

An Empirical Study of Technological Frauds in Banks

Dr. Jaimin Patel

Assistant Professor, Faculty of Commerce, GLS University, Ahmedabad, Gujarat.

Email: jkpatel2309@gmail.com

Abstract: *The Indian banking sector has experienced considerable growth and changes since liberalisation of economy in 1991. Though the banking industry is generally well regulated and supervised, the sector suffers from its own set of challenges when it comes to ethical practices, financial distress and corporate governance. Banks are the engines that drive the operations in the financial sector, money markets and growth of an economy. With the rapidly growing banking industry in India, frauds in banks are also increasing very fast, and fraudsters have started using innovative methods.*

Keywords: *Technology, bank, financial distress, Fraud.*

1. INTRODUCTION:

The role of banks in economic development is to remove the deficiency of capital by stimulating savings and investment. A sound banking system mobilizes the small and scattered savings of the community, and makes them available for investment in productive enterprises. In any plan of economic development, capital occupies a position of strategic importance. No economic development of sizable magnitude is possible unless there is an adequate degree of capital formation. A very important characteristic of an under developed economy is deficiency of capital which is the result of insufficient savings made by the community.

In recent years, instances of financial fraud have regularly been reported in India. Although banking frauds in India have often been treated as cost of doing business, post liberalisation the frequency, complexity and cost of banking frauds have increased manifold resulting in a very serious cause of concern for regulators, such as the Reserve Bank of India (RBI).

2. WHAT IS FRAUD?

RBI had not defined the term “fraud” in its guidelines on Frauds. A definition of fraud was, however, suggested in the context of electronic banking in the Report of RBI Working Group on Information Security, Electronic Banking, Technology Risk Management and Cyber Frauds, which reads as under:

“A deliberate act of omission or commission by any person, carried out in the course of a banking transaction or in the books of accounts maintained manually or under computer system in banks, resulting into wrongful gain to any person for a temporary period or otherwise, with or without any monetary loss to the bank”.

The Institute of Internal Auditors „International Professional Practices Framework“ (2009) defines fraud as, “Any illegal act characterized by deceit, concealment, or violation of trust. Frauds are perpetuated by parties to obtain money, property or services; to avoid payment, or loss of services; or to secure personal or business advantage.” It should be noted that frauds generally impacts a bank by causing financial, operational or psychological loss.

3. TYPE OF FRAUDS:

(1) The bank frauds are primarily deposit related, advances related and services related. Of these, the deposit related frauds which used to be big in number though not in size, have been on the wane, thanks to the improvements in cheque and payment processing, usage of technology and tightening the provisions of the Negotiable Instruments Act. The advances related frauds continue to be the major concern for banks, especially because of their size and far reaching implications to their financial soundness and integrity. A special variety of frauds, which are increasing in number and in terms of speed, are the cyber frauds. Yet another special type relates to trade or documentary credit related, special because of cross border implications.

(2) When we discuss about bank frauds, we will not discuss about bank frauds committed by third parties which can suitably be classified as thefts. These types include cyber frauds committed by tricksters, or techsters. For our discussions, we will include bank frauds committed by some connected parties like the depositors, the borrowers, the users of bank services or by their own staff, their outsourced agencies, their vendors, their agents like assayers, valuers, auditors, etc.

4. LITERATURE REVIEW:

- (1) Anju R, Bansal I (2017), this research paper is devoted toward the identifying the measures to combat with frauds specifically loan & advance related fraud in the banking sector of India. The case study methodology has been used to accomplish the objective of the study. This study found that the advance related fraud result into increase into NPA's. On the basis of the entire study a framework is proposed for the early detection of the fraud.
- (2) Singh, C., Pattanayak, D., Dixit, D., Antony, K., Agarwala, M., Kant, R., & Mathur, V. (2016), The report touches upon the case of rising NPAs in the past few years across various scheduled commercial banks, especially public sector banks. The study finally proposes some recommendations to reduce future occurrence of frauds in Indian banking sector. The credibility of third parties such as auditing firms and credit rating agencies is also questioned in the study and is believed to be a significant contributor amongst other causes, such as oversight by banks and inadequate diligence.
- (3) Bhasin (2015) As part of the study, a questionnaire-based survey was conducted in 2012-13 among 345 bank employees "to know their perception towards bank frauds and evaluate the factors that influence the degree of their compliance level." The study revealed that "there are poor employment practices and lack of effective training; over-burdened staff, weak internal control systems, and low compliance levels on the part of Bank Managers, Offices and Clerks.
- (4) Hari Ram A.(2014), The purpose of this study is get rid from fraud and corruption committed by the criminals, outsiders customers and employees of the banks and financial institutions and other State, Central and Local bodies, public and private sectors. The detection of fraud and corruption has become a big problem. This phenomenon surprisingly is not limited to a particular area, city, or country. It is throughout the world. The word fraud is defined under Sec. 17 of the Indian Contract Act, 1872 and Forgery is defined under Sec.163 of the Indian Penal Code, 1860. The main objectives of this research paper are is to study the information's of law relating to fraud and corruption in banks and financial institutions is essential.
- (5) K. C. Chakrabarty, (2013), the impact of frauds on entities like banks, which are engaged in financial activities, is more significant as their operations involve intermediation of funds. The economic cost of frauds can be huge in terms of likely disruption in the working of the markets, financial institutions, and the payment system. Besides, frauds can have a potentially debilitating effect on confidence in the banking system and may damage the integrity and stability of the economy. It can bring down banks, undermine the central bank's supervisory role and even create social unrest, discontent and political upheavals. The vulnerability of banks to fraud has been heightened by technological advancements in recent times.

5. RESEARCH OBJECTIVE:

- (1) The objective of this research paper is to provide the measures to prevent fraud.
- (2) The objective is to suggest a framework for preventing technological Fraud.

6. RESEARCH METHOD:

This study is based on Qualitative study and based on the cases of the frauds committed in the Indian banking sector both nationalised and private banks. The main objectives of this study have to identify the preventive measures for technological frauds and to accomplish the objective of the study the author has studied the multiple cases of the frauds. In this study, I used the multiple sources of data collection such as: Fraud cases published in Newspaper, Articles published in Journal, RBI publications and speech, Interview & Observation. Interviews can provide additional information that was missed in observation and can be used to check the accuracy of observations.

Bank Group wise Technology Related Frauds

(No. of cases in absolute terms and amount involved in ` Crore)

Bank Group	2009-10		2010-11		2011-12		2012-13		Cumulative total (As at end March 2013)	
	No. of cases	Amount involved	No. of cases	Amount involved	No. of cases	Amount involved	No. of cases	Amount involved	No. of cases	Amount involved

Nationalised Banks including SBI Group	118	1.82	143	3.39	172	7.26	190	9.85	824	25.60
Old Private Sector Banks	9	0.15	4	0.46	9	0.06	6	1.09	55	2.30
New Private Sector Banks	14387	34.53	9638	21.41	6552	16.54	3408	33.97	74321	183.48
Sub Total	14396	34.68	9642	21.87	6561	16.6	3414	35.06	75200	211.38
Foreign Banks	5273	26.88	4486	14.77	3315	14.60	5161	22.45	36455	145.95
Grand Total	19787	63.38	14271	40.03	10048	38.46	8765	67.36	111655	357.33

Source: Report by K.C. Chakrabarty (Deputy Governor of RBI): Frauds in Banking sector- causes, concern and cures, presented during National Conference on Financial Fraud organised by ASSOCHAM, New Delhi. Dated 26th July 2013.

From the above table we can see that the technological fraud increases in nationalized banks and private sector banks. Government has to take the actions to prevent the fraud. Otherwise it will create a problem for the development and growth of the banking industry.in comparison to year 2009-10 fraud is increased in 2012-13.

7. PREVENTIVE MEASURE FOR REDUCING FRAUD:

(1) Multi-Factor Authentication:

The best approach is to start with a multi-factor authentication/multi-layered security structure. This is what Romeo is seeing from the institutions that are successfully thwarting fraud. "Remember, there is no one silver bullet that will solve this problem, so if you put all your hope in a single solution, you'll get compromised, and the intruder will have everything."

This multi-layered approach from a software perspective, combined with old-fashioned out-of-band phone calls to the customer to confirm a questionable transaction, can cut the institution's headaches and the business' fraud losses.

In the old days, Romeo says, calendars were put in place for all set transactions for all accounts, whether they were large corporates or small businesses. "If they had a weekly payroll, that only went out once a week, and then all of a sudden we saw something going out every day -- that would be a red flag; we would question it," he says.

(2) Banks: Monitor Transactions:

In his days in bank operations, Romeo says, the bank used to set up daily limits on each user. "We used to set these limits on our mainframe processor in the bank, along with file limits and batch limits, so if there were something added, or out of the ordinary, we would spot it." Another thing to watch for is a whole lot of activity right under \$9,000. "Because the fraudsters know they won't draw suspicion of a bank if they fly under \$10,000 mark."

(3) Businesses: Reconcile Corporate Accounts Daily:

For businesses, Romeo recommends reconciliation of banking accounts and transactions on a daily basis -- either at end of day or at least at the beginning. "This will help catch any transactions you didn't make, and the sooner you bring it to your bank's attention, the better chance to retrieve the money, with the bank doing a recall or reversal of the transaction. The longer you wait, the less likely it is that you'll see that money recovered."

(4) Employ Dual, Triple Controls:

Dual controls at the corporate side are, at the very least, tables takes. Romeo suggests even triple controls, where one person creates the transaction, a second person approves it, and then a third person actually sends the transaction.

"If you don't have the people, then set up the ACH transactions with the institution, an out of band confirmation, whether it is a phone call to confirm that you've sent it, and confirmation of the correct information was received," he notes. This can be done live or through an automated voice response system. Usually, only one person would have the password and ID to call the bank, which would be totally separate from the person's computer.

(5) Raise Fraud Awareness:

Finally, Romeo says, continuous education of business customers is important. At the national level, this problem of corporate account takeover has gotten real attention. But real solutions won't come until financial institutions and their corporate accounts alike realize the real risks they face - and simple solutions they can implement to help mitigate those risks.

8. CONCLUSION:

While the banking industry in India has witnessed a steady growth in its total business and profits, the amount involved in bank frauds has also been on the rise. This unhealthy development in the banking sector produces not only losses to the banks but also affects their credibility adversely. The effective customer education and communications programs helps customers to recognize how to prevent fraud, but also helping them understand their own responsibilities, should go hand-in-hand with sophisticated cyber security measures.

REFERENCES:

1. Anthala H. R. (2014), Research paper on Case laws of Fraud, forgery and Corruption in Banks and Financial Institutions in India, IOSR Journal of Economics and Finance, e-ISSN: 2321-5933, p-ISSN: 2321-5925. Volume 3, Issue 6. (May-Jun. 2014), PP 53-57
2. Bhasin, M. L. (2015), “An Empirical Study of Frauds in the Banks”, European Journal of Business and Social Sciences, Vol. 4, No. 07, October 2015. P.P. 1-12
3. Chakrabarty, K. C. (2013, July). Fraud in the Banking Sector—Causes, Concerns and Cures. In National Conference on Financial Fraud organised by ASSOCHAM, New Delhi (Vol. 26).
4. <https://www.bankinfosecurity.com/5-tips-to-reduce-banking-fraud-a-2534>
5. Rohilla, A., & Bansal, I. (2017). COMBAT LOAN & ADVANCE RELATED FRAUDS—A STUDY OF INDIAN BANKING SECTOR. International Journal of Research in Finance and Marketing, 7(6), 26-36.
6. Singh, C., Pattanayak, D., Dixit, D., Antony, K., Agarwala, M., Kant, R., & Mathur, V. (2016),”Frauds in the Indian Banking Industry”, IIM Bangalore Research Paper No. 505. Available at SSRN: 2741013.