



The impregnable role of forensic accounting in detecting financial frauds

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Abstract

In the current transient era of hyperbolic competition and ever increasing cynicism, people have been witnessed to be highly dubious of each other. With the prodigious growth in the knowledge and skills of people as well as the latest amplified technologies, any sort of discrepancy can be infused and wielded. In this light, financial firms of today are faced with an arduous task of detecting and dodging any kind of financial fraud. In order to blight the menace of such frauds, Forensic Accounting is playing a mammoth role. Most of the financial firms are undertaking the help of Forensic Accounting as mechanism for more comprehensive detailed information swirling financial frauds. Forensic Accounting is making use of several specialized tool for the purpose of fraud detection. Forensic accountants are presently high in demand as a result of public need for honesty, financial lucidity and ethical legitimacy. The present research study purports to investigate crux objective of exploring the instrumental role Forensic Accounting in detecting financial frauds keeping in view the various Indian financial nerve racking scams. The results of the study bring out the efficacy of Forensic Accountants and in turn the relevance of Forensic Accounting in detecting financial frauds. The study albeit theoretical is pivotal as it provides an exquisite conceptual base for further extended research. This study has brought out some of the most infamous financial frauds that took place in India. It has also highlighted the significance of Forensic Accounting in the current scenario.

Keywords: forensic accounting, forensic accountants, financial frauds, fraud detection

1. Introduction: Background of the Study

The prolific amelioration in technology and skillsets of people in the modern day has boosted the efficacies of financial firms but leaving it with much to mull over, especially when dealing with deluding. The sustainability and growth of financial firms over the years has been heavily reliant on the financial and accounting operations showcasing its lucidity, accountability and profitability, thereby enticing investors. But in certain instances, firms are beguiled to imply excessive profitability following accounting fraud involving manipulation of financial statements thereby incurring significant financial failures, lawsuits, and bankruptcy. Despite savouring the ephemeral economic benefits from such accounting frauds, the aftermath of such culpable firms is a spiralled financial performance, lump sum fines and bankruptcy, hence leaving the firms to bear the ignominy of a tarnished image. This is where the essence of Forensic Accounting comes to the limelight. Forensic Accounting is basically used an effective tool for investigation and prevention of financial frauds. In the Indian backdrop, greater emphasis has been laid on Forensic Accounting taking into consideration the public dealings with financial collapses, escalated financial scams popularly called "white collar-crimes" and ever increasing occupational frauds calling for more sound professionalism in accounting and finance. This is the crux reason for conducting this study in India where tackling financial frauds has almost been an anomaly and a much talked about conundrum.

2. Introduction to the Study

The impending usage of systems has changed the modus vivendi of the society making us reliant on it like never before. But alongside it has brought with it the rampaging bane of financial frauds with an alarming rate. Truth to be told, the juggernaut of financial frauds seems unstoppable at the moment, thus imploding the performance of the financial firms and derailing the economic growth of a country in the long haul. Stonewalling and eviscerating such menace is an arduous task, incumbent on the part of the financial firms. The recent ramifications as a result of financial frauds particularly in India has witnessed an upsurge in the growth of Forensic Accounting and the employment of Forensic Accountants in the financial firms who scrutinizes even the miniscule details of financial firms for combating even the slightest of discrepancies. The present research study not only highlights the role and relevance of Forensic Accounting but also throws valuable light on its inception and its usage in India.

2.1 Concept of Forensic Accounting

Contrary to the name, Forensic Accounting has got nothing to do with forensic sciences, or criminology for that matter. Forensic accounting sometimes also known as Forensic Audit is the process of applying accounting methods for detection and gathering evidence of frauds, embezzlement, or any other such white-collar crimes. In the current scenario, it has taken up a significant role in public as well as private organizations.

Forensic Accounting is simply the examination and analysis of evidences. Forensic accounting is that special practice area of accounting resulting from original or anticipated litigation support services and investigative or fact finding services where the essence lies in the integration of accounts, audit and investigation related skills. Forensic accounting is the assistance of finance professionals (Forensic Accountants) to settle disputes concerning allegations, fraudulence, suspicion of fraud and misconduct in business by analysing, interpreting and summarizing complex financial and business matters. Frauds in various sectors (stock market, insurance, bank, etc.) require a sharp scientific tool for investigation and dispute settlement and thus Forensic Accounting plays a pivotal role in serving such purpose.

2.2 Forensic Accounting vs. Forensic Auditing

Both the terms Forensic Accounting and Forensic Auditing are synonymously used. But a more intimate analysis of literature would reveal that there exists a primary difference between these two terms. In order to unfurl the difference between the two terms, one has to have a better understanding of the gamut of financial frauds. There are two types of frauds in a business world. The first one is Frauds against Business which is generally committed by the employees or clients or vendors or in connivance of these three with a purpose to delude. The second one is Frauds for Business which is generally committed by the promoters and shareholders of the business to deceive the bankers, revenue authorities and regulators. Hence, the primary difference between forensic accounting and forensic auditing lies in the very purpose of the audit itself. A Forensic Accounting assignment relates to Frauds against Business. This issue may involve employee fraud or a dispute with a vendor or customer. On the other hand, Forensic Auditing related to Frauds for Business. Forensic Accounting requires investigative techniques and technology whereas Forensic Audits relate directly to financial statement frauds. Forensic Accounting assignments are complex in nature seeking answers to the questions like the origination and perpetration of fraud, the losses resulting from the fraud, etc. On the other hand Forensic Auditors are engaged to check the trail of money searching answers to the questions such as motives of the businesses behind the fraud.

3. Literature Review

Maurice E. Peloubet is credited with developing the term forensic accounting in his 1946 essay “Forensic Accounting: Its Place in Today’s Economy.” By the late 1940s, Forensic

Accounting did eventually prove its worth especially during World War II. “Since the 1980s in some Western countries, particularly in the USA, a new profession in the field of accounting and auditing emerged. This profession identifies a field composed of accounting, auditing, and investigative skills (Ozkul and Pamukc, 2012).”

“Forensic Accounting is defined by Zia (2010) as the science that deals with the relation and application of finance, accounting, tax and auditing knowledge to analyse, investigate, inquire, test and examine matters in civil law, criminal law and jurisprudence in an attempt to obtain the truth from which to render an expert opinion.”

“In most of the corporate organizations, Forensic Accounting investigation is widely believed as a mechanism that provides more comprehensive details information concerning financial fraud (Eliezer & Emmanuel, 2015; Efosa & Kingsley, 2016).” “Modogu and Anyaduba (2013) consider Forensic Accounting as the special investigation process through the utilization of accounting skills, auditing skills, and investigative skills to determine the extent of financial fraud in legal matters.” The significance of Forensic Accounting lies in the detailed enquiry of fraud and determining why it happened (Crumbley, 2009).

4. Objectives of the Study

1. To bring out the role of Forensic Accounting in detecting financial frauds.
2. To juxtapose between Forensic accounting and Forensic Auditing.
3. To highlight the relevance of Forensic Accountants and the scope of Forensic Accounting in India.

5. Financial Frauds and Scams in India

Over the past few years financial frauds in India has been skyrocketing at a devastating rate. In fact, India has witnessed some of the most nerve racking frauds and scams over the last couple of decades. Financial fraud occurs when anyone gets hold of money or other assets through delusion with a deliberate purpose. A closer and in-depth study of literature will show certain consensus that fraud include: (1) window dressing; a term in the field of accounting which means to manipulate financial records; (2) purposive misrepresentation of events, transactions, accounts or other; (3) misinterpretation and misapplication of accounting standards, GAAP, accounting policies and other such methods done with a deliberate cause; (4) omissions or disclosures or presentation intentionally done.

The following table contains the details of such frauds and scams.

Table 1

Company Name	Year	Issue	Estimated Price (Rs.)	Current Status
Vanishing Companies Scam	1998	More than 650 companies raised money and then vanished from stock markets.	More than Rs. 800 crore	Only 77 companies officially identified
Plantation Scam	1999	With interest rates promised up to 300 per cent, investors were lured to invest in teak saplings	Rs. 3000 crore	Not under purview of SEBI or RBI, hence no action could be taken against the companies
Ketan Parekh Securities Scam	2001	Ketan Parekh raised a huge amount of money from the banks to invest in the market.	Rs. 1250 crore	Arrested
Stamp Paper Scam	2003	Illegal stamp papers were printed in 13 states operated through 176 offices	Rs. 175 crore	Deceased
Satyam Scam	2008	The stock prices soared as company forged sales invoices and bank statements	Rs. 15000 crore	Arrested
Golden Forest India	2008	Investors were lured to invest in forestry farm	Rs.2000 crore	Assets of the company liquidated

Scam				
Seashore Group Chit Fund Scam	2008	Investors were tempted to invest in tourism sector with 24 per cent returns	Rs.500 crore	Arrested
Housing Loan Scam	2010	Senior LIC and LIC Housing Finance officials were bribed to facilitate loans to builders	Rs.40000 crore	Probe still on
NSEL Scam	2013	In NSEL, the contracts were made on paper but the underlying commodities did not exist	Rs.5000 crore	Arrested and on bail
Internet Scam	2017	Daily return of Rs.625 for one year was promised on an investment of Rs.57,500	Rs.3700 crore	Arrested
Vikram Investments Scam	2018	Collected money promising 40 per cent returns on commodity trading	Rs.800 crore	Arrested
Bitcoin Scam	2018	Collected Rs.2000 crore from 8000 people for mining bitcoins. Also provided bitcoin mining hardware	Rs.2000 crore	Arrested
Punjab National Bank Scam	2018	Bank fraud with help of senior officials	Rs.13700 crore	Absconding

6. Forensic Accounting in India

Forensic Accounting is a very much upcoming field in India. While Forensic Accounting developed in the early 1995 in USA, its advent in India took place a few years back. Rewinding to the days of Kautilya in ancient history brings to the limelight his famous book 'Arthashastra' in which he mentioned the forty ways of misappropriation. In India, Forensic Accounting has risen to prominence due to increased financial frauds popularly known as white collar crimes in India. After scams like Satyam, Rajat Gupta and Enron, the sector of Indian business firms hit a nadir and wide scale recriminations ensued. Taking into account such ramifications, the Companies Act 2013 paved the way for a special approach to prevent economic fraud. The lack of perception in the law enforcement agencies of India coupled with the price at which white collar crimes have escalated fuelled the amelioration of Forensic Accounting in India. Granted the fact that Forensic Accounting is an emerging field in the accounting panorama of India but it has got tremendous potential as an exciting area of practice for Chartered Accountants in India. Indian Chartered Accountants with their extensive knowledge, skills and experience are well capable of creating the domain of Forensic Accounting and Auditing as their niche area. Chartered Accountancy firms like Sharad Joshi Chartered Accountants is currently providing Forensic Accounting services. There are also a number of consultancy firms like Deloitte, Ernst & Young, Price Water House Coopers and KPMG which are also providing Forensic Accounting services. The Institute of Chartered Accountants of India (ICAI) started a course on Forensic Accounting but only for its members. Currently, only a small number of academic institutions are offering courses on Forensic Accounting, be it part time or full time. The Indian institutions are found lagging behind in this area when juxtaposed to foreign institutions. Some leading organization such as India Forensic located in Pune, Maharashtra have already started have already started providing courses on Forensic Accounting. Institute of Chartered Financial Analyst of India (ICFAI) University has also joined the bandwagon. The foundation of Serious Fraud Investigation Office (SFIO) in India is the landmark genesis for Forensic Accountants. In addition to this, the Government has also established a couple of more agencies like Central Bureau of Investigation (CBI) and Central Vigilance Commission (CVC) for the purpose of combating and blunting the menace of financial frauds.

7. The role of Forensic Accountants

Since forensic duties are concerned with judiciary or semi-judiciary dispute resolutions, this is incumbent on the part of the forensic investigators to have a thorough understanding of the relevant legal jurisprudence and laws. Commerce graduates who are willing to take Forensic Accounting as a career option have to qualify as a chartered accountant and then differentiate and specialize in Forensic Accounting. The experience in audit and accounting as a chartered accountant further boosts prospects of Forensic Accounting. However, to be a proficient Forensic Accountant it is indispensable to work with experienced and well-qualified Forensic Accountants to learn the nitty-gritties and ropes of the trade. As mentioned earlier in this study, a number of well-established organizations offer instructional coaching, guidance, training and certification for Forensic Accountants. These certificates reveal that a Forensic Accountant has acquired the requisite instruction and training beyond that of an average accountant. Forensic Accountants are renowned for rendering a plethora of exquisite services which include fraud detection, criminal investigation, matters related to negligence, arbitration service, settlement of disputes as well as settlement of insurance claims, etc. Thus there are myriad scopes for Forensic Accountants at the present scenario.

8. Forensic Accounting and Fraud detection

As businesses and society have become more enlightened and complex, methods of perpetrating frauds have also become more sophisticated. Fraud defaulters are now smarter than before making the job of Forensic Accountants rather gruelling in detecting frauds. There is much need for deeper understanding on the ways these defaulters work their fraudulent activities. Without constant public involvement and amelioration in Forensic Accounting, it will be extremely difficult to detect financial frauds. As a result, frauds will continue wreaking havoc leading to wide scale failures of a financial firm to meet the demands of public expectations and the company's own shareholders. Shambling corporate governance and accounting failures are said to be certain key reasons for the emergence of fraud cases. Lack of loyalty and translucency in the reporting of financial statement is another major problem. Fraud investigations in Forensic Accounting vary significantly when placed in juxtaposition with Traditional Accounting. Forensic Accounting involves the intuitive ability to investigate fraud as well as the experience to perform a

Competent investigation which is missing in case of Traditional Accounting. Fraud investigations In Forensic Accounting often curl up proper communication with people who had access to the resources and a careful scrutiny of documents. Forensic Accounting helps in assisting theft investigations and defalcation of corporations and individual assets calling upon the precious use of knowledge and skills of Forensic Accountants thus helping to ascertain the level of theft or misappropriation. Forensic Accounting is also helpful in the review of business accounting systems and making recommendations for the improvement of internal system in order to prevent theft and fraud. Forensic Accounting involves the application of many tools and techniques some of which are Theory of Relative Size Factor (RSF), Computer Assisted Auditing Tools (CAATs), Benford's Law, Data Mining Techniques like Discovery, Predictive modelling and Deviation & Link analysis and Ratio Analysis. Truth to be told, Forensic Accountants are not legal practitioners, winning or losing cases; rather, they seek the truth while conducting their evaluations, tests, investigations and reporting the original and correct results without any biasness.

9. Conclusions

Truth to be told, the advent and amelioration of Forensic Accounting was a much needed tonic keeping in mind the devastating pace at which financial frauds and scams are skyrocketing, especially in India. With a plethora of rapidly emerging changes, the complexities of the modern day world are ever increasing. Frauds have become extremely common these days and not at all surprising. However, to curb the rampage of these financial frauds is not an easy task. Forensic Accounting is playing its part in detecting and preventing these types of frauds which indeed is shambolic, not only tarnishing the image of the company but the country in the long haul. Greater emphasis needs to be laid on Corporate Governance. The employees, the shareholders as well as the management needs to carry on their activities in true accordance to the ethics, un-biasness and lucidly In India, it is mainly used for the purpose of detecting of fraud rather than preventing it. Hence, Forensic Accounting in India is still very much at its nascent stage. More and more professional accounting institutions should start offering courses on Forensic Accounting in order for the youths of today's society to become aware of such menacing fraud and acquire the knowledge and skills to blight it out. This research study carries a strong message to the corporate bodies as well as professional accounting institutions about encouraging courses on Forensic Accounting. Albeit, the research done mostly on the basis of Secondary data, this study still is a worthwhile endeavour which can be further extended for empirical survey in the future. Also, it has thrown valuable light on the present scenario of Indian financial frauds as well as traced back to the days of Indian rich history where the very seeds of Forensic Accounting were laid which almost everyone were oblivious of. This research study has clearly brought out the difference between Forensic Accounting and Forensic Audit, albeit they are regarded almost same and used interchangeably as well as thrown valuable light on the role on Forensic Accounting which is indeed impregnable.

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