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# Banking is all about risk, requires a better process to deal with corruption

BY [SALONI SHUKLA](#), ET BUREAU | UPDATED: MAY 09, 2018, 07.54 AM IST

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*Lending is not just about numbers. It involves subjectivity and discretion. Banking, like any other field, has its share of black sheep, but charging officers by mixing up malfeasance and wrong decisions could send state-run bankers into a shell. What is needed is a better process to deal with [corruption](#), writes Saloni Shukla:*

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When Finance Minister Arun Jaitley promised to amend the Prevention of Corruption Act (PCA) to limit harassment of bankers by gumshoes, it was a new dawn. But nearly 20 months later what the industry has is — a few of its officers behind bars, dozens more charged with corruption and little comfort to decide even on small matters.

The banking industry that was just beginning to crawl back after a hefty dose of [bad loans](#) dragging it for the past five years is back in a funk with fear gripping people across the board. Indecision is the new normal.

Loan sanctions for new projects have come to a grinding halt as neither bankers nor independent directors are willing to stick their neck out as a series of charges has numbed the banking system into inaction.

“In banking, we have decided to criminalise all defaults, but a bad business call should not be punished,” says Amit Tandon of shareholder advisory services IAS. “Due to this, banks are pulling back on credit. I have spoken to enough companies to arrive at a conclusion that there is total credit paralysis right now.”

The Indian banking industry for the first time in decades is seeing some of its top executives being charged for alleged corruption and mala fide intentions in granting loans. The record high bad loans and public outcry over events like the Rs 13,000-crore fraud by Nirav Modi have raised investigative heat, often mixing up frauds and decisions that turned sour.

In a Rs 600-crore IDBI Bank loan to entrepreneur Sivasankaran's firm that defaulted, CBI last month charged many, including former IDBI Bank executives — Kishor Kharat, now CEO of Indian Bank, and Melwyn Rego, the CEO of [Syndicate Bank](#). Other former and current IDBI employees under probe include GM Yadwadkar, BK Batra.

Independent directors PS Shenoy, a former chairman of Bank of Baroda, and S Ravi, who chairs the BSE, have also been charged.

The CBI has alleged that IDBI Bank officers modified various conditions of the loan, including interest rates, its classification as 'medium-term loan', corporate guarantee and collateral proposed by Sivasankaran, who is wellknown in corporate circles as Siva. What has shocked more is the charges against independent directors whose role the CBI doesn't seem to have understood.

"The job of the board is to give direction on the macro level, we lend our experience to a company to avoid mistakes that we committed or came across in our professional careers and grow the business," says Rajesh Gupta, managing partner, SNG Partners, a law firm. "Micro management is not the job of the board."

# The Heat is On



**APR 2018:** CBI books former CMD of IDBI, MS Raghavan; current MD of Syndicate Bank Melwyn Rego; PS Shenoy, former CMD of Bank of Baroda; B K Batra, former deputy MD of IDBI Bank; Ninad Karpe, former independent director of IDBI Bank; and S Ravi, currently chairman of the BSE in the ₹600-crore loan given to Aircel promoter C Sivasankaran

**APR 2018:** CBI books former CMD of UCO Bank Arun Kaul in connection with an alleged ₹621-crore loan fraud in which he purportedly facilitated loans to Era Engineering

**JAN 2017:** CBI arrests the then DMD of IDBI Bank BK Batra, including the ex-chairman of the bank Yogesh Agarwal, in connection with a ₹950-cr loan given to defunct Kingfisher Airlines

**AUG 2014:** CBI arrests the then CMD of Syndicate Bank SK Jain for allegedly taking bribe of ₹50 lakh from MD of Bhushan Steel Neeraj Singhal and increasing credit limit of some companies in violation of banking rules

**NOV 2013:** Shyamal Acharya then DMD of State Bank of India charged by the CBI for taking pecuniary benefits to clear a loan despite an internal SBI enquiry giving him a clean chit

## **RIGHT VS WRONG MOTIVES**

Any loan can turn bad. Fulfilling loan obligations depends on the cash generated by a business, the state of the economy, government policies and competitive environment.

When banks sanction loans, it is done on the basis of estimates of future cash flows and the viability of a business. While things go as planned in many cases, sometimes changes in business conditions lead to a collapse in profitability and subsequent defaults.

Power, telecom, airport and other infrastructure industries were the darlings of bankers as well as investors since early 2000. But overcapacity, regulatory changes and corrupt practices led to judicial intervention that threw businesses out of gear.

Several telecom licences and spectrum allocations were scrapped, permission for foreign equity in aviation was delayed, coal mine licences got abolished, states reneged on power purchase agreements. There was little option but to default.

“On the hindsight based on all available information, we may pretend to be intelligent, but when the credit committee takes a decision, it is on the basis of prevailing conditions,” says Kuntal Sur, partner-financial services, PwC India. “If there is a mala fide intention, there will be quid pro quo and that has to be established, otherwise, it is a reputational risk for bankers.”

The Tatas couldn't run a telecom business which they sold to Bharti Airtel for free. The likes of GVK and GMR had to go for fire sale of assets to remain afloat. The Jaypee group which executed many infrastructure projects, including the Formula 1 race track, is grounded.

## **BANKERS OR POLICEMEN?**

Few professionals argue that the corrupt should be spared, but the actions of investigative agencies without sufficient evidence of malfeasance and understanding are crippling the system. Banking isn't just based on [credit rating](#) or some formula. For complex projects, the requirement of funding is structured in many ways. Most of the companies in India are rated below single A, which carries risk. But banking is all about risk-taking.

The CBI arrested IDBI Bank's BK Batra and former chairman Yogesh Agarwal last year alleging corruption in extending a Rs 950-crore loan to Kingfisher Airlines. The agency has based its charge sheet on below-investment grade rating of the company, which the industry believes is flimsy. Furthermore, its track record on convictions has been patchy and the delays have wrecked many a careers.

“Banking is a risk-taking business,” says PwC’s Sur. “Even if companies don’t have very high credit ratings and lenders believe in the business model, they may give proper justifications to lend to some sectors. But just because the decision went awry, that doesn’t mean it was done with criminal intent.”

In November 2013, Shyamal Acharya, a deputy managing director of State Bank of India, was charged by the CBI for corruption. Ironically, later Acharya returned as the head of the inspection and audit department in Hyderabad.

Syndicate Bank chairman SK Jain was arrested in August 2014 for allegedly taking a bribe of Rs 50 lakh from Bhushan Steel promoter Neeraj Singhal for increasing credit limits. Even after four years, the case is yet to see the light of the day. When these events shook the industry, Finance Minister Jaitley applied balm.

“We need to give public sector banks level-playing field with others,” Jaitley said in September 2016. “The ability of private sector banker to settle a stressed loan would depend entirely on banking considerations, but a state-run bank is still constrained by some of the obsolete laws. I think the fear of consequences at times dilutes the process of resolution.”

There have been instances of promoters siphoning off funds which have resulted in defaults. Forensic audits into companies such as Deccan Chronicle Holdings, NSEL, Kingfisher Airlines have shown frauds by management. But the criminal investigative system has failed to convict them.

Bankers can assess a project and lend in good faith, but to expect them to do the job of a policemen is absurd.

“Banking decisions are taken after a lot of scrutiny, it goes through various levels and if at no stage the decision was objected to ... in all such cases the intervention of investigative authorities should not be there,” says Gupta.

### **RISK COMPLIANCE A BURDEN OR NECESSITY?**

Despite all the regulatory overkill, banks have also been at fault for not keeping their houses in order. Adherence to risk-based compliance is seen as an encumbrance rather than a prerequisite to building a sound institution.

The Nirav Modi episode on PNB fraud exposes the chinks in the armour of banks. Many public sector banks have been way behind in developing a robust system that would prevent frauds.

Although committees are in place, many of them do not follow a rigorous process for loan appraisals and they lack follow up and monitoring.

“One of the problems which the RBI is trying to plug is that the minutes are not detailed enough,” says TT Ram Mohan of IIM Ahmedabad. “If you are disbursing a loan of Rs 1,000 crore and have a one-line statement ‘the loan of Rs 1,000 crore was discussed and approved by the committee’, well then you are asking for trouble.”

Decades of political influence led to unprofessionalism and corruption. A mechanism like a panel comprising retired judges and bankers could be set up that would clear suspected cases to be taken up by the CBI, so that there’s no fear of a witch hunt.

“Let these people scrutinise whether it is a wrong business decision or a fraud,” says Gupta. “They should give a prima facie opinion based on documents produced before them. Once this first stage is through, then the matter should go to CBI.” While an amendment to the PCA or a panel to scrutinise the cases may not be on the horizon in an election year, bankers are in a state of terror.

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