DEPOSIT INSURANCE IN LIGHT WITH THE JASBIR SINGH COMMITTEE REPORT: AN ANALYSIS

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CHAPTER 1- INTRODUCTION

Deposit insurance is a protection cover available for bank depositors if the bank fails financially and go for liquidation. In India, the deposit insurance activity is done by an RBI subsidiary called Deposit Insurance Corporation. All types of deposits such as savings deposits, term deposits are covered by deposit insurance corporation or DICGC. But, some institutional deposits are not covered. Also, deposits of all banks (except primary cooperative societies up to one lakh is covered under this scheme. DICGC is fully owned by the Reserve Bank of India. It has been constituted under the Deposit Insurance and Credit Guarantee Corporation Act of 1961. Deposit insurance is mandatory for all banks. The premium charged is on flat rate basis which is 10 paisa per 100. The amount of coverage is presently limited to five lakhs. Also a deposit insurance fund is build up from the premium received from insured banks and the coupon received from investment in central government securities. In case of event of a bank failure, DICGC protects bank deposits that are payable in India. The DICGC insures all deposits such as savings, fixed, current, recurring etc. But there are various challenges generally faced by the deposit insurance scheme in India, which could be broadly classified into challenges from governance and structure, operational and sectoral. In order to find out these challenges and provide solutions to them, a committee was constituted under the leadership of Jasbir Singh who was the then executive director of the DICGC and a report has thus been created on differential premium system. This research project is concentrated on what are the major challenges associated with the deposit insurance scheme as pointed out by the committee report and the solutions provided by them and how to frame an alternate model on the basis of it.

RESEARCH PROBLEM

Deposit Insurance plays a very pivotal part for those people who put on their trust in depositing their monetary assets in the bank. Hence, it is the duty of the authorities associated with the

deposit insurance sector in India to create a transparent, efficient and systematic deposit insurance regime. But there are many problems associated with the deposit insurance scheme in India in most aspects, including the structural, operational and sectoral. A committee report has been formed on the leadership of Jasbir Singh, the former executive director of Deposit Insurance and Credit guarantee corporation in India. On the basis of the report thus formulated, how the deposit insurance scheme in India can be rejuvenated by rectifying the current problems, thus altering the existing model?

LITERATURE REVIEW

RESEARCH QUESTIONS

1. The concept of deposit insurance and institutionalization to guarantee such has been prevalent in the world much before it came into force in independent India. How, the concept of deposit insurance and institutionalization of it has evolved in global and Indian Scenario?
2. The Deposit insurance scheme in India has its positives and negatives. What are the various advantages and drawbacks of the deposit insurance regime in India and how far the functioning of it has been effective?
3. How far the Jasbir Committee Report rectify the problems of deposit insurance scheme in India?

HYPOTHESIS

The Jasbir Committee report on Differential Premium system of banks recommend risk based deposit insurance rather than the flat rate based so that it would be more secured for the depositors.

SCOPE AND OBJECTIVE

The scope of this research project is narrowed down to the ambit of problems and solutions identified by the Jasbir Singh committee report regarding the deposit insurance scheme in India. The objective of this research is try creating an alternative model regarding the deposit insurance scheme in India with the aid and assist of the Jasbir Singh Committee Report. The Research is thus limited to the purview of the Jasbir Singh Committee report and suggestions by it rather than adapting any other suggestions and mechanisms regarding deposit insurance provided elsewhere.

RESEARCH METHODOLOGY

The research methodology that has been used in this research project is doctrinal research method along with qualitative approach, as the research is mostly focused upon non numerical data. The primary resources used in this research are statutes and case laws. The major secondary source used in this research is Jasbir Singh Committee Report regarding deposit insurance in addition to online articles, journals, books etc.

CHAPTER 1: EVOLUTION OF DEPOSIT INSURANCE

1.1 EVOLUTION OF DEPOSIT INSURANCE IN INDIA

Deposit insurance, as we know it today, was introduced in India in 1962. India was the second country in the world to introduce such a scheme - the first being the United States in 1933. Banking crises and bank failures in the 19th as well as the early 20th Century (1913-14) had, from time to time, underscored the need for depositor protection in India. After the setting up of the Reserve Bank of India, the issue came to the fore in 1938 when the Travancore National and Quilon Bank, the largest bank in the Travancore region, failed. As a result, interim measures relating to banking legislation and reform were instituted in the early 1940s. The banking crisis in Bengal between 1946 and 1948, once again revived the issue of deposit insurance. It was, however, felt that the measures be held in abeyance till the Banking Companies Act, 1949 came into force and comprehensive arrangements were made for the supervision and inspection of banks by the Reserve Bank.

It was in 1960 that the failure of Laxmi Bank and the subsequent failure of the Palai Central Bank catalysed the introduction of deposit insurance in India. The Deposit Insurance Corporation (DIC) Bill was introduced in the Parliament on August 21, 1961 and received the assent of the President on December 7, 1961. The Deposit Insurance Corporation commenced functioning on January 1, 1962.

The Deposit Insurance Scheme was initially extended to functioning commercial banks. Deposit insurance was a measure of protection to depositors, particularly small depositors, from the risk of loss of their savings arising from bank failures. The purpose was to avoid panic and to promote greater stability and growth of the banking system - what in today's argot are termed financial stability concerns. In the 1960s, it was also felt that an additional the purpose of the scheme was to increase the confidence of the depositors in the banking system and facilitate the mobilisation of deposits to catalyst growth and development.

When the DIC commenced operations in the early 1960s, 287 banks registered with it as insured banks. By the end of 1967, this number was reduced to 100, largely as a result of the Reserve Bank of India's policy of the reconstruction and amalgamation of small and financially weak banks to make the banking sector more viable. In 1968, the Deposit Insurance Corporation Act was amended to extend deposit insurance to 'eligible co-operative banks'. The process of extension to cooperative banks, however, took a while it was necessary for state governments to amend their cooperative laws. The amended laws would enable the Reserve Bank to order the Registrar of Co-operative Societies of a State to wind up a co-operative bank or to supersede its Committee of Management and to require the Registrar not to take any action for winding up, amalgamation or reconstruction of a co-operative bank without prior sanction in writing from the Reserve Bank of India. Enfolding the cooperative banks had implications for the DIC - in 1968 there were over 1000 cooperative banks as against the 83 commercial banks that were in its fold. As a result, the DIC had to expand its operations very considerably.

The 1960s and 1970s were a period of institution building. 1971 witnessed the establishment of another institution, the Credit Guarantee Corporation of India Ltd. (CGCI). While Deposit Insurance had been introduced in India out of concerns to protect depositors, ensure financial stability, in still confidence in the banking system and help mobilise deposits, the establishment of the Credit Guarantee Corporation was essentially in the realm of affirmative action to ensure that the credit needs of the hitherto neglected sectors and weaker sections were met. The essential concern was to persuade banks to make available credit to not so creditworthy clients.

In 1978, the DIC and the CGCI were merged to form the Deposit Insurance and Credit Guarantee Corporation (DICGC). Consequently, the title of Deposit Insurance Act, 1961 was changed to the Deposit Insurance and Credit Guarantee Corporation Act, 1961. The merger was with a view to integrating the functions of deposit insurance and credit guarantee prompted in no small measure by the financial needs of the erstwhile CGCI.

After the merger, the focus of the DICGC had shifted onto credit guarantees. This owed in part to the fact that most large banks were nationalised. With the financial sector reforms undertaken in the 1990s, credit guarantees have been gradually phased out and the focus of the Corporation is veering back to its core function of Deposit Insurance with the objective of averting panics, reducing systemic risk, and ensuring financial stability.

In DICGC .v. Raghupathi Raghavan and others[1], it was held that an official liquidator must be appointed in consensus of both parties while solving a deposit insurance deposit.

In DICGC .v. Sunita Haribahu Joshi[2], it was held that without the merits of the insurance claim proven, it cannot be claimed.

1.2 EVOLUTION OF DEPOSIT INSURANCE: A GLOBAL SCENARIO

The recent studies of deposit insurance funds have focused on the perverse incentives created by deposit insurance when it is not priced. Insurance encourages excess risk-taking by existing banks-particularly if prior losses leave them with little capital to lose from pursuing long shots-and allows unscrupulous, or simply inexperienced, entrepreneurs to enter banking to finance their risky enterprises. The discipline of the market, which normally would prevent such intermediaries from having access to funds, is removed by insurance. Depositors of insured institutions have little incentive to discriminate with respect to where and with whom they place their funds.

Renewed discussion of the purpose and proper structure of deposit insurance has focused attention on the history of financial intermediaries and their regulation. U.S. financial history contains the answers to three fundamental questions of interest to would-be reformers. Why was bank liability insurance created in the first place? What evidence supports this presumed "special" need of banks? Which experiments with insurance were most successful, and which aspects of these experiments account for the accomplishment of legitimate goals? The answer to the first question is similar across various historical instances-bank insurance was instituted to protect the economy's payments system from financial panics. Recent theoretical work on banking echoes this theme.

Banks are especially vulnerable because they offer short-term (typically demandable) claims backed by longer- term assets whose value is not easily observable to depositors. Thus, banks are vulnerable to panics induced by depositors' uncertainty about the value of their portfolios. Disturbances that increase the probability of insolvency of some class of bank borrowers-even if they are small relative to aggregate bank assets and concentrated in only a few banks-can provoke widespread disintermediation from all banks by depositors who lack information about the incidence or degree of the shock.

[1] Civ Appeal No. 5333 of 2012
[2] Civil Appeal no.2554 of 2010

Bank insurance was not exclusively the domain of the government historically. The information externality created by depositors' confusion about the precise incidence across banks of a given shock prompted private coinsurance among banks to reduce the potential for disinter- mediation and to coordinate the banking system's response to such crises when they did occur. Formal coinsurance arrangements among bank clearinghouse members, and less formal arrangements among other banks-especially in the branch-banking states of the antebellum South-provided many of the features of government deposit insurance. In these private insurance regimes banks agreed to make markets in each other's liabilities, to make interbank loans, and to coordinate suspensions and resumptions of convertibility to minimize disruptions during panics. In all cases, self-imposed regulations and mutual monitoring kept members of the privately established coalitions from "free riding" on the collective insurance.

Historians long have stressed the destabilizing influence of unit banking and linked its peculiar prevalence in the United States to the unique vulnerability of U.S. banking historically. Indeed, studies of the political history of deposit insurance legislation show that it was the desire to preserve unit banking, and the political influence of unit bankers, that gave rise to the perceived need for deposit insurance, both in the antebellum period and in the twentieth century. It was under- stood early on (through observing the successful operation of branch banks in the South and in other countries) that branching-with its benefits both of greater diversification and coordination-provided an alternative stabilizer to liability insurance. But unit banks and their supporters successfully directed the movement for banking reform toward creating government insurance funds. All six antebellum states that enacted liability insurance were unit-banking states. In the antebellum branch-banking South neither government insurance, nor urban clearinghouses, developed. Similarly, the eight state insurance systems created from 1908 to 1917 were all in unit-banking states.

New York's Safety Fund was established in 1829, funded by limited annual contributions of members and regulated by the state government. Losses severely depleted the accumulated resources of the fund from 1837 to 1841 until, in 1842, it ceased to be able to repay losses of failed banks and thus ceased to provide protection to the payments system. New York in 1838 created an alternative to the insured system through its free banking statute and allowed Safety-Fund banks to switch to that system. The depletion in membership of the insured system kept its losses small during subsequent panics. After 1840 Safety-Fund banks comprised a small and continually shrinking proportion of total banks or total bank assets. Losses were also limited by the 1842 restriction on coverage of member banks' liabilities to bank notes, thus

excluding the growing liability base in deposits. Ultimately the small number of banks that chose to remain in the system and make continuing annual contributions to its fund did manage to repay in 1866 the obligations incurred some thirty years earlier, but this "success" was not anticipated in the intervening years (as shown by the high note discount rates attached to failed member-banks' notes during the 1850s), and the fund did not protect current bank liabilities or the payments system ex ante, as it was intended to do. Not only did the system fail to provide protection to the payments system, it suffered unusually large losses due to fraud or unsound banking practices. While a supervisory authority was established to prevent fraud and excessive risk-taking, supervision was ineffectual, and fraud or unsafe practices were common. Ten of 16 member-bank failures prior to 1842 (the period when insurance was still perceived as effective) were traceable to fraud or unsafe practices. Moreover, such problems were not detected until after they had imposed large losses on the fund. The failure of the Safety Fund was not the fault of external shocks, severe as they were. In aggregate, banking capital was large relative to losses, and thus coinsurance among all New York banks would have been feasible. Rather it was the design of the insurance system that made it weak. Upper bounds on annual premia prevented adequate ex ante insurance during panics, and ineffectual supervision allowed large risk-takers to free ride on other banks. Finally, adverse selection caused a retreat from the system through charter-switching to the alternative free-banking system once solvent banks realized the extent of losses.

The eight deposit-insurance fund systems of the early twentieth century failed to learn the lessons of the antebellum experience; they repeated and compounded the earlier errors of New York, Vermont, and Michigan. Supervisory authority was placed in government, not member-bank, hands, and often its use or disuse was politically motivated. Furthermore, the numbers of banks insured were many more than in the antebellum systems (often several hundred), and this further reduced a bank's incentive to monitor and report the misbehaviour of its neighbour banks, since the payoff from detection was shared with so many, and the cost of monitoring was private. During the halcyon days for agriculture, from 1914 to 1920, deposit insurance prompted unusually high growth, particularly of small rural banks on thin capital. The insured states' banks grew faster, were smaller, and had lower capital ratios than their state-chartered counter- parts in fast-growing, or neighbouring states.

Reformers of current deposit insurance plans might apply the lessons of the successful antebellum insurance programs by creating a greater role for incentive-compatible self-regulation and coinsurance among banks. Today's futures clearinghouses, which regulate

members' risks and provide incentive-compatible liquidity coinsurance, also success- fully apply this principle.

A role remains for the government, however, in regulating bank insurance programs. At the very least the government should ensure freedom of entry into co-insuring groups of banks and competition among groups. In a unit-banking scenario, the need for many groups dictates special attention to potential problems of local market monopolization. In contrast, today's futures clearinghouses can rely on national, and soon international, competition to limit the power of any group.

One might also argue, notwithstanding the evidence from the 1920s reported here, that government should provide some stop-gap protection against systemic collapse of the banking system-that is, shocks greater than those that could be absorbed by bank capital. To this end the government might establish an insurance plan with a "deductible." For example, coinsurance among banks would be relied on entirely for reimbursing depositors of the first banks that failed; the government would share increasingly in subsequent losses of failed banks. This would provide the incentives for interbank discipline and for market discipline of banking coalitions without risking systemic collapse. Moreover, since it is likely that the government will intervene in such crises even without an explicit commitment to do so, it would be best to have that commitment spelled out. This would limit Congressional intervention to serve constituents' interests.

Absent the political feasibility of fully self-regulating, co-insuring groups of banks, some smaller steps could be taken to reduce the costs of government deposit insurance by enlisting the assistance of banks in the supervision process. For example, banks could be assigned to groups, and banks within a group could be penalized (with higher insurance premia) for failing to detect and report violations or insolvency of other banks in the group. At the very least this would provide a strong counterbalance to political encouragement of excessive "forbearance" by creating an interest group that would have an incentive to monitor banks and "blow the whistle" early on insolvent institutions.[3]

[3] Calomiris, C. W. (1990). Is deposit insurance necessary? A historical perspective. Journalof Economic History, pp 283-295

CHAPTER 2: POSITIVE AND NEGATIVE ASPECTS OF DEPOSIT INSURANCE SCHEME

2.1 THE ADVANTAGES OF DEPOSIT INSURANCE

Deposit insurance is an insurance program that insures peoples' bank deposits in case of bank failure or a run on the bank. During the period of last two decades financial markets across the world have been frequently plagued by instabilities and banking crises, giving the rise to the global trend of instituting explicit deposit insurance schemes. Deposit insurance programs for banking industries have been shown to facilitate additional economic stability by insuring a sound, competitive banking system, which is critical to a nation's economic vitality.

2.1.1 ADVANTAGES TO INDIVIDUALS

The biggest advantage of deposit insurance to individuals is the peace of mind in knowing that their deposits are not going to become inaccessible if their bank becomes illiquid or insolvent. This means that people are more inclined to put money into their bank rather into other investments or under their bed. It also helps people on a society-wide basis. If more people put money into the bank, then the bank has more funds to access. This means it has more funds to lend, which in turn lowers interest rates.

2.2.2 ADVANTAGES TO BANKS

Banks, like all businesses, cannot function without an influx of cash. They get this cash from people lending them money at low interest rates in the form of savings and checking accounts. If people lost faith in banks, they would put their money elsewhere, buying commodities, investing in property or simply hanging onto cash. This would render banks insolvent and they would go out of business.

Banks also benefit from the protection that deposit insurance offers. If they make too many bad investments, or leverage themselves too much and end up failing, they do not necessarily go bankrupt.

Deposit insurance systems are designed to minimize or eliminate the risk that depositors placing funds with a bank will suffer a loss. Deposit insurance thus offers protection to the deposits of households and small business enterprises, which may represent life savings or vital

transactions balances.[4]

2.2 DRAWBACKS OF DEPOSIT INSURANCE

This sense of public assurance is important. Public concern about the safety of deposits whether based on fact or only on rumor can lead, and has led, to the aforementioned damaging bank runs that can cause banks that are otherwise sound to fail. Similarly, concerns about one bank have at times led to concerns about others, resulting in so-called "contagion runs". Public confidence in the safety of bank deposits, in contrast, promotes the stability of individual banking institutions. Public confidence reduces the likelihood that depositors at an individual bank will panic and withdraw funds suddenly if concerns arise about the condition of that institution. Thus, deposit insurance can enhance stability by preventing bank runs.

It is easy to underestimate the value of deposit insurance when times are good. When times are bad, governments often re-evaluate the need for such arrangements. Typically, deposit insurance systems are adopted in the aftermath of severe banking crises or when industry conditions are deteriorating and unstable. A recent IMF survey of deposit insurance systems in 60 countries indicated that 40 of these systems were initiated during the 1980s and 1990s, largely in response to actual banking problems or the perceived threat of instability.

2.3 EFFECTS OF DEPOSIT INSURANCE SYSTEM

By providing a guarantee that depositors not subjected to loss, deposit insurance has two somewhat contradictory effects. On the positive side it removes the incentive to participate in a bank run, while on the negative side it eliminates the need for depositors to police bank risk taking. Public confidence in the safety of bank deposits promotes the stability of individual banking institutions. Public confidence reduces the likelihood that depositors at an individual bank will panic and withdraw funds suddenly if concerns arise about the condition of that institution[5]. Thus, deposit insurance can enhance stability by preventing bank runs.

While deposit insurance systems contribute to stability and thereby promote economic growth, they can also generate perverse effects.

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[4] Demirguc-Kunt, A., Kane, E. J., &Laeven, L. (2008).Determinants of deposit-insurance adoption and design. Journal of Financial Intermediation, 17, 407-438

[5] (Nicholas J. Ketcha Jr., 2007).

With their deposits protected against loss, insured depositors have little incentive to monitor bank risk-taking and may simply seek the highest return possible on their deposits. Thus, deposits may tend to flow away from conservatively managed institutions toward those willing to pay higher returns by assuming more risk. Supervision and regulation of insured institutions, as well as some degree of market oversight, are essential for controlling moral hazard in order to maintain safety and soundness.

2.3.1 BANKING SUPERVISION AND REGULATION

Deposit insurance program because of reduced market discipline and increased moral hazard at depositories has intensified the need for supervisory authorities to supervise and regulate banks. . Regulations have a purpose to prevent bank management from undertaking activities that excessively increase risk to the detriment of existing depositors and creditors or the insurance fund. Capital requirements serve to reduce the incentives of owners to increase risk since, the greater the amount of capital, the larger is the owner's loss in the event of failure.

The specifics of bank supervision and regulation will vary from nation to nation given their institutional, cultural, historical and legal differences, but the basic goals are quite similar maintaining public confidence in the banking system, protecting depositors funds, fostering an efficient and competitive banking system and insuring compliance with banking laws and regulations. In this regard, bank supervision, examinations and regulations provide effective mechanisms for limiting excessive risk-taking by banks. Effective supervision is aimed at ensuring stability in the banking system, which in turn, allows banks to reform their various roles effectively.

There are certain recommendations on Working Group on Reforms in Deposit Insurance

• Aimed at improving functioning and efficiency: Introduction on of Risk Based Premium; Enhancing statutory ceiling on premium rate; altering priority of the Corporation; accountability regime in the system; qualification criteria f or membership

• Aimed at improving Financial Strength: Enhancement in authorized capital; income tax exemption; robust back- up funding support.

Deposit insurance schemes can help to maintain financial stability, thereby enabling banks to intermediate effectively and support economic growth. As with other components of the safety net, however, deposit insurance can create perverse effects. The potential for hazard,

misallocation of resources, and excessive regulatory burden point to the need for appropriate balance in designing deposit insurance systems. It is important to note that there is not a "one size fits all" approach for any of the important elements in the deposit insurance system. Institutional, cultural, historical and legal differences among countries will dictate certain differences in the design of the deposit insurance system as well as in the other elements of the nation's financial safety net.[6]

CHAPTER 4: JASBIR SINGH COMMITTEE REPORT; A PATHBREAKER IN DEPOSIT INSURANCE REGIME OF INDIA

Deposit insurance collect demandable deposits and raise fund in the short term markets and invest them in long term assets. This maturity mismatch allows the depositors to offer risk sharing to depositors but also allows them to withdraw the money early. It prevents crises and allows the economy to reach optimal allocation without any costs. Although accompanied with these benefits, the scope of deposit insurance is quite narrow and is mostly relied upon restrictive assumptions.[7] In India, deposit insurance is regulated by the Deposit Insurance and Credit Guarantee Corporation Act, through which a corporation has been established for the purpose of insurance of deposits and guaranteeing of credit facilities and for other matters and connected therewith or incidental therewith. The Act was incorporated in 1961 where in which within a span of five decades, there were problems arising in the deposit insurance regime India. Henceforth the Jasbir Singh Committee made some suggestions to solve the problems associated with the deposit insurance scheme and tried to create an alternate model of it.

This report lays down the moral hazard that has happened to the deposit insurance regime in India due the recession happened in 2008 as the major reason for the creation of this committee report. The report aims to devise and recommend a model of risk assessment for banks, both co operative and commercial. For that purpose, the international methodology followed by different countries of risk based premium ensuring the insurance rating system has been adapted in this model. By implementing the report, it aims to create a robust and simple model with both quantitative and qualitative aspects equally weighed, with a good predictive power.

The committee aims to introduce the risk based premium system instead of the flat rate system

[6] Nicholas J. Ketcha Jr., "Deposit Insurance System Design and Considerations", Bank for International Settlement, Policy Papers, 2007 http://www.bis.org/publ/plcy07o.pdf

[7] Allen Franklin, Carletti Elena, Leonello Agnesse, "*Deposit insurance and Risk Taking*"(2011) Oxford Review of Economic Policy Vol. 27 Issue 3

which was adapted by various countries and having a comparative study between the various countries following risk based premium system. The reason behind such a shift is that flat rate deposit insurance shelters banks from the true level of risk taking and encourages poor undertaking and moral hazards. Risk based deposit can prevent bank failures more than the flat rate based premiums. The committee finds out that premium differentiation among banks is done in such a way that there it does not measure the exact risk but will have a comparative aspect on how the differential premium scheme in deposit insurance is regulated in each bank. Thus, instead of having a flat rate system, the committee proposes to introduce a premium system on differential basis regarding the stature of the banks.

Further, the committee has made about thirty recommendations in creating a model for revamping the deposit insurance sector in India. The important points that could be pointed out while considering these recommendations are;

1. A simple model of deposit insurance is suggested by the committee which places reliance on international practices, where the committee recommends that number of categories of assigning premium rates should not exceed four to five.[8]
2. The committee recommends that any model on which the banks could be rated should have predictive power of risk of insured banks.[9]
3. The committee insists that the corporation should utilize the supplementary information available from sources easily available, to upgrade the market intelligence of general well being of the member banks and also to use the information to validate the corporation's assessment on banks.[10]
4. The committee suggests that for a newly started bank, such bank may be assigned a premium category corresponding to base premium rate till it produces its first financial accounts.[11]
5. In case of merger situations of banks , the committee recommends that merging entity will pay the pay the premium till the deregistration by the corporation and in case of providing incentives for a better rating, the committee provides that premium rates should move in a curvilinear position.[12]

[8] Para 3.7, Report of the committee on Differential premium system for Banks in India, 2015
[9] Para 3.9, Report of the committee on Differential premium system for Banks in India, 2015
[10] Para 3.12, Report of the committee on Differential Premium system for Banks in India, 2015
[11] Para 3.14, Report of the committee on Differential premium system for Banks in India, 2015
[12] Para 3.16, Report of the committee on Differential premium system for Banks in India, 2015

6. The committee aims to bring up a pro cyclicality in premium rates reset with the intention of collecting higher period during the performance for the faster build up of Reserve fund ,or lower premium during period of stress. This committee also suggests the key characterstics of rating model to be published in the Pubic domain.[13]
7. The committee suggests that the rating must only be known to a key person and should not be used for any other purpose like business of its own, or canvassing funds etc.[14]
8. The committee recommends capturing risk through various sub ingredients to obtain higher objectivity.[15]

4.2 AFTERMATH OF THE JASBIR SINGH COMMITTEE REPORT

4.2.1 THE FINANCIAL RESOLUTION AND DEPOSIT INSURANCE BILL, 2017

The bill was meant it establish a Resolution Corporation to monitor financial firms, anticipate risk of failure, take corrective action, and resolve them in case of such failure. It tried to introduce the risk based assessment as was reflected in the Jasbir Singh Committee Report. The Corporation will also provide deposit insurance up to certain limit, in case of bank failure. The bill would have been applied to banks, insurance companies, stock exchanges, depositaries, payment systems, non banking financial companies, and their parent companies. Here, the Resolution corporation classifies the firm, on the risk of failure, into low, moderate, material, imminent and critical, and it will take over the management firm only when it is critical. The resolution corporation will provide deposit insurance to banks up to a certain limit. This implies that a repayment of a certain amount to each depositor will be guaranteed by the Corporation, in case bank fails. The Corporation subsumes the functions of DICGC. But the bill was withdrawn by the Central Government on 2019 following the lack of clarity over protecting the existing levels of deposit insurance for smaller deposits.

Later, the DICGC board has kick started to revamp the country's deposit insurance scheme in 2019, on the basis of the recommendations of the Jasbir Singh Committee Report. After the controversial Punjab Maharashtra Bank Scam, a revised scheme is being in consideration to added up to the deposit insurance regime, where the categories of depositors will be divided into two; personal and institutional, whereas the former will cover the retail and small businesses and the latter will cover the large depositors, trusts and government agencies. This

[13] Para 3.26, Report of the committee on Differential premium system for Banks in India, 2015
[14] Para 3.28, Report of the committee on Differential premium system for Banks in India, 2015
[15] Para 4.12, Report of the committee on Differential premium system for Banks in India, 2015

revised framework will be taken up soon. It will also be implementing the key recommendations provided by Jagadish Kapoor Committee on Reforms of Deposit insurance in India, the Committee on credit risk model in 2006 along with the Jasbir Singh Committee Report.

Further, as a progressive step, the insurance coverage of the bank deposit was increased from Rs one lakh to five lakhs on the 2020 budget, for scheduled commercial banks. This was a necessary step to boost the depositors confidence which gives a certain sense of security to the depositors.

CHAPTER 5: CONCLUSION

The Jasbir Singh Committee Report was a path breaking document introduced to revamp the Deposit Insurance mechanism in India. It mainly aimed at introducing the concept of differential premium system instead of the risk based mechanism. The DICGC act 1961 has enabled the corporation charge the premium at different rates for different banks in India. Earlier, recommendations were made by the Report on the Banking Sector reforms or the Narasimham Committee and the same view was issued in the Capoor committee. The Committee on credit risk model also suggested the same but it was Jasbir Singh committee which gave an intensive study of the concept by deeply analyzing the issues and introducing a comparative prospect with those countries following the risk based premium. For example, the committee extensively looked upon the Federal Deposit Insurance Corporation in United States, which introduced the risk based premium in its deposit insurance regime. There are many advantage to the high risk premium in comparison with the flat base risk premium such as it is easy to use, where the depositor has higher rate of return beyond the risk free rate. For example, the Dodd Frank Act of 2010 enacted in USA attempted to mitigate some of the moral hazard in big corporations by requiring them to design plans for how to proceed if they got into financial trouble. The major aim in adapting the risk based premium is reducing the moral hazards. As an aftermath of the savings and loan crisis that happened in United States of America, the credibility of the then functioning Federal Home Loan Bank Act of 1932 was questioned in addition to the flat rate risk based premium adopted by the act. Thus, the former act was amended and replaced by the Federal Deposit Insurance Corporation Act of 1991. The same trend is being tried to follow in India by the DICGC through recommending risk based premium approach. The Financial Resolution and Deposit Insurance Bill of 2017 was introduced for the same purpose but was found abrupt and inadequate by the government.

However, initiatives have been made by the DICGC in introducing the risk premium rather than the flat rate, which would be beneficial considering the circumstances nationally and internationally, and hence, the hypothesis proved.

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