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# Forensic Accounting: Improve Skillset and Forming Regulatory Body for Forensic Accountants in India

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**Abstract**

Forensic accounting is barely a new field, but in present years the increased in number of frauds and the helplessness of the professionals to combat them have brought the Forensic Accounting in the limelight. Forensic accounting is the province practice area of accounting that designates engagements which result from actual or anticipated litigation. Forensic accounting is very important mechanism to detect, investigate and prevent the frauds. In order to identify and prevent financial frauds and white-collar crimes Forensic accounting is creating use of various tools. Forensic Accountants are currently in great demand, with the public need for honesty, fairness and transparency in propagation and increasing exponentially. These Forensic accountants need accounting, finance, law, investigative and Research skills to identify, interpret, correspond and prevent fraud. As more and more companies look for forensic accountants and professional institutes offer certifications in the area, it is becoming apparent that the forensic accountant has a skill set that is very different from an auditor or a financial accountant. In India unfortunately it is being used as an exploratory tool, rather than a proactive tool. If forensic auditing is made mandatory in various sectors, many of the scams can be controlled. It has been suggested that appointment of forensic accountant should be made compulsory in public sectors and large-scale companies for the sustainable development of the country.

**Keywords**: Forensic Accounting, Scams, Investigative skills, Forensic Accounting Tools.

## Introduction

Forensic Accounting is a simply assessment of evidence. Forensic accounting is the speciality exercise area of accounting that explains engagements, which result from real or predicted litigation. The word forensic accounting can be divided into two parts, Forensic and Accounting.

Forensic means connecting to, or used in courts of law or public debate or argument.

Accounting means language that offers information about the financial situation of an organization.

According to American Institute of Certified Public Accountants (AICPA): Forensic accounting is the application of accounting principles, theories and regulations to facts or hypothesis at issues in a legal dispute and comprehends every branch of accounting knowledge.

To make it simple, the assimilation of

- Accounting skills
- Auditing skills and
- Investigative skills generate the speciality known as forensic accounting.

Forensic accounting is used for fraud inspection and fraud examination covers fraud allegations from inception to disposition, including obtaining confirmation, interviewing, writing reports and testifying.

In the current scenario the emphasis is on the forensic accounting as the public deals with financial collapses, increased white collar crime and increasing occurrences of occupational fraud.

Forensic accounting affords investigative functions and litigation support services to understand the depth and width of the financial scams happening in any economy.

India's image on confronting corruption has not improved with Transparency International's Corruption Perception Index (CPI) placing it at 94$^{th}$ rank out of 176 nations.

Frauds, in the different sectors like bank, insurance, stock market, cyber world etc, need a sharp scientific instrument, for investigation and clearance of disputes.

The term Fraud essentially comprises using deceptiveness to dishonestly make a personal gain for oneself and or crate a loss for another. Although the legal definitions of fraud may vary from country to country, most are based around these general themes. Examples of fraud commonly include activities such as theft, corruption, conspiracy, embezzlement, money- laundering, bribery and squeezing.

## Objectives of the study:

- Highlighting the problems so as to improve future predictions of Forensic Accounting and its importance in India.
- To determine the extent to which financial and economic crimes have affected on the Indian economy and the effectiveness of forensic accounting functions.
- To understand the historical perception of forensic accounting in India.

## Historical Perspective of Forensic Accounting in India

Recent cases of fraud and monetary scams in India require more professionalism in accounting and finance. Investigative audit has always been there, it is only the techniques involved that has been changing in line with difficulty of the financial fraud involved (Krancher,2006).

Maurice E. Peloubet who coined the term Forensic Accountant in 1946 essay Forensic Accounting: its place in Today's Economy, Archaeological findings reveal that, during 3300-3500 BC, accountants of their day in Egypt were involved in the avoidance and detection of fraud. During 188 close relationships developed between accountancy and legal profession. Many modifications to financial statement disclosure can be attributed to frauds in corporate. In 1930's America's Eliot Ness was credited to bring down gangster

AI Capone, but his case was based on the investigative work done by Emer Irey, an accountant with the Internal Revenue Service that ensured capone's conviction for tax avoidance. He was probably America's first high- profile forensic accountant. But in Indian framework history of investigative accounting goes back to ancient times of Mauryan Times. Kautilya was the first person to mention the famous forty ways of embezzlement in his famous Kautilya arthashastra.

As pointed out by Black (2010), Financial statement fraud was a contributing factor to the recent financial crisis and it threatened the competence, liquidity and safety of both debt and capital markets. Further- more, it has very significantly improved uncertainty and instability in financial markets, shaking investor assurance worldwide. It also reduces the credibility of financial information that investors use in their investment decisions (Rezaee and Kedia,2012).

Chartered Accountancy firms which provide the Forensic Accounting services are as follows:

- ✓ Shared Joshi Chartered Accountants who investigated the Delhi based Xerox fraud case
- ✓ Deloitte
- ✓ Ernst and Young
- ✓ Price Water House Coopers
- ✓ KPMG

In order to control the increasing financial fraud cases, scams Government of India has established three four agencies that warfare frauds as follows:

1. SFIO (Serious Fraud Investigation Office) It is formed by Government of India under Ministry of Corporate Affairs which looks after frauds in the areas of Income tax, FEMA, RBI etc.
2. CBI (Central Bureau of Investigation) It has its specific wing to deal with the financial frauds called as Economic Offenses Wing control.
3. CVC (Central Vigilance Commission) It takes care of the professional frauds such as corruption. It has developed the Forensic Cell which takes care of the Banking frauds governed by RBI and financial frauds are covered by SEBI.

## Scope and Importance of Forensic Accountants

- ✓ Fraud detection where employees commit fraud
- ✓ Criminal Investigation
- ✓ Matters related with professional negligence
- ✓ Arbitration service
- ✓ Settlement of Insurance claims
- ✓ Dispute settlement

## Problem Identification:

1. With sluggish economy and struggling stock market there has been in increase in % frauds in following manner:
a. Money Laundering 12%
b. Occupation Frauds 49%
c. Cyber Frauds 2%
d. Bank Fraud 30%
e. Stock Market Fraud 8%
f. BPO Fraud 3%
2. Due to digitalization of the records, it is difficult to maintain accounting and audit trail.
3. Due to complex and traditional Judicial and political system it is difficult to seek the information.
4. No specific control system is influenced by the management which results in fraudulent financial statements.
5. According to Kessler International study:
a. 39% companies are in need of adoption of Forensic Accounting
b. 18% companies are not assisted
c. 15% companies are not aware of the Forensic accounting.
6. No specific guidelines are prepared for adoption of Forensic accounting.
7. Model should be prepared for continuous audit based on the probability of fraud detection based on the perception of fraudsters seeking perceived opportunity to commit fraud.
8. As per Sarbanes Oxley Act, Internal Financial Control Report should be prepared.

## Various Scams in India

| Year and type of scam | Amount | Scam Reason |
|---|---|---|
| Harshad Mehta 1992 | Rs. 4000 crores | Stock exchange |
| VP NHRM 2008 | Rs. 10000 crores | Siphoned funds kept for Rural Immersion |
| Ketan Parekh 2008 | Rs. 1500 crores | Stock exchange |
| Satyam scam 2009 | Rs. 8000 crores | Falsified revenues |
| 2G spectrum 2010 | Rs. 175000 crores | Irregularities in License issued on first cum first basis, no auction. |

| | | |
|---|---|---|
| Common wealth games 2010 | Rs. 10000 crores | Misuse of funds, public funds raised for infrastructure(construction) |
| Indian coal allocation 2012 | Rs. 186000 crores | No auction in allotment of Blocks. Falsified data to losses framed to CAG |
| Fodder scam 2012 | Rs. 950 crores | Embezzlement by falsification in Expense reports |
| VVIP Chopper deal 2013 | Rs. 362 crores | Acceptance of bribe and jurisdiction discipline |

## Tools and techniques used for the purpose of Forensic Accounting

➢ Theory of Relative Size Factor (RSF): The relative size factor test is an operative test for detecting errors. This test highlights all the possible fluctuation. It measures the ratio of largest number to the second largest number in the given set. Higher the difference specifies higher chances of occurrence of fraud and error.

➢ Computer Assisted Auditing Tools (CAAT): Computer assisted audit techniques is an automated tool to perform audit process.

CAAT are used by the auditors to perform various auditing procedures such as,

✓ Testing details of transactions and balances,
✓ Identifying inconstancies or significant fluctuations,
✓ Testing general as well as application control of computer systems,
✓ Sampling programs to extract data for audit testing, and
✓ Redoing calculations performed by accounting systems.

➢ Data Mining Techniques: It is a set of supported techniques designed to automatically mine large volumes of data for new, hidden or unexpected information or patterns.

➢ Ratio Analysis: Data analysis ratios for key numeric fields are also a useful technique used for forensic accountants to detect the frauds.

## Suggestions

New legislative body should be made in order to make Forensic Accounting a part of day-to-day auditing and accounting practices. Roles, responsibilities, duties and powers of Forensic accountant should be outlined by the regulatory body. Prosecution for fraudsters should be done by keeping in mind the framework or model applicable to users of fraudulent practices in IT. This model should act as a powerful tool to prevent the occurrence of frauds.

✓ Conferences, seminars and training programs need to organized to enhance skills and ability of professional accountants regarding Forensic issues.

✓ There is further scope of research in this field if this subject is integrated into the academic curriculum.

✓ Traditional judicial system should be abolished which is free from Red Tapism and bureaucracy.

✓ SEBI and RBI should create cell for Forensic accounting in field of corporate crimes and financial offences respectively.

✓ Software should be developed to make a test run of all the tools and techniques as stated.

✓ AICPA and other International professional bodies have already adopted Forensic Accounting since 1995 and hence the review of their practices can be done in order to prepare a model of Forensic Accounting in India.

✓ Participation of midsized Chartered Accountancy firms in work of Forensic Accounting should be done with Big five so as to increase the importance of the same and hence to reduce the chances of occurrence of fraud and error.

## Conclusion

To conclude Forensic accounting as a correction is an interesting area and can be highly useful to both the society and the investigator. However, it is related to note here that only persons of such skills and courage with an attitude to know the secrecy can be successful in the procedure of forensic investigation. With increase in the use of computers in accounting and auditing there are more chances of occurrences of the fraud. The check list can be prepared as and when the accounting is done by the management and there should be accuracy and detailed trail of each and every transaction. Investigators act as sniffer dogs but if disclosure is transparent and authentic then the chances of frauds would reduce. Further research can be done to find the combination of the subject outline for the academicians and also investigative skills and model to the accountants so as to have forensic accounting as preventive measure rather than to have it as investigative tool.

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