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Banking Frauds and Their Impact: Harnessing Technology for Early Detection

Anish Shrimali
Chief Manager, Union Learning Academy- Digital Transformation, Union Bank of India, Mumbai, India

Abstract: *Fraud in the banking sector poses significant risks, including financial losses, operational disruptions, increased compliance costs, and reputational damage, particularly in India's rapidly digitalizing financial landscape. This research examines the impact of fraud on banks and highlights the role of advanced technologies like artificial intelligence (AI), machine learning (ML), and big data analytics in mitigating these risks. By leveraging early warning systems for real-time monitoring, predictive analytics, and automated fraud detection, banks can enhance their resilience against evolving threats. The study offers actionable insights through case studies and industry practices to strengthen fraud management frameworks, safeguard assets, and rebuild customer trust in an increasingly digital environment.*

Keywords: Frauds, Artificial Intelligence, Machine Learning, Big Data Analytics, Real-time monitoring, Predictive Analytics

I. INTRODUCTION

Fraud in the banking sector encompasses a wide range of deliberate deceptive practices designed to secure unauthorized financial gains. These activities undermine the integrity of financial institutions, eroding their stability and damaging their reputation. In the Indian banking landscape, fraud has emerged as a critical concern, particularly with the rapid digitalization of financial services. The Reserve Bank of India (RBI) and other regulatory bodies have reported a notable increase in fraud incidents in recent years, highlighting a growing trend of cybercrimes and technologically sophisticated schemes. This escalation is largely driven by the proliferation of digital payment platforms, online banking, and the evolving methods of malicious actors.

The impact of fraud on banks is multifaceted, extending beyond immediate financial losses to include operational disruptions, increased compliance costs, and a decline in customer trust. Such incidents can severely compromise a bank's financial performance, affecting profitability and market value. Additionally, recurring frauds tarnish the institution's credibility, leading to long-term reputational damage that is difficult to repair.

To counter these threats, banks are turning to advanced technological solutions. Early warning systems powered by artificial intelligence (AI), machine learning (ML), and big data analytics have become critical tools in identifying suspicious activities and preventing fraud before it escalates. These technologies enable real-time monitoring of transactions, predictive analysis of fraud patterns, and automated responses to potential risks.

This research delves into the implications of fraud on the operational and financial health of banks. It aims to assess the effectiveness of technological innovations in fraud detection and mitigation, providing a comprehensive understanding of how these tools can bolster the resilience of financial institutions.

1.1 Types of Frauds

- **Credit and Debit Card Fraud:** Credit and debit card fraud is one of the most prevalent forms of financial crime, with fraudsters exploiting vulnerabilities in digital payment systems to make unauthorized transactions. The rise of e-commerce, contactless payments, and digital wallets has increased the risk of such fraudulent activities.
- **Loan Fraud:** Loan fraud involves obtaining loans through fraudulent means, such as submitting forged documents, falsifying income statements, or colluding with bank officials. These frauds not only result in financial losses but also increase the burden of non-performing assets (NPAs) on banks.

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- **Phishing and Social Engineering Attacks:** Phishing and social engineering attacks are increasingly common as fraudsters exploit human vulnerabilities rather than technological flaws. Through deceptive emails, messages, or phone calls, they trick individuals into sharing sensitive information such as login credentials, OTPs, or bank account details.
- **Insider Fraud:** Insider fraud, perpetrated by bank employees or individuals with privileged access, poses a unique threat due to the trust placed in internal stakeholders. These frauds often involve the misuse of internal systems to embezzle funds or manipulate records.

1.2 Key Factors Contributing to the Rise in Bank Frauds

Technological Advancements

- **Increased Digital Transactions:** The shift towards online banking and digital payments has created new avenues for fraud. According to a Deloitte survey, 93% of respondents indicated that fraud incidents have increased over the last two years, with retail banking being particularly affected due to its reliance on digital channels.
- **Cybersecurity Vulnerabilities**: The rise of online transactions has also led to an increase in cybercrime, including phishing attacks and identity theft. The RBI reported that UPI fraud cases surged by 85%, highlighting vulnerabilities in digital payment systems.

Poor Internal Controls

- **Lack of Oversight:** A significant factor contributing to fraud is the lack of effective internal controls and oversight within banks. The Deloitte survey noted that poor oversight by line managers and inadequate segregation of duties have increased the likelihood of fraudulent activities.
- **Inadequate Fraud Risk Frameworks:** Many banks lack comprehensive fraud risk frameworks, making it difficult to identify and mitigate potential risks effectively.

Economic Pressures

- **Business Pressure to Meet Targets:** The economic downturn has intensified pressure on banks to meet financial targets, leading some employees to engage in unethical practices. The Deloitte survey found that business pressures were cited by 22% of respondents as a reason for increased fraud risks.
- **Loan Portfolio Frauds:** Fraudulent lending practices, such as inflating project costs or diverting loans for personal use, have become more prevalent, contributing significantly to non-performing assets (NPAs) in banks.

Immoral Behaviour and Ethical Lapses

- **Corruption and Nepotism:** There is a growing concern about the moral fibre of banking professionals. Reports indicate that unethical behaviour among bankers and collusion with external parties have led to increased instances of fraud.
- **Lack of Accountability:** Insufficient accountability measures within banks can foster an environment where fraudulent activities go unchecked.

Changing Consumer Behaviour

- **Increased Vulnerability:** As consumers increasingly rely on online banking services, they become more susceptible to various types of fraud. Many individuals are unaware of the risks associated with online transactions, leading to inadvertent disclosure of sensitive information.

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1.3 Impact of Frauds on Bank's Performance

Fraud not only causes massive financial losses but also leads to severe indirect consequences like regulatory penalties, reputational damage, and increased operational costs. It erodes customer trust, hampers retention, and can even trigger a sharp decline in stock prices for banks failing to manage fraud effectively.

Financial and Reputational impact of frauds on banks can be summarized as below:

Table 1 Financial Impact of Frauds

Aspect	Financial Impact
Direct Losses	Financial losses due to fraudulent activities reduce profitability.
Increased Costs	Higher expenses on fraud detection, prevention systems, and compliance measures.
Capital Adequacy	Fraud losses affect capital buffers, impacting regulatory compliance.
Credit Risks	Fraudulent loans increase non-performing assets (NPAs).

Table II Reputational Impact of Frauds

Aspect	Reputational Impact
Customer Trust	Loss of trust results in customer attrition and reduced deposit inflows.
Brand Value	Negative publicity damages the brand, reducing customer acquisition and retention.
Regulatory Scrutiny	Increased audits and penalties tarnish the bank's image in the industry.
Employee Morale	Fraud scandals lead to decreased employee morale and productivity.

II. METHODOLOGY

The research methodology involves a comprehensive review of existing literature, including reports from the Reserve Bank of India (RBI), Annual Reports of various Banks, National Payments Corporation of India (NPCI), I4C s. The study also analyses recent fraud statistics and trends, focusing on their impact on the banking sector.

III. LITERATURE REVIEW

The literature highlights the growing challenges of fraud in the banking sector amidst rapid digitalization and the adoption of advanced technologies. Mehdipour et al. (2024) emphasize the pervasive nature of banking fraud and its global economic implications. While digital transformation has enhanced banking services, it has also introduced vulnerabilities to scams like phishing and investment fraud. Their mixed-methods research reveals that while users are aware of fraud, few have an in-depth understanding, with prior banking experience playing a key role in evading scams. Institutional gaps in proactive fraud prevention are evident, with limited government and financial sector interventions. The study advocates for enhanced public awareness, collaborative efforts, and legislative reforms to address these challenges effectively.

In exploring technological solutions, several studies highlight the pivotal role of machine learning and artificial intelligence (AI) in fraud detection. Layek (2024) evaluates machine learning models like Random Forest and XGBoost, finding them effective in addressing skewed financial datasets, with specific recommendations tailored to institutional needs. Similarly, Mytnyk et al. (2024) emphasize AI's role in mitigating fraud through advanced techniques like artificial neural networks (ANNs) and stacked generalization, demonstrating their effectiveness in managing imbalanced datasets and improving detection accuracy. Aziz et al. (2023) delve deeper into AI applications, emphasizing its transformative impact on fraud prevention, risk management, and regulatory compliance. AI's real-time anomaly detection, predictive capabilities, and integration with tools like NLP and graph analytics are shown to enhance fraud detection and operational security.

Other studies, such as those by Subudhi and Pursani (2024), Bhasin (2016), and Patel (2023), focus on the interplay between digital transformation and fraud in India's banking sector. Subudhi and Pursani underscore the rise in fraud due to weak internal controls, phishing attacks, and regulatory gaps, advocating for AI/ML adoption, blockchain, and biometric authentication to bolster security. Bhasin highlights managerial lapses and inadequate control mechanisms, recommending stringent audits and legal frameworks. Patel links fraud to rising NPAs and declining profitability, emphasizing the need for regulatory interventions to safeguard financial stability. Bhargavi and Sravanthi (2023)

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further underline the critical role of AI, multi-factor authentication, and fraud detection systems in combating fraud, stressing the importance of combining technological solutions with human vigilance and customer awareness.
Collectively, the literature underscores the multifaceted nature of financial fraud in the digital era, advocating for the integration of advanced technologies, robust policies, and collaborative frameworks to strengthen the resilience of the banking sector.

IV. RESULTS AND DISCUSSION

4.1 The key findings from the secondary data collected from RBI and Bank's annual reports and market research

- **Increase in Fraud Cases:** A total of 36,075 fraud cases were reported in FY 2023-24, marking a 166% increase from 13,564 cases in FY 2022-23. This dramatic rise indicates a shift in the frequency and nature of fraud incidents within the banking sector. Despite the increase in the number of cases, the total amount involved in these frauds decreased by 46.7%, falling to ₹13,930 crore from ₹26,127 crore in FY 2022-23. This suggests a trend towards smaller, more frequent frauds rather than large-scale scams.
- **Increase in Number of Fraud Cases (FY24 vs. First Half of FY25) :** Fraud amounts increased 8 times in the first half of FY25 compared to the same period in FY24, rising from Rs. 2,623 crore to Rs. 21,397 crore.
- **Fraud Case Volume:** In FY24, total fraud cases stood at 36,066, with 14,480 cases reported in the first half.
- In FY25, the first half alone reported 18,461 cases, marking a 27.5% increase from the corresponding period in FY24.
- **Digital Payment Fraud:** The majority of fraud cases are occurring in the realm of digital payments, particularly through cards and internet transactions. This category accounted for about 80% of reported fraud cases, although it represented only 10% of total financial losses. Digital payment frauds, though lower in value, are increasing in frequency due to the rise in online transactions.
- **UPI Fraud:** UPI (Unified Payments Interface) fraud cases surged by 85%, increasing from 7.25 lakh incidents in FY 2022-23 to 13.42 lakh incidents in FY 2023-24, with a total value of approximately ₹1,087 crore.
- **Loan Portfolio Frauds:** Public sector banks reported that frauds primarily concentrated within their loan portfolios. These accounted for a significant portion of financial losses despite fewer cases compared to digital transaction frauds. Loan portfolio frauds dominate the monetary impact, constituting 86.16% of the fraud value in 2023-24.
- **Prevalence of Account Takeover (ATO) Fraud:** ATO frauds account for 55% of all digital banking fraud in India, where unauthorized access to accounts is achieved by exploiting weak authentication protocols.
- **PSB vs. PVB:** Public Sector Banks (PSBs) report higher monetary losses due to loan portfolio frauds, indicating systemic weaknesses in credit monitoring. Private Sector Banks (PVBs) show a significant rise in fraud cases, primarily in digital payments, reflecting growing vulnerabilities in online channels.
- **Emerging Fraud Types:** New forms of fraud, such as synthetic identity fraud and cryptocurrency-related scams, are gaining traction. Traditional methods like phishing, vishing, and malware attacks continue to persist alongside these modern threats.
- **AI-Driven Fraud:** Fraudsters employ sophisticated tools like Fraud-as-a-Service (FaaS), deepfake technology, and automated credential stuffing to exploit system weaknesses.
- **Social Engineering Techniques:** A notable rise in voice scams and phishing exploits human psychology, using fear (e.g., fake account block alerts) or greed (e.g., lottery scams) to deceive victims.
- **Mule Accounts:** Fraud networks increasingly utilize mule accounts to launder stolen funds. Many of these accounts are created through scams, such as fake job offers, and used to obscure fraudulent transactions. A notable trend is the rise of voice scams, which now account for up to 40% of reported fraud cases. This reflects a shift towards social engineering tactics where fraudsters manipulate individuals into providing sensitive information.

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- **Delayed Detected in Fraud Reporting:** Around 90% of the fraud cases reported in FY23 were related to incidents from prior financial years. This delay reflects a lack of efficient real-time fraud detection mechanisms.
- **Impact on Financial Institutions:** The lag in identifying fraud increases the cost of recovery and damages customer trust, leaving financial institutions vulnerable to reputational harm.
- **Fragmented Systems:** Most banks use separate tools for different fraud types (e.g., card fraud, synthetic identity fraud), leading to inefficiencies and gaps in comprehensive fraud detection.
- **Operational Inefficiencies:** Manual processes, disjointed data systems, and outdated workflows amplify the risk of fraud by delaying responses to suspicious activities.
- **Lack of Public Awareness:** Customers' limited understanding of digital risks, such as phishing and malware, makes them easy targets for fraudsters.
- **Inadequate Security Systems:** Legacy systems reliant on text-based one-time passwords (OTPs) are increasingly ineffective against advanced threats. OTPs are vulnerable to interception and social engineering attacks.
- **Underutilization of Advanced Authentication:** While customers trust biometrics, only 32% of businesses adopt behavioural and biometric analytics for fraud detection. This gap limits the potential of more secure and efficient methods. Biometric and Behavioural Authentication strengthens security but requires multi-layered measures to counter spoofing.
- **Data Silos:** Siloed data structures in banks hinder the ability to perform integrated and accurate fraud analysis, affecting overall efficiency.
- **Pressure on Employees**: Unrealistic targets and coercive management practices lead to unethical behaviors and systemic fraud. Employees are often coerced into meeting unrealistic performance targets, leading to practices such as inflating digital metrics or engaging in unauthorized transactions.
- **Unauthorized Transactions:** Many cases involve debiting customer accounts without consent, particularly in relation to government-backed financial schemes.

The stark increase in the number of fraud cases amidst a decrease in total monetary loss suggests that fraudsters are opting for lower-value but higher-volume scams. This shift may be due to increased security measures that make high-value scams riskier and more difficult to execute.

The data indicates a significant lag between when fraud occurs and when it is detected or reported, with nearly 90% of the value of reported frauds originating from incidents that happened in previous financial years. This highlights challenges in timely detection and response mechanisms within banks.

Technologies like AI/ML and blockchain have shown promise in fraud detection, yet their adoption and effectiveness vary across banks.

4.2 Use of Technology for Early Warning of Frauds

The banking sector is increasingly leveraging advanced technologies to stay ahead of fraudsters and safeguard customer assets. These technologies are not only improving the accuracy and efficiency of fraud detection but also helping banks proactively prevent fraudulent activities. The fiscal year 2023-24 witnessed significant advancements in this area, as banks adopted a multi-faceted approach to enhance their fraud management systems.

- ***Artificial Intelligence (AI) and Machine Learning (ML):*** AI and ML have emerged as critical tools in fraud detection, enabling banks to analyze vast amounts of transactional data in real time. These technologies utilize algorithms to identify patterns, predict potential fraud risks, and flag suspicious transactions automatically. Their ability to learn from past fraud incidents allows for continuous improvement in detection accuracy.
- ***Big Data Analytics****:* Big data analytics enables banks to process and analyze massive volumes of structured and unstructured data from various sources, including transaction records, customer profiles, and social media activity. By identifying correlations and anomalies, big data analytics helps detect potential fraud before it escalates.

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- ***Blockchain Technology:*** Blockchain technology is revolutionizing fraud prevention by offering a decentralized and immutable ledger system. Each transaction recorded on a blockchain is secure, transparent, and virtually tamper-proof, making it an effective tool for reducing fraud risks in areas like trade finance, cross-border payments, and document verification.
- ***Biometric Authentication****:* Biometric authentication has become a reliable security measure for preventing unauthorized access to banking systems. Techniques like fingerprint scanning, facial recognition, and voice authentication add an extra layer of security by ensuring that only authorized users can access accounts or perform transactions.
- ***Robotic Process Automation (RPA):*** Robotic Process Automation (RPA) is being increasingly used to streamline fraud detection processes by automating repetitive tasks, such as transaction monitoring and alert generation. RPA helps banks efficiently analyze vast datasets and flag potential fraud cases for further investigation.

Table III Key Technological Tools for EWS (Early Warning Signal)

Tool	Description	Capabilities	Examples/Use Cases
AI and ML Algorithms	Uses predictive modeling to identify patterns and anomalies indicative of fraud.	Real-time analysis, predictive scoring, and adaptive learning.	Detects fraudulent transactions or behavior anomalies.
Data Analytics Tools	Combines structured and unstructured data to generate actionable insights.	Analyzes transaction history, customer behavior, and risk indicators.	Identifies outliers in loan applications or payment gateways.
Blockchain	Ensures secure and immutable transactions, reducing fraud opportunities.	Provides transparent ledgers, smart contracts for risk management.	Prevents document tampering in trade finance and digital lending.
Biometric Solutions	Uses fingerprint, facial recognition, or iris scanning to authenticate users.	Prevents identity fraud, enhances customer verification.	Mitigates fake account creation in KYC processes.

4.3 Common Fraud Prevention Technologies used by Banks

- **Machine Learning and Artificial Intelligence (AI):** These technologies analyse vast amounts of transaction data to identify patterns and detect anomalies that may indicate fraudulent activity. Machine learning models continuously learn from new data, improving their accuracy over time. It is used for real-time transaction monitoring, risk scoring, and predictive analytics to flag potentially fraudulent transactions before they are processed.
- **Behavioural Biometrics:** This technology assesses user behaviour, such as typing patterns, mouse movements, and navigation habits, to authenticate users based on their unique behavioural characteristics. It helps in identifying legitimate users and detecting anomalies that could suggest account takeover or unauthorized access.
- **Multi-Factor Authentication (MFA):** MFA requires users to provide two or more verification factors to access their accounts, such as passwords combined with a one-time code sent to a mobile device. Widely used to enhance security during login processes and transactions, making it more difficult for fraudsters to gain unauthorized access.
- **Real-Time Transaction Monitoring Systems:** These systems monitor transactions as they occur, using predefined rules and machine learning algorithms to identify suspicious activities. Banks implement these systems to flag unusual transactions for further investigation, reducing the likelihood of fraud before it happens.

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- **Fraud Detection Software:** Specialized software solutions designed to detect and prevent various types of fraud, including credit card fraud, identity theft, and loan fraud. Often integrated with existing banking systems to provide comprehensive fraud detection capabilities across multiple channels.
- **Encryption and Tokenization:** Encryption secures sensitive data by converting it into unreadable formats, while tokenization replaces sensitive data with unique identifiers (tokens) that have no exploitable value. Protects customer information during online transactions and storage, reducing the risk of data breaches.
- **Identity Verification Solutions:** Technologies that verify the identity of customers through various means, including document verification (e.g., scanning IDs), facial recognition, and knowledge-based authentication. Used during account opening processes and for high-risk transactions to ensure that the person initiating the action is indeed the legitimate account holder**.**
- **Automated Reporting Tools:** Tools that automate the reporting of suspicious activities and compliance with regulatory requirements related to fraud prevention streamlines the process of documenting and reporting fraud cases to regulators, enhancing compliance while reducing manual workload.
- **Cybersecurity Solutions:** Comprehensive cybersecurity measures, including firewalls, intrusion detection systems (IDS), and anti-malware software protects bank networks from external threats that could facilitate fraud or data breaches.

4.4 Use Cases of Generative AI in Fraud Detection and Prevention

- **Moody's Enhanced Fraud Detection:** It leverages a GenAI assistant to streamline credit analysis and enhance fraud detection. By synthesizing data from live events, credit ratings, and peer group analysis, it reduces data collection time by 80%, analysis time by 50%, and boosts financial analysts' productivity by 27%. This proactive approach identifies potential anomalies and discrepancies, enabling effective fraud prevention.
- **The Citi Compliance Assistant**: It uses GenAI to help compliance teams navigate complex regulations and assess their strategic impact. By analysing extensive documentation, like US Federal capital rules, it identifies risks, ensures regulatory compliance, and reduces the likelihood of fraud or penalties.
- **Mastercard Enhanced Fraud Protection** leverages Generative AI integrated with Decision Intelligence (DI) to improve real-time fraud decisioning. It analyses complex transactional relationships in under 50 milliseconds, achieving a 20% increase in fraud detection rates. By enhancing risk scoring and identifying nuanced fraudulent patterns, it enables faster and more accurate fraud prevention.
- **Visa Enhanced Fraud Protection** uses Generative AI to combat enumeration attacks and reduce operational losses by analysing 182 risk attributes. It delivers risk assessments within 20 milliseconds, reduces false positives by 85%, and enhances fraud detection accuracy for precise attack prevention.
- **Commonwealth Bank's (CommBank) Enhanced Fraud Protection** uses GenAI to analyse over 20 million daily payments, providing real-time alerts for suspicious transactions. This proactive approach has reduced scam-related losses by 50% and customer-reported frauds by 30%, enhancing fraud detection and boosting customer trust.
- **Commerzbank's GenAI Virtual Avatar** revolutionizes mobile banking with a 3D assistant that delivers personalized advice, banking services, and fraud-related support. It performs tasks like blocking cards and transferring funds, enabling swift action against fraud, reducing response times, and enhancing customer satisfaction.

4.5 Recommendations and Suggestions for Addressing Fraud and Operational Challenges in Indian Banking

Technological Advancements for Fraud Detection

- **Adopt AI-Powered Fraud Detection Systems:** Banks should invest in advanced AI and machine learning models to enable real-time monitoring and analysis of transactions. These systems can detect patterns and anomalies more efficiently than traditional methods, significantly reducing false positives and enhancing response times. Expand AI-driven tools for anomaly detection, fraud patterns, and predictive analytics.

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- **Use Behavioural Biometrics:** Incorporate behavioural analytics to detect unusual activities, such as irregular typing seeds or device usage patterns, to flag potential fraud in real-time.
- **Implement Fraud Detection Platforms:** Use integrated platforms that combine geolocation data, device fingerprinting, and transaction history to build a comprehensive fraud detection framework.
- **Utilize Blockchain technology** for tamper-proof recordkeeping in high-value transactions. Blockchain ensures data integrity and eliminates the risk of document forgery, a common issue in trade finance. Scale up blockchain technology to secure transactional data across all bank groups.
- **Leverage Generative AI:** To strengthen fraud detection, banks should adopt scalable GenAI solutions, integrate them with legacy systems for seamless operation, and ensure continuous learning to adapt to emerging fraud patterns. Additionally, leveraging GenAI for customer education and fostering cross-industry collaboration will enhance fraud prevention efforts, improve operational efficiency, and build customer trust.

Create Centralized Data Repositories

Establish or leverage data lakes to consolidate information from siloed systems. Centralized data enables seamless access for fraud investigators, improving efficiency and accuracy in identifying fraudulent activities.

Enhance Authentication Protocols

- **Replace OTPs with Multi-Factor Authentication (MFA):** Transition to MFA that integrates biometrics and behavioural data to mitigate risks from intercepted OTPs and phishing attacks.
- **Use Liveliness Detection:** Deploy technologies that verify the authenticity of biometric inputs to counter spoofing attempts effectively.

Securing Digital Channels:

- Expand the adoption of AI/ML-powered fraud monitoring systems to detect anomalies in digital payments.
- Educate customers on safe banking practices to minimize user-caused frauds.

Operational Efficiency and Governance

Streamline Internal Processes

- Automate redundant tasks such as payment verification and account monitoring. Automation not only improves efficiency but also reduces human errors that can be exploited by fraudsters.

Strengthen Internal Controls

- Implement robust segregation of duties to reduce the risk of insider fraud.
- Conduct regular audits and compliance checks to identify vulnerabilities. Enforce strict monitoring of employee access to sensitive accounts. Flag unusual activities promptly to prevent internal malfeasance. Internal fraud accounts for 10–15% of all banking fraud cases. Regular audits can uncover discrepancies early. A strong system of checks and balances deters collusion and unauthorized activities.

Internal control and organizational culture had a significant positive effect on early warning for fraud in the banking industry.

Adopt Ethical Workplace Practices

Address unrealistic performance targets that force employees into unethical behaviours. Establish a balanced approach to goal setting and reward systems to promote a healthy work environment.

Enhanced Due Diligence:

- Use advanced on boarding mechanisms with robust identity verification to detect synthetic and first-party fraud.
- Integrate fraud detection tools with business decision-making for streamlined operations.

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Regulatory Oversight and Compliance

Regular Audits and Inspections

The bank should conduct periodic and independent audits of banking practices, including digital initiatives and loan disbursement processes. This will ensure compliance with ethical and operational standards.

Centralized Fraud Reporting System

Implement a unified, integrated real-time fraud reporting platform accessible to all banks. Such a system will enhance transparency and enable quick responses to emerging fraud patterns.

Reform Financial Inclusion Policies

Revise guidelines for financial inclusion schemes to include stricter eligibility criteria and enhanced monitoring mechanisms. This will reduce exploitation and minimize non-performing assets (NPAs).

Mandate regular rotation of employees handling sensitive transactions.

Employee Training and Customer Empowerment

Fraud Awareness Training for Employees

Regularly train employees to identify and respond to emerging fraud tactics such as social engineering and synthetic identity fraud. Training should emphasize both technical skills and ethical decision-making. Simulate fraud scenarios and provide case-based learning. Regular training helps staff recognize red flags early, leading to timely interventions.

Public Awareness Campaigns

- Launch nationwide campaigns to educate customers about the risks associated with digital banking, emphasizing cybersecurity best practices like recognizing phishing attempts and safeguarding personal information.
- **Use Simple Messaging:** Leverage social media, print media, and educational workshops to ensure the messages reach diverse demographics effectively.

Grievance Redressal Mechanisms: Establish robust channels for customers to report unauthorized transactions and fraudulent practices. Ensure timely resolution to rebuild trust and enhance customer satisfaction.

Enhanced Fraud Mitigation Strategies

Invest in Fraud Insurance

Utilize fraud loss insurance models to offset financial risks, reduce capital reserve requirements, and encourage the on boarding of higher-risk customer segments like millennial.

Target Mule Accounts

- Deploy AI-powered tools to detect mule accounts, focusing on unusual transaction patterns and VPN usage. Collaborate with law enforcement to dismantle these networks effectively.
- Banks must integrate RBI's MuleHunter.AI platform to combat the rising tide of digital fraud, especially mule accounts used for money laundering. By leveraging its AI and machine learning capabilities, banks can accurately detect illicit fund flows, reducing fraud and enhancing security. For smaller banks, MuleHunter.AI offers crucial infrastructure to safeguard customer trust and improve fraud detection, contributing to a more secure digital payments ecosystem and supporting India's digital economy.

Continuous System Updates

Regularly update fraud detection algorithms to counter emerging tactics, such as deepfake-driven scams and credential stuffing attacks.

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Monitor Transactions and Accounts Proactively

- Set up real-time transaction monitoring systems to flag high-risk transactions. Real-time monitoring can significantly reduce the average fraud detection time, minimizing financial losses.
- Perform regular account reviews for dormant accounts, as these are often exploited by fraudsters and constitutes a major portion of internal fraud cases.

Strengthening Loan Monitoring:

- Implement advanced analytics for risk assessment in loan portfolios to prevent high-value frauds.
- Enhance due diligence for large loans through automated Early Warning Systems (EWS).

Collaboration and Industry Partnerships

Industry-Wide Collaboration

- Foster partnerships with fintech companies, technology providers, fraud detection solution providers and insurance entities to share insights, tools, and best practices to mitigate risks and tackle fraud comprehensively.
- **Global Alignment:** Collaborate with international banking institutions to adopt proven fraud prevention models and tailor them to the Indian context.

Joint Public-Private Initiatives

Partner with government bodies to strengthen regulatory frameworks and provide resources for enhanced fraud detection technologies and customer education initiatives.

Customer-Centric Reforms

Consent-Based Enrolments

Ensure all financial products and schemes are customer-consent-driven, with transparent communication about their features and benefits.

Visual Authentication for High-Value Transactions

Introduce visual cues for transaction confirmations, such as OTPs accompanied by identifiable images or information, to reduce phishing risks.

Dynamic Risk Assessment

Proactive Fraud Prevention Strategies

Implement predictive analytics to anticipate fraud trends and adapt detection systems accordingly. This approach ensures banks remain ahead of evolving threats.

Localized Strategies

Recognize regional fraud patterns and design tailored interventions. For example, areas with high mule account activities can receive focused monitoring and awareness programs.

Reducing Detection Lag:

- Adopt real-time fraud analytics to detect and respond to fraudulent activities promptly.
- Integrate fraud detection systems with external databases for quicker flagging of suspicious transactions.

By integrating these recommendations, Indian banks can create a robust framework that combines technological innovation, operational efficiency, and ethical practices. This holistic approach not only minimizes fraud risks but also builds customer trust, enhances employee morale, and aligns the banking sector with the goals of financial inclusion and digital transformation.

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V. CONCLUSION

Fraud continues to be a critical challenge for the banking sector, directly impacting financial stability, operational efficiency, and customer trust. The surge in fraud cases and amounts during FY25 underscores the urgency of addressing this persistent issue with innovative and effective strategies. A detailed analysis reveals that fraud not only increases financial provisioning but also diverts resources, erodes customer confidence, and strains banks' operational capacities.

Technology emerges as the cornerstone of a robust fraud prevention strategy. Advanced tools such as artificial intelligence, machine learning, and real-time monitoring systems are pivotal in identifying fraudulent patterns and issuing early warnings. These technologies empower banks to act proactively, significantly reducing the window for fraudsters to exploit vulnerabilities. Additionally, fostering a collaborative ecosystem, as envisioned by initiatives like the RBI's Digital Payments Intelligence Platform (DPIP), can ensure seamless data sharing and network-wide intelligence. Such measures, combined with heightened customer awareness and stringent regulatory frameworks, can create a resilient banking environment that effectively mitigates fraud risks while enhancing performance and trust.

APPENDIX

Analysis of secondary data collected from RBI Annual Report and other reports

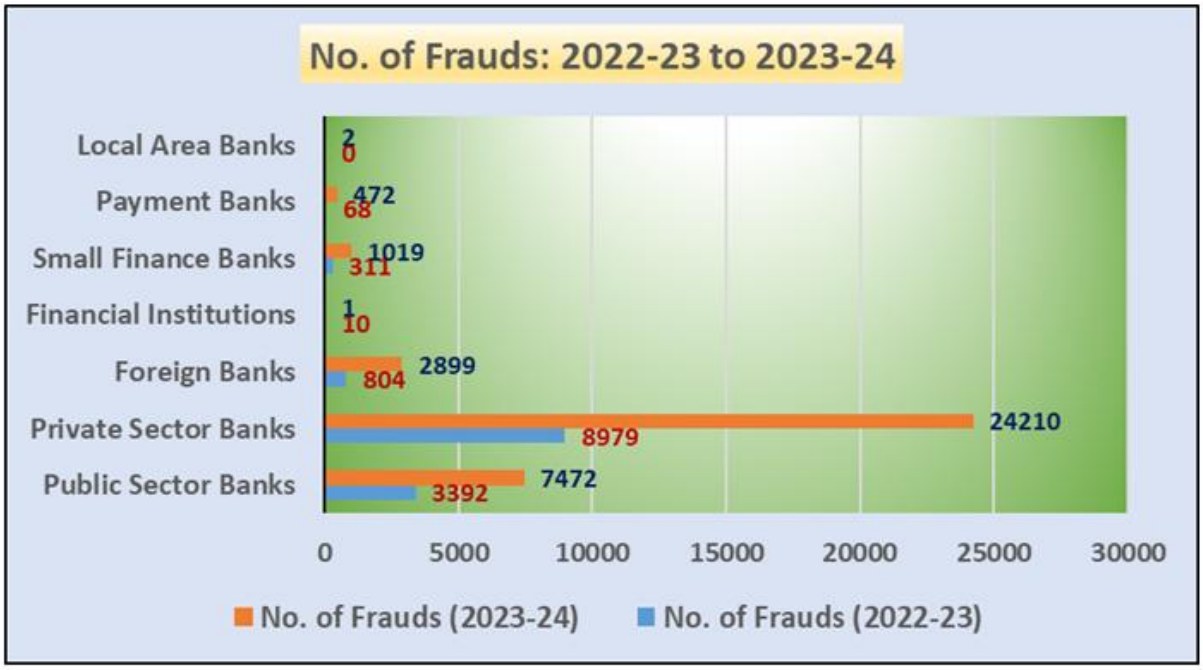

Fig I. Number of Frauds -FY 2023 vs. FY2024 (Source: RBI Annual Report 2023-24)

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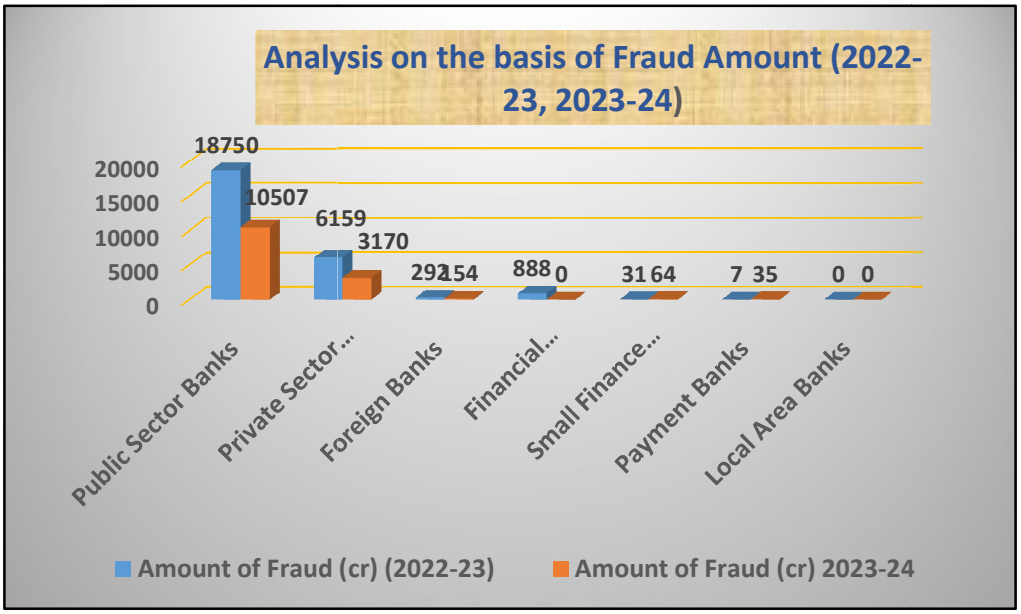

Fig 2. Amount of Frauds -FY 2023 vs. FY 2024 (Source: RBI Annual Report 2023-24)

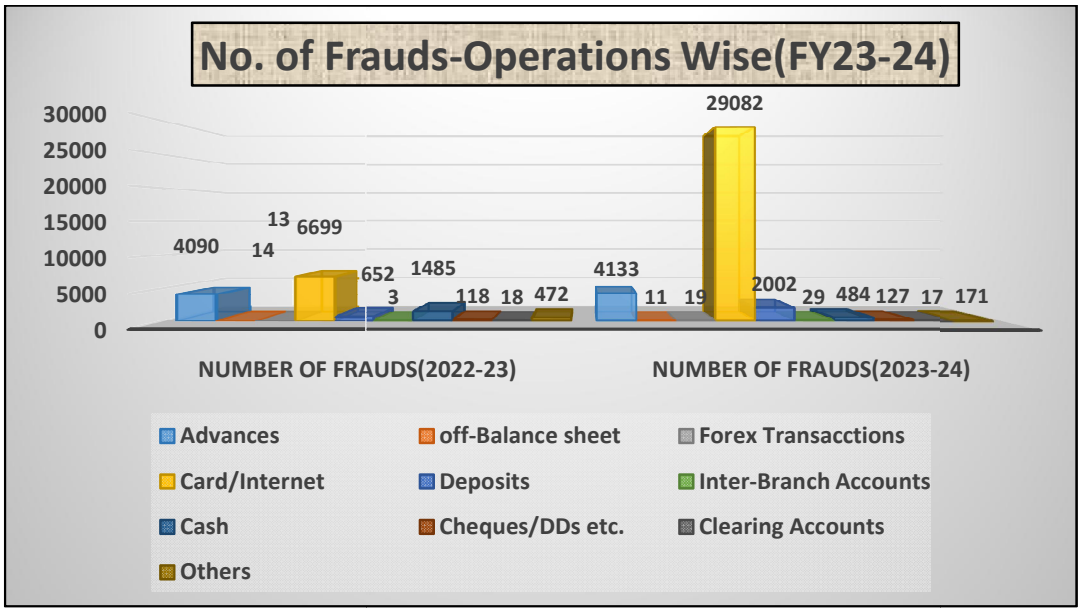

Fig 3. Number of Frauds Operation wise (Source: RBI Annual Report 2023-24)

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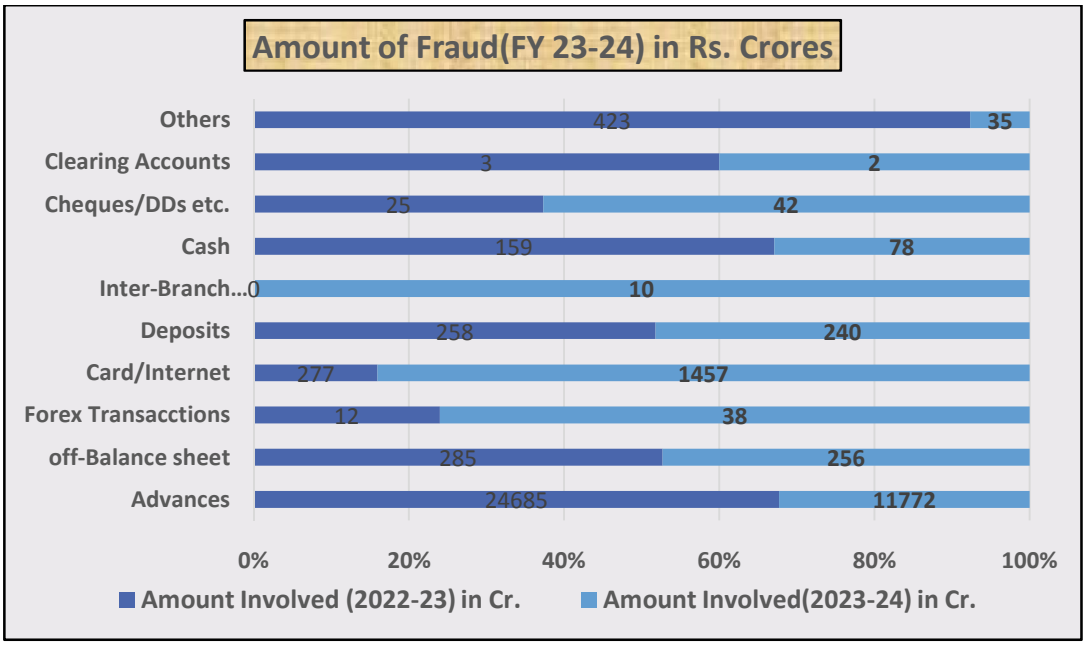

Fig 4. Amount of Frauds Operation wise (Source: RBI Annual Report 2023-24)

Data Interpretation:

- Private Sector Banks reported significantly higher fraud numbers in both years, primarily due to small-value frauds in digital payments.
- Public Sector Banks, while reporting fewer cases, had more high-value frauds in loan portfolios.
- Public Sector Banks accounted for the largest share of fraud amounts, with a significant portion stemming from loan portfolio frauds.
- The fraud amounts in Private Sector Banks remained relatively low but saw a slight increase due to digital payment fraud proliferation.
- Both sectors show a substantial lag between fraud occurrence and detection, highlighting the need for improved early warning systems and fraud detection frameworks.

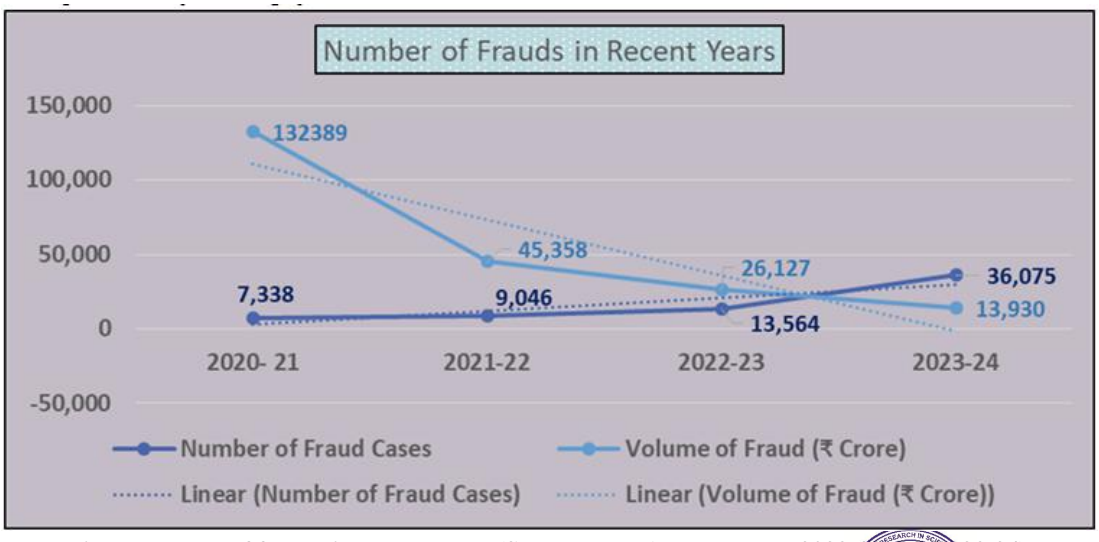

Fig 5. Number of frauds in recent years (Source: RBI Annul Report 2022-23 and 2023-24)

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Data Interpretation: This chart indicates through a trend line that there is a consistent upward trend in the number of fraud cases despite a decline in the total volume involved, suggesting a shift towards smaller but more frequent fraudulent activities.

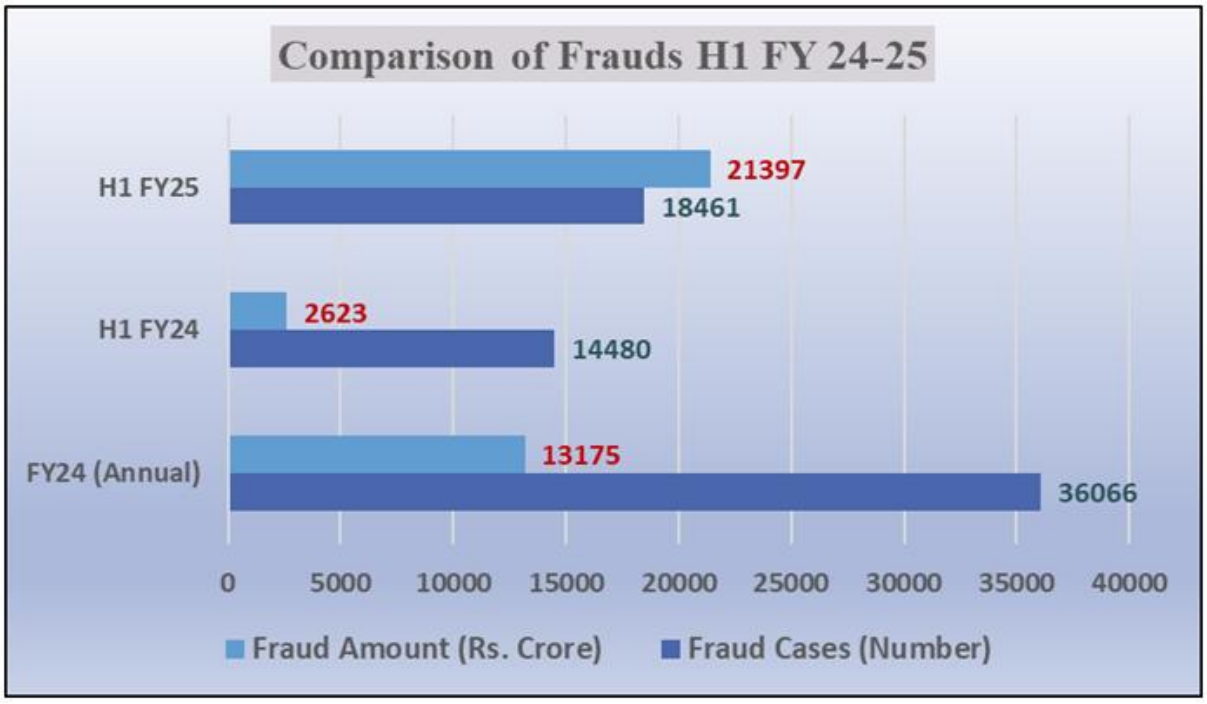

Fig 6. Comparison of Frauds H1 FY 24-25 (Source: RBI Report on Trend and Progress of Banking in India 2023-24)

Data Interpretation:

Increase in Fraud Amounts:

- FY24 vs. FY25: Fraud amounts increased 8 times in the first half of FY25 compared to the same period in FY24, rising from Rs. 2,623 crore to Rs. 21,397 crore.
- Annual Comparison: FY24 reported the lowest fraud amount in a decade at Rs. 13,175 crore, a significant drop from Rs. 23,863 crore in FY23.

Fraud Case Volume:

- In FY24, total fraud cases stood at 36,066, with 14,480 cases reported in the first half.
- In FY25, the first half alone reported 18,461 cases, marking a 27.5% increase from the corresponding period in FY24.

Nature of Frauds:

- Internet and Card Frauds: Accounted for 44.7% of the fraud amount and 85.3% of the total number of cases in FY24.
- Bank Group Analysis: Private sector banks (PVBs) reported 67.1% of fraud cases, while public sector banks (PSBs) had the highest share in fraud amounts.

Sectorial Trends:

- Fraud cases involving cards and internet transactions dominated across all bank groups in FY24.

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