



Red Flag Indicators Report

**Analysis of Major Media Stories that
Indicate Serious Breach of Internal Controls
“ Coverage - April to June 2016”**

**Compiled by
VERITA Management Advisors Pvt Ltd**

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Preface

This publication aims to create awareness on the subject of Fraud Risk Governance. Fraud is a real risk impacting Indian organization in a big way. The techniques deployed by fraudsters are complex and usually masked in a web of falsehood, forgery and cheating.

Businesses find it very difficult to unearth frauds and serious control breaches therefore we believe that dissemination of Red Flag Indicators report and related information (primary goal of this publication) would assist in developing robust defense mechanisms.

It is famously said that forewarned is forearmed keeping this in mind our publication team has researched on newspaper and electronic media stories from leading portals on the subject of fraud and red flags. Post research a crisp compilation of red flag stories has been compiled for readers highlighting the nature of breach, quantum of impact and modus of the operator to the extent available in public domain.

We welcome your valuable feedback and review comments on this publication on contactus@verita.co.in.

VERITA KNOWLEDGE MANAGEMENT TEAM

September, 2016
MUMBAI

1. Falsification of books of accounts

Company: Ricoh India, Subsidiary of Ricoh, Japan

Sector: Managed Print Services

Nature: Fraudulent Financial Reporting/ Falsification of Accounts

Modus: It appears to be a case of falsification of accounts, violation of accounting standards and principles. Media reports suggests that revenue, receivables and loan figures were padded up to show a rosy performance of the company.

Quantum & Impact: INR 1,123 Cr (approx.), however, total quantum yet not established. Company has accepted accounting fraud and conclusive investigations are in progress. Following this incident, Ricoh India's chief executive and managing director, Manoj Kumar resigned along with the chief financial officer (CFO) Arvind Singhal and senior vice-president and chief operating officer (COO) Anil Saini, after they were asked to go on leave. The stock exchange, in its notice, said Ricoh India, would be shifted to the "Z" group, with effect from 28 March (2016) due to non-compliance with listing norms for two consecutive quarters. Ricoh India's shares have since been suspended from trading. Tetsuya Takano's (the recent director/chairman) resignation is the most recent high-profile casualty of this fraud.

Sources: Live Mint, Print Week

Comments: This report appears to be similar to the Satyam fraudulent financial reporting scandal where the executive team showed rosy performance by window dressing the books to mislead stakeholders.

2. Bogus share trading and tax evasion

Company: Om Investments

Sector: Brokerage

Nature: Bogus share trading and evasion of tax

Modus: OM Investment allegedly cheated the government by not paying taxes by working as a share trading operator but not trading on any stock exchanges. They would write down details through the day, while the investors were told that investment was being done. Since no contract notice is given and all transactions were done secretly, no tax was paid to the government on these transactions.

Quantum & Impact: Daily turnover of Rs 5 crores the fraud is expected to run into several crores. The Economic Offences Wing (EOW) of the Mumbai Police arrested Vinod Shah - owner of Om Investments, Arun Singh and Pradeep Chavan from their Malad Office. A case of cheating under Securities Contract Act was registered against the three.

Source: Indian Express

Comments: It appears to be a case where bogus trading and documentation are created for clients so that they can evade taxes

3. Fake share transfer & dividend diversion

Company: Sharepro

Sector: Share Registry

Nature: Diverting of dividends and wrongful transfer of shares

Modus: Sharepro created demat accounts under fake names to transfer shares of its clients to the relatives of the company.

The legal manager of Asian Paints, filed a case of cheating with the Mumbai Police during end March this year, against Sharepro, to whom Asian Paints had transferred the job of handling its share market related work like distributing the company profits to shareholders with a contract for the period 2003-2017. After shareholders of Asian Paints complained they had not been receiving profits / dividend due to them, the company found the money was given to some other people by Sharepro.

Quantum & Impact: Rs. 17.98 crores – The amount cheated over the period. The Economic Offences Wing (EOW) of Mumbai police arrested Govindraj Rao, 75, the managing director, and Indira Karkera, 52, the operations head, and produced them in court where they were remanded to police custody till April 5.

Sebi imposed an interim ban on Sharepro, its promoters and other related entities after serious lapses were found post investigation. In an order, Sebi said it found Sharepro indulged in falsification of records, forgery and not maintaining internal checks and balances while transferring shares and dividend encashment. Rao and Karkera have been booked for cheating, and forgery under the Indian Penal Code.

Sources: Business Standard; Live Mint5

4. Castor seeds cartelization

Company: Ruchi Soya, National Steel and Agro Industries

Sector: Agriculture

Nature: Fraudulent market controlling of soya trading to acquire and control dominant market share.

Modus: The Ruchi group entities traded in high magnitude with the potential to disturb the market equilibrium and harm market integrity. On 18 occasions Ruchi group entities violated commodity level client position limits and on six occasions it violated near month client position limits. Ruchi Soya actually provided funds to five clients for creating and maintaining open position on long side in castor seed contract.

Quantum & Impact: Collectively, Ruchi Group Entities were holding 111600 MT of Castor Seed position in February 2016 out of total 283260 MT or 39.39% of open position available in February 2016; with a value of approximately Rs 340 crore. Sebi barred Ruchi Soya Industries and National Steel and Agro Industries from the securities market for this fraudulent and manipulative in trading.

Sebi noted that prima facie Ruchi Soya Industries and National Steel and Agro Industries, being part of 'Ruchi group, have violated the position limits prescribed by erstwhile Forward Markets Commission (FMC) in October and December 2014. The scheme was not only to disturbed market equilibrium, but also to form a cartel and corner the Castor Seed market

Noting that detailed investigation of entire scheme, plan, device and artifice employed by concerned entities is necessary, Sebi said the role of four other entities funded by Ruchi Soya Industries -- Stride Multitrade Pvt Ltd, Bharat Foods Co-operative Ltd, Anuj Jain and Sisne Polymers Pvt Ltd.

This latest crack down for irregularities in the commodities derivatives market comes less than three months after it banned 16 brokers and traders from the securities market for manipulation in castor seeds trading at the bourse.

Sources: Economic Times, First Post, Live Mint, Sebi.gov.in

1. Fraud by tech junkie

Company: NA

Sector: NA

Nature: SIM card and e-wallet fraud

Modus: Rajesh Kumar Gupta and his associate Rajesh Mondal opened around 2,000 accounts with a bank across West Bengal, against which they opened over 18,000 e-wallets, siphoning off crores of rupees, by using some inherent lacunae in the functioning of these e-wallets. The gang used thousands of pre-activated SIM cards for it.

Quantum & Impact: The private bank from Kolkata was duped of Rs. 8.5 crore. Based on a complaint lodged by the bank officials in December, 2015, the police arrested eleven people, including five engineering students.

Source: Times of India

Comments: It appears that information security and related vulnerabilities have been exploited.

2. Diversion of funds

Company: Leela Ventures, Nagpur

Sector: Real Estate, Pharmaceutical

Nature: Banking Fraud through Cash Credit

Modus: A Nagpur branch of Union Bank had sanctioned cash credit and term loans to Leela Ventures. However, instead of using the money for the stated purpose, Leela Ventures diverted the funds to its sister concern. The company also did not submit bills of suppliers to the bank as required and mortgaged a property which was already acquired by the government. The collateral security was also not adequate and the company had defaulted in repaying the loans.

Quantum & Impact of Fraud: According to CBI, the bank has been defrauded to the tune of ~ Rs. 38 crores.

The CBI conducted searches at the company's offices in Mysore and Pune apart from the city office in Nagpur and recovered documents related to the case leading to the banker as well as the business couple being booked for criminal conspiracy, fraud and breach of trust.

Leela Ventures is run by businessman YVSS Raju and his wife Y Suvarchala, and are prominent names in the local realty sector.

Sources: Times of India, Business Standard

3. Siphoning of public money

Company: Varia Engineering Works Ltd, Ahmedabad

Sector: Cold Rolling

Nature: Cheating & forgery

Modus: Himanshu Varia, the director of the company, who is accused of siphoning off public money by cheating a subsidiary of a nationalized bank, had obtained factoring facility from Canbank Factors Ltd, through signed applications and forged and fake authority letters and other documents. He did not return the money that was expected to be returned within the stipulated time period.

Quantum & Impact: The amount in question is Rs 5.66 crore.

While a criminal complaint for cheating and forgery was filed against Himanshu Varia, Gujarat high court (HC) denied anticipatory bail to him. Fearing arrest, he moved to the High Court, which again refused him protection with observation that his role is prima facie established right from the date of filing application for factoring facility. The HC mentioned that the complainant is a subsidiary of Canara Bank and huge public money has been siphoned off as alleged and therefore, no lenient view can be taken in the case. And since Varia himself had signed all papers and applications and submitted forged and fake authority letters and other documents - for free, fair and meaningful investigation, interrogation of the applicant is eminent without any umbrella to reach the truth.

Sources: Times of India, Hunt News

Comments: It appears that on fake documents and authority letter were created in this case. Therefore, the vulnerability exploited in lack of supervision and management review of authority and other key documents

1. Impersonation

Company: NA

Sector: NA

Nature: Cheating & Impersonation

Modus: A mimicry artist from Lucknow, Ajay Kumar Yadav, posed himself as a girl and made phone calls to the employees of a leading telecom company until he gained their confidence. He would then extract codes related to money transfer schemes and used it to defraud its dealers.

Quantum & Impact: Quantum undisclosed. Ajay Kumar Yadav was arrested on the complaint of Sachin Jani a dealer from Amethi in end April 2016.

Sources: Times of India, nyoooz.com

2. Advance monies collected towards flats without approvals to construct

Company: Sai Enterprises, Navi Mumbai

Sector: Real Estate

Nature: Cheating by collecting money from prospective buyer of flats on development without proper permissions.

Modus: The builder had floated a project, Parth Residency and collected money from prospective flat buyers. CIDCO issued a notice to the firm in 2015, ordering it to stop construction, as no permission was obtained under the Maharashtra Regional Town Planning Act, post which construction was abandoned. An HC bench in March 2015 gave the builder a month to obtain permission from CIDCO. Despite no approval to construct the building the company had gone ahead and sold the flats collecting money.

Quantum & Impact: 69 flats were sold without permission.

The Bombay high court rejected Anil Nanaware, the owner's plea for pre-arrest bail noting that cheating people by promising them flats is a serious offence that affects society. "Prima facie, the applicant dishonestly induced persons to book apartments when he (did not have) valid authority or permission to develop. The applicant secured huge amounts from the public at large. The offence has serious repercussions on society as well as public at large. He breached the trust reposed in him by his customers. This court has noticed several such instances of cheating by builders," said Justice Anant Badar.

Though Anil Nanaware had offered to repay the amount collected from the flat buyers, the HC said that it can't be considered. "Considering the nature of offence and involvement of the interest of many people, preference cannot be granted to the personal liberty of (Nanaware). That apart, his custodial interrogation is necessary," the judge said.

Source: Times of India

3. High Return on Investment Trap

Company: Kamakshi Forex Pvt. Ltd, Margao

Sector: FOREX

Nature: Cheating and Misappropriation of investments

Modus: Nilesh Raikar, the owner, used to give post-dated cheques to people who exchanged foreign currency with his firm. Raikar had asked several Goan seamen and their families to invest their foreign exchange in his company and promised them triple interest on their money. Some of these post-dated cheques issued were not proper, with no proper signatures and in many cases the cheques were signed by the employees. Several of these cheques bounced.

Quantum and Impact: 550 investors duped to the tune of over Rs 35 – 50 crore. On April 22, EOC arrested Nilesh Raikar after he surrendered to them and is in judicial custody. EOC had also taken into custody Raikar's wife Nilima and mother Rekha, but subsequently released them on bail. The FIR was registered under Sections 406 (criminal misappropriation of property entrusted to someone), 420 (cheating) and 120-B (criminal conspiracy) of the Indian Penal Code (IPC).

The case is now (June 2016) transferred to Central Bureau of Investigation (CBI) as per the Bombay High Court's directive. The investors have sought reinvestigation of the case by CBI citing nexus between police, politicians and government servants in the case.

Sources: Herald Goa, Times of India, Navind times

4. A call center of frauds

Company: NA

Sector: NA

Nature: Cheating and Impersonation

Modus: Santosh Mahato from Dhanbad, Jharkhand is a member of the gang that used to call up people posing as bank employees and get confidential details of their accounts. The gang collected ATM PINs from these people and siphoned money from their bank accounts. According to Santosh, he had given the management of his bank account to one Babloo Das who used to pose as bank employee and make phone calls to people and keep 10 per cent of the siphoned cash for himself and kept the rest for Babloo. But the police suspect that Santosh too used to make such calls.

The duo had employed youngsters between 15 to 25 years of age to operate the scam just like an organized call centre. These people were, however, spread out in different places and worked at their convenience. They are even trained in speaking English to convince the people targeted.

Quantum & Impact of Fraud: From Jharkhand, amount of money siphoned approximates ~Rs 74,000.0. On investigation it was found that Santosh's bank account saw deposits worth Rs 11.29 lakh between January 2015 and June 2016 proving that the gang may have duped many people across the country and was not operational only in Dhanbad.

Santosh was arrested by the detection of crime branch (DCB) sleuths from Vadodara and was brought to the Jharkhand city for further investigation.

Sources: Times of India, Rediff Local News.

1. Credit rating agencies face SEBI action

Company: CARE & CRISIL

Sector: Rating & Research

The case: Investigation is initiated against rating agencies Credit Analysis and Research Ltd (CARE Ratings) and Crisil Ltd in the matter of rating Amtek Auto's debt paper and JP Morgan's corporate debt fund. Sebi launched the probe after JP Morgan India Treasury Fund and JP Morgan India Short Term Income Fund faced the redemption crisis in August 2015 brought on by a sharp downgrade and withdrawal of ratings on Ametek bonds, which was on the verge of defaulting on Rs.800 crore in bond repayments.

The crisis drew attention to the conduct of the rating agencies in assigning a credit rating to the Amtek Auto bonds and the JP Morgan schemes. CARE Ratings chose to suspend its rating on Amtek Auto on 7 August 2015. The agency had earlier given Amtek Auto an AA- rating, which signifies a high degree of safety regarding timely servicing of financial obligations. Such instruments carry very low credit risk. The 'minus' with the rating signifies a low standing within the category.

As per Sebi regulations, a credit assessor cannot suspend its rating on an outstanding debt security unless the security is clubbed with another security or the company merges with another. Such Suspension of rating is a violation as per Sebi regulations. Even if a company is not disclosing relevant information pertinent to the rating, an agency is required to assign a rating based on available information, with a caveat that there is lack of information. Crisil Ltd had assigned a rating of AAAmfs (signifying the highest portfolio credit quality) to the JP Morgan India Treasury Scheme in May 2015. Subsequently, Crisil revised the rating for the scheme in three stages over two months. On 1 September, it downgraded the scheme from AAAmfs to A+mfs. On 29 September, the scheme was downgraded to BBBmfs, which meant an eight notch downgrade within a month. Finally, on 15 October, Crisil placed the scheme on "notice of withdrawal".

The Impact: SEBI is likely to act against two rating companies and this action would mark the first time the Securities and Exchange Board of India taking any rating companies to task.

Sebi is in the final stages of its investigation and will decide the nature of action to be taken once the investigation is complete.

While investigating individual agencies, Sebi is also in the process of tightening rules and disclosure norms for rating agencies in general. Sebi is likely to ask rating agencies to set up independent internal assessment teams, which will be required to determine whether the rating assigned to a company is appropriate or not.

This will be over and above the team which assigns the initial rating. Sebi may also ask rating agencies to give clear reasons if they choose to withdraw their rating on a company.

Tougher norms for rating agencies have become necessary in the light of recent developments. Apart from the Amtek Auto episode, there have been other cases where sharp and sudden downgrades have left investors in the lurch.

Sources: Business Standard, Live Mint, Money Control

2. The Curious Case of Freedom 251

Company: Ringing Bells

Sector: Telecom

Details: Ringing Bells launched India's most affordable smart phone called Freedom 251 for a price of Rs 251 in February 2016. The company claimed 30,000 people paid for booking the phones, and over 7 crore people registered for it. The payment was facilitated by CC Avenue and PayU Biz.

With the frenzy about Freedom 251 growing wild in February, the then Telecom Minister Ravi Shankar Prasad asked Department of Electronics and IT Secretary (Deity) Aruna Sharma to look into the scheme of Ringing Bells offering a smart phone for just Rs 251.

DoT also came into the picture when it said that the pricing of the phone as offered is not possible, as a smart phone with such specs would at least cost Rs 2,300 just to build.

Indian Cellular Association, which represents the handset makers industry in India and has members like Apple, Samsung, Microsoft, Lava and Micromax, wrote to Telecom Minister to intervene.

ED is also investigating Ringing Bells for alleged FEMA violation.

More curiously, when Ringing Bells first launched Freedom 251, it gave out some 'review units' of their phone which was later discovered to be a different phone by another company called Adcom. Ringing Bells had simply erased the Adcom branding using a whitener. Adcom threatened legal action against Ringing Bells.

Trouble didn't end here for Ringing Bells. Cyfuture, a provider of data center and business process outsourcing (BPO) services filed a police complaint against the company alleging fraud and non-payment of dues and seeking Rs 80 lakh as damages. Cyfuture claims it was contracted by Ringing Bells to provide call-center support for its smart phone brand in India, and the company did not fulfill payments due to them.

The other complaints against Ringing Bells are related to its claim that the phone is "Made in India" while this phone is made in China and the company doesn't have any factories in India; the other being the phones' noncompliance with BIS registration based on Indian safety standards effective September 13, 2015 which is mandatory for all electronics goods since Oct 2012.

Current Situation: Ringing bell has returned money to its subscribers post the bad press and has offered cash on delivery to its customers. It has made its first set of deliveries of 2,200 handsets on July 10, 10 days after its promised delivery date of 30th June. The company had promised to deliver 200k handsets out of 7 crore people who registered for Freedom 251. Other cases are pending.

Sources: Indian Express, Economic Times, Times of India, India Today, news 18

About VERITA

Verita Management Advisors is a Private Limited Company incorporated in India. The company offers Governance, Risk, Compliance, Direct and Indirect Tax Advisory and Outsourcing Services. Head quartered in Mumbai with a network of like-minded, quality conscious network firms across the country. Outside India Verita has network offices at UAE and Oman. This publication has been prepared by the knowledge team of Verita Management Advisors Pvt. Ltd. The team has exercised due care while preparing this publication, however, it has been written in general terms and should be taken as a broad and indicative reference only. The knowledge team has placed reliance on various public sources on the internet and as such does not vouch for their accuracy.

Contact Us

VERITA MANAGEMENT ADVISORS PRIVATE T LIMITED

A-78, First Floor, Virwani Estate, Opposite: Westin,
Off. Western Express Highway, Goregaon (East),
Mumbai – 400 063.
Tel: 022 29272030

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