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Admission Open

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Admission Open

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1. AIR-1, CE Akash Chouksey
   2. AIR-1, CE Reema Agarwal
   3. AIR-3, CE Souvik Saha
   4. AIR-4, CE Alok Shakti
   5. AIR-5, CE Ankush Agarwal
   6. AIR-9, CE Praveen Kumar
   7. AIR-9, CE Yadagir Shashank
   8. AIR-9, CE Vikram Garg

ME 10 in Top 10 | 19 in Top 20
1. AIR-1, ME Amit Kumar
   2. AIR-2, ME Anuj Prajapat
   3. AIR-1, ME Arshish Singh
   4. AIR-3, ME Shazad
   5. AIR-5, ME Roachk Singh
   6. AIR-6, ME Shubhang
   7. AIR-7, ME Shashank T.
   8. AIR-9, ME Kapil Manik
   9. AIR-9, ME Aman Singh
   10. AIR-9, ME Animesh P.

EE + EC 13 in Top 10 | 23 in Top 20
1. AIR-2, EE Rahul
   2. AIR-3, EE Pinal M
   3. AIR-3, EE Naveen Kaushal
   4. AIR-4, EE Aditya Jayak
   5. AIR-5, EE Shantanu Srivastava
   6. AIR-6, EE Prashant
   7. AIR-9, EE Dava Ajay
   8. AIR-10, EE Supratik Bh.
   9. AIR-10, EE Deshna
   10. AIR-10, EE Dhovaraj Kumar

CS 7 in Top 10 | 11 in Top 20
1. AIR-1, CS Namita Kastra
   2. AIR-2, CS Rishabh Gupta
   3. AIR-4, CS T. B. Deepak
   4. AIR-4, CS S. Prakash
   5. AIR-7, CS Paarth Gupta
   6. AIR-7, CS Shreyas
   7. AIR-9, CS Chandrashish

IN 10 in Top 10 | 16 in Top 20
1. AIR-1, IN Naman Jaiswal
   2. AIR-2, IN Ashwin Kumar
   3. AIR-2, IN Manish Mehta
   4. AIR-4, IN Amit Shankya
   5. AIR-4, IN Ramesh Kamula
   6. AIR-6, IN Sumesh Paliwal
   7. AIR-7, IN Somesh
   8. AIR-8, IN Tarun Gupta
   9. AIR-9, IN Shree Pandey
   10. AIR-10, IN Vipin Chander

PI 7 in Top 10 | 14 in Top 20
1. AIR-1, PI Odima Khanna
   2. AIR-2, PI Bhattacharya
   3. AIR-3, PI Divyanshu
   4. AIR-3, PI Shikha Jain
   5. AIR-5, PI Anil Bajpai
   6. AIR-6, PI Sumit Dhal
   7. AIR-9, PI Najiba Fatima

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Streamwise selections in Top 10 and Top 100 in GATE 2018 from MADE EASY

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PNB FRAUD

In February 2018, Punjab National Bank (PNB) disclosed fraud allegedly by Nirav Modi relating to fraudulent letter of undertaking worth ₹ 11,600 crore.

Who are involved in the scam?

- In its complaint, PNB has alleged that the fraud was led by Nirav Modi, a jeweller who’s No. 85 on Forbes’s 2017 list of India’s richest people.
- It is alleged that Modi and his relative Mehul Choksi and companies linked with them colluded with a former PNB employee, Gokulnath Shetty, who was a deputy general manager in the foreign-exchange department in one of its branches in Mumbai to pull off the heist.

Fraud:

- In PNB fraud, letters of undertaking (LOU) were issued in favour of Nirav Modi bypassing the bank’s reporting system (Core Banking Solution-CBS) through SWIFT messages to overseas banks without authorisation, without proper import documents and without obtaining margin money.
- These LoUs — which are equivalent to providing credit and should be recorded as contingent liabilities — were not so recorded in CBS, so as to avoid detection by audit system and internal controls.
- Overseas bank remit funds to Nostro account of PNB, backed by LOU.
- Under RBI guideline, buyer’s credit for import of gems should not exceed 90 days from the shipment date; however in this case they were rolled over repeatedly. By rolling over the credit, Nirav Modi ensured that subsequent LOUs repaid the dues on earlier LOUs.

Society for Worldwide Interbank Financial Telecommunication (SWIFT)?

Society for Worldwide Interbank Financial Telecommunication (SWIFT) is a messaging network for securely transmitting instructions for all financial transactions through standardised system of codes.

How did it come to Light?

- The scam came to light in January 2018, when representatives of Nirav Modi’s companies approached PNB for a fresh loan. By then, Shetty had retired and his successor declined to honour Modi’s request.
- At this, the firms contested that they have been availing this facility in the past also but the branch records did not reveal details of any such facility.
- This was when the fake letters of undertaking were discovered.

How the Fraud was Accomplished?

Gokulnath Shetty at PNB allegedly sent Letters of Undertaking without recording them in the bank’s internal software system.

1. Gokulnath Shetty (Deputy Manager) makes SWIFT letters of undertakings (LoUs) and bypasses PNB’s internal banking system.
2. SWIFT LoUs are transmitted, in a fraud which PNB says amounted to $1.77 billion.
3. Companies linked to billionaire jeweller Nirav Modi, Jewellery retailer Gitanjali, led by Modi’s uncle Mehul Choksi, and representatives of Modi and Choksi deny the allegations.
4. Overseas branches of other banks, mostly Indian, credit to:
   - Bank credit to:
   - Shetty allegedly logs in as a different user. The bank usually has a security check, but the deputy manager circumvents it by using multiple passwords, allowing him to both enter and verify transactions.
About:
- LoU is a bank guarantee under which a bank allows its customer to raise money from another Indian bank’s foreign branch in the form of short-term credit.
- It is an assurance given by one bank to another to meet a liability on behalf of a customer.
- **Usage:** The loan is used to make payment to the customer’s offshore suppliers in foreign currency. I.E. It is issued for overseas import remittances.

Working:
- An LoU involves four parties — an issuing bank, a receiving bank, an importer and a beneficiary entity overseas.
- According to norms, the term of an LoU is 180 days, and can be rolled over once for six months. Since LoUs are a form of lending, they are typically backed by security.
- LoUs are conveyed from bank to bank through Society for Worldwide Interbank Financial Telecommunication (SWIFT) instructions, which pass through a triple layer of checks.
- A SWIFT instruction, which represents a bank’s consent, is cleared by a maker, a checker and a verifier before it is sent across. There is no reported instance so far of a breach in SWIFT instructions anywhere in the world.
- After acknowledging and accepting the LoU, the foreign branch of Indian bank transfers money to the Nostro account of the bank that has issued the LoU.

**NOSTRO Account?**
Banks maintain foreign currency stocks in the form of bank accounts with their overseas branches; these are called Nostro accounts.

**Example:**
- So, let’s say Nirav Modi wants to import diamonds for a new collection. He approaches PNB and asks it to arrange for a guarantee in the form of LoU for short-term loans from the foreign branches of Indian banks, to pay his diamond supplier.
- Bank officials promptly send instructions from PNB’s Mumbai branch to other overseas banks offering LoUs.
- The messages are sent through SWIFT — an inter-bank messaging network for securely transmitting instructions for financial transactions.
- Theoretically, such SWIFT instructions need to be recorded in a bank’s core banking system. But thanks to the connivance of bank officials at PNB, the actual LoUs issued over the past seven years to Nirav Modi managed to escape scrutiny.

**Importance of LoU:**
- It is an important instrument for importers for carrying out their business or import.
- It is a much cheaper and convenient way to raise credit in foreign currency because of their attractive pricing.
- According to an estimate, bank finance for imports into India is around $140 billion, of which over 60% is funded through such instruments.

**Ban:**
- After PNB scam, the Reserve Bank of India has decided to ban such instruments.
- Post the ban on issuance of LoU/LoCs by RBI for trade credit, companies have the option of using bank guarantees to raise buyer’ credit, based on a sanctioned limit.
- **Impact of ban:**
  - The ban will negatively impact the $85 billion buyers’ credit market which was legal and in accordance with the law.
  - Ban of LoUs will increase the cost for importers. They will now have to rely on instruments like letters of credit, bank guarantee, etc. which are more expensive.
  - It will also negatively impact the competitiveness of exporters who import raw materials for their products.

**Way forward:**
- In the PNB scam, though LoUs were misused but the problem was not with LoUs per se. The problem was failure of supervisory and regulatory failure.
- RBI could have tightened the norms for LoUs and introduced safeguards instead of completely banning the LoUs.
About:
• SWIFT is a global member-owned cooperative society under Belgian law.
• Founded in: It was founded in 1973 by a group of 239 banks from 15 countries
• Headquarters: La Hulpe, Belgium.
• Sibos: Sibos (Swift International Banking Operations Seminar), is an annual banking and financial conference organized by the SWIFT in various cities around the world.

What it Does?
• Primary role:
  • The SWIFT is a secure financial message carrier — in other words, it transports messages from one bank to its intended bank recipient.
  • Its core role is to provide a secure transmission channel so that Bank A knows that its message to Bank B goes to Bank B and no one else. Bank B, in turn, knows that Bank A, and no one other than Bank A, sent, read or altered the message en route.
• SWIFT codes: Apart from this, it also sells software and services to financial institutions, much of it for use on the SWIFTNet Network, and ISO 9362. Business Identifier Codes (BICs, previously Bank Identifier Codes) are popularly known as “SWIFT codes”.

What it Doesn’t?
• SWIFT does not facilitate funds transfer: rather, it sends payment orders, which must be settled by correspondent accounts that the institutions have with each other.
• It does not hold accounts for its members.
• It does not perform any form of clearing or settlement.

Status of Usage:
• The majority of international interbank messages use the SWIFT network.
• As of 2015, around 11,000 financial institutions in more than 200 countries were linked with SWIFT. They were exchanging around 15 million messages per day.

Benefits of SWIFT:
• Before SWIFT, Telex was used for message confirmation for international funds transfer.
  • It was slow and there were security concerns as well.
  • It didn’t have a unified system of codes like SWIFT to name banks and describe transactions.
• The senders were to describe every transaction in sentences which were then interpreted and executed by the receiver. This led to many human errors.
• In comparison, SWIFT is a faster means of communication between financial institutions.
• It is much more secure than earlier system. SWIFT established the customer security programme (CSP) in early 2016 to support customers in the fight against a growing cyberthreat.
• The communication is done in a standardized way. This eliminates human error.

In News:
• In the PNB scam it was found that the funds were siphoned off from the bank by willfully manipulating the SWIFT.
• Infact, in the aftermath of PNB Scam, Reserve Bank of India (RBI) stated this week that it had privately warned Indian banks about the prospect of misuse of SWIFT at least three times since August 2016.
• However, this is not the first time that as SWIFT has been misused by miscreants on a number of occasions.
  • In 2016, there was a cyber-heist of $81 million from Bangladesh’s central bank.
  • Russia’s central bank recently reported that $6 million was stolen from a Russian bank last year by exploiting the SWIFT system.

Concerns with SWIFT:
• With increase in volume of transactions, there is increased need of automation. This will increase the cost and operational overhead.
• SWIFT is often used as instrument of foreign policy, especially by USA and European countries. SWIFT ban was one of the method to persuade Iran to negotiate on its nuclear policy. Their frequent use will hamper its credibility and neutrality.
  • Russia and china are already planning to develop an alternative network.
• SWIFT is not infallible and can be hacked as was evident in the recent case of $81 million heist from Bangladesh’s central bank.
• It is also vulnerable to manipulation by bank insiders as was seen in case of PNB scam.

Way Forward:
• At present, SWIFT is an important component of international financial infrastructure.
• Thus there is need to make it more secure to increase confidence in it. It should be able to maintain its neutrality to enable it to be widely used in the world.
Implications of PNB Fraud:

- Impact on Banking sector:
  - Depositor’s faith in banking system: People faith in keeping their savings in banks has been affected more so after limited protection to bank deposits under Financial Resolution and Deposit Insurance (FRDI) Bill, 2017.
  - NPAs: Indian Public sector banks already facing great challenge of mounting Non Performing Assets (NPA), this case has put additional pressure on banks. The scam may increase the NPAs of the banks, specially the banks who are directly exposed to the scam.
  - Buyer’s credit: RBI had banned LoUs after the scam. This will impact the $85 billion buyers’ credit market and affect the earnings of banks.
  - Basel norms: Despite Centre government capital infusion plan of Rs 1 Lakh core in 21 capital stared PSB, PNB will be back to the same level before the recapitalisation due to loss suffered due to this fraud.

- Impact on Trade: Ban of LoUs will increase the cost for importers. It will also negatively impact the competitiveness of exporters who import raw materials.

- Impact on Gems and jewellery sector: The Banks will now be cautious and reluctant towards the sector. It will impact the sector’s ability to access credit. It will dampen the market sentiments towards the gems and jewellery.

Steps taken in aftermath of PNB scam:

- The government has asked PSBs to ensure strict compliance with all regulatory norms and proper audit of their foreign branches.
- Fugitive Economic Offenders Bill, 2018 was introduced in Lok Sabha in March 2018 to seize all domestic assets of a person deemed to be a fugitive economic offender.
- National Financial Reporting Authority (NFRA) is to be setup as an independent regulator for the auditing profession (CAs).
- Malegam panel has been setup by RBI to look into frauds.

Way Forward to Prevent Bank Frauds:

- Strengthening Corporate Governance:
  - The basic line of defence against fraud is the internal controls in a bank. Thus there is need to strengthening corporate governance in public sector banks and infuse greater professionalism, transparency and accountability.
  - For this, bank boards, and especially the audit committees, must have clear responsibilities.
  - Banks can also set up a special fraud monitoring agency, with officials specially trained to detect incipient frauds.

- Use technology:
  - Technology should be used for internal controls as it can reduce the chances of human connivance, make it difficult for individual employees to bypass controls and can be used to detect outlier lending or guarantees.
  - Blockchain technology could be used to make banking transactions more transparent. This would mean that every link in the chain can be scrutinized publicly.

- Role of RBI:
  - Reserve Bank of India (RBI) will have to build capabilities, both in terms of designing rules and making sure that they are effectively implemented.
  - It will be a delicate balancing act, since over-regulation could scare bankers off any sort of lending. For now, the RBI has done well to constitute an expert committee to look into the rising incidence of frauds.

- Audit the auditors:
  - The role of third parties such as chartered accountants, auditors, and advocates who figure in bank frauds should also be examined with a tough eye.
  - In fact, the regulator should design stringent systems where auditors are not able to get away with fraudulent financial statements.

- Consider privatization:
  - According to some quarters, government should consider the idea of privatizing public sector banks (PSBs), as reforms will be successful only when banks are free of political and bureaucratic control.
  - However, this is debatable.

Apart from this government should consider the following steps:

- Restore faith of Depositors by raising Deposit Insurance cap of Rs. 1 Lakh can to 5 lakh under FRDI bill.
- Pass FEO bill, 2018 to seize all domestic assets of a person deemed to be a fugitive economic offender.
Arguments for Privatisation:

- **Political interference:**
  - PSBs are often subjected to political pressures to disburse loans to friendly companies or industrial houses which also contribute to mounting NPAs.
  - It will also end steps like farm loan waiver and will help in ending vote bank politics in country.

- **Conflict of Interest:** By holding stakes in PSB, Government’s role as owner of banks as well as regulation of banks leads to conflict of Interest. This needs to change.

- **High NPA in PSBs:** As much as 90% of the Non-Performing assets (NPA) is in books of PSBs.

- **Use of Public Money for bailout of PSB:**
  - Government is recapitalizing PSBs to address the problem of NPAs.
  - But recapitalization alone is not a permanent solution and will be ineffective if inherent structural problems of PSBs are not address. Privatization of PSB is expected to address these issues.

- **Prone to Corruption and Crony Capitalism:** PSB’s employees as well as top management are paid less than their private counterparts; further there is pressure from bureaucracy and politicians creating fertile ground for PNB like frauds.

- **Risk management:** Privatization will streamline their risk management. It will improve the risk assessment before disbursement of loans and will also lead to better and timely recovery of loans.

- **Level playing field:** Privatization of PSBs will provide level playing field in the banking sector with respect to supervisory restrictions and it will improve competition in the sector.

- **Customer satisfaction:** Privatization would foster increased competition, which would reduce the cost of financial intermediation, improve bank profitability and improve customer service.

Arguments against Privatisation:

- **Problem lies in regulation:** Pro-privatisation argument is predicated on the neat ‘government is bad, private is good’ binary, which is wrong. The key reason for PNB like fraud is one of poor regulation, and not ownership.
  - Corporate India’s biggest scam involved a private sector company, Satyam Computers, not a much derided PSU.

- **Lesson from subprime mortgage crisis of 2008:**
  - The world was shaken by the Lehman Brothers’ collapse and the subprime mortgage crisis in the US. None of the banks involved in this mess was under public — government — control.
  - Ironically it was the US government that had to ‘bail out’ these privately-owned banks by pumping money into them and ensuring they didn’t keel over.

- **Risky private banks loans:** Private sector banks are not immune to NPAs and other problems present in PSB. Private Banks such as Axis and ICICI also face large NPAs, often with the same companies that are defaulting on public banks.

- **Parallel re-nationalization development in UK:**
  - Right now, infact there is an intense debate in the UK over whether or not the railways and others should not be re-nationalised.
  - A significant section of citizens, mostly supporters of the Labour Party, feels that the privatisation initiated by Margaret Thatcher has not worked.

- **Financial inclusion:** Privatization may result in excessive focus on profit and may make banking costly for common man. PSBs were at forefront in implementation of financial inclusion schemes like Jan Dhan Yojana. Privatization may affect financial inclusion.

- **Welfare schemes:** PSBs act as a channel to extend benefits of their welfare schemes to the people and sectors like MSMEs. Privatization will close this route and make it difficult for government to carry its many schemes.

- **Development agenda:** PSBs are at the forefront to finance sectors like infrastructure and big projects. Privatization may affect such sectors and may affect development of country.

- **People’s faith in banking:** Implicit sovereign guarantee through PSB still generates trust among people in the public banking system.

Way Forward:

- Privatization of PSB is not the golden bullet which is going to solve all the problems of PSBs and banking sector.
- There is need for stricter adherence to sound banking rules and more transparency and accountability from both public and private players.
- For addressing the structural problems of PSB, government should consider the implementation of PJ Nayak committee recommendations.
- Even if we go for bank privatization, it should be done in phased manner.
- But it should be remembered that Bank privatization requires significant political consensus and thus may not be politically feasible.