PNB Banking Fraud Case

Why in news?

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One of the branches of State-owned Punjab National Bank (PNB) has recently detected fraudulent transactions worth over Rs 11,000 crores.

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What is Letter of Understanding (LoUs)?

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- LoU is an assurance given by one bank to another to meet a liability on behalf of a customer.
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- It is similair to a letter of credit or a guarantee.
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- It is used for overseas import remittances and involves four parties — an issuing bank, a receiving bank, an importer and a beneficiary entity overseas.
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- According to norms, they are usually valid for 180 days.
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- LoUs are conveyed from bank to bank through “Society for Worldwide Interbank Financial Telecommunication” (SWIFT) instructions.
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- Notably, till now, there is no record of a breach in SWIFT instructions anywhere in the world.
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What has happened with PNB?

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- PNB has alleged that two of its employees had “fraudulently” issued LoUs and transmitted SWIFT instructions to the overseas branches of Indian Banks.

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- This was done to raise buyer’s credit for the firm of a diamond merchant without making entries in the bank system.
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- The bank has alleged that one such fraudulent LoU issuance took place on January 2018, the trail of which revealed the entire design.
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- These LoUs were mostly issued to two Hong Kong branches of Indian Banks and was for the aforesaid diamond merchant.
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- The details on whether LoUs were backed by collateral or the quantum of liability that the bank faces against these LoUs aren’t out yet.
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How will the fraud impact PNB?

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- Hong Kong branches of Allahabad Bank and Axis Bank have given money to the beneficiary entity on behalf of Modi’s firms.
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- As a result, PNB will have to settle the LoUs with these branches according to the norms of the Hong Kong Monetary Authority.
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- Market sentiment has already been impacted and PNB stock fell 9.81% in a single day, which consequently saw investors loose over Rs 3,000 crores.
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- The bank may have to set aside higher provisioning in the next few quarters if it unable to recover the money from the accused firms.
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- The fraud has been unearthed at a time when Indian banks are reeling under a pile of stressed assets of about Rs 10 lakh crore.
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- Also, higher provisioning and a rise in bond yields, has resulted in losses for most public sector banks in the previous quarter.
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Source: The Indian Express

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