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Citi Case: A Setback for Foreign Banks in India

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NEW DELHI—For years, foreign banks have been trying to gain greater access to India's vast financial services market, but a scandal at a Citibank branch near New Delhi threatens to complicate those efforts, banking experts say.

Police in Gurgaon, a high-technology hub southwest of the capital, are investigating a case in which an employee at the branch allegedly colluded with others to siphon off an estimated \$67.2 million from wealth-management customers. The alleged scam included making false promises on investment returns and forging government documents.



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Excel Media/Splash News

Citibank employee Shivraj Puri was arrested last month in connection with an investment scam in India.

Police arrested the relationship manager, Shivraj Puri, last month and on Jan. 2 arrested an executive at New Delhi-based Hero Group, a conglomerate that is a large stakeholder in India's biggest motorcycle maker. The Hero executive allegedly received commissions for helping direct money from his firm into the scheme.

On Wednesday, Hero Group said it put two other employees on leave while it investigates whether they were involved. In a statement, Hero Group said it will take "further appropriate action" once it completes its inquiry.

Mr. Puri has made no public statement since his arrest; his lawyer couldn't be reached.

Analysts of India's financial-services sector said the alleged fraud at Citibank could have happened at any bank. Citigroup Inc., Citibank's parent, has firmly defended its internal controls. The bank said in a statement Tuesday that it detected the fraud in its branch and initiated the case against Mr. Puri with police.

Police said Wednesday that they won't pursue a case against top Citigroup executives, including Chief Executive Officer Vikram Pandit.

Still, the timing of the episode, coming just as regulators are reviewing whether to allow foreign banks to increase their presence in India, could increase regulatory scrutiny and upset their expansion efforts, executives say.

"Regulators could rightfully say, 'Show us that you're able to manage your existing network of branches in a prudent and effective manner before we let you expand,'" said Arun Duggal, the former chief executive of [Bank of America Corp.](#)'s India operations.

There are 32 foreign commercial banks in the country, but they have a total of just 310 branches, or just 0.4% of the national total, according to figures from the Reserve Bank of India, the nation's central bank. The nation, with a population of 1.2 billion, is relatively underserved by banks. India's newly emerging wealthy also are viewed as a

potentially lucrative market for upscale banking services.

Foreign banks have been pushing for years to increase the number of branches they can open in India, so far with little success. Under a World Trade Organization agreement, the RBI must let foreign banks open a minimum of 12 branches a year. Central-bank officials say they have been giving permission for more than the required dozen.

But the central bank has been conservative overall in its approach to bank expansion, bankers say. Indian officials have said they would be more receptive to foreign bank expansion if the U.S. and other markets gave Indian banks more branch licenses. The RBI had 18 pending applications from foreign banks to begin operations in the country, a finance ministry official said last summer.

An RBI spokeswoman declined to comment on whether the Citibank case will influence the review of foreign banking regulations. She said the government is reviewing rules related to foreign banks, including restrictions on the rollout of branches, and may soon release a discussion paper.

She added that the central bank has been notified by Citibank about the Gurgaon case. A senior bank official said Wednesday the RBI is looking into it.

Banking analysts say the government is also weighing whether to require foreign banks to register local subsidiaries in India so they can more easily regulate the firms. Currently, foreign banks simply operate in India as branches of parent companies overseas.

Vyapak Desai, an attorney at Nishith Desai Associates, a law firm that represents foreign banks and private equity firms in India, said the incident "may prompt the regulators to make changes in the manner in which the foreign banks are set up in India."

But he said inadequate corporate oversight at banks is an industry-wide issue, not an issue specific to foreign banks.



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Bloomberg News

India's central bank has been conservative in its approach to bank expansion. Above, pedestrians walk past a Citibank branch in N.Y.

Indeed, another high-profile banking scandal in recent months involved state-run Indian banks. In November, India's top federal investigative agency arrested eight people, including four senior bankers at state-run banks and an executive from a state-run insurer, in connection with allegations they accepted bribes to facilitate loans.

The case against Citibank, which has had operations in India for more than a century and operates 43 branches, has received heightened attention after a prominent venture capitalist, Sanjeev Aggarwal, complained that he lost \$7 million through the alleged scheme. Mr. Aggarwal says Citibank should have notified him when his account balance was diminishing suspiciously.

A complaint he filed with Gurgaon police names Mr. Puri as well as top Citigroup executives, including Mr. Pandit. A top police official said Wednesday the claims against the Citigroup officers won't be pursued because the fraud was local to Gurgaon.

Citigroup says Mr. Aggarwal's claims against senior executives "are completely without basis."

Mr. Aggarwal, managing director of venture firm Helion Venture Partners, has had a wealth management account at Citibank since 2004, and the relationship manager was Mr. Puri for the past three years, according to his complaint and his public comments.

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