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INDIA'S NPA CRISIS AND NEW RBI POLICY AND FRDI BILL

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ABSTRACT

Banks are the most important financial institutions in a country. They contribute to economic development through the process of financial intermediation. Non Performing Assets (NPAs) and banking frauds tend to reduce the efficacy of the banking sector. According to Financial Stability Report 2017, India's gross NPA stands at 9.6%. It is a large figure when compared to other Asian economies. The basic metal and cement industries contribute to the largest share of NPAs. Public sector banks in India have the largest amount of NPAs in their balance sheets. This paper has taken into consideration the secondary data available from various research papers and article downloaded from SSRN, JSTOR, and Research Gate to analyze possible reforms to resolve the NPA problem of the economy. FRDI bill which attempted to reform the resolution mechanism has been discussed. The paper also emphasizes on certain reforms for public sector banks, RBI's governance mechanism and the overall banking sector that can help to clean up the balance sheets of Indian banks and make them more efficient in their core functions. The paper also throws light on the recent banking frauds that wiped out billions of rupees from the banking system and discusses the steps that RBI has taken to prevent such frauds in the future.

KEYWORDS: *Non Performing Assets, Public Sector Banks, Recapitalization, Private Banks, RBI.*

Introduction

One of the biggest challenges in the Indian financial system is the poor health of its banking sector. Indian banks are plagued with Non-Performing Assets (NPAs). As defined by RBI, An asset, including a leased asset, becomes non-performing when it ceases to generate income for the bank. A 'non-performing asset' (NPA) is defined as a credit facility in respect of which the interest and/ or installment of principal has remained 'past due' for a specified period of time. The specified period has been reduced in a phased manner. Currently, the specified period is of 90 days. As per Financial Stability Report 2017, India's gross NPA stands at 9.6%. It is a grave situation because an increase in the total size of NPAs means lower revenue stream for banks. It then leads to lower credit creation in the economy. High NPAs also mean lower confidence in the market and increased the cost of credit. This severely affects total investment and consumption expenditure in the economy. A lower overall demand is the ultimate result and thus a setback in GDP growth figures. This paper attempts to focus on various aspects of the NPA problem of our banks, compares the size of our NPAs with other global economies, highlight which industries and which banks are most affected. It also throws light on various steps taken by the government to combat this disease of Indian banking system with a major focus on FRDI bill. Some of the major themes as brought out by recent roundtable organized by Brookings India on NPA resolution have been deliberated upon. In the end, the recent banking frauds have been summarized along with the steps taken by RBI to prevent such frauds.

Objectives of the Study

- To understand the meaning of NPAs.
- To understand how the government has reacted to the NPA problem.

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- To understand the meaning and criticism of FRDI bill.
- To understand various reforms suggested for public sector banks for NPA resolution.
- To understand the ways in which RBI governance and regulations can be revamped.
- To understand how the banking system can be re-engineered.
- To get updated about recent banking frauds of 2018 and RBI's steps to prevent such frauds.

Organization of Paper

This paper is structured in a number of sections. Section 1 introduces the concept of NPA, the outcome of the NPA problem on the economy and objectives of the study. Section 2 provides a review of literature o various aspects of bank's NPA. Section 3 describes the scope and methodology of the study. Section 4 presents the subject matter of the study. Finally, it has been concluded by summarizing the study and discussing the outlook for further studies.

Review of Literature

Prashant K Reddy (2002) compares the Indian experience of NPAs with that of China, Thailand, Korea, and Japan. He compares and contrasts the causes and measures taken by other Asian countries to resolve the problem of NPAs. Some of the similarities related to NPAs in all these nations were related to informational quality, weak legal system, extensive usage of government guarantees and funding. Some of the differences among these countries were related to the core causes, business structure, macroeconomics, and fiscal policy. India should learn from the foreign experiences and attempt to strengthen its legal norms, align its prudential norms with international standards, enhance participation of private sector and foreign players in the asset reconstruction companies, develop its debt market and promote healthy securitization.

Tamal Datta Chaudhuri (2005) discusses which all strategies can a lender apply and at what time depending on various characteristics of the lender like market growth, competitive position, skill set, management quality, outstanding liabilities, debt-equity ratio, nature of the industry, overall macroeconomic condition, asset quality, and provisioning. The study also establishes that NPA which initially is a micro problem of a bank through domino effect in the economy can translate into a banking crisis which further gets interlinked with a currency crisis. Some recovery strategies suggested are financial restructuring, change in management, one-time settlement, merger, asset reconstruction companies, securitization, adoption of credit rating modules, improved corporate governance practices, HR management and adoption of proper IT environment.

Justin Nelson Michael, et al (2006) analyzes the impact of Non Performing Assets on central Co-operative banks (CCBs). It establishes that NPAs at macro level affect the operational efficiency of CCBs by creating a banking distress due to the erosion of the bank's capital. At micro levels, NPAs affect the profitability, liquidity, and solvency of central co-operative banks. There is an emergent need for effective recovery strategies in such banks because of their immense importance in the economy.

Vighneswara Swamy (2012) examines the impact of macroeconomic and endogenous factors on Non Performing Assets for a study period extending from 1997 to 2009. Some of the macroeconomic factors that affect the level of NPAs in an economy are GDP growth, inflation, natural calamities, ownership pattern, market strength, etc. some of the endogenous factors are bank's capital adequacy, credit growth, operational efficiency, branch spread, and regional concentration. Some other factors that also contribute to NPAs are a business failure, cost overruns in implementing projects, strained labor relations, inefficient management, technological failure, product failure etc. the study also concludes that large banks and private or foreign banks are more efficient in their credit management as compared to PSBs. It also establishes that priority sector lending does not have a significant effect on NPAs.

Anita Sheopuri, et al (2014) compares public sector banks and private sector banks over various financial parameters and also enquires where all PSBs lack behind. Human resource policies are highlighted as a major factor which let private sector banks (PVBs) perform far better than PSBs. It establishes that both PSBs and PVBs both face problems in hiring and retaining the right kind of employees. Various challenges for PSBs in HR management, marketing environment, product development and IT have been discussed.

Balaji Chinatala (2016) has compared the overall financial performance of selected public and private sector banks from 2011 to 2016 based on secondary data. The study concludes that total income, net interest income, and operating profits for public sector banks were higher than that of private sector banks. Profits for public sector banks were highly fluctuating over the study period but that of private

banks were continually increasing. There was a steady growth in return of assets for private sector banks whereas a declining trend was observed for public sector banks. The writer has also made suggestions for banks to improve their performance.

Charan Singh (2016) emphasizes on the role of banking sector in influencing the macroeconomics of a nation. He defines banking and talks about the origin of the banking system in the world, functions of banking and the role of central banks in enhancing economic growth. The concerns behind nationalization of banks in 1969 and 1980 and evolution of priority sector lending have been discussed. A major focus is on the role of public sector banks in the Indian economy. They have a large volume of stressed assets in mining, iron and steel, textiles, infrastructure and aviation sector as compared to private sector banks. PSBs are meant to focus on social objectives and spreading financial inclusion in the unbanked areas. They shoulder the major burden of implementing welfare schemes but still perform at par with private sector banks as per many financial parameters.

Charan Singh, et al (2016) through secondary research and 360-degree analysis of banking affiliates, retired bankers, policy makers, auditors, and compliance officers discuss in detail about banking frauds in India. It says that there are three types of frauds that are deposit-related, advance related or services related. It establishes that in recent times the number of frauds has reduced but the amount involved in such frauds has increased with the largest share being of PSBs. Some of the reasons of frauds are lack of adequate supervision of top management, faulty incentive mechanism, collusion between various parties, weak regulatory system, lack of appropriate tools and technologies and lack of awareness. Some of the recommendations to prevent frauds in the banking industry are also discussed.

Sujoy Dhar (2016) analyzes the impact of the recapitalization plan under the Indradhanush framework on PSBs. Secondary data from various research articles and knowledge reports have been used. Factors influencing NPAs have been divided into micro and macroeconomic factors. Microeconomic factors are specific to particular banks like corruption, political interference, size of total assets, bank branch expansion and loan concentration. Macroeconomic factors have a direct influence on overall credit risk like GDP, inflation, and interest rate.

Prasenjit Bose (2017) introduces the objectives of FRDI bill which was introduced in the LokSabha in August 2017. He establishes that the overhaul in resolution regime was not driven by domestic financial conditions because bank failures are rarest of rare in India. Instead, it followed the steps of 'key attributes of effective resolution regimes for financial institutions' as adopted by the Financial Stability Board. It also establishes that advanced economies have pushed for such resolution reforms but not the emerging economies because of the relatively small size of banks that EMEs have. It also highlights the pros and cons of Resolution Corporation as the single authority to deal with the entire financial sector.

Shraddha Kokane, et al (2017) confirms that recapitalization of public sector banks by Rs.25,000 crore in 2016 and 2017 and rs.10,000 crore in 2018 and 2019 will reduce the NPA levels. He establishes a negative correlation between the NPA levels and Capital Adequacy ratios of banks from 2009 to 2015. He also discusses that recapitalization has had a positive impact on American and European banks.

Inchara PM Gowda (2018) discusses the key issues of FRDI bill which were highly criticized to bring possible instability in the financial system. Possible repeal of Deposit Insurance and Credit Guarantee Corporation 1961 Act was highly criticized because FRDI bill did not mention the maximum limit of insured deposits and thus brought vagueness to the system. Also, the clause that gave residual claims to depositors on the amount realized from sale proceeds of liquidation assets was not welcomed. 'Bail-in-clause' was the major issue because it was to introduce a resolution mechanism where the consent of creditors/depositors was not required for bail-in of the banks. In place of money, it aimed to give security papers or bonds to the depositors. It establishes that FRDI bill was to give disproportionate powers to the resolution corporation.

Scope and Methodology

The study looks into various aspects of the NPA problem that Indian banks are going through and how the government has reacted to it. It also looks into various reforms suggested for PSBs, RBI governance, and overall banking structure to resolve the NPA crisis. This study is primarily based on secondary data. A number of industry journals, recent RBI reports, Indian economic survey, online articles and newspaper articles have been used for analysis.

Analysis of Study

Stressed assets of Indian banks amount to around Rs.10 lakh crore ($150 million), roughly twice the GDP of Sri Lanka. Some of the reasons for this problem are the lack of adequate supervision of top management, lack of appropriate tools and technologies, a weak regulatory system, and collusion between staff, third party, and government. The government has taken many steps to cure this virus spreading quickly in both state-owned and private banks. If this pile of NPAs keeps growing then the growth rate of the Indian economy will be severely affected. Encouraging privatization of state-owned banks, merging smaller banks, the introduction of Insolvency and Bankruptcy Code (IBC), and proposals for the recapitalization of banks are few of the steps taken by the Indian government in this direction.

Meaning of NPAs

Non Performing Assets or NPAs are the assets (loan and advances) that cease to generate income for the bank. According to RBI norms, an asset becomes NPA if its interest payment or installment of principal amount remains unpaid for at least 90 days. This section tries to explain the process of credit creation by the Indian banking sector. Regulation of the supply of money in the economy is the primary function of RBI. It uses instruments like the Cash Reserve Ratio (CRR), the Statutory Liquidity Ratio (SLR), the repo rate, and the reverse repo rate. When banks make poor lending decisions, the size of bad loans tends to increase. CRR is the money calculated as a percentage of the net demand and time liabilities (NDTL) that commercial banks have to keep as reserves with the RBI. As of October 2018 RBI has fixed this at 4%. Banks also have to deposit a portion of their money in relatively liquid assets such as government bonds, securities or gold. This ratio is termed as SLR. The current SLR is 19.5%.

The mechanism is explained here with a numerical. Say, if Rs.100 deposited in a bank, then Rs.4 is to be kept as the reserve with the RBI and Rs.19.5 to be invested in liquid assets like bonds or gold. Hence, nearly a quarter of the money in the banking sector can be retrieved in case of any contingency and the bank is left free to lend the rest of Rs.76.5 to borrowers. The interest earned on these loans made to the corporate and retail sector is used to make interest payments to the bank's customers, and the remaining is the bank's profit. NPAs arise when banks lend to such customers who default on their repayment. According to RBIs Financial Stability Report December 2017, NPAs currently stands at 10.2 percent of all assets, while stressed assets (NPAs in effect), stand at 12.8 percent. Related frauds stand at Rs. 612.6 billion in the last five financial years. The banking system is already plagued with governance failures on account of integrity and competence issues.

Indian Banks Compared with their Global Counterparts

When compared with other major economies, it is shocking to know that India has the second highest ratio of NPAs. As per RBI's 2017 Financial Stability Report, India's gross NPAs stands at 9.6%. This is the sum total of all stressed assets held by all lending institutions of the country. Only Italy has NPAs higher than India. It has stressed assets of around 16.4%. as per the International Monetary Fund (IMF) Soundness Indicators, China has only 1.7% NPAs even though its huge economic growth is largely fuelled by borrowings. However, India's NPA problem is much better than the debt-ridden countries like Greece and Ukraine which have 36.3% and 30.5% NPAs respectively.

Major Defaulter Industries

According to various research works conducted by RBI, the basic metals and cement industries, construction, infrastructure, and automobile industries contribute to a sizeable amount of banks' NPAs. Out of these metal and cement industry are most indebted with 45.8% and 34.6% stressed assets respectively.

Banks with the Most NPAs

Studies show that public sector banks (PSBs) are the most affected by NPAs. Private Banks and foreign banks are much more effective in dealing with this plague. The gross NPAs of PSBs increased by 311.22% from Rs.1,55,890 crores in 2013 to Rs.6,41,057 crores in 2017. While the gross NPA ratio of total assets rose from 3.84% to 12.47%. whereas, the gross NPAs of private banks increased by 269.47% from Rs.19,986 crores in 2013 to Rs.73,842 crores in the same period. According to the rating agency CARE, State Bank of India tops the list of scheduled banks with the highest NPAs worth Rs.1,88,068 crores of stressed assets as of June 2017. Punjab National Bank and IDBI Bank follow SBI with Rs.57,721 crores and Rs.50,173 crores of gross NPAs respectively.

However, in percentage terms IDBI Bank tops the list having the highest exposure to liabilities, with 24.11% gross NPAs. Indian Overseas Bank has 23.6% s NPAs while private lenders like Kotak Mahindra Bank and HDFC have only 2.58% and 1.24% gross NPAs respectively. State Bank of India has a gross NPA ratio of 9.97% but the highest stressed assets in absolute terms. It is a matter of grave concern because studies by the Ministry of Statistics and Programme Implementation (MOSPI) and World Bank reveals that economic growth tapers off with a spike in the bad loan ratio.

Government's Reaction to the NPA Crisis

To recover outstanding loans, a slew of legislation including the IBC (Insolvency and Bankruptcy Code), the SARFAESI (Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest) Act, and the RDDBFI (Recovery of Debts due to Banks and Financial Institutions) were instituted. To fast-track proceedings related to bank's assets, Debt Recovery Tribunals (DBT) was set up. The Financial Resolution and Deposit Insurance (FRDI) Bill was an attempt at revolutionizing the resolution mechanism of financial institutions. Also, the recapitalization plans of the PSBs are the most desirable step taken according to many studies. The SARFAESI Act empowers banks to auction the collateral assets or properties. Under this Act, 64,519 properties were already seized in 2015-16.

What is the Financial Resolution and Deposit Insurance (FRDI) Bill?

The FRDI Bill was first introduced in the Loksabha in August 2017 was later withdrawn in August 2018. It was aimed at ensuring the money of a bank's depositors in the case of an eventuality where the bank would have to be liquidated. However, some of the provisions of the draft had drawn the ire of depositors and bank employees alike, since it compromised the interests of the depositor. The bill proposed the setting up of a Resolution Corporation, "whose direction and management vested with the Board, subject to the terms and conditions of the Act."

The bill gave the government overweening powers by the fact of greater representation in the Resolution Corporation. The Board consisted of a Chairperson, one member each from the Finance Ministry, the RBI, Securities and Exchange Board of India (SEBI), the Insurance Regulatory and Development Authority of India (IRDAI), the Pension Fund Regulatory and Development Authority (PFDA), three full-time members and two independent members, both of whom were to be appointed by the Central government. This implies that six of the 11 members of the Board were to be nominated by the government, giving it the final say in decision making. It was thus criticized for giving disproportionately more power to the government.

The bail-in clause had emerged as the major cause of contention with depositors. This gave banks the authority to issue securities in lieu of the money deposited. However, their value was not be immediately commensurate with the deposit amount since if a bank had filed for bankruptcy, the value of assets held would have also eroded. It also did not expressly mention the amount of funds insured as the Deposit Insurance and Credit Guarantee Corporation was to be repealed. Thus after so much of criticism, it was finally withdrawn in August 2018.

Possible Reforms

Reforms need to attack the direct and distant cause of NPAs. According to SujoyDhar (2016), some of the major causes are related to corruption, political interference, bank branch expansion strategies, a bank's total assets size and loan concentration. Whereas some micro-level factors are related to GDP trends, inflation levels, and interest rate levels. In a wide-spanning discussion of Brookings India, a few key themes emerged as possible reforms to resolve the NPA problem in India. Some of the reforms suggested for PSBs, RBI governance, and overall banking industry are discussed here.

- **Public Sector Banks**

Public Sector Banks (PSBs) constitute over 70 percent of the banking system and are the most affected by the so-called NPA crisis. Fundamental reforms are the need of the hour to improve the health of PSBs.

- **Privatization:** Nationalization of banks in the 1970s was considered necessary at that time to bring industry and finance closer. But the grey part is that nationalization has over time become a strong thread connecting the PSBs to politicians and bureaucrats.
- There are very strong arguments for privatizing some of the problematic PSBs because PSBs have given rise problems like disempowered boards, defective incentive programs, continual bureaucratic meddling, paralyzed decision-making, red-tapism causing frauds and endemic corruption, opacity at various levels, defective human resource management. Privatization is believed to bring market discipline to PSBs.

- **Bank Holding Company structure:** The bank holding company (BHC) structure was recommended by the P.J. Nayak Committee. It basically means a company owning one or more banks and that company may not directly indulge in banking activities. It involves divesting the government's shareholding to below 52 percent and routing it through a holding company. This is highly common in the USA.
- **Changing of the social sector lending vehicle:** PSBs arealso famous for their social sector lending function. PSBs (and indeed all banks) are required to lend 40 percent of their total assets to "priority sectors" such as agriculture, small and medium enterprises, social infrastructure, renewable resources and weaker sections of the society. Priority Sector Lending (PSL) is deemed unprofitable for several reasons and leading to a drag on the earnings of the banks also called "PSL drag." These banks may then try to make money from risky lending. Accordingly, it may be beneficial for the entire sector if all agricultural and social sector lending is routed through a separate entity. This entity could be government owned and controlled but allow the corporate lending part of the PSBs to be privatized. This may allow many market distortions to be corrected.
- **Recapitalise, Reform and then privatize:** If steps to privatize PSBs be implemented in near future there will be hardly any takers because of their current state of impaired balance sheets. Also, recapitalizing PSBs repeatedly creates moral hazard issues. Recapitalization and governance reform should be taken first to enhance market valuations of PSBs and then to a path for privatization should be taken.
- **Single Big Bank:** The idea of a single large PSB looks attractive as larger banks have better NPA management as per Vighneswara Swamy (2012). But such an entity could create serious problems of moral hazard from the too-big-to-fail syndrome. SBI and its associates can be merged as a big bank but the next biggest bank would be one-fourth of its size.
- **Governance reforms:** just privatizing PSBs is no full proof solution. The defective governance policies should be reformed to make the system cleaner from within. Multiple areas like HR management, CG policies, IT environment, etc must be reformed.
- **Role, purpose and business strategy:** PSBs suffer from a severe identity crisis. They do not have a coherent business strategy. It is urgent to clarify the role and purpose of PSBs and to let them concentrate on specific regions or business segments. The need for the existence of each PSB must be clear and its business and expansion should follow that.
- **Term lengths:** The terms of bank chairpersons must be elongated to hold them accountable. As the heads change, they tend to leave the banks with an NPA "bloat". Terms of chairpersons should be aligned with the life of the loan because it shall allow defaults to be detected and penalties to be imposed on time.
- **Penalties for wrongdoings:** it is noted than vigilance mechanisms do exist in the Indian scenario but enforcement is weak because of which wrongdoers escape without being penalized. Steps should be taken to make the enforcement part stronger.
- **Rotation of staff:** The Punjab National Bank is an example of operational and risk management failures in PSBs. Improvements of HR practices can help mitigate frauds. If officers are rotated in the inspection and supervisory roles then bank supervision may become stronger.
- **Credit appraisal and monitoring:** Credit appraisal and monitoring are the basic principles but unfortunately obviated in PSBs. Adoption of credit rating modules can help to detect problematic assets in the initial stages only.

- **RBI Governance and Regulation**

The RBI as a regulator has achieved many successes. But still disqualifies in the face of many structural impediments.RBI is blamed to have limited control over PSBs. The internal governance mechanism of RBI can be reformed to strengthen it as the regulator of the banking industry.

- **Strengthening Supervisory Capacity:** RBI lacks the supervisory capacity to conduct forensic audits and this must be strengthened. Human and technological resources can be employed to make the supervisory function even stronger and directional.

- **Preventing Ever Greening:** RBI regulations have permitted banks to "evergreen" and in effect delay the recognition and therefore the resolution of NPAs. RBI regulations must ensure that PSBs so not get chances to "extend and pretend" with their balance sheet assets because such a practice leads to a seizure of new lending. The recent actions of RBI to end schemes like Corporate Debt Restructuring (CDR) are few steps forward in this direction.

- **Reengineering of Banking Systems**
  - **Secondary Market:** A vibrant secondary market for NPAs is crucial to resolve the NPA crisis at a faster pace. But the lack of transparency in asset pricing is holding this back.
  - **Concurrent Audit:** The internal audit of banks is believed to be no more effective in identifying problems standing in the balance sheets. Concurrent audit system is the part of a bank's early warning system. Although even it has failed to identify the red flags. Hence concurrent audit system needs to be made much more effective and purposive.
  - **Using technology for maker-checker:** Currently, the maker-checker system requires human intervention and are therefore prone to capture and corruption. Use of Artificial Intelligence must be promoted for the supervision of financial transactions.
  - **Enhanced communication within the industry:** Business intelligence must use traditional means of conversing with different kind of people in the industry like suppliers and customers. This can be an invaluable source of financial information.

Bank Frauds in the Indian Banking Sector in 2018

2018 has already seen a string of bank frauds and scams across India and this has again raised questions about the governance and credit managing practices of both private as well as public sector banks. According to Charan Singh, et al (2016), the number of banking frauds has reduced in current times but the money involved in them has increased. This section throws light on some of the scams that have taken place in 2018 by the month of September.

- **PNB Scam**

Punjab National Bank (PNB) which is the second largest public sector bank in India brought to limelight the biggest banking fraud of the country. In February 2018, it shocked the entire banking industry when it revealed a fraud of Rs 14,356 crore or $2.1 billion at PNB's Brady House Branch in Mumbai. Jeweler Nirav Modi, his family and his business partner Mehul Choksi who is also the owner of Gitanjali Gems were the main accused. Fraudulent issuance of Letter of Undertaking (LoUs) was at the core of the scam. Employees of the bank bypassed the bank's core banking system. They issued LOUs to overseas branches of other Indian banks using the international financial communication system, SWIFT. All of this came into light when a new employee noticed the irregularities. Several employees at the bank were suspended from their post for their suspected involvement. It is the biggest scam in the Indian banking sector. Efforts are being still made by CBI, RBI and Enforcement Directorate to bring back the main accused from Britain and Antigua.

- **Rotomac Case**

Rs 3,700 Rotomac fraud came into limelight after the PNB scam. Kanpur based Rotomac Global allegedly cheated a consortium of seven public sector banks for Rs 3,700 crore. The investigation agency filed case against Vikram Kothari and Rahul Kothari, directors of the business group for taking foreign letters of credit (LC) on the pretext of making payments to its buyers and suppliers in Dubai, Sharjah, and Hong Kong. But there were no such payments made. It was just a way of round-tripping the money. This was being done from 2008. The seven banks approached are Indian Overseas Bank, Bank of India, Union Bank of India, Bank of Baroda, Allahabad Bank, Oriental Bank of Commerce and Bank of Maharashtra. The largest exposure was of Indian Overseas Bank.

- **SBI Fraud Case**

Chennai jewelry network Kanishk Gold Pvt Ltd (KGPL) defrauded a consortium of 14 banks led by SBI for an amount of Rs 824.15 crore. It is alleged that the accused falsified its records and financial statements to take loans from these banks which have now turned into NPAs. This continued for over 10 years since 2008. Central Bureau of Investigation (CBI) filed an FIR against the KGPL, its directors Bhoopesh Kumar Jain, and his wife Neeta Jain, its auditors TejrajAchha, Ajay Kumar Jain, Sumit Kedia and other unknown persons.

- **R P Infosystem Scam**

Computer manufacturer R P Info Systems and its directors were alleged for cheating Canara bank and nine other members of the consortium for Rs 515.15 crore. Other members of the consortium were State Bank of India, State Bank of Bikaner and Jaipur, and State Bank of Patiala (both now part of the CBI), Allahabad Bank, Union Bank of India, Oriental Bank of Commerce, Central Bank of India, Punjab National Bank, State Bank of Patiala, and Federal Bank. The firm has been fabricating its books and taking had taken funds from the consortium from 2012 onwards.

- **PNB 91 Million Scam**

It was the second fraud reported by PNB in 2018 after the Nirav Modi scam. Issuance of two fraudulent and unauthorized LoUs for Rs 91 million on the account of Chandari Paper and Allied Products Pvt Ltd was the crux of the scam. The fraud was again spotted at the PNB's Brady House Branch in Mumbai.

RBI has taken Many Steps to Prevent Frauds in the Banking System

Frauds are basically of three types. i) Deposit-related, ii) advance-related and iii) services related (Charan Singh 2016). The advance/credit related frauds are most evident because of the high amount involved in them. RBI has taken various actions to prevent possible frauds. Some of these steps are:

- A framework for letting banks classify potential fraud accounts as red-flagged accounts based on observation/evaluation of early warning signals.
- An online searchable database of frauds in the form of Central Fraud Registry for timely identification, control, and mitigation of fraud risk. It can also help to carry out due diligence during credit sanction process.
- Issuance of caution advised by RBI, detailing names of fraudsters and their Modus Operandi.
- Re-verification of title deeds in respect of all credit exposures of Rs. 5 crore and above by banks, as mandated by RBI.
- Issuance of various master circulars to banks, with a view to restricting imprudent practices and at the same time ensuring sound procedures for the conduct of business.
- Requiring banks to put in place adequate audit and compliance mechanisms with Board-level reporting through the Audit Committee of the Board.
- Subjecting the systems and procedures in banks to supervisory review by RBI as part of the Risk-Based Supervisory framework for banks.

Conclusion

The banking system of a nation is the vehicle by which various monetary policies of the government get implemented. Indian banks have a high percentage of Non-Performing Assets (NPAs) which affect the operational efficiency, profitability, liquidity, and solvency of the entire system. A high proportion of NPAs can make the entire economy crippled so RBI has taken a number of initiatives to resolve this problem. Plans for the recapitalization of PSBs have been established. Insolvency and Bankruptcy code (IBC), Recovery of Debts due to banks and financial institutions were established. FRDI bill was introduced in 2017 to reform the resolution mechanism of financial institutions but due to huge criticism, it was withdrawn in August 2018. Public sector banks which constitute the largest amount of NPAs should be reformed by initiating privatization, introducing bank holding company structure, creating few but big banks, reforming governance structure, modifying business strategies, etc. RBI's internal governance should also be improved to detect the problem in its early stages itself. A vibrant secondary market for NPAs, concurrent audit, technological improvements, etc should be introduced. Not just NPAs, but also the banking scams or frauds tend to reduce the efficiency of the Indian banking system. In recent times, the number of banking frauds has reduced but the amount involved in such frauds has increased. Some of the recent frauds include the PNB scam, Rotomac scam, SBI fraud case and RP Infosys scam. RBI has taken many steps to prevent such frauds in future like the introduction of attempts to identify red flagged accounts, online database verification, re-verification of title deeds, the requirement of adequate audit and supervisory review of banks. It is now urgent to make the Indian banks healthy to boost the growth and development of the economy.

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