
SCANNING THROUGH SCANDALS TO STANDARDS: A COMPARATIVE ANALYSIS OF THE PNB FRAUD AND YES BANK CRISIS FOR STRENGTHENING BANKING GOVERNANCE IN INDIA

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ABSTRACT

The title encapsulates the journey of India's corporate governance from financial misconduct to the establishment of stringent regulatory frameworks. Over the years, India has witnessed several corporate frauds that have exposed severe weaknesses in financial transparency, auditor accountability, and regulatory enforcement. Financial scandals such as Satyam (2009), Punjab National Bank (2018), IL&FS (2018), Yes Bank (2020), DHFL (2021), Sahara (2014), and NSEL (2013), etc. serve as case studies to understand the systemic flaws that enabled financial mismanagement. These scandals have not only resulted in massive financial losses but have also eroded investor trust in corporate governance. As a result, regulatory bodies have introduced several reforms to enhance financial reporting, ethical accounting, and corporate accountability. Because of the limitation of time we only took two major banking frauds under the study of Indian banking sector which shook the Indian financial market tremendously viz., Punjab National Bank (2018) and Yes Bank (2020). The regulatory changes they triggered, and the extent to which these reforms have been successful in preventing further frauds.

Keywords: *Ethical accounting, corporate fraud, PNB scam, Yes bank scam, statutory audit limitations, corporate governance, regulatory reform, financial transparency.*

INTRODUCTION

The word "Scanning" in the title represents a detailed investigation into financial frauds and governance failures. It signifies the process of analysing how corporate misdeeds unfolded, the loopholes that allowed fraud to persist, and the measures taken to detect and rectify them. Financial scandals such as Satyam (2009), Punjab National Bank (2018), IL&FS (2018), Yes Bank (2020), DHFL (2021), Sahara (2014), and NSEL (2013) serve as case studies to understand the systemic flaws that enabled financial mismanagement. By scanning these scandals, the researcher seeks to uncover patterns of corporate fraud and evaluate how ethical accounting practices could have prevented them.

The term "Scandals" highlights the root causes of regulatory failures that led to corporate frauds in India. These financial misdeeds ranged from misreporting profits, fraudulent lending, investor fraud, Ponzi schemes, and banking frauds. For example, the Satyam scam involved inflating revenue and cash reserves, while the PNB scam exposed banking loopholes that allowed fraudulent Letters of Undertaking (LoUs) to go undetected for years. Each of these scandals led to widespread economic losses and raised critical concerns about India's corporate governance structure.

To combat these financial scandals, regulatory agencies introduced "Standards"—a set of laws and reforms aimed at strengthening corporate accountability. Post-scandal regulations such as the Companies Act, 2013, SEBI LODR Regulations, Ind AS (Indian Accounting Standards), RBI Guidelines, and ICAI's Code of Ethics were established to enforce ethical financial practices. These standards were designed to ensure accurate financial reporting, auditor independence, and better risk management within India's corporate sector. However, despite these regulatory frameworks, financial frauds continue to emerge, raising questions about their actual effectiveness and whether companies still exploit loopholes.

At the heart of this discussion lies "Ethical Accounting", which is fundamental to ensuring transparency, honesty, and integrity in financial reporting. Ethical accounting involves truthful representation of financial statements, strict auditing practices, and compliance with accounting norms. Companies that follow ethical accounting ensure that their financial reports are accurate and free from manipulation. However, cases like IL&FS and DHFL show that even after regulatory changes, some corporations continue to engage in unethical practices, indicating that compliance remains superficial rather than deeply ingrained in corporate culture.

Focusing on India's corporate sector, this study aims to analyse whether financial regulations have effectively strengthened ethical accounting practices or if corporate frauds persist despite the introduction of stricter laws. By critically examining two major banking corporate frauds and their impact on financial governance, this

research seeks to identify whether India has successfully transitioned from scandals to strong regulatory standards or if further reforms are needed. The findings will provide valuable insights into gaps in financial oversight, loopholes in regulations, and recommendations to enhance ethical accounting in India's corporate sector.

COMMON TRENDS IN CORPORATE SCANDALS IN INDIA:

An analysis of major financial scandals in India (Satyam, PNB, IL&FS, Yes Bank, DHFL, Sahara, NSEL, Kingfisher Airlines, and many more) can reveal recurring patterns in how corporate frauds take place. These frauds typically follow a systematic sequence of unethical financial practices, weak governance, regulatory loopholes, and delayed detection and below is a detailed breakdown of the common trends observed in these financial scams:

1. Initial Manipulation of Financial Statements:

Companies often **inflate revenue, assets, and profits** to create an illusion of financial strength, misleading investors and regulators. **Undisclosed liabilities and bad loans** remain hidden until the fraud collapses. A prime example is the **Satyam Scam**, where profits were **overstated by ₹5,000 crore**, deceiving investors and boosting stock prices. Such financial misrepresentation **attracts more investors, banks, and regulatory approvals**, sustaining the fraud for years.

2. Fraudulent Loans & Misuse of Funds

Many financial scams involve companies securing **high-risk loans without due diligence**, which are then diverted for **personal luxuries, unrelated businesses, or money laundering**. The **PNB Scam (₹14,000 crore)** involved the fraudulent issuance of **Letters of Undertaking (LoUs)** by Nirav Modi, while the **Yes Bank Crisis** saw **high-risk loans** being extended to struggling companies like IL&FS and Jet Airways, leading to a liquidity crisis. These fraudulent loans often result in **massive NPAs (non-performing assets), bankruptcy, and significant losses for investors and financial institutions**.

3. Auditor & Rating Agency Collusion

Auditors, who are responsible for ensuring financial transparency, often **fail to detect fraud due to conflicts of interest or direct involvement in the scam**. Credit rating agencies contribute by assigning **high ratings to financially weak companies**, misleading investors and delaying corrective action. In the **IL&FS Crisis**, auditors and rating agencies-maintained **AAA ratings for IL&FS**, even when the company was near financial collapse. Similarly, in the **DHFL Scam**, auditors failed to detect **₹31,000 crore worth of fraudulent loans and fund diversion**, allowing the scam to continue for years. This misrepresentation **gives investors a false sense of security**, only for the truth to emerge when the company fails.

4. Regulatory Loopholes & Weak Enforcement

Regulatory bodies often fail to **detect fraud early** due to **insufficient monitoring and gaps in financial laws**. Scammers **exploit these weaknesses** to sustain frauds for years. In the **Sahara Scam**, the company illegally collected **₹24,000 crore from investors**, benefiting from **SEBI's weak enforcement mechanisms**. Similarly, in the **NSEL Scam**, loopholes in commodity trading laws allowed **NSEL to operate a Ponzi scheme worth ₹5,600 crore**. Such regulatory failures **result in delayed intervention**, causing enormous financial damage.

5. Market Manipulation & Stock Price Inflation

Fraudulent companies manipulate stock prices using fake news, insider trading, or pump-and-dump schemes. Artificially inflated stock prices attract more investors before the fraud collapses. Example: Satyam Computers' stock price crashed by 77% overnight after the fraud was exposed. Yes, Bank shares plummeted from ₹404 to ₹5 when its financial crisis became public. Outcome: Retail investors lose billions, while fraudsters often escape with profits.

6. Political & Corporate Nexus Enabling Fraud

Fraudsters use political influence to escape regulation and secure financial support. Government agencies delay investigations due to political interference. Example: Kingfisher Airlines – Vijay Mallya secured loans worth ₹9,000 crore despite poor financial health, due to political influence. DHFL Scam – Loans were allegedly diverted to political entities, delaying investigations. Outcome: Fraud continues for years before action is taken, causing major financial damage.

7. Scam Exposure & Sudden Collapse

Whistleblowers, investigative journalists, or regulatory audits expose financial frauds. Mass withdrawals by investors and banks lead to liquidity crises. Example: Satyam Scam – Chairman Raju confessed, leading to a

77% stock price crash. IL&FS Crisis – Default on debt triggered market panic and NBFC sector instability. Outcome: Massive financial losses, investor panic, and regulatory intervention.

8. Delayed Legal Action & Limited Recovery

Legal proceedings take years, allowing fraudsters to escape or transfer assets abroad. Recovery of funds is slow, leaving investors and creditors with massive losses. Example: Nirav Modi (PNB Scam) fled India in 2018, and extradition is still pending. Sahara investors are still waiting for refunds, years after SEBI's intervention. Outcome: Fraudsters often escape justice, and investors rarely recover their money.

Yes Bank Crisis: A Detailed Analysis

1. Introduction

The Yes Bank crisis (2020) was one of the most significant failures in India's private banking sector, exposing weak corporate governance, risky lending practices, and regulatory lapses. Yes Bank, once India's fifth-largest private bank, suffered a severe liquidity crisis due to its high exposure to risky corporate loans and failure to raise fresh capital.

The crisis led to government intervention, the RBI taking control of the bank, and a ₹10,000 crore rescue plan led by State Bank of India (SBI) and other major banks. The failure highlighted the importance of strong financial oversight and resulted in stricter banking regulations.

2. Company Background

Founded in 2003 by Rana Kapoor and Ashok Kapur, Yes Bank emerged as one of India's fastest-growing private banks. The bank focused on corporate banking, retail banking, and asset management, positioning itself as a high-growth financial institution. By 2019, Yes Bank was the fifth-largest private lender in India, with rapid loan book expansion, growing 334% between 2014 and 2019. Despite its aggressive lending strategies and rising non-performing assets (NPAs), the bank maintained an AAA credit rating, misleading investors and depositors about its actual financial health.

3. Nature of the Scandal

The crisis stemmed from excessive lending to high-risk businesses, underreported NPAs, and insider corruption. Yes Bank provided over ₹34,000 crore in loans to financially unstable groups, including DHFL, Reliance ADAG, Jet Airways, and IL&FS. Instead of recognizing bad loans, the bank engaged in evergreening, issuing new loans to defaulting companies to prevent classifying them as NPAs. Additionally, top executives, including Rana Kapoor, were accused of accepting bribes in exchange for approving high-risk loans. To maintain a false sense of financial stability, Yes Bank falsified financial reports, manipulated credit ratings, and misled investors and depositors.

4. How the Fraud Was Executed

The fraudulent practices were carried out in multiple ways. The bank underreported NPAs and overstated profits, misleading regulators and the market. Rana Kapoor allegedly took kickbacks from borrowers and engaged in insider trading, selling Yes Bank shares at inflated prices for personal profit. Credit rating agencies were influenced to maintain an artificially high rating, ensuring continued investments despite the bank's financial instability.

5. Discovery & Exposure

Warnings about Yes Bank's financial health surfaced in 2017-2018, when the Reserve Bank of India (RBI) found ₹3,277 crore in underreported NPAs and issued a warning. By 2019, credit rating agencies downgraded Yes Bank, triggering investor panic. In March 2020, the bank failed to raise new capital, prompting the RBI to take control. Rana Kapoor was arrested under money laundering charges, marking a turning point in the bank's downfall.

6. Regulatory & Legal Actions

a) RBI Intervention & Government Takeover

- March 5, 2020: RBI superseded Yes Bank's board and imposed a 30-day moratorium.
- Withdrawals were capped at ₹50,000 per customer, causing public panic.
- State Bank of India (SBI) and other banks infused ₹10,000 crore to rescue the bank.

b) SEBI & CBI Investigations

- Rana Kapoor was arrested for fraud, bribery, and money laundering.
- Deloitte and BSR (Yes Bank's auditors) faced scrutiny for failing to detect fraud.

7. Impact of the Scandal

The crisis had a major impact on India's banking and financial sector. It eroded trust in private banks, causing mutual funds and NBFCs with exposure to Yes Bank bonds to suffer losses. The RBI imposed stricter asset quality monitoring for all banks to prevent future failures. Investors and customers were severely affected, as depositors faced withdrawal restrictions, and Yes Bank's stock price collapsed from ₹404 (2019) to ₹5.65 (2020), wiping out shareholder wealth. The liquidity crisis led to panic withdrawals, with ATMs running out of cash.

8. Regulatory Reforms Introduced

- a) Strengthened RBI Oversight on Private Banks-RBI now monitors private banks more closely to prevent similar crises.
- b) Mandatory Board-Level Risk Management-Private banks must now have stronger independent oversight on lending decisions.
- c) Stricter NPA Disclosure Rules-Banks must declare stressed assets more transparently to prevent hidden NPAs.

9. Lessons Learned & Preventive Measures

- a) Stronger Corporate Governance: Independent directors must monitor bank activities more effectively.
- b) Transparent Lending Practices: Strict background checks before approving loans.
- c) Accountability for Bank Executives: Regulations must ensure CEO and board accountability in case of fraud.

10. Current Status of Yes Bank

Currently, Yes Bank is under stable management following the SBI-led rescue plan. The bank has implemented new risk management policies and stronger governance structures to prevent future instability. While its stock price has shown signs of recovery, investor trust remains fragile, requiring sustained financial transparency and regulatory vigilance.

PNB Scam: A Detailed Analysis

1. Introduction

The Punjab National Bank (PNB) scam (2018) is one of the biggest banking frauds in India, involving fraudulent transactions worth ₹11,400 crore. This scam was orchestrated by Nirav Modi, Mehul Choksi, and senior PNB officials, exploiting loopholes in banking regulations. The fraud revolved around the misuse of Letters of Undertaking (LoUs)—a financial instrument used to obtain overseas credit. By bypassing core banking systems, Nirav Modi's firms secured unauthorized loans from foreign banks. The scam went undetected for seven years (2011-2018), exposing serious weaknesses in banking oversight, audit mechanisms, and fraud detection systems.

2. Company Background

PNB, India's second-largest public sector bank, was at the centre of the fraud, involving high-profile businessmen Nirav Modi and Mehul Choksi, who owned Gitanjali Gems and Gitanjali Group, respectively. Key bank officials, including Gokulnath Shetty (PNB Deputy Manager) and Manoj Kharat (PNB Single Window Operator), were allegedly complicit in the fraud. The financial exposure extended beyond PNB to other Indian banks with overseas branches, including Allahabad Bank, Axis Bank, and UCO Bank, making it a significant crisis for the banking sector.

3. Nature of the Scandal

The fraud revolved around forgery, fake loan approvals, and unauthorized financial transactions. Fraudulent Letters of Undertaking (LoUs) were issued without collateral, enabling Nirav Modi's firms to secure massive loans from overseas branches of Indian banks. The scam bypassed the Core Banking System (CBS), allowing transactions to remain undetected for years. Bank officials misused the SWIFT messaging system, facilitating the transfer of funds without proper authorization. The fraud persisted through evergreening of loans, where old loans were repaid using newly issued LoUs, delaying detection while inflating the total scam value.

4. How the Fraud Was Executed

a) Issuance of Fake LoUs

- LoUs act as a guarantee by a bank for obtaining overseas loans.
- PNB officials issued LoUs fraudulently, bypassing internal banking protocols.
- Foreign banks, trusting these guarantees, lent money to Nirav Modi's firms.

b) Concealment Using SWIFT Messages

- The fraudulent transactions were recorded only on the SWIFT system, not on the Core Banking System (CBS).
- This ensured that PNB's internal audit team never detected the missing funds.

c) Continuous Loan Renewal (Evergreening)

- When loans became due, new LoUs were issued to repay old ones, hiding defaults.
- This process continued for seven years, inflating the scam's value.

d) Fraudulent Collaborations with Bank Officials

- Gokulnath Shetty & Manoj Kharat, PNB employees, manipulated records and ensured loan approvals without following standard procedures.

5. Discovery & Exposure

The fraud came to light in January 2018, when a newly appointed PNB employee refused to renew a LoU without proper collateral, leading to an internal investigation. PNB discovered unauthorized LoUs worth ₹11,400 crore, exposing the massive scale of fraud. In February 2018, PNB officially reported the fraud to the Central Bureau of Investigation (CBI), triggering a nationwide banking crisis. By March 2018, both Nirav Modi and Mehul Choksi fled India, with Modi escaping to the UK and Choksi taking refuge in Antigua to evade legal action.

6. Regulatory & Legal Actions**a) Government & RBI Intervention**

- RBI banned LoUs in March 2018 to prevent future scams.
- Stronger fraud detection measures were introduced in public sector banks.

b) CBI, ED & SEBI Investigations

- CBI arrested multiple bank officials, including Shetty and Kharat.
- ED attached ₹700 crore worth of Nirav Modi's assets.
- SEBI tightened disclosure rules for publicly listed companies.

c) Extradition Proceedings

- Nirav Modi was arrested in London (2019); extradition proceedings are ongoing.
- Mehul Choksi remains in Antigua, avoiding deportation.

7. Impact of the Scandal**a) Banking Sector Crisis**

- Indian banks suffered huge losses, affecting public confidence.
- RBI imposed stricter monitoring on public sector banks.

b) Investor & Public Trust Erosion

- PNB's stock price crashed by over 50%, impacting investor wealth.
- The scandal damaged India's global reputation in banking governance.

c) Increased Banking Regulations

- Mandatory fraud detection audits introduced for all major banks.
- Tighter controls on SWIFT transactions.

8. Regulatory Reforms Introduced**a) Lou Ban & Stricter Trade Credit Rules**

- RBI banned LoUs to prevent similar frauds.
- Banks must now verify borrower credibility before issuing guarantees.

b) Improved Audit Mechanisms

- Internal banking audits strengthened to detect hidden transactions.
- SEBI introduced stricter disclosure norms for publicly traded companies.

c) Strengthening Corporate Governance

- Banks must rotate risk assessment officers periodically.
- Auditors held accountable for negligence.

9. Lessons Learned & Preventive Measures**a) Need for Stronger Internal Controls**

- Banks must integrate SWIFT with Core Banking Systems (CBS) for transparency.
- Fraud detection algorithms must be improved.

b) Better Employee Accountability & Background Checks

- Strict vetting of banking staff handling sensitive transactions.
- Mandatory job rotations for employees in loan approval departments.

c) Faster Legal Action Against Economic Offenders

- Quicker extradition of fugitives like Nirav Modi & Mehul Choksi.
- Stronger legal framework to prevent scamsters from fleeing India.

10. Current Status of PNB & Nirav Modi

Currently, PNB has managed to partially recover its losses through asset seizures. Nirav Modi remains in UK custody, awaiting the completion of extradition proceedings. Mehul Choksi continues to fight legal battles in Antigua, resisting deportation to India. In the aftermath of the scandal, Indian banking regulations have been significantly tightened, with enhanced fraud detection mechanisms in place to prevent future scams of this magnitude.

Comparative Conclusion from both the cases:

The Yes Bank crisis and PNB scam exposed critical flaws in India's (private) banking system, risk assessment, corporate governance and financial regulation systems. While RBI's intervention helped prevent a major banking collapse, the crisis highlighted the need for stricter financial regulations, better auditing practices, and greater transparency in lending operations. While stronger regulations have been introduced, the delay in legal proceedings shows the need for faster action against economic offenders. The ban on LoUs, improved bank audits, and tighter fraud detection are steps in the right direction, but continued vigilance is necessary to prevent future financial frauds.

The study revealed recurring patterns in financial frauds, including financial misreporting, weak corporate governance, auditor failures, and regulatory loopholes. Despite the introduction of stricter financial regulations such as the Companies Act, 2013, SEBI LODR Regulations, and ICAI's Code of Ethics, corporate frauds continue to persist due to poor enforcement, political influence, and delays in legal proceedings. These scams have severely impacted investor confidence, contributed to rising non-performing assets (NPAs) in banks, and caused significant disruptions in financial markets. The impact of financial fraud extends beyond financial losses, as it affects public trust, disrupts the economy, and weakens the credibility of India's financial institutions. Regulatory agencies such as SEBI, RBI, NFRA, and ED need to coordinate more effectively to prevent large-scale frauds, while legal delays in prosecuting financial criminals allow fraudsters to evade justice and transfer assets abroad.

To mitigate these risks, a multi-stakeholder approach is essential. Regulators and the government must strengthen enforcement mechanisms, improve inter-agency coordination, and introduce fast-track courts for financial crimes. Banks and financial institutions need to enhance risk assessment processes, implement real-time fraud detection systems, and hold executives accountable for reckless lending. Auditors and accounting professionals should focus on improving independence, conducting mandatory forensic audits, and enforcing stricter penalties for negligence. Additionally, investors and the general public must be educated on financial literacy, transparency in stock markets, and the importance of whistleblower protection mechanisms.

Corporate frauds pose a serious threat to economic stability and investor trust. While regulations have evolved to address emerging financial risks, their effectiveness depends on strict enforcement, corporate accountability, and greater transparency in financial reporting. Ethical accounting practices, strong corporate governance, and a proactive regulatory framework are essential in preventing future financial scandals.

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