

MERGER OF PRIVATE OR PUBLIC SECTOR BANKS– REGULATORY AND REASON

Richa Gupta AP in Commerce, SD (PG) College Panipat

In the globalization era it has become imperative for the policy makers to retain competitiveness within the banking sphere so as to ensure the acceleration of market driven economy. Financial liberalization as an essential part of reforms has encouraged setting up of privately owned banks on the platform of advanced technology and best practices of prudential norms for governance. Regulating authority's role has been limited to the macro level supervision of ensuring the smooth flow of the system and manages the risks against potential blocks. According to the Mark Dorfman "Risk Management is the logical development and execution of a plan to deal with potential losses." It is a misconception that the objective of risk management is the complete elimination of risk. In practice, risk management must aim at keeping the risk in an acceptable range. In a dynamic situation where the factors affecting the risks to the overall system change continuously, the regulator or risk manager has to evaluate the risk level on an ongoing basis and make an attempt to bring it to the desired level.

Reserve Bank of India (*RBI*), the super coordinator and regulator of banking system is authorized by Banking Regulation Act, 1949 to manage the risk level of banking system that is necessary to avoid the financial stress and strain on the economy. RBI normally steps after the expiry of gestation period made available to an ailing bank to establish itself amidst turbulent market competition. The scenario is quite challenging to both the policymaker and the regulator in arriving at a decision either to wind up the sick bank or merge with another healthy bank. RBI is left with no option but to cancel the licences of many small cooperative banks notwithstanding the distress caused to the small depositors and investors. The move to cancel licenses for bigger banks can have negative consequences on the other tiers of the system owing to linkages and adverse impact on the credibility of the system. The word 'Moratorium' in legal parlance refers to a delay or temporary pause in an activity or postponement or waiting period – a legally authorised suspension in discharging a legal obligation. In the context of this paper, moratorium placed on a banking company by the regulating authority, directing temporary suspension of business is the topic of discussion. Reserve Bank of India is empowered by section 45 of the Banking Regulation Act, 1949 to apply to Government of India for imposing a moratorium. It is always imposed by a sudden public notification as any prior information would defeat the very purpose for which the action is meant. The decision to impose the moratorium is guided by the consideration of public interest at large; while at the same time intended to prevent a 'run' on the financial vulnerabilities of the said bank. Recent imposition of moratorium on Global Trust Bank (*GTB*) by RBI is only part of the series of such frequent actions taken by RBI on some errant banks in the last two decades when public trust is dissipating. Moratorium and subsequent merger of Global Trust Bank has

evoked greater public reaction because of the size of the bank and the trust and promise it projected as a new generation private bank. Even though the imposition of moratorium and merger of a weak bank is governed by such legal framework, the reasons behind such actions by the regulator are nevertheless points of public concern and hence are debated upon profusely to draw comparison from the past and also to justify the present actions.

The moratorium decision not being intended as an arbitrary act must also meet the test of transparency and good reason in tune with the a system of good governance. This is more so important when the errant bank is a private bank with the capital contributed by both the public and private investors. The present paper is an attempt to bring out the regulatory perspectives and implications on rights and obligations of shareholders, depositors and creditors by critically evaluating the experience gained from the Global Trust Bank.

LEGAL FRAMEWORK GOVERNING MORATORIUM - MERGER OF PRIVATE COMMERCIAL BANKS

- Moratorium (Section 45(1) of the Banking Regulation Act, 1949)

“Notwithstanding anything contained in the foregoing provisions of this part or in any other law or any agreement or other instrument, for the time being in force, where it appears to the Reserve Bank that there is good reason so to do, the Reserve Bank may apply to the Central Government for an order of moratorium in respect of a Banking Company.” _Section 45(1) avoids scope for any arbitrary bureaucratic action by placing the deciding powers with the Central Government as the act of Central Government is open to debate in Parliament.

Imposition of Moratorium (Section 45(2) of the Banking Regulation Act, 1949)

“The Central Government, after considering the application made by the Reserve Bank under sub-section (1), may make an order of moratorium staying the commencement or continuance of all actions and proceedings against the company for a fixed period of time on such terms and conditions as it thinks fit and proper and may from time to time extend the period so however that the total period of moratorium shall not exceed six months.”

_The limitation period of moratorium to six months is intended to expedite the revival of ailing bank. However, this limitation period is subject to extension and hence this section does not offer any substantial succour to the aggrieved depositors, if Government is undecided on the revival of the bank.

- Amalgamation (□Section 45(4) of the Banking Regulation Act, 1949)

“During the period of moratorium, if the Reserve Bank of India is satisfied that:

- (a) In the public interest; or
- (b) In the interests of depositors; or
- (c) In order to secure the proper management of the banking company; or
- (d) In the interest of the banking system of the country as a whole,

It is necessary to do; the Reserve bank may prepare a scheme –

- (i) For the reconstruction of the banking company, or

(ii) For the amalgamation of the banking company with any other banking institution”

3_This section makes it obligatory on the part of RBI to come to a reasonable conclusion before making a scheme of merger or reconstruction.

Section 45(5) (f) of the Banking Regulation Act, 1949

“The reduction of the interest or rights which the members, depositors and other creditors have in or against the banking company before its reconstruction or amalgamation to such extent as the Reserve Bank considers necessary in the public interest or in the interests of the members, depositors and other creditors or for the maintenance of the business of the banking company.”

Section 45(5) (g) (i) of the Banking Regulation Act, 1949

“The payment in cash or otherwise to depositors and other creditors in full satisfaction of their claim in respect of their interest or rights in or against the banking company before the reconstruction or amalgamation.” _Section 45 (5) (f & g) while leaving discretion to RBI to reduce interest on deposits before reconstruction or amalgamation also makes it obligatory to make the due payments to depositors in cash before actual amalgamation.

Section 45(7) of the Banking Regulation Act, 1949

“The scheme shall thereafter be placed before the Central Government for its sanction and the Central Government may sanction the scheme without any modifications or with such modifications as it may consider necessary; and the scheme as sanctioned by the Central Government shall come into force on such date as the Central Government may specify in this behalf, provided that different dates may be specified for different provisions of the scheme.” _Central Government is empowered by virtue of this section to accept or even change the scheme of amalgamation as prepared by RBI.

- Shareholders Rights (Section 36AG (5) of the Banking Regulation Act, 1949)

“If, before the date notified under sub-section (4), the Central Government receives requests, in terms of that sub-section, from not less than one-fourth in number of the shareholders holding not less than one-fourth in value of the paid-up capital of the acquired bank, or where the acquired bank is a banking company incorporated outside India, from the acquired bank, the Central Government shall have the matter referred to the Tribunal for decision.” _This is an important section governing the compensation payable to shareholders of the acquired bank. If atleast 1/4th of the shareholders holding atleast 1/4th of value of paid up share capital of acquired bank make any representation central government will have to refer to a tribunal constituted by the Central Government for this purpose.

Application to Company Law Board for relief in cases of oppression

Section 397 of the Companies Act, 1956

- “Any member of a company who complain that the affairs of the company are being conducted in a manner prejudicial to public interest or in a manner oppressive to any member or members (including any one or more of themselves)

may apply to the 4 Company Law Board for an order under this section, provided such members have a right so to apply by virtue of section 399.

- If, on any application under sub-section (1), the Company Law Board is of opinion (a) that the company's affairs are being conducted in a manner prejudicial to public interest or in a manner oppressive to any member or members; and (b) that to wind up the company would unfairly prejudice such member or members, but that otherwise the facts would justify the making of a winding up order on the ground that it was just and equitable that the company should be wound up ; the Company Law Board may, with a view to bringing to an end the matter complained of, make such order as it thinks fit.”
- Insider Trading (□Power to make Inquiries and Inspection)

Regulation 4A of the SEBI (Prohibition of Insider Trading) Regulation, 1992

“If SEBI suspects that any person has violated any provision of the SEBI (Prohibition of Insider Trading) Regulations, 1992, it may make inquiries with such persons or any other person as mentioned in section 11 of the SEBI Act, 1992 as may be deemed fit, to form a prima facie opinion as to whether there is any violation of these regulations. SEBI may appoint one or more officers to inspect the books and records of insiders or any other person as may be mentioned in section 11 of the SEBI Act, 1992.”

- The State Bank of India Act, 1955 empowers SBI at the request of management of any banking institution to acquire its business including assets and liabilities. The approval of RBI and Government of India is necessary to finalise the process. Several banks were acquired by SBI under this Act.
- Amalgamation of a non-banking finance company with a banking company is dealt with under Section 39(1) of Companies Act, 1956. Further, provisions are incorporated under the new BR Amendment Act to facilitate such amalgamation.
- Compensation to Employees (□Compensation to workmen in case of transfer of undertakings) Section 25FF of the Industrial Disputes Act, 1947

“Where the ownership or management of an undertaking is transferred, whether by agreement or by operation of law, from the employer in relation to or that undertaking to a new employer, every workman who has been in continuous service for not less than one year in that undertaking immediately before such transfer shall be entitled to notice and compensation in accordance with the provisions of Section 25F, as if the workman had been retrenched: Provided that nothing in this section shall apply to a workman in any case where there has been a change of employers by reason of the transfer, if— (a) the service of the workman has not been interrupted by such transfer; 5 (b) the terms and conditions of service applicable to the workman after such transfer are not in any way less favourable to the workman than those applicable to him immediately before the transfer; and (c) the new employer is, under the terms of such transfer or otherwise, legally liable to pay to the workman, in the event of his retrenchment, compensation on

the basis that his service has been continuous and has not been interrupted by the transfer.”

Regulatory Rhyme and Reason In GTB Episode

A. In a moratorium, the RBI imposes a freeze on bank's liabilities and a restriction on all banking activities but does not impose the liquidation of the bank. Depositors, too, are restricted from withdrawing all their money. It is the rescuing act and practice of RBI to freeze the operations of a sick bank before merging with a healthy bank to protect depositors' interests. RBI moratorium is mainly intended to protect the depositors' interests and prevent a possible run on the bank. The RBI imposition of moratorium on GTB is not the first case of its kind. Earlier too, to protect the interests of depositors, it has imposed the same on a good number of sick banks before attempting a merger as shown under exhibit I.

Exhibit I

MORATORIUM RECORDS INCENATIONALIZATION (PRIVATE SCHEDULED BANKS)

2002, Nedungadi Bank merged with Punjab National Bank (PNB).

2000, Benares State Bank merged with Bank of Baroda.

1990, Karur Central Bank merged with Bank of India.

1990, Lakshmi Commercial Bank merged with Canara Bank.

1988, Hindustan Commercial Bank merged with PNB.

1980, Bank of Thanjavur merged with Indian Bank.

1980, Bank of Cochin merged with State Bank of India.

B. the RBI Moratorium is not an arbitrary act but is governed by section 45 of the Banking Regulation Act, 1949. Accordingly, notwithstanding any contest, the RBI for a good reason may apply to Central Government for issuance of an order imposing moratorium (*temporary suspension of business*) on any Banking Company; and to prepare a scheme for reconstitution or its amalgamation with some other healthy bank.

C. Good Reasons for imposition of RBI Moratorium

- To protect the interests of depositors of the banking company; or
- To secure the proper management of the banking company; or
- To protect the interest of banking system as a whole; and
- To protect the interest of public at large.

D. Procedure for RBI Moratorium

The Reserve Bank of India with any of the aforesaid one or more good reason(s) may make an application to Central Government for issuance of an order imposing moratorium on Banking Company.

After due consideration of the application so made by the RBI, the Central Government may pass an order of moratorium on a Banking Company terminating the commencement or continuance of all actions and proceedings against the company for a fixed period of time on such terms and conditions as it thinks fit and proper and may from time to time

extend the period of such moratorium so that the total period of moratorium shall not exceed six months. Unless otherwise stated by the Central Government, the Banking Company shall not during the period of moratorium make any payment to any depositors or discharge any liabilities or obligations to any other creditors. During the period of moratorium the RBI may prepare a scheme – for the reconstruction of the Banking Company; or – for the amalgamation of the Banking Company with any other banking institution.

MORATORIUM ON MERGER OF GTB WITH ORIENTAL BANK OF COMMERCE (OBC)

Global Trust Bank popularly known as GTB India's first new generation private sector bank established its banking business after obtaining RBI licence in the year 1990. It started with stringent capital adequacy standards of atleast Rs.100 crores to begin with and a technology platform that even foreign banks did not have and above all on a clean slate. The most striking feature of GTB is that it is typically a symbolic new generation private bank that came with the financial liberalisation of the 1990s. It was offered permission to enter the industry with the intention of increasing competition, improving efficiency of operations with new technology, offering better services to the customers, and in the process to be a model against low-profit public sector banks. Before RBI moratorium it was working with 103 branches and 276 ATMs having more than 8.5 lakh customers. As on 30/06/2004, Indian promoters of GTB held a 19.28% stake while the Indian Public held a massive 51.28% stake in GTB. It is one of the largest private banks placed under RBI moratorium.

Good reasons for imposing RBI Moratorium on GTB

The bank's net worth (the sum of its share capital and general reserves) was wiped out two years ago under the weight of bad debts. These non-performing assets were the outcome of large, indiscriminate and dubious loans advanced to companies, which included garment exporters, diamond traders and stock brokers — in Mumbai and Hyderabad. The bank is said to be saddled with bad loans of anything between Rs.1, 200 and Rs.1,500 crore. Its equity share capital and reserves stood at just Rs.300 crore. GTB's audited balance sheet for March 31, 2002, showed net worth of Rs.400.4 crore & a profit of Rs.40 crore. However, RBI inspection revealed that its networth was negative. To overcome the varied conclusions, an independent chartered accountant has been appointed to reconcile and state the actual financial position of GTB. On reconciliation, RBI assessment is proved to be correct.

As a step further, RBI positioned GTB with certain directions relating to certain types of advances, certain premature withdrawal of deposits, declaration of dividend and its capital market exposure. It also started monitoring GTB on monthly basis. □In view of the need to complete the statutory audit and to assess the steps necessary to be taken on the future set up of the bank, RBI permitted GTB, time up to Sept 30, 2003 to publish its annual accounts. Accordingly, GTB announced that as on March 31, 2003 it's deposits

were Rs.6,921 crores and advances (loans) of Rs.3,276 crores. On its balance sheet, it showed gross non-performing assets of Rs.916 crores while total provisions (against bad loans) were Rs.268 crores. The capital market exposure is Rs.156 crores and its capital adequacy ratio was at negative (-0.07) % much below the required 9%. □RBI's inspection showed that bank's net worth was further eroded and capital adequacy ratio (CAR) was negative. On November, 2003, GTB was advised to take immediate steps to infuse fresh capital to restore its CAR to 9% and indicate a time-bound programme. Bank was also advised to explore options of raising capital through domestic sources or through merger with another bank. □Accordingly, in July, 2004 GTB came out with a proposal to raise its capital by infusing fresh equity from Newbridge Capital, a private equity investor, which is prima facie rejected by RBI because the suggestions and bailout package conditions imposed by the private investor proved to be unreasonable or unacceptable as per the RBI guidelines (*i.e., summarily, Newbridge wanted full management control as well as the right to report to the regulator of its parent than to RBI*). Further, the RBI declared that the guidelines for equity participation by foreign investors were already in existence at the time of submission of application for approval by GTB and that the new set of proposed guidelines had not been invoked. Earlier Centurion Bank was successful in getting RBI permission for Sabre Capital of Rana Talwar to infuse capital to bail out from its financial crunch but GTB failed in its attempt to get RBI permission for infusion of capital from NewBridge Capital and to get it restructured. □To protect the interest and safety of funds of depositors of GTB, RBI imposed three month moratorium on it from 24/07/2004 to 23/10/2004. During the period of moratorium the bank is not allowed to carry on any of its operations – taking deposits or rendering loans till a solution to reconstruct the bank is obtained by RBI. This was the move taken in consultation with the Finance Ministry and after the bank failed to come up with a viable proposal for raising additional capital. Infact, the Finance Ministry declared that the RBI's move was only a temporary one aimed mainly to protect the interests of depositors and to utilise the period of moratorium to work out a long-term solution.

Steps taken by RBI during Moratorium on GTB

Towards moratorium on GTB, the RBI has appointed three directors — Regional Director of RBI, Hyderabad, and former General Manager of Bank of Baroda and a Deputy General Manager of RBI— on the GTB board to monitor the activities of the bank. □RBI provided some relaxation to the depositors by allowing them to withdraw from their deposits an amount upto Rs.10, 000/- only through the bank's branches and not from the bank ATMs. ATMs' remained disabled throughout the moratorium period.

8 It was open to RBI to raise the ceiling limit of such withdrawal, but had fixed Rs.10, 000/- as ceiling limit on withdrawals in order to ensure that demands of the most of the depositors are met by the GTB branches. – it stood by its assurance to meet any requirement of cash at the branches of the bank for making permitted payments under the

moratorium, since cash balances of GTB are maintained with it; – the bank allowed to permit withdrawal in excess of Rs.10,000/- but subject to a maximum limit of Rs.1 lakh under the following situations: – medical treatment of the depositor or any person dependent on him; – cost of higher education, in India or abroad, of the depositor or any person dependent on him; – marriage or other ceremonies of the depositor or his children or any other person dependent on him; and – in case of any other unavoidable emergency. – all Demat accounts and safe deposit lockers of customers were to be operated as usual. – RBI has set up help lines to assist the members of public at Mumbai and Hyderabad. Within 48 hours of declaring Moratorium on GTB, RBI announced that GTB is to be merged with the financially-strong public sector bank –Delhi based Oriental Bank of Commerce (*OBC*) with effect from August 14, 2004 in order to protect the interests of its clients. *OBC* is a bank of zero NPA (*Non Performance Assets*) record and a strong capital adequacy ratio. *The record date for GTB-OBC merger has been fixed at August 31, 2004.*

The salient features of scheme of merger are as follows:

- _ All types of deposit accounts of GTB shall be transferred to OBC.
- GTB depositors shall receive the same rate of interest on their deposits as offered by OBC to its depositors.
- Every savings bank account, current account or any other deposit account, including fixed deposit, cash certificate, monthly deposit, deposit payable at call or short notice with GTB, shall be transferred to OBC on the prescribed date in the name of the respective account holders, crediting the full amount including interest to the extent payable under the scheme.
- _ All GTB employees shall continue in service with OBC.
- GTB employees (1300 odd employees) shall be deemed to be appointed in OBC at the same remuneration and on the same terms and conditions of service applicable immediately before the close of business on July 24, 2004.
- GTB employees salaries shall be protected even after it being amalgamated into OBC for a maximum period of three years (Because, GTB salary scales are significantly higher than those of OBC).
- Before the stipulated period, salary levels be aligned at both the banks depending upon the qualification and experience of the employee.
- GTB employees who have their intention not to continue to be the employees of OBC shall at any time by notice in writing before the expiry of one month following the prescribed date, shall be entitled to compensation, under the provisions of the Industrial Disputes Act, 1947 and pension, gratuity, provident fund and other retirement benefits as may be ordinarily admissible under the rules or authorizations of the bank as in force immediately before the close of business on July 24, 2004.
- _ All assets and liabilities of GTB will be transferred to OBC.

- All assets and liabilities of GTB shall be transferred to OBC after proper valuation is done. Investments other than Government securities shall be valued at market rates.
- All realizable assets of GTB shall be set aside in a separate Asset Account - Escrow Account which would be used to meet all the outstanding liabilities (including any amount payable to preference shareholders) of the troubled bank – GTB. In case any surplus is left over in the Asset Account, the same is distributed on pro-rata basis to the equity shareholders of GTB after 12 years or an earlier date specified by the Government after consulting the RBI for this purpose. Infact, OBC shall, in consultation with GTB, value the assets and reckon the liabilities.
- The entire amount of the paid-up capital and reserves of GTB shall be treated as provision for bad and doubtful debts and depreciation in other assets of OBC.
- OBC shall call upon every person who was, as on the prescribed date, registered as the holder of an ordinary share of the bank or would have been entitled to be so registered, to pay within three months from such date or dates as may be specified, the uncalled amount remaining unpaid by him in respect of such share or shares and the calls in arrears, if any.
- OBC shall take all available steps considering the circumstances of each case of equity holders to demand and enforce the payment of the amounts due with interest at six per cent per annum for the period of the default.
- GTB's books shall be closed and balanced and the balance sheet prepared in the first instance as at the close of business on July 24, 2004 and thereafter at the close of business on the date immediately preceding the prescribed date. The balance sheet shall then be audited and certified by a chartered accountant or a firm of chartered accountants, approved or nominated by the RBI for the purpose.
- GTB Advances will be scrutinised by OBC and the securities held as cover examined and verified. Thereafter the advances, including portions thereof, will be classified into two categories — 'advances considered good and readily realisable' and 'advances considered not readily realisable and/or bad or doubtful of recovery'.
- With respect to 'advances considered not readily realisable and/or bad or doubtful of recovery' or 'which are or may be realisable wholly or partly' after the prescribed date, OBC shall take all steps to demand and enforce payment, and may enter into a compromise or arrangement with the debtor or any other person, or write-off any such debt or asset, or sell or otherwise dispose off any securities transferred to it or any other asset taken over by it.
- OBC can take all steps to demand and enforce the payment of amounts, if any, awarded as damages by the High Court against any promoter, director, manager or any other officer of GTB under relevant sections of the Banking Regulation Act and the Companies Act. What this means is that GTB's promoters and other functionaries cannot escape accountability.

Role of SEBI

RBI had informally asked the Securities and Exchange Board of India (*SEBI*) to investigate those responsible for selling the stock, with special reference to the promoters, the financial institutions and other large stakeholders. However, the regulator decided to formally ask SEBI to scrutinize the current movements and ascertain the people who are buying the GTB scrips. SEBI launched a full fledged probe into the trading in the GTB stock, including alleged insider trading prior to it being placed under moratorium and announcement of merger, because insider trading is one of the most serious crimes on the faith of fair dealing in a capital market and SEBI is the regulating authority under the Securities and Exchange Board of India (Insider Trading) Regulations, 1992.

Shareholders of GTB - The ultimate losers on GTB-OBC merger

OBC has ruled out any share-swap on GTB –OBC merger. The GTB equity shareholders shall not get any value for their holding now but they can expect some relief only after 12 years that too if the troubled bank is left with any surplus (*assets – liabilities*) value.

Mutual funds exited the stock totally while financial institutions, banks and foreign institutional investors hold negligible stakes. That means only small shareholders have been left high and dry since they had no way of knowing what was in store for the bank.

However, a good portion of the investors are of the opinion that any losses sustained by them in this transaction can be set off against other gains. But the RBI clarified that this is not possible since the capital of the company, theoretically, does not exist as it has no value attached to it. Pursuant to this, the Shareholders of GTB are planning to file a public interest litigation: □for the repeal of section 45(2) of the Banking Regulation Act, 1949 under which the aggrieved parties in the case of the amalgamation of GTB with OBC are prevented from taking recourse to any legal remedy; □□making Securities and Exchange Board of India (*SEBI*) a party to the case considering its regulatory role; the implication of section 397 of Company Law that protects shareholders' rights. Lifting of RBI Moratorium on GTB

RBI announced that the government of India had sanctioned the scheme for amalgamating GTB with OBC with effect from August 14, 2004. RBI Moratorium on GTB has been lifted and all branches of GTB shall now function as the branches of OBC. Customers (*including depositors*) of GTB shall be able to operate their accounts as customers of OBC. Infact, RBI asked OBC to make necessary arrangements to ensure that the services as usual are provided to customers of GTB.

CRITICAL APPRAISAL OF REGULATORY INTERVENTIONS IN GTB EPISODE

Is there avoidable delay?

– The sequence of regulatory interventions as illustrated in exhibit II indicates an unexplained delay of ten months from Sept. 2003 when RBI was convinced of the erosion of net worth and consequent CAR until July, 2004.

Exhibit II

SEQUENCE OF REGULATORY INTERVENTIONS BY RBI

RBI inspection as of March 31, 2002 reveals negative Networth as against networth of Rs.400.40 crores reported in balance sheet Appointment of independent Chartered Accountants Report in Feb, 2003_ Placed under directions of RBI for advances, premature withdrawal of deposit, capital market exposure, dividend declaration _ Change of Statutory Auditors _ Monthly Monitoring.

Further erosion of Net worth /Capital Adequacy Ratio (CAR) –negative as on 31.03.2003. Balance Sheet figures submitted in Sept. 2003 found incorrect. On Nov. 2003, GTB advised to explore options for capital infusion/merger On July 24, 2004, GTB placed under moratorium. – Interestingly, IFC and World Bank have reportedly chosen to exit from their investments much earlier to the detection of balance sheet irregularities by RBI in March, 2002. – Even though RBI inspection report as on 31.03.2002 has been taken as cutoff date for tightening the supervision, the previous inspection reports appear to have not seriously prompted RBI in respect of – Share rigging in GTB shares,

_ Risky projects in entertainment sector,

_ Uncovered advances to stockbrokers,

_ Unwarranted exposure to diamond trade, real estate sector,

_ Unethical schemes to shareholders and speculative manoeuvre to earn profits.

– Timely interaction and coordination between two regulators viz SEBI and RBI could have lessened the damage to the genuine interests of investors.

How the scheme of amalgamation is different from the previous ones?

– A cursory look at the following salient features of scheme of amalgamation between Banaras State Bank Limited (*BSB*) with Bank of Baroda (*BOB*)-19th July, 2002 reveals a preferential treatment to GTB depositors.

BSB-BOB amalgamation scheme interalia has provided for

_ all staff security deposits to be paid in full with accrued interest,

_ All outstanding liabilities excluding deposits,

_ Payment in full for deposits upto Rs.1 lakh by BOB or DICGC and balance of deposits above Rs.1 lakh to be paid pro-rata on basis of evaluation of assets.

– GTB-OBC amalgamation scheme provides for payment in full to all depositors without any limit and along with accrued interest. It is likely that aggrieved depositors of BSB-BOB may resort to litigation on grounds of discrimination. – It is probably for the first time that employees' interests are protected for a considerable period of three years in the

scheme of amalgamation. It is to be believed that wiser counsels have prevailed after bitter disputes witnessed in the merger of New Bank of India with Punjab National Bank.

□□Is there unfair prejudice towards small investors of GTB?

– It appears so for small investors of GTB. Nearly 43% of stake in GTB is held by small investors amounting to approximately 26 crores. These equityholders can expect some relief only after 12 years, if the erstwhile bank account is left with any surplus after meeting all liabilities. OBC ruled out any share swap on GTB-OBC merger for the present.

– Considering huge tax concessions against NPAs given to OBC, a fair compensation package for small investors could have prevented litigation by shareholders of GTB under section 397 of Companies Act, 1956 against unfair prejudice to shareholders.

CONCLUSION

The forced merger of Global Trust Bank, a pioneer private bank of new generation with Oriental Bank of Commerce revives the debate for a transparent and uniform policy towards ailing sick banks in private sector including cooperative sector. It is true that Deposit Insurance and Credit Guarantee Corporation (*DICGC*) with its fragile capacity would not be able to meet the depositors' interests of even a portion of insured deposits. GTB episode has once again exposed the vulnerability of banking system to the exploitation of stockbrokers and dominating promoters of banking companies who could conveniently divert the depositor's money to seek their own ends. Reserve banks delayed surveillance over the weaker banks and deficiencies in audit and inspection of affairs of banks as in GTB episode pose serious concerns on the safety and soundness of banking system and the efficacy of prudential norms. The solutions to unending challenges thrown by vested interests do not lie totally in the legal framework as the efficient use of law and regulation rests only with the enforcing authorities supported by the will of the State Instrumentality.

References

1. www.rbi.org.in2. The Banking Regulation Act, 1949
2. The Companies Act, 1956, 5. The State Bank of India Act, 1955
3. The SEBI (Prohibition of Insider Trading) Regulations, 1992
4. <http://www.banknetindia.com/banking/gtb.htm>