attract new customers.
4. Provide services offered by competitors.
5. Reduce customer attrition.

A multi-layered security architecture comprising firewalls, filtering routers, encryption and digital certification ensures that customers account information is protected from unauthorized access.

Apart from this, the Reserve bank of India has issued circular²¹ for the convenience of working with electronic banking as there is a steep rise in the risk involved due to internet banking. The need of the hour is to meet the global challenge of providing different services to customers and also keeping vigil eye, to curtail the risk arising due to e-banking.

In the light of above discussion over the matter, the researcher warrants to make certain suggestions-

1. Banks are under obligation to maintain secrecy of customers account²². The new RBI new circular has given guidelines to minimize risk of hacking. However, it is the duty on the banker to adopt technology to discharge his duty in a more effective manner. Reserve Bank of India should also ensure that the banks are

²⁰ <http://www.banknetindia.com/banking/ibkg.html> retrieved on 21/02/2011

²¹ *Supra* note 15

²² *Supra* note 9

- using new technology. The RBI should appoint technicians and ask them to report the same under security policy.
2. The auditor appointed²³ to inform as the misappropriation of funds even at the minutest level. Electronic banking has enhanced the risk of misappropriation of funds by the bankers as it goes undetected.
 3. The Automatic Teller Machine is widely used today. It is observed that these machines fail frequently and causes inconvenience to the customer. RBI in its next circular has to mention the number of times banks are not penalized for such failures. After a particular limit the banks should pay penalty which alerts them to keep check on the working of the machine.

Speedier and cheaper justice is the hallmark of the Consumer Protection Act and as discussed above the Act is application to banking service also. The scope of the Act should be extended specifically to electronic banking also in cases of frequent failure of ATM machines, non compliance of security which results in hacking, and exuberant charges levied by bank for fund transfer, etc. Though these are covered under RBI circular, they should be brought within the purview of the legislation, which will be convenient to customers.

²³ Section 35 of *RBI Act 1935*.