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ijmrset@gmail.com



www.ijmrset.com



Forensic Accounting in Indian Perspective: A Review

Dr. Mahima Gupta

Assistant Professor-A.B.S.T. , SD Govt College, Beawar, India

ABSTRACT: Forensic accounting is upcoming trend in Indian accounting field, forensic accountant is differ from other accountant, while other accountant look at the number but forensic accounting look beyond the number, it involves integration of investigation ,auditing, accounting skills to proceed in legal matter. It came to limelight in India after corporate frauds and white collar crimes; however there is difficulty in adopting it and lack of awareness among people regarding forensic accounting. Forensic accounting is used for fraud examination and fraud examination covers fraud allegations from inception to disposition, including obtaining evidence, 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 growing occurrences of occupational fraud. Forensic accounting provides investigative functions and litigation support services to understand the depth and width of the financial scams happening in any economy.

The objective of the study is to understand the significance of forensic accounting in the wake of recent financial scams in India and to highlight the problems of forensic accounting in India. This paper is conceptual in nature and information is collected from the secondary sources. In India due to the complex and traditional judicial system, political compulsion etc., forensic accountants are facing the challenge of gathering information against „big shots“ that is admissible in the court of law. It has been suggested that appointment of forensic accountants should be made mandatory in public sector and large scale companies. Forensic accounting is an essential tool in the emerging economic scenario to discover or investigate financial crime and the path of justice, providing strategic information on the evidence found related to financial crime. It is a new area, but in recent years, the use of forensic accountants has increased banks, insurance companies and now even police. Increased white collar crime Forensic accounting is an essential tool for discovering or investigating financial crime and the direction of justice in the emerging economic scenario, providing strategic information on the facts found in connection with financial crime. With the growing complexities of business and commercial operations, the financial irregularities also increases because of the mindless obsession with profit maximization at any cost when carried to any extreme can lead to failures like ENRON, WORLDCOM, SATYAM has extreme negative impact on the survival and growth of any economic entity. But there are no appropriate conventional accounting and auditing procedures that can provide absolute assurance in preventing and detecting all fraudulent financial reporting.

As a mechanism to detect and prevent corporate frauds and scams, forensic accounting has emerged as a relatively new and effective tool in the hands of accountants to find out mistakes and malpractices in accounting world. Forensic accounting in India has come to limelight only recently due to rapid increase in white-collar crimes and the belief that our law enforcement agencies do not have sufficient expertise or the time needed to uncover frauds. This paper focuses on the conceptual framework, various provisions and applicability of forensic accounting in investigating corporate frauds and scams in India. The fundamental objective of GAAP states that the financial statements must depict ‘true and fair’ view of the financial state of affairs. The ambiguity of ‘true and fair’ view created a loophole towards the rise of financial frauds, thereby weakening the trust of the users of financial information on the reported statements. Unbridled increase in the financial reporting irregularities, corporate frauds, and the ‘white-collar’ crimes has popularized the concept of forensic accounting in India. Forensic accounting, an integration of investigation and accounting, is an art and science of detecting and preventing financial frauds. The present research is exploratory and theoretical in nature and attempts to highlight the scope and modus operandi of forensic accounting in the backdrop of rising corporate frauds in India. The research largely makes use of secondary sources of data and the previous literature on forensic accounting, along with the experts’ views on the same. In a nutshell, the research suggests immense possibilities for forensic accounting to assume a separate ‘niche’ and provides opportunities for forensic experts to offer litigation support, investigative accounting, and consulting services. There is an urgent need to regularize the forensic accounting movement by the government and recognized accounting bodies in India.



I. INTRODUCTION

Frauds and losses appearing in the financial performance have a negative impact on the financial reporting. The users and economic decision makers lose their trust in the accounting and auditing profession itself when these phony reporting takes place, which lead to the need of investigation in these fields and this grounds the naissance of Forensic accounting. In Indian context the need for forensic accounting developed because of the increase in white collar crimes such as Satyam, common wealth games, etc. Forensic accounting is a specialized field of accountancy which investigates scams and frauds and analyze financial information to be used in legal proceedings in the court. It uses auditing, accounting and investigative skills to conduct investigations into fraud and theft by way of investigative accounting and litigation support. The main aim of paper is to discuss scams, frauds and their investigation as well as to create awareness about the necessity and role of forensic accounting and forensic accountant in development and betterment of the Indian economy.[1]

All information is collected from secondary data. The paper also tries to provide framework for forensic accounting and the methodology in which forensic accounting is conducted. The rise of financial scams in India especially in governmental sector requires that forensic auditing should be made mandatory as the current statutory audit are not in the state of in depth audit which is required to detect the financial scandals which have become a real threat against the development agenda for developing and emerging nations like India. Economic and accounting scandals and scams have become a global concern in recent times. Financial frauds and crimes are old concepts in the world, but their solution forensic accounting is a relatively new one. Fraud, as all of us know, is the wrongful act of deception done willingly for a personal, or to be more specific, financial gain; and the answer to this deep-rooted problem is forensic accounting which is the use of accounting skills to investigate fraud and financial crimes. During the last few decades, there have been numerous financial frauds and scandals, which acted as milestones with lot of historical significance. Financial scam has become a real threat against the development agenda for developing and emerging nations. Forensic Accounting is very helpful for the Indian Government to solve this problem. In India, there is no awareness of forensic accounting in many companies. This paper aims to highlight just that.

The paper also clears the misconception regarding what kind of motives form a base for fraud and gives an insight to the profession and life of a forensic accountant. In this paper, techniques, growth, reasons, fraud cases and others important aspects of forensic accounting also discussed for conclusion. In short, a forensic accountant is a bloodhound of accounting, not a watch dog. In the present scenario, accounting has been diversified in many domains such as cost accounting, management accounting, human resource accounting, social accounting and even green accounting. With the introduction of this concept, FBI's announcement in the 1990s significantly revised the detection of fraud, particularly white collar scams Forensic accounting is mainly the composite of three pre-requisite skills namely auditing, accounting and investigative skills. The suitability of these skills, together with expert witnessing and various other litigation services is the primary function of forensic accountability. In short, it is a question of proving or contesting the fraudulent claim. The person who exercises these skills to prove or disprove fraud in court proceedings shall be called a forensic accountant. The services provided by forensic accountants include Analyzing, interpreting, summarizing and

- presenting complex financial and business transactions in an obvious and simple manner. They also analyze the evidence before them and
- use computerized applications to help them present this evidence. They even identify the basic documents to
- protect the case. They also evaluate all information from
- accounts to prepare an effective statement of disposition or testimony. They even review and evaluate the disposition
- testimony or the accounting reports from the other party. To know the real loss or commercial damage
- through their models for insurance companies as well They also play a crucial role in determining the • real income of both the spouses in divorce cases to the jury. They also help to determine the damage caused[2]
- to the environment using their damage model. Forensic accountants in the corporate world perceive and expose white collar scams, which are complicated in nature and difficult to present.

To further understand forensic accountants, we must detect the importance of detecting white collar scams. Like any other wistfulness, the rate of scams with white collars is increasing worldwide. Since these scams are increased daily, aversion can be detected in recognition of these scams. These scams are really very intricate to detect and measure; which is not covered by the media for many reasons. This usually involves large amount of money and impinge on significant portion of public. There is a highly secretive risk of scams with white collars compared with scams with blue collars. In addition, the cost measurement of white collar scams is not uniform in nature and in different situations



is measured differently. In this context, a forensic accountant is extremely important; where the accountant has the task of verifying all accounts and preparing documents without a preconceived idea.

II. DISCUSSION

The term Forensic Accounting was first used by Maurice E. Peloubet in 1946 in his essay "Forensic Accounting: Its Place in Today's Economy." During 3300-3500 BC, Archaeological studies show that accountants of Egypt were involved in the prevention and detection of fraud. A close relationship was being developed between accountancy and legal profession during the 18th century.[3]

The following are a few major milestones in forensic accounting:–

- 1942: Maurice E. Peloubet distributed "Forensic Accounting: its place in today's economy."
- 1982: Francis C. Dykman composed "Forensic Accounting: The Accountant as an Expert Witness."
- 1986: The AICPA issued Practice Aid # 7, delineating six zones of case administrations – harms, antitrust examination, accounting, valuation, general counseling, and investigations.
- 1988: Association of Certified Fraud Examiners set up
- 1988: another class of criminologist books where the Forensic bookkeeper was the star.
- 1992: The American College of Forensic Examiners was established.
- 1997: The American Board of Forensic Accountants was established
- 2000: The Journal of Forensic Accounting, Auditing, Fraud, and Taxation were established.

In India, Kautilya was the first person who used this term to mention the famous forty ways of misappropriation in his famous book Kautilya Arthashastra.

Forensic accountant

According to Justin Pope, "Forensic accountants inhabit a cloak and dagger corner of the accounting world. Their job: respond at a moment's notice when a client spots trouble – anything from procurement fraud to a top executive cooking the books to industrial espionage." [5]

Forensic Accountant's work is to search and compile financial evidence and develop a computer application to oversee the information collected and to communicate their findings within the frame of reports or presentations. He may also be asked to prepare visual aids to bolster trial evidence. He can be an expert witness, a consultant, or play other roles such as referee, arbitrator, or mediator. [4]

III. RESULTS

Forensic Accountants can be engaged in Public Practice or employed by insurance companies, banks, police forces, government agencies and other organizations.

- (i) Criminal Investigations: Practicing forensic accountants could be called upon by the police to assist them in criminal investigations which could either relate to individuals or corporate bodies. The forensic accountant would use his/her investigative accounting skills to examine the documentary and other available evidence to give his/her expert opinion on the matter. Their services could also be required by Government departments, the Revenue Commissioners, the Fire Brigade, etc for investigative purposes.
- (ii) Personal Injury Claims: Where losses arise as a result of personal injury, insurance companies sometimes seek expert opinion from a forensic accountant before deciding whether the claim is valid and how much to pay. (iii)
- (iii) Fraud Investigations: Forensic accountants might be called upon to assist in business investigations which could involve funds tracing, asset identification and recovery, forensic intelligence gathering and due diligence review. In cases involving fraud perpetrated by an employee, the forensic accountant will be required to give his/her expert opinion about the nature and extent of fraud and the likely individual or group of individuals who have committed the crime. The forensic expert undertakes a detailed review of the available documentary evidence and forms his/her opinion based on the information gleaned during the course of that review.
- (iv) Matrimonial Disputes: Solicitors often need the services of forensic accountants in divorce cases involving disputes about matrimonial assets. Assignments of this sort might require the forensic accountants to trace, locate and evaluate assets. Such assets, for instance, might technically be owned by a business in which one of the parties to the divorce case has a share. The assets would need to be accurately valued to ensure equity when splitting the divorcing couples' assets and liabilities.
- (v) Professional Negligence: The forensic accountant might be approached in a professional negligence matter to investigate whether professional negligence has taken place and to quantify the loss which has resulted from the negligence. A matter such as this could arise between any professional and their client. The



professional might be an accountant, a lawyer, an engineer etc. The forensic expert uses his/her investigative skills to provide the services required for this assignment.

- (vi) Expert Witness Cases: Forensic accountants often attend court to testify in civil and criminal court hearings, as expert witnesses. In such cases, they attend to present investigative evidence to the court so as to assist the presiding judge in deciding the outcome of the case.
- (vii) Mediation and Arbitration: Some forensic accountants because of their specialist training they would have received in legal mediation and arbitration, have extended their forensic accounting practices to include providing Alternative Dispute Resolution (ADR) services to clients. This service involves the forensic accountant resolving both mediation and arbitration disputes which otherwise would have been expensive and time consuming for individuals or businesses involved in commercial disputes with a third party.
- (viii) Litigation Consultancy: Working with lawyers and their clients engaged in litigation and assisting with evidence, strategy and case preparation. (ix) Computer Forensics: Assisting in electronic data recovery and enforcement of IP rights etc.[5]

Financial scams have a habit of cropping up with an alarming regularity in the Indian financial system. In the present article author has compiled a list of ten leading financial scams in India, which have affected a large population of investors, and involved huge sums of money. They managed to shake the very foundations of our financial system, and were driven by that most basest of human instincts “Greed”. In most cases, it was the greed of just one individual, or a very small group of individuals, who managed to pull off such huge scandals.

- (i) Insurance Scam: This scam had originated and prospered in the period immediately following Independence in 1947. At that time, the insurance sector was not nationalized, and a handful of private companies ruled the roost. These companies were more concerned with providing benefits to selected industrialists, and ignored the interests of the common man. The government responded by nationalizing the insurance sector, and the LIC was founded under a special Act passed by the Parliament. This scam laid the foundation of the nationalization culture in India.
- (ii) Securities Scam: This is perhaps the most well known of all financial scams probably because it happened in a highly visible period economic reforms had just been started in 1991. Harshad Mehta was quick to understand the weaknesses of the banking system, and exploited these weaknesses to the hilt. He managed to procure huge amounts of money using the so called “Ready Forward” deals, and used this money to purchase large amounts of shares at hugely inflated prices. He earned the sobriquet of “Big Bull” due to this penchant. Later, the banks got a clue of his shady deals, and demanded their money back. The house of cards collapsed, and the rest, as they say, is history.
- (iii) CRB Scam: This scam took place in the years 1992-1996, the period immediately following the Harshad Mehta fallout. This makes the scam even all the more daring and surprising. CR Bhansali, the perpetrator of this scam, floated more than 100 companies, such as CRB Mutual Funds and CRB Capital Markets. The primary purpose of these companies was to attract huge funds from the public by promising high rates of interest. This interest was later paid from further borrowings, and so on. In 1995, the stock market collapsed, and this proved to be the undoing of CR Bhansali. He was investigated, and later arrested. After a brief 3 months stint in jail, he has disappeared without a trace, and nobody is asking.
- (iv) UTI Scam: The UTI scam involved the flagship US-64 scheme of UTI, which was meant to channel the funds of small investors into instruments bearing high returns. Gradually, US-64 developed an investor base of around 2 crore investors. The economic liberalization in India, coupled with the absolute opacity in the operations of UTI, led to a situation wherein the Government was forced to announce a huge bailout of about Rs 3,500-4,000 crores in an order to prevent default in payments to the investors. The consequences of such a situation are unimaginable. But the story does not end here. Later, it turned out that the UTI Chairman appointed at this time, Mr P S Subramanyam, along with a couple of executive directors, acted wrongly to selectively benefit a powerful coterie of brokers and industrialists, while at the same time, jeopardizing the interest of lakhs of small investors.
- (v) Home Trade: Around the year 2000, a finance portal emerged on the financial landscape, and gained quick recognition on the back of endorsements by personalities like Hrithik Roshan, Sachin Tendulkar and Shahrukh Khan. The portal, owned by Sanjay Agarwal, claimed to deal in gilts. Soon, RBI got suspicious of activities of some cooperative banks in the gilt market, and a scam was uncovered. The same old saga brokers and bankers combining to rob people of their hard earnings were repeated. Funds from Seaman’s Provident Fund and PPF were affected. The total scam size

- was reported to be around Rs 300 crores, and more than Rs 200 crores were spent on publicity costs alone.
- (vi) Securities Scam: That our system never learns its lessons was proved by this scam. Ketan Parkekh, a qualified CA, and a stock broker, identified a number of stocks (popularly called the K-10), and took up huge positions in these. For this purpose, he used a large number of Benami accounts and smaller stock exchanges, such as the Kolkata and Ahmedabad stock exchanges. He also borrowed heavily from banks such as Global Trust Bank and Madhavpura Mercantile Cooperative Bank. Unfortunately, he was stuck in a bear cartel, and was soon pounded to pulp on the stock exchange. The extent of the scam was estimated to be around Rs 1,500 crores.
 - (vii) Fake Stamp Papers: This scam promised to be the mother of all scams in India, with the initial reports quoting a figure of Rs 30,000 crores as the scam size. Later, RBI clarified that this figure was “rather exaggerated”, and the “correct” figure was around Rs 200 crores. Again, this scam exposes how the India system works – Mr Abdul Karim Telgi, the scam kingpin, paid bribes to get access to the security press in Nasik, where stamp papers and currency notes are printed. He later used this knowledge to print fake stamp papers. At the height of the scam, Telgi’s network spanned 14 states, 125 banks and more than 1,000 employees.
 - (viii) DSQ Software: Though this scam was modest in terms of money involved (only Rs 600 crores), and did not affect the general public to a great extent, yet it is notable for how it came into being. The main player in the scam was Mr Dinesh Dalmia, who was the MD of DSQ Software Ltd. This company issued around 1.3 million shares in 2001, and these shares were allotted to four companies on a preferential basis. NSDL, a stock depository, dematerialized and helped in delivering the shares. Nothing wrong in that, except that the shares were not even listed on any stock exchange.
 - (ix) IPO Scam – A number of key operators, including corporate stock brokers such as Karvy and Indiabulls, were involved in the IPO scam that spanned the years 2004 – 2005. The modus operandi was simple – the operators would open thousands of fake accounts to purchase shares in IPOs, in the hope of selling later at huge profits. A spate of IPOs issued during this period was heavily oversubscribed due to this scam, sometimes by as much as 40 times.
 - (x) Satyam: On a cold January morning in 2009, Ramalinga Raju, chairman of Satyam Computer Services, admitted to falsification in the company accounts and various other irregularities, and sent a chill down the collective spine of the Indian financial system. Coming on the back of the global recession, this incident promised to bust the Indian outsourcing industry and the stock market, but for some deft bailout work by the government. The matter is still under investigation and litigation, and the true extent of the scam will be known in the future, perhaps. Mr Raju himself had admitted to irregularities worth around Rs 12,000 crores.[6]

IV. CONCLUSION

Forensic accounting in India has come to limelight only recently due to rapid increase in Frauds and the white collar crimes and the belief that our law enforcement agencies do not have sufficient expertise or the time needed to uncover frauds. A large global accounting firm believes the market is sufficiently large to support an independent unit devoted strictly to „forensic“ accounting. Therefore, forensic accountants are currently in great demand, with the public need for honesty, fairness and transparency in reporting increasing exponentially. These forensic accountants need accounting, finance, law, investigative and research skills to identify, interpret, communicate and prevent fraud. However, as the incidence of white collar crime (fraud, bribery and corruption, money laundering etc) continues to increase, demand for the services of the forensic accountant looks set to grow.[7,8]

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In the emerging economic scenario, forensic accounting is an essential tool for uncovering or inquiry of financial crime and the direction of justice, providing decisive information about the facts found related to financial crime. It is a new area, but in recent years, banks, insurance companies and even police have increased taking help of forensic accountants. The increase in white collar crime and the difficulties faced by law enforcement agencies in uncovering fraud 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 courses on forensic auditing in India In the emerging economic scenario, forensic accounting is an essential tool for uncovering or inquiry of financial crime and the direction of justice, providing decisive information about the facts found related to financial crime. It is a new area, but in recent years, banks, insurance companies and even police have increased taking help of forensic accountants. The increase in white collar crime and the difficulties faced by law enforcement agencies in uncovering fraud 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 courses on forensic auditing in India



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