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Research Paper

A Study of Financial Crimes in the Banking Sector of Bangladesh

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Abstract: In recent years, Bangladesh has witnessed significant financial crimes within the banking sector, which pose a serious concern for the country. This research investigates the nature and contributing factors of financial crime in the banking sector, along with its primary causes and consequences. The study adopts a qualitative and descriptive approach to examine the modus operandi and impacts of such crimes. Secondary data have been collected from relevant literature, annual reports of Bangladesh Bank, and reviews of pertinent laws and legal cases. Additionally, this study explores various legal measures that can be implemented to curb financial crime in the banking sector. It also highlights the most critical actions that could be taken to prevent these crimes. The aim is for readers to gain a deeper understanding of financial crime and the mechanisms by which law enforcement addresses such offenses. The researcher has analyzed the nature, causes, effects, and potential preventive measures regarding financial crime in Bangladesh's banking sector.

Keywords: Banking Scandals, Banking Sector, Financial Crime, Legal Reform, Scam.

1. Introduction

With the advancement of communication technology, business operations have become transnational, and large corporations are now regarded as key drivers of the global economy. Corporations, as recognized entities, possess a separate and artificial legal status that confers privileges, rights, and obligations distinct from those of their members. Moreover, with the increasing globalization of financial transactions, financial crime has grown in complexity. Financial crime refers to any conduct by a business that harms institutional actors or society and is subject to sanctions under criminal law [1]. Such illicit activities, often discussed under the umbrella of "white-collar crime," are defined as "violations of criminal law by individuals or members of an upper socioeconomic class in the course of their employment." Unlike white-collar crime, which typically involves individuals of high social status committing offenses in their professional roles, financial crime often involves misconduct where these aspects are secondary considerations.

Major studies on financial crime have been conducted in the fields of criminology, law, and economics. From a criminological perspective, financial crime refers to offenses carried out by corporations, banks, or individuals employed by these institutions. It represents a direct abuse of corporate or financial power. Financial crime has been described as "illegal and harmful acts committed by corporate officers and employees to promote both corporate and personal interests." Some sociologists describe corporate crime as "acts of economic domination" [2]. Financial crime frequently occurs in organizations with a complex hierarchical structure, involving directors, managers, executives, and employees.

The banking sector plays a crucial role in every economy. A transparent, efficient, and responsible banking system is essential for the stability of financial markets and sustainable economic growth. In Bangladesh, financial inclusion programs, rural banking, and microcredit initiatives have been implemented to expand the financial sector. However, the banking industry faces significant challenges due to weak governance, non-performing loans, and regulatory non-compliance. The sector has been plagued by scams, theft, and fraud.

Reports suggest that corruption is a major issue in Bangladesh, exacerbating financial crimes such as consumer fraud, tax evasion, money laundering, stock market manipulation, and falsification of financial statements. These crimes thrive in an environment of widespread corruption, and the public has become increasingly aware of regular stock market manipulation. To date, the Bangladeshi Parliament has enacted only a limited number of scattered laws to regulate financial crimes. As a developing country with insufficient legislation on economic crime, Bangladesh has become a safe haven for both domestic and international financial criminals. Consequently, the problem has grown more complex, and the actual perpetrators often escape legal accountability. Despite numerous instances of financial fraud, Bangladesh still lacks comprehensive legislation and specialized courts or tribunals to address these offenses.

2. Literature Review

This study assesses the impact of internal control on the financial performance of banks in Bangladesh. Key factors such as the banking environment, risk management, information and communication, and control activities were identified through factor analysis. The findings suggest that the monitoring system, as well as the information and communication process, contribute positively to the financial performance of commercial banks, whereas the environment, risk measurement, and control activities show no significant impact. Additionally, the regulatory authorities have limited power in ensuring that commercial banks fully comply with laws and regulations [3].

In the book Fundamentals of Company Law with Law of Partnership, the development of company legislation is traced from its origins in England, through the British Raj in the Subcontinent, the Pakistan period, and post-independent Bangladesh. The book covers key legal concepts such as the memorandum and articles of association, the effects of company registration, and the lifting of the corporate veil. It also discusses the roles of company officers, their decision-making powers, the rights of company members and directors, and the conduct of company meetings. Corporate social responsibility and its legal framework in Bangladesh are also examined [4].

The book Company and Securities Laws offers a comprehensive commentary on the company and securities laws of Bangladesh, analyzing their application, interpretation, and shortcomings with reference to a large body of case law, including cases from the English-speaking world. It focuses on the complexities of these laws and highlights the importance of protecting the rights of all stakeholders, particularly minority shareholders [5].

This research also explores financial irregularities, particularly bank fraud, in Bangladesh. Using a structured Likert-scaled questionnaire, the study identifies various human behaviors, psychological factors, and societal pressures that influence financial misconduct in the country. Factors such as greed, dissatisfaction with personal circumstances, social status, materialism, the pursuit of luxury, and the desire to emulate undesirable behaviors are found to contribute to bank fraud in the Bangladeshi economy. The study highlights that a culture of bad loans and default is prevalent due to the lack of effective enforcement of laws and regulations in the banking sector [6].

Several theoretical perspectives on financial crime emerge from the literature. This paper provides an overview of theories that are relevant for further conceptual and empirical research into financial crime. In particular, it highlights behavioral theories of financial crime, which focus on explaining the individualistic aspects of such offenses [7].

Another study highlights the influence of top management and political pressure on bank lending decisions in Bangladesh. Corruption and dishonesty within Bangladesh Bank have been identified as significant concerns. While proper documentation is required for lending, some banks offer additional incentives or exhibit flexibility. Issues such as lending to unsuitable borrowers, unhealthy competition among banks, fund misappropriation, inadequate audits, and insufficient collateral are detrimental to the banking sector. Furthermore, banks do not always adhere to the regulations and standards set by Bangladesh Bank, which are intended to protect the banking system and promote stable business practices [8].

This literature also outlines the principles and best practices relevant to the commercial sector, financial institutions, state-owned enterprises, and non-governmental organizations. Bangladesh's banking sector has been heavily criticized due to recent financial scandals and loan defaults. As a key indicator of the country's economy, the sector has experienced multiple scams, which have posed significant threats to economic stability. Despite these issues, the rapid expansion of new banks and branches has boosted deposits and credits, contributing to the country's economic growth [9].

3. Methodology

The present research is both analytical and diagnostic in nature. Data were gathered from various secondary sources, including journals, books, newspaper articles, and online resources related to financial crime. A qualitative and descriptive method of analysis has been employed. National statutes and verified news sources were utilized as techniques for secondary data collection. The data were drawn from existing literature on the subject, annual reports of Bangladesh Bank, relevant websites, and a review of statutory and case law pertaining to financial crime in Bangladesh's banking sector. Discussions on conceptual issues are grounded in the secondary literature reviewed.

4. Findings and Discussion

4.1. Findings

The analysis of various cases reveals common patterns through which individuals, groups, or companies embezzle money from banks, committing financial crimes. These methods and their corresponding punishments, as stipulated under current Bangladeshi laws, will be discussed below:

1) *General Causes of Increasing Financial Crime in Bangladesh's Banking Sector*
   a) *Criteria for Choosing Borrowers*
   Some banks fail to properly assess individuals or businesses when selecting borrowers. If the borrower selection process is flawed, the entire financing mechanism can collapse. Banks must choose borrowers who are financially capable of repaying loans. If fraudsters are chosen, the bank will suffer from an increase in non-performing loans, potentially leading to operational failure.
   b) *Influence of Management*
   Managerial influence in the lending process often results in high levels of classified and default loans. Lending decisions are largely controlled by upper management, including the board of directors and senior officials. In some cases, loans are granted despite insufficient documentation or collateral, influenced by management pressure [10].

c) *Lack of Awareness of Bangladesh Bank Circulars*
Bangladesh Bank issues circulars periodically to help commercial banks maintain efficient and safe operations.
However, not all officials are aware of or adhere to these circulars, putting the bank's reputation and stability at risk [11].

d) *Monitoring Borrowers*
Banks primarily earn profits through loans and bonds. Hence, they must carefully monitor clients to ensure they are capable of repaying loans. Monitoring how the loans are used can help prevent fund diversion. Corruption among bank officials contributes to fraud, as they exploit their knowledge of banking regulations to facilitate illegal activities [12].

e) *Fake Mortgages or Insufficient Securities*
Proper evaluation of collateral is essential when loans are issued. In some cases, borrowers create fake properties by colluding with land officials, bank legal advisors, or employees. The audit teams may miss these discrepancies, intentionally or not. One example is the Hallmark case involving Sonali Bank, where non-existent land was used as collateral [13].

f) *Lack of Proper Documentation*
Accurate documentation is crucial in all transactions. If proper documentation is missing, the bank may face difficulties recovering unpaid loans. For example, Basic Bank issued a loan against a fixed deposit, but the borrower withdrew the deposit before repaying the loan, leaving the bank vulnerable.

g) *Inadequate Auditing*
A thorough audit process is critical in detecting fraud. However, audits are often incomplete due to management pressure or bribery. Some banks conduct only one audit per year, despite regulations requiring at least two audits annually.

h) *Cyber Vulnerability*
While banks implement security protocols to prevent cyberattacks, these measures are ineffective if not properly enforced. Employees must be trained to follow procedures, and organizations must remain vigilant to prevent future attacks, as demonstrated by the Bangladesh Bank heist [14].

2) *Effects of Financial Crimes on Bangladesh's Economy*

a) *Shortage of Money*
Financial crimes can lead to a scarcity of funds in the economy, affecting not only the banking sector but also investment, trade, and commerce. Public distrust in banks may cause a withdrawal of funds, exacerbating liquidity shortages.

b) *Collapsed Banking Sector*
Banks rely on deposits from individuals to provide loans. However, following major banking scandals, public trust in banks declines, leading to potential mass withdrawals. This can destabilize the banking system and have negative consequences for the overall economy.

c) *Insufficient Investment*
A lack of confidence in banks affects the broader economy by reducing investment. Scandals, such as the Bangladesh Bank Scam, have a significant impact on GDP growth by discouraging investors.

d) *Increased Dependency on Imports*
Financial instability resulting from bank fraud increases Bangladesh's reliance on imports, negatively affecting the balance of trade [15].

e) *Unemployment*
Reduced investment in the economy leads to higher unemployment. A lack of capital flow due to financial crimes hinders job creation, worsening the unemployment problem.

Financial crime consists of multiple complex steps. The banking sector in Bangladesh has faced significant challenges in mitigating these crimes. Individuals with advanced knowledge and skills often engage in such illegal activities. While it is impossible to completely eradicate financial crime, it can be significantly minimized through the implementation of various initiatives and process controls. Several actions can be taken to substantially reduce financial crimes, as discussed below:

1) *Legal Measures*

The procedures for trials under the Artha Rin Adalat Ain, 2003 are often lengthy and time-consuming. There is no specific provision for the immediate attachment of assets or detention of the accused, allowing them the opportunity to flee without repaying their debts. To address this, the introduction of speedy trials and preventive measures is essential. Financial crimes can be curbed through the empowerment of an independent commission, free from external influence.

The Penal Code of 1860 does not clearly define bribery. Given its age and outdated provisions, it cannot adequately address modern forms of bribery and related financial crimes. With new forms and methods of bribery emerging frequently, the act is no longer sufficient. Bangladesh should collaborate with other nations and establish bilateral agreements to protect national funds. Additionally, the establishment of more monitoring agencies is necessary.

The Companies Act of 1994 governs the formation and operation of companies but lacks clarity on provisions regarding the creation of fraudulent or anonymous companies and their roles. In many cases, individuals obtain loans in the name of anonymous companies. To address this, Bangladesh Bank should issue regulations concerning the age and operations of companies when banks are issuing loans. Furthermore, money laundering laws must be more specific, and new regulatory mechanisms should be introduced by the relevant authorities.

The Bank Companies Act of 1994 does not contain strict provisions to hold bank officials accountable if they are involved in financial crimes. To expedite the judicial process, it is necessary to conduct summary trials for such offenses. An efficient judiciary can significantly reduce financial crime. The enforcement of laws and the proper functioning of the judicial system are critical to controlling corruption. A society free from corruption can be achieved if the courts operate effectively and justly.

2) *Other Measures*

Financial crimes can be reduced by increasing competition within the banking sector. A more competitive private sector can lead to less corruption in the public sector. Enhancing transparency in bank ownership and operations can further strengthen competition. Additionally, the implementation of online banking systems can help reduce corruption. Although Bangladesh is a developing country, it is important to establish an e-banking system, which would enable customers to perform various financial transactions through the bank's website.

Government employees who receive low wages are more prone to engaging in corrupt activities. In Bangladesh, inadequate compensation makes it difficult for individuals to maintain a decent standard of living. Therefore, the government should work to improve salaries, which would help ensure a better quality of life and reduce incentives for corruption.

Proper inspection of securities, mortgages, and documents by the bank authorities is essential. When purchasing banking software, careful attention must be paid to ensure it is certified and rated based on its vulnerabilities. Furthermore, Information Technology (IT) hardware and software should be regularly audited by qualified professionals. This is a critical component of the core risk management guidelines set forth by Bangladesh Bank.

Effective corporate governance is a key element in preventing fraud. A dedicated department for internal control and compliance, equipped with sufficient personnel and resources, is essential. The board must grant this department the authority needed to carry out its duties without interference. If employees are aware of the system's vulnerabilities, they should be able to take action swiftly, before any exploitation occurs. In many cases, senior officials facilitate the disbursement of funds based on fraudulent documents and subsequently halt oversight, which requires stringent monitoring.

4.2. Discussion

The study of recent incidents of financial crime in Bangladesh reveals the significant impact that both economic and technological advancements in developed and developing nations have had on the rise of financial crime. As previously mentioned, globalization has played a substantial role in shaping the nature of commercial fraud across the globe. As an emerging economic hub in Asia, Bangladesh has experienced numerous instances of financial crimes. Notable examples include the Bangladesh Bank heist, the misappropriation of funds in Sonali Bank's trust fund, the Hallmark Ltd scandal, and the scams involving P.K. Halder, BASIC Bank, and Crescent Group.

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1) Case Study 1: The PK Halder Scam (2009-2019)

Prashant Kumar Halder, commonly known as PK Halder, is a prominent figure in one of the largest financial scams in Bangladesh. Authorities first became aware of his fraudulent activities in early 2020, and by the end of 2019, he had already fled the country. Initially, Halder was suspected of embezzling BDT 3,500 crore, but the Anti-Corruption Commission (ACC) later expanded its investigation to cover BDT 11,000 crore. On January 8, 2020, the ACC officially accused Halder of illegally acquiring and laundering over Tk 275 crore.

PK Halder orchestrated his schemes primarily through various Non-Bank Financial Institutions (NBFIs) and numerous shell companies. By exploiting these entities, he siphoned off BDT 3,500 crore from Bangladesh's financial sector. NBFIs, according to Bangladesh's banking regulations, are permitted to engage in certain banking activities without functioning as full-fledged banks.

According to a Prothom Alo source, PK Halder established multiple dummy companies to execute his fraudulent activities. Before fleeing with the stolen funds, he had planned to transfer the money to India. Halder crossed into India via the Benapole border, as confirmed by immigration authorities. The Indian federal intelligence agency revealed that PK Halder and his associates held 88 bank accounts across India, including in West Bengal, with combined assets worth BDT 300 crore. PK Halder alone holds more than BDT 60 crore in cash across his 44 bank accounts.

A formal request has been submitted to India for PK Halder's extradition to Bangladesh. However, due to violations of laws in both India and Bangladesh, it is likely that Halder will face trial in India before being returned to Bangladesh. To date, the ACC has filed 36 cases related to PK Halder's scam, implicating 83 individuals, including Halder. Among these, 11 individuals have provided confessional statements in court, and 13 have been detained. In one of the 36 cases, the ACC has already submitted a charge sheet to the court.

2) Case Study 2: The Hallmark Group Scam (2010-2012)

The Hallmark Group orchestrated one of the largest debt scandals in the history of Bangladesh's banking sector. Between 2010 and 2012, the company embezzled BDT 2,731 crore from the Ruposhi Bangla Hotel branch of the state-owned Sonali Bank. According to Sonali Bank's audit and inspection report, Hallmark Group utilized 42 different companies to withdraw the entire sum from the bank. In addition, several other companies adopted similar methods to embezzle a total of BDT 3,550 crore from the same branch.

Upon being assigned to investigate the scandal, the Bangladesh Anti-Corruption Commission (ACC) filed a total of 38 cases against the Hallmark Group, as well as various officials and employees of Sonali Bank. Hallmark exploited the bank's Letter of Credit (LC) system, a financial instrument that guarantees payment to the seller by the bank on behalf of the buyer in large local transactions, such as import-export trade. Tanvir Mahmood, along with his associates and the assistance of corrupt bankers and bank managers, executed the embezzlement. Sonali Bank's audit and inspection report revealed that Hallmark used 42 companies to withdraw funds, many of which were initially identified as fraudulent. However, an investigation by Bangladesh Bank uncovered the existence of 84 such institutions, with approximately 20 confirmed to be fake.

To date, the ACC has filed 37 cases related to the Hallmark Group loan scandal. The accused include Hallmark Group chairman Jasmine Islam, Tanvir Mahmood, and former Sonali Bank General Manager Humayun Kabir. Additionally, 20 other bank officials and several relatives of Tanvir Mahmood have also been implicated. These cases are currently pending in court.

3) Case Study 3: The BASIC Bank Scam (2009-2013)

Between 2009 and 2013, Tk 4,500 crore was misappropriated from BASIC Bank through fraudulent loans, marking one of the largest loan scandals in Bangladesh's history. Although the Anti-Corruption Commission (ACC) filed 61 cases in connection with the scam, former chairman of BASIC Bank Sheikh Abdul Hye Bachchu and the bank's board of directors were not named as defendants in the cases.

In 2015, the ACC filed 56 additional cases related to the loan fraud, yet neither Bachchu nor any board members were included among the accused. The ACC informed the High Court that approximately Tk 3,100 crore out of the Tk 4,500 crore involved in the scam had been recovered and deposited into the government treasury.

4) Case Study 4: The Crescent Group Scam (2017-2018)

Crescent Group, in collaboration with certain employees of the Imamganj branch of Janata Bank in Dhaka, allegedly laundered Tk 1,297.65 crore abroad using 657 falsified export bills, as reported by Customs Intelligence. Additionally, the Anti-Corruption Commission (ACC) uncovered evidence that the Group misappropriated Tk 1,303.69 crore from the same bank branch, based on an ongoing ACC investigation. These findings followed a Bangladesh Bank audit from the previous year, which indicated that Crescent Group had "skimmed" at least Tk 765 crore in export funds from both Janata Bank and Bangladesh Bank between January 2017 and February 2018.

Crescent Group had borrowed a total of Tk 3,443 crore from Janata Bank. When the company defaulted on its loan, the state-owned bank was forced to hold an auction in an attempt to recover the lost funds. According to Customs Intelligence, 15 officials from Janata Bank and Crescent Group were implicated, while the ACC identified 17 officials as being involved in the scam.

5) Case Study 5: The Bangladesh Bank Cyber Heist (2016)

The "Bangladesh Bank Cyber Heist" of 2016 is regarded as one of the most significant bank robberies in history. The perpetrators initially aimed to steal $1 billion but ultimately managed to abscond with $81 million, making it one of the largest bank heists in modern times. Interestingly, after the heist, Bangladesh Bank initially hired a U.S.-based IT company to erase evidence of the incident, rather than immediately focusing on recovering the stolen funds.

The Criminal Investigation Department (CID) identified 40 individuals from six different countries as active participants in the theft. The international media first covered the incident when Bangladesh Bank filed a complaint in a Philippine court seeking restitution of the stolen money, after domestic media outlets became aware of the heist.

Like many other central banks, Bangladesh Bank holds an account at the Federal Reserve Bank of New York in the United States. This account is typically used to store reserve currency for the purpose of international transactions and enhanced security. The global financial network processes an average of 35 million transactions daily, with Bangladesh Bank using an 8- or 11-digit SWIFT code for all transactions. While SWIFT facilitates the transmission of payment orders rather than the actual transfer of funds, a group of hackers managed to compromise this highly secure system in 2016.

6) Case Study 6: The Islami Bank Bangladesh Ltd. Scam (2022–Present)

A criminal group embezzled Tk 20 billion from Islami Bank Bangladesh Limited (IBBL) by using two non-existent organizations. This fraudulent group withdrew over Tk 70 billion using various methods and the names of eight fictitious companies. An alarming Tk 24.9 billion of the total was withdrawn in just the first 17 days of November 2022, prompting bank officials to refer to the period as "Nasty November."

In addition to IBBL, these entities also withdrew Tk 23.2 billion from First Security Islami Bank and Social Islami Bank Limited. The total loans granted to these businesses by the three banks amount to Tk 95 billion, including interest. This withdrawal occurred during a period of liquidity crisis in the banking sector, exacerbated by a dollar shortage. These details were uncovered through documentation from the three banks involved.

The loans were issued under the Murabaha TR (Trust Receipt) facility, which typically requires records of the purchase of imported goods. However, bank officials reported that none of the three banks possessed records of any product purchases, raising serious concerns about the legitimacy of the transactions.

5. Conclusion

Bangladesh, as a developing country with a low per capita GDP, faces challenges typical of many developing nations, such as overcrowding, poverty, hunger, illiteracy, and limited resources. Additionally, the country grapples with an unstable economy, political instability, and corruption across various levels of society and government. The banking sector in Bangladesh is growing and plays a crucial role in the country's economic development. However, when financial crimes occur within the banking sector, the economy suffers significantly.

Financial crimes within the banking industry may benefit a select few, but they inflict harm on the majority of people and undermine the country's economic progress. These crimes also reduce international investment, further damaging the economy. Therefore, comprehensive efforts must be made to combat corruption not only in the financial sector but throughout the entire government system.

The causes of financial crimes are as varied as the crimes themselves. However, the pervasive culture of nepotism and corruption is at the root of the problem. A cultural shift is urgently needed. The government must adopt a coordinated and well-understood approach to minimize the misuse of public office. While laws exist to regulate financial crimes, they are often outdated and insufficient to address current challenges. Additionally, civil society must be made more aware of these issues. Reducing financial crimes, both in the banking sector and other industries, requires the enforcement of laws and the promotion of social awareness.

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Documents that form an essential part of the legislation and regulatory framework governing various aspects of legal, financial, and technological activities in Bangladesh:

- Anti-Corruption Commission Act, 2004 (Act No. V of 2004): This is a statute that established the Anti-Corruption Commission in Bangladesh to combat corruption and enforce anti-corruption measures.
- Artha Rin Adalat Ain, 2003 (Act No. VIII of 2003): Also known as the Artha Rin Adalat Act, this statute pertains to the recovery of debts and financial disputes, particularly related to loans and financial transactions.
- Bangladesh Bank Order, 1972 (President's Order No. 127 of 1972): This is a presidential order that established the Bangladesh Bank, the central bank of Bangladesh, and outlines its functions and powers.
- Bank Deposit Insurance Act, 2000 (Act No. VVIII of 2000): This act provides for the insurance of bank deposits to protect depositors in the event of a bank failure.
- Digital Security Act, 2018 (Act No. XLVI of 2018): This statute addresses issues related to digital security, cybercrime, and the protection of information technology infrastructure.
- Financial Reporting Act, 2015 (Act No. XVI of 2015): This act mandates financial reporting standards for organizations to ensure transparency and accountability in financial reporting.
- Foreign Exchange Regulations Act, 1947 (Act No. VII of 1947): This act regulates foreign exchange transactions and controls the movement of currency in and out of the country.
- Money Laundering Prevention Act, 2012 (Act No. V of 2012): This act aims to prevent and combat money laundering activities, providing measures to detect and prosecute such crimes.
- Penal Code, 1860 (Act No. XLV of 1860): This is a comprehensive criminal code that defines various offenses and prescribes punishments for them in Bangladesh.
- The Anti-Corruption Commission Rules, 2007: These rules provide detailed procedures and guidelines for the operation of the Anti-Corruption Commission established under the Anti-Corruption Commission Act.
- The Banking Companies Act, 1991 (Act No. XIV of 1991): This act regulates banking companies, including their operations, management, and financial practices.
- The Bankers' Book Evidence Act, 1891 (Act No. XVIII of 1891): This act provides rules regarding the admissibility of bank records as evidence in legal proceedings.
- The Information and Communication Technology Act, 2006 (Act No. XXXIX of 2006): This act covers legal issues related to information technology and electronic communications.
- The Negotiable Instruments Act, 1881 (Act No. XXVI of 1881): This act regulates negotiable instruments such as promissory notes, bills of exchange, and cheques, outlining their usage and enforcement.