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31 May 2019

(Circular No. 156/ 2019-20) DOS-15

The CEO /Chairman
All State Cooperative Banks/District Cooperative Banks /Regional Rural Banks

Dear Sir

Study on adherence to Fraud Monitoring & Reporting guidelines by banks

As per the directions of the Board of Supervision (BoS), a national level study was conducted covering sixteen banks to examine the fraud monitoring system in banks as well as the degree of adherence to fraud monitoring and reporting guidelines prescribed by NABARD vide circular No. 239/DoS.25/2017 dated 29.09.2017 for StCBs/DCCBs and No. 284/DoS-43/2016 dated 06.12.2016 for RRBs.

2. The Study revealed that staff involvement with or without collusion of customer was a common feature in as much as 92% of the frauds. Laxity in following the systems and procedures and delays in inter-branch reconciliation and other loopholes were also reported as other reasons for frauds. Delay in detection has been observed in over 50% of the fraud cases. This is a pointer to the need for establishment and implementation of robust systems and procedures coupled with effective internal checks and controls. Quality of appraisals and effectiveness of credit monitoring system was reported to be inadequate. 50% of the banks studied reported that annual review of loan accounts is not being carried out including examination on adequacy of stock, receipt of stock statement etc.

3. Delays in conduct of concurrent audit, internal inspection prescribed stock audits, legal audits and poor compliances to audit and inspection observations as well as not rotating of staff ultimately weaken the internal checks and controls leading to occurrence of fraud and delay in detection of frauds. Laxity in taking basic precautions to be followed in a computerised environment has also resulted in frauds. User ID-password compromise, loop holes in system etc. have been exploited to commit fraud. Sensitisation of staff on precautions to be taken while working in a computerised environment is required. Overall risk management in banks is reported to be inadequate.

राष्ट्रीय कृषि और ग्रामीण विकास बैंक

National Bank for Agriculture and Rural Development

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4. In this connection, we reiterate the major aspects of the Fraud Monitoring guidelines for compliance as under:

- i. Banks should, with the approval of their respective Boards, frame internal policy for fraud risk management and fraud investigation function.
- ii. Banks should conduct an annual review of the frauds and place a note before the Board of Directors for their information and guidance.
- iii. Fraud cases should be analysed to identify the root causes, examine whether the systems and procedures are scrupulously followed or lapses observed. If so necessary improvements in systems and procedures has to be made.
- iv. In cases of fraud where the systems and procedures have been flouted, staff accountability must be fixed.
- v. Banks to ensure frauds are reported to the local Police / CBI for investigation as per extant guidelines.
- vi. Audit Committee of the Board (ACB) shall be responsible to monitor all the cases of frauds
- vii. Constitute a Special Committee of the Board for monitoring and follow up of cases of frauds (SCBF) involving amounts of Rs 20.00 lakh and above exclusively.
- viii. Ensure that 100% provision is made covering the total amount of fraud. Adequacy of provision to be examined quarterly and also updated in the reporting platform (ENSURE) of NABARD.
- ix. For monitoring of Early Warning Signals (EWS) and Red Flagging of Accounts, necessary systems need to be put in place by the banks.

This circular along with the above mentioned guidelines may be placed before the next Board meeting for compliance.

Please acknowledge receipt of this circular to our Regional Office concerned.

Yours faithfully



(K. Raghavendra Rao)
Chief General Manager