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Analytical Overview of Fraud Cases of Selected Indian Banks

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ABSTRACT

The paper examines the history of banking sector frauds and discusses the recent instances of frauds taking place in the Indian banking sector. The paper also presents a few selected statistical reports related to the theme of the paper. The causes and risk factors associated with the frauds in the banking sector have been also addressed. Various cases of fraud related to the Indian banking sector have been discussed and the paper also suggests measures to check such frauds. The RBI too has constituted a specialised working group and different types of internal committees to monitor increasing cases of fraud in the banking sector. Thus at an aggregate level there have been measures in the proper direction and the government should not lose their focus on major broad areas in their battle against banking sector frauds. To tackle frauds is the need of the hour, hence various regulatory reforms to handle banking frauds have been also discussed in the paper.

Keywords: *Financial sector; Bank frauds; Blockchain; Money laundering; Quantum computing; RBI; Regulatory reforms.*

1.0 Introduction

In the year 1913, Keynes (2006), wrote in Indian Currency and Finance, "In a country so dangerous for banking as India, (it) should be conducted on the safest possible principles". Indian banking industry is facing fraud-related issues for the past few years. Indian banks, especially public sector banks are suffering from mounting losses and a rise in NPAs on account of increased level of frauds. In most of the cases, there is an involvement of top-level management creating a halt on banking activities.

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Loan sanctioning for new projects, as happened in the recent case of Nirav Modi, have brought sufferings for the industry. Many of the top executives have been charged for alleged corruption and deceitful intentions in granting loans. This creates a question mark on corporate governance and ethics in the industry. In fact, the menace of rising NPA is a global crisis that is responsible for slowdown in the industry.

The strength of the financial system of any economy can be judged by its level of production and consumption. The living standard and status of people can be judged with the soundness of the financial system; but if the financial system is packed with frauds and a high degree of NPAs, it should be a cause of worry for any nation. The Indian economy, in fact, is suffering for the past many years from these issues.

If the financial system or banking system is strengthened, it will be reflected in the GDP growth and living standard of the people. But if the system is a failure, then it reflects the inefficiency of the country's governance and causes distress among various stakeholders. The number of frauds in the year 2016-17 was more than 3870, involving an insane amount of 17,750 crores including both commercial and private banks. If we compare this with 2013-17, we seen that the number of frauds was almost doubled as a total of 17,501 frauds were reported in this period. Out of these, 2,084 had insider involvement.

Bank frauds are not only related to advances or loan-related activities, but also to deposits and services. In short, frauds are divided into three parts: deposit related, advance related and service-related. The main reason for increasing fraud in banking and financial services is the increasing use of technology. On one side, the technology is giving many comforts and benefits like paperless transactions, cashless transitions and direct home services, while on the other hand, it is also increasing risks such as the spread of viruses, occurrence of financial frauds by various means like identity theft, phishing, card skimming. Fraudsters are employing newer and diverse means like spyware, social engineering, Trojans, website cloning and cyber stalking and so on for their illegal activities.

2.0 History of Banking Frauds

Bank frauds and failure are not new in Indian history. Presidency Bank of Bombay (PBB) was formed by the East India Company in 1840 that operated and functioned prudently in a stable manner till the mid-1860s. Due to the civil war and less supplies from the US at that time British mainly started relying on Bombay cotton markets. Hence a lot of cotton companies and banks began to spring up in Bombay in order to cater to much thriving demand for capital. Thereafter PBB started issuing loans hastily not only against shares of private companies but also on merely personal security. As the civil war finished, the jubilation in the Indian cotton market turned to fright mode and the bank came to a hasty close.

Then, many of the banking failures in the year 1910, happened in Punjab. In 1913-14, out of 54 closed banks, 28 were from Punjab and 11 from Bombay. The position of failures then moved radically towards South India and West Bengal. During the period of 1913-66 around 1800 banks were failing—25% in Kerala, 21% in West Bengal and 20% in Madras.

For a while absence of the central bank was to be blamed for these collapses. During 1913 and 1934, around 350 banks were closed in India. India finally formed its own central bank in 1934. In 1992 and 2001 there were stock market scams that took place because of fraud cases in the Indian banking sector. During that period, there was a scam in the Indian Banking sector in 1996. Within the newly licensed banks of the 1990s, Global Trust Bank was mainly responsible for stock market scam in 2001. There has been also a bad loan crisis during the decade of the 80s and 90s.

3.0 Literature Review

According to Singh (2005), "The Indian banking sector is very much distinctive and has no match in the banking history of any nation in the world. The Indian banking sector has evolved through three stages of lending ideologies since Independence. Post-Independence, the Indian banking industry has evolved through three stages: character-based lending to ideology-based lending to competitiveness-based lending."

Kumar and Sriganga (2014) stated, "Banking sector of India accommodates 1175,149 employees, with a total of 109,811 branches in India (and 171 branches abroad), and manages an aggregate deposit of Rs. 67,504.54 billion and bank credit of Rs. 52,604.59 billion. The banking sector in India is characterised by a very wide network of branch operations with a very huge human resources base."

Mittal (2019) stated that a federal set up creates a multiple polity based on divided functions and powers among central, state and local governments. Fiscal federalism, as a branch of public finance, deals with financial settings, provision and their functioning in a federal polity. Calderon and Green (1994) made an analysis of 114 real-life instances of cheating and frauds taking place in the corporate world from 1986 to 1990. The study found that professional and managerial employees were involved in 45% of the cases. Hence bank employees have an important role to play in the fraudulent instances to a great extent.

Ziegenfuss (1996) conducted a study to find out the quantum and type of frauds taking place in the government sector at the state level and local level. The study discussed instances of different forms of fraud that took place in the financial sector during the study time frame.

Willson (2006) investigated a case study of Barring Bank and studied the causes that were responsible for their breakdown. The main reasons for the collapse of Baring Banks were poor and inefficient management, poor financial control and operational inefficiency. The study further suggested that the collapse of the banking sector is directly associated with the fraudulent instances taking place in the banking sector".

Bhasin (2015) examined the reasons to investigate frauds, the scale of frauds in Indian banks, and the manner in which the proficiency of internal auditors can be synchronised for the purpose of detection and prevention of frauds instances in the banking sector. The study also highlighted few cases of frauds in the Indian banking sector.

Banking regulations have become more strict over the passage of time but the increased cases of fraud and failures to control them are quite frustrating as the Indian banking sector is even now regulated by both International Basel Regulations and domestic norms. RBI has extensive powers to inspect banks. One significant challenge for banks is the investigation of innovative technology and its applications for system regulation and security concerns.

4.0 Objectives of the Study

- To determine the reason for various types of frauds in banking.
- To check different forms of fraud and their impact on different stakeholders.
- To find out various measures to stop these frauds so as to protect different stakeholders.

5.0 Risk Factors in Financial Sector

The financial sector has evolved with the following types of risk factors for fraud and cybercrime - almost all banks, offer online and mobile banking services. Debit cards, credit cards and other payment methods are used for banking transactions. ATM's machines and other electronic channels used for these payments is the main target of cyber-attacks.

Money laundering: Money laundering activities increase the chance of terrorist funding. Rigorous Regulatory requirements and control and media scrutiny by banks and financial institutions are necessary to control fraud.
Black Money: Cybercrime and financial frauds lead to financial instability in the country. India is one of the top positions in the world for increasing Black money.
Loan loss: The risk of increasing NPA and Bad debts in India in the increased manifold, due to lack of appropriate methods of monitoring of loans and not by proper due diligence.
Credit growth: Increasing rate of fraud also affects the credit growth of any country. The increase in fraud affects faith in the financial sector, which eventually affects the credit growth of the economy.

6.0 Selected Statistical Reports

Estimated case of banking fraud is increasing year by year is shown in Table 1. As per RBI data, during the period 2013-2017, 17,504 bank frauds reported. Around 5,200 officials were held for fraud in Public sector banks during the period 2015-2017.

Table 1: Banking Fraud Cases

Year	No. of cases(Cyber Crime)	No. of Cases (ATM, Debit Card)
2015-16	9622	1159
2016-17	11522	1372
2018-18	12317	2059

Source: https://www.ijbmi.org/papers/Vol(5)7/version-2/A05720109.pdf

The study shows that the top bank in the list of frauds by bank officials was State Bank of India (SBI), Indian Overseas Bank (IOB) and Central Bank reporting 1538, 449 and 406 cases respectively (Table 2). One of the popular public sector banks that is Punjab National bank is also facing fraud committed by billionaire jeweller Nirav Modi. Most of the cases in case of frauds have insider involvement. If we see data for the period, 2013-2017, out of 3870 cases, in 450 cases had insider involvements. Central Bank that is RBI has been issuing circulars to banks about how effectively report cases and also put in place mechanisms to prevent them. The country's banking sector has reported a total of 12,553 fraud cases worth Rs 18,170 crore in 2016-17. While Bank of Maharashtra reported 3,893 cases of fraud, private lender ICICI Bank came a close second with 3,359 cases followed by HDFC Bank with 2,319 cases, the Institutional Investor Advisory Services (IiAS) said.

Table 2: Fraud Cases involving Bank Officials

BANK	No of Cases involving Bank Official (2015-17)
State Bank of India	1538
Indian Overseas Bank	449
Central Bank	406
Union Bank	214
Punjab National Bank	184

a)Total Fraud Cases involving Private & Public sector bank: 17,504

b) Amount of money involved in these cases: Rs 66,066 crores

Source: https://www2.deloitte.com/us/en/pages/advisory/articles/fraud-trends-banking-industry.

In terms of value, Punjab National Bank (PNB) tops the list with fraud worth Rs 2,810 crore. It was followed by Bank of India at Rs 2,770 crore, the State Bank of India at Rs 2,420 crore and Bank of Maharashtra at Rs 2,041 crore (Table 3).

Table 3: Bank Fraud Cases (Nos & Value) in Indian Banks

Bank	No of Fraud Cases	Value (Rs Crore)
Bank of Maharashtra	3893 Cases	
ICICI Bank	3359 cases	
HDFC Bank	2319 cases	
Punjab National Bank		2810
Bank of India		2770
State Bank of India		2420

Source: https://www.telegraphindia.com/business/reality-check-on-bank-frauds/cid/1481007

7.0 Cases of Bank Fraud

In the year 2014, Rs.139 crore fraud from industrialist Bipin Vohra and others who basically belong to Kolkata were booked by the CBI for allegedly cheating Central Bank of India for taking a loan with documents, which are forged. In the year 2011 Rs, 150 crores from Executives of Bank of Maharashtra, Oriental Bank of Commerce and IDBI created about 10,000 fictitious accounts and transferred loans to these accounts, a CBI investigation had found.

There is another case, In the year 2015 of Rs, 2 crore fraud recorded by CBI, to former deputy general manager of Central Bank of India and three directors of Jain Infraprojects Ltd - MK Jain, Rekha Jain and Sunil Kumar Dangi, for allegedly involved in defrauding the bank.

In the year 2017, CBI arrested the promoters of Abhijeet Group - Manoj Jayaswal and Abhishek Jayaswal and TL Pai, a former DGM of Canara Bank, for allegedly defrauding Canara and Vijaya Banks for Rs. 290 crore.

There is a case of involvement of bank employees, in the year 2014, in which Officials of Ahmedabad-based Electrotherm India allegedly cheated Central Bank of India. The amount involved in this case was Rs. 437 crore.

That was the year 2017, when CBI arrested officers of the Bank of Maharashtra Padmakar Deshpande, from Pune, along with the director of Siddhi Vinayak Logistics Limited, a private logistics company from Surat, for their alleged involvement in Rs 836-crore fraud case.

CBI also booked four people including Chief Manager of Syndicate Bank in an alleged scam in which the accused used fake cheques, letters of credit and LIC policies to withdraw money of Rs. 1000 crore in the year 2016.

In the Year 2015, Rs. 6000 crore fraud was related to money laundering/fund siphoning scam. Scamsters exploited loopholes in remittance rules to bring back illegal money parked abroad disguised as export revenues. The persons were involved in transferring money abroad claiming that to be an advance payment to overseas vendors. The Employees of few banks including the Oriental Bank of Commerce and Bank of Baroda were allegedly party to the scandal.

A case of Rs. 8000 crore in the year 2014, was recorded for the bribe-for-loan scam, CBI found a well-oiled nexus between top bank officials and companies. Bank chiefs were bribed by companies wanting loans. There was an arrest of ex-chairman and MD of Syndicate Bank, S. K. Jain in the above case.

One of the most well-known alleged frauds of Rs. 9000 crores in India's banking history, is by liquor baron Vijay Mallya who was accused of defrauding a consortium of lenders. He is still in the UK and Indian authorities are trying to extradite him to India. This was the most popular banking fraud case in the media.

In the year 2018, there was a case of fraud by Kolkata–based gold trader Nilesh Parekh. He was arrested by the Directorate of Revenue Intelligence sleuths for allegedly siphoning off 1,700 kg of imported duty-free gold and defrauding 25 banks. He was earlier arrested by CBI for allegedly siphoning off bank loans worth Rs 2,672 crore through hawala channels to dummy companies in different countries i.e Singapore, Dubai and Hong Kong.

One of the recent cases is of diamond trader Nirav Modi and his uncle Mehul Choksi in the year 2018 fled India before they could be arrested. The amount involved in the case was Rs. 14,000 crore. They were defrauding Punjab National Bank. It is considered as one of the biggest financial frauds in India.

8.0 Causes of Fraud in the Banking Sector

First and foremost reason for fraud in the case of the banking sector is the direct and indirect fault of their own officials. The fault could be intentional manipulations of rules and regulations for financial gains or could be unintentional due to lack of knowledge/ awareness of procedure and systems.

The other reason for fraud is non-adherence to KYC guidelines. During peak season, sometimes banks officials open accounts of customers, without completing all KYC norms, due to pressure and carelessness. The fraudster uses this benefit and opens their account, deposit forged cheques and withdraw the amount.

To achieve the business target, the staff of banks uses unethical ways. If there is lack of proper audit and inspection and suitable system, fraudulent activities increase in the system. Lack of proper internal control systems increases the chances of fraud. Poor control environment, improper documentation and inadequate accounting system also increase chances of fraud.

Use of new technology and financial software is also one of the causes. The lack of proper data security in new technology increases the chances of theft, cybercrime and other online frauds. Use of electronic channels like online banking, debit card, credit card, ATM, NEFT, Internet banking and mobile banking provides new ways to fraudsters.

Inexperience from the side of staff and lack of awareness from the side of customers also create fraudulent activities in the financial and banking system.

9.0 Regulatory Reforms Required to Handle Fraud in Indian Banking Industry

As elaborated in the paper that handling of financial frauds is a need of the hour. In order to avoid misuse of data and unscrupulous elements, Indian financial system needs to take stringent measures. Data which is shared from people to companies and to different institutions is misused, so it needs to be secured. People with low financial literacy have more chances to be trapped by frauds. Blockchain and Quantum computing are the new technologies that can be adapted to handle these issues. People living in rural area and women are the category in India, who has more chances to risk of financial abuse. Even for small and medium scale enterprises formal finance availability is a key challenge for them. The Reserve Bank of India has formed an expert committee to look into increasing cases of fraud. These are the steps which is necessary and need of the hour for our country. The government will need to build investigatory and judicial capabilities so that cases are decided in a reasonable time frame. Only time-bound closure of cases will reduce fraudsters. Our country also need to build institutional capabilities to be able to negotiate with foreign authorities in order to bring back fugitives and prosecute them under Indian laws. Thirdly, there is a need for proper governance norms for our public sector banks. Case like what happened in Punjab National Bank fraud is the consequence of a complete collapse of governance. Governance in PSBs needs an overhaul and government interference in appointments should be minimized. In this context, the P. J. Nayak committee (2014) rightly noted: “Government officers and regulators may not possess the skills to appoint the top management of commercial banks. Banking is a much specialized activity, and top management needs to combine strategic foresight with a good commercial knowledge of sectors to lend to, prudent risk management and human resource skills." Bank Board Bureau also needs to be established to tackle this issue. So our regulatory authorities should needs to revisit the way appointments are made in PSBs, starting with the Board. Only a professional board will be in a position to make the right decisions. It is important for banks to continuously improve operational efficiency by making the right investments in technology and human resources. As the government is in the process of recapitalizing PSBs, so it is the right time to initiate reforms. The increasing number of frauds affect the credit flow in the economy. In order to stabilize all this central bank of the country should revise frameworks. RBI has made it mandatory to report those accounts above rupee five crores on a weekly basis, which will help in timely action and continuous tracking of fraud cases.

There should be a strong rating agency who should evaluate projects in order to sanction loans. That agency should honestly evaluate projects before sanctioning without any external influence. The help of external auditors can also be taken to handle this type of situation. To ensure effective implementation of Red Flagged accounts proper information technology is the key requirement. Fraudulent reporting by auditors is also a major issue, strong implementation of law is mandatory to avoid fraudulent reporting. The persons who are declared as wilful defaulters, strong action must be taken to handle these. In many countries, it is a criminal offence while in India it is still a civil offence.

Financial literacy as discussed earlier is a key requirement. Customers, as well as staff members, should be educated, workshops special seminal to train them should be organize time to time. Banks should strictly follow corporate governance norms. Business ethics practices and corporate governance norms should be strictly followed.

Responsible position of bank staff should be filled with experienced and reliable persons. Incentive schemes of bans staff members should be introduced based on their integrity and efficiency to manage fraud, especially top management positions. There is a need to have strong coordination of banks, RBI and other investigating agencies in order to find out fraud cases.

There is a strong need for strengthening the appraisal and monitoring system in public sector banks. Poor technology, lack of proper automation, lack of motivation among staff are some reasons for increased inefficiency in the banks.

Besides bankers, customers also need to do the following to avoid fraud. All banking customers should register their contact information (mobile) with banks to receive SMS/email alerts and other mobile banking operations etc. Customers should regularly check emails and messages received from the bank. Customers should learn that they should never share passwords or OTP (One time Password) with anyone. For any suspicious transaction immediately report to the bank about that and customers using debit and credit cards should not share numbers displayed at their back with anyone as it will end up losing money.

10.0 Conclusion

The study reveals that there are many reasons for fraud, primarily related to the poor regulatory system, carelessness of employees, lack of proper supervision by top management, improper use of technology, lack of awareness of customers and employees and poor coordination. To overcome these issues, banks should constantly monitor the system and regularly review and check transactions which may cause online fraud. With the increasing usage of e-banking and internet and mobile banking, the risk of fraud is increasing. To address this issue, there is a need to educate customers and create awareness. It is high time that we make more stringent laws to curb the growing menace of corruption among the banking officials. The foremost challenge for bankers is to secure banks and customers from internet-related crimes. Banking operations such as Inter-branch transactions, Loans, Deposits and other online transactions should be highly secured. Legal requirements and procedural control should also be adequate to deal with that. Therefore, focus should shift towards strengthening the audit quality by plugging procedural gaps and streamlining the checks and balances. Moreover, programmes related to awareness and education to bank staff and customers should be organised from time to time to save the nation from these frauds, which have the potential to create a question mark on the reputation of our economy.

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