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Forensic Accounting: A Conceptual Study In Indian Context

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ABSTRACT

Financial sectors are prone to frauds and scandals, these frauds are not easy to investigate or detect by traditional auditors or investigators. Forensic accounting is an umbrella term which involves application of special skills such as accounting, auditing procedure, financing quantitative methods, research and investigative skills. Forensic means "suitable for use in a court of law." Forensic Accounting is useful for detecting such financial frauds and helps in the investigation of financial issue related. Forensic Accounting is not same as auditing. Auditing is the process of checking for the compliance of a company's book to GAAP, Accounting Standards and company policies. Whereas, forensic accounting is the process of in-depth analysis of financial transactions to discover the true picture of financial transactions, also it helps in settling legal disputes; forensic accountant and its report is used as witness and evidence in court respectively. Forensic Accountants need to have a special skill and knowledge in financial investigation. This paper is an attempt to highlight the genesis and modus operandi of forensic accounting in India. The study also aims at identifying the problems of forensic accounting in India. The contents of this paper includes; introduction, conceptual framework, literature review, objective and methodology of the study, genesis of forensic accounting in India, modus operandi, problem of forensic accounting in India, suggestion and conclusion.

Keywords: Auditing, Forensic Accounting, Forensic Expert, Fraud, Investigative Accounting

INTRODUCTION

Finance is an essential element for running and growth of any business organization. The growth of business organization is an essential factor for the development of a regional and national economy. The requirement of finance by the business organization is facilitated by different financial institutions. The financial institutions is also a business organization who play a very crucial role in developing and functioning of the economy because it helps to mobilize the financial resources from savers to investors.

As the financial sector plays an important character in the development of a regional, national and worldwide economy with broad range of financial activities running through diverse sectors of the economy, this financial sector is prone to frauds and scandals. Due to increasing frauds and scams in financial sector, there is a need for forensic accounting to combat such frauds and scams.

Forensic accounting involves the process of understanding, detecting, identifying and communicating fraud patterns and schemes to relevant stakeholders for improving investigation process or activity (Ozili Peterson k,2015). According to Chilvers (2000), forensic accounting can be defined as the use of investigative techniques, accounting skills and auditing skills, to develop information and opinions to use as an evidence by expert in court of law. According to Dhar and Sarkar (2010), Forensic Accounting is defined as an application of accounting concepts and techniques to solve legal problems. From the various definitions reside in the area of litigation services, accounting investigation helps in preparing evidences for court of law, which are importance to the banking sector. Forensic accounting may be one of the most efficient and effective ways to detect and prevent fraudulent activities in the financial institutions as it is concerned with the evidence of accounting information and as a practical field concerned with accounting fraud, auditing and risk assessment for detection of financial misrepresentation. Skousen and Wright, (2008).

Recently, forensic accounting has become an indispensable tool for investigation in India due to rapid increase in financial fraud and other white-collar crimes, and our law enforcement agencies do not have the expertise or time to uncover such frauds. Scams like Satyam, 2-G Spectrum, Commonwealth games, Railgate scam, Tatra Truck scam, Chopper scam, PNB frauds and other frauds and scams in India had enhance the scope for forensic accounting in India. According to the Corruption Perception Index 2018 Report released by Transparency International, India's rank is 78th among 180 countries.

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CONCEPTUAL FRAMEWORK

Forensic Accounting: The general meaning of Forensic accounting is the use of accounting, investigation, and auditing skills to investigate fraud and embezzlement to analyze financial information for use in legal proceedings. Forensic accounting is an umbrella term which involves application of special skills such as accounting, auditing procedure, financing quantitative methods, research and investigative skills. Forensic means "suitable for use in a court of law." Forensic accounting can be described as a specialized field of accountancy which investigates fraud and analyze financial information to be used in legal proceedings.

Forensic accounting professionals should have the skilled of quantifying damages and determining the complete extent of losses. They have been involved in four basic areas of forensic investigation: data collection, data preparation, data analysis and reporting. The tasks of the forensic accountants includes: examining of records, analyzing historical data, checking for irregularities in business, checking journal entries, analyzing historical trends, tracing the flow of funds, communicating and interviewing the relevant parties, analyzing digital/electronic data and performing an overall evaluation of the situation in questions. Beyond this, they can serve as consultants or expert witnesses. When required, they may collaborate with other experts.

Fraud: Fraud implies dishonesty with a motive to device, to mislead, or at least to conceal the truth. Thus fraud is considered more dangerous than errors. Errors may be due to omission, commission, error of principle, compensating error or error of duplication. These errors may be an intentional or unintentional, but fraud is an intentional act. Fraud may be of different types, some of most committed type of frauds are:

i).Misappropriation of Cash;

ii). Misappropriation of Goods;

iii). Manipulation of Accounts;

Beside these, as the development of advance technology, sophisticated tools are used for cyber frauds and other digital frauds. Due to use of sophisticated tools, it's not an easy task to detect such frauds by traditional auditors or accountant.

Auditing: Auditing is concerned with the verification of accounting information which determining the accuracy and reliability of accounting statements. Verification of accounting information involves a careful evaluation of data available to the auditors in support of recorded transactions. The auditor examines internal data, that is, the record vouchers and books of accounts. Thus, Auditing is primarily involves in testing the reliability, competency and adequacy of evidence in support of financial transactions of an entity.

Forensic Accounting and Auditing: Forensic Accounting is not same as auditing. Auditing is the process of checking for the compliance of a company's book to GAAP (Generally Accepted Accounting Principles), Accounting Standards and company policies. Whereas, forensic accounting is the process of in-depth analysis of financial transaction to discover the true picture of financial transactions, also it helps in settling legal disputes; forensic accountant and its report is use as witness and evidence in court respectively.

Auditor's task is to audit the annual report, while auditing they may find fraudulent reports. Forensic Accountant's task includes both investigation of fraud and non fraud disputes. Thus, Forensic Accounting and Auditing has a correlation in the work of prevention and combating financial fraud. Hence, we can say that Auditor is a watchdog and Forensic Accountant is a sniffer dog or bloodhound.

Difference between forensic accounting and auditing is given below

Forensic Accounting Vs Auditing

Basis	***Forensic Accounting***	***Auditing***
Meaning	It is an in-depth analysis and investigation is conducted for establishing a specific fact.	It is the process of inspecting the books of accounts of an entity and reporting on it.
Legal binding	Not compulsory	Compulsory under the

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		Companies Act, 2013
Time	As per requirement	Annually
Performed by	Experts	Chartered Accountant
Nature of task	Critical and in-depth examination	General examination
Documents	It considers the audited accounts	It does not consider the audited or investigated accounts
Appointed by	Forensic Accountant can be appointed by a specific organization, authority or an individual when required	Auditors are appointed by shareholders or proprietor.

LITERATURE REVIEW

Cendrowski at el. (2007) has defined forensic accounting as a comprehensive form of fraud deterrence. According to them, Fraud deterrence is the proactive identification and removal of the causal and enabling factors of fraud. Fraud deterrence is based on the premises that fraud is not a random occurrence, fraud occurs where the conditions fit for it to occur. Deterrence of fraud targets the root causes of fraud and its enablers, this analysis help to reveal the potential fraud opportunities, but it is performed on the premises that organizational procedures are improved to reduce or eliminate the factors of fraud is the best preventive measure against fraud.

Bhasin et al. (2007) worked on Forensic Accounting: A New Paradigm for Niche Consulting. The study finds that the services of forensic accountants are in great demand in the areas which include criminal investigation, settlement of outgoing partner; settlement of insurance claims, detection of employee fraud and case relating to professional negligence.

Ozkul, Pamukcu et al. (2012) studied on Fraud Detection and Forensic Accounting. The study concluded that fraud may involves: the alteration or manipulation of financial records, supporting documents, or business transactions; intentional mis-statements, omissions, misrepresentation of events, transactions from which financial statements are prepared; knowingly misinterpretation and wrong application of accounting standard, principles, policies and methods used to measure, recognize, and report economic events and business transactions; intentional omissions and disclosures or presentation the use of aggressive accounting techniques such as illegitimate earnings management strategies; and the manipulation of accounting practices under rule-based or principle-based accounting standards that allows the organization to hide their economic performance.

Ozili Peterson k (2015) examined several issues on: the nature of fraud, forensic accounting, core and enhanced skills of the forensic investigators as well as issues with forensic education. The study concluded that while forensic accounting is gaining significant interest among academics, the progress in forensic accounting study will depend on the extent to which fraud perpetrators leave traces. Because fraud perpetrators leave some traces after performing the act. But the regulators need to be more concerned about fraud perpetrators who do not leave any trace of some sort. This will create a problem for the regulators if fraud perpetrator learned thorough knowledge of accounting standards, auditing techniques and investigative skills. This knowledge would eliminate possible traces of frauds.

OBJECTIVE AND METHODOLOGY OF THE STUDY

The central focus of the study is to highlight the genesis and modus operandi of forensic accounting in India. The study also aims at identifying the problems of forensic accounting in India.

The study is based on exploratory in nature and the source of data is exclusively based on secondary data. Secondary data are collected from various books, journals, newspapers, reports published by GOI, RBI and other research papers on Forensic Accounting

GENESIS OF FORENSIC ACCOUNTING IN INDIA

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The term ‘Forensic Accountant’ was coined by Maurice E. Peloubet in 1946, but the forensic accounting can be traced back to ancient age. The Archaeological findings reveal that, in Egypt during 3300-3500 BC; accountants were involved in the prevention and detection of fraud. Chakrabarti Manas (2014).

In India, Kautilya was the first person to mention about the financial misappropriation in his famous book ‘Kautilya Arthashastra’. Kautilya has mentioned forty ways of embezzlement. Traditional auditors and experts were used in India to identify such misappropriation or fraud. Usually, the Chartered Accountants are called upon to take up such investigative task.

But due to increase in financial fraud and the use of sophisticated tools by the fraudsters, it is difficult to detect and prevent such fraud. To deal with such fraud, use of Forensic Accounting and training institute for Forensic Accountant should be developed in India. Forensic Accountants use the skills of auditing, investigating and accounting.

After Satyam scam, Forensic Accounting has come to limelight recently due to rapid increase in financial crimes and the belief that our law enforcement agencies do not have the expertise needed or time to uncover frauds. The scam like Harshad Mehta, Ketan Parekh, Sanjay Seth and recently India bull scam, Kingfisher Airlines, Credit card fraud, coal block scam and most recently Punjab National Bank fraud lead to improves the scope of forensic accounting in India. Forensic Accounting is becoming an indispensable tool for investigation in India, whether the fraud is stock market fraud or bank fraud or cyber fraud. Chakrabarti Manas (2014).

MODUS OPERANDI OF FORENSIC ACCOUNTING

Forensic Accountant not only investigates the company accounts, but also reviews employee records, views the physical plant, interviews employees, monitors cash and inventory flows and uses various methods to determine how items in the financial statement of the company came to be. Forensic Accountant likes a detective looks for clues, it is not just a matter of checking figures and tables but it also involves study of human behaviour. There are many indicators to look for, even the study of body language is also necessary for detection of fraud. Forensic Accountant does not start his work suspecting every employee, but the chief suspect is a person who controls major transactions. The nature of fraud varies from company to company so therefore, there cannot be any standard method for Forensic Accounting.

The Forensic Accountant uses some tools and technique, such as

1. Benchmarking: It is the process of comparison of financial data with the performance of different centre or organization units, also comparing the organization overall performance with its pre decided standards.
2. System Analysis: It is the analysis of whole system to identify weak spot or loopholes, which may be opportunities for the fraudster.
3. Data Mining: It is a statistical technique to mine large volume of data. It help to identify hidden data from large volume of data.
4. Ratio Analysis: It is the computation of data into ratio. Such as financial ratios that indicate the financial health of an organization, data analysis ratios technique locates the fraud by identifying abnormal ratio and possible symptoms of fraud.
5. Specialist Software: Computer Assisted Auditing Tools (CAAT) is a computer programs that help an auditor in audit procedures.

According to Bhasin, M. L. (2016)**,** some of the useful areas of expertise for forensic accountants are as follows:

- Good knowledge of financial statements and the ability to critically analyze the financial statements, these skills help forensic accountants to uncover abnormal patterns in accounting information and recognize their source.

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- Proficiency in computer and knowledge of networking systems will help forensic accountants to conduct investigations in the area of e-banking and computerized accounting systems.
- Knowledge of psychology helps to understand the impulses behind criminal behavior and to set up fraud prevention programs that motivate and encourage employees.
- Interpersonal and communication skills, which aid in disseminating information about the company's ethical policies and help forensic accountants to conduct interviews and obtain crucial information.
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PROBLEMS OF FORENSIC ACCOUNTING IN INDIA

Though Forensic Accounting is an indispensable technique to detect and investigate financial frauds, it faces certain problem in its implementing in India:

1. Forensic Accounting field is in developing stage in India
2. There is lack of educated and trained forensic accountants.
3. If there is an involvement of politician in a financial fraud case, then it will be difficult to investigate such cases.
4. Due to new economic reforms of 1991, foreign investors have increased in India. It is difficult to proceed foreigners who involved in financial fraud.
5. Due to continuous development and adoption of new technology in financial fraud, it is difficult to investigate by forensic accountant.
6. As per company Act, 2013 the appointment of auditor is compulsory whereas Forensic Accountant is not compulsory in a Company.
7. Lack of specific guideline or legislation on forensic accounting in India.

This branch of accounting has not got due recognition in India even rapid increase in complex financial fraud/crimes has been reported. The work of Forensic Accountants is done by CA (Chartered Accountants) who usually take part in traditional auditing practices under the Companies Act, 2013. The CA or CWAs are best suited for forensic accounting profession as they have acquired well knowledge and skills during their training, which can be further enhanced by providing post qualification or diploma degree in Investigation and Forensic Accounting practice.

This branch of accounting has not got its due recognition even after alarming increase in the complex financial crimes and lack of adequately trained professionals to investigate and report on the complex financial crimes. The task of Forensic Accountants is handled by Chartered Accountants who apart from handling traditional practice of auditing under the Companies Act, 1956 or Income Tax Act are called upon by the law enforcement agencies or the companies or private individuals to assist in investigating the financial crime or scam. The CA or CWAs in India are best suited for this profession due to their financial acumen acquired during their rigorous training which can be further honed by introducing post qualification degree or diploma in Investigating and Forensic Accounting. The CA or CWA who acquire post qualification in Investigative & Forensic Accounting can use the designation CA-IFA or CWA-IFA and be legally recognized as the Forensic Accounting Expert to handle the investigation of financial crimes and give expert testimony in the Court of Law.

However, due to increase in financial fraud cases, Govt. of India set up Serious Fraud Investigation Office (SFIO) under Ministry of Corporate Affairs. This step of the central government can be regarded as first step to recognize the importance of forensic accounting in India.

SUGGESTION

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Some steps for the improvement of forensic accounting in India:

1. Reform judicial system and develop legislation or guideline for forensic accounting like auditing.
2. Develop skills and knowledge for forensic accountant. Conferences, seminars and training programmes can be organized to improve the skills and ability of traditional accountants in forensic issue.
3. Update academic curriculum, Higher education institution should integrate forensic accounting knowledge.
4. Like auditors, it should be mandatory to recruit a forensic accountant in the company of public sectors.
5. A regulatory body of forensic accounting should be set up to regulate the role, duties, responsibilities and power of forensic accountant in India.
6. There should be training institute for forensic accountants.

CONCLUSION

Forensic Accounting plays an important role in detecting and preventing financial frauds. Forensic Accounting knowledge need to be improves in India. It should be integrated as part of Indian academic curriculum at undergraduate and post-graduate level. This will enhance the awareness and knowledge of forensic accounting in India, and it will help to increase forensic accountants in the country. As a positive signal for forensic accounting profession in India, SEBI has decided to create forensic accounting cell, which will help to improve the quality of financial information disclosed and to detect financial irregularities. Also RBI has made forensic accounting audit compulsory for banks in India.

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