

A Review of Forensic Accounting in India

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Abstract- Forensic accounting is the application of accounting principles, theories and disciplines to facts or hypothesis at issues in a legal dispute and encompasses every branch of accounting knowledge. In other words, forensic accounting is the assimilation of accounting, auditing and investigative skills. It is used for examination of fraud from inception to disposition, including obtaining evidence, interviewing, writing reports, and testifying. Although of recent origin, but in recent years, banks, insurance companies and even police have started taking help of forensic accountants. Significant increase in white collar crime now these days and the problems faced by the law enforcement agencies in resolving them have also contributed to the growth of the profession. In this backdrop the present study attempts to provide an insight into the development of forensic accounting in India as an effective measure to combat with surging number of financial scams and frauds these days.

Indexed Terms- Forensic Accounting, Financial Scams, Forensic Accounting Techniques

I. INTRODUCTION

India's image on dealing with corruption is not promising. As per Transparency International's Corruption Perception Index (CPI) in 2021, India is placed at 85th rank out of 180 nations. Due to increased number of frauds in banking, insurance, stock market, cyber world and other sectors, forensic accounting has become need for the day for unveiling the financial scams, giving justice and providing decisive information about the facts found from such financial frauds. The term 'fraud' involves using deception to dishonestly make a personal gain for oneself and/or create a loss for another. It includes acts as theft, corruption, conspiracy, embezzlement, money laundering, bribery, extortion etc. Forensic accounting is the application of different accounting facts collected through auditing methods and procedures to

resolve financial irregularities. According to American Institute of Certified Public Accountants (AICPA): "Forensic accounting is the application of accounting principles, theories and disciplines to facts or hypothesis at issues in a legal dispute and encompasses every branch of accounting knowledge". In other words, forensic accounting is the assimilation of accounting, auditing and investigative skills. It is used for examination of fraud from inception to disposition, including obtaining evidence, interviewing, writing reports, and testifying. Although of recent origin, but in recent years, banks, insurance companies and even police have started taking help of forensic accountants. Significant increase in white collar crime now these days and the problems faced by the law enforcement agencies in resolving them have also contributed to the growth of the profession. Organizations like Indiaforensic, Institute of Chartered Accountants of India (ICAI) and Association of Chartered Certified Accountants (ACCA) offer various designated courses in this field.

II. REVIEW OF LITERATURE

Most of literatures on forensic accounting are explanatory in nature based on secondary data sources by combining the available studies on the topic and by collecting views from the experts in the field.

Zysman (2004) viewed forensic accounting as assimilating accounting, auditing and investigative skills while conducting an investigation. He was also of the opinion that the ability to response promptly and communicating financial information clearly and concisely in a courtroom setting is equally important. Bhasin (2007) in his study has found that the services of forensic accountants are in great demand for criminal investigation, settlement of outgoing partner; settlement of insurance claims, detection of employee fraud and case relating to professional negligence.

Bhasin (2017) in another study, conducted a survey-based research to identify the skills, training, and

education required for forensic accountants in India that can strengthen the corporate governance. He pointed out that skills relating to auditing, communication (both written and oral), critical, analytical and deductive proficiency, domain of knowledge related to law, unstructured problem-solving and investigative flexibility etc. as the relevant skills required for the forensic experts.

Mehta and Mathur (2007) described a forensic accountant as a financial detective with a suspicious mind, a financial bloodhound, someone with a sixth sense that enables reconstruction of past accounting transactions and an individual who looks beyond the numbers.

Luke (2013) described forensic accounting as an exercise complementary to the statutory audit which ensures the robustness of the audit report.

Mazumder (2011) was of the opinion that on the wake of surging white collar crimes, law enforcement personnel are lagging the training and expertise in combating such crimes. They are efficient in combating violent or personal behavior crimes, but needs to expand their knowledge and expertise into the genre of economic crimes.

Hopwood, Leiner & Young (2008) described forensic accounting as the application of investigative and analytical skills for the purpose of resolving financial issues in a manner that it should meet standards and requirements as per the court.

Besides, Okoye and Akenbor (2009), Owojori and Asaolu (2009), Das (2012), Prakash (2013), Shaheen et al. (2014), Eyisi and Ezuwore (2014), Chakrabarti (2014), Peshori (2015), Chaturvedi (2015), Moid (2016), theoretically discuss the opportunities of the forensic accounting by throwing lights on its concept, characteristics and techniques, along with the functions of a forensic accountant in fraud examination in Indian context.

III. OBJECTIVE OF THE STUDY

Considering the noticeable surge in corporate failures resulting from several financial and economic scams and failure to prevent the same on the part of the

statutory auditor, this paper aims at addressing the following issues:

- To understand the concept of forensic accounting
- To know about the evolution of forensic accounting in India
- To know about various techniques adopted by forensic accountants
- To discuss about major scams taken place in India
- To enquire into the future prospect of this profession

- **Concept of Forensic Accounting**

The word 'forensic' can be defined as something meeting the standards of law and suitable to courts of judicature or to public discussion and debate. The word 'accounting', on the other hand, can be defined as an art and science of identifying, measuring, classifying, recording, verifying, summarizing, interpreting and communicating financial information, with an overall objective of depicting the financial performance and financial position of a firm. The GAAPs worldwide suggests that the financial statements must represent true and fair view of the financial state of affairs. The subjectivity of the term 'true and fair view' leaves a gap for practicing manipulations which ultimately lead to financial frauds, thereby abating the trust of business stakeholders on the reported statements. This paves the way for emergence of forensic accounting for prevention, detection and examination of fraud.

- **Evolution of Forensic Accounting in India**

Kautilya was the first person to mention various ways of misappropriation in his famous book Arthashastra. After the cases of ENRON, Rajat Gupta and SATYAM, use of forensic accounting has emerged widely. In ENRON scandal, its shareholders lost \$74 billion in four years resulting in its bankruptcy, and its employees lost pension benefits in billions. The scam has shown to the world that how a crime of numbers can result in billions of losses and drew attention of main stream media houses and general public. In Rajat Gupta case, he was convicted in June 2012 on insider trading charges of four criminal offences of conspiracy and securities fraud. In Satyam Computer Services scandal, Chairman Byrraju Ramalinga Raju confessed that the company's accounts had been falsified. Chartered accountants were assigned with such

investigations, but very few chartered firms were used to provide specialized service of fraud examination. This area was used to be dominated by big four consultancy firms viz. Deloitte, KPMG, Price water House Coopers and Ernst and Young. The establishment of Serious Fraud Investigation Office (SFIO) is the landmark creation for the forensic accountants in India. The discipline is now popular in India due to growing rate of financial crimes and offences and lack of trained professionals to trace out the culprits. Later on, the Companies Act 2013 introduced a special approach relating to prevention of economic fraud and preservation of national wealth in tune with American Law and British Bribery Act. As per a study conducted by Ernst and Young in 2012, frauds have become more complicated and sophisticated than before to detect, with major crimes being reported in the areas of telecommunication, financial services and real estate. The top five risks that emerged from the survey are data or information theft and IP infringement, bribery and corruption, including coercion, fraud perpetrated by senior management officials, dealer fraud or kickbacks and regulatory non-compliance. The surging practice of frauds and scams and gaps in compliance culture necessitated proper investigation thereof as well as a strong preventive environment. Thus, forensic accountants were called for to detect planning, execution and consequences of the fraud and spot the culprits on immediate basis.

- Techniques used in Forensic Accounting

The forensic accounting techniques should be customized and as per the need of the situation while examining a financial fraud or irregularity, as against the prototype procedures followed in statutory auditing techniques. Some of the important forensic accounting techniques are highlighted here.

Benford's Law: It takes help of mathematics to assess whether the irregularity detected is the outcome of an unintentional mistake or a fraudulent activity. In this method, patterns of the figures of the variable under study are observed and compared to the pre-defined standards using Z-test at certain level of confidence. Significant differences between them may be considered to be a signal for further investigation to detect any potential fraud.

Theory of Relative Size Factor (RSF): To find out presence of any outliers in the dataset which may have arisen due to fraud, RSF may be calculated as the ratio of largest number to the second largest number in the dataset. An unusually high RSF gives an indication that the highest number is not in line with the other numbers in the dataset and hence need further investigation for detecting any potential fraud.

Computer Assisted Auditing Tools (CAATs): While dealing with huge volume of clients' data, these tools help auditors in performing his audit procedures like matching of transactions and balances, identifying abnormal fluctuations, re-calculations, etc.

Data Mining Techniques: These techniques facilitate extraction of large volume of data for further analysis to determine the patterns in data through trends and variations, to forecast the outcome on the basis of patterns identified, to detect the items that deviate from the established norms, to detect any unusual pattern by employing various graphical techniques.

Ratio Analysis: Ratio analysis identifies symptoms of fraud, if any. Examples are the ratio of maximum value to minimum value, maximum value to the second maximum value, current year figure to the previous year figure etc. These ratios assist in identifying the relationships, any abnormal ratio is an indication for potential fraud which may need further examination. Asset quality index, gross margin index, sales to receivables ratio, etc. are some of the commonly used ratios.

The global consultancy service provider KPMG has suggested the use of certain contemporary techniques of forensic accounting in the light of increasing sophistication and technology in the commitment of corporate frauds and economic crimes like spot the unusual (looking for the accounting transactions entered into on holidays), fraud risk management (enables to sense the potential fraud at the earliest and avoid it), use of forensic technology lab (enables to collect, recover, and preserve the evidence in the digital format to assist in fraud examinations and legal prosecution), corporate intelligence (providing due diligence check conducted on the third parties, either individual or organization, while entering into a business transaction with them), verification of

employees checking thereby background and credentials of employees such as, address, education, past employment(s), pending lawsuits, mental and physical check, criminal record, etc.

- Some of the Major Scams in India

Ketan Parekh Scam 1992: Ketan Parekh, a stock broker from Mumbai, was accused of involved in circular trading with companies like Global Trust Bank and Madhavpura Mercantile Co-operative Bank and sent to jail with two others for taping off Rs.48 crore from a unit of Canara Bank in 1992. He was also banned from trading till 2017.

Harshad Mehta Scam 1992: Harshad Mehta, popularly called the Big Bull among traders, was accused of using the funds from inter-bank transactions to buy shares at a premium across many sectors. He had set a trend in the stock market before this scam involving Rs.4000 crore being revealed.

Fodder Scam 1996: This scam took place in Chaibasa, Bihar where the animal husbandry department embezzled funds of around Rs.950 crore allocated for purchase of cattle fodder, medicines and animal husbandry equipment. Lalu Prasad Yadav, the then Chief Minister of the state along with the former Chief Minister Jagannath Mishra were the main accused.

Satyam Scam 2009: Satyam Computers Chief B. Ramalinga Raju misappropriated books and falsified revenue figures which led to a scam involving a loss of Rs.8000 crore.

2G Spectrum Scam 2010: The illegal issuance of 2G licenses by government officials to various telecom companies on first cum first basis instead of auctioning, the deal amount, as estimated by CAG was about Rs.176000 crore

The Commonwealth Games Scam 2010: Suresh Kalmadi, chairman of the Organizing Committee of the Commonwealth Games was accused of engaged in a number of corrupt deals involving overstated contracts. Kalmadi was also accused of giving away Rs.141 crore contract to Swiss Timing for its timing equipment, which was inflated by Rs.95 crore.

Indian Coal Allocation Scam 2012: The government had reported a loss of Rs.185591 crore. The CAG has blamed the Indian government of giving unjustified benefits to companies by distributing huge coal acres in an arbitrary manner instead of auctioning to the highest bidder during 2004-2009

Tatra Scam 2012: Bharat Earth Movers Ltd in collaboration with Tatra Vectra Motors had sold over 7000 trucks to the Army. When General V. K. Singh took over as the Army Chief, he refused to authorize the purchase of trucks after he was offered a bribe. Estimated deal amount was Rs.750 crore

Chopper deal scam 2013: The deal amount was Rs.74.5 crore. The Italian firm Finmeccanica was involved in one of a series of corruption scandals in defence deal making in India

Saradha Scam 2013: This scam involving Rs.30,000 crore relates to Saradha Group, a group of over 200 private companies that was believed to be running collective investment schemes but incorrectly referred to as chit funds, caused by collapse of a Ponzi scheme Future Prospects of Forensic Accountants in India

With the introduction of the new Companies Act 2013, organizations of national interest like Institute of Chartered Accountants of India (ICAI), India forensic and Department of International Forensic Sciences (IFS) come up with various certification courses in forensic accounting. ICAI has introduced a 7 day certificate course on fraud detection and forensic accounting wherein it provides to the participants the knowledge regarding essentials of forensic accounting, concept and types of frauds, corporate, civil, criminal, cyber and taxation laws, concept of red flags and green flags, digital forensics etc. It also provides training of applications of Microsoft office and real-time applications of various forensic techniques viz., Benford's law, theory of Relative Size Factor (RSF), Computer Assisted Auditing Tools (CAATs), field investigations, etc. A participant has to go through an assessment in the form of written examination, research papers publication and model forensic audit report to qualify for the certification.

The India forensic Center of Studies also provide forensic accounting education and training. The

registered participants undergo practical training and assessed through written examinations to get awarded with the designation of Certified Forensic Accounting Professional (CFAP). Besides CFAP, the other courses offered are Certified Anti-money Laundering Expert (CAME) and Certified Bank Forensic Accountant (CBFA). Whereas CAME focuses on discovering doubtful transactions by referring to similar past cases, CBFA equips participants with analytical and investigative skills for forensic analysis in a methodical way such as locating signals of fraud or misconduct, evaluating risk etc.

Forensic Accounting and (Financial) Fraud Examiner, a similar certificate course has been introduced by the IFS education department of government of India to enhance awareness about forensics. The duration of the course varies from two months to twelve months post which certificate is awarded on qualifying an online examination. The course structure provides exhaustive knowledge in the areas of forensic sciences, fraud fundamentals, financial statements preparation, analysis and reporting, Indian and international legal frameworks concerning corporate governance, accounting, taxation, crimes etc.

CONCLUSION

At the end of the above discussion, it has become evident that forensic accounting is a holistic concept which encompasses skills and expertise in all aspects of finance, knowledge about different types of fraud, awareness about business malpractices, understanding of business reality and working of the legal system with investigative skill. Forensic accountants' job is to detect fraud and criminal transactions in banks, corporate entities, public sector or any other organization's financial statements and books of accounts. With an abnormal surge in the rate of financial fraud cases and crimes, stock market scams, failure of non-banking financial corporations, money laundering etc., the absence of a proper regulatory mechanism to weed it out from the roots was strongly felt which has forced the Government of India to form Serious Fraud Investigation Office (SFIO) under the Ministry of Corporate Affairs as an initial step by the Government of India to recognize the importance and need for advancement of the profession of forensic accountants in India. There are strong reasons that

vouch the consideration of forensic accounting as a separate discipline and provides opportunities for forensic experts to offer litigation support, investigative accounting, and consulting services. Despite of various positive developments in this field, much scope for further advancements in the sophisticated forensic accounting techniques is there in the light of increasing complexity of corporate scams.

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