

# Scams in Indian Banking System: an Analytical Study

Nisha<sup>1</sup>, Dr. Seema Dahiya<sup>2</sup>

<sup>1</sup>Research Scholar, B.P.S. Women University, Khanpur Kalan (Sonipat)

<sup>2</sup>Assistant Professor, Department of Laws, B.P.S. Women University, Khanpur Kalan (Sonipat)

**Abstract:** In India, the banking sector has been operating since the early stage of civilization. But the modern banking system which includes giving money loans, large amount transactions from mid 18th century. It is beneficial for economic growth if transactions are done honestly and in a beneficent manner. Due to failure, banks are facing problems in recovery of loans and fluctuating non-payment assets since last two decades. If the bank money is locked with some defaulters, then it prevents the money from being used by thousands of other who could put it to productive use. Therefore, recovery of loans becomes important for the banking sector. The person may use malpractices to obtain money which will be the easiest way to commit a fraud. The frauds have been increased in Indian banks with the liberalization of the economy which started in 1990. And at that time no effective steps were taken to prevent frauds. As time passed there was a tremendous increase in the frauds in Indian banks. Harshad Mehta and Ketan Parekh were the well known people who were indulged in banking frauds. They represented how a middle class person can think to get rich in short term by playing around with the existing rigid systems. Since 2000, there had been approximately 2085 frauds reported to the Reserve Bank of India.

**Keyword:** Indian Banking system, Frauds and Scams, NPA (Non-Performing Assets), legislation

## I. INTRODUCTION

In the banking sector, the non-performing assets (NPA) by lenders create threats to the existence of the banks. The banking system of any country comprises of the small savings of the people. When a large number of people deposit their money into banks, it becomes the responsibility of the bank. Commercial bank lends this money to traders, institutions and individuals in turns to earn profits in the form of interest.<sup>1</sup> Banking fraud has been continuing since 1992, when the financial fraud started with Harshad Mehta for non-professional safety management in banks.

From cricket event organizers, liquor barons to diamond merchandisers all have been accused of multi crore scams and the tendency of suddenly leaving the shores of India. The data assumes significance as banks are grappling with high profile fraud cases involving absconding billionaire Nirav Modi and liquor baron Vijay Mallya among other.<sup>2</sup> The famous cases which shook the entire banking system includes PNB bank scam, Airlines Kingfishers scam, Allahabad bank scam, Rotomac Pen scam, Kanishka Gold Pvt. Bank scam, RP info system bank scam, Simbhaoli Sugar Mills bank scam, Harshad Mehta Scam, Ketan Parekh Scam, Indian Bank Scam (Gopala Krishnan case), Winsome Diamonds scam and PMC Bank Scam. Recently, Sterling Biotech bank fraud is highlighted by the Enforcement Directorate. The Enforcement Directorate agency said that it has issued an order of attachment of assets worth Rs.9778 Crore.<sup>3</sup> On June 27, 2017, the ED attached

several properties of Sterling Biotech promoters. The probe agency said that the Sterling group promoters not only siphoned off these loan funds to finance their Nigerian oil business but also used the money for their personal use. Recently RBI founded Yes Bank's failures to raise new funding to cover its NPAs, inaccurate statements of confidence in its ability to receive new funding.

### Definition of Fraud

**Oxford Dictionary** describes 'fraud' as criminal deception, use of false representations to gain unjust advantage, by dishonest artifice or trick.

According to Ghosh committee report in 1990, Bank fraud may be committed by the employees of the bank or by the employees of the bank in collusion with the outsiders and also by outsiders. But now, there is no limit and anyone who is smart enough to outwit the bankers and the bank can indulge in a bank fraud.

## II. STUDY OF SOME BANK FRAUDS AND SCAMS

### The Pay-Off Scandal / Security Scam (1993)

In 1990, Harshad Mehta had risen to prominence in the stock market. He had been buying stock heavily. The shares which attracted his attention were: Apollo Tyres, Reliance, Tata Iron and Steel Company, BPL, Videocon and Associated Cement Co. (ACC). He manipulated the stock market rate by lobbying and the share prices rose tremendously. Due to which many people lost their life saving.<sup>4</sup> His illicit methods were exposed on 23 April, 1992, when Sucheta Dalal wrote an article in the

<sup>3</sup> <https://m.businessstoday.in>

<sup>4</sup> <http://www.indianmirror.com>

Times of India detailing about the scam.<sup>5</sup> He and his brother Ashwin and Sudhir, who masterminded and executed this scam together were arrested and banished by the CBI on Nov. 9, 1992 from the stock market with investors holding him responsible for causing a loss more than 2.8 million shares of about 90 companies.

#### **The Stock Scam/UTI Scam (2001)**

A Joint parliamentary committee (JPC) investigation ensued which found Ketan Parekh involved in circular trading throughout the time period and with a variety of companies, including Global Trust Bank and Madhavpura Mercantile Co-operative Bank.<sup>6</sup> A thirty member JPC team investigated the 2001 Indian stock market scam who found him to have played a major role in artificially rigging the prices of a set of 10 Indian companies, from 1995 up to 2001.<sup>7</sup>

In March 2014, he was convicted by special CBI court in Mumbai for cheating and sent to Jail with two others for imprisonment of one year as a result of swindling transactions of Rs. 48 billion from a unit of Canara Bank in 1992. Therefore he was debarred from stock trading in the Indian stock exchanges till 2017.

#### **Punjab National Bank Fraud Scam (2011)**

This case related to alleged fraudulent letter of undertaking worth Rs. 11600 crores that took place at its branch in Brady House, Mumbai, making Punjab National Bank potentially liable for the amount. The fraudulent transactions are allegedly linked to designer and jeweler Nirav Modi, against whom a complaint has been filed by the CBI. The transactions were first noticed by a new employer in the bank.

The bank said that two of its employees at the branch were involved in the scam, when the Bank's core banking system was bypassed by using the international financial communication system, SWIFT, to rise to overseas branches of other Indian Banks and Union Bank of India. Three jewelers-Gitanjali Gems Ltd. and its Subsidiaries Gill and Nakshastra are also under the scanner of investigation agencies.

On 20 February 2018, The CBI official arrested Rajesh Jindal, a general manager – rank officer of the Punjab National Bank posted at the bank's head office at New Delhi. He was the head of the Brady House branch of the Mumbai bank during 2009-11. Issuance of LOUs to Nirav Modi group firms without sanctioned limits allegedly started during his tenure.

Same day, the RBI broke its silence on this scam saying that it had warned banks at least three times since August 2016 of possible misuse of the SWIFT infrastructure. The Central bank also announced the appointment of chartered accountant YH Malagam, who was part of the RBI's board for 17 years, to

head a panel that will look into the causes of fraud at lenders and the reason for their failure in identifying defaulters.<sup>8</sup>

Enforcement and investigating agencies such as CBI, ED, tax department etc. in the meantime have upped the ante to get to the bottom of the scam. News agency IANS reported that the Enforcement Directorate is probing 120 shell companies allegedly linked to diamond trader Nirav Modi and Gitanjali Group. The IT department raided 20 premises linked to Gitanjali gems promoter Mehul Choksi and associated firms in connection with a tax evasion case.

The CBI arrested five senior executives in connection with multi-crore PNB Fraud including Vipul Ambani, the head of finance of Nirav Modi's Firestar Diamond, who is a relative of well-known Industrialist brothers Mukesh and Anil Ambani. Kavita Mankikar (Executive assistant and authorized signatory of three accused firms), Arjun Patil (senior executive, Firestar group), Kapil Khandelwal (CFO, Nakshastra and Gitanjali group) and Niten Shahi (Manager, Gitanjali).

#### **Allahabad Bank Scam**

To do this scam in the Allahabad bank; the SWIFT (Society for Worldwide Interbank Financial Telecommunications) technique is misused by the internal employees of the said bank. Because Swift technique is used by the financial institutions for transmit information and instructions through a standardized system of codes. But the internal banking system of the bank was not attached to the SWIFT that is why the transactions were not mentioned in the accounting book of the bank and then there was no transaction record found between the PNB and Nirav Modi. The Kolkata-based Allahabad Bank has said it has an exposure of Rs. 2365 crore in the PNB Fraud case.

#### **Kanishka Gold Pvt. Company bank fraud scam**

The CBI has registered a case against Chennai-based Company named Kanishka Gold Pvt. which allegedly misappropriated loans worth Rs. 824 crore and the total outstanding amount, including interest on it which is Rs. 1000 crore. The Enforcement Directorate started investigating the fraud but the director of the company Bhupendra Kumar Jain and his wife Neeta Jain fled.<sup>9</sup> Recently, the Fraud scam investigation is in progress.

#### **Simbhaoli Sugar Mills Bank Scam**

The CBI has booked another bank fraud against one of the India's biggest sugar mill, Simbhaoli Sugar Mill Limited amounting to worth Rs. 200 crore. There are 10 people who also have been accused including chairman of this mill.

#### **Winsome Diamonds and Jewellery Scam**

<sup>5</sup> From thequint.com

<sup>6</sup> [www.livemint.com](http://www.livemint.com), 8 February, 2010. "SEBI settles HFCL share price rigging case with consent order".

<sup>7</sup> JPC Report on the 2001 Indian Stock Market Scam tabled in the 13<sup>th</sup> Lok Sabha, New Delhi: Government of India.

Updated: Available at

[https://wikivividly.com/wiki/ketan\\_parekh\\_scam](https://wikivividly.com/wiki/ketan_parekh_scam)

<sup>8</sup> Available at <https://m.timesofindia.com/> updated 21 February, 2018.

<sup>9</sup> Ibid 13

The CBI agency has registered a case against the then director of the company Jatin Mehta and Jordanian Hathyam Salman Ali Obaidah for allegedly cheating Bank of India by diverting the bank's funds to the tune of Rs. 82.55 crore. The banks declared account of winsome Diamonds and Jewellery as non performing asset on June 30, 2013 and declared it fraud on Dec.3, 2015. Mehta used funds from the bank for setting up family business in the name of Gemesis in Singapore. On April, 2017, the CBI registered six cases against them for cheating three government banks tune of Rs. 1,530 Crore.

#### **Indian Bank Fraud (GopalaKrishnan)**

The CBI Court in Chennai convicted former chairman and managing director of Indian Bank M Gopalakrishnan and 11 other individuals on allegations that they had sanctioned loans without proper verification and assessment and without obtaining proper collateral securities from a company named M/S Enkay Foods Pvt. Ltd. and had caused wrongful loss of Rs. 29.87 Crore to bank. The scam was exposed after Subramanian Swami approached the court and alleged that the bank fell into crisis after bad loans were given under the direction of Gopalakrishnan.

#### **PMC Bank Scam**

The higher management of the bank has sanctioned huge loan to the Housing Development and Infrastructure Ltd. and its associated companies and it had caused loss of Rs. 4355 crore. When this case comes to highlight publicly, then the customers of the bank moved to the PMC bank to withdraw their deposited money but the banks were refused to give their deposited money.<sup>10</sup> As a result, Raghuram Rajan has said that it is a matter of systematic failure. The investigating agencies blamed the banks and said bankers are highlighting the fraud slowly after the fraud has actually taken place, because they know that once they call a transaction as fraud, they will be subject to harassment by the investigating agencies without substantial progress in catching the crooks.

### **III. LEGISLATION TO CURB THE BANKING SCAMS**

Onward 1991, there was need for the legal framework on securitization. That's why various committees recommended a law on securitization and enforcement. It is very difficult for the banks to approach civil court asking for a decree and getting that decree executed. With the intention of enabling the banks to reduce their NPAs through faster recovery of dues, 'The Recovery of Debts Due to Banks and Financial Institutions Act, 1993' was enacted. Despite constituting 'Debt Recovery Tribunal(DRT)' under the RDDBI Act, 1993 and providing special procedure to be followed before the Tribunal, Banks could not reduce their NPAs as expected and it has led the legislature to enact ' The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002'. Insolvency and Bankruptcy (Amendment) Code, 2019 is also provided for a fast way to recover bank debts. In spite of the lots of legislations and

efforts, the incidences of reporting of economic offences have been on a steep rise. One may possibly attribute the reasons for such rise to the growing proximity of rich and wealthy with the powerful Center, best described as crony capitalism.

The commissioning of economic offences and fleeing to a foreign territory not only undermines the Rule of law in India but also causes a strain on the overall economy.

Now, it is need of the hour that the central government needs to make some strict policies to prevent such banking frauds in the country. It is necessary to restrict the political intervention in the functioning of the Indian Banks.

### **IV. SUGGESTIONS TO CONTROL FRAUDS IN BANKING SECTOR**

To prevent the menace of frauds occurring in the banking system, the management of bank must be careful and vigilant to prevent occurrence of fraud in banks. They should use screening system upon customers, if they found any doubtful personality and troublesome account. This should be informed at the initial stage. There should be rotation of employee's counter, if they remain at one seat for number of years they knows everything about the system and it leads to increase in the chances of misuse of seat. A person who has high skill or professional knowledge and ability to judge must be appointed as an official who conducts surprise inspections in the branches. If there is any customer complaint about any fraudulent activity, immediate action should be taken to prevent the commission of fraud. The customers must be aware of the frauds and scams to avoid frauds. People must be aware of the safety measures needed to be taken in any such case. This awareness could be incorporated through awareness programs or campaigns through private and government agencies.

<sup>10</sup> M.jagranjosh.com/general-knowledge