Special Bulletin

Indian Institute of Banking & Finance

ANALYSIS OF TOP 100 BANK FRAUDS

BY

CENTRAL VIGILANCE COMMISSION

NEW DELHI

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OCTOBER, 2018

Analysis of Top 100 Banks Frauds

The rising trend in Bank frauds has been a cause of concern at all levels. In view of the alarming rise in Bank frauds, the Central Vigilance Commission has undertaken a review and analysis of top 100 Banks Frauds, as on 31.03.2017.

1. The analysis mainly focused on the Modus- operandi; Amount involved; Type of lending viz. Consortium/ Multiple/Individual; anomalies observed; loopholes that facilitated perpetration of concerned fraud and systemic improvements required to plug the loopholes in the system & procedures, etc.
2. The Top 100 Banks frauds were classified and analysed for the following sectors :-----

S. No.	Sector	S. No	Sector
(i)	Gem & Jewellery	(viii)	Trading
(ii)	Manufacturing/Industry	(ix)	Information Technology
(iii)	Agro	(x)	Export Business
(iv)	Media	(xi)	Fixed Deposits
(v)	Aviation	(xii)	Demand Loan
(vi)	Service/project	(xiii)	Letter of Comfort
(vii)	Discounting of Cheques		

3. The findings have been shared with Reserve Bank of India and Deptt. of Financial Services, (Ministry of Finance). The Deptt. of Financial Services has circulated the above analysis done by CVC amongst all Public Sector Banks. Similarly, the RBI has also acknowledged the analysis to be very useful and assured the Commission to use the findings for Systemic Improvements in relevant areas.
4. A consolidated report is enclosed for your kind perusal/ ready reference. We hope that the suggestions given for systemic improvements shall pave a long way in reducing / obviating Bank frauds.

(Dr. T.M. Bhasin)
Vigilance Commissioner
Central Vigilance Commission

New Delhi,
15.10.2018

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Gem & Jewellery Sector

The cases of frauds perpetrated by three companies in this sector have been analysed. The companies were in business of the Diamonds & Jewellery. The companies had adopted a business model by which they imported gold/ gem through foreign Banks/private parties against SBLC/LC/ Cash Credit for value addition and production of Jewellery for export to its customers located aboard. The Companies availed credit facilities from the banks under consortium arrangement led by one of the banks.

Modus operandi:

- The companies deliberately inflated the valuation of diamonds with the malafide intention to avail higher credit facilities from the lenders and also to indicate the security coverage available with the lenders.
- Export bills which remained unpaid on due date were purchased by the consortium Banks. Simultaneously, the disruption of the cash flow led to the devolvement of SBLCs and outstanding of cash credit remained unpaid.
- The group of the companies informed that as their receivable were not being realized in time due to financial difficulties of the foreign buyers; they could not meet the SBLC (Standby Letter of Credit) commitment on time.
- The details of receivable/debtors submitted by the companies to the bank in order to avail credit facilities appeared to be manipulated, false and fabricated.
- The companies acted cleverly to avail entire pre-shipment as Standby Letter of credit instead of packing credit loans, for which consortium succumbed to their innovative funding ideas. The companies also resorted to availing post-shipment finance by discounting "Export Bills" from one of the member banks, while pre-shipment finance was obtained from another member bank by way of SBLC, leading to double financing.

Loopholes/Lapses:

- Due diligence report on borrowers were not obtained before submitting the sanction/ renewal proposal. While recommending the proposal for enhancement in limits, quantum of export was focused to get the limit enhanced. However comforts like LC/ SBLC were not insisted to ensure timely payments of exports whereas imports were on the basis of SBLC.
- The entire group of existing buyers companies was controlled by a single person. No credit assessment was done for these customers. There was no evidence for proof of delivery of the goods to customers. Later on, the investigating agency have raised the issue regarding proof of delivery of sales of gold and diamond jeweller to foreign companies.
- In the absence of any effective mechanism to monitor the movement of discounted Export bill proceeds towards liquidation of SBLCs across member banks, the companies manipulatively diverted and round tripped the funds to their related/ shell companies.
- Consortium Mechanism under the leadership of lead bank broadly failed to check and monitor the transactions. The exchange of information was more a ceremonial formality rather than to sift the data. The lead bank did not share the areas of concern. They did not take note of warning signals mentioned in the business rating reports. The lead bank did not exchange the information in meetings to alert other member banks at early stages.

- It is evident that Bullion Trade and Merchant Trading were not genuine transactions carried out in the ordinary course of the business. The losses were deliberately booked through related party transactions to siphon off/ divert the funds availed from the consortium thus committing default in making payment/ repayment thereof. The high value transactions were made without the specific approval of the consortium.

Systemic Improvement:

- There should be control of financers on movement of stocks. Genuineness of buyers
- should have been verified to ascertain whether buyer is capable of such a huge buying.
- Banks should have exercised due diligence on the buyers and have executed a tripartite agreement with the buyers & exporters to remit proceeds to bank account of the companies in India. Confidential Report (CR) on all foreign buyers should have been obtained/ analyzed.
- Gem & Jewellery Sector credit facilities to these companies increased manifold within a short span of time in an effort by the banks to increase their credit dispensation. There should have been some segment related limits on such type of credit exposures.
- There were frequent attempts by fraudsters to fabricate documents and avail finance from banks. Heightened awareness of loopholes, consequences of bypassing procedural aspects and check points for evaluating genuineness of various essential documents was very much necessary. These points should be the learning lesson for future.
- It should be ensured that appropriate accountability is fixed in the chain of command including sanctioning authority in the event of such frauds instead of fixing entire responsibility on lower functionaries.
- Investigation should be done to find out the trail of diversion so as to find as to where the money has gone whether any money has been remitted /parked aboard.
- Bank must immediately delist such third party valuers, Chartered Accountants/ Chartered Engineers, Advocates etc. who have questionable credentials/have been negligent in their professional duties or have caused financial loss to the bank by their willful acts of omission/commission/ dishonesty. A periodical review of all empanelled professionals should be ensured by banks for weeding out undesirable third party service providers.
- In such cases of frauds the concerned banks should get forensic audit done and concerted efforts should be made by banks to get back the money lost.
- Jewellery sector units may also be asked to furnish a monthly declaration to its lender Banks declaring details of all transactions /financial agreement/ contract entered into by its subsidiaries with their business associates.

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Manufacturing Sector

The cases of frauds perpetrated by five companies in this sector have been analysed. The companies were in business of manufacturing in Pharmacy, Textile, Ferrous metals, pharmaceuticals products and various ranges of steel products. The Companies had started availing credit facilities in form of working capital (Fund based & Non fund based) from the banks under consortium arrangement led by one of the banks.

Modus operandi:

- One of the Companies had exported the goods against the shipping bills and had discounted export bills on different dates. Since the bills were long outstanding, the lead bank requested Commissioner of Customs Duty to verify the genuineness of these bills.
- As per Commissioner's report, out of all shipping bills, only a small number were genuine, a few shipping bills pertained to ICD, Ludhiana and rest of shipping bills were not genuine, and were forged.
- The other Company made purchases to the tune of Rs.6740 crore. Out of this, Rs.1679.45 crore was for purchase of fancy shirting.
- On review of purchase invoices and stock records of this item indicated that purchase invoice did not define any code, grade, make etc. It was unable to confirm physical movement of fancy shirting material.
- Mismatches were found in products mentioned in LC invoice documents and products mentioned as per books of the company.
- In case of another company, the turnover was inflated. There was no actual purchase or movement of stocks as depicted by the borrower company in its books of accounts and financial statements.
- There had been misappropriation of funds by the management of the company. They explored all possible avenues to divert the funds. There was mis-match of accounting data vis-à-vis the banking statements and the non-reporting of the same in the audited financials by the auditors of company.
- The payment made to the beneficiaries of LCs was diverted to the accounts of the debtors of the company from where it was finally routed either to the account of the borrower company or to its subsidiaries.
- Another company had been importing pharmaceutical products and chemicals from overseas suppliers based at Singapore and were exporting its products to Hong Kong and Singapore having a branch office at Dubai. The exporting company owned by the same proprietor as the supplier company.
- The company was dealing in computers, computer peripherals and other commodities. There were consignment transactions of computers and computer peripherals, whereby the company was sending computers and computer peripherals to its branch office at Dubai by way of Branch transfers.
- The export and import documents submitted to bank by company in respect of the Merchanting Trade transactions purported to be relating to pharmaceutical and allied products appeared to have been falsified.
- The other Company finalized its Balance Sheet for the year 2011-12 and got it audited on 30.04.2012 showing profit of Rs. 23.74 crores. On the basis of the Balance

Sheet, the company got credit facilities from consortium banks. Subsequently, the company revised its audited B/s for 2011-12 on 05.09.2012 without informing any of the member Banks. The profit in the revised balance sheet was reduced to Rs.0.34 crore.

- The Company was maintaining current accounts with the Banks, which were not part of consortium. The credit turnover in these accounts was Rs.176.96 crore. The Company had incurred loss of Rs.241.83 crore during 2012-13 as against profit of Rs.0.34 crore during 2011-12 against same volume of turnover of Rs.2178 crore in both years.
- The Company routed sales proceeds through account with non consortium Banks without prior permission of consortium. The Company had not submitted Book Debt statements certified by CA.
- The Companies had defrauded the banking system by unscrupulous activity such as manipulation of books of accounts, removal, depletion & disposing of hypothecated stocks without the bank's knowledge.

Loopholes/Lapses:

- The Company had submitted forged Bills of Entries/Postal documents to banks and huge amounts of foreign exchange were remitted to various overseas accounts.
- The status of Bill of Entry in the ICEGATE system under option "Bill of entry at ICES" was not checked and "Out of Charge" (OOC) date in the concerned column of OCC was not verified with the print out of exchange control copy of the Bill of Entry submitted by the importer as proof of import.
- The company had generated entire set of documents for exporting the goods, but cancelled later on. Directorate of Revenue Intelligence had submitted details of 13 shipping Bills.
- It was also found that 35 shipping bills were issued by CFS (Container Freight Station) and rests of shipping bills were not genuine but were forged.
- Apart from Bank accounts with consortium members, transactions were carried out in other Bank accounts of company. The nature and purpose of these transactions could not be ascertained.
- Incorrect and non existing debtors were included in the debtors' statement of the company. The company resorted to circular transactions to report higher sales/ purchases figures, Mismatch were noticed in the stocks/debtors as per the books of the company and as per the stock statement submitted by the company.
- In circular transactions, the parties were related to each other either by way of common directorship in other companies in individual capacity or through family members.
- The majority of the transactions reflected in their respective Bank's statements were in nature of the same day fund transfers to connected parties. The majority of LC payments used for circular rotation of money had been made against purchase of Fancy Shirting which was trading product of the company.
- Most of the debtors were not available. The debt confirmation letters sent by the consortium leader by Regd. post were returned undelivered in most of the cases. Confirmations were received only from 22 debtors, but they denied the dues reported by the borrower company to the consortium lenders.
- Perusal of the statement of bank accounts of beneficiaries of the LCs revealed that the payments received were re-routed

through various accounts and channelized back either to the account of the borrower company or one of its subsidiary/ associate concern.

- Out of the 12 transport operators, two were fictitious and enquiries in the vicinity revealed that no such transport operators ever existed at these addresses. The two available transport companies informed that the lorry receipts attached with the invoices were fake which were not issued by them.
- To find out the authenticity of the data of the debtors, the audit company selected 10 top buyers of the borrower company and found that all the 10 parties were not traceable at the given addresses.
- The company/ firms to whom payments were made by banks were dealing with products not related to the business of the borrower company.
- The Company had made sale/purchase transactions of the same products with same companies/related companies. There was no evidence of any processing value addition to the products.
- The Company had sold goods to a firm on merchant export basis which was dealing in information and technology, telecommunications, office automation and electrical appliances. The company had made purchases from a firm which was engaged in manufacturing and distribution of computer components, consumer electronics, and digital electronics.
- Three associates/subsidiaries were shown in the balance sheet of the company. However, these companies virtually existed on papers without any functional or business activities.
- The bills of lading were wrongly generated by non-existent forwarders. Their Dubai office responded that they could not trace the details of bills of lading. Four companies were involved in fake merchant trade transactions with the company.
- A complaint lodged by the bank with CBI has revealed that the directors of the company in collusion with each other fabricated the records and faked non-existent transactions as genuine transactions and indulged in fabrication of purchases and sales of the same products from firms which were actually dealing in IT, telecommunication, electric and electronic products.
- The stock audit was conducted on 20.05.2013 and 21.05.2013. It was observed that Drawing Power comes to Rs.20.64 crore against total sanctioned limit of Rs.465.00 crore whereas the company submitted stock statement showing D.P. of Rs.467.59 crore in Feb 2013. The company did not submit stock statement after Feb 2013.
- The Company had reduced the holding of sundry debtors at the end of March 2013 in the age group of 90 days from Rs. 525.76 crore to Rs.216.04 crore. The Company could not produce documentary evidence for such reduction.
- From the stock statement, it was observed that holding had substantially increased from Rs.58.74 crore as on 31.03.2012 to Rs.1216.17 crore as on 31.03.2013 which represented increase by 114.78% in comparison to previous year.
- No records were maintained for stores & consumables which constituted Rs.47 crore during 2012-13 indicating lack of internal control system. Due to lack of detailed information the auditors had not commented in respect of end use of funds.
- The Company had not complied with bank's instruction to submit Book Debt statement certified by CA along with VAT returns for the financial year 2011-12 and 2012-13 which implied that Book Debt statement submitted to Bank were inflated.

Systemic Improvement:

- Due diligence of major debtors should be carried out by direct visit, direct balance confirmation, engaging agencies and comparing the realization of receivables as per stock/BD statements with routing of funds through lending banks to ascertain diversion through non lending banks.
- Meaningful analysis of stock statements should be carried out. Confirmation should be obtained from debtors at periodic intervals. Regular monitoring of the operative account should be ensured.
- The past track record of the borrower or the length of his satisfactory association with the Bank should be one of the considerations. The status of the customer should be more critically analyzed while renewing the existing facilities.
- The field level functionaries should be advised to scrutinize the financial statements submitted by the borrowers thoroughly and whereever it is observed that the short term funds are used for long term purposes and vice versa they should be advised to ascertain from the borrower the reasons and purpose there of and record the same in appraisal notes.
- Investigation should be done to find out the trail of diversion of fund so as to where the money has been done and whether any money has been remitted /parked aboard.
- The irregularities arising out of credit transactions should be meticulously looked into to satisfy whether these were on account of genuine trade/business transactions, market conditions, general state of industry and economy or overflow of corporate fraudulent transactions, which were being attempted to or were being concealed.
- Field functionaries should be advised to ensure end use of funds. They should follow the proper due diligence and not to rely entirely on documents/papers produced, before them. Documents and disbursement should be cross verified.

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Agro Sector:

The cases of frauds perpetrated by three companies in this sector have been analysed. The companies were in business of processing of basmati Rice, manufacturing of sandal wood oil and producing of castor oil. The Companies had started availing credit facilities from the banks under consortium arrangement led by one of the banks.

Modus operandi:

- One of the companies resorted to diversion of funds through group/ associate concerns, inflated level of debtors for availing higher limits/DP, higher cost of capital expenditure.
- Capital expenditure advances were given to 3 vendors without any purchase transactions and the same was used for investment in acquiring shares of another company. All these vendors were holding shares of that company.
- The debtors' levels more than doubled during the last two years while sales turnover had come down. It was also observed that the sale had been made to debtors throughout the year without any amount having been realized from them during the year.
- The Company had capitalized the warehouse building, the cost of construction of which was shown on a higher side compared to similar type of buildings that were constructed at much lower cost. Thus the Company inflated the cost of capital expenditure.
- Another Company obtained drawing powers in the account from consortium against the book debts outstanding in their books majority of which were found to be non-existent and were based on fake invoices/ debtors. In this way, the Company diverted working capital funds.
- The Company did not route proportionate sales with the member Banks. The matter was taken up with the company repeatedly, but the turnover in the accounts maintained with member Banks did not improve.
- The company had shown debtors which were non- existent. The company got the enhanced facilities sanctioned on the basis of fake inventories of debtors and funds were siphoned through personal accounts of Directors.
- Packing credit advance had been taken from member Banks, but the company failed to execute export business.
- Another Company initiated an alternate procurement model whereby pre-harvest farm loans were extended to farmers through Village Level Aggregators (VLA) supported by Post Dated Cheque (PDC) as collateral security.
- With the introduction of pre-harvest financing, its traditional practices and controls failed resulting in embezzlement of funds. Fake inventories were created through collusion of employees and associates involved in procurement.
- The company suppressed the facts regarding depletion of stocks and did not inform the misappropriation of stocks by their employees to the consortium. It was reported that their employees had embezzled the stocks.
- The management of the company had misrepresented the performance of the company to the consortium lenders at various occasions.

Loopholes / Lapses :

- Proportionate sales transactions were not routed through working capital limits with consortium member banks. Round-tripping of funds was resorted between various working capital limits with member banks.
- The percentage of working capital loan vis-a vis Sales turnover of the Company was on higher side sometime, even crossing 100%. This ratio was not commensurate with its peers in the industry.
- There was no system of preparing sales order. In majority of the cases, the companies did not maintain the supporting documents except for invoices.
- The Companies resorted to round-tripping of funds between various working capital limits with member Banks for diverting the funds raised from various Banks.
- Purchase was mainly confined to two suppliers and sales to three buyers only. The units of buyers were found inoperative.
- Commodities were not exported in the case of export finance availed from the consortium member Banks. Working capital fund was diverted to another entity controlled by a company and various other accounts including current accounts of promoters of the company.
- The funds were diverted on a large scale which establishes the fact that fraudulent activities were undertaken.
- Alternate procurement model was initiated by which pre-harvest farm loans were extended to farmers through Village Level Aggregators (VLA) supported by Post Dated Cheque (PDC) as collateral security.
- Fake inventories were created through collusion of employees and associates involved in procurement. With the introduction of pre-harvest financing, traditional practices and controls failed resulting in embezzlement of funds.
- Facts regarding depletion of stocks were suppressed and were not intimated to consortium. The management of the companies had misrepresented their performance to the consortium lenders at various occasions.

Systemic Improvement:

- Assessment of working capital limit should be done as per Bank guidelines/procedure. While assessing working capital limit, the scale of operations as reflected in VAT returns, stock records and sales register etc should be examined properly. This process should also be followed at the time of further enhancing the limit.
- Any enhancement by the member Bank should be first discussed in consortium meeting to maintain maximum permissible Bank finance and to ascertain the position of advance taken from other members of consortium.
- A proper scrutiny with respect to the number of debtors and the amount due from each debtor be done with reference to the records maintained by the firm and the debtors.
- There are frequent attempts by fraudsters to fabricate documents and avail finance from Banks. Creating awareness about loopholes, consequences of bypassing procedural aspects and check-points for evaluating genuineness of various essential documents become necessary.
- Investigation should be done to find out the trail of diversion so as to find as to where the money has gone and whether any money has been remitted /parked aboard.
- Immediately after filing the case with CBI, all the accounts of the promoters be confiscated and bank should take adequate measures

like appointment of administrator /receiver to take stock of all the accounts.

- CBI files the charge sheet in the trail court for criminal action without investigating the trail of money on account of fraud. Therefore, CBI should also investigate the trail of money so that action could be taken for recovery of money lost.
- Bank must immediately delist such third valuers, Chartered Accountants/ Chartered engineers, Advocates etc. who have questionable credentials/ have been negligent in their professional duties or have caused financial loss to the bank by their willful acts of omission/ commission/ dishonesty. A periodical review of all empanelled professionals should be ensured by banks for weeding out undesirable third party service providers.
- The Banks should pay the required attention to the area of internal control system and the fraud prevention measures to ensure compliance of instructions issued by them from time to time. The controlling offices should play their role of overseeing the functioning of branches effectively.
- The irregularities arising out of credit transactions should be meticulously looked into to satisfy whether these are on account of genuine trade/business transactions, market conditions, general state of industry and economy or overflow of corporate fraudulent transactions, which are being attempted to or are being concealed.
- Field functionaries should be advised to ensure end use of funds. They should follow proper due diligence and not to rely entirely on documents/papers produced before them. Documents and disbursement should be cross verified.
- It may be ensured that proportionate accountability is fixed in the chain of command including sanctioning authority in the event of fraud instead of fixing entire responsibility on lower functionaries.

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Media Sector:

The cases of frauds perpetrated by two companies in this sector have been analysed. The companies were in business of broadcasting on television channels, printing and publishing news paper and periodicals. Their projects were financed by banks under consortium led by one of the banks and the company also availed other credit facilities from various banks.

Modus operandi:

- The funds disbursed were got transferred from no lien account to various suppliers and group accounts by way of DDs or RTGS. The funds credited in suppliers a/cs were transferred to other companies where promoters were Directors or authorized signatories.
- Funds were diverted through suppliers' accounts which were the associates/ connected accounts of the borrowing companies. Further, there was huge difference in cost of equipments as per investigation report and the invoices submitted by the party.
- The Companies had submitted inflated and fabricated invoices which amounted to misrepresentation of facts to the Banks for securing higher limits and misutilisation of the same.
- One of the Companies had submitted a certificate from CA regarding infusion of capital. The Chartered Accountant had in writing denied having issued the said certificate. Hence, the company had submitted fabricated certificate to avail loans.
- Fraud element had been apprehended due to the fact that one of the suppliers was non-existent and in case of 3 major suppliers, the promoters had managerial interest by virtue of being on board of the supplier companies at different times.
- Funds were thus siphoned off and re-routed into the accounts of the promoters and their group companies which were further misused.
- One of the Companies raised loans from various Bank/ FIs through its two balance sheet periods by concealing the information/ details of its borrowers/ names of the lenders.
- The balance sheet figures were fudged/ fabricated with particular reference to the outside borrowings from Banks/ FIs. The company did not give the details of the lender wise exposure in the schedules of the audited balance sheets.
- The Company effectively prevented the lenders from insisting on NOC/ Confidential opinion from other lenders which otherwise would have revealed the true picture of total borrowings of the company.
- The funds were diverted to their accounts with other banks and were not utilized for the purpose for which these were given and the company misrepresented the facts and cheated the bank.
- The Company produced end use certificate issued by an auditor other than the one who audited company's balance sheet. The company concealed the information on existence of prior charge on one of the machineries offered as collateral security to the bank.

Loopholes/Lapses:

- Public money availed from banks in the form of loans, had been diverted through shell companies. The loans were granted at the highest level by most of the banks.

- Bank financed one of the companies overseas and end use was not ensured. Instead, the funds were remitted to various other companies not connected with the related activities of the company.
- Banks, which were not members of consortium had allowed the company to open account and transferred the money to siphon it off.
- No appraisal and due diligence was exercised by member Banks independently as they depended entirely on the lead bank for this purpose.
- Operations in cash credit account were neither monitored nor scrutinized/analysed properly. No enquiry was made to ascertain sources of funds brought by the company to build-up/ increase in tangible net worth.
- There were also a large number of credits in the accounts from group companies. The terms of sanction clearly stipulated that funds should not be diverted to sister/ group/associates concerns.
- There was lack of competence & skills to appraise technical aspects of a project for finance from banks & invariably banks accepted whatever was stated by the borrower.
- There was no mechanism to verify & counter check the antecedents of suppliers of equipments regarding their capacity, life of equipments, maintenance etc.
- The objective of forming different companies for similar activities was not enquired. No action was taken by the banks to ensure segregation of securities.
- The other Company did not publish its audited balance sheet for the relevant period. The company made the lenders to forcibly fall back on the immediately previous audited balance sheet for appraising the loan proposals.
- The Company had committed the purported fraud with the connivance of Chartered Accountant of the agency responsible for due diligence. The balance sheet of the company does not reveal true picture of the financial position of the company.
- The Company had also got the valuation of the securities manipulated by reporting inflated value in connivance with the valuers.

Systemic Improvement:

- The main company had formed further companies which were engaged in similar business of post production activities and were actually working in close clusters/ premises. Banks should scrutinize the objective of forming different companies for similar activities.
- At the time of carrying out the review, the past track record of the borrower or the length of his satisfactory association with the bank should be one of the considerations. The status of the borrower should be more critically analysed.
- The field functionaries should find out the kite flying operations from the nature of transactions and their respective character.
- The field level functionaries should be advised to scrutinize the financial statements submitted by the borrowers thoroughly and where ever it is observed that the short term funds are used for long term purposes and vice versa, they should be advised to ascertain from the borrower the reasons and purpose of the same and record the same in appraisal notes.
- Due diligence of suppliers of machinery equipment should be done by the branches even when it is not specified in the sanction letter. In some cases no efforts were made by the branch to enquire whether the supplier is a manufacture or a trader.

- Branches should read and study the Audited balance Sheet of the borrower as expected. Adverse observations by the auditors should be read and critical observations be discussed in the credit appraisal.
- Field functionaries should be advised to ensure end use of funds. They should follow the proper due diligence and not to rely entirely on documents/papers produced before them. Documents and disbursement should be cross verified.
- The Banks should pay the required attention to the area of internal control system and the fraud prevention measures to ensure compliance of instructions issued by them from time to time. The controlling offices should play their role of overseeing the functioning of branches effectively.
- Any enhancement by a member Bank should be first discussed in consortium meeting to maintain maximum permissible bank finance and to ascertain the position of advance taken from other members of consortium.
- Immediately after filing the case with CBI, all the accounts of the promoters be confiscated and bank should take adequate measure like appointment of administrator/receiver to take stock of all the accounts.
- The Bank should adopt coordinated approach in expeditiously taking the issues in hand instead of adopting compartmentalized approach.
- CBI files the charge sheet in the trail court for criminal action without investigating the trail of money on account of fraud. Therefore, CBI should also investigate the trail of money so that action could be taken for recovery of money loss.

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Aviation Sector:

The case of frauds perpetrated by a company in this sector has been analysed. The company commenced its commercial operations in this sector in May 2005. The company was a leading Airlines company of India with a market share of 21% in domestic operations. The company was promoted by another group which had presence in several countries.

The company was one of the domestic companies offering service on international routes and operated in both segment of the market, i.e. low-cost segment and full serve segment. The company availed credit facilities from the banks under consortium arrangement led by one of the bank.

Modus operandi:

- The Company cheated the bank by suppressing facts in the financial statements and diverting the funds to related entities for the purpose other than those for which finance was made.
- The Company ran its operations mostly on leased aircraft for which an overseas entity (vendor) was created which in turn had created fictitious invoices with inflated bills. The money was transferred to it through legal means. Whatever the money the company owed to the leasing company would be disbursed and rest parked with the entity.
- The entire transaction carried out was legal as it was done through proper banking channels. The vendor had submitted invoices and created intermediaries which had nothing to do with the leasing of aircraft. Therefore, funds received by the vendor were illegal.
- The Company willfully cheated the banks with an intention to siphon off funds. The money apparently was diverted to several shell companies in seven countries.
- The Company's promoter willfully and malafide intension did not pay the dues covered by his personal and corporate guarantees. Despite restraining orders from High Court, the promoter entered into an arrangement with overseas company to receive a big amount for stepping down from his office and position as Director and Chairman of group.

Loopholes/Lapses :

- The lapses with respect to loans extended to the defunct airline which was under scanner. The company's balance sheet was never strong and its credit rating was lower than what was required for sanctioning loans.
- All Banks under consortium financed the company on the basis of brand capitalization. Valuation got done through a private company which was much higher than what was valued by other valuers.
- There was alleged conflict of interest of at least three independent Directors on the board of the airline. SFIO had alleged that certain private companies and three independent Board Directors of the Company had a commercial relationship with the airlines.

Systemic Improvement:

- Advances/credit facilities were sanctioned to the company on the basis of Brand name which does not form any tangible security for the purpose of recovery. The practice should be discontinued in future.
- The Company submitted brand evaluation done by private entities. Banks blindly accepted the higher one. Bank considered

report of only one valuers for the valuation of brand and based on that loans were given to the carrier. Regulations issued by RBI require that at least two different valuation reports should be considered before deciding credit facility on the basis of brand in case the brand name is to be considered as security.

- The past track record of the borrower or the length of his satisfactory association with the bank should be one of the considerations. The status of the customer should be more critically analyzed while renewing the existing facilities.
- Managing fraud risk in large value advances need a comprehensive approach. There has to be changes in mindsets, fine tuning of work processes and human resources skills. There has to be better information sharing among banks. There has to be more effective fraud management systems. There has to be better support from enforcement agencies and there has to be legislative.
- Multiple banking arrangements in large value financing have done more harm than good to banks. This type of arrangement enabled corporate to secure multiple finances from various banks far in excess of their requirements. Funds raised were easily diverted through company's accounts with various banks in the absence of effective exchange of information between the banks.
- Banks do not have a fool-proof system of checking and confirming whether the company has actually been working on the contracts and whether the contracts were genuinely business based.
- The Government should consider examining the role of third parties such as Chartered Accountants, Advocates, Auditors and rating agencies that figure in accounts related to bank frauds and put in place strict punitive measures for future deterrence.

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Service/Project Sector

The cases of frauds perpetrated by three companies in this sector have been analysed. The companies were in business of providing corporate logistic services, Industrial and engineering projects, plants & machineries, equipments etc under lease agreement. The Companies were enjoying working capital/ term loans from the banks under consortium arrangement led by one of the banks.

Modus operandi:

- One of the companies induced the bank to sanction and disburse loans for 2804 vehicles to the company and its' employees/ drivers on the basis of false assurances and tampered/forged vehicle registration documents.
- In respect of the loans availed by giving false assurance of getting the vehicles transferred to the drivers/ employees by clearing past dues of the existing lenders, the Directors of the company deliberately and with intent to cheat, willfully neglected to transfer the ownership to the said drivers/employees as a result of which amount disbursed by bank towards finance of vehicles became overdue.
- The loans availed for purchase of new trucks was willfully diverted by the accused Directors and the trucks were never purchased. The funds for transfer of old vehicles to the drivers were also diverted for other purposes. In most of the instances, even the registration documents were not submitted to the bank whereas in several other instances old vehicles were passed off as new.
- Another Company got issued performance cum mobilization advance guarantees in favour of aggregators. The mobilization advance should have been utilized for execution of contracts against which the advances had been remitted by the beneficiary.
- A part of the funds was utilized for giving margin/charges to the banks instead of providing such margin by the promoters from their equity. The Company also partly remitted the fund back to the mobilization advance received from the Aggregator which was not comprehensible and was highly questionable.
- The Banks sanctioned enhancement in bank guarantee limits for more than 10 years based on such information as provided by the Company. The guarantees were eventually invoked. Defaulted guarantees account was debited and after adjusting the cash margins available with Banks amount was paid to overseas Banks. It was dishonesty on the part of the Company to avail the facility by misrepresenting and concealment of facts.
- Another company did not have loan policy approved by board as envisaged for Non-Banking Financial Companies (NBFC). The company had not fixed prudential
- limits as part of Assets Liability Management (ALM) for individual gaps and cumulative mismatches as envisaged by RBI.
- Thereafter, the company was reclassified from Deposit taking NBFC to Non-deposit taking NBFC. After an inspection of the company's accounts for a particular period, RBI directed that until further orders, the company would not sell, transfer, create charge or mortgage or deal in any matter with its property and assets without prior permission from RBI.

- As per report of the forensic auditors, the fraud was perpetrated by camouflaging the Balance Sheet in collusion with Statutory/ Internal Auditors to avoid detection.
- It was identified that the methodology followed by the company was for window dressing. It was found that the company had inflated income and assets by creating falsified entries.
- The financial accounting and loan assets data of the company were maintained in Oracle data-base. This software being a proprietary one, lacked security controls. The company's top management, senior executives and employees manipulated the records by using this software.

Loopholes/Lapses:

- The signatures of applicants/ borrowers were not obtained in person. Bank handed over the documents to the officials of the company for getting them executed. Therefore, there was no base document with the specimen signature of the borrower which could be relied upon to conclude that the documents were signed by the respective borrowers only.
- The company transferred only 227 vehicles in the name of drivers as against 1652 vehicles financed by the bank for the purchase of second hand vehicles. The company had failed to transfer the vehicles although it had received sale consideration from the bank and thus it had defrauded the bank in respect of second hand trucks.
- Bank had sanctioned the loans for purchase of new vehicles to drivers of the company but the vehicles were not transferred /registered in the name of drivers. Thus the company had defrauded the Bank in respect of new trucks.
- There was inter-relationship between the buyer, vehicle dealer and body building unit. The Proforma invoices issued for body building /trailer were inflated. There was diversion of funds/ round tripping of funds.
- Business model of the company including the existence of Master Agreement with Aggregators/ Agreement between the company and its vendors, were not disclosed to bank/consortium. Thus, it concealed the existence of the said agreement and misrepresented its lenders with regard to it business model. It was found that there were a number of clauses which were exclusively in favour of the Aggregators which were not informed to the bank.
- The Company did not utilize the funds for the purpose i.e. for execution of the contracts. 30-35% of the funds were utilized for giving margin/charges to the banks from the mobilization advance as against the normal practice of providing such margin by the promoters from their equity.
- The Company had not provided the bankers any evidence of having utilized the mobilization advance for execution of the contracts for which these guarantees were issued which in normal case should have been remitted to its vendors for the execution of the specific contracts.
- The Company had not utilized the mobilization advances received under BGs/ SBLCs for execution of the projects for which BG/SBLCs had been issued. Further, reports of various consultants appointed by the Consortium indicated lapses on the part of the company with regard to compliance of FEMA regulations, ROC regulations etc.
- It was also revealed that the overseas beneficiaries had discounted the BG/SBLCs with banks in Europe and remitted the

funds back to the company as mobilization advance. However, the company had not utilized the funds for execution of projects; but instead diverted the same and utilized as margin for the guarantees issued on their behalf.

- The Company had submitted end use verification certificate issued by Chartered Accountants stating that the loan had been utilized by the company for its working capital requirement and general corporate purpose which was not correct.
- The facts of the case reveal that the fraud occurred due to dishonesty on the part of company who got the limit sanctioned by misrepresenting & concealment of facts coupled with lapses in pre-sanction appraisal and post sanction follow up.
- The stocks on hire under hire purchase agreement were calculated as per the agreement value less the installments received from the corporate and net of un-matured financial charges.
- The Company availed finance from the banks against the value of stock on hire under hire purchase agreement. The company had financed other companies in the form of corporate loans and was refinancing hire purchase loans for purchasing of old assets.
- The promoter of the company and statutory auditors of the company engineered the fraud in a systematic way against the bank by flouting the relevant provisions of Companies Act, incorrect filing of returns under service Tax, VAT and income Tax.
- Various lease transactions were pre closed, but the assets were not written off and the same were continuing in the books of account of the company. Part of the amounts received through pre closure was directly booked as income and part amount was kept in debtor suspense account. The lease rentals as per the original tenure were continued and income was recognized.
- The Company formed satellite companies with employees of the company as directors. The satellite companies were formed mainly to acquire share of the company and to transfer the NPA of the company to these satellite companies.
- The satellite companies were granted loans by the company through bogus loan agreement for acquiring NPA accounts of the company. With this NPA provisions were reduced and profit of the company boosted.

Systemic Improvement:

- Genuineness of quotations should be verified through visits and direct contact with dealers. In case of vehicle loans visit to the dealer must be performed to check genuineness of dealership. The credentials, genuineness, capability to supply of vehicle and line of trade of the dealers should be verified through documents and personal visits before sanction of loan.
- Bank may issue supply orders in consultation with dealer on the basis of quotations or contract agreement between supplier and borrower duly considered by Bank in the proposal /sanction instead of direct payment to the supplier before supply. This will ensure generation of bills/invoices and facilitate delivery of goods in proper custody before payment.
- Field functionaries should be advised to ensure end use of funds. They should follow the proper due diligence and not to rely entirely on documents/papers produced before them. Documents and disbursement should be cross verified.
- The contractual obligations between the parties need to be verified from the point of view of onerous clauses by legal advisor. Banks should take extra care when advance

payments under BGs are received and ensure end use as being done in the fund based limits.

- While considering/sanctioning such limits in future, it may be stipulated that amount received as mobilization advance be credited to an Escrow account and its end use be monitored.
- There are frequent attempts by fraudsters to fabricate documents and avail finance from banks. Heightened awareness of loopholes, consequences of bypassing procedural aspects and check-points for evaluating genuineness of various essential documents become necessary.
- The Banks should clearly outline requirement of field visits by the controllers and also stock inspection of large borrowal accounts above a cut-off point by an external agency. This would be in addition to the regular inspection/ field visits by the line staff and the controller. Observations of the visiting officers/stock/ credit Auditors must necessarily find place in every review/enhancement proposal of the borrower.
- The Banks should pay the required attention to internal control and fraud prevention measures in addition to instructions issued by them from time to time. The controlling offices should play their role of overseeing the functioning of branches effectively.
- The loan asset management should require to be prudentially monitored with a view to ensure that no potential fraud in the garb of temporary irregularity, liquidity crunch etc is allowed to go undetected for an unduly long period. The appraisal, sanction, monitoring, review and renewal of borrowal accounts should be objective and discretion free.
- The irregularities arising out of credit transactions should be meticulously looked into to satisfy whether these are on account of genuine trade/business transactions, market conditions, general state of industry and economy or overflow of corporate fraudulent transactions, which are being attempted to or are being concealed.
- The system of credit audit should ensure that all the credit decisions beyond a cut-off point would be scrutinized to ensure that the norms of appraisal, review and renewal have been duly complied.

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Discounting of Cheques & other issues:

The case of fraud perpetrated by a Chartered Accountant & others in this sector has been analysed. A firm was empanelled for conducting concurrent audit of the bank branch. A qualified CA who was a sleeping partner in the firm had gone through the nitty-gritty of the CBS system while conducting audit of the branch. The CA had created several fake and false documents pertaining to his clients. Misusing this information, CA committed a mind boggling fraud against the bank.

Modus operandi:

- The CA accessed the Pan and Voter ID cards, business details, financial statements and IT returns etc pertaining to his client who was required for opening of accounts and availing of bank loans.
- The CA had created several fake and false documents for his own manufacturing factory at a location. He had forged signatures in various documents.
- The officials of the Banks at branches in the different cities and also at controlling office of bank colluded with a group of customers and defrauded the bank by purchasing/ discounting fake/fraudulent cheques, discounting of fake inland bills, arranging overdraft/loan limits against non- existent LIC policies and also arranging housing Loan /Loan against property without proper title/security or through dummy borrowers. The CA was the main person behind all the fraudulent transactions.
- The fraudulent transactions had been taking place since 2011.These transactions were nullified with proceeds of new fraudulent transactions to avoid deduction.
- There was inter-link between transactions in three branches with many customers having accounts at all the three branches. The fraudulent transactions were carried out mainly through the discounting of cheques, discounting of fake bills and overdraft against LIC policies.
- The surrender values of the policies were unusually high, often not found in such numbers. Verification of policies with LIC of India revealed that these policies were issued in the name of different LIC offices, for different terms and sum assured.
- There were number of accounts involving a huge amount under the Housing loan category which had either a commonality of the name and/or had some linkage to the audit trail of the fraudulent transactions. In most of the cases security/ assets were not created.

Loopholes/Lapses:

- The accounts were opened without complying with KYC guidelines. The customers would not come to the branch for opening the accounts. No personal interaction took place. Their credentials were never cross verified with the original/ through net and there was no practice of independent verification of addresses provided in the application.
- The accounts were opened with an intention to allow discounting of cheques on a continuous basis to selected parties which were related to each other either by blood or bondage or through financial considerations.
- No standard operating procedures ; may it be purchase/discounting of cheques/bills, sanctioning of loans/overdrafts against LIC policies and /or sanctioning loan/ overdrafts for acquiring house/commercial properties were followed.
- The system in the bank did not furnish any alert when the account was opened with

the same officially valid documents of a person already having account with the bank. As a result, accounts of the borrowers were opened at three branches to facilitate fraudulent transactions.

- The concurrent auditors failed to take note of such fake transactions. The Internal Inspectors also failed to detect and comment about unabated purchase and discounting business, KYC norms, non compliance of systems and processes and the bogus/ fictitious documents produced by the branch officials while compiling the reports.
- The officials of the controlling office of the bank ignored the alerts communicated by off-site monitoring cell (OMC), HO, and communicated their full satisfaction about the genuineness of the transactions.
- The Regional Office of the bank failed to take notice of the way the business was being conducted in these branches. The branches discounted cheques beyond their delegated powers on several occasions without obtaining permission/ approval from the Regional Office of the bank.
- All the discounted cheques were serially numbered and all were for round figures which were the characteristics for accommodation purpose. The wrong practice which was going on in the branches of bank was well within the knowledge of officials of the bank.

Systemic Improvement :

- Bank should set up centralized processing centers for opening of accounts. This will be an additional tier for online cross verification of KYC documents like PAN, Aadhar etc. These measures would minimize the incidence of fraudulent KYC documents. Bank should also introduce alerts in the system while opening the account on the basis of same KYC (i.e. Pan Card, Aadhar etc.) document in different branches.
- Bank should set up centralized loan processing hubs which will help in streamlining the selection of borrowers with enhanced due diligence, assessment of proposal etc, thus delinking the sanction process from the business owner i.e. branch heads.
- The monitoring system should be strengthened to detect the frauds. Offsite monitoring by the offsite monitoring cell at Head Office and respective Regional Offices should also be strengthened.
- Spurt in advances should be periodically monitored and such identified branches shall be subjected to detailed verification of loan portfolio. Retired officers for assisting in the internal audit of the Bank should be empanelled.
- Integrity, honesty and administrative skills be yard stick for selecting Branch Heads, Regional Heads, Zonal Heads and inspection and monitoring officials. Training system should be reviewed and issues pertaining to vigilance should be made mandatory in the training system. It will help understand the participative, preventive and detective methodology, particularly for those who have newly joined the bank.
- Inspection system should not be for name sake and it should be manned by knowledgeable and experienced persons to prevent, detect and report malpractices in the bank to the top management. Selection of Concurrent Auditors & Statutory Auditors should be appointed in consultation of Institute of Chartered Accountants of India (ICAI). Advocates and Architects (valuers) should be appointed in consultation with respective associations.
- LIC policies should be checked through online to verify the surrender value. Advance against LIC policies be entertain through CIBIL. Secrecy of password be maintained at all levels. ◆

Trading Sector

The cases of frauds perpetrated by three companies in this sector have been analysed. The companies were in business of trading in coal, pulses and agro commodities, and aluminum foil rolls. The companies had adopted a business model by which they imported goods from foreign banks/private parties against SBLC/ LC/ Cash Credit for trading in domestic market. The Companies availed credit facilities from the banks under consortium arrangement led by one of the banks.

Modus operandi:

- The company had diverted a substantial amount of fund to related parties/ associate concerns. The creditors had not been deducted for the purpose of calculation of drawing power. The scrutiny of purchases and sales of the company revealed that there were many cases where the same party was the customer as well as the supplier.
- The Company violated accounting principles and misutilised funds for other purposes. Funds were utilized towards purchase of real estate in the name of the director and his relatives.
- The other Company submitted the documents with the bills drawn under the letters of credit issued/opened on behalf of the borrowers which were fabricated and the underlying transactions were not real merchant trade transactions. The letter of credit mechanism/ RTGS facility for kite flying transactions involving unconnected parties were grossly misused by the borrowers.
- When the bills drawn under the letters of Credit (LC), opened on behalf of the company, started devolving, the bills were met by creating overdrafts in the accounts as fund was not provided by the company.
- In case of another company, the credit facilities were given by the banks to the borrower for the purpose of manufacturing and exporting of aluminum foil containers, its lids and covers. However, the company instead of utilizing the funds for which the credit were granted, utilized the same for granting loans for the other entities without any security or documents and that too in the sectors which were not even remotely related to the core business activity of the company.
- The Company resorted to falsification of the account by manipulating the position of LCs/ Buyers credit outstanding in the monthly stock statement thereby overstating the drawing power in the cash credit account.
- The company's debts increased substantially during a particular period. The funds were utilized for investments mainly by way of loans and advances, the returns of which were not immediately forthcoming.
- During Investigation, some unusual transactions were observed in the account of another company. Funds were diverted to finance various sister concerns/associates dealing in various areas of business ranging from real estate development to gambling business (breeding price bulls and race horses).

Loopholes/Lapses:

- The Company dealt with many related parties including subsidiaries/associates including their key management. The gross amount receivable from the related parties was much higher while amount payable was much less.
- The bills which remained unrealized from the associate concerns reflected funds

which had already gone out of working capital cycle for long since in many cases there were cross transactions of sales and purchases from the same party i.e the same party was the buyer as well as the supplier on different occasions.

- The Company had not made transactions in accordance with RBI guidelines on merchant trade. In the case of LC opened, it was noticed that major transactions had taken place in a bank with 2 parties with same address where they had acted as customers as well as suppliers.
- The Company had routed transactions from banks outside the consortium to keep the business going as devolvement had taken place in majority of banks. The 60% sale of the company had such cases where records of delivery/ movement of goods had not been maintained.
- The promoters in connivance with their Chartered Accountants had submitted doctored financial papers for getting finance from different banks. The Chartered Accountants wrongly certified the balance sheets for three years from 2007-08 to 2009-10 overstating the profits /understating the losses.
- The bills drawn under LCs opened by the bank were suspected to be accommodation bills for the purpose of raising finance. The method adopted by the company revealed that the underlying transactions were not real merchant trade transactions and were only kite flying transactions.
- During investigation, it was observed that there were major diversion of funds from the borrower company's cash credit account to personal SB and CD accounts of the promoter directors and other unrelated accounts.
- The company was consistently showing inflated sales, stock holding levels and trade debtors. Book debts statement was given with assumed and artificial figures. Names of debtors were not mentioned by the company.
- Out of loans & advances sanctioned, a substantial amount of loan was free of interest by the company extended to various entities. Loans were extended in accounts, wherein no movement of receipt or payment was observed during a particular period.
- The Company had advanced loans various companies engaged in trading of bullion. Out of these advances, a large amount had been adjusted against expenses not directly attributable to company's business.
- On review of stock statement submitted to the lead bank, it was observed that the scrap was included as stock in monthly statements. Hence, stock statements were inflated.
- As per the monthly stock & statement submitted to the Bank, it was observed that creditors had substantially decreased as compared to creditors as reported in the previous month.

Systemic Improvement:

- End use of fund disbursed should be monitored and due diligence procedures should be applied to identify instances of utilization of funds for purposes not related to the business of the client.
- Even in the cases where the funds were disbursed for the purpose of working capital, its end use should be verified so as to avoid diversion of funds. Confirmation may be obtained from the customer on the utilization of funds.
- Periodic balance confirmation from top five suppliers/ buyers (creditors/ debtors) should be obtained/ ensured in stock audits

and should be analyzed as a part of stock statement.

- Banks should have a fool-proof system of checking and confirming whether the company is actually working on the contracts and whether the contracts are genuinely business based.
- Corporate governance in banks in the present form is a matter of concern and has to be strengthened. Housekeeping and internal control of banks have to be strengthened.
- Multiple banking arrangements in large value financing have done more harm than good to banks. This type of arrangement enabled corporate to secure multiple finances from various banks far in excess of their requirements. Funds raised are easily diverted through company's accounts with various banks in the absence of effective exchange of information between the banks. There is a need to review the multiple banking arrangements.
- Realization of receivables and payment to creditors are required to be monitored. In case transactions routed through the accounts with consortium members do not tally with corresponding movement reflected in the stock statements, Concurrent Auditors to monitor the transactions need to be appointed by the member banks.
- The debtors' position of the borrowers should be closely monitored. It should be a part of the Stock Audit and Inspection and audit report. Controller should critically go into on the quality of business booked by branches and sudden spurt, if any, observed in business growth should be thoroughly investigated.
- Operating officials are being equipped with inputs on Forensic Audit areas and to understand the complex business models especially transactions through Associates concerns/ wholly owned joint ventures.
- Bank must immediately delist such as third party valuers, Chartered Accountants/ Chartered engineers, Advocates etc. who have questionable credentials have been negligent in their professional duties or have caused financial loss to the bank by their willful acts of omission/commission/ dishonesty. A periodical review of all empanelled professionals should be ensured by banks for weeding out undesirable third party service providers.

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Information Technology (IT) Sector

The cases of frauds perpetrated by three companies in this sector have been analysed. The companies were engaged in assembling of computer peripherals, system integration/ solution, data center activity, software solution & consultancy, integration & other hardware related products and networking. The Companies availed credit facilities from the banks under consortium arrangement led by one of the banks.

Modus operandi:

- One of the companies did not take off the project of two organizations as planned for various reasons including the company not agreeing to certain terms and condition of both the projects.
- Earnest Money Deposit (EMD) in the form of a Bank Guarantee issued by a bank in favour of one organisation was invoked on account of non- agreement on certain terms and conditions of Letter of Intent by the company. The project of the other organization was also cancelled in June 2013, as the other bank did not issue performance Guarantee of Rs.69 crore.
- After the disappearance of CMD of the company, it emerged that the employees' salaries had not been paid. Thereafter, the business operations of the company came to standstill.
- As per Annual Balance Sheet of the company as on 31.03.2013, stock and book-debts were shown at Rs.204.75 crore and Rs.587.97 crore respectively. The account became NPA on 29.05.2013 with bank. After 01.04.2014, there was negligible turnover in the accounts with banks. As per audit report, stock as on date was Rs.30 to 35 crore and book-debtors were Rs.7 to 15 crore. Sudden decline in value of stock/book debt without corresponding credits in the accounts aroused suspicion.
- It appeared that the company had fudged the figures in the balance sheet and had represented wrong/inflated financials to avail credit facilities from all members of banks in the consortium. Further, the debtors did not acknowledge the debts when banks wrote to them.
- Another company availed credit facilities to implement ISP services in three states. The promoter of the company obtained loan from the banks by making false and misleading disclosure with an intention to cheat the banks.
- The Company did not create assets out of bank's fund and diverted funds through fake companies floated for the purpose. The company had created 3 fly by night operator companies in a state as vendors for raising fake bills who never supplied any software/ hardware.
- Where about of these India based suppliers were not known. RTGS were sent to the accounts of these companies with private Banks on disbursement of term loan. Thereafter, money from these accounts was transferred to company's accounts of interested parties maintained with these Banks.
- SEBI in its order, based on the preliminary investigation into the matter of violation of SEBI Act, observed that the company had diverted the loan funds for playing in stock market through entities. These entities played with the scrip of the company presumably to jack up its price.
- Another Company had submitted debtor's statement as on 29.06.2013 for availing Drawing power. Accordingly 34 major debtors were selected and job of verification

of debtors was distributed among the member banks of the consortium.

- Three member banks informed that the list of debtors provided by the company was false having no outstanding in the books of debtors.
- Drawing Power (DP) calculation could not be justified as the basis for calculation of DP was not provided such as valuation of work in progress, debtors position etc. Moreover, the damaged goods and or obsolete goods were included in the stock statement.
- The Company had submitted a statement of fake receivable to the consortium for availing DP Loans from other financial institutions were availed without permission of consortium.
- One of the member banks had disbursed limits on the basis of the allocation letter purportedly issued by the lead bank which had denied having issued such allocation letter. It was revealed that the company had produced forged letter and got the limit disbursed.

Loopholes/Lapses:

- It appeared that CMD of the company, in connivance with other directors, had provided false book debts/ stock statements and had inflated the profit & loss account.
- There was transfer of funds including siphoning off funds, diversion of term loans disbursed by the banks for creation of Data Centre Racks by the company. There was an involvement of group companies in misappropriation of funds.
- Finance was made on the basis of stock statement. The company did not co-operate for conducting stock audit. The auditors expressed their inability to carry out audit.
- Majority of receivable were non-existing. Information from debtors of the company was sought. The replies of debtors pointed to suppression of facts and falsification of financial statements.
- The Company created hypothecation over stock, book-debts/receivable through hypothecation agreement. However, it conspired against the banks and siphoned of funds by disposing of hypothecated goods.
- Loans availed from two banks were not reflected in the financial statement as on 31.12.2012. Similarly, loan availed from L & T finance was not reflected in the books of account in spite of creating charge in its favour. The liabilities with four other banks were shown as other current liabilities which were apparently borrowings.
- Verification of invoices revealed raising of multiple invoices. With reference to all contracts entered into with customers, though the work was supposedly executed in India or controlled from India and the invoices were raised from India, there was no direct remittance through Indian Banking channel from the customers.
- The funds released under Packing Credit were seen directly transferred to the bank accounts of the company in USA and utilized for US operations, which was a clear indication of diversion of funds. Book debts were hypothecated to the bank as floating charge and no registered power of attorney was there so the bank could not realize the dues directly from the debtors.
- The stock position was not satisfactory/ encouraging in view of outstanding level of debt and fast obsolescence of computer items. All the debtors were more than 180 days and chances of recovery were bleak.
- The Company had not furnished clarification regarding non-confirmation of debts by some of the debtors. This indicates the fraudulent intention of the company & its promoters. The Company did not route sales

proceeds through accounts of any bank in the consortium.

- The investigation revealed that the borrowers/promoters had indulged in fraud with another financial institution which was being investigated by EOW, Delhi police.
- Risk Based Internal Auditor revealed certain irregularities such as CA certified age wise statement of book debt, credit report of overseas parties were not obtained.
- Monitoring of the time schedule of supply as per the order was not done by lead bank which resulted in non- realization of debtors and liquidity crunch. During investigation, it was revealed that the lead bank had failed in discharging its duty as the DP communicated to the members was not properly calculated.

Systemic Improvement:

- Adequacy of credit monitoring measures. It must be ensured that all the required safeguards in disbursement of loan and ensuring intended end use of funds are in place.
- Advising the operating offices that all term loans details of major suppliers/vendors should be finalized at the time of sanction of term loan and disbursements made to the specified parties directly.
- In consortium banking arrangement, any new bank entering into the consortium must take credit opinion report at least from the lead bank if not from all the existing banks and must take written consent from the lead bank before release of funds.
- The business model, especially in an IT company needs to be understood in its entirety. Highly technical/complex projects need to be subjected to independent verification by subject expert, invariably.
- Meaningful analysis of stock statements to be carried out. Confirmation to be obtained from debtors at periodical intervals. D & B Report/Opinion Report on major debtors to be obtained. Also regular monitoring of the operative account to be ensured. Scrutiny of large withdrawal/transfer to be made.
- The debtors position of the borrowers to be closely monitored. It has been made a part of the stock audit and Inspection & Audit Reports.
- A member bank under consortium released the limits based on the allegedly forged letters purportedly issued by Leader Bank. The lead bank must send intimation to the other members about the drawing limits released by it and seek confirmation/ acknowledgement of the same.
- Bank must immediately delist such third party valuers, Advocates/ Chartered Accountants/ Chartered engineers etc. who have questionable credentials/have been negligent in their professional duties or have caused financial loss to the bank by their willful acts of omission/commission/ dishonesty. A fair transparent procedure needs to be devised in appointing such professionals.
- The Government should consider examining the role of third parties such as Chartered Accountants, Advocates, Auditors and rating agencies that figure in accounts related to bank frauds and put in place strict punitive measures such as cancellation of the registration by respective regulatory authorities for future deterrence.
- There should be no deviation from Bank's extent operating instructions in handling discounting of bills drawn under LCs. Suitable briefing to stock auditors and using stocks & receivable audit as an effective tool for control and supervision of advances.

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Export Business Sector

The cases of frauds perpetrated by four companies in this sector have been analysed. The companies were engaged in exporting cotton bales, cotton & synthetic yarn, agro/ engineering goods and readymade garments to China, Dubai, Singapore and other countries. The Companies availed credit facilities from the banks under consortium arrangement led by one of the banks.

Modus operandi:

- Bank was discounting the export bills of the company against LCs from prime banks of the buyer. The payment/acceptance of bills was delayed. On the request of the company bank had extended the due date of bills.
- As per information gathered from Custom authorities, export had not taken place against most of the bills. Goods produced for exports against packing credit (PC) were also not available. It appeared that either goods were not produced against PC or disposed off locally and funds were siphoned off.
- The Customs authorities had informed that exports did not take place in 200 cases out of the pending 203 bills, as these consignments did not relate to any exports.
- Another company availed multiple loans from different banks/ institutions for acquisition of the same set of equipments from the same suppliers at almost similar estimated cost.
- Completion of projects was confirmed to respective banks/institutions by submitting false/ fabricated certificates from Chartered Accountants and false status reports. Term loans were not accounted for in the year of their receipt/payment.
- The cash inflows and out flows were dealt with outside the books of accounts and not reflected in the audited balance sheets of the company during respective years.
- One other company had given the same export orders to various banks in consortium and availed packing credit facility. The company did not submit the export documents to the same bank from whom the packing credit was availed.
- The Company submitted contract documents to member bank for availing the credit facilities. The company had obtained export packing credit disbursement from another bank against the same contract document.
- The list of book debtors submitted by the party showed that most of the debtors were foreign buyers. In the backdrop of payment received from third parties and the bills getting returned, earlier the company had stated that the goods were sold to alternate buyers as the original buyers were renegotiating the price after dispatch of consignments.
- In respect of the creditors for suppliers, full details of such suppliers were not available. The investigating officer stated that the creditors for the supply were fabricated in order to artificially boost the purchase, sale and receivable.
- The borrower companies cheated the bank by submitting fake and forged export bills for purchase/discount which were drawn in nonexistent overseas buyers.

Loopholes/Lapses:

- The bank had discounted the bills against the terms of the sanction without ensuring acceptance of bills and confirmation of due date for payment from LC issuing bank. The bank did not obtain GR form of shipping bills verified/issued by custom authorities.

- There were several apparent major discrepancies in set of bills submitted for discounting which should have aroused suspicion about genuineness of bills. Due date of bills extended at the request of the company without ensuring acceptance of bills, analyzing reasons for non acceptance of bills and delay in acceptance of bills.
- The Chartered Accountants including Statutory Auditors tended to collude and conspired to be a party in submitting false, fabricated and misleading financial statements and certificate to the institutions/ banks with the only intention of obtaining disbursement of the financial assistance.
- The company had managed affair of the company based on false and fabricated books of accounts to ensure easy and smooth flow of credit without any restraint by way of term loan from financial institutions for funding cash losses.
- The proceeds of packing credits & FBPs credited to the account were withdrawn on the same day in clearing suggesting improper end use and diversion of loan proceeds.
- The export transaction undertaken by the company was suspect considering the fact that within a span of less than 3 months the utilization of the limit was to the brim under PC and negotiation of bills under LC.
- Realization proceeds of export bills credited to current account of the company which was subsequently withdrawn by the company when bank packing credit was outstanding.
- Credit report of all associates/ sister concerns was not obtained from their banker as per terms of sanction. Periodical inspection for packing credit disbursement to ensure end use was not carried out.

Systemic Improvement:

- Monitoring of systems and MIS generation has to be strengthened. Housekeeping and internal control of banks also have to be strengthened.
- There are lacunae in bank's credit and risk management policies. Proper mechanism to be devised for review of the policies of the bank and to keep it updated as per change of environments.
- Multiple banking arrangements in large value financing have done more harm than good to banks. This type of arrangement enabled corporate to secure multiple finances from various banks far in excess of their requirements. Funds raised are easily diverted through company's accounts with various banks in the absence of effective exchange of information between the banks. There is a need to review the multiple banking arrangements.
- There should be no over confidence on the borrowers based on their stature. Bank's top management should take considered decision on the merits of the proposal irrespective of the reputation of the company.
- Fraud monitoring in financial services should be a specialized area and a specialized cadre may be created to monitor and investigate such cases. The skill gaps in banks should be addressed through proper training.
- Management of fraud risk in large value advances need a comprehensive approach. It requires being changes in mindsets, fine tuning of work progress and human resources skills. Banks need to have a system of real time information sharing among them. To deal the fraud effectively, there has to be better support from enforcement agencies coupled with strong legislative.

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Fixed Deposit Fraud

The miscreant pretended to the Govt Organizations/Corporates as representative of a Bank and to the Bank as financial advisor of these Organizations/ Corporates, brought bulk deposits to the branch of different Banks. He kept the original TDRs issued by the branches with them and submitted fake copies to the depositors.

Thereafter the miscreant opened loan/overdraft accounts in the name of depositors by submitting fabricated documents along with original TDRs to the branch. They had siphoned off the money through RTGS in his various associate accounts with different banks.

Modus Operandi:

- The deposits were canvassed by the branch manager through a private person and mobilized bulk deposits of about Rs.604.33 crore through the private person from the seven Government Organizations/ Corporates.
- Term deposits accounts were opened at the branch after obtaining KYC documents from the concerned organization. The KYC documents were received through the private person. Term deposit receipts (TDR) were delivered on the basis of the Organizations/ Corporate authority letters.
- Later on the private person submitted application for loan, purportedly made by Organization/Corporate holding deposits with branch for loan / overdraft against TDR.
- The loan applications accompanied with original TDR receipt, duly discharged by the signatories who had signed the documents earlier submitted to the branch. The sanctioning authority, after completing the necessary formalities, sanctioned the loan/ overdraft.
- The fraudsters acted as representatives of the organizations, created a forged fixed deposit receipt and handed over the same to the beneficiaries. Subsequently, the original deposit receipt was utilized by the fraudsters for availing loan against the deposit without the knowledge of the organization.
- While disbursing the loan amount, letters of request for RTGS transfer to parties or cheques duly signed by the authorized signatories were received from the Organizations/Corporates.

Loopholes/lapses:

- The private persons with assistance of other unknown persons falsely represented themselves to the Government Organizations/Corporates as representative of bank and to the bank as financial advisors of the Organization/Corporates.
- While collecting the KYC documents from the Organizations/ Corporates, presumably retained the original documents with them and generated fake documents of KYC, signatures, stamps, letter heads etc, purported to have been prepared by concerned Organizations/ Corporates and handed over to the banks.
- After collecting the original TDR receipts from the banks, private persons presumably retained them and handed over photocopies to the concerned Organizations/ Corporates.
- To avail a loan against original TDR retained by them, they presumably created fabricated documents on the basis of the documents submitted to the banks earlier. Original TDR duly discharged by the authorized signatories accompanied the loan applications.
- The branch managers without assessing the genuineness of these apparently looking

genuine documents acted on the mandate and recommended/sanctioned loan against TDRs and also remitted the money to various accounts in several banks as per the mandate.

- RTGS for opening TDR accounts were sent by the Organizations/Corporates to the banks but they declined having ever applied for loan/ overdraft availed. It also transpired that the private persons presented themselves as representatives of bank and collected various papers/documents from Organizations/Corporates.
- It is also suspected that current accounts were also opened at the branches in the name of Organizations/Corporates where funds by way of RTGS were received and disbursed by RTGS transfer to various other banks.

Systemic Improvement:

- Proper due diligence and precautions should be taken by the branches while dealing with the bulk deposit accounts opened in the names of organizations, corporates and public sector undertaking etc. The bank's systems and procedures should not be diluted.
- Branches, on receipt of bulk term deposits of Rs.1.00 crore and above should report the complete details of such deposits to Treasury Management Department. In the said report branch should also confirm that KYC guidelines have been complied with.
- Controller should critically go into on the quality of business booked by branches and sudden spurt, if any, observed in business growth should be thoroughly investigated.
- Branch manager should enquire about customers' requirement and brief them about the details of Loan/overdraft schemes such as rate of interest, maximum eligible amount of loan, requirement of signatures, KYC documents etc.
- For limited companies, trusts, associations, co-operative, it should be ascertained whether the company /director/trustees/ office bearers having borrowing powers and the extent of these powers. The copy of the necessary resolution passed by the borrowing organization for borrowing against the fixed deposit receipts should be obtained.
- Bank should not depend on private person for accepting the bulk deposits. Officers to verify details of Organization/Corporate and verify the signature of all the joint holders as per bank record.
- Bank officer should obtain requisite documents executed in person from the applicant and enter the proposal in loan sanction register along with original TDR.

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Fraud Committed by Staff member (Demand loan)

The fraud perpetrated by a staff member of PSU bank by way of sanctioning of unauthorized Demand loans, unauthorized entries in Demand loan accounts, Saving Bank accounts, funds transfer accounts etc.

Nine fraudulent Demand loans aggregating to Rs.252.34 crores had been sanctioned by branch manager against the deposits of a Development Authority without the request/authorization from the depositor. No documents were available. The transactions had been carried out by then senior manager of the branch.

Modus operandi:

- Fraudulent demand loans were sanctioned purportedly against deposits of the Development Authority. It was reported that nine fraudulent Demand Loans aggregating to Rs.252.34 crores had been sanctioned against the deposits of the Development Authority without request/ authorization from the depositor.
- The loans had been sanctioned in the name of the Development Authority and loan proceeds were credited to various accounts of different persons. While few credits had been affected directly from demand loan, few credits had been routed through three fictitious Saving Bank accounts of the Development Authority.
- No documents were available in the branch. The entire accounts stood closed. The transactions had been carried out by then Senior Manager of the branch. Indiscriminate credits and debits without any authorization, outward RTGS remittances, opening and closure of loan accounts etc had been indulged by then Senior Manager of the branch and other officials had passed the transactions in a routine manner.
- The said three saving bank accounts were used for parking the proceeds of fraudulent demand loans raised by then Senior Manager of the branch and also for transmission of money to various accounts for accommodation purpose. All the transactions in those three saving bank accounts were fraudulent.
- The Development Authority had confirmed that no request was made by them for opening the said three saving bank accounts. Transactions circumventing the provisions of Anti-money laundering approved by then Senior Manager were noticed.

Loopholes/Lapses:

- Fictitious demand Loans were allowed to be opened by the branch manager and the proceeds were misutilised to accommodate few constituents.
- Anti-Money laundering provisions had not been adhered to. Reporting was not done. Irregular transactions pertaining to interest charged /paid were passed.
- Three fictitious saving bank accounts in the name of the Development Authority were opened and fraudulent transactions were put through by the staff member.
- Branch officials failed to alert controlling office regarding fictitious demand loans. Vouchers were posted/ approved without proper verification of its regularity and genuineness of underlying transactions.
- Outstation cheques were debited to the branch funds transfer account. Fictitious cheque numbers were entered and passed. Transactions disproportionate to the known sources of income and large value transactions were permitted.

- Transactions disproportionate to their known source of income were allowed.

Systemic Improvement:

- Controlling offices should critically go into the quality of business booked by the branch and sudden spurt, if any observed in business growth should be thoroughly investigated.
- Monitoring of systems and MIS generation has to be strengthened. Housekeeping and internal control of banks has to be strengthened.
- Controlling Offices have to receive the details of all the loans sanctioned under power of the branch along with related account wise Appraisal notes through credit appraisal form every month. The return should be critically scrutinized and adverse conditions, if any, should be taken up with the concerned branch for rectification without delay.
- Due diligence for sanctioning of loans and observations of Bank's system and procedures should not be diluted.

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Fraud Committed by Staff member : (Letter of Comfort)

The fraud was perpetrated by staff member of a bank in buyers' credit transactions. The matter came to light when the main branch of bank received intimation from overseas branches of the bank that payment towards buyers' credit was not received by them.

When branch records were verified, it came to light that no such buyers' credit had been raised from those banks. It was further observed that several other buyers' credit had also been raised from those banks through fake Letters of Comfort (LOC) via SWIFT which became due for payment from 01.07.2016 onwards. It was reported that the branch had issued

20 buyers credit for Rs.429.33 crore due for payments upto January 2017.

Modus Operandi:

- The Letters of Comfort were fraudulently conveyed through SWIFT messages which emanated from the main branch of bank where there was involvement of staff member.
- On 25.07.2016, the main branch received a message from overseas branches of PSU bank that payments towards buyers' credit were not received by them. On verification, it was observed that no such buyers' credit had been raised from these banks.
- It was reported that the branch had issued 20 buyers' Credit for Rs.429.33 crore due for payments upto January 2017.
- On verification, it was found that there were no documents and sanction letters of credit facilities for such transactions. Further, the transactions were not routed through the bank's Nostro Account as per prescribed guidelines. The SWIFT messages sent were reportedly fraudulent.

Loopholes/ Lapses:

- SWIFT transactions were not linked to the Core Banking Solution (CBS) of the bank, which contain transaction histories and other data of the customers.
- The transmission of the messages is usually a three layer process that did not take place either at the branch or its office.
- SWIFT transactions were therefore automatically recorded and were not seen by officials of the controlling offices.
- In SWIFT system one bank official is designated as a maker, another verifier and third as authorizer. All have different logins and passwords and work independently of each other. But in this case functions were performed by a single person.

Systemic Improvement:

- CBS-Finacle should be integrated with SWIFT (STP-Straight Through Processing) for all payment messages.
- Each and every login into SWIFT system would be only through biometric authentication thereby virtually preventing any unauthorized login through password compromise.
- SMS alert feature should be introduced wherein all SWIFT users will get an alert message in their mobile phones for every login into the SWIFT with their roll number and password including failed login attempt.
- The access to SWIFT connect should be restricted based on IP address-only 2 PCs per branch should be permitted.

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