



## Avanti Microfinance Private Limited

# Fraud Risk Management Policy

This document was:

Version	Drafted by	Reviewed by	Board approval and adoption date
Version 1	Mr. Manish Thakkar, Director	Mr. Nagaraj Subrahmanya, Director	August 14, 2023
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## **1. Purpose and Scope**

This Fraud Risk Management Policy (“Policy”) aims at safeguarding the Company’s resources, business and customers from the unethical activities of fraudsters through effective fraud risk management, institute a robust internal audit and control framework and define measures to create awareness of fraud risk across the organization.

The Policy is applicable to all employees of Avanti Microfinance Private Limited (“Company”) at all levels of management. It is also applicable to personnel associated with the Company such as partners, contract employees, interns, consultants etc. This Policy shall be read in conjunction with the Risk Management policy and the Code of Conduct.

## **2. Objectives of Policy**

- i. Assign roles and responsibilities with respect to combating fraud.
- ii. Define measures and controls for prevention, early detection, investigation, monitoring, recovery and timely reporting of incidents of fraud to RBI and Law Enforcement Agencies (LEA).
- iii. Create awareness of fraud risk among employees, partners and others associated with the Company.
- iv. Authorise the audit department to conduct surprise audits at all entities associated with the Company to enable the prevention or detection of fraud.

## **3. Definition of Fraud**

Fraud may be defined as an act or omission that is intended to cause wrongful gain to one person and/or wrongful loss to the other, either by way of concealment of facts or otherwise. The Company also defines fraud as “deliberate abuse of procedures, systems, assets, products and/or services of the Company by those who intend to deceitfully or unlawfully benefit themselves or others”.

Internal fraud involves acts intended to defraud, misappropriate property or circumvent regulations, the law or Company's policy in the events which involve at least one person internal to the Company or temporary workers, third-party contractors, interns and consultants associated with the company

External fraud involves acts intended to defraud, misappropriate property or circumvent the law, by a third party and thereby causing or intending to cause losses to the Company. External fraud with regard to systems, assets, products, fraudulent financial reporting e.g. improper revenue recognition, overstatement of assets or understatement of liabilities, services to the detriment of the Company committed by borrowers, potential clients, third parties including vendor(s) or Partner(s).

## **4. Categorisation of Fraud for reporting**

The Company shall use the categorization of RBI for classifying fraudulent activities::

- (i) Fraudulent encashment through forged instruments;
- (ii) Manipulation of books of accounts or through fictitious accounts, and conversion of property;
- (iii) Cheating by concealment of facts with the intention to deceive any person and Misappropriation of funds and criminal breach of trust;
- (iv) cheating by impersonation;

- (v) Forgery with the intention to commit fraud by making any false documents/electronic records;
- (vi) Wilful falsification, destruction, alteration, mutilation of any book, electronic record, paper, writing, valuable security or account with intent to defraud;
- (vii) Fraudulent credit facilities extended for illegal gratification;
- (viii) Cash shortages on account of frauds;
- (ix) Fraudulent transactions involving foreign exchange;
- (x) Fraudulent electronic banking / digital payment related transactions committed on NBFCs.
- (xi) Any other type of fraud not coming under the specific heads as above.

## **5. Fraud Risk Management Life cycle:**

### **5.1 Fraud prevention and standards:**

Risk management will be responsible towards prevention, early detection, investigation, staff accountability, monitoring, recovering and reporting of frauds occurring across the Company.

The Company will undertake various measures for prevention of frauds including:

1. Management supervision for the compliance of risk governance and reporting;
2. Periodic training of employees and associated entities on fraud risk awareness for identifying potential fraud areas;
3. Strictly adhering to the due diligence for borrower accounts;
4. Introducing organization controls like:
  - a) Segregation of duties;
  - b) Maker checker principles;
  - c) Two factor authentication.;
5. Using standardized and transparent processes;
6. Periodic reconciliation of books and transactions;
7. Access control to data and IT systems;
8. Using historical experience as case studies for future;
9. Strict adherence to KYC norms while customer onboarding;
10. Regularly referring to the caution list(s) such as Cibil, Equifax, Highmark at the time of sanction of loans;
11. Partner monitoring and Internal audit work at periodic intervals.

### **5.2 Fraud detection Sources**

#### **Detection of frauds are done through:**

- (i) Early Warning Signals ("EWS"): An Early Warning System (EWS) for Fraud Risk Management is a proactive approach that helps detect, prevent, and mitigate potential fraudulent activities before they cause significant harm.  
The EWS system will have 3 major components
  - a) Data collection: Data is collected from various sources such as transactional data (Payments, Transfers, Refunds), user behaviour (Login patterns, Geolocation, IP) and External Data (Watchlists, Blacklists, Sanctioned Entities, Bureau) etc
  - b) User Profiling and Portfolio monitoring: Risk triggers such as EMI bounces, early defaults, customer non-contactability and other instances of deviations from normal patterns.

- c) Triggers and Alerts: Platform triggers for unusual activities such as large or frequent transactions, multiple failed login attempts etc
- (ii) Complaints from customers.
- (iii) Internal audit and partner monitoring reports.
- (iv) Whistle blower complaints
- (v) Anonymous/pseudonymous complaints with verifiable facts.

### **5.3 Investigation of Fraudulent Activities**

In case where there is a suspicion / indication of wrongdoing or fraudulent activity, the company shall use the internal audit team for further investigation in such accounts. In cases where the Company intends to appoint an external auditor for conducting the investigation approval will be sought from the Board.

In cases where Law Enforcement Agencies (LEAs) have suo moto initiated investigation involving a borrower account, the Company shall initiate investigation and follow the process of classification of account as fraud as per this Policy.

### **5.4 Classification of frauds:**

In the event of a fraudulent activity, the Company shall:

- (i) issue a detailed Show Cause Notice ("SCN") to the persons, entities and its promoters / whole-time and executive directors against whom allegation of fraud is being examined. The SCN shall provide complete details of transactions / actions / events basis which declaration and reporting of a fraud is being contemplated.
- (ii) provide 21 days to the persons / entities on whom the SCN was served to respond to the said SCN.
- (iii) examine the responses minutely and without any prejudice made by persons / entities prior to declaring such persons / entities as fraudulent.
- (iv) issue well-reasoned order(s) ("Order") regarding declaration / classification of the account as fraud or otherwise which shall contain relevant facts and/or circumstances relied upon by the Company.

### **5.5 Staff Accountability**

The Company shall initiate and complete the examination of staff accountability in all fraud cases in a time-bound manner, the process for which is as set out in the Code of conduct.

### **5.6 Recovery of losses arising from fraud:**

The Company shall explore avenues for recovery of losses on account of fraud, these could include:

- (i) Ensuring enforcement of available security;
- (ii) Filing of police complaints/FIRs wherever the frauds are established;
- (iii) Filing civil suits against the fraudsters;
- (iv) Recovery of amount from fraudster.

## **6. Special Committee for Monitoring and Follow-up cases of Fraud / Committee of the Executives:**

As the Company is a middle-layer NBFC as per the regulation, a Committee of the Executives (CoE) will be formed with a minimum of three members, at least one of whom shall be a Whole-

time director or equivalent rank Official for the purpose of performing the roles and responsibilities of Special Committee for Monitoring and Follow-up cases of Fraud.

The roles and responsibilities of CoE are as set out below:

- (i) CoE shall oversee the effectiveness of the fraud risk management in the Company.
- (ii) CoE shall review and monitor cases of frauds, including root cause analysis, and suggest mitigating measures for strengthening the internal controls, risk management framework and minimising the incidence of frauds. The review may include, among others, categories/trends of frauds, industry/sectoral/ geographical concentration of frauds, delay in detection/classification of frauds and delay in examination/conclusion of staff accountability, etc.

The CoE shall meet as and when deemed necessary with atleast 1 meeting in every quarter of the financial year. Taking into account the scale and complexity of operations of the Company, the threshold amount of fraud cases to be placed before CoE shall be:

- I. INR 25,000 for individual perpetrator
- II. INR 50,000 for frauds by loan service providers/entities

## 7. Responsibilities of Senior Management

The Senior Management of the Company is responsible for implementation of this Policy. A periodic review of incidents of fraud is placed before Board of the Company, on a quarterly basis, by the Senior Management of the Company.

## 8. Guidelines on submission of returns and reporting

### **Reporting of Frauds to Law Enforcement Agencies (LEAs):**

The Company will:

- (a) immediately report the incidents of fraud to appropriate LEAs involving an amount of ₹1 lakh or more, subject to applicable laws and/or offences listed under Section 33 of Bharatiya Nagarik Suraksha Sanhita, 2023 (BNSS). The CoE will however have the authority to report incidents under ₹1 lakh, depending on nature of the case.
- (b) establish suitable nodal point(s) / designate officer(s) for reporting incidents of fraud to LEAs and for proper coordination to meet the requirements of the LEA.

### **Reporting of Frauds to the Reserve Bank of India**

- I. The Company shall report incidents of fraud to RBI through Fraud Monitoring Returns (FMRs) using online portal under the heads as specified in Clause 4 above. For the purpose of reporting under FMR:
  - o The 'date of occurrence' is the date when the actual misappropriation of funds has started taking place, or the event occurred, as evidenced/reported in the audit or other findings.
  - o The 'date of detection' to be reported in FMR is the actual date when the fraud came to light in the concerned branch/audit/department.
  - o The 'date of classification' is the date when due approval from the Committee of Executives (CoE) has been obtained for such a classification, and the reasoned

order is passed.

- II. The Company shall furnish FMR in individual fraud cases, irrespective of the amount involved, immediately but not later than 14 days from the date of classification of an incident/account as fraud.
- III. The Company report frauds perpetrated in its group entities to RBI separately through email, if such entities are not regulated/supervised by any financial sector regulatory/supervisory authority. However, in the case of overseas financial group entity of the Company, the Company shall also report incidents of fraud to RBI. The group entities will have to comply with the principles of natural justice before declaration of fraud.
- IV. The Company shall adhere to the timeframe prescribed in the Master Directions for reporting of fraud cases to RBI.
- V. The Company shall examine and fix staff accountability for delays in identification of fraud cases and in reporting to RBI.
- VI. While reporting frauds, the Company shall not report names of persons / entities who / which are not involved / associated with the fraud in the FMR.
- VII. The Company may, only under exceptional circumstances, withdraw FMR / remove name(s) of perpetrator(s) from FMR by providing a due justification to RBI and with the approval of a senior official (at least in the rank of a Director).

#### **9. Post classification and reporting as fraud:**

- Persons / Entities classified and reported as fraud by Applicable NBFCs and also Entities and Persons associated with such Entities, shall be debarred from raising of funds and / or seeking additional credit facilities from financial entities regulated by RBI, for a period of five years from the date of full repayment of the defrauded amount / settlement amount agreed upon in case of a compromise settlement.
- Lending to such Persons / Entities being commercial decisions, the lending Applicable NBFCs shall have the sole discretion to entertain or decline such requests for credit facilities after the expiry of the above mandatory cooling period as mentioned above.
- If an entity classified as fraud undergoes resolution under IBC or other resolution framework, resulting in change in management and control, re-examination of the fraud should be done. However, this would be without prejudice to continuance of criminal action against erstwhile officials detailed in the circular. Penal measures not applicable after implementation of resolution plan.
- In case an account is identified as a fraud by the Company, the borrowing accounts of other group companies (with the Company), in which one or more promoter(s)/ whole-time director(s) are common, shall also be subjected to examination concerned from fraud angle.

#### **Closure of Fraud Cases Reported to RBI**

The Company shall close fraud cases using 'Closure Module' of RBI's CIMS portal where the actions as stated below are complete:

1. The fraud cases pending with LEAs / Court are disposed of; and
2. The examination of staff accountability has been completed.

The Company may, for limited statistical / reporting purposes, close those reported fraud cases involving amount upto ₹25 lakh, where examination of staff accountability and disciplinary action, if any, has been taken and:

1. The investigation is going on or charge-sheet has not been filed in the Court by LEA

for more than three years from the date of registration of First Information Report (FIR); or

2. The charge-sheet is filed by the LEAs in trial court and the trial in the court has not commenced or is pending before the court for more than three years from the date of registration of FIR.

In all closure cases of reported frauds, the Company shall maintain details of such cases for examination by auditors.

In cases where withdrawal of FMR / removal of name(s) of perpetrator(s) is necessitated due to Court directions, the Company may arrange to withdraw FMR / remove name(s) of perpetrator(s) immediately. Such cases shall subsequently be placed before the Board.

#### **10. Legal Audit of Title Documents in cases of Large Value Loan Accounts Fraud accounting**

The Company shall conduct periodic legal audits of title deeds and other related title documents in respect of all credit facilities of ₹1 crore and above.

#### **11. Reporting Cases of Theft, Burglary, Dacoity and Robbery**

- i. The Company shall report instances of theft, burglary, dacoity and robbery (including attempted cases), to Fraud Monitoring Group (FMG), Department of Supervision, Central Office, Reserve Bank of India, immediately (not later than seven days) from their occurrence.
- ii. The Company shall also submit a quarterly Return (RBR) on theft, burglary, dacoity and robbery to RBI using online portal, covering all such cases during the quarter. This shall be submitted within 15 days from the end of the quarter to which it relates.

#### **12. Regulatory Reference**

Master Direction- Reserve Bank of India (Non-Banking Financial Company- Scale Based Regulation) Directions, 2023 along with Master Directions on Fraud Risk Management in Non-Banking Financial Companies (NBFCs) - 2024.

#### **13. Policy Review and Updates**

The Policy and its implementation of this Policy shall be monitored and reviewed annually by the Board of the Company.

This Policy comes into effect from date of Board Approval.