Fraud Cases in Public Sector Banks

Why in News

Public Sector Banks (PSBs) have been **reviewing loan accounts** and are expected to report more fraud cases in accounts which have earlier been put under their **Early Warning Signals** (EWS) system.

- The **Reserve Bank of India** (RBI) developed the EWS framework as it noticed a delay in the detection and reporting of banking frauds.
- The **objective of the EWS framework** is to prevent and detect these offences, to provide timely reporting to regulators and to initiate staff accountability proceedings thereby ensuring that the operations and risk-taking ability of the banks is not impacted.

Key Points

- **Data Analysis:**
  - The **total cases of frauds** (involving Rs. 1 lakh and above) reported by banks and financial institutions **shot up by 28% by volume** and **159% by value during 2019-20** despite the Reserve Bank of India (RBI) tightening the supervision and vigilance.
  - While there were 6,799 frauds involving Rs. 71,543 crore as of March 2019, the number of frauds jumped to 8,707 involving Rs.1,85,644 crore, says the **RBI's Annual Report 2020.**
  - **PSBs topped the fraud table** with 4,413 cases involving Rs. 1,48,400 crore.
  - **Private banks** reported 3,066 frauds involving Rs. 34,211 crore.

- **Current Scenario:**
  - Banks are **going through their accounts which were put on alert earlier.** They will **report fraud** wherever such instances are found in case of large accounts, and **make 100% provision against them.**

    These are being reviewed thoroughly to **ensure that banks have adequately provisioned balance sheets.**
  - The RBI also indicated that the **frauds registered during 2019-20 actually occurred** in the **loans sanctioned during 2010-2014.**
    - The **average lag between the date of occurrence of frauds and their detection** by banks and financial institutions was 24 months during 2019-20.
    - In **large frauds,** of Rs. 100 crore and above, the **average lag was 63 months.**
  - After **forensic audit and investigation** into these accounts, **diversions and other issues** were found.

    RBI defines **diversion of funds** as utilisation of short-term working capital funds for long-term purposes not in conformity with the terms of sanction; deploying borrowed funds for purposes/activities other than those for which the loan was sanctioned; and transferring borrowed funds to subsidiaries/group companies or other corporates by whatever modalities.
- **Reasons:**
  - Weak implementation of EWS by banks.
  - Non-detection of EWS during internal audits.
    - **Internal audits** evaluate a **company's internal controls, including its corporate governance and accounting processes.**
    - They ensure compliance with laws and regulations, help maintain accurate and timely financial reporting and data collection.
  - Non-cooperation of borrowers during forensic audits.

    Forensic audit is an **examination and evaluation of a firm's or individual's financial records** to derive evidence that can be used in a court of law or legal proceeding.
  - Inconclusive audit reports.
  - Lack of decision making in Joint Lenders' meetings account.

- **Overcoming Measures:**
  - The EWS mechanism is getting **revamped alongside the strengthening of the concurrent audit function,** with **timely and conclusive forensic audits** of borrower accounts under scrutiny.
  - RBI is engaged in **interlinking various databases and information systems** to improve fraud monitoring and detection.
  - Online reporting of frauds by the **Non-Banking Financial Companies** (NBFC) and the **Central Fraud Registry** (CFR) portal of **Scheduled Commercial Banks** (SCBs) augmented with new features, are **likely to be operational by January 2021.**

    RBI has put in place CFR, which is a **searchable database to help banks detect instances of fraud** by borrowers early on.

Source: IE