



Cases in Bank Fraud (Unit 9 – Module 1) Part 1

DFA

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Query Responses – 25.02.2022

- ◆ Achala Mohan
- ◆ Sir, if management say that they are not responsible as they have appointed competent IT chief and Internal Audit committee with the responsibility. Accordingly, if they that they should sign the letter then, what is the option we have
- ◆ Management has to sign the MR , as it is their Overall responsibility to institute robust ICS. If not signed, matter to be reported to appointing authority & MR para to be included in Audit Report
- ◆ Sir, can you please explain Professional skepticism please?
- ◆ Skepticism = alertness & not accepting info / documents at face value
- ◆ If a person was engaged by one of the group companies for establishing a management system and say after 2 years if the same person is appointed as forensic auditor. Will it be viewed as conflict of interest?
- ◆ Usually , cooling period of 3 to 5 years recommended , else = Self-Review Threat , also facts of particular case to be considered
- ◆ RAM SWAROOP YADAV
- ◆ sir whether indicators of frauds are same as red flags
- ◆ Red flags = qualitative , Indicators = sometimes , quantitative & more powerful symptoms = eg – direct RPT at above ALP but purchase of sub-standard quality OR , opening shell companies in tax havens & routing bank loan proceeds

Responses

- ◆ Arunava Chakraborty
- ◆ FAIS - does the auditor consider multiple hypothesis and have a process to examine each or they one have a single hypothesis?
- ◆ There may be multiple hypothesis & process are there to examine each of them
- ◆ Vinaykant Pareek - provide link of FAIS sandards
- ◆ **FAIS = Source**
- ◆ https://icai.org/new_post.html?post_id=17013
- ◆ sivaraman viswanathan
- ◆ stock exchanges comes under regulatory authority? doubt on it
- ◆ SEBI laws are applicable
- ◆ Achala Mohan
- ◆ Can 2 teams be appointed as forensic auditors for one organization with same scope or the scope has to be different sir?
- ◆ Usually single forensic auditor appointed, parallel investigation may be on from CBI / ED/ SFIO / Cyber-police etc . Cases of multiple forensic auditors working parallely with same / different scope is rare & not seen
- ◆ Aniketh Deb
- ◆ how to establish - significant influence?
- ◆ KMP, Roles & responsibility, shareholding, RPT etc parameters

Responses

- ◆ Aniketh Deb
- ◆ whatsapp communication can be intercepted?
- ◆ Technically, yes , powers vested in Govt via IT Rules 2021
- ◆ Achala Mohan
- ◆ Sir, the objective FAIS 530 states prior to loan approval
- ◆ FAIS 530 covers 3 of the possible situations :
 - ❖ To identify and report any shortcomings by the loan sanctioning authorities in proper due diligence prior to loan approval (Eg KFA)
 - ❖ To identify and report any defaults by the borrower of loan agreement terms and covenants
 - ❖ To identify and report the true utilization of the borrowed funds, as per the stipulated terms and conditions

Major scams , control failures , frauds – ‘VUCA’ business era

Boardroom failures: Satyam , Enron , Xerox, Adelphia, Reebok, Toshiba

Securities market scams – 1992, 1999 , NSEL / FMC (2014)

Governance fiascoes – 2G, CWG, Coalgate, Vyapam

Money laundering / illegal remittance

Auditor conflicts of interest: Satyam, Enron, Chit funds - Saradha

Banking practices & Valuation: Lehman Brothers, Kingfisher case

Executive compensation & insider trading : Rajat Gupta

Panama Papers – FATCA - Info sharing of offshore a/c holders

PNB - NiMo, Rotomac, ICICI Bank-Videocon

Shell Companies : 6 lakh out of 15 lakh registered companies file Return

2019-20 :559 agents laundered Rs.3900 Cr, 2.26 lakh **Shell companies**
deregistered, Impact : 3.1 lakh directors, **Freezing of Bank Accounts**,

Bank frauds, NPA & Defaults

◆ ***A. Deposit Account Frauds:***

- ◆ ¶¶ Value inflation of cheques deposited.
- ◆ ¶¶ Changing the nature of the cheques (crossed to bearer).
- ◆ ¶¶ Operating a dormant account fraudulently

◆ ***B. Purchased Bill Frauds:***

- ◆ ¶¶ Discount on stolen or fake Railways Receipts and motor receipts along with other necessary bills.
- ◆ ¶¶ Fake/forged bills for valueless goods are discounted.

◆ ***C. Hypothecation Frauds:***

- ◆ ¶¶ Inflation of stock statements.
- ◆ ¶¶ Hypothecating same goods in the favour of different banks

- ◆ ***D. Loan Frauds:***
- ◆ ¶¶ Two different person taking loans on the same item or product.
- ◆ ¶¶ Loan taken for one purpose but used for a different purpose
i.e., loan taken for agriculture but used for personal purposes.
- ◆ ***E. Cheque Frauds:***
- ◆ ¶¶ Cheques are stolen, filled and signed spuriously and
encashed.
- ◆ ¶¶ The signed cheques are stolen & encashed with alterations, if
needed
- ◆ ¶¶ Cheques issued by organisations for employees are duplicated

Developments – Banking & follow up of fraud cases

- ◆ **July 27, 2018 : PMLA Court summoned NiMO & MC on ED's petition – FEO Law , on Sep 25 & 26, 2018 (confiscate & sell of assets Rs 3500 cr), Mallya to appear – Aug 27**
- ◆ **RCN against NiMo, FEO Bill invoked against Mallya & NiMo,**
- ◆ **July 19, 2018 : LS passed Fugitive Economic Offenders Bill 2018**
- ◆ ***Seeks to declare a person as FEO if arrest warrant issued , default amount > Rs 1 billion, if offender refuses to return to India***
- ◆ ***RS passed Prevention of Corruption (Amendment) Bill 2018***
- ◆ ***Introduced in LS : 'Banning of unregulated Deposit Schemes Bill, 2018'***
- ◆ **July 23, 2018 : More than 20 Banks signed Inter-Credit Agreement (ICA) : for borrowers in consortium lending = > Rs 50 Cr , (SBI, PNB, LIC etc)**
- ◆ **RBI : Rs 3.10 lakh cr total loans in Rs 50-500 cr category- banker to intimate consortium leader within 30 days of default – structure Resolution plan , approval by 66 % of lenders – if overdue for 180 days – refer to IBC**
- ◆ **Fearing probe, best bankers avoiding Bank's Credit department**
- ◆ **Banks expect turnaround from recoveries from IBC (CIRP) process**

Background : UBI– Q3, 2013-14

- ◆ Due to fresh slippage of Rs. 3172 crore Gross NPA increased to Rs. 8546 cr from Rs. 2902 crore
- ◆ □ Gross NPA ratio 10.82% , 7.52% in last quarter.
- ◆ □ Net loss - Rs 1238 crore, Rs 42.2 crore profit (QoQ)
- ◆ **CBS Failure ?**

Lower trend in

- ◆ Business per employee , GP / employee, Business per branch , GP / Branch;

Forensic audit of UBI

RBI ordered forensic audit of United Bank of India (UBI).

- Deloitte and RBI examined if there are any hidden NPAs in the bank and if proper systems are in place to identify them.
- They were also see if there is any manual intervention by the employees in the process of NPA recognition.
- The RBI team also examined large value loan accounts of the bank
- The bank which has the highest bad loans among state-run lenders was downgraded by ICRA, a unit of Moody's Services.
- "The automated system that detects NPAs was found switched off", said a person familiar with the findings. Whether it was intentional or by mistake remains a big question".

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KFA – crash

- ◆ Vijay Mallya, had offered banks Rs 6,600 crore but nobody took that offer
- ◆ Court issued non-bailable warrant , UK Courts : ‘prima facie evidence of dishonesty’
- ◆ Jan 18 2018 : arrest warrant issued against 18 accused in KFA
- ◆ Delhi court orders attachment of Vijay Mallya's properties in PMLA case
- ◆ Mallya expresses concern on quality of Indian jails - Arthur Road Prison
- ◆ Mallya arrested twice in UK but secured bail in a matter of few hours.
- ◆ Special court summoned Vijay Mallya to appear on August 27 , 2018 on ED's plea seeking action under Fugitive economic Offenders Ordinance (FEOO) – intention to return

RBI – Willful defaulter definition, fresh NCLT referrals

- ◆ Defaults done despite repayment capacity
- ◆ Money diverted by promoter, Siphoned out, not available
- ◆ Borrowers selling fixed assets kept as collateral and cheating banks
- ◆ Lenders prepared **Evaluation Matrix** with qualitative and quantitative parameters to shortlist bidders for companies under insolvency.
- ◆ **Quantitative parameters** - upfront cash
- ◆ **Qualitative parameters** - financial track record of the bidders and their ability to turnaround stressed assets.

WINSOME Group Fraud – 2013

- **PNB exposure Rs 1,800 cr** : Of the Rs 6,800 crore credit extended by consortium led by Standard Chartered Bank
- Banks issued SBLC, or guarantees in favour of parties which supplied gold to Winsome Group. **SBLC** – secondary payment mode / contingent on non-performance of party (duration = upto 1 year)
- Winsome claimed that ***they were unable to repay*** as their clients in the Middle East suffering huge losses. SBLC devolved.

- ◆ On 13th June, 2017 : promoters of a mining company Abhijeet Group were arrested for being defaulters in loans payment of over ₹.11,000-15,000 crore from 20 banks and FI s through 132 shell companies of the group.
- ◆ Abhijeet group created vehicle company Jas Infrastructure to provide contract for erection, procurement and construction of a power plant at Bihar to its group company Abhijeet Projects and misusing loan amounts worth Rs 790 Crore from Canara Bank & Vijaya Bank.
- ◆ **॥॥ Ganesh Jewellery**
- ◆ On 8th May, 2017, Nilesh Parekh, promoter of the Kolkata-based Shree Ganesh Jewellery House arrested in connection with loss of ₹.2,223 crore to 25 banks led by SBI.

PNB – fraud :

Rs 14,000 Crore (Feb , 2018) & counting ?

- ◆ CBI report (March 14) – PNB filed for additional Rs 942 Cr credit exposure (NM-MC owned firms)
- ◆ Diamond firms approach PNB for opening LC for import of rough stones.
- ◆ Fake LoUs were Issued – no credit limit – no cash margin – no entry in CBS
1,212 fake LoUs issued in favour of NiMO & MC firms- SWIFT message
- ◆ Transactions are equivalent of 8 times PNB's 2017 net income of about Rs 13.2 billion
- ◆ Alleged : Some PNB employees misused the SWIFT network
- ◆ PNB has alleged “clear criminal connivance” of NiMO & MC
 - GM Credit of PNB in CBI custody
 - Audit & Consulting Firm BDO appointed to carry out forensic audit.
 - PNB new CRO appointed, CMD, CVO questioned by CBI
 - NSE fined Gitanjali for non-filing of results for Dec 2017 quarter
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ICICI Bank & Videocon Case – April 2018

- ◆ Media reports suggested ICICI Bank had granted a loan worth Rs 3,250 crore to Videocon. Conflict of Interest case for ICICI Bank CMD
- ◆ *Quid pro quo* ? Deepak Kochhar, Chanda Kochhar's husband, is an indirect beneficiary
- ◆ SEBI, CBI & SEC review : ICICI – Videocon case
- ◆ ICICI Bank, & other banks may also undergo scrutiny
- ◆ Letter sent to PM, CVC, FM, SEBI, CBI , MCA
- ◆ RBI imposed a penalty of Rs 58.9 crore on ICICI Bank for violating RBI guidelines governing treasury operations
- ◆ Chanda Kochhar's CTC (2017) = Rs 5.54 Cr – Median = $1/112$ = Rs 4.95 LPA , Impact on market cap in banking sector
- ◆ ICICI Bank board sent CEO Chanda Kochhar on forced leave on 19th June till completion of independent investigation into charges of conflict of interest.
- ◆ ICICI Bank CEO faced Rs 25 Cr penalty by SEBI –removal from office ,
- ◆ Fresh allegation :ICICI bank favoured Ruias of Essar for allegedly round-tripping investments into NuPower