

Nirav Modi: A Case Study on Banking Frauds and Corporate Governance

Fehmina Khalique

Professor, Lloyd Business School, Greater Noida

Email: fehminas@hotmail.com

Smriti Srivastava

PGDM Student, Lloyd Business School, Greater Noida

Email: smritisrivastava0810@gmail.com

ABSTRACT

In August 2018, Interpol and the Indian government filed charges against Belgian businessman Nirav Deepak Modi, who is wanted for illicit breach of confidence, deceiving, and dishonesty. The charges include illegal property dealing, corruption, criminal conspiracy, money-laundering, cheating, embezzlement, and contract breaching. Nirav is under investigation in connection with Punjab National Bank's \$2 billion fraud scandal, later in March 2018, he filed for bankruptcy in The United States of America. Finally, in June 2018, he was traced in the United Kingdom, where he is living by taking political asylum. Further, in June 2019, the total assets of US\$6.6 million were frozen in his Swiss Bank Account. Corporate Governance initiatives were laid down by government officials and intervention by reserve Bank was seek in the case to avoid future occurrence of such fraudulent practices.

1. INTRODUCTION

Nirav Modi was raised in Antwerp, Belgium, after being born in Palampur, Gujarat. His family has been in the diamond industry for many generations. At the age of 19, Modi came to Mumbai with his parents to work for his uncle Mehul Choksi, the renowned owner of the Gitanjali Group, a retail jewelry corporation with more than 4,000 outlets throughout India. Modi attended the University of Pennsylvania's

Wharton School but finally left. When he was just a student, he met Ami, the future wife of diamond billionaire Amuk raj Choksi.

In 1989 he relocated to India and received training in every facet of the diamond trade industry, Nirav in 1999 established Firestar, a trading company known for diamond previously known as Firestone. Rio Tinto's Argyle pink diamonds are only distributed by Firestar in India. His business began producing jewelry under contract in 2002. Later in 2005 he attained Frederick Goldman and Sandberg, Sikorski, and A. Jaffe in 2007 in the United States. After a close friend requested that Modi construct a set of earrings in 2008, he went on to launch the brand. He opened his own diamond store in 2010 in the Defence Colony of New Delhi. He then opened another store in Mumbai's Kala Ghoda.

In 2010, he appeared on the catalog covers of Christie's and Sotheby's, marking the first display of an Indian jeweler. By 2013, he was listed among Indian billionaires by Forbes.

Around the world, 17 more store openings transpired afterward. In 2015, Modi made its global debut with boutiques in New York, USA as well as Hong Kong. Two more boutiques in Hong Kong debuted in 2016, and one at the MGM Macau in the same year. He rose to fame in 2010 when he created the "Golconda Lotus Necklace," which used an antique 12-carat pear-shaped diamond as its focal point. The diamond was repolished after it was first sold in the 1960s. A lattice of pink and white diamonds was displayed. It was featured on the Hong Kong Christie's catalogue cover and sold for USD 3.6 million at auction in 2010. He allegedly overextended himself for a number of years and utilized fresh MOUs to cover the previous ones for roughly seven years. "He wanted to grow his business, and to do in five years what might have taken twenty years," stated one of his employees. "Maybe he could have pledged his equity, raised some money, and finally paid the bank back," he asserted, had he gone public. Maybe that's what he would have done. Nirav Modi is wanted by Interpol and is well-known for his bank fraud in the Diamond Business. He was taken into custody in London on March 20, 2019. Nirav Modi and Ami Modi are wed, and they have three kids together. He faces accusations of deceit, criminal conspiracy, and criminal breach of trust. Since 2018, both have been sought after by the Police of Royal

Canadian Mounted, Los Angeles Police Department, Interpol, the Judicial Authorities of India, and the Federal Bureau of Investigation.

2. DEALINGS WITH INDIAN BANKS

A lawsuit was brought by the Union Bank of India against Nirav Modi in a court in Hong Kong. Union Bank claimed that Modi had sanctioned two loans provided to Firestar Diamond on November 15, 2011, and Firestone Trading Private on October 21, 2011, in a suit filed with the High Court on September 26, 2018. According to reports, the bank demanded that \$5.49 million plus interest, claiming that both businesses had fallen behind on their obligations.

Three American companies controlled by Nirav Modi who filed for bankruptcy in the US following the colossal PNB scam have objected to allegations from Union Bank of India's Branch in London, thereby, attempting to reject the claims of USD 3.2 million from the former and around USD 0.4 million from the latter. Seth R. Freeman, a bankruptcy in San Francisco, stated, "The key problem for Union Bank of India and Bank of India is that while they may have engaged in credit transactions with Modi-controlled entities, the banks making the claims are not direct creditors of the US companies."

The Indian banks are unable to pursue their claims against Firestar Diamond specifically since the company is currently facing bankruptcy proceedings, even if they may have claims against other businesses in the Firestar corporate family. It seems that the vast network of shadow companies with legal addresses in Dubai, Belgium, and other nations that Nirav Modi utilized to carry out the USD 4 billion scam could make it extremely difficult for PNB and other banks to recuperate anything from lawsuit in the US. The deceptive acquisition of false Letters of Undertaking (LoUs) was a component of the scam that ran from 2011 to 2018. With the help of LoUs, an importer can get short-term credit from its Indian bank, backed by invoices for items that are yet to be imported. The multibillion-dollar PNB scam that surfaced exposed Nirav Modi's use of fictitious transactions to exaggerate the import figures of Indian companies like Diamonds R Us, Solar Export, and Stellar Diamond in order to secure additional LoU funds.

The multiple shadow companies set up to launder money taken fraudulently from PNB and other banks were also verified by the US bankruptcy court-appointed examiner last year. Union Bank filed a proof of claim for USD 3,168,074 against Firestar Diamond Inc. and Old AJ (A Jaffe, Inc.) on April 26, 2018. Its claim is based on money that Firestar Diamond is purportedly owing to Firestar Diamond BVBA, Belgium, a different firm in the group that is presently facing bankruptcy in Belgium. "The Nirav Modi scam is incredibly intricate and was made possible by dishonest bank employees who gave it the impression of legitimacy by enabling it to grow and persist for a long time. The investors of party transactions ignored due diligence and trusted in PNB's relationship and credit management with Modi, which is nearly akin to what we refer to as "affinity fraud," according to Freeman. He continues by saying that watching the intricate workings of Firestar Diamond US could be educational. "It includes Indian creditors who provide loans to Indian exporters and importers who have overseas subsidiaries and could face bankruptcy procedures in the United States. Getting cross-border skills will be more and more crucial.

Economic Offenders Ordinance, commenced the asset seizure process for all the accused, aiming for their swift forfeiture. In March 2019, Nirav was detained by police officials in London on charges encompassing conspiracy, breach of trust, theft, corruption, and money laundering, which involved the conveyance of property. The fraudulent employees manipulated the SWIFT international financial communication system to generate letters of intent for foreign branches of various Indian banks, thereby circumventing the bank's core banking system.

2.1 Punjab National Bank (PNB) Fraud Case

The 2018 Punjab National Bank (PNB) Fraud Case centers around a fraudulent letter of undertaking issued by the bank's Mumbai branch, totaling INR12,000 crore (USD 1.4 billion). PNB is consequently held accountable for the entire amount. Allegedly masterminded by jeweler and designer Nirav Modi, the scheme is detailed in a charge sheet released by the Central Bureau of Investigation (CBI), which names Nirav, his wife Ami, brother Nishal Modi, uncle Mehul Choksi, and associates from companies such as M/s Diamond R US, M/s Solar Exports, and M/s Stellar Diamonds. The implicated parties include PNB employees, officials, and directors of Mehul Choksi's

and Nirav Modi's enterprises. Shortly before the revelation of the fraud in 2018, Nirav Modi and his family went missing.

Initially, the bank attributed the scam to two employees at the branch, but a recent hire detected the transactions. Subsequently, the bank made a complaint to the CBI, which, along with the Enforcement Directorate and the Reserve Bank of India, investigated the conspiracy. In a chargesheet, the CBI implicated prominent figures like Usha Anantha Subramanian, the former CEO of PNB, and executive directors KV Brahmaji Rao and Sanjiv Sharan, accusing them of defaulting multiple RBI circulars and caution notices related to the reconciliation of SWIFT messages and core banking systems.

In February 2018, Punjab National Bank filed a complaint with the CBI, alleging a conspiracy involving Modi and his associates collaborating with bank employees to acquire fraudulent Letters of Undertaking, aiming to defraud the bank of Rs 2800 crore (approximately US\$4 billion). The CBI initiated investigations into the allegations, and though the reported fraud stands at Rs 2800 crore, the potential loss for Punjab National Bank could extend to Rs 11000 crore. The CBI filed a fraud case, while the Enforcement Directorate conducted further inquiries.

Regarding the PNB fraud, an official informed the agency that two employees at the bank's Branch office in Mumbai, namely, Gokul Nath Shetty, retired Deputy Manager of PNB, and another bank official issued fraudulent Letters of Undertaking (LoUs) to Hong Kong-based investors on behalf of three firms associated with Nirav Modi and the Gitanjali Group. The first information report (FIR) filed by the CBI stated, "The public servants committed abuse of official position to cause pecuniary advantage to Diamonds R US, Solar Exports, and Stellar Diamonds and wrongful loss of INR 280.70 crore to PNB during 2017."

As part of the PNB fraud probe, on June 13, 2018, the Central Bureau of Investigation (CBI) contacted Interpol, urging the issuance of a red corner notice (RCN) for Nishal, the brother of Nirav Modi who was an accomplice in the case. The CBI additionally sought Interpol's cooperation in issuing an RCN for Nirav Modi and Mehul Choksi of the Gitanjali group.

Usha Anantha Subramanian, the ex-MD and ex CEO of Allahabad Bank, was granted bail on August 20, 2018, subject to a INR 1 lakh surety bond by the Special CBI Court in Mumbai. Usha was terminated by the government on her last day of employment a week prior. Between August 2015 until May 2017, Anantha Subramanian served as the MD of Punjab National Bank. She also served as its executive director. Her dismissal was effective right away. Gokul Nath Shetty, a prominent accused and retired deputy management of Punjab National Bank, is the target of a disproportionate assets case filed by the CBI on the grounds that he accumulated fortune 200 percent beyond his known sources of income. Gokul Nath Shetty, a prominent accused and retired deputy management of Punjab National Bank, is the target of a disproportionate assets case filed by the CBI on the grounds that he accumulated fortune 200 percent beyond his known sources of income.

A special court issued an order on Wednesday for the release of eighteen properties with a combined value of approximately Rs 71 crore linked to the absconding diamond trader Nirav Modi and his companies. These assets were designated for the bank and the appointed liquidators. The bank asserted its ownership over specific properties that the Enforcement Directorate (ED) had previously attached, both individually and on behalf of a consortium of banks. The bank claimed a loss exceeding Rs. 7,000 crores due to the accused's alleged actions involving the acquisition of fictitious Letters of Understanding (LoUs). The bank sought the release or restoration of properties falling under various categories, such as those exempt from seizure, secured, mortgaged, and hypothecated. These included 18 properties, including eight cars (including a Rs 26 lakh Bentley), office spaces in Kurla, 16 pieces of jewelry from a five-star hotel's display stock, and valuables at the custodian of Bharat Diamond Bourse from Hong Kong and Dubai, valued at over Rs 40 crore.

The court directed the release of these properties to PNB and the liquidators of two Modi enterprises, Firestar International Limited and Firestar Diamond International Limited, categorizing them based on their respective classifications. Additionally, the court mandated the issuance of an undertaking to ensure adherence to legal procedures during the restoration of the properties.

3. IMPACT ON NEERAV MODI'S BUSINESS

Modi has lost all of his wealth as a result of his brand failing. He was taken off Forbes' yearly list of billionaires, and the company estimated his current net worth to be less than \$100 million on March 9, 2018. Due to the debacle, the RBI no longer issues LoCs for imports, which has reduced importers' financial flexibility. In May 2018, he put his company, A. JAFFE, up for auction. Parag Diamond won the deal, which he had obtained through his Synergies Corporation. Since then, every store has closed.

A handful of Modi's stores, such as the one at Marina Bay Sands in Singapore, continued to operate as usual at first, but they have all eventually shuttered. Modi's company, Firestar Diamond Inc., filed for bankruptcy on March 7, 2018, in a Manhattan bankruptcy court, to safeguard its US assets and its revolving credit arrangement with Israel Discount Bank. In his response to the bank on February 15 and 16, 2018, Modi said, "Your actions have destroyed my brand and business and now have restricted your ability to recover all the dues leaving a trail of unpaid debts. Your actions have been driven by your anxiety to recover your dues immediately, despite my offer (on February 13, a day before the public announcement and on 15)."

Modi stated that "this could have helped reduce/ discharge the debt to the banking system" and valued his domestic company at approximately Rs. 6,500 Crore. However, he asserted that this is no longer feasible because all of his bank accounts have been stopped and his assets have been confiscated. Along with his spouse Ami Modi, Modi purchased a seafront home in Mumbai's highly sought-after Samudra Mahal neighborhood for Rs 900 crore. The Enforcement Directorate has attached his properties in India, which include jewels, paintings, and real estate valued at approximately Rs 523 crore (almost USD 75 million).

Modi's four 9.6-megawatt (MW) wind power projects in Rajasthan have been connected to the Enforcement Directorate (ED). Thanks to a share purchase arrangement with Rajasthan's State power board, the plants can make up to Rs. 5 crores annually. Since 2014–2015, these wind power stations have been in operation. A 5.24 MW solar power project covering 135 acres in Ahmednagar district, was attached by the ED in March 2018; the plant was valued at Rs 60 crore. To look into the matter, the ED and the CBI each filed two FIRs in May 2018. It is rumored that

Mehul Choksi and Modi both departed the nation before criminal charges were brought against them.

The Telegraph claimed to have seen Modi visit the UK in March 2019. It was reported that he was spending eight million dollars on an apartment. In response to the report, Indian authorities stated that they had requested extradition to the UK. He was taken into custody in London on March 20, 2019, following the issuance of an arrest warrant. A portion of his art collection was auctioned off later that month to garner \$8 million for Indian tax officials. 68 pieces from Modi's art collection were auctioned in March 2019 on behalf of the income tax authorities in India. In total, the artwork fetched nearly €5.3 million, with a painting by Vasudev S. Gaitonde bringing in €2.6 million. Following the valuation, the renowned music store Rhythm House in Kala Ghoda, Mumbai, is set to go up for auction; Nirav Modi had purchased it in 2017. One day after his remand was extended, on May 31, Modi filed an application for bail in the UK High Court. As of October 2020, all of his motions for bail have been denied.

The Prevention of Money Laundering Act (PMLA) Court announced the order for seizing Nirav Modi's property, valued at approximately Rs 1,400 crores on June 8, 2020. The UK court, on February 25, 2021, granted the Indian government's request for Modi's extradition as a key defendant in the PNB fraud case. The extradition order, signed by the UK Home Secretary on April 15, paved the way for his return to India. Following this, Modi had a 14-day window to appeal to the UK High Court, which he exercised on May 1, contending that he would not receive a fair trial under Indian law. While awaiting the outcome of the extradition appeal, Modi remained in Wandsworth Prison in southwest London for several months. On June 23, 2021, the UK High Court denied Modi's request to contest demand to go back to India. The October 2021 Pandora Papers revealed that just a month before leaving India, his sister Purvi Modi established an offshore company. However, the UK Royal Courts of Justice in London rejected the UK Home Secretary's decision for Nirav Modi's extradition to India in December 2022. Additionally, he was obligated to pay legal fees amounting to euros 150,247.

4. ALLEGATIONS AND INVESTIGATIONS

Since June 2018, Nirav Modi, who went missing in February 2018, has been living in the United Kingdom's capital. On March 19, 2019, he was captured in central London after a bank employee of Indian origin recognized him and informed the police. The UK authorities arrested him at the request of the Indian government, which was seeking Modi's extradition. Modi appeared in court on March 20, 2019. Due to concerns about his potential to flee the country, the UK court denied him bail and he was ordered to remain in custody until May 24, 2019. The court cited flight risk and the possibility of falsifying evidence if released. The court hearings revealed that Modi had made threats to eliminate a key witness and attempted to influence another to evade prosecution.

In June 2019, Swiss authorities "froze" four of Nirav Modi's and Purvi Mehta's Swiss bank accounts as part of the scam. The Enforcement Directorate has requested the freezing of the entire sum of Rs. 283.16 crore. Subsequently, on July 2, 2019, the Singapore High Court issued an order to freeze all the bank accounts linked to Modi, Purvi, and her husband, Mayank Mehta which amounted to INR 44 crore. Red Corner Notices were issued against Purvi and Mayank by Interpol.

CBI in August 2019 submitted an application in the special CBI Court, seeking the declaration of Nirav Modi, his brother Nishal Modi, and associate Subhash Parab as proclaimed offenders, and requested the seizure of their assets. All three individuals are identified as "wanted" in the charge sheet connected to the INR13,700 crore PNB scandal.

In September 2019, Prime Minister Gaston Browne of Antigua and Barbuda openly labeled fugitive diamondaire Mehul Choksi of the Gitanjali Group as a "crook." Browne also suggested that Choksi would eventually be repatriated to India once all legal avenues were exhausted. In contrast, Choksi maintained that he had left India for medical treatment and committed to returning once he was deemed medically fit.

In December 2019, an additional charge sheet filed in the CBI court in Mumbai implicated Nirav Modi, his stepbrother Nehal Modi, and two business associates in attempting to intimidate witnesses and destroy evidence. The Enforcement Directorate auctioned off luxury goods seized from Nirav Modi for INR 2.29 crore in March 2020. Nehal Modi was once again subject to Interpol's Red Corner Notice in May 2020 for his involvement in assisting his stepbrother in defrauding the PNB.

Nehal and Nishal Modi's challenge to the Red Corner Notice from the previous year led to Nehal's name being removed from the Interpol website. According to an investigation, Nehal operated two businesses for Nirav Modi that received \$50 million from fabricated corporations. When the fraudulent scheme was exposed, he misappropriated significant assets and allegedly threatened witnesses while destroying digital evidence in Dubai. Later, a court under the Prevention of Money Laundering Act (PMLA) ordered the seizure of Nirav Modi's properties valued at over Rs 1,400 crores.

The Nirav Modi trial was postponed by the UK court from May 2020 to September 2020 for a five-day extradition trial. Following five UK denials of his release, Modi has asked for political asylum. The Enforcement Directorate (ED) filed a charge sheet against Mehul Choksi in July 2020, claiming that he operated a well-organized scheme to defraud lenders and clients in the US, India, and Dubai. Gitanjali Groups is one of the biggest branded jewelry dealers in the world. The company's main office was in Mumbai, India. Gitanjali had controlled a market share of more than 50% of the Indian organized jewelry sector and sold its products through more than 4,000 points of sale. Nakshatra, D'damas, Gill, Asmi, Sangini, Maya, Giantti, World of Solitaire, and Shuddhi were among the well-known brands that the group possessed.

ROLE OF CORPORATE GOVERNANCE IN BANKING SECTOR

Governance is the process of decision making and the process by which decisions are implemented or not implemented. From the Academic Point of View “Corporate governance addresses problems that result from the separation of ownership and control.”. According to *The Hindu Business line*, July 9, 1997, “Corporate governance is not just corporate management; it is a much broader concept and includes a fair, efficient and transparent administration to meet certain well-defined objectives. It is a system of structuring, operating and controlling a company with a view to achieving long-term strategic goals to satisfy shareholders, creditors, employees, customers and suppliers and complying with the legal and regulatory requirements, apart from meeting environmental and local community needs.”

In the realm of corporate governance, values, codes, and internal control systems play a crucial role in facilitating the flow of capital, combating corruption, safeguarding stakeholders, and promoting industrial and economic development. The advantages of

sound corporate governance extend to fostering a positive corporate culture in an organization, thereby enhancing stakeholders' confidence. Well-governed companies are often perceived favorably, commanding a premium for their stocks and contributing to the creation and strengthening of a corporation's competitive edge.

Since the four-fifths of the banking business in India is under the control of public sector banks, it complicates the corporate governance since the effective management vests with the government, while top management and board of banks operate merely as functionaries (Reddy, 1998). It is time that the nation debates whether corporate governance is compatible with the present form of public ownership as it makes the head of the institution accountable to political institutions (Sarkar and Sarkar, 2000). The Joint Parliamentary Committee on Stock Market Scam observes that it is imperative for banks to follow strategies and techniques basic to all tenets of corporate governance (Verghese, 2002).

4.1 Corporate Governance in Banking Sector

The concept of the duty of care in banking has a long and contentious history. The first case to define the contemporary "tort-based duty of care for bank directors" was *Briggs v. Spaulding* (141 U.S. 132, 1891). In this case, the president of a National Bank in Buffalo, United States, took the bank to insolvency by making illegal and fallacious loans in his and his family members accounts along with individuals with doubtful financial history. The board of directors of the bank ignored the management of the bank, rather relied only on the president to manage the business. Consequently, Briggs recognized a federal common law standard of negligence for directors of federally chartered and federally insured depository institutions by mandating that directors exercise "ordinary care" in conducting the affairs of the bank.

In August 1999, the Basel Committee also issued a guidance paper titled "Enhancing Corporate Governance for Banking Organizations." This document was directed towards supervisory authorities worldwide, providing assistance in encouraging the adoption of robust corporate governance practices by banks within their respective countries.

4.2 Importance of Corporate Governance for Banks

From a banking industry perspective, corporate governance involves the manner in which their boards of directors and senior management govern the business and affairs of individual banks, affecting how banks set their corporate objectives, run day-to-day operations, consider the interests of various stakeholders, align corporate activities with the expectation that banks will operate in a safe and sound manner and in compliance with applicable laws and regulations and protect the interests of depositors (Becker and Stigler, 1974).

According to Hay and Shleifer (1998) some of the best corporate governance practices for banks include establishing strategic objectives and a set of corporate values communicated throughout the organization, strong risk management functions, special monitoring of risk exposures, setting and enforcing clear lines of responsibility, etc.

4.3 Role of the Reserve Bank in Effective Corporate Governance

The escalating competitiveness and interconnectivity among banks and financial institutions, both domestically and internationally, underscore the heightened significance of corporate governance in the banking and financial institutions in India. Establishing corporate governance in banks involves adherence to a comprehensive set of legal, accounting, financial, and economic rules and regulations. Ensuring competence and integrity within the banking sector necessitates the implementation of uniform standards for governance in both private and public sectors. The regulatory framework enforced by the Reserve Bank plays a pivotal role in influencing the overall health and stability of the banking sector.

4.4 Corporate Governance in Banks

Many bank failures in the past have been attributed to inadequate and insufficient management which enabled the banks to accept low quality assets and assume additional risks that extend beyond the level appropriate for the banks' capacity (Kohli, 2003). Some of the best practices for promoting corporate governance in banks are:

- Banks need to acknowledge the volatile and changing landscape where corporate governance has become a prominent concern. Even smaller banks

should prioritize corporate governance restructuring to address the perceived lack of honesty and integrity in the operations of corporations.

- Banks should strive to establish proficient and steadfast Board of Directors by engaging well-qualified individuals with proven integrity. Emphasizing a majority of truly independent directors ensures board effectiveness, periodic meetings, and the formulation of long-term policies, strategies, and values.
- Banks must institute a Corporate Code of Ethics, originating from the top, to govern both short-term and long-term operations. Regular annual reviews are essential to ensure compliance, as relying solely on the intrinsic adherence of rank-and-file employees may prove insufficient.
- Banks should contemplate creating an office of the Chairman of the Board, reporting to the board and acting as its daily eyes and ears in overseeing the functions of the bank.
- Banks are encouraged to establish effective and operating Audit, Compensation, and Nominating/Corporate Governance Committees, all comprising independent, outside directors. These committees should operate independently, with access to external attorneys and consultants to prevent bias in decision-making.
- Banks must consider fair compensation for directors, commensurate with the risks they undertake.
- Banks should prioritize disclosure of information, realizing that the process may now be quicker and more burdensome. Communication methods, such as quarterly letters to shareholders, should be utilized for effective disclosure.
- Banks need to recognize their duty to establish Corporate Governance practices that promote shareholder value. The board's main objective should be to maximize shareholders' wealth, incorporating corporate governance procedures into the long-term strategy for shareholder value maximization.

The unique nature of banking institutions requires a comprehensive perspective on corporate governance, particularly with the need for regulations to safeguard depositors. Developed economies typically rely on a system of prudential regulation to protect depositors in a deregulated environment. However, in emerging economies, this protection has challenges such as the absence of qualified supervisors, insufficient disclosure requirements, the cost associated with raising bank capital etc.

To adhere to best corporate governance practices for banks, several key considerations are highlighted. These include recognizing the evolving times, establishing honest and reliable board of directors, implementing a corporate code of ethics, considering the establishment of an office of the chairman of the board, ensuring the presence of effective and operating audit, compensation, and nominating/corporate governance committees, evaluating board compensation strategies, prioritizing information disclosure et.al.

5. BANKING REFORMS

Prominent officials from the Reserve Bank of India have consistently emphasized the necessity for reforms in public sector banks grappling with Non-Performing Assets (NPAs). Former Governor of the Reserve Bank of India, Urjit Patel, articulated on April 25, 2018, that the Indian banking system could witness improvement if some public sector banks were consolidated to create fewer yet more robust entities. Patel highlighted that such consolidation could effectively address the challenge of stressed assets within the banking sector.

During a lecture at Columbia University, Patel expressed, "As many have pointed out, it is not clear that we need so many public sector banks. The system could be better off if they are consolidated into fewer but healthier banks." He further suggested that certain banks could be merged, providing an opportunity for timely government intervention.

Later, on December 7, Patel underscored that the recapitalization package for public sector banks should not only be linked to their capital requirements but also tied to reform initiatives. This linkage aims to ensure that the funds injected into the banks do not contribute to sowing the seeds of the next "boom and bust cycle of lending." Patel mentioned that the central bank is collaborating with the government to finalize the recapitalization plan, emphasizing the importance of incorporating reform measures into the process.

At that time, the Finance Minister, Arun Jaitley, unveiled an unprecedented plan for the recapitalization of PSU banks, amounting to Rs 2.11 trillion, with Rs 1.35 trillion allocated for recapitalization bonds. Viral Acharya, the Deputy Governor of RBI, emphasized the pivotal role of public sector banks on April 28, 2017, stating that a

bank should embody a sense of reliability. He highlighted the true essence of "banking upon something" as a testament to credibility, confidence, and trust—a reputation that banks ideally cultivate over time through judicious decision-making.

Acharya clarified that essentially, if a significant economic upheaval, such as a substantial decline in house prices, a global economic downturn, or underperformance across various industrial sectors, were to impact the banking system, and the bank chose to remain heavily exposed to these risks, a considerable portion of its assets could be deemed risky simultaneously. In such a scenario, coping with an unexpectedly large deposit withdrawal would prove challenging for any bank situated on the shores of this economic turmoil.

Moreover, Acharya pointed out that when a bank begins repaying some depositors in response to such a crisis, it may instil fear among other depositors that the bank's liquidity is diminishing, raising concerns about the safety of their savings. This fear is exacerbated if the underlying assets are either unsafe or lack liquidity in inter-bank markets. In such a situation, depositors might initiate withdrawals, triggering a bank "run." As the news of this run circulates, depositors in other banks, particularly those with similar assets, may also start withdrawing funds, leading to a widespread banking panic. In such a scenario, there is a significant risk of the entire banking system undergoing disintermediation. This can lead to a standstill in the payments and settlements of financial transactions. Banks, lacking the capacity on their balance sheets, are unable to extend new loans to aspiring entrepreneurs, first-time home buyers, and established families. Consequently, this can result in a halt to economic activity, bringing it to a grinding stop. Although banks may still exist, the essence of banking, which serves as the lifeblood of the economy by channeling savings into productive uses and facilitating job creation, is compromised.

REFERENCES

1. Reddy Y.R.K. "Corporate Governance and Public Enterprises: From Heuristics to an Action Agenda in the Indian Context", *The Asci Journal Of Management*, Vol.27, pp.1-24, 1998
2. *Briggs v. Spaulding*, 141 U.S. 132 (1891)

3. Sarkar J., Sarkar S, “Large Shareholder Activism in Corporate Governance in Developing Countries: Evidence from India”, International Review Of Finance, Vol.1, pp.161- 1945, 2000
4. Verghese K.C., “Best Practices for Corporate Governance IBA BULLETIN” pp. 13-15, 2002 [24] 141 U.S. 132 (1891). [25] 141 U.S. 132, 149 (1891), quoting In re Forest of Dean Coal Mining Co., 10 L.R.-Ch. 450, 451 (Rolls Court).
5. Basel Committee on Banking Supervision (BCBS) Enhancing Corporate Governance for Banking Organisations. Switzerland: Bank for International Settlements
6. Becker G., Stigler G., “Law Enforcement, Malfeasance and Compensation of Enforcers”, Journal of Legal Studies, Vol.3, pp. 1-18, 1974
7. Hay J.R., Shleifer A., “Private Enforcement of Public Laws: A Theory of Legal Reform”, American Economic Review. Papers And Proceedings Vol.88, pp. 398-403, 1998
8. Kohli S.S., “Corporate Governance in Banks: Towards Best Practices”, IBA Bulletin, pp.29-31, 2003
9. <https://www.governancenow.com/news/regular-story/nirav-modi-why-we-need-banking-reforms>
10. <https://m.economictimes.com/news/nirav-modi/amp>
11. https://www.thehindu.com/topic/PNB-Nirav_Modi_case/
12. <https://www.business-standard.com/about/what-is-pnb-scam>
13. <https://www.businesstoday.in/industry/banks/story/nirav-modi-case-pnb-fraud-11400-crore-scam-ed-cbi-raid-101200-2018-02-15>