

## URBAN COOPERATIVE BANKS SCAM

### THE LOOT FROM WITHIN

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Urban Cooperative Banks (UCBs) have been in the news for quite some time for wrong reasons. The collapse of a number of UCBs in Maharashtra, Gujarat and Andhra Pradesh has seriously jeopardized financial interests of millions of small investors. Many desperate investors have committed suicide. In September 2003, Aruna and Vinita – two sisters ended their lives by consuming poison. Next day their brother Achyuta and mother Jana also committed suicide. The cause of suicide: dejected over not getting back Rs.4 lakhs they had deposited in the scam hit Charminar Urban Cooperative Bank. In January 2004, a retired employee Mohd.Abdul Basith set himself ablaze and died. He too failed to get his hard earned money deposited in Prudential Urban Cooperative Bank, which he needed desperately for performing marriage of his grown up daughters.

In Andhra Pradesh, Charminar Urban Cooperative Bank, Krushi Urban Cooperative Bank, Vasavi Urban Cooperative Bank, Prudential Urban Cooperative Bank and a host of other Urban Cooperative Banks collapsed in quick succession. With over Rs.4000 Crores deposits of lakhs of small investors in the UCBs at risk in Andhra Pradesh alone, the State Government took a slew of measures to improve functioning of the UCBs besides initiating civil and criminal action against the wrongdoers.

The sleuths of CID assigned to probe the criminal misdeeds of the scamsters unravelled the whole gamut of criminal activities as well as financial mismanagement, which led to the collapse of these Urban Cooperative Banks and arraigned fraudsters to face justice.

#### **GROWTH OF UCBs IN THE STATE:**

The growth in UCBs since 1997-98 can be ascribed to the liberalization of RBI norms for UCBs and tightening of Non-Banking Financial Companies (NBFCs) in the wake of CRB scam in 1997. While 69 UCBs came into existence, in nine decades (1906 to 1995), as many as 101 UCBs were given licences in just six years. In Hyderabad City and Ranga Reddy District alone 42 new banks sprung up during this period. Not surprisingly many unscrupulous promoters with dubious past obtained licences from the RBI only to loot the public money. And almost all of them are either weak/sick or under liquidation.

#### **MUSHROOM GROWTH OF UCBS IN ANDHRA PRADESH**

<b>Period</b>	<b>No. Of UCBs</b>
1906-1995 (89 Yrs)	69
1996-2002(7 Yrs.)	101
<b>TOTAL</b>	<b>170</b>

#### **FRAUDS UNRAVELED:**

In-depth and thorough investigations revealed a series of illegalities committed by the management and staff of the banks in collusion with borrowers, which led to the collapse of these banks. Following are some of the glaring acts of criminalities:

- Directors themselves siphoned off crores of rupees never to repay. The loans were availed by them against the specific direction of the RBI not to sanction big loans to Directors.
- Many of the Directors used the money taken from the bank for construction of their palatial houses and buying cars.
- Some Directors purchased farmhouses and deposited the amount in their personal accounts.
- The information regarding Directors availing loan was either not intimated or partly furnished to the RBI.
- Many of the Directors got crores of rupees sanctioned to their Class-IV employees, though the latter had no credit worthiness and source of income generation. Not surprisingly these amounts reached the pockets of their masters and the amounts were never repaid.
- Term loans were converted into overdrafts and loan amounts were enhanced without any formal request from the borrowers.
- Huge amounts of loans were sanctioned on the basis of the properties mortgaged with the bank, which had fake and fabricated sale deeds and therefore had no legal value. There is an instance wherein a borrower obtained a loan of Rs.50 lakhs by mortgaging a Municipal Park in Hyderabad City. In yet another sensational instance, a borrower mortgaged the land belonging to Wakf Board and obtained a loan of Rs.2.5 crores. And there are instances, where crores were sanctioned even on the basis of non-existing properties.
- Most of the properties mortgaged were grossly over valued by the valutors of the banks.
- Single individuals borrowed 25-30 crores from the banks and used the funds for the purpose other than indicated in the proposals.
- In some instances, banks did not enquire about existence of borrowers let alone about the nature of business mentioned by them.
- Fictitious entries indicating repayment of huge amount of cash and subsequent withdrawal on the same day with a view to prevent the said amount from being classified as Non-Performing Assets (NPA).
- The Chairman of a Bank purchased shares worth Rs.3.75 Crores in his name from the money siphoned off from the bank.

#### **IMPRUDENT BANKING:**

Prudence is central to banking. But the Prudential Urban Co-operative Bank and other UCBs that collapsed were anything but prudent. In fact, the Prudential Banking norms of the RBI were followed more in breach than in practice.

- The application for sanction of big loans were received in the head office directly by Chairman / Managing Director and the loan amounts of crores of rupees were sanctioned on the same day without obtaining any verification reports from the field officers regarding viability of the project / business, repaying capacity, credit worthiness etc. of the applicant.
- The UCBs offered unviable very high interest rates as well as incentives to the depositors.
- The banks continuously defaulted in the maintenance of CRR and SLR.
- The CEO sanctioned several advances far in excess of delegated authority.
- Observations made by the RBI in its inspection report were ignored.
- Establishment costs of banks were far in excess of 2% of the working capital.

- Ignoring the RBI directive, the Banks sanctioned huge loans to the prohibited and risky sectors.
- Many borrowers with no capacity to run business and repay amounts were sanctioned huge loans.
- Some of the big advances sanctioned against mortgage of immovable properties without considering the end use.
- Loan proposals instead of routing through the Branch Managers were directly recommended by the Directors.
- In several instances crores of rupees were sanctioned to the individuals, who were not even income-tax payers.

The Bank placed its funds with other cooperative banks in violation of the RBI directive.

- Loans were disbursed in cash.
- End use of loans was not verified.
- Advances were sanctioned for unproductive / consumption / ceremonial purposes.
- Excess drawl was allowed in many Over-Draft accounts.
- Ever greening of non-performing assets was resorted to.
- The system of internal audit did not exist in many of the banks.

As a result of total mismanagement and frauds, the Non-Performing Assets – which do not yield any income increased abnormally and the banks became weak/sick.

#### **THE FAILED BANKS – NAKED TRUTH**

Name of the UCB	No. Of Depositors	Deposits	Non-Performing Assets (NPA)	Capital to Risk Weighted Asset Ratio (CRAR)
Krushni	8,247	Rs.35.69 Cr.	32.22 Cr.	N.A.
Charminar	1,38,000	Rs.297 Cr.	63.20 % (64.52 Cr)	N.A.
Vasavi	1,38,511	Rs.143 Cr.	67.20% (84.64 Cr.)	0.25%
Prudential Bank	1,86,765	Rs.451.39 Cr.	66.50% (300.22 Cr.)	-23.6%

\* A bank becomes sick when its NPA is more than 15%.

A dozen banks had more than 80% its advances as NPAs. The fate of such banks can be well imagined.

\*\* It is mandatory for banks to maintain 3% CRAR

#### **STATE GOVERNMENT INITIATIVES:**

The Andhra Pradesh Government has taken a number of initiatives to effectively deal with the burgeoning economic offenders and protect the interest of the depositors. The legislation of the **A.P. Protection of Depositors of Financial Establishments Act, 1999, is a significant measure in this regard.** The Act inter-alia provides for imprisonment up to 10 years to the Directors and others of a financial establishment, for its failure to repay to the investors on maturity of their deposits. The Act also provides attachment of the properties of the borrowers and disbursement of the liquidated properties on pro-rata basis

to the depositors. The State Government is likely to enact a special Act for improving functioning of the Urban Cooperative Banks. The proposed Act among other things will provide for appointment of professionals in the Board of Directors, Prohibition on availment of loans by the Directors and their relatives, punishment for furnishing false information to the RBI and the State Government, Punishment for corrupt practices in sanction of loans, etc.

The proposed Act prescribes ceilings on the individual exposure as follows:

- 1) In case of bank having deposit up to Rs.5 Crores - Rs.2 Lakhs
- 2) In case of banks having deposits above Rs.5 Crores but below Rs.25 Crores – Rs.10 Lakhs
- 3) In case of bank having deposits above Rs.25 Crores – Rs.20 Lakhs

**OR**

1% of lendable resources of the bank, whichever is less.

- 4) Banks having deposits above Rs.100 Crores – Rs.40Lakhs.

Further, the offences listed in the proposed Act are being made cognisable.

#### **CONCLUSION:**

The collapse of a score of Urban Cooperative Banks in the State was mainly on account of the unabashed greed of their Directors, who sanctioned huge loans to themselves and many unscrupulous borrowers, ignoring the norms of prudent banking. Unless the UCBs performs their intended role of purveyor of micro-credit and function in the frame work of prudent banking norms laid down by the RBI in professional and ethical manner, their survival is doubtful.