



A PROJECT REPORT



ON

**"A PROJECT REPORT ON FINANCIAL FRAUDS AND SCAMS IN
INDIAN BANKING SYSTEM"**

Submitted To:-

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INTRODUCTION

INTRODUCTION

The Indian banking sector has experienced significant growth and changes since liberalization of economy in 1991. Though the banking industry is generally well regulated and supervised, the sector suffers from its own set of challenges when it comes to ethical practices, financial distress and corporate governance. In recent years, instances of financial frauds have regularly been reported in India. Although banking frauds in India have often been treated as cost of doing business, post liberalization the frequency, complexity and cost of banking frauds have increased manifold resulting in a very serious cause of concern for regulators, such as the Reserve Bank of India (RBI).

Fraud vitiates every solemn proceeding and no right can be claimed by a fraudster on the ground of technicalities.

The definition of fraud as defined in the Black's Law Dictionary, which is as under:
“Fraud means:

- A knowing misrepresentation of the truth or concealment of a material fact to induce another to act to his or her detriment. Fraud is usually a tort, but in some cases (especially when the conduct is wilful) it may be a crime.
- A misrepresentation made recklessly without belief in its truth to induce another person to act.
- A tort arising from a knowing misrepresentation, concealment of material fact, or reckless misrepresentation made to induce another to act to his or her detriment.

- Unconscionable dealing; esp., in contract law, the unconscientious use of the power arising out of the parties' relative positions and resulting in an unconscionable bargain."

Informally, the terms "fraud" and "scam" are often used interchangeably to describe any type of financial wrongdoing. However, from a legal perspective, fraud typically encompasses a broader and more serious criminal offense, while scams are a specific category within fraud.

A scam refers to a deceptive scheme that usually involves money and some form of business transaction. Scams can take on different forms and shapes. For instance, you might have encountered situations where someone promised you a prize if you provided your credit card details or asked you to donate money to a non-existent charity. Scams can reach us through various channels, such as telephone calls, emails, or even in-person encounters.

Fraud implies a deception. It is a breach of confidence or trust. Fraud is a serious crime and a violation of civil law. The motivations for fraud can be many. These include monetary gain, discrediting an opponent or adversary. It can be to gain prestige as well as a financial advantage.

Various authors on banking including even those who are writing books distinctively on the issue of Banking Frauds have not attempted to define Banking Fraud, rather have tried to give the broad outline of the Banking Frauds by enumerating different instances of frauds in banking sector.⁷ The term 'Banking Fraud' contains two elements namely 'Banking' and 'fraud'. Beginning with simple money-changing as per its the earliest traced history, the term 'banking' has today found synonymy with five core functions of accepting deposits, lending, investment, repayment and facilitating of withdrawal of money. And in common parlance, 'fraud' is a dishonest act done with the intention of gaining benefit by causing loss to others. Legally speaking, 'fraud' refers to a false statement of fact by a person or his agent who himself doesn't believe the statement to be true,

made with an intention of deceiving another party, and inducing him to enter into a contract on that basis. Thus 'fraud' is a very wide term which includes any behaviour by which one person intends to gain a dishonest advantage over another.

It signifies not only act of commission but also an act of omission which is intended to cause wrongful gain to one person and/or wrongful loss to another. Accordingly 'Banking fraud' is a broad term used to signify all types of frauds committed in a banking system. It may be committed with accounts, negotiable instruments, loans, securities or any other banking service. Again, it may be pulled off by customer, employee, outsider or by the bank itself, or by two or more of parties in connivance with each other. A common term to describe all such frauds is 'Banking Fraud'. Banking frauds may be committed by way of concealment, embezzlement, breach of trust, theft, cheating, forgery, falsification of accounts, conspiracy etc.

AIMS & OBJECTIVES **OF STUDY**

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- To determine the reason behind 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 in order to protect different stakeholders.
- To trace out the various traditional as well as modern technological frauds prevailing in the banking system.
- To find out the relevancy and adequacy of Indian law on Banking Frauds.
- To judge the impact of modern techniques and trends of the business system in allowing or excluding Banking Frauds.
- To find out the existing preventive and curative measures in place to address the menace of Banking Frauds.
- To determine the desirability of a new comprehensive independent legislation to check Banking Frauds in India.
- To make efforts to suggest positive steps to curb the menace of Banking Frauds which pose a legal challenge in the 21st Century.

RESEARCH METHADODOLOGY

RESEARCH METHADODOLOGY

❖ Sources of data:-

Research is totally based on primary data, secondary data can be used only for the preference, research has been done by primary data collection, and primary data has been collected by interacting with various people, the secondary data has been collected through various journals and website.

- **Primary data: -**

To achieve the objective of the study author relies on past data available with the RBI.

- **Secondary data: -**

The data were gathered from the secondary sources such as Annual Reports of the Banks, RBI Report of Trends and Progress of Banking in India, Manuals of instructions on loans and advances, journals, research paper and articles published online and offline on various newspapers and websites.

LIMITATION OF THE STUDY

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The study is for limited period of Indian public sector banks of 2010 to 2021.
The focus is on study of banking scams and frauds.

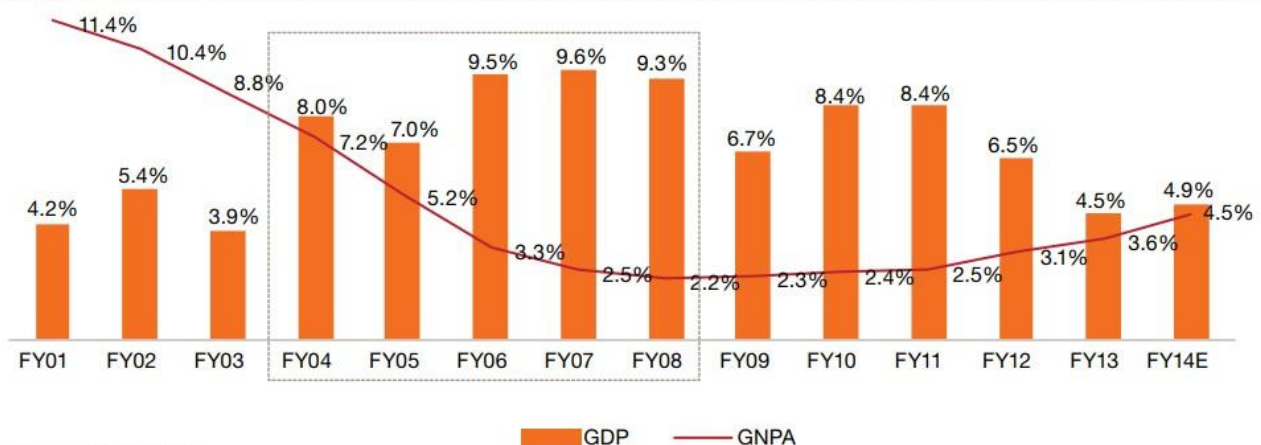
FINANCIAL FRAUDS AND
SCAMS IN
INDIAN BANKING SYSTEM

FINANCIAL FRAUDS AND SCAMS IN INDIAN BANKING SYSTEM

An effective banking system plays a crucial role in the economic growth and progress of any country. As numerous economic factors come into play, both at national and global levels, the role of the banking sector has evolved significantly over time. This evolution has enabled the financial industry to explore new opportunities and expand its influence beyond national boundaries.

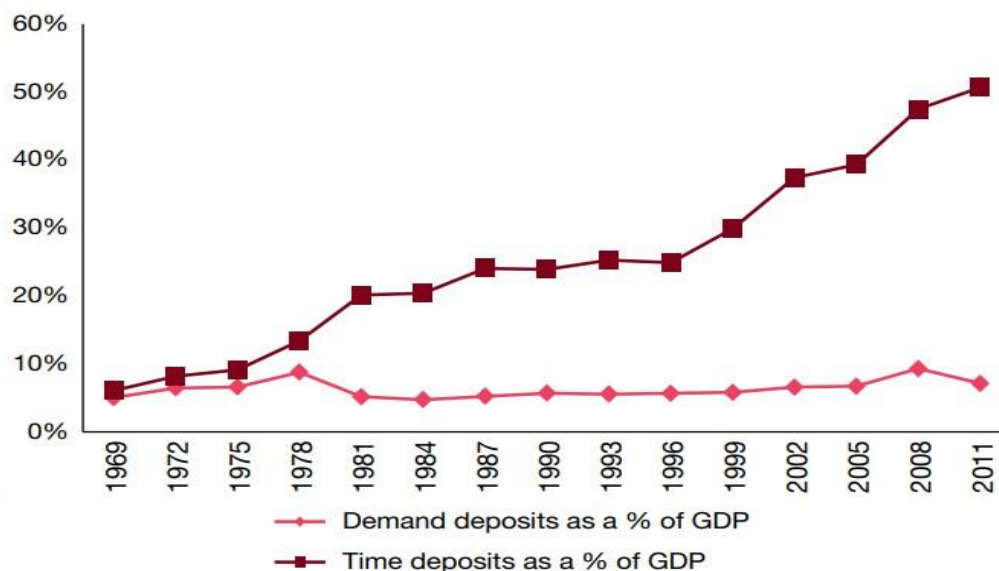
The banking industry has undergone major transformative changes in line with the shifting landscape of trade and commerce. These reforms include the entrance of new private sector banks, the adoption of information technology (such as NEFT and Smart Cards), and revisions to capital adequacy standards, among others. These changes have significantly enhanced the efficiency and productivity of the banking sector. However, while India's banking sector continues to grow in terms of overall revenue and profits, the occurrence of bank fraud has been on the rise, causing concern for both the Reserve Bank of India and bank management.

Gross NPA vs GDP in India



Source: Reserve Bank of India

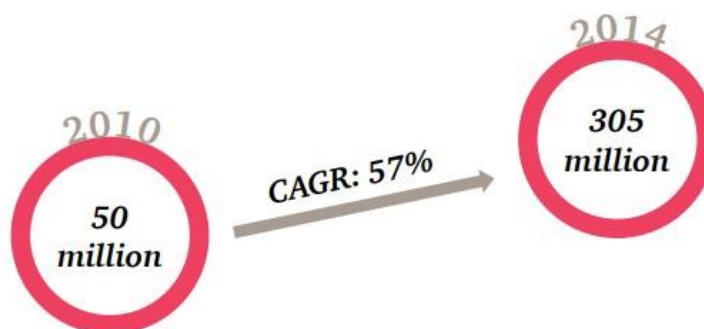
Scheduled commercial banks' deposits as a % of GDP



Total growth of deposits and credit of scheduled commercial banks (1980–2010)



Number of basic saving bank deposit accounts (BSBDAs)



In recent years, instances of financial fraud have regularly been reported in India. Although banking frauds in India have often been treated as cost of doing business, post liberalization the frequency, complexity and cost of banking frauds have increased manifold resulting in a very serious cause of concern for regulators, such as the Reserve Bank of India (RBI). RBI, the regulator of banks in India, defines fraud as “A deliberate act of omission or commission by any person, carried out in the course of a banking transaction or in the books of accounts maintained manually or under computer system in banks, resulting into wrongful gain to any person for a temporary period or otherwise, with or without any monetary loss to the bank”

These instances of bank fraud appear to be unique in terms of their modus operandi and involve substantial sums of money. This unfavorable trend in the financial system not only leads to financial losses for banks but also erodes trust in the banking sector.

❖ **Fraud as Defined In Section 17 of Indian Contract Act, 1872**

“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:

- the suggestion, as a fact, of that which is not true, by one who does not believe it to be true;
- the active concealment of a fact by one having knowledge or belief of the fact;
- a promise made without any intention of performing it;
- any other act fitted to deceive;
- any such act or omission as the law specially declares to be fraudulent.

In order to amount to Fraud, an act must be confined to acts committed by a party to contract with an intention to deceive another party or his agent or to induce him to enter into a contract.

Fraud, which vitiates the contract, must have a nexus with the acts of the parties entering into the contract.

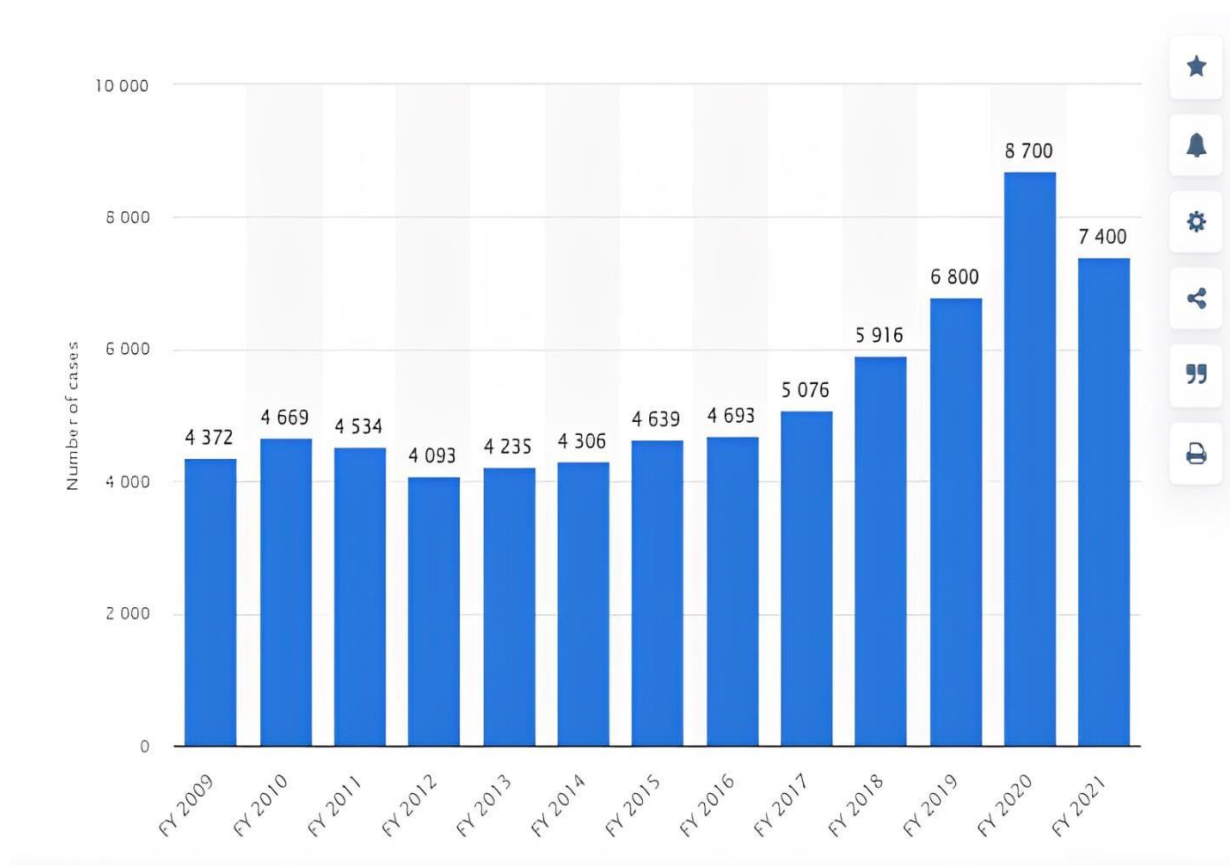
This definition highlights the precondition to prove the intention of the person who has committed Fraud. If that person has willingly committed a Fraud, then he will be punished. Here the person means himself or his agent. The acts which include fraud are wrong suggestions or concealment of facts or false promises or any fraudulent act to deceive others.

❖ **Fraud under the Companies Act, 2013**

The Companies Act, 2013 focuses on the issues related to corporate Fraud, as is visible, it may continue in the future too. As per Section 447, Fraud in relation to affairs of a company or a body corporate, includes any act, omission, concealment of any fact or abuse of position committed by any person or any other person with the connivance in any manner, with intent to deceive, to gain undue advantage from, or to injure the interests of, the company or its shareholders or its creditors or any other person, whether or not there is any wrongful gain or wrongful loss;

- “wrongful gain” means the gain by unlawful means of property to which the person gaining is not legally entitled;
- “Wrongful loss” means the loss by unlawful means of property to which the person losing is legally entitled.

❖ Number of bank fraud cases across India between from Financial year 2009 to 2021



Source: <https://www.statista.com/statistics/1012729/india-number-of-bank-fraud-cases/>

Over the past decade, Public Sector Banks (PSBs) in India have suffered significant financial losses due to various banking frauds. The Indian banking system has been grappling with the growth of Non-Performing Assets (NPAs) in recent years, creating a destructive cycle that affects its sustainability. In its annual report for the year 2020-21, published in May 2021, the Reserve Bank of India (RBI) disclosed that a staggering 22,864 banking frauds were reported in the last three years, involving a massive amount of over INR 3.95 trillion.

Some notable frauds that occurred during this three-year period include the ICICI Bank-Videocon bribery for loan scam in 2020, the crisis at Punjab and Maharashtra Co-operative Bank in 2019, and the Nirav Modi and Gitanjali Gems-Punjab National Bank scam in 2018. Investigations into these cases have revealed the involvement of not only mid-level employees but also senior management within the banks.

❖ **Major bank scams in India in last decade:-**

- **Scam by Vijaya Mallya :-**

Vijay Mallya, once a prominent Indian businessman, enjoyed success as the leader of United Breweries and the founder of Kingfisher Airlines. However, his ventures encountered severe financial difficulties. Despite United Breweries becoming a major player with a net turnover of approximately 300 crore, Mallya's ambitious expansion plans and economic challenges led to financial strain.

Kingfisher Airlines, which aimed to provide luxurious air travel, faced mounting debts. The airline accumulated a staggering debt of around 9,000 crore, including loans from multiple banks. External factors like a global recession, rising crude oil prices, and a depreciating rupee added to the airline's financial woes.

Unable to sustain operations, Kingfisher Airlines ceased operations in 2012, leaving unpaid debts and disgruntled creditors. Mallya faced legal troubles and was accused of loan default and financial irregularities. In 2016, he left India and took refuge in the United Kingdom to avoid legal repercussions, becoming a fugitive from justice.

The case of Vijay Mallya serves as a cautionary tale, illustrating the risks of overexpansion and financial mismanagement in the business world. It highlights the importance of responsible financial practices and the consequences of defaulting on financial obligations.

- **Nirav Modi scam:-**

Nirav Modi, a renowned jeweler, obtained loans from overseas branches using Letters of Undertaking (LOUs) issued by Punjab National Bank (PNB). These LOUs were issued through PNB officials using the SWIFT messaging system, bypassing the mainstream banking system's evaluation parameters.

The fraudulent activities came to light when the PNB official responsible for issuing the LOUs retired in 2017. The successor, unable to find records of past transactions in the system, refused to roll over the LOUs that were due in January 2018. This raised suspicions and led to an investigation.

On February 14, 2018, PNB made a shocking announcement, revealing that fraudulent transactions worth \$1.77 billion (approximately Rs 11,400 crore) had been discovered at one of its branches in Mumbai. The fraudulent activities involved Nirav Modi and his associates, who had taken advantage of the LOUs to obtain funds from overseas banks.

The revelation of this massive fraud scandal had a significant impact on PNB's reputation and the Indian banking sector as a whole. It exposed weaknesses in the bank's internal control systems and raised concerns about the effectiveness of regulatory oversight.

The case of Nirav Modi's fraudulent transactions serves as a stark reminder of the importance of robust risk management, stringent internal controls, and thorough monitoring of financial transactions to prevent such fraudulent activities within the banking industry.

- **Rotomac scam:-**

In 2018, Vikram Kothari, the Managing Director of Rotomac Global Pen Ltd, came under scrutiny for allegedly cheating seven banks out of Rs 3695 crores. It is claimed that he misappropriated loans amounting to Rs 2919 crore from these banks. The fraudulent activities of Rotomac Global have triggered investigations by both the Enforcement Directorate and the Central Bureau of Investigation (CBI), prominent law enforcement agencies in India.

As part of the ongoing investigations, Vikram Kothari was subsequently arrested by the CBI, marking a significant development in the case. The Enforcement Directorate, responsible for probing financial crimes and money laundering, and the CBI, specializing in complex criminal cases, are diligently working to gather evidence and ascertain the full extent of the fraud committed by Vikram Kothari and his company.

The events surrounding the alleged fraud perpetrated by Vikram Kothari and the subsequent investigations and arrest highlight the importance of combating financial malpractices. These incidents unfolded in the year 2018, shedding light on the consequences individuals may face when engaging in fraudulent activities and the dedication of law enforcement agencies to ensure accountability.

- **IL&FS, September 2018:-**

It has multiple businesses and highest ratings but was unable to pay its loans. The rating agencies stated that company showed an increase of 99 percent NPAs during March 2017, Rs 410 crore to March 2018 Rs 816 crore. The company was reconstituted by the government. At present, it is pursuing asset sales to realize funds and pay off book debts. In spite of restructuring Rs 5,100 crore debts, the group still has external debt of Rs 94,216 crore. Due to collapse of IL&FS, the entire banking system witnessed biggest liquidity freeze. Most NBFCs are now struggling for their survival due to liquidity shortage across banks and NBFCs.

- **IDBI Bank, March 2018:-**

The IDBI Bank scam refers to a fraudulent scheme that took place in 2018, involving IDBI Bank, a prominent Indian public sector bank. The scam revolves around loans extended by IDBI Bank to certain companies, primarily Kingfisher Airlines, which later turned into non-performing assets (NPAs).

In this case, it was alleged that IDBI Bank officials colluded with the borrowers to facilitate the disbursement of large loans without proper due diligence or adequate collateral. The loans were granted to these companies despite their poor financial condition and repayment capacity, leading to a significant financial loss for IDBI Bank.

The scam came to light when the loans granted to Kingfisher Airlines, owned by Vijay Mallya, defaulted. It was revealed that the bank officials had overlooked proper risk assessment and disbursed loans without proper safeguards. The scam raised concerns about the integrity of the banking system and the role of bank officials in facilitating fraudulent activities.

As a consequence of the scam, investigations were launched by various authorities, including the Central Bureau of Investigation (CBI) and the Enforcement Directorate (ED). The authorities focused on uncovering the details of the fraudulent loan disbursements, identifying the individuals involved, and determining the extent of financial irregularities.

The IDBI Bank scam of 2018 serves as a reminder of the importance of robust risk management, due diligence, and adherence to regulatory guidelines in the banking sector. It highlighted the need for greater accountability and transparency to prevent such fraudulent practices and safeguard the interests of financial institutions and their stakeholders.

❖ Classification of frauds

The RBI's Master Directions on Frauds – Classification and Reporting by commercial banks and select FIs (Updated as on July 03, 2017) provides different categories of offences that constitute fraud, putting specific reliance on the Indian Penal Code, 1860. The classifications are provided hereunder:

1. Misappropriation and criminal breach of trust.
2. Fraudulent encashment through forged instruments, manipulation of books of account or through fictitious accounts, and conversion of property.
3. Unauthorised credit facilities extended for reward or for illegal gratification.
4. Negligence and cash shortages.
5. Cheating and forgery.
6. Irregularities in foreign exchange transactions.
7. Any other type of fraud not coming under the specific heads as above.

❖ **Fraud by insiders:-**

- **Rogue traders**

A rogue trader is a high-ranking insider who is ostensibly authorized to invest large sums of money on behalf of the bank. This trader secretly makes increasingly aggressive and risky investments with the bank's funds, and when one investment fails, the rogue trader engages in further market speculation in the hope of making a quick profit to cover or hide the loss. Unfortunately, when one investment loss follows another, the expenses to the bank can quickly mount into the hundreds and millions of rupees resulting in a grave loss for the bank.

- **Fraudulent loans**

Taking out a loan is one of the methods to get money out of a bank, and it's a behavior that bankers would be happy to encourage if they knew the money would be repaid in full with interest. A fraudulent loan, on the other hand, is one in which the borrower is a business entity managed by a dishonest bank officer or an accomplice, and the money is lost when the borrower files bankruptcy or disappears. The borrower might even be a non-existent organization, with the loan serving as a front to cover a large-scale bank robbery. Based on the recommendations of an Internal Working Group constituted by the Bank, a framework for dealing with loan frauds was put in place vide circular dated May 7, 2015.

- **Wire fraud**

Wire transfer networks, such as the international interbank fund transfer system, are appealing targets since a transfer is difficult or impossible to reverse after it has been done. Rapid or overnight wire transfers of large sums of money are commonplace because these networks are used by banks to settle accounts with one another. While banks have put checks and balances in place, there is a risk that insiders will try to use fraudulent or forged documents claiming to request a bank depositor's money be wired to another bank and often an offshore account in some faraway foreign country.

- **Forged or fraudulent documents**

Banks like to count their money precisely, thus every cent must be accounted for, hence forged documents are frequently used to mask other frauds. A document declaring that an amount has been obtained as a loan, withdrawn by an individual depositor, transferred, or invested might therefore be useful to a criminal who wants to hide the minute detail that the bank's money has been stolen.

- **Theft of identity**

Depositors' personal information has been known to be disclosed by dishonest bank employees for use in identity theft and fraud. The information is then used to get identity cards and credit cards in the victim's name and personal details.

- **Demand Draft (DD) fraud**

The Bunko Banker is generally one or more dishonest bank workers that commit DD fraud. They take a few DD leaves or DD booklets from the stock and use them as normal DDs. They understand the coding and punching of a demand draft since they are insiders. These demand drafts will be produced without debiting an account and will be payable in a faraway town/city. It will be cashed at the payment branch after that. It's just another DD for the paying branch. This type of fraud will only be uncovered when the head office does branch-by-branch reconciliation, which typically takes at least 6 months. By that time, the funds are no longer recoverable.

❖ **Fraud by others**

From the name itself, it stands clear that fraud by others signifies those outside the financial institution but are interested in earning profit illegally by exercising fraudulent activities in targeted banks.

- **Forgery and altered cheques**

Cheques are often tampered with to modify the name in the cheque in order to deposit cheques intended for someone else or the amount on the face. Rather than tampering with a genuine check, some fraudsters also try to counterfeit a depositor's signature on a blank cheque or even print their own cheques drawn on other people's accounts, non-existent accounts, or even supposed accounts held by non-existent depositors. Before the cheque may be rejected as invalid or for lack of cash, it will be deposited in another bank and the amount is extracted.

- **Stolen cheques**

Some fraudsters get access to facilities that handle significant numbers of cheques, such as a mailroom or post office, or the offices of a tax authority (which receives a high number of cheques), or a company payroll, or a social or veterans' benefits office (which receives a huge number of cheques) (issuing many cheques). Forgers cherish stolen blank cheque books because they may sign as if they are the depositor.

- **Accounting fraud**

Often firms have been known to utilize false bookkeeping to overestimate sales and revenue, inflate the value of the company's assets, or declare a profit while the company is operating at a loss in order to conceal major financial issues. These altered documents are then used to solicit investment in the company's bond or security offerings or to submit fake loan applications in the last effort to raise funds to stave off the eventual collapse of an unproductive or mismanaged business.

- **Bill discounting fraud**

Essentially a confidence trick, a fraudster utilizes a corporation to garner confidence from a bank by posing as a legitimate, lucrative customer. To provide the impression of being a desirable customer, the corporation employs the bank to collect money from one or more of its consumers on a regular basis. These payments are always paid because the consumers in issue are complicit in the scam and actively pay all of the bank's invoices.

- ❖ **Cheque kiting**

Cheque kiting takes advantage of a system in which money is made accessible immediately after a cheque is placed into a bank account, even if the money is not taken from the account on which the cheque is drawn until the cheque clears. A cheque is cashed, and the money is placed into another account or withdrawn by writing further cheques before the bank receives any money by clearing the cheque. The initial deposited check is frequently discovered to be a counterfeit check. On a daily basis, some offenders have switched checks between multiple banks, using each to offset the deficiency from a prior check.

- **Credit card fraud**

Credit card fraud is a common method of stealing from banks, businesses, and customers. A credit card is made up of three polyvinyl chloride plastic sheets. The core stock refers to the card's centre layer. These cards are of a certain size and include a lot of information embossed on them. However, credit card theft may take many forms. It is expected that when e- Commerce, m-Commerce, and internet capabilities become more widely available, fraudulent financial freaking by means of credit cards would rise dramatically. White plastics are the name provided to counterfeit credit cards.

- **Fraudulent loan applications**

Individuals using false information to disguise a credit history full of financial issues and unpaid debts, as well as organizations employing accounting fraud to overestimate revenues in order to make a hazardous loan appear

to be a solid investment for the bank, are all examples of fraudulent loan applications. Some companies have overextended themselves by borrowing money to fund expensive mergers and acquisitions and overstating assets, sales, or income to look solvent despite being severely financially strained. The consequent debt burden has bankrupted huge corporations, such as Parmalat, an Italian dairy behemoth, and exposed banks to significant losses from bad loans.

- **Phishing and Internet fraud**

Phishing works by sending forged emails imitating an online bank, auction, or payment site. The email takes the user to a forged website that looks like the original site and subsequently tells the user to update his or her personal information. The stolen information is subsequently utilized in various crimes, such as identity theft and online auction fraud. Several malicious “*Trojan horse*” programs have also been used to eavesdrop on internet users while they are online, stealing keystrokes or personal data and sending it to third-party websites.

- **Booster cheques**

A booster cheque is a forged or bad check used to make a payment to a credit card account in order to “*blow out,*” or increase the amount of credit available on otherwise legal credit cards. The bank credits the amount of the check to the card account as soon as the payment is made, even if the check has not yet been cleared. Before the fraudulent check is discovered, the offender goes on a shopping spree or takes out cash advances until the card’s newly increased allowable limit is reached. The initial check then bounces, but it’s too late by then.

- **Impersonation and theft of identity**

Identity theft is on the rise. The fraud involves getting information about a victim and then using that information to apply for identification cards, accounts, and credit in that person’s name. A birth certificate may often be obtained with just a name, parents’ names, date, and place of birth. Each document received is then used as identification to get other identity documents. Standard identifying numbers issued by the government, such

as social security numbers, PAN numbers, are also beneficial to identity thieves. Unfortunately for the banks, identity thieves have been known to take out loans and then flee with the money, happy to have the incorrect people accused when the bills default.

- **Money laundering**

Money laundering has been around since the days of Al Capone. Money laundering has subsequently come to refer to any scheme that conceals or hides the real source of finances. The surgeries are carried out in a variety of ways. One variation involves buying securities (stocks and bonds) for cash, putting them in a safe deposit box at one bank, and using a claim on those assets as collateral for a loan at another. After then, the borrower would default on the debt. The securities, on the other hand, would retain their full value. The transaction simply helps to conceal the monies' original source.

- **Forged currency notes**

At the personal level, paper cash is the most common means of money transaction, however, checks and drafts are also widely employed in the business. The term 'bank note' is defined under Section 489A of the Indian Penal Code, 1860. If currency note forgery is effective, it has the potential to provide the forger with a fortune while simultaneously destroying the nation's economy. A currency note is constructed of a special paper with plastic covering bonded on both sides to preserve the ink and anti- counterfeiting technology from harm. These notes also include security threads and watermarks. However, the majority of individuals are unaware of these facts.

- **Stolen payment cards**

A phone call from a credit card issuer asking if the person has gone on a spending spree is often the first indication that a victim's wallet has been stolen. The simplest form of this theft involves stealing the card itself and charging a number of high-ticket items to it in the first few minutes or hours

before it is reported as stolen. A variation of this is to duplicate only the credit card numbers rather than taking the card itself and then utilize the numbers in online scams.

- **Duplication or skimming of card information**

This can take many forms, from a dishonest merchant copying customers' credit card numbers for later misuse or a thief stealing the information using carbon copies from old mechanical card imprint machines to the use of tampered credit or debit card readers to copy the magnetic stripe from a payment card while a hidden camera captures the numbers on the face of the card. A fraudulent card stripe reader would record the contents of the magnetic stripe, while a covert camera would take a glimpse at the user's PIN. The data from the fake equipment would then be used to create duplicate cards that could be used to make ATM withdrawals from the victims' accounts.

❖ **Frauds assisted by digital technology**

Digital technology has facilitated efficient and quick banking services in most bank offices, except for those in rural and distant areas. While computerization in Indian banks is relatively new, there have been limited discussions about computer-related scams in banks. However, Western nations regularly report a significant number of cybercrimes in the financial industry. Understanding the nature of these crimes is crucial to developing effective preventive measures. The following types of frauds are commonly committed:

- **Password cracking:**

Cybercriminals create spy software to crack passwords. They gain unauthorized access to banks' computer systems and manipulate data to transfer money from others' accounts.

- **Computer viruses:**

Malicious individuals develop computer viruses, often distributed through email, to gain access to computer systems. These viruses corrupt saved data and can significantly slow down the entire system. There is a common belief that some anti-virus software firms create viruses to promote their products in the market.

- **Hacking:**

Hackers, who are skilled computer professionals, steal passwords and access sensitive data stored on computers. They may target various entities, including government agencies and military bases, with the intention of causing damage and destroying data for personal satisfaction rather than financial gain.

- **Wiretapping:**

Wiretapping involves a person tapping into the wire of a bank's ATM to access someone else's account and withdraw money. Fraudsters connect a wireless microphone to the telephone connection between the ATM and the bank's computer. By intercepting and recording signals while a client is using the ATM, they later utilize these signals to withdraw money.

Preventing and combating such frauds require robust security measures and ongoing efforts to stay ahead of cybercriminals' tactics.

DATA ANALYSIS
AND
INTERPRETATION

DATA ANALYSIS AND INTERPRETATION

As apiece RBI data, during the stage 2013-2017, 17,504 reservoir frauds reported. Around 5,200 officials were seized for fraud in known sector banks during full stop 2015-2017. The research shows that summit layer in the incline of frauds by veer officials were turmoil mound of India (SBI), Indian Overseas deposit (IOB) and key mass coverage 1538, 449 and 406 luggage resp. One of the current open sector banks that is Punjab state-run row is furthermore facing fraud committed by billionaire jeweller Nirav Modi. mainly of the gear in situation of frauds retain the insider involvement. If we establish facts for the period, 2013-2017, out of 3870 case, in 450 cases had insider involvements. Fundamental incline that is RBI has been issuing circulars to banks about how in effect testimony gear and additionally put in site means to avert them

Number of cases which involved Bank officials 2015-2017 as shown in the table

Bank	Number of cases which involved Bank officials 2015-2017
State Bank of India	1538
Indian Overseas Bank	449
Central Bank	406
Union Bank	2014
Punjab National Bank	184
fraud cases involving private and public sector banks 2013 to 2017	17404
fraud cases involving private and public sector banks 2013 to 2017	66066 crores
number of cases which involved Bank officials	2084

❖ **Frauds in Various Banking Operations Based on the Date of Reporting**

(At the end-March)

(Cases in number and amount in ₹crore)

	2014-15		2015-16		2016-17		2017-18		2018-19	
	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount
Advances	2251	17122	2125	17368	2322	20561	2525	22558	3606	64548
Card/ Internet	845	52	1191	40	1372	42	2059	110	1866	71
Deposits	876	437	757	809	695	903	691	457	593	148
Cash	153	43	160	22	239	37	218	40	274	56
Others	179	162	176	146	153	77	138	242	197	244
Cheques/demand drafts	254	26	234	25	235	40	207	34	189	34
Off-balance sheet	10	699	4	132	5	63	20	16288	33	5538
Clearing, etc accounts	29	7	17	87	27	6	37	6	24	209
Foreign exchange transactions	16	899	17	51	16	2201	9	1426	13	695
Non-resident accounts	22	8	8	9	11	3	6	5	3	0
Inter-branch accounts	4	0	4	10	1	1	6	1	3	0
Total	4639	19455	4693	18699	5076	23934	5916	41167	6801	71543

Source: RBI Bulletin 2019

❖ **Interpretation: -**

Above table depicts the no. of cases and rupees in crore of frauds in banking operations based on the date of reporting. The analysis of the table is as follows:-

- The cases of advances fraud are higher than all other frauds. It is increasing rapidly year by year. It was just 2251 in 2014-15 and it increased upto 3606 in no. of cases in 2018-19. The amount of fraud has risen nearly thrice between 2017-18 and 2018-19.
- Fraud through Cards and Internet transactions were also increasingly continuously from 2014-15 to 2017-18 but in 2018-19 it becomes go down in no. of cases. Most cases have been filed of card and internet between 2016-17 and 2017-18 i.e. 687 cases.

- Frauds through deposits have been continuously go down in no. of cases. As the amount concerned it has risen in 2015-16 in comparison with 2014-15 with 372 crores which is very high. In 2018-19 it has go down by 309 crores in comparison with 2017-18 which is a good sign for the banks.
- Frauds cases through others have go down to 77 crores in 2016-17 in comparison with 2015-16 which was a good sign for the banking sector. But again in 2017-18 it has been risen again very rapidly, which was not a good sign for the banking sector.
- Fraud through off- balance sheet has rising very rapidly in 2017-18 which is very high i.e. 16288 corers and 5538 crores in 2018-19. It means that total fraud of 21826 crores in the last two years. This was the mode of banking fraud which highly used and bank has to take action to control these types of frauds.
- Frauds in clearing etc. Accounts has been increasing very rapidly in 2018-19 almost very high i.e. 209 crores.
- Frauds through foreign exchange transactions have been gone down by 848 crores in 2015-16 which was a good sign for the banking sector. But again in 2016-17, fraud through foreign exchange transactions become rising very rapidly i.e. 2201 crores. After that in 2017-18 and 2018-19, the amount of fraud has been gone down in 2017-18. In 2018-19 it also becomes go down.
- Cases of frauds through non-resident accounts and inter-branch transactions were very low in number and also very low in amount. But still we have to work on it.

❖ **Frauds in Various Banking Operations Based on the Date of Occurrence**

(At the end-March)

(Cases in number and amount in ₹crore)

	2014-15		2015-16		2016-17		2017-18		2018-19	
	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount
Advances	1897	18168	1743	14570	1265	9550	1024	8863	632	3634
Card/ Internet	918	58	1173	43	1367	40	2127	101	1477	58
Deposits	790	214	719	600	602	665	524	294	320	45
Cash	159	36	155	20	276	41	207	38	193	40
Others	161	33	133	165	132	50	98	146	83	27
Cheques/demand drafts	272	23	235	131	217	33	199	34	104	12
Off-balance sheet	13	1720	11	1132	13	15023	4	298	8	2569
Clearing, etc accounts	23	79	19	4	29	7	33	5	13	205
Foreign exchange transactions	18	3361	9	205	15	473	5	83	4	145
Non-resident accounts	16	3	6	0	7	1	5	4	1	0
Inter-branch accounts	2	0	4	9	4	1	2	0	1	0
Total	4269	23695	4207	16779	3927	25884	4228	9866	2836	6735

Source: RBI Bulletin 2019

❖ **Interpretation: -**

Above table depicts the no. of cases and rupees in crore of frauds in banking operations based on the date of occurrence. The analysis of the table is as follows:-

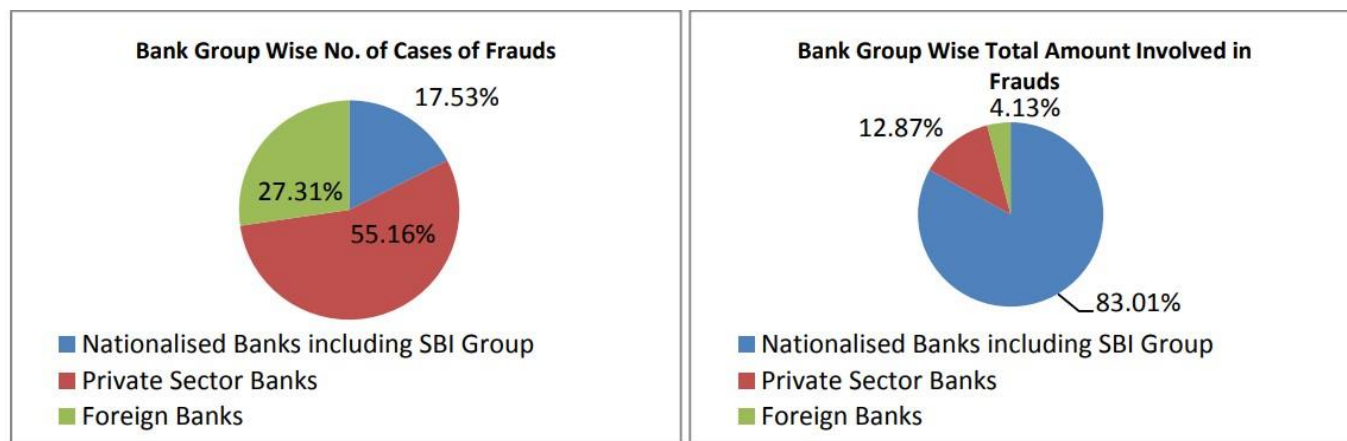
- Frauds of advances have become go down regularly in no. of cases as well as in rupees, from 2014-15 to 2018-19. It was 1897 cases in 2014-15, and it has reduced to only 632 cases in 2018-19. Likewise frauds of 18168 crores in 2014-15 have gone down to 3634 crores in 2018-19.
- Fraud through Cards and Internet transactions were also increasingly continuously from 2014-15 to 2017-18 but in 2018-19 it becomes go down in no. of cases. Most cases have been filed of card and internet between 2016-17 and 2017-18 i.e. 760 and 650 cases respectively.

- Frauds through deposits have been continuously go down in no. of cases. As the amount concerned it has risen nearly thrice in 2015-16 in comparison with 2014-15 with 372 crores which is very high. In 2017- 18 it has go down by 371 crores in comparison with 2017-18 and by 249 crores in 2018-19 in comparison with 2017-18, which is a good sign for the banks.
- Frauds cases through others have go up by five times in crores rupees in 2015-16 in comparison with 2014-15 which was a good sign for the banking sector. But again in 2017-18 it has been risen again very rapidly, which was not a good sign for the banking sector.
- Fraud through cheques and demand drafts has rising more than five times in 2015-16 which is very high in comparison in 2014-15, which was not a good sign for banking sector. After that fraud through cheques and demand drafts has gone down regularly till 2018-19.
- Fraud through off- balance sheet has rising very rapidly in 2016-17 which was very high i.e. 15023 crores. It has gone down in 2017-18 but after that in 2018-19, it arisen again which was not a good sign for the Indian banking sector.
- Frauds in foreign exchange transactions has been gone down in 2015- 16 by 3156 crores in comparison with 2014-15. It increased again more than twice in 2016-17, and again gone down in 2017-18 by five times.
- Cases of frauds through non-resident accounts and inter-branch transactions were very low in number and also very low in amount.

❖ Frauds in Various Banking Operations Based on Deposits, Advances and Services

As per the RBI, bank frauds can be classified into three broad categories: deposit related frauds, advances related frauds and services related frauds. Deposit related frauds, which used to be significant in terms of numbers but not in size, have come down significantly in recent years, owing to a new system of payment, and introduction of cheque truncation system (CTS) by commercial banks, use of electronic transfer of fund, etc. Advances related fraud continue to be a major challenge in terms of amount involved (nearly 67 percent of total amount involved in frauds over last 4 years), posing a direct threat to the financial stability of banks. With ever-increasing use of technology in the banking system, cyber frauds have proliferated and are becoming even more sophisticated in terms of use of novel methods. Also, documentary credit (letter of credit) related frauds have surfaced causing a grave concern due to their implications on trade and related activities.

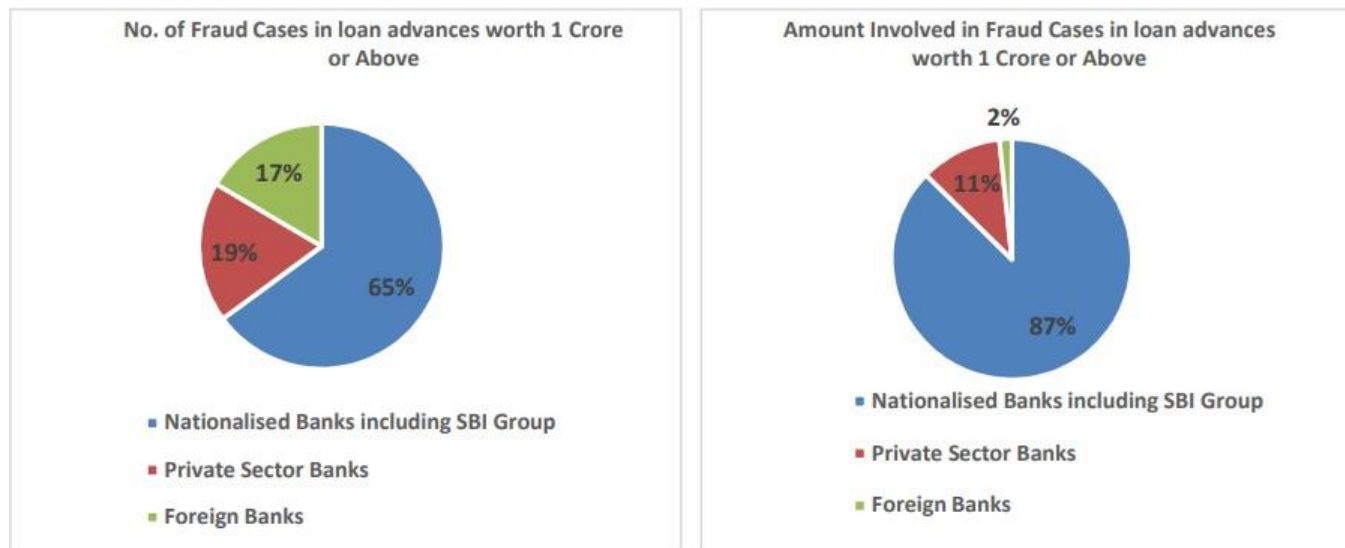
. Figure 1: Group wise summary of bank fraud cases



Note: Data pertains to the period from March 31, 2010 to March 31, 2013.

Source: Chakrabarty (2013).

Figure 2: Group wise summary of advance related fraud cases



Note: Data pertains to the period from March 31, 2010 to March 31, 2013.

Source: Chakrabarty (2013).

❖ Interpretation: -

- Commercial banks account for over 95 percent of the total number of fraud cases and amount involved in fraud.
- Public sector banks (PSBs) represent around 18 percent of the total number of fraud cases but contribute to a significant 83 percent of the total amount involved.
- In contrast, private sector banks have about 55 percent of the number of fraud cases but only contribute to around 13 percent of the total amount involved.
- PSBs are particularly vulnerable to large-scale advance-related frauds (amounting to 1 crore or more) in terms of both the number of reported fraud cases and the total amount involved.

- The correlation between the increasing level of non-performing assets (NPAs) in PSBs and frauds suggests a possible lack of corporate governance standards and potential collusion between corporate entities and top bank officials.
- Private banks, on the other hand, experience a higher number of fraudcases with relatively lower costs, indicating a prevalence of online, cyber, and technology-related frauds that occur frequently but with less significant associated costs.

According to findings of Deloitte (2015), number and sophistication of frauds in banking sector have increased over the last two years. Around 93 percent of respondents suggested an increase in fraud incidents and more than half said that they had witnessed it in their own organizations. Retail banking was identified as the major contributor to fraud incidents, with many respondents saying that they had experienced close to 50 fraudulent incidents in the last 24 months and had lost, on an average of Rupees ten lakhs per fraud. In contrast, survey respondents indicated that the non-retail segment saw an average of 10 fraud incidents with an approximate loss of Rupees two crore per incident. Many respondents could not recover more than 25 percent of the loss.

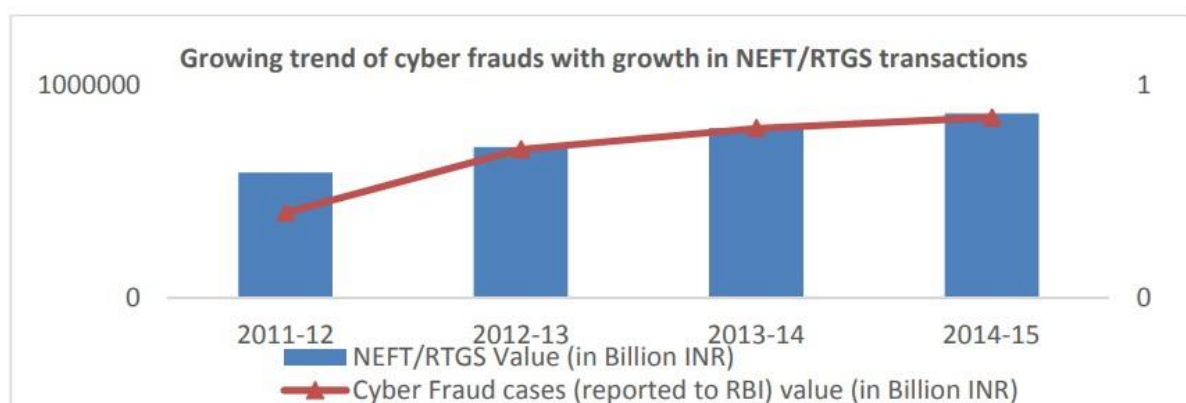
The risks undertaken by banks are still a cause of worry although it has moderated a bit. This is indicated by the bank stability indicator. Similarly, banks were worried by poor asset quality. System level credit risk is determined by gross NPA ratio which is expected to be around 5.4% by September 2016 and 5.2 percent in March 2017 as per RBI (2015c).

Further, the ratio of stressed assets has increased significantly in the last few years. As of September 2015, stressed and written off assets (SWA)⁴ are at 14.1%.

❖ Frauds in Various Banking Operations Based cybercrime and identity theft

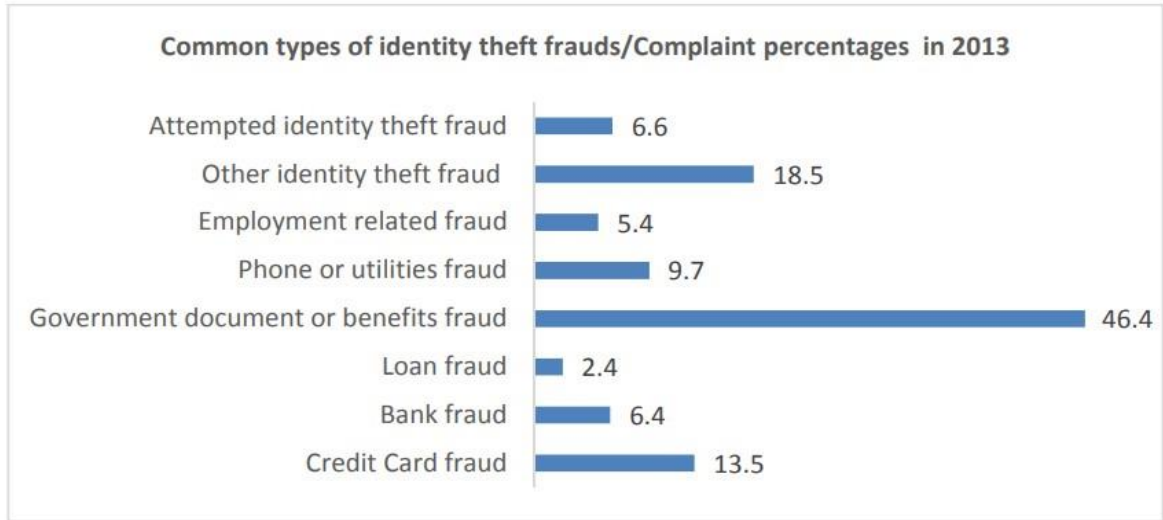
India has witnessed a massive surge in cybercrime incidents in the last ten years - from just 23 in 2004 to 72,000 in 2014-15 (Figures 3 and 4). As per the government's cyber security arm, computer emergency response team- India (CERT-In), 62,189 cyber security incidents were reported in just the first five months of 2015-16.

Figure 3: Cyber Frauds



Source: PWC India and ASSOCHAM (2014).

Figure 4: Identity Theft Fraud



Source: PWC India and ASSOCHAM (2014).

❖ **Interpretation: -**

- **Impact of COVID-19:** The COVID-19 pandemic led to organizations shifting to digital operations, resulting in new risks and incidents of fraud.
- **External Attacks and Collusion:** 67% of organizations in India reported that the most disruptive fraud incidents were caused by external attacks or collusion between external and internal sources. This proportion increased from 56% in the previous year.
- **Types of External Perpetrators:** Among external perpetrators, 49% were hackers, 41% were customers, and approximately 31% involved organized crime groups.

- **Misconduct and Conduct Risk:** Misconduct emerged as the biggest challenge for organizations during the pandemic, as bad actors took advantage of the uncertainty and volatility. Conduct risk, associated with individuals within the organization, vendors, agents, and customers, was identified as the most significant threat at 90%.
- **Platform Risks:** The rise of digital platforms for business operations increased platform risks. These risks include those associated with social media, services like rideshare and lodging, and e-commerce. Approximately 53% of surveyed organizations in India reported experiencing platform-related fraud risks.

The COVID-19 pandemic and the shift to digital operations brought about new challenges and risks for organizations, with external attacks, collusion, and misconduct posing significant threats. As digital platforms gained prominence, organizations faced increasing risks associated with them. Preventing and managing fraud in this evolving landscape requires robust measures to address both internal and external risks, as well as adapting to emerging threats in the digital realm.

CONCLUSION

CONCLUSION

India is one of the fastest growing economies and so is the case with the country's banking sector. In conclusion, it can be said that though adoption of technology comes with the evolution of time, but protection of public money and people is the greatest challenge responsibility of a modern day banker. From the above description, we can see that frauds in various banking operations based on the date of reporting frauds in advances has been increasing at very high rate. Off- balance sheet frauds are also rising at a very high rate also. Another aspect is frauds through foreign exchange transactions are also become very high in rate. So banks have to make a proper strategy to control the frauds through banking operations.

There is a growing recognition among banks of the need to improve their fraud risk management practices in light of regulatory requirements and therising occurrences of fraud. One of the challenges faced by banks is the lack of advanced forensic analytical tools that can effectively identify potential fraud risks in various processes.

To address these challenges, banks should establish a more systematic and structured framework for fraud risk management. This involves leveraging their expertise and experience in managing fraud and compliance, and integrating innovative technologies and data analytics to detect and prevent fraudulent activities.

By adopting a proactive approach and investing in robust fraud prevention measures, banks can mitigate the risks associated with fraudulent activities. It is essential for banks to continuously evaluate and enhance their fraud risk management strategies to stay ahead of evolving fraud tactics and safeguard the interests of their customers and stakeholders.

- Defining the scope of Banking Fraud is crucial because it determines the nature and impact of an offense. It should encompass both traditional and emerging forms of fraud, requiring the expertise of a dedicated committee.
- The integration of banking institutions with other commercial activities like insurance and securities blurs the line between banking and other economic sectors. While this may facilitate economic growth, it also means that any financial fraud occurring in such entities could be considered a Banking Fraud.
- Prevention is better than cure, and this holds true for Banking Frauds as well. Establishing a fraud-proof banking environment requires effective investigation by specialized agencies.
- The justice delivery system plays a vital role in enforcing laws against Banking Frauds. Implementing certain changes within the existing court system, such as summary trials for smaller cases and shifting the burden of proof to the accused in economic offenses, can expedite the resolution of cases and increase effectiveness.
- Since the ultimate economic loss in Banking Frauds affects customers who rely on banking services, there is a need to strengthen consumer rights in this context. Customers should be viewed not just as parties to a banking contract but also as consumers of banking services who are central to the entire banking system.
- Banks face various challenges in the 21st century, requiring a re-evaluation of legal strategies and processes to adapt to the dynamic environment. Outdated laws, supplemented by piece-by-piece legislations, are insufficient in combating the ongoing wave of Banking Frauds facilitated by technological advancements.

FINDINGS
&
SUGGESTIONS

FINDINGS & SUGGESTIONS

❖ Findings: -

An analysis of the cases reveals several factors responsible for the occurrence of frauds in public sector banks:

- Active involvement of staff: Fraudulent activities are often carried out by bank staff either independently or with the help of external individuals.
- Failure to follow instructions: Bank staff may neglect to adhere to laid down instructions and guidelines, creating opportunities for fraud to occur.
- Forgery and manipulation: Frauds can occur through the forgery or manipulation of banking instruments and documents, allowing individuals to deceive the banks.
- Collusion: There have been instances where business entities, senior bank executives, and civil servants collude to defraud banks, indicating a high level of internal corruption.

The Central Vigilance Commission identified various loopholes and lapses in the banking system that contribute to frauds:

- Lack of competence and skill: Banks may lack the expertise to properly assess the technical aspects of projects seeking financial support.
- Insufficient due diligence: Banks may fail to conduct thorough due diligence processes, leading to inadequate assessment of borrowers' credibility.
- Funds diversion: Promoters of companies may divert funds using shell companies, making it difficult for banks to trace the actual flow of funds.

- Fabrication of information: False information provided by borrowers can mislead banks during the loan approval process.
- Frauds committed by companies: Companies themselves may engage in fraudulent activities, causing financial losses to banks.

These causes can be attributed to various factors such as inadequate supervision by top management, faulty incentive mechanisms for employees, weak regulatory systems, lack of effective fraud detection tools and technologies, lack of coordination among banks, collusion between employees and external parties, inadequate training, and excessive workload on bank staff.

According to the Reserve Bank of India (RBI), more than 23,000 fraud cases involving around Rs 1 lakh crore have been reported in the past five years. Anand Baiwar, Executive Director of the Securities and Exchange Board of India (SEBI), has emphasized the close connection between corporate frauds and corporate governance, highlighting the importance of strong governance practices to mitigate fraudulent activities.

A fraud poses significant threat to the integrity of financial institutions. Fraud destabilizes the confidence of investors. It can bring down institutions to closure and cause employees loss of their livelihood and investors lose their savings. These frauds threaten the stability of banking system and challenge the authorities to disentangle the schemes.

- Lack of robust data governance models for data ownership/verification and adherence to data management standards
- Lack of proper standards for collection and storage of risk data
- Lack of information and data shared during consortium lending
- Non-integration of risk data
- Lack of sufficient market intelligence deployed within the bank.

❖ **Suggestions: -**

PREVENTIVE MEASURES:-

21 St Century has witnessed a tremendous change in almost all the walks of life. Technology has promised unprecedented development to the mankind and provided computerization as a fountain of new age wisdom and delivered a flood of new quick and efficient banking services. But this facility also created risks in various banking activities which need well defined and timely precautionary measures. Computer automation providing innumerable services are subject to certain security/precautionary measures against its inbuilt flaws and RBI to explaining the activities suggests the preventive vigilance steps to be taken to minimize such risks.

The precautions to be adopted to avoid/minimize occurrence of computer related frauds involve to a large extent in moulding attitudes of the persons engaged in computer fields attitudes needing thorough overhaul are outlined below:

- A) Easy to get away and cannot get caught.
- B) Stealing a little from big company would not hurt.
- C) Everybody else is stealing, why not me.
- D) Computer security is not a priority.
- E) Computer will take care of everything-no checking is required.
- F) Lack of input control - output verification.
- G) Lack of evidence.
- H) Lack of access control-audit trails.

I) Lack of dual checks in sensitive and high-value transactions.

J) Long serving trusted operators/supervisors/Managers.

K) Missing EDP audit.

CURATIVE MEASURES:-

- There should be strong internal rating agencies which evaluate each project before sanction of loan.
- Indian government should also consider the role of third parties like auditors, chartered accountants and rating agencies and determine punitive measures for future deterrence.
- Periodic disclosures to RBI, SEBI and other regulators
- Strengthening KYC norms to prevent fraudulent financial reporting
- Financial literacy among employees in areas of early fraud detection and prevention.

❖ Key components of an effective anti-fraud programme



- A well-defined governance structure
- Develop policies and procedures to provide guidance to business
- Policies to be structured in layers to cover all products and services across locations
- Data capturing to be consistent and adequate
- Data flow from various systems to be unhindered
- Data sanctity to be preserved
- Employ qualified and experienced staff to enable supervision and monitoring
- Effective technology solutions to be implemented for business to run in sync and data to be available consistently
- Periodic reviews and transparent management reporting

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