

Red Flag Indicators Report

**Analysis of Major Media Stories that
Indicate Serious Breach of Internal Controls
“ Coverage - June to September 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 amrita.pandilwar@verita.co.in and huzeifa.unwala@verita.co.in

VERITA KNOWLEDGE MANAGEMENT TEAM

November, 2016

MUMBAI

1. Fraudulent Payments to Interested Parties

Company: A large Insurance Player

Sector: Life Insurance

Nature: Cheating, Fraud, Criminal Conspiracy

Modus: It appears to be a case of Cheating and Criminal Conspiracy. Investigations have revealed that public funds were siphoned off by four insurance company officials into the bank account of Mechmen Motors using National Electronic Funds Transfer (NEFT) route in March this year.

Quantum & Impact: Approximately Rs. 2.4 crores were paid through National Electronic Funds Transfer (NEFT) to the directors of Machmen Motors in March 2016. A case of cheating (section 420) and criminal conspiracy (section 120B) of IPC and also for offences under the Prevention of Corruption Act has been registered against the LIC officials and the directors of Machmen Motors.

Source: Hindustan Times

Comments: Control deficiency in the area of authority limits set for bank payments. It appears that authority was centralised for payments and it was possible to override controls on account of lack of segregation of duty in the bank payment transfer process.

Web link: <http://www.hindustantimes.com/bhopal/rs-2-4-crore-lic-fraud-cbi-raids-11-places-in-bhopal/story-MYt9exDVfVmLT7BKimaJfP.html>

2. False representation of a Bank Guarantee

Persons Involved: Dayashankar Singh and Jitendra Singh

Sector: Banking

Nature: False Bank Guarantees

Modus: It appears to be a case of false bank guarantees to get dealership for selling Tractors. It is observed that false guarantees are given by the agency (partnership business).

Quantum & Impact: A false representation of a guarantee given upto the extent of Rs. 60 lakhs by the Sukhpura Branch of a Public Sector Bank was given by the above persons to Mahindra & Mahindra for the purpose of securing an agency for tractors and their spare parts. Mahindra & Mahindra had given its dealership to the above persons on the basis of the guarantee and supplied tractors & parts worth Rs. 72 lakhs for which it did not receive any payment.

Source: Economic Times

Comments: Failure to conduct proper due diligence on customer documents before the contract is entered into. Forged documents represent a growing risk and organisations should develop forensic test checks to verify the authenticity of customer documents either through document examination techniques or third party confirmatory checks

Web Link: <http://economictimes.indiatimes.com/news/politics-and-nation/dayashankar-singh-brother-booked-for-fraud/articleshow/54461578.cms>

3. Falsification of documents and accounts for personal benefit

Company: Essex Holdings

Sector: Investments and holdings

Nature: Falsification of Financial Statements, Forgery, False promises of Fixed rates of returns.

Modus: It appears to be a case of falsification of financial statements, forging documents and incompatible promises of fixed rate of returns to Investors to induce more investors to invest in the company. The fraud proceeds were used for personal purposes by the CEO and his wife.

Quantum & Impact: The CEO, Navin Shankar Subramaniam Xavier, used a false financial statement, forged documents, and false promises of fixed rates of return, to induce investors to invest with Essex Holdings and raised more than USD 29 million from nearly 100 investors for supposed investments in sugar transportation and shipping, as well as iron ore mining in Chile. In a second scheme, Xavier used Essex Holdings to obtain USD 1.2 million in payments and approximately USD 1.5 million worth of commercial real estate from the South Carolina Coordinating Council for Economic Development (SCCED), a division of the South Carolina state government, that was supposed to be used to develop a dilapidated industrial property into a diaper plant and rice packaging facility, by providing false financial documentation and fake contractor invoices and bank statements.

Source: Economic Times

Comments: This is a classic case of fraudulent scheme involving falsification of documents and accounts to paint a rosy picture thereby cheating the innocent investors. Investors should follow due diligence norms prior to placing investments that should at a minimum include verification of registrations of with government authorities, credit rating reports, auditor report, past performance track records, investor cross checks, etc.

Web Link:

http://economictimes.indiatimes.com/articleshow/54375238.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst

4. Fraud by Investee Company

Company: VSoft Technologies

Sector: Software

Nature: Fraudulent and deceitful diversion of funds

Modus: The case is about deceitful diversion and fraudulent diversion of funds to the related party. Peepul Capital, the investor company filed a complaint with Hyderabad police against accused company i.e. VSoft Technologies. The CEO of the accused company is charged with diverting funds from VSoft Technologies to another company which he and his wife jointly own.

Quantum & Impact: VSoft Technologies is primarily accused of fraudulent and deceitful diversion of funds to a related party, amounting to Rs. 25 crore. The legal tussle is still on wherein the CEO claims that the funds paid to the said related party, i.e. Smart Staffing was expense for the services received and was duly disclosed in the books of the company.

Source: Economic Times

Comments: It appears to be a case where funds are siphoned by the the management of the company under the guise of expenses for their own benefit.

Web Link:

http://economictimes.indiatimes.com/articleshow/54418638.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst

1. Manipulation of Interest rates

Company: Barclays Bank PLC

Sector: Banking

Nature: Interest rate Manipulation

Modus: In this case The British financial giant Company Barclays Bank PLC undergone interest rate manipulation in the financial crisis era. As part of a 16-member panel of banks making submissions to help set daily Libor rates, Barclays manipulated submissions between 2005 and 2009 to avoid the appearance that it paid more than its competitors to borrow or to favour traders' positions.

Quantum & Impact: A settlement of \$100 million has been reached between the bank and 44 US States and the District of Columbia which will be used to compensate other organizations holding investment contracts with Barclays who may have been victimized while the rest will cover the costs of investigation and administration.

Source: NDTV News

Comments: This appears to be the case where bank has indulged into fraudulent interest manipulation for the purpose of exploiting the instability in financial markets. Such frauds are committed at the highest level and only comprehensive entity level controls can be a good deterrent against such frauds. Entity level controls can prevent management override provided they are designed, approved, implemented and communicated effectively. Audit Committees can play a pro-active role in reviewing Entity Level Controls at organisations.

Web Link: <http://profit.ndtv.com/news/international-business/article-barclays-us-states-in-100-million-libor-fraud-settlement-1441965>

2. Credit Card Fraud

Company: NA

Sector: NA

Nature: Unauthorized money transfer

Modus: In this case, Sawan Verma, (25) and Manish Rai (26), convinced people to share their passwords, which they then used for shopping and other transactions. They then reportedly transferred the duped amount through a mobile banking app. "The duo used to gather details about the credit, ATM and debit cards from people, posing as bank officials on the pretext of card verification and used Paytm Mobile Solutions' to transfer the amount in another bank account in Jharkhand.

Source: Hindustan Times

Comments: There has been an increase in the number of frauds by conniving persons who lure the public into sharing their passwords and other confidential details. Public awareness regarding such frauds should be increased.

Web Link: <http://www.hindustantimes.com/delhi/techie-among-two-held-for-credit-card-fraud-in-delhi/story-HEL8qbOzAqx61mtTyYOAnM.html>

3. Fraudulent Insurance for crops

Company: NA

Sector: Agriculture

Nature: Over insurance of risky Crops

Modus: Farmers have found an ingenious but improper way to maximize their cash flow -by taking loans and insurance cover for a much bigger area and a more capital intensive crop than they cultivate, while banks don't bother to cross check as they are under pressure to show higher lending to the priority sector.

Quantum & Impact: The government is considering strict measures including heavy penalty for misdeclaration of the crop and the area insured to end the menace which includes scaling down of subsidies given on premium payments. The Centre is determined to rectify during the implementation of the Pradhan Mantri Fasal Bima Yojana (PMFBY), the biggest-ever crop insurance scheme, for which Rs. 5,500 crore have been allocated in the budget.

Source: Economic Times

Comments: This is a case where the farmers have taken advantage of a favourable incentive of government to increase their cash flows.

Web Link:

http://economictimes.com/articleshow/54437516.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst

4. Manipulation of Currency Prices

Company: MNC Bank

Sector: Foreign Exchange Trading

Nature: Misusing confidential information to manipulate currency prices

Modus: Two senior executives have been accused of doing front-running by cheating a client that was selling part stake in an Indian subsidiary. Cairn had selected MNC Bank to conduct the Forex conversion transaction from amongst ten banks it had asked to bid for the right while asking them to sign a confidentiality agreement regarding the information about the transaction. MNC Bank was later mandated by Cairn for carrying out the foreign exchange transaction and also signed a confidentiality pact, but the duo conspired to buy sterling "in advance of the transaction, knowing that the transaction would cause the price of sterling to increase, thereby generating substantial trading profits for the bank and the defendants".

Quantum & Impact: The overall impact of the fraud was \$3.5 billion with a profit of \$8,000,000 to the bank from its execution of the forex transaction for the victim company, including profits generated from the front running conduct.

Source: NDTV News

Comments: This is a case where misrepresentations are made regarding the foreign exchange transactions which lead to currency manipulation.

Web Link: <http://profit.ndtv.com/news/corporates/article-india-link-emerges-in-3-5-billion-forex-trading-fraud-at-hsbc-report-1434435>

5. Compromise in Debit Card Details

Banks affected: Leading bank

Sector: Banking

Nature: Breach of financial data due to hacking of payment systems

Modus: The breach is said to have originated in malware introduced in systems of Hitachi Payment Services, which provides ATM, point of sale (PoS) and other services, enabling fraudsters to steal information allowing them to steal funds. A forensic audit has been ordered by Payments Council of India on Indian bank servers and systems to detect the origin of frauds that might have hit customer accounts. Around 3.2 million cards were used on Hitachi network, the data of which might have been compromised. As a precautionary measure, a leading bank has blocked 6 lakh cards which would be re-issued shortly.

Source: Economic Times

Comments: This is an instance of a cyber-crime in which advantage is taken of an inherent weakness in the software of the payment system adopted by the banks is exploited which has resulted in a serious breach of confidential financial data and subsequent misuse of funds. To avoid it, there can be periodical tests and controls through ethical hacking to test the system's robustness.

Web Link:

http://economictimes.indiatimes.com/articleshow/54945561.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst

1. Bribery by Airport Director

Company: NA

Sector: Airline

Nature: Corruption and Bribery

Modus: In this case, the culprit demanded bribes for ground clearance. The complainant had alleged that the Director, Airport Authority of India, posted at [Aurangabad Airport](#) (Maharashtra) was maintaining details of the non-scheduled flights and demanded bribe per flight from the ground handling private companies at Aurangabad Airport.

Source: Times of India

Web Link: <http://timesofindia.indiatimes.com/city/aurangabad/Aurangabad-airport-director-arrested-for-graft/articleshow/53474120.cms>

2. ATM Card Cloning

Company: NA

Sector: Banking

Nature: Stole money from ATM

Modus: It appears to be a case of theft. A fraudster stole money from the account of a property broker by cloning the data of his debit card and using it in an ATM in Mumbai. The data was copied by just rubbing the card on one side of the outer body of ATM thrice, police said.

Source: Times of India

Web Link: <http://timesofindia.indiatimes.com/city/surat/Broker-loses-Rs-65000-to-debit-card-fraud/articleshow/53318070.cms>

3. Online Lottery Fraud

Company: NA

Sector: Lottery (Cyber Crime)

Nature: Winning Lottery and Collecting Money

Modus: It is the case of duping innocent people in the city on pretext of winning lottery and collecting money from the victims. Women received phone calls from Shruthi, Deepak Bansal, Akash, Arun Srivastav representing Global India Services, India Today Book Club (ITBC) and others and informed that she won the prize money. Believing their version, she deposited Lakhs of Rupees in different bank accounts provided by the accused.

Quantum & Impact: The victim deposited Rs 32,99,110 in different bank accounts provided by the accused. The accused are now apprehended and the money is being recovered.

Source: Indian Express

Web Link: <http://www.newindianexpress.com/cities/hyderabad/Woman-duped-of-Rs-33-L-in-online-lottery-fraud/2016/07/07/article3517402.ece>

4. Scam in National Rural Health Mission

Company: NA

Sector: Rural healthcare

Nature: Misappropriation of Money

Modus: It appears to be a case of misappropriation of public funds.

Quantum & Impact: Over Rs. 80 Lakh was misappropriated in the purchase of sterilisation kits in Rae Bareli by some health officials and drug suppliers.

Source: NDTV News

Web Link: <http://www.ndtv.com/india-news/cbi-raids-across-uttar-pradesh-in-national-rural-health-mission-scam-1465258fraud/articleshow/53318070.cms>

5. Tele-calling fraud

Company: NA

Sector: BPO

Nature: Impersonation through tele-calling

Modus: The employees of the alleged call centre pose as officials of Internal Revenue Service (IRS) of US and threaten the victim with arrest and legal proceedings for default in payment of taxes and thereby demand payments of \$5,000 - \$3,000.

Quantum & Impact: This bogus call centre has robbed US citizens of an amount of around Rs. 500 crore in the year 2015-16. The three call centres--Hari Om IT Park, Universal Outsourcing Services and Oswal House--were collectively pocketing around Rs 1 to 1.5 crore daily.

Source: Economic Times

Comments: This a case of fraud due to misrepresentation and could have been avoided if the victims would not have believed the fake phone calls and reported the same to appropriate authorities.

Web Link:

http://economictimes.indiatimes.com/articleshow/54710487.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst

1. Cyber Heist via Hacking

Company: NA

Sector: Informative Technology

Nature: System Hacking

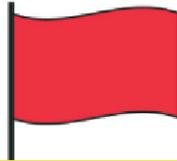
Modus: Hacking the system to acquire monetary benefits.

Quantum & Impact: The hackers sent fraudulent messages, ostensibly from the central bank in Dhaka, on the SWIFT system, to the New York Federal Reserve seeking to transfer nearly \$1 billion from Bangladesh Bank's account there. Most of the transfers were blocked but about \$81 million was sent to a bank in the Philippines. It was moved to casinos and casino agents and much of it is missing. Bangladesh Bank officials have said they believed SWIFT, and the New York Fed, bear some responsibility for the cyber heist, but SWIFT has rejected the suggestion.

Source: Reuters.com

Comments: The inherent weakness in the IT system of SWIFT was being utilised by hackers to leak funds out of the Bangladeshi financial system to the other countries. Cyber security measures require urgent attention of stakeholders worldwide. Vulnerability assessments and penetration testing to exploit gaps in the information security value chain should be conducted regularly by banks and companies. Regulators in India have provided specific advisories on the subject.

Web Link: <http://www.reuters.com/article/us-cyber-heist-philippines-idUSKCN0YAOCH>



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**Compiled by
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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.

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