

Banking Scams in India

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Abstract

Banking scam is also known as banking fraud. Banking fraud is a criminal act. The top three fraud risks that are currently the highest concern for banks are: Internet banking and ATM frauds, e-banking (credit card, debit card, etc.), and identity fraud. Fraud and its redressal is a major concern area for the banking sector and across all portfolios – retail, corporate, and priority sector. Bank fraud is almost always a federal crime. This is because most banks are protected by the Federal Deposit Insurance Corporation, a federal program that protects consumers' deposits in banks and other financial institutions. Bank fraud is considered to be a white-collar crime. Common types of bank frauds include: Bank impersonation, stolen checks, forgery, fraudulent loans, internet fraud, etc. Offences related to banking activities are not only confined to banks but have a harmful impact on their customers and society at large. These frauds are now becoming more and more frequent and can be considered as one of the main reasons for damaging the economy of the country. Nirav Modi bank scam, bank scam by Vijay Mallya, Allahabad Bank scam, Rotomac Pen scam, RP Info Systems bank scam, Simbhaoli Sugar Mills bank scam, United Bank of India, Karnataka Bank case, SBI fraud case, etc., are the bank frauds that have rocked Indian banking sector. In this article, the researcher aims to provide an overview on the most important banking frauds.

Keywords: Scam, Credit card, Debit card, Frequent, Indian banking sector, Economy

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MEANING OF BANK FRAUD

In contractual term, as described in the Indian Contract Act, according to Sec. 17 *fraud* means and includes any of the following acts committed by a party to a contract, or with his connivance, or by his agent, with intent to deceive another party thereto or his agent, or to induce him to enter into the contract:

- (1) the suggestion, as a fact, of that which is not true, by one who does not believe it to be true;
- (2) the active concealment of a fact by one having knowledge or belief of the fact;
- (3) a promise made without any intention of performing it;
- (4) any other act fitted to deceive; The expression 'any other act fitted to deceive' obviously means any act, which is done with the intention of committing fraud.
- (5) any such act or omission as the law specially declares to be fraudulent.

Bank fraud is a criminal act in which a person or organization tries to illegally obtain money from a bank or financial institution or that occurs when a person uses illegal means to receive money or assets from a bank or other financial institution. Bank fraud is distinguished from bank robbery by the fact that the perpetrator keeps the crime secret, in the hope that no one notices until he has gotten away. Any illegal act that involves the use of deception to obtain money or other property from a financial institution, or from a bank's depositors, is often categorized as bank fraud. Banking fraud constitutes a criminal offense subject to monetary penalties and incarceration. There are many different ways that bank fraud can be carried out. One of the oldest and most traditional forms of banking fraud is money laundering. Money laundering involves taking large sums of illegally obtained money and filtering it through a legitimate business or source in order to make the money seem legitimately earned, or clean. Common sources of laundered money include

drugs and organized crime. The term bank fraud also refers to attempts by a person to obtain money from a bank's depositors by falsely pretending to be a bank or financial institution. Banking Frauds constitute a considerable percentage of white-collar offences being probed by the police. The court system views fraud as a civil wrong known as a *tort*. Unlike ordinary thefts and robberies, the amount misappropriated in these crimes runs into lakhs and crores of rupees. Bank fraud is a federal crime in many countries, defined as planning to obtain property or money from any federally insured financial institution. It is sometimes considered a white-collar crime. The four most important elements for constituting fraud are: the active involvement of the staff; failure to follow the instructions and guidelines of the bank by the staff; collusion between businessman, executives, and politicians to bend the rules and regulations; and any other external factors. In general, banking fraud involves the use of illegal means to obtain money, property, or assets held by a bank or financial institution. It also encompasses situations in which an individual falsely poses as a bank for the purpose of obtaining another individual's investments or deposits.

CLASSIFICATION OF BANK FRAUD

Banking frauds can be classified as:

- Fraud by insiders
- Fraud by outsiders
- Both

Fraud by Insider

Fraud by insiders includes loan fraud, cash shortages, fraud in borrower's account, fraud in investment portfolios, fraud in foreign exchange areas, purchased bill fraud, deposit account fraud, frauds in computerized environment, frauds in inter-branch and inter-bank account, etc.

Purchased Bill Frauds

These are generally expensive and can take the following forms: discount on stolen or fake railway receipts and motor receipts along with other necessary bills, forged/fake bills with inflated value, drawn on sister concern are discounted, fake/forged bills for valueless goods are discounted. The fraudster discounts

bogus or stolen railway receipts. False bills are drawn on sister concerns for the purpose of discounting. Bills are inflated in collusion with the supplier. Payment is obtained before the bill is presented by the bank for encashment. Worthless goods are dispatched and bills discounted on the strength of dispatched papers [1].

Loan Fraud

Many loaning agencies only require a small amount of information in their lending application process. This makes it easy for identity thieves to use your stolen information anything from your social security number to your banking information to get a quick loan. Payday loans make it easy for thieves to obtain cash in your name without much verification. Or worse, with enough stolen details, they could open up a legitimate car, home, or business loan.

Fraud in Borrower's Account

For all borrower loans, the borrower's identity is verified against data from consumer reporting agencies and other identity and anti-fraud verification databases. Advance against clean/documentary bills purchased /discounted.

Fraud in Foreign Exchange Areas

Foreign exchange fraud is any trading scheme used to defraud traders by convincing them that they can expect to gain a high profit by trading in the foreign exchange market.

Frauds in Computerized Environment

As computers and related devices such as smart phones have become more common increasingly, they have also been used by criminals [2]. Computer fraud can be described as a subset of computer crime. Computer fraud uses electronic resources to present fraudulent or misrepresented information as a means of deception [3]. Computer frauds include Phishing/Vishing/SMiShing. Phishing refers to an e-mail that appears to have been sent by a legitimate party, such as a bank, government agency, or well-known business. The e-mail asks you to take action on an urgent matter by clicking on a link to a seemingly official website and providing your information. This is when a criminal tricks you into handing over your personal information via e-mail or

phone With a similar ruse, vishing attempts to gain access to your information by providing a fraudulent phone number to contact after informing you of unusual activity via voice-mail, e-mail or text message. Through SMiShing, fraudsters try to acquire your information via step-by-step instructions sent by text message from what appears to be a credible source [4].

Deposit Account Fraud

The following types of frauds are generally committed: value inflation of checks deposited, changing the nature of the checks (crossed to bearer), operating a dormant account fraudulently, non-deposition and misappropriation by agents.

Frauds in Inter-Branch and Inter-Bank Accounts

Debiting bank accounts without remitting cash; debiting branch-adjusting account without remitting cash.

Fraud by Outsider

Fraud by outsider includes bill discounting fraud, forgery and altered checks, accounting fraud, stolen check frauds, credit card frauds, booster checks, etc.

Booster Checks

A booster check is a fraudulent or bad check used to make a payment to a credit card account in order to raise the amount of available credit on otherwise legitimate credit cards.

Bill Discounting Fraud

Fraudster uses a company to gain confidence with a bank, by appearing as a genuine, profitable customer. The company regularly and repeatedly uses the bank for discounting the bills of its customers. Bills are paid timely, as the customers also are part of the fraud.

Forgery and Altered Checks

A check that bears a forged signature of the drawer or payee is generally not properly payable from the customer's account because the bank is not following the instructions of the depositor precisely as he gave them. Check fraud involves tampering with the rules of checking account transactions for illegitimate reasons and uses [5].

Stolen Check Frauds

Check frauds include frauds relating to customer's checks, banker's checks (drafts) or traveler checks. They are the most important frauds loss-wise. Stolen blank checkbooks are also of value to forgers who then sign as if they were the depositor [6].

Accounting Fraud

In order to hide serious financial problems, some businesses have been known to use fraudulent book keeping to overstate sales and income, inflate the worth of the company's assets or state a profit when the company is operating at a loss. These tampered records are then used to seek investment in the company's bond or security issues or to make fraudulent loan applications in a final attempt to obtain more money to delay the inevitable collapse of an unprofitable or mismanaged firm [7].

Credit Card Frauds

Credit card skimming is the type of fraud you have to worry about when you are out and about. In order to siphon off card information, thieves install devices known as skimmers on ATMs or payment terminals [8]. The crime of credit card fraud begins when someone either steals a credit or debit card, or fraudulently obtains the card number and other account information necessary for the card to be used successfully. Credit card fraud is broadly used to refer to the use of a credit card, debit card, or any similar form of credit, to make purchases, or to obtain financial gain with the intention of avoiding payment. This includes identity theft, identity assumption, and fraud spree. In the eyes of the law, certain elements are required for a financial or identity theft crime to be classified as a form of credit card fraud. These include: credit card theft: the taking of a credit card, or credit card number, from another person, without the cardholder's consent, with the intent of using or selling it. Credit card forgery: purchasing of something of value using a credit card, by someone other than the cardholder, or an authorized user, with the intent of defrauding the card's issuer. Credit card fraud: taking of a credit card, or credit card number, from another person, with the

intent to use, sell, or transfer it to another person, or using the credit card or card number to purchase something of value, with the intent to defraud.

BANKING SCAM IN INDIA

Nirav Modi Bank Scam

Fraud amount: 11,400 crore. On 14th February 2018 one of the India's biggest banks disclosed an almost \$2 billion fraud allegedly by one of the country's richest men, who deals in pearls and diamonds. Shares of the lender, Panjab National Bank, plunged on the news, dragging down other lenders when it said the scam may extend to multiple banks. Panjab National Bank is country's second largest public lender is the middle of a Rs. 11,400 crore transaction fraud case. This bank scam is being called the biggest scam (Rs. 11,400 crore) in the banking sector of India. The main accused of the scandal is billionaire jeweler Nirav Modi and his uncle Mehul Chokshi owner of Gitanjali Gems). Both of them had received "Letter of Undertaking" from the consent of the employees of PNB's Mumbai branch and withdrawn the funds from the foreign banks on the guarantee of Punjab National Bank. However, the Enforcement Directorate has seized assets of Nirav worth over Rs. 5870 crore. Kolkata-based Allahabad Bank has claimed of having an exposure of Rs. 2363 crore in the PNB fraud case. The scam in the Allahabad Bank involved the misuse of SWIFT technique by the internal employees of the Allahabad Bank.

Bank Scam by Vijay Mallya

Fraud amount: Rs. 9432 crore. Vijay Mallya, the "king of good times", a beer baron has always been in news. All thanks to his over-the-top, extravagant lifestyle, Mallya and his companies have been embroiled in financial scandals, and controversies since 2012. In November 2015, it came to limelight that Mallya owed at least \$1.35 billion to the banks in India. In March 2016, a consortium of banks approached the Supreme Court of India to stop Mallya from going abroad due to pending money his companies owed them. Courts then issued non-bailable arrest warrants against the businessman. Mallya's Kingfisher Airlines had borrowed Rs. 9432 crore from 13 banks till February 2018. The State Bank of

India was the biggest lender with Rs. 1600 crore, followed by the PNB Rs. 800 crore, IDBI Rs. 650 crore and Bank of Baroda Rs. 550 crore. Mallya left India on March 2, 2016, and is hiding in London. The government of India is fighting for his extradition till date. Mallya's case is unique in the Indian banking industry in many ways. It is both shocking and demeaning that an individual has successfully managed to take some 17 banks for a ride. Banks acting as charity houses for lending loans to Mallya calls people to question the credibility of authorities involved in credit appraisal process. There is finally light at the end of the tunnel as the banking system has finally decided to lay their hands on "rich and powerful".

Allahabad Bank Scam

Fraud amount: Rs. 2363 crore. Kolkata-based Allahabad Bank has said it has an exposure of Rs. 2363 crore in the PNB fraud case. However, Allahabad Bank stressed that it is sure about the recovery of the payment as the exposure was fully secured by Letter of Undertaking (LoU) documents. The bank, through its overseas branch at Hong Kong, has been taking exposure with Punjab National Bank as counter-party under various Letters of Undertakings issued through authenticated SWIFT messages. SWIFT stands for the "Society for Worldwide Interbank Financial Telecommunications". It is a messaging network that financial institutions use to securely transmit information and instructions through a standardized system of codes. To do the scam in Allahabad bank, the SWIFT technique was misused by internal employees of the bank. The internal banking system of Allahabad Bank was not attached to SWIFT that is why the transactions were not mentioned in the accounting books of Allahabad Bank. That is why there was no transaction record found between PNB and Nirav Modi.

Rotomac Pen Scam

Fraud amount: Rs. 3695 crore. The promoter of Rotomac Pen, Vikram Kothari, allegedly fraudulently cheated Rs. 3695 crore with seven banks. Kothari has misappropriated loans worth Rs. 2919 crore from seven banks and the total outstanding amount, including

interest on him, is Rs. 3695 crore. The CBI has arrested managing director of Rotomac Global Pvt. Ltd., Vikram Kothari [9]. Vikram Kothari, allegedly fraudulently cheated Rs. 3695 crore with seven banks. Rotomac Global Private Limited cheated a consortium of banks to the tune of Rs. 36.95 billion (Rs. 3695 crore), including interest by siphoning off loans sanctioned to the company for procurement of wheat and other goods for export. The CBI registered a case after receiving a complaint from Bank of Baroda against Kanpur-based Rotomac Global Private Limited, its director Vikram Kothari, his wife Sadhana Kothari, and son Rahul Kothari and unidentified bank officials. Initially, the alleged scam was estimated to be of Rs. 8 billion (Rs. 800 crore) but after the CBI started to probe into the accounts of the company, it was found that the company had allegedly taken loans from Bank of India, Bank of Maharashtra, Indian Overseas Bank, Union Bank of India, Allahabad Bank, and Oriental Bank of Commerce.

Seven banks acted as the consortium. These include:

Bank of India – Rs. 7.55 billion (Rs. 754.77 crore)

Bank of Baroda – Rs. 4.57 billion (Rs. 456.63 crore)

Indian Overseas Bank – Rs. 7.71 billion (Rs. 771.07 crore)

Union Bank of India – Rs. 4.59 billion (Rs. 458.95 crore)

Allahabad Bank – Rs. 3.31 billion (Rs. 330.68 crore)

Bank of Maharashtra – Rs. 489 million (Rs. 49.82 crore)

Oriental Bank of Commerce – Rs. 974 million (Rs. 97.47 crore)

In Rotomac pen scam, the principal loan is about Rs. 824 crore, adding the interest due would indicate a loss of more than Rs. 1000 crore to the banks. The main accused in this scam is Kanishka Gold Pvt. Ltd. This company did not pay a loan of Rs. 824 crore, which has been converted into “NPA”. The CBI has registered a case against Chennai-based company Kanishka Gold and ED has started investigating the fraud. The director of this company Bhupendra Kumar Jain and his wife Neeta Jain have fled the country.

These banks have lent money to the Kanishka Gold Pvt Ltd

1. State Bank of India: Rs. 240 crore
2. Punjab National Bank (PNB): Rs. 128 crore
3. Bank of India: 46 crores
4. IDBI:- 49 crores
5. Syndicate Bank: - 54 crores
6. Union Bank: - 53 crore
7. UCO Bank: - 45 crores
8. Central Bank of India: - 22 crores

RP Info Systems Bank Scam

Fraud amount: Rs.515.15 crore. The CBI booked a computer manufacturer RP Info Systems and its directors for allegedly cheating a consortium of 9 banks with amount of Rs. 515.15 crore. This company has used fraud documents to take the loan. CBI raided the offices of the company in Kolkata and other places on February 28, 2018. Shivaji Panja, one of the directors of RP Info System, was questioned after the CBI booked RP Info Systems and its officials for the alleged fraud on a consortium of banks, and carried out searches at the homes of all the accused and the corporate office in Kolkata, an official said. It was alleged that the company's directors, Shivaji Panja, Kaustuv Ray, and Vinay Bafna, cheated Canara Bank and nine other members of the banking consortium to the tune of Rs. 515.15 crore. Canara Bank had clarified that the complaint filed against RP Info Systems and its directors for allegedly cheating a consortium of banks, in which it is a member, is a revised one. RP Info Systems allegedly obtained credit facilities from at least 10 PSU banks, including SBI and two of its erstwhile associate banks, by submitting fabricated documents [10].

Simbhaoli Sugar Mills Bank Scam

Fraud amount: Rs. 200 crore. CBI has registered another bank fraud against one of India's largest sugar mills- Simbhaoli Sugars Ltd, amounting to Rs. 200 crore. There are 10 people who have been booked, including the chairman of Simbhaoli Sugar Mills Limited, Gurmeet Singh Mann, Deputy Managing Director, Gurpal Singh, and CEO, GSC Rao. The loans were taken from Oriental Bank of Commerce. The CBI (Central Bureau of Investigation) registered a case of bank fraud, against one of India's

largest sugar mills – Simbhaoli Sugars Ltd. amounting to Rs. 200 crores.

The Uttar Pradesh-based private sugar company, its top officials, along with unknown bank officials have been booked by the agency for allegedly defaulting on loans taken from the Oriental Bank of Commerce (OBC). According to the CBI, the Hapur-based Simbhaoli Sugars Ltd. in 2011 fraudulently diverted funds received as loans for sugarcane farmers and self-help groups. Officials said that the bank sanctioned a loan amounting to Rs. 148.60 crore in 2011 to the private company for financing individuals, joint liability groups, and self-help groups under the tie-up arrangement under the RBI scheme to 5762 sugarcane farmers supplying sugar produce to the said private company during the period from January 25 to March 13, 2012.

But, allegedly, the funds were diverted for personal use. The loan amount was then converted into a non-performing asset on March 31, 2015.

CONCLUSION

Money is laundered through a web of companies located in different geographies, making it difficult to check such transactions. To fight this, the Reserve Bank of India (RBI) has introduced Legal Entity Identifier or LEI. Its key aim is to check and prevent banking frauds [11].

National Financial Reporting Authority (NFRA) as an independent regulator for the auditing profession. It has come as a suggestion by the Supreme Court to bring about an independent regulator for the auditing profession. Parliament passing the Fugitive Economic Offenders Bill into law to help solve the NPA problem of the banking system: The Fugitive Economic Offenders Act, 2018 came into force on 21st April 2018. There have been various laws that deal with economic offenders leaving the country to escape criminal proceedings, it was felt that the existing civil and criminal provisions in the law were not enough to deal with the existing problems in the system. YH Malegam Committee was constituted by RBI to look

into the rising instances of fraud: RBI constituted this specific committee to look into the whole matter of bad loans, including matters of the effectiveness of audits, classification of bad loans and the rising number of incidents of fraud cases. It is to be headed by YH Malegam, who is a former member of the Central Board of Directors of the RBI [12].

The impact of frauds on entities like banks, and the economic cost of frauds can be huge in terms of likely disruption, confidence in the banking system and may damage the integrity and stability of the economy. It can bring down banks, undermine the central bank's supervisory role and even create social unrest, discontent and political upheavals. The vulnerability of banks to fraud has been heightened by technological advancements in recent times. The challenge before investigation agencies lies in shape of capacity building, quality of investigation, support from experts. The Government of India enacted the Information Technology Act, 2000, to provide for punishment and penalties in respect of frauds committed in respect of computers.

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