



GS Mahanagar Co-op. Bank Ltd.,

Hiramani Super Market, Dr. B. A. Road,

Lalbaug, Mumbai-12.

Fraud Risk Management Policy

Year 2026-27.

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GS MAHANAGAR CO.OP. BANK LTD., MUMBAI.

Fraud Risk Management Policy.

Preamble :

Banks are vulnerable to frauds, probability of which is more when procedural checks are inadequate or laid down process is not followed. Frauds can be done by both – insiders and outsiders, either individually or in collusion. Increased use of computerization and various platforms /channels by banks has added into new ways of frauds and has increased the potential for the same. As such, banks have to continuously strengthen its operational practices, procedures, controls and review mechanism so as to prevent frauds. Our thrust should always be on preventive fraud management since it is always superior to post fraud investigation.

Reserve bank of India issued Master directions on fraud risk management for urban co-operative banks vide its circular RBI/DOS/2024-25/119 Dated 15th July, 2024. These directions are applicable to all co-operative banks. These directions are basically issued with a view to provide a framework to co-operative banks for prevention, early detection and timely reporting of fraud to law enforcing agencies, reserve bank of India and dissemination of information by RBI and matters connected therewith.

Scope

The purpose of this policy is to put in place a framework for detection and early reporting of frauds and taking timely actions like reporting to investigating agencies so that fraudsters are quickly brought to book, examining staff accountability and effective fraud risk management. It would be applicable to all branches / offices of the bank and in conjunction within the related operational guidelines /instructions issued from time to time. This policy will be linked with and will overlap banks vigilance policy.

Objective

The policy stresses on prevention and detection of frauds through early warning signals and prompt initiation of appropriate corrective measures to pre-empt attempts to breach the system through a review mechanism.

Definition and classification of frauds:

“Any behavior with an intention to receive dishonest benefit over the other is a fraud” fraud in bank is a deliberate act of omission and commission on the part of an employee while discharging his duties which may result in passing benefit to him to which he is otherwise not entitled.

Frauds can be classified as under:

1. Misappropriation and criminal breach of trust.
2. Fraudulent encashment through forged instruments, manipulation of books of accounts or through fictitious accounts and conversion of property.
3. Unauthorized credit facilities extended for reward or for illegal gratification.
4. Negligence and cash shortages.
5. Cheating and forgery.
6. Irregularities in foreign exchange transactions.
7. Any other type of fraud not coming under the specific heads as above.

Nature of frauds:

Frauds can be of following four types of natures:

- i. Committed by insiders
- ii. Committed by insiders in collusion with outsiders
- iii. Committed by outsiders with insider support / involvement
- iv. Committed by outsiders

Detection of frauds:

Some sources of fraud detection can be :

- Customer complaints
- Various audits and inspections, either by concurrent auditor or statutory auditor
- Visits of inspection by vigilance officer of the bank or of senior management personnel
- Re-conciliation of office accounts.
- Appointment of new person, either by transfer or recruitment
- Information given under banks whistle blower policy
- Anonymous letter with verifiable facts

Framework of early warning signals (EWS) & Red Flagging of accounts (RFA):

The bank will identify early warning signals and based on that red flagged accounts will be identified. A Red flagged account is the one where suspicion of fraudulent activity is thrown up by the presence of one or more EWS indicator/ parameters shall be integrated with the banking system of the bank creating EWS triggers, either in the form of reports or alerts. The system shall include both quantitative and qualitative indicators. The indicators shall be based on the transactional data of accounts, financial performance of borrowers, market intelligence, conduct of borrowers, etc.

Classification of Early Warning Signals:

RBI Master Directors on frauds dated 1st July 2016 lists out 42 early warning signals of frauds. They can be broadly classified into following categories.

1. **Operations of account** – Bouncing of high value of cheques, frequent invocation of BGs and development of LCs, frequent request for general purpose loans, frequent adhoc sanctions, etc.
2. **Concealment or falsification of documents** - substantial increase in unbilled revenue year after year, poor disclosure of materially adverse information, material discrepancies in annual report, etc.
3. **Diversion of funds** – Non –routing of sale proceeds through consortium bank's high value RTGS payment to unrelated parties, increase in borrowings despite huge cash equivalents in the balance sheets, etc.
4. **Issues in primary / collateral security** – critical issues highlighted in the stock audit report, significant movements in inventory and receivables disproportionately differing vis-à-vis change in the turnover, etc.
5. **Inter – group / concentration of transactions** – Funds coming from other banks to liquidate the outstanding loan amount, substantial related party transactions with inter- connected companies and large outstanding from such companies, etc.
6. **Regulatory concerns** – Default in undisputed payment to the statutory bodies, raid by tax authorities.
7. **Others** – Resignation of key personnel and frequent changes in management, significant reduction in stake of promoters, etc.

These early warning signals are red flags, which need immediate attention and action by the management of the banks. The classification given above is broad, and various instances can overlap each other.

As such, it should be remembered that –

- a. No one signal can be seen in isolation
- b. Existence of such signals does not necessarily mean that there is a fraud
- c. In case of fraud, several signals would appear together.

Frauds Risks involving Information Technology (IT):

Information Technology (IT) plays a significant role in development of digital banking to make the banking fast, effective and efficient. Use of IT in banking system made banking more customer oriented, quality driven and easy to use by both bank and customer. Now a days banks have implemented various initiatives like core bank. ATMs, mobile and Net Banking, IMPS, UPI, Debit Cards, POS. However, there are various ways by which these initiatives can be exploited by the hacker or thief or an anti social element. As such, all these channels call for proactive alertness and periodical monitoring of accounts, e.g. Accounts having all inflow transactions by way of IMPS or UPI only and outflow by way of online transactions like ATM withdrawals only can be Red Flagged accounts. Such accounts might be used by fraudsters to do the fraud. Especially new accounts should be monitored by branches for this purpose.

Deposit related frauds –

These are mainly because of lack of compliance with KYC guidelines, misuse of inoperative / dormant accounts, Non –reconciliation of suspense and sundry accounts and lack of control or monitoring of transaction, in these accounts.

Advance portfolio frauds –

Majority of credit related frauds are on account of deficient appraisal system, poor post disbursement supervision and inadequate follow-up. Most of the frauds relating to advances come to light only during the recovery process initiated after the accounts have been classified as NPA. Fabricated /fudged financial statements, inflated security valuation report, defective search report for title deeds of mortgaged property are commonly discovered.

The most effective way of preventing frauds in loan accounts is for banks to have a robust appraisal and an effective credit monitoring mechanism during the entire life cycle of the loan account. Any weakness that may have escaped attention at the appraisal stage can often be mitigated, in case the post disbursement monitoring remains effective.

In order to strengthen the monitoring processes, including of the following checks during the different stages of the loan life cycle shall be carried out :

- a. **Pre-sanction :** As a part of the credit process, the checks being applied during the stage of pre-sanction may consist of the bank collecting independent information and market intelligence on the potential borrowers from the public domain on their track record, involvement in legal disputes, raids conducted on their businesses, if any, validation of submitted information / data from other sources like the ROC, scanning the defaulters list of RBI / other government agencies, etc., which can be used as an input by the sanctioning authority.
- b. **Disbursement :** Checks during the disbursement stage normally focuses on the adherence to the terms and conditions of sanction, rationale for allowing dilution of these terms and conditions, level at which such dilution were allowed, etc. the dilutions shall strictly conform to the broad framework laid down by the board in this regard. As a matter of good practice, certain terms and conditions laid down by sanctioning authority as core shall not be diluted.
- c. **Annual review:** While the continuous monitoring of an account is important, banks also need to be vigilant from the fraud perspective at the time of annual review of accounts. Among other things, the aspects of diversion of funds in an account, adequacy of stock, stress in group

accounts, etc. shall be considered at the time of review. Besides, the bank shall track market developments relating to the major clients of the bank. This would involve collecting information from the grapevine, following up stock market movements, etc.

- d. Short mortality accounts :** The early default in payments within the first year of disbursement can be the most important early warning signal and cannot be neglected. In such situation, the entire loan documentation done shall be reviewed to decide on whether there was any lapse at the sanctioning stage.

Further Monitoring Mechanism :

- i. Role of Auditors :** During the course of audit by concurrent or statutory or external independent stock auditor, auditors may come across instance where the transactions in the account or the documents point out the possibility of fraudulent transactions in the account. In such a situation, the auditor may immediately bring it to the notice of the top management and If necessary to the audit committee of the Board (ACB) for appropriate action.
- ii. Staff Empowerment :** Employees shall be encouraged to report fraudulent activity in an account, along with the reasons in support of their views under the whistleblower policy of the bank. Protection shall be available to such employees so that the fear of victimization does not deter the act of reporting.
- iii. Roll of Vigilance Department :** Vigilance department staff will do surprise visit to various branches / departments and carry out different random checks like checking of sundry accounts, accounts having exceptionally high number of online transactions or small amount transactions or of unusual pattern, short mortality overdue loan accounts.
- iv. Special Committee of the Board :** The Present vigilance committee of the Board will act as a “Special Committee of the Board for Monitoring and Follow-up of cases of Frauds”. This committee shall oversee the effectiveness of the fraud risk management in the bank and monitor the cases of frauds, including root causes analysis, and suggest mitigating measures for strengthening the framework.
- v. Whistle Blower Mechanism:** Bank shall ensure that whistle blower complaints on possible fraud cases/suspicious activities in account are examined and concluded appropriately.
- vi. Legal audit of title documents in respect of Large Value Loan Account :** Bank shall do legal audit and re-verification of title deeds and other related title documents in respect of all credit facilities of Rs. 1 Cr. And above till the loan is fully repaid.

Investigation, Disciplinary Action & Staff Accountability :

- The Audit department shall jointly conduct detailed investigation in case of a fraud. The bank shall appoint an external competent authority to conduct forensic audit, if required.
- The principle of natural justice shall be followed during the entire process.
- A detailed show cause notice (SCN) shall be issued to the persons, entities and its executives against whom allegation of fraud is being examined. The show cause Notice (SCN) shall provide complete details of transactions / actions / events basis which declarations and reporting of a fraud is being contemplated under these directions.
- Reasonable time not less than 21 days shall be provided to the persons / entities on whom the SCN was served to respond to the said SCN.
- A reasoned order shall be served on the person / entities conveying the decision of the bank regarding declaration / classification of the account as fraud or otherwise. Such order(s) shall contain relevant facts / circumstances relied upon, the submission made against the SCN and the reasons for classification as fraud or otherwise.
- Bank shall complete the examination of staff accountability in all fraud cases in a time-bound manner.

Penal Measures :

Persons/entities reported as fraud and also entities and persons associated with such entities shall be debarred from raising funds and /or seeking additional credit facilities from financial entities regulated by RBI for a period of five years from the date of full repayment of defrauded amount.

Reporting of Frauds to Law Enforcement Agencies (LEAs)

- Bank shall immediately report the incidents of fraud to appropriate LEAs viz. State Police authorities, etc. subject to applicable laws.
- Chief Compliance Officer of the bank shall be the nodal / designated Officer for reporting incidents of fraud to LEAs and for proper coordination to meet the requirements of the LEAs.

Reporting of Incidents of Fraud to Reserve Bank of India (RBI) :

To ensure uniformity and consistency while reporting incidents of fraud to RBI through Fraud Monitoring Returns (FMRs) using online portal, Bank shall choose the most appropriate category from any one of the following:

- a) Misappropriation of funds and criminal breach of trust.
- b) Fraudulent encashment through forged instruments;
- c) Manipulation of books of accounts or through fictitious accounts, and conversion of property;
- d) Cheating by concealment of facts with the intension to deceive any person and cheating by impersonation;
- e) Forgery with the intention to commit fraud by making any false documents/electronic records;
- f) Willful falsification, destruction, alteration, mutilations of any book, electronic record, paper, writing, valuable security or account with intent to defraud;
- g) Fraudulent credit facilities extended for illegal gratification;
- h) Cash shortages on account of frauds;
- i) Fraudulent transactions involving foreign exchange;
- j) Fraudulent electronic banking / digital payment related transactions committed on bank and
- k) Other type of fraudulent activity not covered under any of the above.

Modalities of Reporting Incidents of Fraud to RBI

- Bank shall furnish FMR-1 in individual fraud cases, irrespective of the amount involved. Immediately but not later than 14 days from the date of classification of an incident / account as a fraud.
- While reporting frauds, Bank shall ensure that persons / entities who / which are not involved / associated with the fraud are not reported in the FMR.

Closure of Fraud : Bank shall close fraud cases using 'Closure Module' where the actions a stated below are complete:

- a) The fraud cases pending with LEAs/Court are disposed of; and
- b) The examination of staff accountability has been completed.
- c) In all closure cases of reported frauds, Bank shall maintain details of such cases for examination by auditors.

Reporting of Cases of Theft, Burglary, Dacoity and Robbery : Bank shall report instances of theft, burglary, dacoity and robbery, including attempted cases to Fraud Monitoring Group (FMG), Department of Supervision, Central Office of RBI immediately, not later than 7 (seven) days from their occurrence.

Review of the Policy : The review of this policy will be conducted every financial year.

Effective Date : This policy will be effective from the date of approval by the Board of Directors of the Bank.

Place : Mumbai

Date : 31.07.2026

(S.L. Abhang)
Dy. Managing Director

GS MAHANAGAR CO-OP BANK LTD.