



A Study on Bank Frauds and the Compliance of Preventive Security Controls in Indian Banking Industry.

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ABSTRACT:

The study seeks to evaluate the various causes for bank frauds. It aims to examine to what extent measures prescribed by RBI, followed by employees. It provides an insight on the perception of bank employees towards preventive mechanism & their awareness towards various frauds. A good system of internal control prevents frauds & scams. The article reveals that lack of training to employees, overburdened staff, low compliance level are the main reasons for bank frauds. The banks should take appropriate measures to prevent frauds and ensures that there is no laxity in internal control system.

KEY WORDS: Preventive measures, Compliance, Bank frauds, Non-performing assets.

1. INTRODUCTION:

Banks deal with public money & hence it is imperative that employees should exercise due care & diligence in handling the transactions in banks. Recent increase in bank frauds calls for tightening of security mechanism. A good system of internal control is the most effective way of fraud prevention. The banks should increase awareness among employees to combat frauds.

2. REVIEW OF LITERATURE:

➤ Wilson(2006), examined the causes that led to the breakdown of Barring bank, in his case study, "the collapse of Barring bank". The collapse resulted due to the failures in management financial & operational controls of banking banks. The failures that were evident include the following areas.

- a) Failure in management supervision.
- b) Lack of segregation between front & back offices of Baring futures, Singapore.
- c) Insufficient actions taken by Barings management in response to warning signals.
- d) No risk management or compliance functions in Singapore.
- e) Weak financial & operational control over the activities & funding of Baring futures Singapore at group level.

- Bhasin in 2007, examined the reasons for cheques frauds & the manner, in which the expertise of internal auditors can be integrated, in order to detect & prevent frauds in banks. He emphasized that, the internal auditor of the bank has to play an important role to prevent frauds. The auditor can take several proactive steps to combat frauds. Checking frauds, requires training account screening signature verification & information sharing with regulators & local authorities.
- Ganesh & Raghuram (2008), survey conducted by them, about 80 executive from corporation bank & Karnataka Bank Ltd., training improves the capabilities of employees by enhancing skill sets, knowledge & commitment towards this work.
- Lokare (2014), reveals that the share of retail loan segment in total NPA's continues to stay high of which credit card loans (2.2) percent have the third highest contribution after personal and housing loans.
- Swalin & Pani (2016), said that frauds occurred due to inadequate supervision of senior management along with the major technological loopholes in online banking.
- Coste & Wood (2016), highlighted significant factors describing characteristics of the fraudsters alarming the fraudulent acts of individuals.

3. OBJECTIVES OF THE STUDY:

1. To identify the procedural lapses & other causes responsible for bank frauds.
2. To evaluate the extent of implementation of internal control mechanism.
3. To evaluate the factors that influence the degree of compliance.

4. RESEARCH METHODOLOGY:

Secondary data has been used to collect the data. RBI annual reports & guidelines, committee reports, Newspapers, Books, Journals, circulars, websites of Banks are the sources of secondary data.

5. BIGGEST BANK FRAUDS:

These are the biggest bank frauds in India, reported in the last decade.

5.1 Vijay Mallya scam (2016): Businessman Vijay Mallya's bankrupt kingfisher airlines owe more than 10,000 crore to more than a dozen banks. He left India in March 2, 2016, the same day that some public sector banks filed a petition against him with the debt recovery tribunal. King fisher airlines, which began operations in 2005, were forced to cease operations in 2012, due to increasing liabilities. A group of 17 Indian banks are trying to collect roughly Rs.10,000 crore in loans that Mallya is accused of using to gain shares in more than 40 companies around the world. The largest lender was SBI, which had 1600 crore, followed by Punjab national banks, which had 800 Crore, IDBI, which had 550 crore, fugitive economic offender in Jan.2019. The government is endeavoring to extradite Mallya from the united kingdom.

5.2 Winsome diamond scam (2016).

Mehta's winsome is India's – largest corporate defaulter, Jatin Mehta, the promoter of winsome diamonds & Jewellery, is a Gujarat based diamond trader. He owes a group of banks more than Rs.6,500 crore. More than 10 cases have been filed against the businessman by the CBI. It filed charges against 21 persons, including Mehta & his wife sania, in 2018. Two Former Canara Bank CEO's & 15 govt. employees were also charged with assisting Mehta in getting the loan. In addition, the CBI instructed Interpol to issue a Red corner notice against Mehta in a letter. The family managed to free the proceedings without leaving a trace. Jatin Mehta relocated to Montenegro, a Balkan country in South-East Europe, with his family. According to the investigating officer, the Mehta family developed their business in different countries after fleeing India.

5.3. The Punjab National Bank Scam.

The Punjab National Bank scam was touted as India's biggest at Rs.11,400 crore and the main accused were jeweler Nirav Modi, Mehul Choksi, Nishant Modi, Amit Modi and others, including some PNB staff. The scam involved 'letters of undertaking' fraudulently issued by a junior official at the bank to get short term loans from overseas bank branches to pay sellers and the transactions never registered with the bank, where officials also did not notice the fraud.

A CBI probe exposed the scam where the accused defrauded 30 Indian banks foreign branches. Modi Choksi fled India a couple of days before the scam was made public. Modi, who was in prison in London had recently appealed against his extradition which has been denied.

5.4 ABG Shipyard fraud case:

The CBI charged ABG shipyard limited, its former chairman & managing director Rishi Kamlesh Agarwal, Santhanam Anantha Swamy, Ashwini Kumar, Ravi vimal Nevetia, Sushil Kumar Agarwal and another firm, ABG international Pvt. Ltd for embezzling Rs.22,842 crore from SBI and 27 other lenders. The loan account was named as a non-performing asset in July 2016 and fraud was detected in 2019.

5.5 Kanishk gold bank fraud:

Kanishk gold Pvt. Ltd., was charged by CBI for allegedly cheating in banks led by SBI out of Rs.824 crores. The owners have been accused of taking huge loans for business & were detrimental to the bank's right and interests. The lowest said, according to media reports. ED in Chennai froze properties worth RS.48 crore of Kanishk gold private Ltd under the PMLA. SBI has said security to cover the loss due to the fraud is around Rs.156 crore.

5.6 Andhra Bank fraud:

Gujarat based Pharma company sterling Biotech ltd. Was involved in the Andhra Bank fraud case as a directors of the company were named as defaulters in the Rs.8, 100 crore bank scam. Nitin Sandesara, Chetan Sandesara, Dipti Sandesara & Hitesh kumar, Narendra Bhai Patel, were designated fugitives in the scam. The company has been accused of acquiring over Rs.5,000 crore in loans from a consortium led by Andhra Bank, which has since become non-performing assets.

5.7 Rotomac Pen scam:

Rotomac Global Private ltd. of Kanpur, its promoter Vikram Kothari & other directors were charged by the CBI of allegedly defrauding lenders of Rs.750.54 crore. The company has a total outstanding of Rs.2919 crore against a consortium of seven banks led by Bank of India. The bank had been providing the company with loans from 2002 and in 2015, the account was labeled as non-performing assets (NPA), Kothari passed away early 2022 after an accident at home. It was arrested in connection with the case in 2018 and spent 2 years in Jail, after which, he was granted bail on health grounds.

5.8 Videocon case fraud:

FIR was filed against former ICICI Bank CEO Chandra Kochhar, her husband Deepak Kochhar, and Videocon group MD Venugopla Doot for alleged irregularities in loans the bank to the group back in 2012. The case pertains to the time when Kochhar was the CEO of ICICI and had loaned Rs.3250 crore to Dhoot's Videocon group. A whistleblower, who owned shares in both the bank and the group, claimed that the loan

to Videocon was influenced by Kochhar in exchange for a deal in no power renewables & supreme energy, a clean energy firm managed by Kuchhar's husband.

6. FRAUDS DETECTION & PREVENTION MECHANISM IN THE BANKING INDUSTRY:

In the last decade, public sector banks in India have lost thousand crore on account of various banking frauds. Indian banking system has remained plagued with growth in NPA's during recent years, which resulted in a vicious cycle affecting its sustainability. In May 2021 the RBI has published its annual report 2020-21, which disclosed that in the last 3 years 22,864 banking frauds have been reported involving huge amount of over INR 3.95 trillion. After investigation it is revealed the involvement of not only middle level employees but also of the senior most management of the banks.

The root cause of weak corporate governance at highest level is directly linked to the very process of appointment of highest level of officials. The inability to hire competent professionals and expertise from market due to existing recruitment policy. Lack of adequate training in contemporary fraud prevention techniques are key HR issues, which indirectly contribute to bank frauds. In fraud cases, within the banks, with suspected involvement of senior management, there is significance resistance while prosecuting officers. Most of the officers retire before they can be booked for a fraud.

Reporting of frauds to RBI:

Banks need to furnish fraud monitoring return (FMR) in individual fraud cases, irrespective of amount involved, to RBI electronically. Fraud reports should also be submitted in cases where central investigating agencies have initiated criminal proceedings Suo moto, where the RBI has directed that such cases be reported as frauds. Banks (other than foreign banks) having overseas branches/offices also report to RBI.

Central fraud monitoring cell (CFMC), department of Banking supervision, central office located at Bengaluru will have a record of officers of all banks/financial institutions responsible for reporting of frauds etc. all banks should furnish to department of banking supervision, central fraud monitoring cell.

7. FINDINGS AND ANALYSIS OF BANKING INDUSTRY FRAUDS FROM 2020-21 TO 2022-23.

As per RBI annual report the following table shows the number of banks frauds and the amount involved for the last three years.

Year	Number of fraud cases	Amount involved in the fraud cases. (Rs. in crores)
2020-21	7,338	1,32,389
2021-22	9,097	59,819
2022-23	13,530	30,252

Source: RBI Report published (30-5-2023)

The number of frauds in the banking sector went up to 13,530 in 2022-23, year on year, but the amount involved nearly halved at Rs.30,252 crore. Frauds occurred predominantly in the category of digital payments (card/internet), in terms of number, said RBI annual report 2022-23.

However, in terms of value, frauds have been reported primarily in the loan portfolio (advance category). A total of 9,097 frauds had been taken place in 2021-22 involving Rs.59,819 crore. In 2020-21, the number of frauds were 7,338 and the amount involved was Rs.1, 32,389 crore.

An analysis of Bank group-wise fraud cases over the last 3 years indicates that while private sector banks reported maximum number of frauds, public sector banks continued to contribute maximum to the fraud amount during 2022-23. Data are in respect of frauds of Rs.1 lakh and above reported during the three years. It is interpreted that there was a 55 percent decline in the amount involved in the total frauds reported during 2021-22 over 2020-21. Further, proportionately, the decline in the total amount involved in frauds continued during 2022-23, with a reduction of 49 percent over 2021-22.

While small value card/internet frauds contributed maximum to the number of frauds reported by the private sector banks, the frauds in the public sector banks were mainly in loan portfolio.

During 2022-23, while public sector banks reported 3,405 frauds involving Rs.21,125 crore, private sector banks reported 8,932 cases involving Rs.8,727 crore, the rest were from foreign banks, financial institutions. Small finance banks & payment banks. As per the data 95 percent of Rs.28,792 crore of the total Rs.30,252 crore was reported in cases related to loans (advance).

The central bank said amounts involved reported do not reflect the amount of loss incurred. Depending on recoveries, the loss incurred gets reduced. Further, the entire amount involved is not necessarily diverted. For many years, we have all witnessed massive political & financial scams/frauds in our country involving multimillion dollar sums of money. Instead of squandering public funds by continuously writing off large corporate bad loans, India has to improve loan recovery processes, strengthen regulatory & lending regulations, perform frequent auditing & separate long term infrastructure funding to private firms from commercial banks.

Instead, the government favors large companies providing them with significant tax breaks & write off on bad loans while shifting the weight of their crimes & taxes on the general masses. With so much money being transacted in frauds one cannot help but question if India would still be a developing economy, if the money had been spent on what it was intended for.

8. CONCLUSION:

The frauds may be primarily due to lack of adequate supervision of top management, faulty incentive mechanism in place for employees, collusion between the staff, corporate borrowers and third party agencies, weak regulatory system, lack of appropriate tools and technologies in place to detect early warning signals of a fraud. Lack of awareness of bank employees and customers and lack of coordination among different banks across India and abroad. The delays in legal procedures for reporting and various loopholes in system have been considered. Some of the major steps to be taken by RBI to prevent frauds in banking industry are strengthening of regulatory & supervisory framework of banks & financial institutions in line with global best practices and updated technology for efficient customer services and effective fraud detection can help in reduction of frauds in banking sector.

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