Reg. **Policy Framework on Fraud Risk Management & Vigilance (2017-18 Version).**

1) Main Contents.

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2. **Fraud & Economic Crime: Global Perspective.**

2.1. Fraud or economic crime[1] is a diversified global issue with 36% of organizations[2] experiencing it across both developed and emerging economies. It is an increasing concern for all financial institutions: from the largest global organizations to the smallest local-area entities and poses a threat to business activities as well as to related systems & processes. According to KPMG International 's May ,2016 report fraud is a "global scourge that harms corporate reputation, costs millions & ruins lives". It (the KPMG) in that survey attributed 3/5th of frauds to "weak internal controls." This survey also reveals:

a) that even if controls are strong, the fraudsters try to "evade & over-ride them";
b) that frauds in groups are likely to be perpetrated twice than in solitude ;
c) that male fraudsters tend to collude more than women-folk;
d) that fraudsters consist of people both from inside as well as outside necessitating better third-party due-diligence for checking & verifying the antecedents of various stakeholders for mitigating fraud-risks ; and
e) that although technology helps both fraudster as well as the business organization yet *there is need for regular risk assessment for prevention & detection of fraudulent acts (both potential & real).*

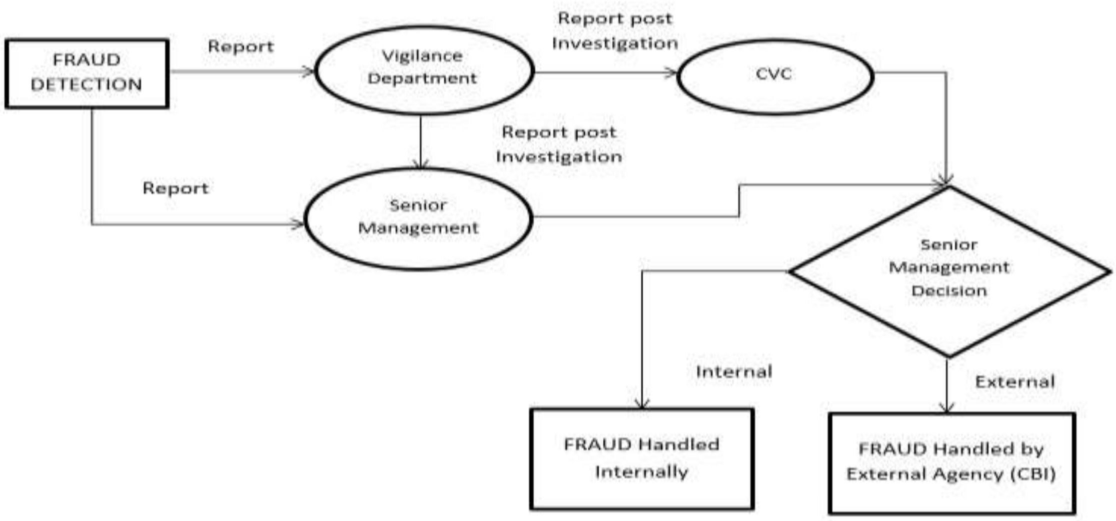
2.2. While commenting on increase in frauds, Deloitte Touche Tohmatsu Limited (commonly referred to as Deloitte) has stated that the **main reasons**[3] for increase in incidence of frauds in Indian banking sector are (i) lack of oversight by line managers/ senior management on deviations from existing processes, (ii) business pressures to meet unreasonable targets; (iii) lack of tools to identify potential red flags, and (iv) collusion between employees and external parties. Regarding the modus-operandi , Deloitte has observed that while in *retail banking* it was mainly fraudulent documentation and over-valuation/ absence of collaterals, in *corporate banking* frauds happened mostly due to diversion/ siphoning of funds and in *private (personal loan segment) banking* the modus-operandi was "identity theft" and fraudulent documentation. Timely **detection of frauds**[4] is very essential. It may happen through anonymous complaints, internal whistle-blower inputs, periodic onsite and offsite inspections (concurrent/ RBIA/ snap/ I.S. Audit/ Statutory Audit/CAG Audit), timely account reconciliation process, data analytic mode, monitoring of suspicious transactions , marking of red flagged accounts/ events, analysis of Early Warning Signals (EWS) as illustrated in the RBI check-list, surveillance & audit, IT controls, through law enforcement/ regulatory agencies like State Vigilance Department, CBI, RBI caution notice/suo-

[1] illegal acts committed by an individual or a group of individuals to obtain a financial or professional advantage : https://definitions.uslegal.com/e/economic-crime

[2] Global Economic Crime Survey -2016 by Price Water Coopers Private Limited.

[3] 2015 Indian Banking Fraud Survey report , Volume II.

[4] Flow Chart depicting **procedures post detection** in public sector banks in India.



motto fraud-declaration communications of the RBI. According to PWC[5] in India, internal tip-off remains the most effective means to detect instances of frauds (22%), followed by detection through routine internal audits (13%), whistle-blower hotlines (12%) and suspicious transaction reporting (12%). On the other hand, globally, the methods of fraud detection vary from the Indian results with 14% of cases through suspicious transaction reporting followed by routine internal audits (11%), internal tip-offs (11%) and detection by accident (11%). Today, an organization's data runs into terabytes and the process and controls around data management are becoming increasingly complex and sophisticated. Hence, there is a growing need to focus on data analytics and periodic fraud risk management (FRM) as means of fraud detection. Currently, only 8% of the Indian entities reportedly use data analytics for fraud detection and only 5% use the FRM. To identify and mitigate fraud risks, there is need to utilize both traditional and innovative fraud detection tools/ techniques with proper incentive to the genuine whistle-blowers and company insiders[6] to come forward in exposing incidents of frauds. The pattern of fraud detection also varies. For solo fraudsters, management review and internal audits are generally found effective. However, for colluders, whistle-blowing and anonymous tip-offs, work better. It is also observed that the presence of anti-fraud controls was correlated with both lower fraud losses and quicker detection. Association of Certified Fraud Examiners (ACFE)[7] compared organizations that had specific anti-fraud controls in place against organizations lacking those controls and found that in cases where controls were present, fraud losses were 14.3%–54% lower and frauds were detected 33.3%–50% more quickly. This gives credence to the need for & efficacy of anti-fraud controls. Equally related is the time-horizon taken for detecting a fraud as the loss caused by a fraud is also a function of how long it lasts before being detected and recoveries effected as longer the perpetrators are able to go undetected, the more financial harm they are able to cause. The good news is that many fraud losses are mitigated by early detection, as more than 25% of cases[8] were reportedly uncovered in the first six months. However, the median duration of the frauds was found to be 18 months, and more than 32% lasted at least two years before they were discovered. Equally important is the need to observe / analyze and monitor the "behavioral red flags of the perpetrators'. The ACFE has identified ***19 common behavior red flags***[9] of occupational frauds which can be used cautiously & carefully in fraud-detection process with a strong sense/ level of accountability and responsibility for avoiding mistaking symptoms for real malady.

2. Incidence of Fraud Cases in the J & K Bank Limited: Recent Perspective.

A snapshot of the fraud incidents and amount involved during the last three years (FY 2014-15, FY2015-16 and FY2016-17) is given in ***annexure "A"***. A perusal of the same indicates:

i) That in all 56 fraud cases (12 in FY2014-15, 19 in 2015-16 and 25 in 2016-17) were detected and reported during last three years i.e. FY 2014-15 to FY2016-17 involving Rs.1226.96 crores with recovery of Rs.404.86 crores and net loss of Rs.822.10 crores. As against 25 fraud cases detected and reported in FY 2016-17, the number of fraud incidents detected and reported in FY 2015-16 and FY 2014-15 were 19 and 12 respectively indicating Y-o-Y increase of 06 cases in FY2016-17 and 07 cases in FY 2015-16;

ii) That thirteen large value (Rs.1.00 crore and above) cases were detected and reported during the above period involving Rs.1218.34 crores with recovery of Rs.401.16 crores and net loss of Rs.817.18 crores;

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5 Global Economic Crime Survey -2016 by Price Water Coopers Private Limited.

6 In the U.S., for example, the Dodd Frank Act provides financial incentives for whistleblowers to provide information. Similarly, the SFO actively encourages company insiders to provide it with information at the start of any investigation. These efforts appear to have paid off – last year the SFO received more tips from whistleblowers than from self-reports.

7 Report to the Nations on Occupational Fraud and Abuse: 2016 Global Fraud Study.

8 Ibid 7

9 namely (1) living beyond means (45.8% cases); (2) financial difficulties (30% cases); (3) usually close relation with vendor-customer (201% cases); (4) wheeler-dealer attitude (15.30% cases); (5) control issues i.e. unwillingness to share duties (15.30% cases); (6) divorce/ family problems (13.4% cases); (7) irritability, suspiciousness and/ or defensiveness (12.30 % cases); (8) addiction problems (10% cases); (9) complaints about inadequate pay (9% cases); (10) non-behavior red flags (8% cases); (11) refusal to take vacations (7.8% cases); (12) excessive pressure from within organization (7% cases); (13) past employment related problems (6.8% cases); (14) social isolation (5.9% cases); (15) past legal problems (5.6% cases); (16) excessive family/ peer pressure for success (5.1% cases); (17) complaints about lack of authority (4.4% cases); (18) instability in life circumstances (4.3% cases); (19) other reasons (5.5% cases).

iii) That most of the large value frauds (12 out of 13) have occurred in advances portfolio covering bills discounting (Rs. 221.04 crores); cash credit (Rs.15.89 crores) and term loans (Rs.980.42 crores);

iv) The one large value fraud of Rs.1.00 crore has occurred in cheque collection/ clearing and the amount stands fully recovered;

v) That most of the large value frauds 92.31% occurred in credit portfolio of the bank;

vi) That in **FY 2014-15** out of twelve fraud cases, one fraud incident occurred in clearing of instruments, one in internet banking, one in inter-branch accounts; two in deposit accounts and seven in credit portfolio;

vii) That in FY 2015-16, nineteen fraud incidents were detected/ reported with 10 episodes in deposit portfolio (savings : 6; current : 2; term : 2), one in remittance-in-transit and seven in advances portfolio. The pattern of most of the frauds being perpetrated in deposit portfolio is in contrast to the segment-wise occurrence of frauds in advances portfolio in FY 2014-15. Hence, it is seen that both deposits and advances portfolios carry similar fraud-risks;

viii) That in FY 2016-17, out of 25 fraud episodes detected/ reported , 15 cases related to advances; 07 to deposits ; 02 to cheques/DDs and one in internet banking; and

ix) That the above trend of fraud cases detected/ reported during last three financial years reveals an irregular pattern wherein both deposits and advances portfolios are observed to be most vulnerable to fraud incidents with a few incidents in cheque clearing/collection and internet banking.

3. Fraud Incident/s : Main Dimensions, Definition & Classification.

3.1. Three-Dimensions for Occurrence of a Fraud Incident: Pressure, Opportunity and Rationalization. Frauds, as they are *popularly understood*, are acts of criminal deception resorted to by persons singly or in collusion with others with a view to deriving gains to which they are not legally entitled. The genesis of a fraud[10] committed in the workplace generally follows a pattern first identified by Donald Cressey, an American criminologist, in 1953. Cressey proposed the “fraud triangle”, which sets out the three factors that need to be present for a workplace fraud to take place and is still in use some 60 years later. Cressey’s fraud triangle consists of pressure, opportunity and rationalization. The first of these, pressure or incentive, describes the motivation that drives the employee to commit fraud, which can range from personal problems brought on by drink or drug abuse, relationship breakdown or gambling addiction, for example, to corporate pressures such as the need to demonstrate performance to superiors or outside stakeholders, such as investors or regulators. Alternatively, the incentive may be a breakdown in the employee’s relationship with his or her managers, leading to a desire for revenge or a sense that legitimate worth and achievements are going unrecognized.

3.2. Opportunity can arise because of poor or non-existent internal controls or because the individual concerned occupies a position of trust that is vulnerable to abuse. If the fraudsters can see an obvious way to cover their tracks they may well conclude that they have a good chance of making a substantial gain with a low risk of discovery.

3.3. Cressey suggests that rationalization is necessary in fraud because **fraudsters do not see themselves as criminals** and therefore need to justify their actions to themselves so that they feel logical and reasonable. Fraudsters offer a range of justifications for their actions, arguing that they were only borrowing the money they stole; that their employer owed them the money; that they are underpaid and should rightfully receive more; that they had to commit the fraud in order to provide for their family; or that their theft is justified because their employer is dishonest or corrupt.

3.4. RBI Definition of Fraud**.** The study group set up by RBI on large value frauds has come out with following definition of Bank Fraud as under:-

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

[10] Temenos and NetGuardians A-Z of Banking Fraud 2016

3.5. **Fraud Incidents in Banks : Their Main Features.** For the purpose of convenience and simplicity, the study group and RBI Master Circulars on frauds have further clarified those transactions which are broadly having ***one or more of the following features***[11] are to be categorized as fraud.

a. Misappropriation and criminal breach of trust.

b. Fraudulent encashment through forged instruments, manipulation of books of account or through fictitious accounts and conversion of property.

c. Unauthorized credit facilities extended for reward or for illegal gratification.

d. Cash shortages.

e. Cheating and forgery.

f. Fraudulent transactions involving foreign exchange g. Any other type of fraud not coming under the specific heads as above.

As regards cases under (d) and (f) above cash shortages resulting from negligence and fraudulent forex transactions involving irregularities / violation of regulations have also to be reported as fraud if the intention to cheat/defraud is suspected or proved. Notwithstanding the above, cases of cash shortage more than Rs.10,000/-, (including at ATMs) and cases of cash shortage more than Rs. 5,000/- if detected by management / auditor/ inspecting officer and not reported on the day of occurrence by the persons handling cash, are to be treated as incident/s of fraud and reported accordingly.

4.5. **Main Instances of Fraud Incidents**.

Some of the main instances / examples of fraud incidents are given under:

a) Cash shortage

b) Fraudulent encashment of drafts/ cheques/ travelers cheques/ dividend warrants etc.

c) Opening bogus bank accounts in the name of non existing person.

d) Collection of fake instruments with or without connivance of bank staff.

e) Siphoning off funds through fake transfers, un authorized debits of impersonal account or concealment of unauthorized transaction by manipulating entries in the books of account.

f) Sudden disappearance of stocks as compared to figures shown in previous statement or fraudulent removal of pledged stocks/ disposing of hypothecated stocks without the banks knowledge / inflating the value of stocks in the stock statement and drawing excess bank finance.

g) Fudging of financial statements.

h) Issuance of letter of credit, bank guarantee of any type without recording liability in the books of accounts.

i) Creation of fixed deposits, credit balances and issuance of drafts, pay orders, transfer of funds through NEFT/RTGS etc. without any consideration.

j) Discounting forged trade documents or documents without underlying trade transactions or kite flying in clearing effects.

k) Transgression of the delegated authority and its concealment from the Competent Authority resulting in loss to the bank.

l) Misuse of system passwords and breach of computer security.

m) Diversion of funds outside the borrowing units , Lack of interest or criminal neglect on the part of the borrowers, their part of the borrowers, their partners etc and also due to managerial failure leading the unit to become sick.

n) Fraudulent transfer of funds through internet banking .

o) Fraudulent withdrawals through ATM/Debit/Credit Cards.

It is related to mention that cases of theft, burglary, dacoity and robbery **are not to be reported to the RBI in the XBRL[12] format**. These cases are to be reported to the bank management only at Corporate Headquarters for their information and necessary action .

4.6. Frauds in Cheques in Collection and/ or Clearing: Paying Banker to report Forged Instruments as Fraud.

To ensure uniformity and to avoid duplication, frauds involving forged instruments may be reported only by the paying banker and not by the collecting fraudulently by a person who is not the true owner, the collecting bank, which is defrauded, will have to file fraud report with the RBI. In case of collection of instrument where the amount has been credited and withdrawn before realization and subsequently the instrument is

[11] mainly on the provisions of the Indian Penal Code

[12] eXtensible Business Reporting Language System

found to be fake/forged and returned by the paying bank, *it is the collecting bank that has to file FMR-1 with RBI as they are at loss by parting the amount before realization of the instrument*.

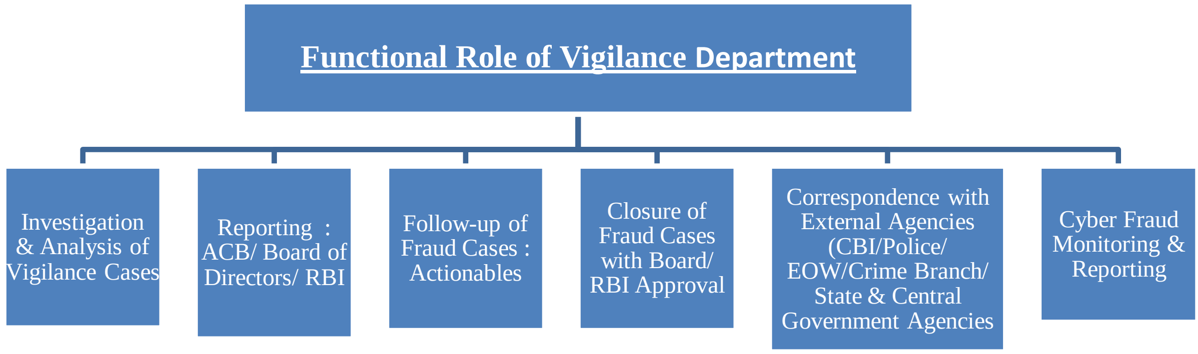
4.7. <u>Encashment of altered /fake Cheques involving two or more Branches of Same Bank.</u>

4.7.1. In case of collection of altered / fake cheques involving two or more business units of the bank, *the Business Unit where the altered /fake cheque has been encashed, should report the fraud to the Vigilance Department Corporate Office.*

4.7.2. In the event of an altered /fake cheque having been paid/ encashed involving two or more Business Units of a bank under Core Banking Solution (CBS), there could be possibility of dispute /difference of opinion as to whether the Business Unit where the drawer of the cheque maintains the account or the Business Unit where the encashment has taken place should report the matter to the corporate office. *In such cases also the Business Unit which has released the payment against an altered/ fake cheque should report the fraud to Vigilance Department Corporate Office.*

5. <u>Existing Standard Operating Procedure (SoP) of and Functional Roles of Vigilance Department.</u>

5.1. In line with its job/ functional role, Vigilance Department, Corporate Headquarters is operating/ will operate under the administrative control f the Chairman & CEO of the Bank through an Executive President/Senior President/ President. The Department is headed by a Vice President / Assistant Vice President and all other staff who are assigned various assignments are reporting to the Executive Manager/ Assistant Vice President. The department has presently following six verticals[13]and their functional roles and associated jobs are tabulated below.



The standard operating procedure/ processes of each of the above verticals is briefly elaborated below:

5.2. **<u>Investigation & Analysis of Vigilance Cases.</u>** Vigilance cases emanate from two sources i.e. external and internal sources. The external sources include the complaints from customers as well as non-customers, State & Central government agencies, print media, CAG and RBI. The internal sources consist of mainly inputs from inspections and audits (snap, concurrent, RBIA, information system (IS) audit, off-site surveillance reports etc.). On receipt of any communication from these sources, the fraud angle is got investigated from the concerned S & C Division[14] of the bank and further examined and analyzed by the investigating officer[15] at Vigilance Department who scrutinize its various aspects and propose suitable actionables depending on the severity of the findings in that case ranging from issuance of caution / displeasure letters to termination and dismissal. In case it is deemed that further action is needed at disciplinary level / department for taking the issues to final conclusion, the case is referred to the Disciplinary Department, Corporate Headquarters for completion of disciplinary proceedings as per the extant rules of the bank.

5.3. **<u>Reporting to the RBI.</u>** The bank is required to report all fraud cases to the RBI. The reporting is done on-line to the RBI through Central Fraud Registry (CFR) as part of credit risk governance and fraud risk management. As per the regulatory requirements, all fraud cases are to be reported individually to the RBI, irrespective of the amount involved, using on-line FMR (Fraud Monitoring Return) Application, in

[13] Subject to such modifications/ changes as will be deemed necessary from time to time.
[14] There are three S&C Divisions: Kashmir, Jammu & Delhi.
[15] Presently, there are five officers handling this job.

XBRL (eXtensible Business Reporting Language)System within three (03) weeks from the date of detection. RBI has also directed to submit reports in all those cases "where central investigating agencies have initiated criminal proceedings suo moto and/or where the Reserve Bank of India has directed that such cases be reported as frauds."[16] Besides, bank are required to send a **Flash Report (FR) for frauds involving Rs.5.00 crore and above within a week of such frauds coming to the notice of the bank's head office**. Any delay in reporting of frauds may entail penal action under Section 47(A) of the Banking Regulation Act,1949[17].

5.4. **Reporting to the ACB/ Board of Directors.** Chapter IV of the latest RBI Master Directions updated as on 03.07.2017 provide that Banks should report all frauds of Rs.1.00 lac and above to their Board promptly on their detection. Similarly, quarterly review reports relating to frauds for the quarter ending June, September and December are to be placed before the Audit Committee of the Board during the month following the quarter to which it pertains. However, the review report of March quarter will be deemed to have been submitted in the Annual Review report for the year ending March, which is to be submitted before the end of next quarter (i.e. quarter ended June,30th). For monitoring and follow-up of **cases of Rs.1.00 crore and above** , the RBI has advised banks to constitute Special Committee of the Board (SCBF) for frauds with five members including the Managing Director of the bank, two members from the ACB and two other members of the Board *excluding RBI nominee*. The periodicity of the SCBF may be decided according to the number of cases involved. Besides, the Committee *"should meet and review as & when"* a fraud involving Rs.1.00 crore and above comes to light.

5.5. **Follow-up of Actionables of Fraud Cases.** After investigation, if any incident is declared a fraud case, there are many action-points that need to be taken to their logical conclusion including addressing loop-holes in the systems & procedures, fixing of staff lapses, filing & registration of FIR with the Police/ Crime Branch/ Economic Offences Wing/CBI etc.; reporting to the RBI and correspondence thereof as & when the RBI desires any further information/ clarification before the case is finally processed for closure of the case file from vigilance view-angle.

5.6. **Closure of Fraud Cases Files with Prior RBI Approval.** The extant RBI guidelines provide that the banks shall report to the Central Fraud Monitoring Cell (CFMC) , and the Senior Supervisory Manager (SSM) of the RBI the details of fraud cases of Rs.1.00 lac and above closed with the reasons for the closure after prior approval from the concerned SSM and completing/ compliance of the following processes/ procedures:

- *That the fraud cases pending with the CBI/Police/Court are finally disposed off;*

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[16] Master Directions on Frauds – Classification and Reporting by commercial banks & selected FIs dated 03.07.2017

[17] 47A. Power of Reserve Bank to impose penalty.—

(1) Notwithstanding anything contained in section 46, if a contravention or default of the nature referred to in sub-section (3) or sub-section (4) of section 46, as the case may be, is made by a banking company, then, the Reserve Bank may impose on such banking company—

(a) where the contravention is of the nature referred to in sub-section (3) of section 46, a penalty not exceeding twice the amount of the deposits in respect of which such contravention was made;

(b) where the contravention or default is of the nature referred to in sub-section (4) of section 46, a penalty not exceeding five lakh rupees or twice the amount involved in such contravention or default where such amount is quantifiable, whichever is more, and where such the contravention or default is a continuing one, a further penalty which may extend to twenty-five thousand rupees] for every day, after the first, during which the contravention of default continues. 3[(2) For the purpose of adjudging the penalty under sub-section (1), the Reserve Bank shall serve notice on the banking company requiring it to show cause why the amount specified in the notice should not be imposed and a reasonable opportunity of being heard shall also be given to such banking company.]

(4) No complaint shall be filed against any banking company in any court of law in respect of any contravention or default in respect of which any penalty has been imposed by the Reserve Bank under this section.

(5) Any penalty imposed by the Reserve Bank under this section shall be payable within a period of fourteen days from the date on which notice issued by the Reserve Bank demanding payment of the sum is served on the banking company and in the event of failure of the banking company to pay the sum within such period, may be levied on a direction made by the principal civil court having jurisdiction in the area where the registered office of the banking company is situated; or, in the case of a banking company incorporated outside India, where its principal place of business in India is situated: Provided that no such direction shall be made except on an application made to the court by the Reserve Bank or any officer authorised by that Bank in this behalf.

(6) The court which makes a direction under sub-section (5) shall issue a certificate specifying the sum payable by the banking company and every such certificate shall be enforceable in the same manner as if it were a decree made by the court in a civil suit.

(7) Where any complaint has been filed against any banking company in any court in respect of the contravention or default of the nature referred to in sub-section (3) or, as the case may be, sub-section (4) of section 46, then, no proceedings for the imposition of any penalty on the banking company shall be taken under this section.]

- *That the examination of staff accountability has been completed;*
- *That the amount of fraud stand recovered or written off;*
- *That insurance claim wherever applicable has been settled; **and***
- *That the bank has reviewed the systems & procedures , identified as the causative factors and plugged the lacunae and the fact of which has been certified by the appropriate authority (Board / Audit Committee of the Board).*
- Banks are also under instructions (i) to pursue vigorously with the CBI for final disposal of the pending fraud cases especially where the banks have completed the staff side action; and (ii) to follow-up with the police authorities and/ or court for final disposal of fraud cases.

5.7. For limited statistical/ reporting purposed, the RBI has allowed bank to close those fraud cases wherein amount involved is upto Rs.25.00 lacs ***provided*** :

*a) the investigation is on or challan / charge sheet has not been filed in the Court for more than three (03) years from the date of filing of the First Information Report (FIR) by the CBI/ Police; **or***

b) the trail in the courts, after filing of charge sheet/ challan by the CBI/ Police , has not been started or is in process.

However, the banks are required to follow the guidelines relating to seeking prior approval for closure of such cases from the SSM and follow-up of such cases after closure as mentioned below:

- the banks are required to submit their proposals, case-wise, for closure to the SSM of the RBI;
- the cases are to be closed after getting the approval of the SSM;
- the banks should maintain separate record of such cases;
- even after closure of the fraud cases for limited statistical purposes, banks are required to vigorously follow-up with the investigating agencies (CBI/Police) to ensure that the investigation process is taken to its logical conclusion;
- the banks to ensure that they are regularly & appropriately represented in the court proceedings as & when required ; and
- all the relevant records to be preserved till the cases are finally disposed off by the CBI/ Police or Courts, as the case may be.
- RBI has advised banks to frame their own board-approved internal policy for closure of fraud cases, incorporating above norms and other internal procedures/ controls as deemed necessary.

5.8. Notwithstanding the fact that banks may close cases of fraud even when the Police / CBI investigation is in progress or cases are pending in the court of law, they should complete , within the prescribed time-frame, the process of examination of staff accountability or conclude staff side action.

5.9. **Correspondence with External Agencies (CBI/Police/ EOW/Crime Branch/ State & Central Government Agencies**

Since crime & fraud incidents including financial crime originate in a real society and entail different stakeholders both inside & outside the financial sector so to address this unhealthy phenomena, there is need for close cooperation and coordination with various external law enforcing agencies so that the collective competencies & skills are utilized to check this menace. Hence there is inter-dependence between the outside agencies and the Vigilance Department of the bank for containing the potential and actual culprits as per the laws of the land and for arresting growing criminal tendency amongst anti-social elements who penetrate the various systems & procedures of banking to the detriment of bank’s interests. Hence, professional communication and correspondence is made with various external agencies like CBI, State Police, Economic Offences Wing, State Crime Branch and other state and central government agencies.

5.10. **Bank’s Cyber Fraud Monitoring & Reporting System : Operationalization of Transaction Monitoring Cell.**

In compliance with the RBI directions, the bank has recently made operational cyber crime monitoring and reporting cell called **“Transaction Monitoring Cell”** which is functioning under the administrative control of Vigilance Department with technical-&-supervisory support from the T&IDS Department through the Chief Information Security Officer of the bank for real time (24*7*365) monitoring of various transactions emanating from debit & credit cards /PoS transactions/ Mobile banking/ Internet Banking/ Core banking etc. so that incidence of potential / actual attempts of frauds are prevented and proper system-based checks put into place.

5.11. Of late, the bank has in collaboration with Deloitte India initiated the project of **business process reengineering (BPR)** which will re-look into the functional roles of the Vigilance Department for streamlining its workings for further improvement.

6. Fraud Risk Management Policy in Bank: Functional Aspects.

i) Roles & Responsibilities.

- Business Unit Functionaries.
  - Fraud Awareness.
  - Continuous & Effective Monitoring of Fraud Prone Areas in Branch Working (as per the check list attached and given in annexure " C").
  - Detection & Reporting of Potential/ Actual Fraud Incidents : Whistle Blower Role
  - Role of Internal & External Auditors: Counter-checking Potential/ Actual Fraud Incidents for timely action
- **Role of Zonal and S & C Departments in Detection & Reporting of Frauds**.
- Cluster / Zonal Level. To randomly check the efficacy of the Fraud Monitoring Mechanism of business units on periodic basis. To impart necessary instructions and ensure that the RBIA inspectors/ Concurrent Auditors/ Stock Auditors report in detail about the potential & actual fraud prone areas in the workings/ functioning of the business units so that no incident of fraud remains undetected/ unreported.
- S&C Divisional Level. To monitor both on-site and off-site basis that so that various Fraud Risk Management Measures are completely & comprehensively complied with by the Business Units under its jurisdiction.
- Vigilance Department.
- To present to the Audit Committee of the Board (ACB)/ Board of Directors (BoD) comprehensive investigations about the cases having fraud angel and timely reporting of the fraud case/ their investigations/ action-taken on Board directions & observations within the stipulated time-line.
- To arrange to get the cases investigated with the highest possible standards of professionalism and objectivity so that true & correct picture of fraud angle of any case is reported to the top management with suitable actionables to take the case to its logical conclusion.
- To monitor & pursue closure of fraud case files in a time-bound manner and as per the regulatory guidelines thereof.
- To share with operational levels the modus-operandi of various fraud incidents across the banking industry and/ or cases of the bank having unique modus-operandi so that there is proper dissemination of information and all staff remain updated/ informed about the latest trends in vigilance cases.
- To convey periodic meeting of Fraud Monitoring Committee headed by the President/ Sr. President / Executive President so that gaps, if any, in fraud-monitoring having cyber & non-cyber nature/ dimensions, are plugged on real-time or near-real-time basis for putting in place the effectiveness of various systems & procedures for avoiding /detecting/containing/ arresting/ monitoring fraud cases.
- To report the *events of overriding* of extant systems & procedures in bank in fraud incidents by external or internal elements and suggest suitable measures for improving the deficiencies in such over-ridden systems & procedures so that the preeminence of compliance to systems & procedures is ensured.
- To avert high-value fraud loan assets fraud of Rs.5.00 crore and above , A &AP Department, Corporate Headquarters will be advised by the Vigilance Department to establish an monitoring arm in its department which will report to the top management on near real-time basis about the likely red-flag borrowal accounts so that timely action is

taken for prevention of fraudulent activities in loan asset portfolio of the bank. The A&AP Department, Corporate Headquarters will be advised to share these reports with Vigilance Department for collaborative and collective monitoring/ detecting/ reporting of fraud incidents.

➢ Role of Top Management : Chairman & CEO /Audit Committee of the Board / Board of Directors of the Bank.

- To get sufficiently involved in avoiding /detecting/containing/ arresting/ monitoring fraud cases as per the regulatory requirements.
- To remain watchful / alert about the fraud risk factors impacting the working of the bank.
- To direct & arrange to observe that professional code of conduct[18] is observed by the entire staff including top management of the bank. Likewise the policies of the bank on staff Code of Conduct and Whistleblower Policy are genuinely pursued/ followed in spirit and letter and not merely as tools of regulatory requirements.
- To monitor & seek compliance of fraud report that have emanated from *overriding* of extant systems & procedures in bank in fraud incidents by external or internal elements and see that the deficiencies in such over-ridden systems & procedures are duly rectified and corrected so that the preeminence of compliance to systems & procedures is ensured both at operational & administrative levels.
- To inquire and oversee existence of adequacy of fraud-mitigant systems & procedures both in terms of policy and practice and wherever needed give directions for clear & complete compliance to regulatory and non-regulatory guidelines so that fraud-incidents go not remain undetected/ un-reported and unattended.
- To periodically obtain evaluation reports about the existence and functioning of fraud prevention , deterrence , detection systems and efficacy of internal controls/ self-policing measures with specific reference to steps taken for arresting criminal conduct amongst the bank staff/ management.

ii. Commitment Statement for Prevention, Reporting of Fraud Incidents of the J&K Bank Employees & Management.

- To ensure compliance to employees code of conduct as given in this policy document.
- To report potential fraud areas without any loss of time.
- To avoid conflict of interest.
- To maintain highest standards of discipline in performance of job roles/ duties.
- To maintain highest level of integrity and ethical values.
- To arrange to devise and follow proper forensic/ due diligence on third parties and outsourced service providers (OSPs), wherever applicable.
- To enhance focus on assessing fraud risks in banking operations for creating an overall fraud-free environment in the whole enterprise/ bank.
- To transfer organizational culture suitably for encouraging result-oriented professionalism and/ or professional approach in performance of their duties so that best business practices are inculcated in the entire bank.

iii. **Fraud Awareness**.

As awareness is the first effective deterrence in management of fraud risks and fraud incidents, so there is need to spread awareness amongst the staff/ other stakeholders to report the unethical behavior related to fraud incidents (potential or real) under whistle blower policy. For this purpose, the following areas need to be focused upon with the measures given against each:

S. No.	**Area of Focus**	**Specific Measures to be Considered**

[18] Given in **annexure "B"**

1.	Code of Conduct	➢ To ensure that the employees acknowledge the code of conduct and abide by it. ➢ To seek employees acknowledgement & acceptance every time the code is revised. ➢ To ensure that the third parties acknowledge the code of conduct proportionate to the scope of their operations/ dealings. ➢ To take periodic review of the code of conduct. ➢ To include specific clauses pertaining to the frauds in the code of conduct. ➢ To form an internal team that researches on new fraud areas and communicates that to the top management. ➢ To revise the policy in line with the fraud risk perceptions .
2.	Establishing a Whistle Blowing System	➢ Already in existence and operational.
3.	Develop a Comprehensive anti-fraud Policy	➢ Under submission in the form of this document.
4.	Align reward system with compliance to core business/ organizational values	➢ To include ethical behavior as a key component of employee performance appraisal. ➢ To recognize that for sound business growth ethical behavior is mandatory and both are complementary. ➢ To create proper atmosphere and to provide proper space for highlighting and discussing difficult business issues or any sensitive matter with senior management.
5.	Periodic Assessment & Review of Fraud Risk Awareness/ Sensitivity Measures.	➢ To conduct fraud and ethical surveys to understand disconnect, if any, between the leadership's tone at the top versus activities at the ground. ➢ To impart information/ data on fraud trends, damage due to some critical fraud cases and practical scenarios that fraud can manifest itself in. ➢ To sort out issues of ethical dilemma & strategic business by discussing emerging issues from time to time. ➢ To use mass media including video, events, online chats, teleconferencing meetings, blogs etc. to communicate with employees on anti-fraud measures.

7. Scope of Policy Framework / Document.

7.1. This policy is framed to put in place comprehensive guidelines /strategy for :

i) *formalizing* a Board approved blue-print for the functional role of various officers / tiers of executives in the Vigilance Department including the Standard Operating Procedures (SoP) for Vigilance Department;

ii) *preventing*[19] occurrence of frauds by improving existing systems & procedures of fraud detection before their incidence;

iii) *detection* of incidence of fraudulent events within the earliest possible time-frame;

iv) *investigation* of incidence of frauds in a complete manner for preventing their recurrence;

v) *dissemination* of modus-operandi of frauds with business units/ other controlling offices for information and necessary precautions;

vi) *reporting* frauds to the regulatory authorities / other concerned offices as per the RBI directions ;

vii) *examining staff lapses* and fixings of staff accountability wherever noticed/ required.

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[19] See **Annexure "C"** on Preventive Vigilance

7.2. **<u>Operational instructions/guidelines are issued from time to time by different departments/ divisions of Corporate Headquarters and the contents of this policy document must be read in lines and combination with those guidelines. Such clauses of this Policy document as are updated/ modified at any point of time by instructions from the Corporate Headquarters shall stand recast/ modified accordingly.</u>**

8. <u>Key Principles & Main Objectives.</u>

8.1. Only through meticulous and ongoing efforts can an organization protect itself against significant attempts/ acts of fraud. The ***<u>key principles & objectives</u>*** for proactively operationalizing a proper fraud risk setup in the bank are listed below:
i) Existence of a **<u>well-documented Fraud Risk Management Policy</u>** clearly conveying the expectations of the Board of Directors and Senior Management relating to fraud risk management at operational levels involving various stakeholder (branch functionaries, concurrent auditors, RBIA inspectors, stock auditors, RBI inspectors, statutory auditors, CAG auditors, top management conducting snap/ surprise inspections etc.) ;
ii**<u>) Periodic assessment of Fraud Risk Areas & Exposure</u>** to identify specific potential areas and events that the bank needs to mitigate. For this purpose, two-pronged strategy is devised: one at grass-root level for taking desired ***<u>steps for prevention of fraud incidents</u>*** *<u>(a suggestive check-list of preventive measures is given at para 21),</u>* and the second at top level, Fraud Monitoring Council, under the control of the Executive President (S) wherein gaps in fraud-prone areas are reviewed on quarterly intervals and necessary steps initiated for addressing/ plugging these gaps;
iii) **<u>Establishing & Operationalization of Fraud Prevention Measures & Techniques</u>** , wherever possible, to mitigate possible impact of potential fraud prone areas on the workings of the bank.
iv) **<u>Detection Techniques/ Modes to be established</u>** to uncover fraud events when preventive measures fail or the unmitigated risk are realized. For this purpose the bank has put into use a robust internal and external audit system along with snap inspections of business units from top executives so that fraud-prone areas are periodically checked for swift & certain action; and
v) Putting in place **<u>a proper Reporting Process</u>** to solicit inputs on potential fraud and a coordinated approach for investigation and corrective action to ensure potential fraud is addressed appropriately and correctly. This is done as per the regulatory framework of the RBI by operationalizing measures like Whistle Blower Mechanism and Fraud Control Plan.

9. <u>Functional Roles & Delegation of Duties of Vigilance Department.</u>

<u>Serial No.</u>	**<u>Executive Level</u>**	**<u>Functional Role</u>**
a)	Vice President	➢ To get investigations conducted through the S&C Divisions in all fraud incidents/ fraud-like cases/ dacoities/ burglaries/ thefts etc.; ➢ To arrange to submit comprehensive investigations reports to the higher levels with specific recommendations; ➢ To monitor with other staff in the Vigilance Department the action-points of investigated cases so that all actionables are taken to their respective logical conclusion in a reasonable time-frame and cases disposed off/ closed without any delay; ➢ To ensure close coordination amongst the staff in the Vigilance Department so that there is complete synergy in the working of the Department and communication flows in different directions (upward, downward, horizontal/lateral, external etc.) is a smooth & business-like way; ➢ To see and ensure that all ACB/Board notes, complete in all respects, are submitted to the ACB/Board on time; ➢ To see that fraud incidents are reported to the RBI without any delay; ➢ To get all compliance reports prepared/ submitted through the concerned officials in Vigilance Department; ➢ To settle claims as per the delegation of powers given at para 18.
b)	President/ Sr. President/	➢ To perform all such functions as are necessary for effective functioning of the Vigilance Department keeping in view its role and various

	Executive President[20]	responsibilities in the organization; ➢ To approve proposals for closure of normal investigation files after the actionables are fully taken to their logical conclusion ; ➢ To ensure submission of all ACB/Board/ Compliance reports in time and in a comprehensive and concise manner; ➢ To see that the staff issues in vigilance cases are dealt with complete objectivity and keeping in view the best interests of the organization; ➢ To ensure that while dealing with vigilance cases complete balance is maintained between operational realities and compliance issues for maintaining a sync business objectives and compliance aspects of banking activities; ➢ To settle claims as per the delegation of powers given at para 18.
c)	Chairman & CEO	➢ To approve initiating of disciplinary proceeding against the staff on the basis of different proposals recommendations submitted by the Vigilance Department from time to time; ➢ To instruct to take up direct investigation by Vigilance Department, Corporate Headquarters in such cases as may be deemed necessary from time to time; ➢ To pass on from time-to-time such directions to the Vigilance Department as are deemed necessary for its effective working, continuous improvement of systems & procedures in line with the changing times and demands of the regulator, operational issues and evolving banking industry; ➢ To give instructions for conduct of special/ extraordinary investigations keeping in view the facts of individual cases/ events / situations and circumstances at any point of time; ➢ To give directions to the Vigilance Department on any aspect of its working at any time. ➢ To monitor the overall working of the Vigilance Department and to act as a effective conduit of communication between the Board and the Vigilance Department so that the overall workings of the Vigilance Department is upto the expectation of the Board . ➢ To settle claims as per the delegation of powers given at para 18.
d)	ACB/ Board of Directors	➢ To approve the policy frameworks from time to time; ➢ To give directions on quality of fraud investigations/ reporting and their mitigants during various reviews; ➢ To review the fraud reports and fraud incidents and the fraud-preventing mechanisms and give, directions for their improvement as per the regulatory (RBI) directions ; ➢ To give directions /make observations/ ask for compliances in respect of the various notes submitted to the Board and any other issues that comes to the knowledge of the Board through any media / mode of communication for conduct of investigations/ re-work or re-examine investigation reports/ board notes submitted to it; ➢ To settle claims as per the delegation of powers given at para 18.

10. <u>Detection of Frauds.</u>

10.1. According to KPMG[21] survey 2016, 24% frauds were detected through tip-offs and complaints (other than formal hotline) followed by management review (22%); formal whistle blowing reports/ hotlines (20%); accidental detection (14%); internal audit (14%); suspicious / vigilant seniors (10%); other internal controls (7%); external audit (6%); self-reported/ admitted (3%) and pro-active data analytics (3%).

10.2. <u>Detection of Frauds :Main Sources.</u>

The bank has in place the proper system and procedure, which if applied with due diligence, can also help in timely detection of frauds. However the following are some of the sources for detection of frauds:-

[20] . Whosoever is to administrative head between Vice President & the Chairman & CEO

[21] Global Profiles of Fraudsters, KPMG International, 2016.

- Visits of senior officers from various quarters.
- Checking of various reports.
- Reconciliation of office accounts.
- Complaints received from the customers.
- Investigation of fraud cases by the law enforcement agencies.
- Internal /External audit reports of business units/offices.
- Periodical verification of securities held by the bank.
- Electronic/Print Media Reports.
- Information from a whistleblower.
- RBI information regarding frauds by unscrupulous borrowers.
- Recovery Action under SARFAESI Act/Recovery suits etc.
- Surprise checking of cash.

11. Reporting of Frauds : Operational Level to Controlling Offices & Regulator (RBI).

11.1. Role of Operational Levels: Reporting of Incidents of Fraud / Attempted Frauds to Vigilance Department, Corporate Headquarters.

All business units/ operational levels and/or their immediate controlling (Cluster/ Zonal) offices must report all incidents of fraud/ attempted fraud directly to the Vigilance Department through email at vigilance@jkbmail.com *without loss of any time*. Copies of the report must also be endorsed/ forwarded to S&C Department, Business Support Department, Operational Risk Management Department, Balance Sheet & Taxation Department, Insurance Department for their information/ necessary action.

11.2. Reporting to the RBI.

The reporting of fraud/ attempted fraud to the RBI will be done by the designated nodal officer (presently President Vigilance Department) after the required information / data is received from the operational levels and the same is captured/ uploaded in the related formats. The time-lines prescribed by the RBI will be adhered to in all cases. It is mandatory/ obligatory on every business unit/office to report the incidence of fraud to Vigilance Department CHQ within 24 hours of its surfacing through a flash message with preliminary report along with the modus operandi of the fraud. **Any delay / inaction including suppression or attempt at hush-up/ non-reporting shall entail direct Disciplinary Action under rules**.

10.3. Online Reporting of frauds to the Regulator.

With effect from 1st April,2017 all fraud/ attempted fraud incidents are to be reported to the RBI on-line through XBRL format. Generally, the various formats (**FMR-I to FMR-III**) prescribed by the RBI are related to the amount of fraud incident. The reporting to RBI on frauds is to be made as per their standing instructions as under:

11.4 Frauds involving Amount below Rs 1.00 lac

Banks need not furnish FMR-1 return in fraud cases involving amount below Rs. 1.00 lac to RBI in either hard or soft copy. However ,banks at their end should make the data entry in respect of such cases through the FRMS package individually in FRM-1 format (less than Rs.1.00 lac) which will get automatically captured in FRM-2 return and will form part of the consolidated database relating to frauds for respective bank.

11.5 Frauds involving Amount of Rs.1.00 lacs and above.

All the frauds cases involving RS 1.00 lac and above are to be reported to RBI . A soft copy of the reports on frauds in FMR formats is to be submitted to the Central Office of the Department of Banking Supervision (DBS) Fraud Monitoring Cell as well as to Regional Office (RO) of DBS/FCMD under whose jurisdiction the Head office of the bank falls while as the hard copy is to be submitted as per the details hereunder ;-

a) Fraud Cases involving an amount more than Rs. 1.00 lacs and upto Rs.50.00 lacs.

i) To the Regional Office under whose jurisdiction the branch where the fraud has taken place is located.
ii) To the regional Office under whose jurisdiction the Head office where the fraud has taken place is located.

b) Fraud Cases involving an amount of Rs. 50.00 lacs and above.

i. To the concerned Regional Office of Department of Banking Supervision, Reserve Bank of India under whose jurisdiction the Head Office where the fraud has taken place is located.

ii. To reserve Bank of India, Fraud Monitoring Cell, Department of Banking Supervision , Central Office , 2nd floor , centre 1, World Trade Centre , Cuffe Parade Mumbai -400005

11.6 **Frauds involving Rs.100.00 lacs and above**

10.6.1. The frauds involving rs.100.00 lacs and above , are required to be reported **by means of a D.O letter under the signs of the Chairman & ECO of the bank** with copies endorsed to the Regional Office of RBI/FCMD under whose jurisdiction the bank-branch, where the fraud has been perpetrate, is functioning.

11.6.2**. As complete details on all related aspects of a fraud perpetrated in the bank are vital for reporting to the RBI, so business units, while reporting any fraud incident must give full details of the incident (like name of the branch/ date of occurrence/ date of detection/ amount involved/ amount recovered/ likely loss and a details write-up on modus-operandi of the incident) so that the same is reported to the RBI for their information, monitoring, supervisory-role and dissemination of information through caution advices / Central Fraud Registry (CFR) to all member banks . This will keep all concerned stakeholders informed besides preventing recurrence of similar incidents.**

11.6.3. **Suo-moto Criminal Proceeding by Central Investigating Agencies and / or RBI Directions to Report a Case as Fraud.**

The RBI has directed that fraud reports should also be submitted in cases where central investigating agencies have initiated criminal proceedings suo moto and/or where the Reserve Bank has directed that such cases be reported as frauds.

11.6.4. **Fraud Incidents in Subsidiaries and Affiliates/Joint Ventures.**

RBI has directed that banks may also report frauds perpetrated in their subsidiaries and affiliates/joint ventures in FMR 1 format in hard copy only. However, such frauds should neither be included in the report on outstanding frauds nor entered in the FRMS package at any stage. In case the subsidiary/ affiliate/joint venture of the bank *is an entity which is regulated by Reserve Bank of India* and is independently required to report the cases of fraud to RBI in terms of guidelines applicable to that subsidiary/affiliate/joint venture, the parent bank need not furnish the hard copy of the FMR 1 statement in respect of fraud cases detected at such subsidiary/affiliate/joint venture.

11.6.5. Delay in Reporting of Frauds : Liable for Penal Action under Section 47(A) of the Banking Regulation Act, 1949

Banks are required to ensure that their reporting system is suitably streamlined so that delays in reporting of frauds, submission of delayed and incomplete fraud reports are avoided. RBI has also directed banks to fix staff accountability in respect of delays in reporting fraud cases . Delay in reporting of frauds and the consequent delay in alerting other banks about the modus operandi and dissemination of information through caution advices / CFR against unscrupulous borrowers could result in similar frauds being perpetrated elsewhere. Hence banks are under advice to strictly adhere to the timeframe fixed for reporting of fraud cases to RBI failing which they would be liable for penal action prescribed under Section 47(A) of the Banking Regulation Act, 1949.

12. Frauds Perpetrated by Unscrupulous Borrowers

12.1 A large number of frauds are committed by unscrupulous borrowers including companies, partnership firms /proprietary concerns and /or their directors/partners/ proprietors by various methods including :

i) Fraudulent Discount of Instruments or Kite Flying in clearing effects.

ii) Fraudulent removal of pledged stocks /disposing of hypothecated stocks without the banks knowledge/inflating the value of stocks in the stock statements and drawing excess bank finance.

iii) Diversion of funds outside the borrowing units, lack of interest o or criminal neglect on the part of borrowers, their partners, etc. and also due to managerial failure leading to the unit becoming sick and due to laxity in effective supervision over the operations in borrowal accounts on the part of the bank functionaries rendering the advance difficult to recover.

12 .2 *Due diligenc*e should be exercised at all operative levels while appraising the *credit needs* of borrowers, borrower companies, partnership/ proprietorship concerns and their directors, partners and proprietors, etc. as also their associates who have defrauded the banks.

12.3 In addition to above borrower-fraudsters, third parties such as builders, warehouse/cold storage owners, motor vehicle/tractor dealers, travel agents, etc. and professionals such as architects, valuers, chartered accountants, advocates, etc. ***are also to be held accountable if they have played a vital role in credit sanction/disbursement or facilitated the perpetration of frauds***. Their names would be reported to Indian Banks Association (IBA) to prepare caution lists of such third parties for circulation among the banks. *However before reporting to IBA, bank would satisfy itself of the involvement of third parties concerned and also provide them with an opportunity of being heard*. In this regard extant procedures are to be followed and the processes suitably recorded as per the RBI guidelines.

13. Frauds in Borrowal Accounts having Multiple Banking Arrangements.

13.1 Certain unscrupulous borrowers enjoying credit facilities under "multiple banking arrangement" after defrauding one of the financing banks, continue to enjoy the facilities with other financing banks and in some cases avail even higher limits at those banks. In certain cases the borrowers use the accounts maintained at other financing banks to siphon off funds by diverting from the bank on which the fraud is being perpetrated. This is due to lack of a formal arrangement for exchange of information among various lending banks/FIs. In some of the fraud cases, the securities offered by the borrowers to different banks are the same.

13.2 In view of this, all the Business Units /Controlling Offices, having financed a borrower under multiple banking' arrangement, should take coordinated action based on commonly agreed strategy, for legal / criminal actions, follow up for recovery, exchange of details on modus operandi, achieving consistency in data / information on frauds reported to Reserve Bank of India. Therefore, business unit /controlling office which detect a fraud should immediately share the details with all other banks in the multiple banking arrangements.

14. Attempted Fraud.

Cases of attempted fraud, where the likely loss would have been Rs. 100.00 lac or more, if the fraud would have taken place, are to be reported to Vigilance Department CHQ within 24 hours of the episode by all the operative levels. The reports on such attempted frauds is to b e placed before the Audit Committee of the Board. The report should cover the following:

- The modus operandi of the attempted fraud.
- How the attempt did not materialize in the fraud or how the attempt failed / was foiled.
- The measures taken by the bank to strengthen the existing systems and controls.
- New systems and controls put in the area where the fraud was attempted.

15. Reporting of Fraud Incidents Audit Committee of the Board/ Committee for Monitoring of High Value Frauds.

15.1. Vigilance Department CHQ should ensure that all frauds of `1.00 lac and above are reported to the Board promptly on their detection. Such reports should, among other things, take note of the failure on the part of the concerned business unit officials and controlling authorities responsible for the fraud, and appropriate action initiated against the erring officials/ officers.

15.2. **Quarterly Review of Frauds: Reporting to Audit Committee of Board**

As per the RBI guidelines , Vigilance Department CHQ would place quarterly review of frauds for the quarters ending June September and December before the Audit Committee of the Board of Directors during the month following the quarter to which it pertains. The quarterly review should contain supplementary material analyzing statistical information and details of each fraud so that the Audit Committee of the Board would have adequate material to contribute effectively in regard to the punitive or preventive aspects of frauds.

15.3. **Annual Review of Frauds**

Vigilance Division CHQ will conduct an annual review of the frauds and place a note before the Board of Directors for information. The report should be for the year ending March and is to be placed before the of end of June quarter every year. The main aspects which may be taken into account while making such a review may include the following:

- Whether the systems in the bank are adequate to detect frauds, once they have taken place, within the shortest possible time.
- Whether frauds are examined from staff angle and, wherever necessary, the cases are reported to Disciplinary Department for further action.
- Whether deterrent punishment is meted out, wherever warranted, to the persons found responsible.
- Whether frauds have taken place because of laxity in following the systems and procedures and, if so, whether effective action has been taken to ensure that the systems and procedures are scrupulously followed by the staff concerned.
- Whether frauds are reported to local Police or CBI, as the case may be, for investigation.

15.4. Annual **Review : Main Details.** The annual reviews should also, among other things, include the following details:

- Total number of frauds detected during the year and the amount involved as compared to the previous two years.
- Analysis of frauds according to different categories detailed in **Paragraph 4** and also the different business areas indicated in the Quarterly Report on Frauds Outstanding (vide FMR – 2).
- Modus operandi of major frauds reported during the year along with their present position.
- Detailed analysis of frauds of ` 1.00 lac and above.
- Estimated loss to the bank during the year on account of frauds, amount recovered and provisions made.
- Number of cases (with amounts) where staff are involved and the action taken against staff.
- Area/Zone-wise/State-wise break-up of frauds and amount involved.
- Time taken to detect frauds (number of cases detected within three months, six months and one year of their taking place).
- Position with regard to frauds reported to Police/ Crime Police / CBI.
- Number of frauds where final action has been taken by the bank and cases disposed of.
- Preventive/punitive steps taken by the bank during the year to reduce/minimize the incidence of frauds.

15.5. **Special Committee for Monitoring of Fraud Incidents.**

As per the RBI guidelines , Bank has constituted a Special Committee for monitoring and follow up of cases of frauds involving amounts of Rs.100.00 lac and above exclusively, while Audit Committee of the Board (ACB) shall continue to monitor all the cases of frauds in general. The major functions of the Special Committee[22] is to monitor and review all the frauds of Rs.100.00 lac and above so as to:

- Identify the systemic lacunae if any that facilitated perpetration of the fraud and put in place measures to plug the same.
- Identify the reasons for delay in detection, if any, reporting to top management of the bank and RBI.
- Monitor progress of CBI/Police investigation and recovery position.
- Ensure that staff accountability is examined at all levels in all the cases of frauds and staff side action, if required, is completed quickly without loss of time.
- Review the efficacy of the remedial action taken to prevent recurrence of frauds, such as strengthening of internal controls.
- Put in place other measures as may be considered relevant to strengthen preventive measures against

16. Reporting of Frauds to Law Enforcing Agencies : Police /Crime Branch / CBI.

16.1. While dealing with cases of fraud/embezzlement, it should not merely be motive to recover expeditiously the amount involved in the fraud, but should also be seen in the public interest so that the guilty persons do not go scot-free. As per the RBI guidelines, the following cases should invariably be referred to the State Police:-

- Cases of fraud involving an amount of Rs. 1.00 lacs and above, committed by outsiders on their own and/or with the connivance of bank staff/officers.

[22] The Special Committee is to be constituted with five members of the Board of Directors, consisting of MD & CEO in case of public sector banks and MD in case of SBI, its Associates and private sector banks, two members from ACB and two other members from the Board excluding RBI nominee.

- Cases of fraud committed by bank employees, involving funds exceeding Rs.10,000/-.

16.2 Fraud cases involving amounts of Rs.100.00 lacs and above should also be reported to the Director, Serious Fraud Investigation Office (SFIO), Ministry of Company Affairs Government of India, Second Floor, Paryavaran Bhavan, CGO Complex, Lodhi Road, New Delhi 110 003, in FMR-1 Format.

16.3 The vigilance Department CHQ, after scrutinizing each fraud case, would direct the concerned Business units/office to report the matter to the police /CBI, as the case may be, for further investigation.

16.4. Fraud Investigation : Need for Investigating Officer with Requisite Competencies. As the fraud investigation is a specialized function, the investigating officers should have vast experience, knowledge in the relevant field besides having investigation aptitude so that they could investigate the case in a professional manner. The HRD Department, Corporate Headquarters should place suitable persons at all S&C Divisional Offices as well as at S&C, Corporate Headquarters and Vigilance Department Corporate Headquarters.

16.5 Investigation of suspected fraud/fraud cases wherever required is to be got conducted through concerned S&C Division under whose jurisdiction the incidence of fraud has taken place. Wherever necessary, the Vigilance Department CHQ may also investigate the fraud incident at their own level keeping in view the sensitivity of the case.

16.6. The fraud investigation report should in detail discuss the modus operandi, lapses and indentify the person/s accountable for the loss to the bank. The investigation should be supported by necessary documentary evidences so that disciplinary proceedings and other action , as may be required under extant rules of the bank, is not delayed and the guilty person/s is/ are punished without loss of time .

16.7. The investigation report is to be analyzed by the officials/ officers posted at Vigilance Department CHQ and inter-alia appropriate action initiated for plugging the lacunae and strengthening the systems and procedures to avoid recurrence of similar incidents.

17. **Training to Investigating Officers for Forensic Scrutiny/ Audit.**

17.1 As per the RBI guidelines, Fraud investigation requires competence in 'forensic audit' and also technical / transactional expertise. In this regard, banks were advised to take immediate steps to identify staff with proper aptitude and provide necessary training to them in forensic audit so that only such skilled staff is deployed for investigation of large value frauds. HRD Department may take necessary initiative in this regard.

17.2 In order to enhance the skill and competence of the investigating officers, continuous training would be imparted to them at various reputed colleges. To expose the investigating officer in forensic audit as per the RBI guidelines, HRD Department should explore possibility of deputing the officers for appropriate training at the approved centers in the country.

18. Settlement of Customer Claims in Fraud Cases.

18.1. It would be endeavor of the Bank to settle the customer's claims expeditiously. A screening committee at CHQ level would be constituted, which would examine the proposal to be initiated by Vigilance Department CHQ after analyzing the investigation report. The committee would place its recommendation to the appropriate Sanctioning Authority as per the powers as proposed below:-

a) *The delegated powers per account/group at various levels are proposed as under:*

S. No	*Sanctioning Authority*	*Limit*
1	*Management Committee (Board)*	*Full Powers*
2	*Chairman*	*Rs. 50.00lacs*
3	*President (Vigilance)*	*Rs. 5.00lacs*
4	*Vice President (vigilance)*	*Rs. 1.00lacs*

b) Constitution of Screening Committee at CHQ is as under:

S. No	*Sanctioning Authority*	*Constitution of screening committee*
1	*Management committee*	1. Chairman 2. President (vigilance) 3. President (law)
2	*Chairman*	1. President (vigilance) 2. Vice President (law) 3. Vice president (vigilance)
3	*President*	1. Vice President(Vigilance) 2. AVP/Ex. Manager (Vigilance) 3. AVP/Ex. Manager (Law)
4	*Vice President*	1. AVP/Ex. Manager vigilance 2. AVP/Ex. Manger Law

18.2 Claim amount should be paid to the bona-fide account holder by debit to ***Operational loss A/c Frauds//Dacoity (other Assets)*** against indemnity bond and stamped receipt to be obtained from the claimants for full and final settlement of the claim. Yearly statement of the cases with powers exercised by the respective authorities should be placed before the Board of Directors during the first quarter of the succeeding year.

18.3 In case of Government / Public Sector Undertaking (PSU) and highly reputed Customers, Chairman is authorized to waive the condition of obtaining of indemnity bond and stamped receipt for full and final settlement of claim.

19 . Staff Accountability.

One of the aspects of detection of a fraud is to identify the erring official/s and conclude the disciplinary action/ departmental action expeditiously especially where the staff involvement is evident. The punishment commensurate to omission and commission should be awarded to such Official/s found directly involved in perpetration of fraud. The punishment awarded should have demonstrative effect on others. Disciplinary /HRD Departments should follow up for staff side action so that the same is finalized within the time schedule.

20. Recovery of Fraud Amount.

20.1 The branches as well as controlling offices should make all efforts immediately after the fraud comes to lime light to recover the defrauded amount from the fraudsters. A systematic approach would be adopted in this regard as explained below;
20.2 It would be logical to see to it that the assets created by the fraudsters with banks may not belong to the fraudsters. If the money trail is traced, the law department will take necessary steps for attachment of the assets. Trace other assets if any available with the fraudsters
20.3 Recovery through appropriation of Provident Fund of fraudster employee/pension of employees/stopping of pension of the employees as per rules.
20.4 Freezing of the amount credited in miscreant's account through fraudulent transfer of funds and steps to be taken for restoration of the same to the victim's account.
20.5 Immediate hot listing of ATM/debit Cards issued to the account where the fraudulent funds have been transferred.
20.6 Coordinated approach with collecting Banks in respect of frauds involving forged instruments paid through clearing.

21. Prevention of Frauds: Some Suggested Measures.

For prevention of fraud incidents, the following measures are inter-alia are suggested for compliance:

i) A strong internal control framework is the strongest deterrence for frauds. The appropriate systems and procedures are well laid down for preventive mechanism;
ii) The fraudsters generally take advantage of lacunae at the compliance level. Stress should be laid down on adherence of prescribed systems, procedures and guidelines issued by the various departments from time to time. Wherever the loopholes would be observed, or compliance are found inadequate necessary guidelines be got reiterated from the concerned department for strict compliance;

iii)The executives at Zonal Office level shall verify level of compliance during their surprise visit to the business unit/offices. The internal inspectors have standing instructions to comment on the same;

iv) In order to alert the staff against the incidence of frauds, modus operandi of peculiar fraud cases on behalf of other banks and also in our bank, are being circulated to the business units/offices along with preventive measures to be taken to prevent such attempts in future;

v) Details of lost instruments are circulated to the business units to check the possible misuse of the instrument by the fraudsters;

vi) Regular training programs on ***"Frauds Prevention and Detection***" shall be conducted at all Training Colleges of the bank for all the cadres so that the staff is well versed to avert frauds. Besides **"fraud awareness week"** shall be observed every year so that proper awareness and sensitivity is created amongst the staff across all the bank about the efficacy of fraud prevention/ detection/ its timely reporting to the concerned levels;

vii) Special Workshop would be conducted at all Zonal levels where the staff would be made aware about their responsibilities in averting the fraud incidents with suitable case studies;

viii) Customer-centric approach continues to be the guiding principle of our organization at operational as well as strategic levels. All the modern means of communication like print media, electronic media and online social media are to be used to inform customers to effectively use banking services. Fraud prevention messages and requisite security tips regarding tokens, ATMs, E-banking, Credit Cards and other services are to be given wide publicity to ensure minimization of risk. These messages in highly comprehensive and customer-friendly format will be published through print media in the form of notices and through electronic media in the form of 10-20 second capsules. Outdoor publicity means like distribution of posters, brochures and pamphlets will also be used to spread awareness about fraud incidents. Besides, the information will also be put to display on Notice Boards in business units;

ix) The system of credit audit & concurrent audit is to be suitably strengthened to prevent the frauds in all borrowal accounts in general and the large value borrowal accounts in particular;

x) The compliance to extant guidelines issued through various policy documents including bank's latest Credit Policy issued by various departments at CHQ in respect of both daily banking operations as well as loans and advances are to be scrutinized by the concurrent auditors and internal inspectors during their monthly and RBIA(Risk Based Internal Audit) respectively ;

xi) Balancing of un-reconciled accounts at some business units with the general ledger balances should be got done promptly;

xii) Daily checking of supplementaries and related vouchers is needed. Despite repeated instructions, this area, at times remains unattended in some business units. Serious efforts need to initiated for its strict compliance;

xiii) The blank passbooks, cheque books, deposit receipts, specimen signature cards and other important documents should be done in the custody of a responsible officer;

xiv) Balance confirmation should be obtained from depositors/ borrowers periodically;

xv) Periodic rotation of duties among staff needs to be reiterated/ ensured at business unit level so that there is not only skill development of staff by handling different jobs but also overdependence on some staff and over-stay of one official/ officer at a certain place is completely ruled out;

xvi) ***Timely rectification of RBIA / snap inspections/ concurrent audit reports / LFAR/ statutory audit reports/ CAG audit reports etc. is to be ensured by the Business unit Head, Manager Credit and Hall-incharge. It shall now be their joint & several responsibility and in case of untoward incident of actual or attempted fraud is noticed suitable action against them will follow under rules*** ;

xvii) Deficiencies pointed out in various inspections & audit reports need to be taken seriously and got rectified. Many a times, the inspecting officials bring out irregularities in various areas of functioning and a critical analysis of these observations is required to initiate preventive steps in the highlighted areas of deficiencies. We could bring about more meaningful improvements by focusing on areas such as systems/procedures, IT systems, Integration and data flow etc.

xviii) ABC Analysis of Vulnerable Fraud Areas.. In the present days diversified /complex banking scenario a constant review of existing Systems and Procedures including manuals and identifying vulnerable areas on a dynamic basis are a must. An ABC analysis through categorization of functional areas may be taken up as under – A – Most Vulnerable B – Vulnerable C – Less Vulnerable The focus of course should be more towards 'A' Category functional area;

xix) Cases of Willful Default : A Criminal Offence. It is no secret that Banking Sector as a whole is saddled with high value NPA accounts involving high profile borrowers who have taken away thousands of crores of lendable resources besides adversely affecting the income / profit portfolios of the banks. Under the RBI norms issued in July 2012, a willful default is said to have happened when either a borrower has not paid the bank even if he is in the capacity to repay, when the funds sanctioned by the bank have been diverted by the borrower for other purposes, when the borrower has siphoned off funds sanctioned by the bank or when the borrower, without knowledge of the lender, has disposed of the property or moveable assets which were pledged for availing the loan. Every such wilful default for the reasons mentioned above, should be made a criminal offence to have a deterrent effect on misuse / diversion of funds by high profile borrowers.

xx) Action against Third Party Entities : Chartered Accountants / Credit Rating Agencies/ Advocates / Valuers' etc. A notable feature of huge NPAs faced by Banks, at present, is that the companies rated as 'AAA' by External Credit Rating Agency (ECRA) were downgraded to 'D' within a short span of time. Similarly, many cases of frauds have been detected where, the companies submitted manipulated financials /Balance Sheets certified by Chartered Accountants and also got their properties overvalued which enabled them to avail substantial financial assistance from PSBs. In such cases, when the account turns into NPA / identified as fraud, these third party entities often get away without any punitive action. The general experience is that the concept of 'Self regulation" under which these professionals work has not been very effective in the past. Hence, punitive criminal action for wrong certification / rating will certainly act as a deterrent on such collusions by third party entities.

xxi) Credit Proposals: Approval of Deviations: There are instances where credit proposals belonging to high profile companies / individuals were received which requires prior approval of the competent authority for approval of the deviations in credit policy. The powers to approve such policy deviations in the credit proposals without any upper cap /ceiling as of now are vested with the Board level committees. For example: There is an instance where approval was accorded by the Board level committees with the following policy deviation in the credit proposal: Debt/ Equity ratio more than 100:1 against the norm of 2:1 implying the borrower is highly overleveraged Debt Service Coverage Ratio (DSCR) of 0.50 : 1 against the norm of 1.5:1 implying that the revenue generation is just 50% of the loan installment and interest to be repaid It later transpired that the account turned into NPA and one of the reasons attributed was that the company was already in the debt trap and 'approval of deviation' by the Board level committees should have been avoided. Therefore, there is a need for bringing a cap /upper ceiling for approval of deviations to be prescribed even for Board level committees.

xxii) The Forensic Audit capability to be Improved: In view of large number of high-value NPAs/ Frauds coming to light, there is a need for forensic audit of accounts. Forensic Audits undertaken by private audit firms have not been effective. These firms often charge exorbitant fees without concomitant benefit to the banks. Therefore, the Forensic Audit capability of CBI needs to be improved. This becomes all the more important in view of RBI guidelines with reference to 'Red Flagged Accounts'. The CBI may also take Bank staff (Chartered Accountants) on deputation, which would improve the quality of investigations by bringing in more domain expertise. It is also suggested that teams of bank officers may similarly be trained in Investigations (by the investigating agencies) so that their Forensic Audit capabilities can also be harnessed/ made use of by the respective Banks for their immediate and emergent needs.

xxiii) Diversion of Sale Proceeds by Borrowers: It is observed that in most of the cases, the borrowers have opened Current Accounts in other banks outside the consortium / multiple lending arrangements and diverted the sales proceeds resulting in the account becoming NPAs for the lending member institutions. The Public Sector Banks (PSBs) are finding it difficult to obtain the required information on diversion of funds from the Private Sector Banks / Foreign Sector Banks especially in respect of high value credit limits. This is due to the non-cooperation on the part of these banks, citing confidentiality of customer relationship. Therefore, sharing of information with Public Sector Banks, especially in case of recalcitrant/ defaulting borrowers, should be made mandatory. All banks, irrespective of the sector (public/ private/ foreign) deal with public money and defaulting borrowers are a threat to the entire economy of a country. Hence, a suitable modification / amendment to Banking Secrecy clause, if required, may obviate this problem.

xxiv) Fraud in one Bank to be treated as a Fraud in all Member Banks. A fraud involves the basic concept of 'mens rea' – hence a borrower who has been found to have committed fraud at one of the member banks of a consortium would automatically have the preponderance of committing fraud with other member banks also, though there may be a time lag. Currently, individual member banks are focusing on accounting entries in their books of accounts before declaring the account as fraud (though they are members of the same consortium/ multiple lending) and not considering a holistic view of the borrower being fraudulent. A study has revealed that there is considerable delay in declaring the account as fraud between the members of consortium. The delay between the first and the last bank in declaring the account as fraud could be as long as 24 months. Hence, fraud in one bank should be automatically treated as fraud in all member banks. This would facilitate lodging of complaint with CBI and initiation of concerted recovery measures without loss of time. It has been seen that the delay is mis-utilized by borrowers for asset stripping.

xxv) Issues faced after Sale of Assets to ARCs. Issues faced after Sale of Assets to ARCs: There are instances where fraud has been detected in a borrowal account after the sale of assets to Asset Recovery Companies (ARC). However, banks are reluctant to declare the account as fraud out of fear that this would jeopardize the likely recovery prospects by the ARC, besides creating legal complications. 4 5 6 7 The issue that needs to be understood is that 'Sale to ARC' is not an absolute sale ie the Banks continue to retain the risk of loss of funds unless the ARCs are able to find a suitable buyer for the assets and redeem the security receipts. Hence, any delay/ non-disclosure of fraud, subsequent to 'sale' to ARC, only further increases the pain for the bank since it continues to pay defined 'maintenance fee' to the ARCs for an asset that does not exist/ is fraudulent. Thus, the Bank continues to 'throw good money after bad'. Further, any delay in declaration of fraud will have its adverse impact on the recovery from assets already assigned, part of which may be genuine. In view of the above, clear directions are required for further course of action in all such cases where fraud is detected / declared subsequent to 'assignment of assets to ARCs'.

xxvi) Access of Income/ Sales/ Tax details to Bankers. It has been experienced that fraudulent borrowers maintain multiple books of accounts to defraud the banks. However, in general, they are particular about submitting the correct figures to the tax authorities as they do not want to be on the wrong side of the tax officials due to the likely stringent criminal penalties. In contrast, the bank cases, if filed, take years of litigation by which time the borrower strips all her/his assets. Hence, if a provision is made to inter-link the Income Tax/ Sales Tax / VAT web-sites and access made available to Bankers so that all the details such as IT /ST / VAT details can be verified at one instance, it would drastically reduce the probabilities of incidence of frauds, as the manipulation in figures/ data submitted by potentially fraudulent borrowers gets immediately detected. It should be remembered that Banks are dealing with public money and any loss to Banks has a ripple effect across the economy including higher interest rates, non-availability of credit to genuine borrowers etc which directly affects the growth of the country.

xxvii) Job Rotation for Staff . In many frauds that have come to light, it is found that staff members who indulged in fraud appeared to be very sincere workers and always helpful to the superiors / customers. They had not availed any leave over the years. Therefore, ensuring availment of leave at periodical intervals by all staff members, leading to automatic job rotation, is seen as one of the most important preventive vigilance measures. Despite clear instructions from RBI, the implementation of availing mandatory Leave by the staff has not been ensured in many Banks. Enforcement of the same is required.

xxviii) Moral Suasion of Corporate Borrowers by Chambers of Commerce. It is common to see high profile individuals / Corporate clients who despite having their accounts under NPA status (with several Banks), continue to enjoy preferential treatment / attention and various benefits at Chambers of Commerce. The Chambers of Commerce play an important role in development of a rule based corporate culture in the country. Hence, in order to bring in value based corporate norms, such unwarranted preferences / benefits to these high profile willful defaulters should be avoided by prevailing upon the Chambers of Commerce for Moral Suasion.

xxix) Allocation of Unique Property ID: A large number of frauds have been perpetrated in housing loans and other loans against immovable properties, through submission of fake titledeeds, fake or multiple mortgages etc. Though, the centralized CERSAI database developed for registering the charge on immovable properties which have been assigned to banks, the registration process is handicapped, in the absence of a unique property identification number in the country, as no data validation is taking place whenever any property is registered. This defeats the very purpose of having a centralized database as multiple mortgages can be registered on the same immovable property in the database. Hence, it is suggested to allocate a Unique Property ID for every property (especially residential property) in the country which would be of immense help to the Bankers by eliminating the risk of fraud through multiple mortgages.

xxx) Verification of Information submitted by Borrowers. The power of the internet should be harnessed effectively by the bankers. There are several web sites[23] which can be browsed for verification of KYC documents / other vital information on the existing clientele / borrowers. These websites should be made more familiar so that the due diligence part is taken care of at the initial stage of loan processing itself.

xxxi) Aggregated data for Identifying Commonality of Interest. There is a need to develop a website that would provide aggregated information on individuals listing the details of companies where an individual is a Director, based on her/ his DIN number. Similarly, aggregated information on the various group/ associate/sister concerns of a company based on say, CIN number is essential, since operationally there are limitations in identifying the group concerns as defined in terms of RBI guiding principle "being commonality

[23] Some of the important websites are : 1 https://incometaxindiaefiling.gov.in-> PAN – of the borrower- of the employer Select your jurisdictional A.O. as per Form -16 2 https://incometaxindiaefiling.gov.in-> TAN– of the borrower Select know your TAN - of the employer as per Form -16 3 https://www.tinxsys.com/TinxsysInternet TIN of the borrower 4 https://cbeceasiest.gov.in/EST Service tax registration of borrower 5 https://contents.tdscpc.gov.in/ Verify with 7 digit certificate number on form 16 (Non-traces) check with the employer /deductor. Probe deeply 6a https://incometaxindiaefiling.gov.in -> Income tax return electronically filed by Select-> ITR-V Receipt Status the borrower. 6b Income Tax Return filed manually at ITO Probe deeply–CA's certificate cross verification 6c If income tax return shows tax as payable, please obtain & verify TAX paid challans. 7 MCA website - Ministry of Corporate Affairs To verify Financial Statements; Registration of Charge details; Minutes of Annual General Body meeting; Change of Directors etc 8 " Aadhaar Verification Services" at http:/ Checking of a keyed-in 12 digit number of resident.uidai.net.in/aadhaar verification Aadhaar data base & other particulars. 9 http://www.icai.org/new_post. To verify the details of Chartered html?post_id=1812&c_id=92 Accountants who have audited/ verified the submitted documents

of management and effective control". Hence an aggregated holistic view would ease the work of all bankers/ investors who need the information on group concerns.

xxxii) Joint Credit Auditors Forum & the Chief Vigilance Officers' Meet : Every Bank has an internal system of periodic Credit Audit of high value borrowal accounts under Standard category. In the current system, the credit audit findings/ irregularities are in disaggregated forms with each credit auditor having access to the books of accounts/ transactions of her/his respective bank in the consortium. Hence, an aggregate view of irregularities and inter-bank movement of funds is not available to the consortium members. Though, the operational/ branch functionaries of consortium members do meet at periodic intervals, their focus is more on business development. Therefore, there is a need for a regular meet of Credit Auditors in case of Standard category accounts also, to have an effective insight into every aspect of a borrowal account such as deficiencies in appraisal / sanction / conduct and compliance to terms of sanction. This would work as an 'Early Warning Signal' for the consortium to take effective remedial steps, before the account turns into NPA. On similar lines, the Chief Vigilance Officers' meet, of consortium members, also should take place at regular intervals particularly with regard to high value NPA accounts for taking a common approach towards identification of irregularity, staff lapses and probability of occurrence of fraud.

22. Provisioning for Fraud Cases.

Provisioning for loss, as per the extant RBI directions, applicable to fraud cases both in borrowal & non-borrowal cases should be made by Balance Sheet & Taxation Department, Corporate Headquarters in consultation with the Vigilance Department CHQ . For this purpose there will be close coordination between the two departments.

23. One Time Settlement / Write Off of Fraud Cases.

All out efforts are to be made for recovery of fraudulent amount and where recovery is difficult in ordinary course, chances of recovery through OTS must be explored. OTS in borrowal fraud accounts will be considered in terms of policy formulated by Remission & Settlement Department CHQ from time to time. OTS in non-borrowal frauds will be considered in consultation with Vigilance Department CHQ. Similarly, borrowal fraud accounts will be written off in terms of related policy document from IAPM, Department Corporate Headquarters, while as non-borrowal fraud would be written off by the bank in consultation with Vigilance Department, after seeking approval from the Board.

24. Closure of Fraud Cases.

24.1 As per the RBI guidelines, closure of fraud cases is considered only after completion of action on the following parameters;-

(a) The fraud cases pending with CBI / Police / Court have been finally disposed off.
(b) The examination of staff accountability has been completed.
(c) The amount of fraud has been recovered or written off.
(d) Insurance claim, wherever applicable, has been settled.
(e) The bank has reviewed the systems and procedures, identified the causative factors, plugged the lacunae and the relative facts have been certified by the appropriate authority (Board / Audit Committee of the Board).

24.2 For limited statistical /reporting purpose as per the guidelines of RBI , the bank should take steps to close all those frauds cases involving amount upto Rs. 25.00 lacs, under relaxed norms where:

- the investigation is on or challan / charge sheet not filed in the Court for more than three years from the date of filing of First Information Report (FIR) by the CBI / Police, or
- The trial in the courts, after filing of charge sheet / challan by CBI / Police, has not started, or is in progress.

However, all such cases will be eligible for closure subject to the fulfillment of other conditions indicated at items (b) to (e) in above.

24.3 In every fraud case, status of completion of action on all parameters applicable for closure should be placed before Board/ACB for certifying that bank has reviewed the systems and procedure , identified the contributory factors and plugged the lacunae. After approval from the Board /ACB recommendation would be made to Regional Office RBI as per the standing instructions for closure of the fraud case.

In closure of fraud cases, the bank will be complying with the above broader guidelines of the RBI.

25. Ownership of Policy Document on Fraud Risk Management.

RBI directions provide that the fraud risk management, fraud monitoring and fraud investigation function must be owned by the bank's CEO, Audit Committee of the Board and the Special Committee of the Board.

26. Other RBI Directions on Frauds.

Banks shall send the Fraud Monitoring Returns (FMR) and data, based on the Frauds Reporting and Monitoring System (FRMS) supplied to banks, under the signs/ email of a specifically nominate official of the rank of General Manager who will be responsible for submitting all the returns to the regulator.

27. Timeline for Completion of Investigation in Fraud Cases, Fixing of Staff Accountability and Other Related Issues.

27.1. In its meeting dated 20.07.2017 the Board of Directors directed to frame a policy document for prescribing time-lines for completion of investigation of Vigilance Cases and fixing of Staff Responsibility for arresting incidence of pendency of such cases . In compliance to these directions for further streamlining the existing process & procedures of investigation of Vigilance Cases in a time-bound manner for their logical conclusion, the time-lines are proposed & tabulated below:

S. No.	**Event**	**Time-line**		**Cumulative Period**
		Start Time	**Time taken for Accomplishment of Task**	
Stage 1: Investigation of the Case & its Analysis at Vigilance Department, Corporate Headquarters.				
1	Directions for Investigation from Vigilance Department	0 Week	1 Weeks	1 Week
2	Conducting of Investigation in the concerned Business Unit/ Office	1/2 Week after instructions	3 Weeks	4 Weeks
3	Submission of Investigation report to Vigilance Department/ Corporate Headquarters	0 Week	1/2 Week	4.5 Weeks
4	Seeking of Clarification and / or further Information on various aspects of the Case	0 Week	1/2 Week	5 Weeks
5	Analysis of Investigation Report at Vigilance Department	0 Week from the date of receipt of last set of Information from concerned S&C Division/ Business Unit	2 Weeks	7 Weeks
	Total Time Consumed in Vigilance Department for the official/ officer to submit report to higher authorities for approval / instructions.			**7 Weeks**
Stage 2: Approval of the Case File.				
	Approval for the Proposal : (a) Within the Powers of the President/ Sr. President/ Executive President;	0 Week	1/2 Week	**7.5 Weeks**
	(b) Within the Powers of the Chairman	0 Week	1 Week	**8 Weeks**

6	Compliance of Actionables in case the file is to be retained at Vigilance Department itself	1 Week after receipt of file from the President/ Chairman's Office.	8 Weeks	**16 Weeks**
Stage 3: At Disciplinary Department.				
7	For preparation of charge-sheet after receipt of file from concerned department. complete in all respects including evidences	1/2 Week	4 Weeks maximum after receipt of final documents/ file from Vigilance Department	12 Weeks (as the file is assumed to be received from Vigilance Department within 03 working days from the date Vigilance Department received the file from Chairman's Office)
8	For submission of reply by charge-sheeted official after receipt of charge-sheet/show cause notice	1 Week	2 Weeks	15 Weeks
9	For analysis of reply of charge-sheeted official	1/2 Week	1 Week	16 Weeks
10	For completion of departmental enquiry & submission of report thereof by the Enquiry Officer(This process is also dependent upon cooperation of the CSO and his defence during enquiry).	0 Week	12 Weeks	28 Weeks
11	For evaluation of report of Enquiry Officer & preparation of Show Cause Notice for proposed punishment	0 Week	1 Week	29 Weeks
12	For personal hearing to the charge-sheeted official after receipt of reply (Usually within 10 days subject to availability of Disp. Authority)	0 Week	1.5 Weeks	30.5 Weeks
13	For final order after personal hearing	1/2 Week	2 Weeks	32.5Weeks
14.	**A+/- : 10% on account of Standard Deviation**		3.25 Weeks	**36 Weeks**

27.2. **Conducting Investigation : Processes & Procedures.**

While conducting investigations in fraud incidents, the following instructions would inter-alia be taken care of:

- Instructions for Conducting Investigation: Fairness, Respect & Dignity.
- Accountability regardless of Position & Power.
- Investigation to be conducted with Highest levels of Integrity, Professionalism and Independence.
- Review & Evaluation of Evidences / Documents by the Investigating Officer.
- Coverage of Critical Areas : All critical & vital areas of a fraud incident will be covered and captured in the investigation report with supporting documents/ evidences and papers.
- Differentiating Non-sustainable Findings vis-à-vis the Sustainable Ones: While preparing an investigation report due care must be taken by the investigating officer on this aspect .

- Personal Interviews/ Contacts and Written Statements. These should be obtained by the investigation officer wherever deemed necessary for taking an objective view of the case under investigation.
- Disciplinary Proceedings. Wherever deemed necessary and depending upon the sensitivity and severity of the fraud incident, the case may be recommended for initiating disciplinary proceedings so that the staff side action is completed and issues taken to final/ logical end.

a. Fraud Angle Complaints : Disposal of Cases within A Month's Timeline.

In case any complaint received for dealing with the fraud angle of any attempted/ actual fraud incident, is apparently found to be genuine, the following procedure will be followed in its disposal:

- Confirmation of Receipt to the Complainant.
- Primary Investigation with 10 Days.
- A view to be taken by the Vigilance Department as to whether administrative (lapses in processes & procedures) or criminal investigation is needed.
- Final Report: Within 30 Days to be finalized.
- Complainant to be informed as per the nature of the complaint.

b. **Cases with Apparent Fraud Angle**.

In situations where there is apparent fraud angle to a fraud case , it would be got immediately investigated and such suitable action against erring staff will be taken as is deemed necessary before and after closure of the investigation process.

28. Conclusion.

Recently, a few regulatory changes were introduced to improve transparency and promote ethical business practices. With the introduction of the Black Money (Undisclosed Foreign Income and Assets) Imposition of Tax Act, 2015, the Benami Transaction (Prohibition) Amendment Bill, 2015, and the Companies (Amendment) Act, 2015, measures are in place for the penalization of prohibited and unethical business activities. These are steps in the right direction

To control, contain and manage frauds, it is essential to develop a strong culture of ethics & compliance in the organization in which employees consider themselves as the main stakeholders and are aware of the risks associated with occurrence-&-impact of frauds so that they remain always alert to situations and events in their respective operational areas by intuitively analyzing the factors and forces that give rise to fraud-like incidents as their alertness & presence of mind will be the first deterrence to prevent occurrence of frauds and/ or attempts-at-frauds. They need encouragement & proper training for using banking reporting mechanism like "Whistle Blower" framework in a responsible manner. We also need to nurture an atmosphere of trust in which staff would not fear for raising a "red flag" incident. Once an alarm is sounded proper prompt action is needed to inquire and investigate. These steps would not , in themselves, put a stop to fraudsters because fraud is an "elusive and cunning enemy that needs a risk-aware culture to keep it in abeyance."[24] When every employee and every stakeholder is vigilant and readily contributes proactively in prevention/ timely detection of fraud incidents, fraud incidents will surely subside.

[24] KPMG: Global Profile of the Fraudsters

29. Main Annexures

Annexure "A"

Snapshot of Fraud Cases of J & K Bank Limited from FY 2014-15 to FY 2016-17

(Amount in lacs)				
Financial Year	**No. of fraud Incidents**	**Amt involved**	**Amt recovered**	**Net loss**
2014-15	12	90289.54	19799.06	70490.48
2015-16	19	1239.73	133.71	1106.02
2016-17	25	31166.64	20552.83	10613.81
TOTAL	***56***	***122695.91***	***40485.60***	***82210.31***
Large Value Frauds	***13***	***121834.08***	***40115.65***	***81718.43***

Annexure "B": Ethical Code of Conduct/ Behavior of J&K Bank Employees

i) **Codes of Conduct: Introduction**. Codes of Conduct or Codes of Behavior are designed to anticipate and prevent certain specific types of behavior; e.g. conflict of interest, self-dealing, bribery, and inappropriate actions. The rational for a written code is that it is necessary to both protect the employee while at the same time protecting the reputation of the bank and its various stakeholders. Standards of Conduct do change over time but it is sometimes useful to look at historical standards in order to recognize that the behavioral problems are often similar over time but technology or social circumstances can have a profound impact on actions that are prohibited.

ii) Main Parameters of Our Ethical Code of Conduct / Behavior .

1) **Integrity** underpins everything that we do at the Bank. We want to ensure that the Bank is a place where people always do the right thing for the institution and our mission. It is a place where we all collaborate and support each other in working for the public good.–
2) The Bank has an **inclusive working environment** where difference is celebrated and discrimination or harassment is not tolerated.
3) We **act with impartiality**. We want to be objective in our decision-making and decisive in our actions.
4) Our nature of services necessitate us **to be open and accountable** for our actions and for the resources we use.
5) Finally, we should **feel empowered** to hold each other to account. We believe that, in all of our interactions with each other, with external stakeholders and with J&K State Government / Central Government/ RBI/ other regulators , we have an opportunity to enhance public trust in what we do and set the best ethical and professional tone for the financial services industry we operate into.
6) We should all feel encouraged and empowered to make positive suggestions, and our expectation is that each of us would do so when necessary, including challenging what we do or how we do it if we see a conflict with our values and our Code. We would encourage our colleagues to 'Speak up' if they believe that our Code is being breached.
7) Our Code applies to all of us (all stakeholders of the bank) including all bank colleagues from across the full range of the business.
8) The values and the expectations embodied in our Code are not new. Our Code encompasses our core ethics policies; seeks to highlight, bring together, and update certain other key existing policies we all are already familiar with and provide context for them.
9) Living within our Code is not simply about observing the letter of the policies referred to in it; they cannot provide for every contingency. We aspire to set an example of the best in banking service: complying with our Code is about understanding and embracing the principles and spirit behind it. In doing so, each of us will make our individual contribution to the Bank's business objective and strategic policies and decision to achieve all business targets in sync with the corporate responsibility that we owe to the individuals and entities outside the bank.
10) Our Code represents our commitment to how we work at the Bank and how we should conduct ourselves (both within and outside the Bank). It applies to all of us i.e. to all employees at operational and administrative/ management level.
11) Our Code will be publicly available on bank's intranet and provides a statement about the behavior our colleagues, counterparties, stakeholders and the public should expect from us.
12) Our Code is based on ***five principles***. These represent the spirit of our Code. These are briefly listed below:

    - **Acting with integrity**

    Integrity is one of the principles of public life, closely related to the principles of selflessness and objectivity. Our personal interests should never influence our decisions at work, and we must be free of any suggestion of inappropriate influence.

- **<u>Creating an inclusive Working Environment.</u>**

We stand for an inclusive environment, and we welcome the benefits that diversity brings. We want an environment where all colleagues feel comfortable being themselves. We support diversity as part of what we do every day. We established our Bank wide values in the Strategic Plan: collaborative, inclusive, decisive, open and empowering. These are embedded in our performance management and development approaches. Both what we do and how we do it, contribute to our performance as individuals and as an institution. We believe in inclusive and collaborative behaviors. We believe in a meritocracy where all get developed, promoted and rewarded fairly. We have a well-established grievance procedure as well as the option for colleagues under whistle-blower framework. Any of us who believe that we have been discriminated against, harassed or bullied or have seen anyone else be the victim of discrimination, harassment or bullying, should feel empowered to raise the matter through appropriate forums/ means provided by the bank.

- **<u>Demonstrating Impartiality.</u>**

We take pride in the quality and impartiality in our dealings and functioning . We engage with others professionally and make decisions fairly and on merit, using the best evidence available and without bias. We recognize that impartiality and objectivity are crucial to the decisive behaviors that form a core part of our Bank values. We know that our reputation for impartiality and independence is vital to our effectiveness, and, if lost, would be hard to recover. Like other colleagues in the banking industry, we know we must be seen to be apolitical and must never allow ourselves to become open to the perception that our decisions have been inappropriately influenced.

- **<u>Being open and Accountable.</u>**

We want to be open and accountable to each other and in our dealings with all our stakeholders including our valued customers .We know our decisions and actions both as individuals and a corporate entity are subject to public scrutiny and we must welcome and facilitate that scrutiny. Open behaviors, practiced every day by all of us, are a core Bank value and are integral to the success of the Bank and its business objectives. We are responsible for the resources and information entrusted to us in the work we do and we have to be accountable for managing those with due care, skill and diligence. We are accountable for engaging with our colleagues constructively and recognize when we should reach out to them. Good record keeping is vital; records represent our institutional memory and allow for proper questioning. In the course of our work at the Bank we make critical policy, supervisory and operational decisions that have a broad impact. We are ultimately accountable to the various stakeholders of the bank for those decisions and we owe it to them as well as to ourselves and each other to properly and securely maintain our records. We all have a responsibility to ensure our records are authentic, accurate, timely, complete, appropriately classified, and retained in line with our records management policies. At the Bank we have access to a wide variety of information which exists in many forms: printed or written on paper, stored electronically, transmitted by post or using electronic means, shown on films, or spoken in conversation, including information regarding access to systems and software versions, processes and passwords. In the wrong hands that information could be used to disrupt or damage our ability to pursue our business objectives. We all have a responsibility to protect that information. When accessing Bank information electronically, we should only use the Bank's devices and systems and Bank-approved software. We must use these safely and securely.

- **<u>Feeling Empowered.</u>**

One of the five values in our Strategic Plan is empowerment and one key aspect of that, the ability to speak up through Whistle-blower mechanism about something that is causing us serious concern, is embedded in our Code. Each of us should feel encouraged to raise serious issues or concerns, whether they relate to the behavior or practice of a colleague which we believe might be in breach of our Code, or to information that could suggest misconduct by external market participants. Our values explicitly seek to encourage an environment where a diversity of opinions and views are brought to bear on all the decisions we need to make. Our approach to performance management recognizes that how we do our work is as important as what we do, and we should all feel encouraged to raise concerns if we feel our values are not being adhered to.

We want to make sure that everyone fully understands what is expected of them and what they need to do to adhere to our Code.

Failure to comply with our Code and its associated principles / policies could lead to disciplinary action.

Annexure "C" : Suggestive Steps towards Preventive Vigilance

1. Checklist of Main Areas Prone to Fraud Incidents.

* Cheque payment frauds, including insertions/alterations in payee, amount payable, date, signature of the drawer/s.
* Misuse of passwords.
* Frauds in staff accounts.
* Cash shortages.
* Misappropriation of funds.
* Depositing less cash in accounts of account holders.
* Not accounting for cash received from customers in books of accounts.
* Opening bogus accounts for en-cashing stolen cheques and other banking instruments.
* Debiting Branch office accounts without any cogent reasons and proper justification.
* Fraudulent transfer of funds to 3rd party accounts without any supporting vouchers / mandate.
* No pre-sanction inspection carried out.
* Proper inspection of units, assets created out of bank funds and margin of the borrower not ensured.
* Second, periodic inspection of the unit and the mortgage property was not carried out.
* Registration of property under CERSAI not done.
* Proposals processed very casually, like,
    (a) Projected sales disproportionately higher.
    (b) Financial ratios below acceptable levels.
    (c) Financial position on provisional profit and projected profit not analyzed.
    (d) No justification / comments were offered for ignoring above vital parameters.
* Failure to obtain status report of the project at the time of processing of the credit proposal and thereafter.
* The credit rating was not assessed and analyzed for impact-analysis.
* CIBIL reports were not generated and scrutinized.
* KYC documents not verified with originals and authenticated by the branch functionaries.
* Exceeding delegated authority.
* Title Search reports not scrutinized.
* Failed to obtain original documents required for creation of equitable mortgage.
* End use of funds not verified.
* Stock statements / book debt statements not obtained.
* Not regulating/ marking of drawing limits as per actual stock / book debt statements.
* Allowing disbursement without complying with terms of sanction / pre-

disbursement conditions.

* Allowing overdrafts and overdrawings beyond delegated authority.
* No ratification for exceeding delegation of powers obtained.
* Credentials of suppliers not verified. In some cases the borrowers managed to take reimbursements of loan amounts from suppliers and goods were not supplied.
* Lack of proper diligence on the borrower and guarantors.
* Insurance of the assets financed by the Bank not done.
* Undue accommodation of borrower without any cogent reasons and proper justification.
* No post sanction inspections.
* Misusing official position to avoid accounts turning into NPA by unauthorizedly debiting / crediting various unrelated accounts without any mandate / authority.
* Undue accommodation of same group or family.
* Reckless financing.
* Granting overdrawings/ overdrafts and additional limits without analyzing economic viability and/ or sustainability of the borrower and without any cogent reasons and proper justification.
* Wrong one time settlement without due diligence on the repaying capacity of the borrower/ guarantors/ mortgagors thereby leading to loss to the Bank.
* Demanding and accepting favours / bribes and nexus of middle-men / arranger.
* Indulging into corrupt practices and maleficence in considering advances.
* Acting on oral instructions without seeking confirmation of such action while initiating process of availing of bills received under FIBC limit.
* Acquiring assets disproportionate to known sources of income.
* Entering into transactions with outsiders without any plausible explanation.
* Not analyzing search reports.
* Not scrutinizing valuation reports.
* Ignoring adverse findings of inspection, CIBIL, search and valuation reports, concurrent auditors, RBIA auditors, Statutory auditors and RBI inspectors observations and addressing the issues involved upto the satisfaction of the bank/ RBI.
* Failure to create proposed security.
* Accepting tailor made reports.

2. <u>Systemic Improvements and their Impact.</u>

a) Due diligence to be done before entertaining request for credit facility and all credit request of a specific borrower be met at one branch only.

b) **To ascertain fair market value of property, in case the original market value of immovable assets charged is Rs. 1 crore and above, two valuation reports be obtained for counter/ cross-checking the security cover.**

c) Timely detection of Early Warning signals & red flagging of accounts to be pursued meticulously.

d) For stock audit closures, the authorities approving closure of stock audit reports to go through the confirmation from Stock Auditors.

e) When a certificate relating to a borrower and/ or his account is issued by Chartered Accountants (CAs), a copy may be sent to the concerned CA for confirmation with a copy to The Institute of Chartered Accountants of India.

f) The acquisition of assets, both movable and immovable by fraudsters / borrowers / customers out of Bank's finance discovered during enquiry / investigation by investigating agencies should be seized / frozen, as part of enquiry endeavor to mitigate losses. This is again a better preventive tool. Discovery of assets acquired by fraudsters from Bank's finance or by successful conviction of fraudsters and public servants will send right signals to fraudsters and others. This is a valuable preventive tool available in the hands of bank authorities administering vigilance function in banks and financial institutions.

g) Recovery mechanism which acts as a deterrent tool, needs to be strengthened by proper application of systems and procedures. The correlation between rising level of NPAs in banks and frauds probably indicates lack of requisite standards of corporate governance leading to more instances of high value bank loan default and possible collusion between corporate entities and higher level bank officials.

h) The nature and sophistication of frauds in banking sector have increased over the period of time requiring equivalent and improved skills for timely detection and prevention of those frauds. This is also one of the future challenges banks will have to cope with. Banking industry has also witnessed a massive surge in cybercrime incidents in the last two decades. This would be another main area of concern for preventive vigilance . Again, matching skilled manpower would be required. There may be instances of frauds involving collusion of staff with third parties to indulge in fraudulent activities. Detection of such frauds takes a long time and are only discovered when there are customer complaints of fraudulent cases. This is an area of great concern for bankers requiring greater scrutiny from vigilance perspective to prevent commission of frauds by collusion. Imparting education to customers who are victims of frauds is also a challenging task for banking system. The conduct of customers is often contributory factor in commission of frauds and may require appropriate preventive measures and customer awareness guidelines. Here whistle blower policy and attending customer complaints with suitable urgency may help and act as a deterrent.

3. Roles and Responsibilities of the Independent Vigilance Officer (IVO).

At Divisional S&C levels, the Vice President (S&C) will act as Independent Vigilance Officer (IVO) who will take up the following steps for activating Perventive Vigilance at Zonal level:

A) *Preventive Vigilance : Role of Independent Vigilance Officer (IVO)*.

i) To undertake preventive measures by conducting or arranging to conduct regular and surprise inspections in sensitive areas / branches / controlling offices so as to ascertain level of adherence to systems and procedures and to create awareness for ensuring compliance for the same. In addition to checking compliance to various policy guidelines, it will be seen that the extant guidelines issued through various circular are strictly followed up at business units/ cluster offices. He will arrange to frame a check-list of the activities to be covered in his zone depending upon business profile and vulnerability assessment and get the same approved from Vigilance Department, Corporate Headquarters.

ii) To take up the issues with functional departments for systemic improvement where pitfalls in the systems and procedures are observed.

iii) Preparation of List of Officers of Doubtful Integrity so that necessary measures are taken to mitigate their impact on the workings of the bank by pro-active & effective measures.

iv) Monitoring submission of Assets & Liabilities statements and its scrutiny in respect of Executives in Scale IV and above.

B) *Investigative / Detective Vigilance Role.*

a) Investigate or cause an investigation into verifiable allegations reported, scrutiny of complaint and timely submission of comprehensive investigation report both in hard as well as soft copy format.

b) Make a scrutiny / analysis of investigation reports and identify areas that need systemic improvement and ensure follow-up action thereon.

c) File or cause to file a criminal complaint through concerned business unit with requisite support from related Zonal Law Department, with crime investigating agencies (such as Crime Branch of Police) for investigation, wherever the bank has taken a call to file criminal complaint..

d) Scrutiny of Special Audit Reports submitted by Central Audit & Inspection Department with a view to identify cases having Vigilance Angle and initiate further action for taking forward the issues involved.

e) Scrutiny of cases of Staff Accountability in NPA accounts above Rs. 100.00 lacs with a view to identify cases having Vigilance Angle and initiate further action after prior approval from S&C Corporate Headquarters/ Vigilance Department, Corporate Headquarters.

4. <u>Areas Prone to Frauds : Credit Portfolio & Other General Measures of Preventive Vigilance.</u>

i) The potential areas of frauds i.e. delays and nepotism may impact credit decisions. The credit dispensation is linked to Credit Policy and related Annual Action Plans of the zones and the Bank which is well conceived. With regard to sanction of credit limits, the sanctions given at Branches, Cluster & Zonal levels may need to be checked **<u>on sample basis</u>** during Management / Credit Audit at one level higher for bringing into light any possible gaps / short comings. Such observations are escalated back to the sanctioning authority for necessary remedial action. The sanctions are also subjected to concurrent and regular audits at Branches and Management Audit at Controlling Offices. Though the existing systems and procedures are adequate, the time given for checking / scrutiny by auditors may need re-examination.

ii) Receipt and disposal of loan proposals is not properly recorded in the system (either manually or through on-line mode for which guidelines are in place). As a result of this the Turn Around Time (TAT) is not being calculated properly. Though TAT is not the only yard stick for measuring or arriving at a conclusion for existence of malpractices in the system, a deeper look with regard to delays reveal the attitude, competence, commitment of the officials/ officers assigned this job.

iii) Similarly, the competence level of the officials' viz. Auditors, Zonal Office Inspections, Vigilance Inspections needs improvement. We need to leverage the use of technology to improve the deficiencies / loopholes in the existing credit delivery system to a greater extent. Further frequent interaction by the Audit and S&C officials with the branches enquiring them about a particular transaction or a particular sanction in a friendly manner would also spread **<u>the message of "being watched</u>**".

iv) Of late some instances of frauds have come to fore wherein the presence of middlemen, especially in transport loan segment, was seen and confirmed. This aspect surfaced only when the accounts became bad or till a complaint was received . The source of the complaint should be seen. It is observed that Due Diligence Reports and Pre-sanction Inspection reports are compiled in a perfunctory manner without assessing the customer, his credentials, his business, aspects of sustainable debt and repayment capacity of the borrower. The documents like IT returns are fake and fabricated and therefore repayment capacity was not properly assessed. On many occasions, qualified legal opinions are given and the same were accepted by the branches without addressing / attending the underlying issues. On some occasions, the Panel Advocates connive with the prospective borrowers and give incorrect Search Reports. This warrants for strengthening the Contact Point Verification (CPV) functioning. The CPV should be made mandatory at least in all semi- urban, urban and metro areas either through the BC's or sales personnel .The engagement of BC's and panel valuers /advocates should be stringent enough to prevent recurrence of similar incidents .

v) On many occasions it has been observed that one person is introducing many advance accounts. Concurrent auditors / RBIA inspectors who may obtain the list of accounts opened at a particular branch with common introduction to examine the presence of middlemen and cross guarantee events in that branch . Ideally, when a person is introducing an account, there should be an immediate check by the Branch Manager on the accounts earlier introduced by him.

vi) On his periodic visit to branches the IVO must impress upon the staff the importance of adherence to Systems and Procedures, popularize the whistle blower policy and look out for any suspicion that requires further investigation / audit.

vii) Instituting Preventive Vigilance Committees at Cluster and Zonal levels with a view to educate the operating staff for curbing the non-observance of the laid down procedures or other malpractices in order to inculcate and nurture a culture of alertness at ground level.

viii) Launch of e-vigilance portal, under the name of 'J & K Bank Vigil', would amongst inter-alia provide for lodging of online complaints with guaranteed confidentiality under Whistle Blower Policy knowledge at ground level as and when required for timely detection of fraud-like incidents.

ix) Sending vigilance quotes on daily/ periodic basis by way of an SMS to field functionaries to build in the subconscious a spirit of following the highest levels of professional standards and desired ethical behavior.

x) To tackle the issue of skill gap in exercising effective control at the branches particularly in case of first time branch managers would necessitate to introduce a properly designed training program 'Empowering Branch Heads' in which not only common irregularities in advances are dealt in detail but other supervisory / administrative inputs are provided for equipping them with necessary skill sets to overcome these deficiencies.

xi) Offsite Surveillance of branches for sudden spurt in advances, abnormal transactions in impersonal accounts, large value / large number of credits in staff accounts and analysis thereof is carried out on regular basis by I.S. Audit Team and any questionable findings/ genuine concerns to be shared with the S&C, Corporate Headquarters / Vigilance Department for necessary remedial action.

xii) As a preventive measure for strengthening vigilance aspects in daily work, a list of officers is prepared, who after inquiry or during the course of inquiry, have been suspected of lacking in integrity but the suspicion does not amount to preponderance of probability. The purpose of maintaining such a list is to ensure that those officers whose names appear in the list are not posted to sensitive assignments.

xiii) The quality of concurrent audit, RBIA and snap inspections/ visits is to be revisited so that steps of preventive vigilance get synergized with these inspections/ audits for addressing the existing issues of compliance and inculcate/ improve substantially on the compliance aspects by escalating irregularities for necessary rectification and other required action as deemed fit so that the time-lag in addressing these issues are curtailed . This will facilitate near real-time compliance culture and act as an effective deterrent in addressing staff-lapses issues besides serving the interests of the bank by early action. The Bank may put in place a system, whereby every concurrent audit, RBIA and snap inspections/ visits report with vigilance aspects is flagged as **<u>“Special Inspection/ Audit Report”</u>** with copies to Vigilance Department, Corporate Headquarters for necessary examination from fraud-angle. **<u>These Special Inspection/ Audit Report will be attended and scrutinized for examining any element of fraud and staff involvement with suitable remedial action.</u>**

xiv) **<u>Legal Audit</u>** of freshly disbursed high value loan assets with threshold limit of Rs..5.00 crores and above will be done by the concerned Incharge of Law Department at Zonal level for verification of enforceability / sustainability and efficacy of security documents / interest during each quarter. Any issues in perfection and completion of security interest will be got attended to on war-footing basis by the branch functionaries under the guidance of Zonal Law Department so that interests of the bank are sufficiently & comprehensively secured.

xv) Offsite Credit Monitoring Cells (OCMC) will be activated at Cluster/ Zonal levels for generating necessary reports as per the “Policy Document for Credit Discipline” and any issues of concern with related information / inputs will be shared with branches as a measure of preventive vigilance on real time basis.

xvi) As regards monitoring function of above action-point, the same should be assigned to officials having necessary skill sets. Among other aspects of the aforesaid Policy document, cases reflecting 2 or more loans to the same borrower sanctioned/ extended in different months, would be escalated and their bankability counter-cheked so that the incidents of multiple lending with fraud-elements are completely ruled out .

xvii) It is also observed that though we have taken all measures to protect the interest of the customers, lack of knowledge on the part of the customers (e.g. Protecting their ATM Card PIN Number, Passwords for their Internet Banking, holding the Cheque Book in lock and key, subscribing to SMS Banking, regular verification of statement of account etc) is resulting in unwarranted frauds at the branches.

xviii) The visiting officials should examine the level of knowledge dissemination to the customers at the branches by the branch staff at the time of selling the product. A systematic procedure to inform the customer the precautions to be taken by him should be adopted.

xix) Ideally, when a person is introducing an account, there should be an immediate check by the Branch Manager on the accounts earlier introduced by him.

xx) In case of third party mortgages / guarantees, the concerned people should be clearly explained the liabilities when the account goes bad and the same should be put in writing.

xxi) To ensure genuineness of the title deeds, certified copies of the documents should be obtained without fail and compared with the original documents to be lodged with bank and comments on the same should form a part of legal search / vetting report. Branch to verify the CERSAI records for the property offered as security for any existing encumbrances. Reliance on customer or third parties to directly deal with the lawyer / valuer to be avoided and to be obtained directly by branch officials. Guidelines with regard to holding on record the photograps of the branch official on site visit of the proposed mortgage with property in the background may need to be reiterated to all business units & operational offices so that proper identification of the mortgaged properties is ensured as & when needed.

xxii) In case of vehicle loans, care should be taken to verify the existence of the dealers from the dealer list on the website of the most of the truck / car / two wheelers manufacturers.

xxiii) To avoid wrongful disbursements and ensure the borrower has paid the margin/ contribution which should be made compulsory that the customer pays the margin amount through the operative account with the bank and disbursement proceeds are sent to the dealer directly with a covering letter and not through the borrower. This step would avoid cases where the customer opens an account in the same name by using forged documents with other banks and en-cashes/ misappropriates the loan funds.

xxiv) During snap/ surprise inspections, the visiting officials must invariably comment on the following aspects of branch functionaries :

- Adherence to systems and procedures;
- Way in which the transactions are being passed;
- Presence of middlemen at the branch; and
- Life style of the staff in key-positions at business unit.

xxv) To conduct of **special audit of investigative nature** of cases where the borrowing amount from the entire banking system including FIs is Rs. 50.00 crore or more by a team of qualified CAs and independent engineers every year covering aspects like verification of end use of funds, genuineness of debtors, vetting of costs incurred or to be incurred, cross holding in group companies, etc.

xxvi) The empanelment / recruitment process panel valuers / advocates etc. should be stringent enough, clearly defining their roles and responsibilities. If their opinion is found to be not true and fair, they should be made liable for the damages and not just debarred / blacklisted.