Chapter 12
Fraud Risk Management in Banks:
An Overview of Failures and Best Practices

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ABSTRACT

White collar crimes refer to the criminal activities by a professional holding a responsible position in the organization. Banking frauds are one of the most pronounced forms of white collar crimes. These frauds impact the reputation of the bank and also effects its financial sustainability. The chapter entails the frauds that happen in banks and identifies reasons for the failure of banks to prevent such frauds. The author pinpoints the best practices in developing fraud prevention frameworks and emphasizes the importance of corporate governance in preventing such frauds. Best practices and future trends are also identified that are important to prevent and detect banking frauds.

INTRODUCTION

White Collar Crimes refers to criminal activities involving a professional holding a responsible position in the organization (Strader, 2011). Most of these crimes involve experts who have been given fair autonomy to make decisions, which may impact the reputation risk of the entity whom the professional represents. Essentially

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these events do not cause physical harm to anyone, however, it may lead to material economic losses to the affected party. In the case of banks, there is also a risk of the economy being impacted by these crimes.

Most of the white-collar crimes take time to be unearthed and proved because they involve professionals who yield enormous power within the organization where they commit the crime. They are also aware of the weakness and loophole in the risk management system and they exploit it to the best of their abilities. This generally creates a fear in the minds of the victims and tarnishes the reputation of the organization. The tarnished image may then materialize into the business loss. White Collar Crimes are committed by people who are involved in otherwise, lawful businesses and covers a wide range of activities. (Sutherland, 1983).

The perpetrators hold respectable positions in the communities unless their crime is discovered. The laws relating to white-collar crimes depends upon the exact nature of the crime committed.

Following are the different category of white-collar crimes:

Fraud by Employees

It refers to the process of circumventing the risk management mechanism in a business organization to profit from it. This is generally tantamount to breach of trust and due to opaqueness in the functioning of banks, it is difficult to detect them before some material harm has already been done.

Blackmail

Blackmail means demand for money by threatening some person to cause physical injury or exposing his secrets. In the banks, there are very few instances of such frauds. Hence, this kind of fraud is outside the scope of the book.

Bribery

It is the process of offering money to influence the judgment of the professional holding discretionary power in the organization. This leads to partisan behaviour and unduly influences the decision- making process and hence is categorized as a crime. Such crimes are typically a function of the culture existing in the organisation. Over the years, an increase in the level of automation has increased transparency and hence reduced instances of bribery.

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