

WESTERN INDIA REGIONAL COUNCIL OF THE
INSTITUTE OF COMPANY SECRETARIES OF INDIA

Forensic Audit & Fraud Detection

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Focus Areas

- Forensic Audit
- Need for Forensic Audit
- Assignments undertaken
- Techniques used
- Tools used

Focus Areas (Contd...)

- Fraud Examination
- Types of frauds (Some examples)
- Causes of Frauds
- Fraud Detection & Prevention

Forensic Audit

- **Forensic**, according to the Webster's Dictionary means, "Belonging to, used in or suitable to courts of judicature or to public discussion and debate."
- "An audit is an "independent examination of financial information of any entity, whether profit oriented or not, irrespective of its size or legal form when such an examination is conducted with a view to express an opinion thereon."
(Wikipedia).

Forensic Audit (Cont'd)

- **Forensic Audit** is a structured examination of the financial records of a business entity in an investigative manner to find out the evidence that can be used for legal proceedings in court. It is one step ahead of an internal audit, and the person who conducts such an audit should know the law and legal frameworks and have expert knowledge of accounting and auditing. (Wall Street Mojo).
- A forensic audit is an examination of a company's financial records to derive evidence which can be used in a court of law or legal proceeding. (Corporate Finance Institute.com)

Advantages of Forensic Audit

- Uncovering Frauds
- Fraud Identification and Prevention
- Formulation of Economic Policies
- Sound Business Decisions

The above is an illustrative list

Need for Forensic Audit

- Investigative Accounting
- Litigation Support

Investigative Accounting

- Conflicts of Interest / Corruption.
- Asset Misappropriation.
- Financial Statement Frauds
- Review of the factual situation and provision of suggestions regarding possible courses of action.
- Assistance with the protection and recovery of assets.

Investigative Accounting (Cont'd)

- Co-ordination of other experts, including:
- Private investigators;
- Forensic document examiners;

Litigation Support

- Assistance in obtaining documentation necessary to support or refute a claim.
- Review of the relevant documentation to form an initial assessment of the case and identify areas of loss.
- Assistance with Examination for Discovery including the formulation of questions to be asked regarding the financial evidence.
- Attendance at the Examination for Discovery to review the testimony; assist with understanding the financial issues and to formulate additional questions to be asked.

Litigation Support (Cont'd)

- Review of the opposing expert's damages report and reporting on both the strengths and weaknesses of the positions taken.
- Assistance with settlement discussions and negotiations.
- Attendance at trial to hear the testimony of the opposing expert and to provide assistance with cross-examination.

Assignments undertaken

- Criminal Investigations
- Stakeholders' and Ownership Disputes
- Insurance and other claims
- Business related Fraud Investigations
- Professional Negligence

The above is an illustrative list

Need for Forensic Audit

Failure of auditors to detect fraud :

- Auditors are normally considered as coast guards of the financial ocean of the country.
- Auditors perform an extensive job under the given guidelines, but when it comes to fraud detection, the liability normally is fixed upon the management of the organisation.
- Auditors normally go through the audit process mechanically (Form over substance). They usually see what is shown to them.
- Auditors work on a materiality concept, thus in case an item does not have an impact on the financial statements, they are generally skipped from the audit process.
- Audit is normally based on assumptions.

Fraud Examination

- **Fraud** is the crime or offense of deliberately deceiving another in order to damage them – usually, to obtain property or services unjustly. [1] Fraud can be accomplished through the aid of forged objects. In the criminal law of common law jurisdictions it may be called "theft by deception," "larceny by trick," "larceny by fraud and deception" or something similar.
- **Examination**, according to the American Heritage Dictionary means, " the act or art of examining" i.e., "to observe carefully or critically; inspect" or "to study or analyze" an issue."
- **Fraud Examination** is the thorough study, inspection or analysis of an issue relating to fraud

Types of Frauds

- Corporate Frauds
- Banking and Financial Frauds
- E - Commerce
- Online Frauds
- Securities Frauds
- Employment Frauds

The above is an illustrative list

Corporate Frauds

❖ Frauds by Corporates

- Statutory Violations (Income Tax, Excise, Customs etc.)
- Defrauding Vendors / Customers
- Manipulating Financial Statements
- Defrauding Banks
- Defrauding Shareholders

The above is an illustrative list

Corporate Frauds

❖ Frauds Against Corporates

- Employee Frauds
- Conflicts of Interest / Corruption.
- Asset Misappropriation.
- Database Hacking
- Connivance with Vendors / Customers
- Misrepresentation by Ex employees
- I P Rights Infringements

The above is an illustrative list

Banking and Financial Frauds

- Stolen / Fake Cheques
- UPI
- Website Cloning
- ATM Frauds
- Booster Cheques
- Fraudulent bank applications
- Phishing and Internet

The above is an illustrative list

E-Commerce

- Coupon Frauds
- Payments
- Deliveries
- Fake promotions

The above is an illustrative list

Online Frauds

- Fake Reviews and Referrals
- Phone
- Fake Website
- Social Media Ads
- Crypto / Gaming

The above is an illustrative list

Causes of Frauds

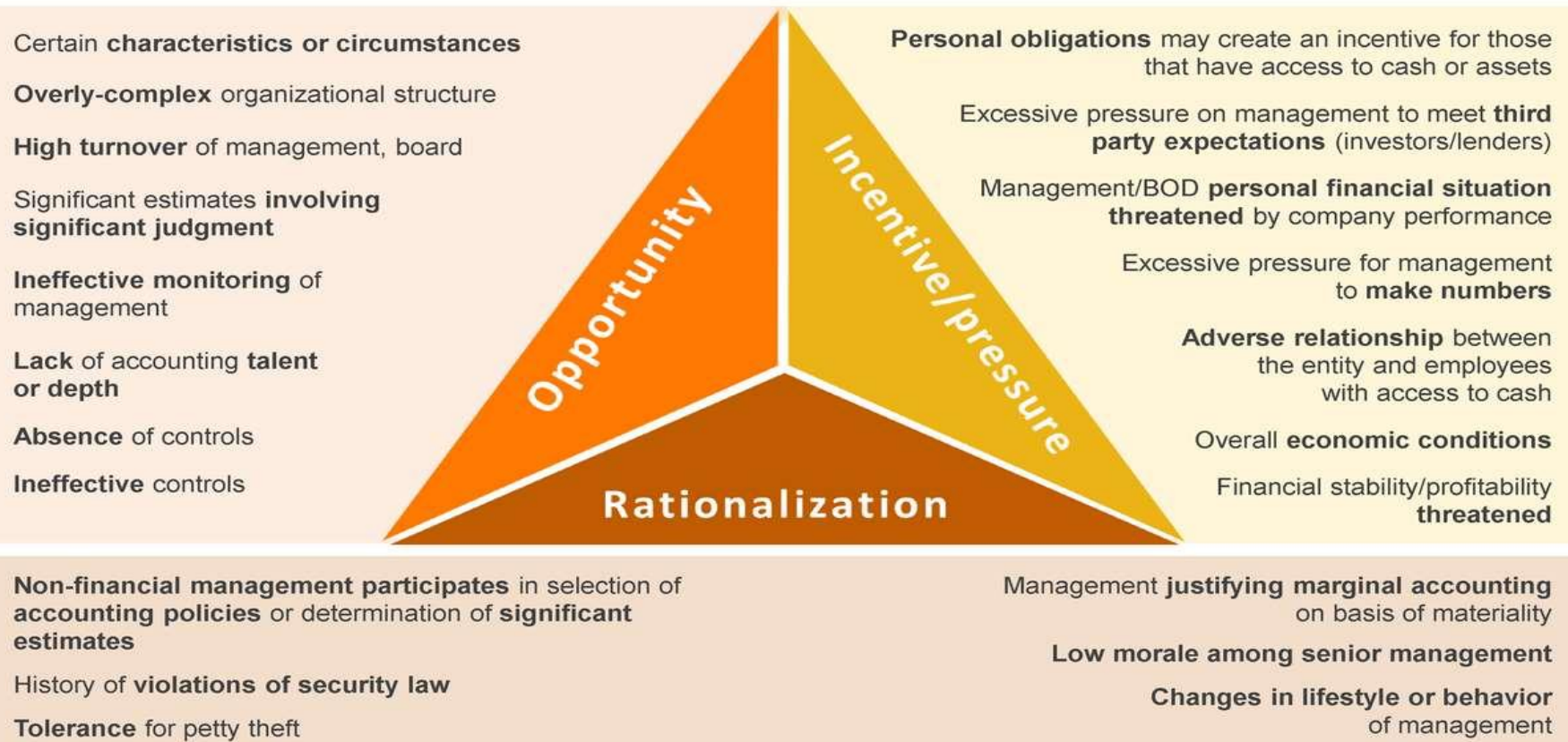
Fraud Triangle

- Incentives / Pressures
- Rationalisation
- Opportunity

Causes of Frauds

Fraud triangle

Fraud risk factors are commonly depicted as a triangle broken up by incentive or pressure, perceived opportunity and rationalization. Examples of each are shown below.



Fraud Detection



Layers

Base Layer Accounting Knowledge.

Middle Layer Knowledge of auditing, internal controls,
risk assessment and fraud detection.

Top Layer Knowledge of the legal environment and
strong communication skills.

Procedure

- Planning
- Interviewing
- Evidence
- Reporting

Approach

Meeting the Client

To get a first hand understanding of the facts and issues involved, Identify parties, Quantify Loss

Perform a conflict check

This should be carried out once the parties are determined.

Perform an initial investigation

A preliminary investigation always helps in developing a proper plan of action and also helps in understanding the issues at hand in a better perspective.

Approach (Cont'd)

Develop an action plan

Clearly outline the objectives to be achieved and the ways and means to achieve them.

Obtain relevant evidence

Based on the nature of the case. Involves tracing documents, financial information, assets and property, persons, other relevant proofs

Approach (Cont'd)

Perform an Analysis

It depends on the nature and gravity of the case involved and would normally require summarizing a volume of data, calculating financial damages, tracing of assets, regression and sensitivity analysis, utilizing various tools and applications (Softwares).

Prepare a Report

The report should normally mention Nature and scope of assignment, methodology adopted, limitations of the scope and/or findings and/or opinions, various graphics, charts and schedules to present in a professional way and also to properly support the findings.

Skill Set Required

- Qualifications and Experience.
- Ability to go beyond the numbers and be analyse substance over form.
- Knowledge and command of all relevant legal provisions including Criminal and Civil and also well versed with the legal system and the court procedures.
- Ability to reconstruct past records.
- Ability to critically analyze financial statements.

Skill Set Required

- Proficiency in Information technology and computer applications.
- Knowledge of psychology in order to understand the thinking and motive behind criminal behavior and to set up prevention programmes that motivate and encourage employees.
- Curiosity, persistence and creativity.
- Confidence to maintain his composure when acting as a witness.
- A good professionally trained team to assist him in his work

Tools used

- Data Analysis Software
- Human Intelligence
- Computer Forensics
- Artificial Intelligence
- Legal Knowledge

Techniques used

Statistical Data Analysis

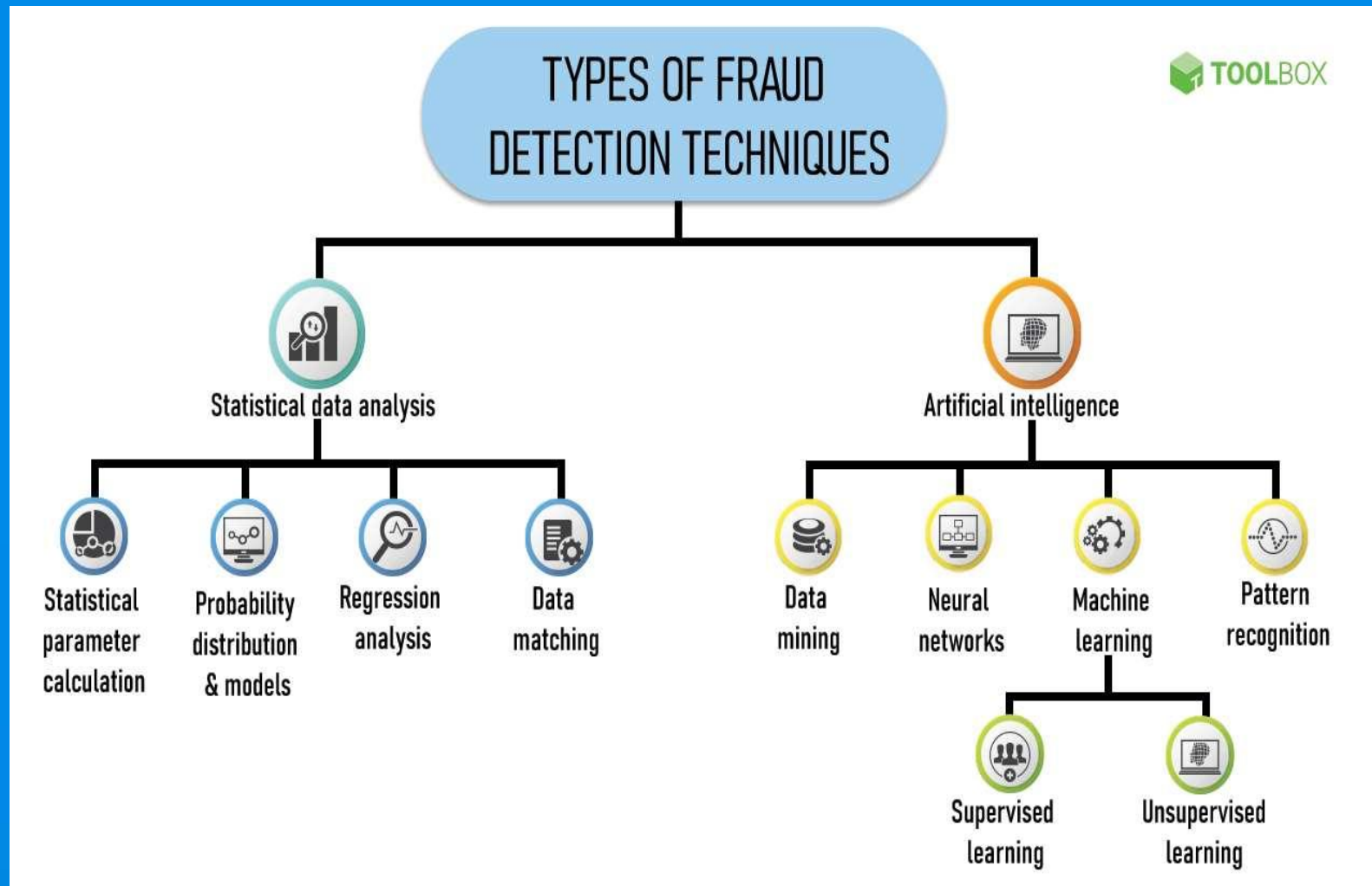
- Statistical Parameter Calculation
- Probability Distribution and Models
- Regression Analysis
- Data Matching

Techniques used

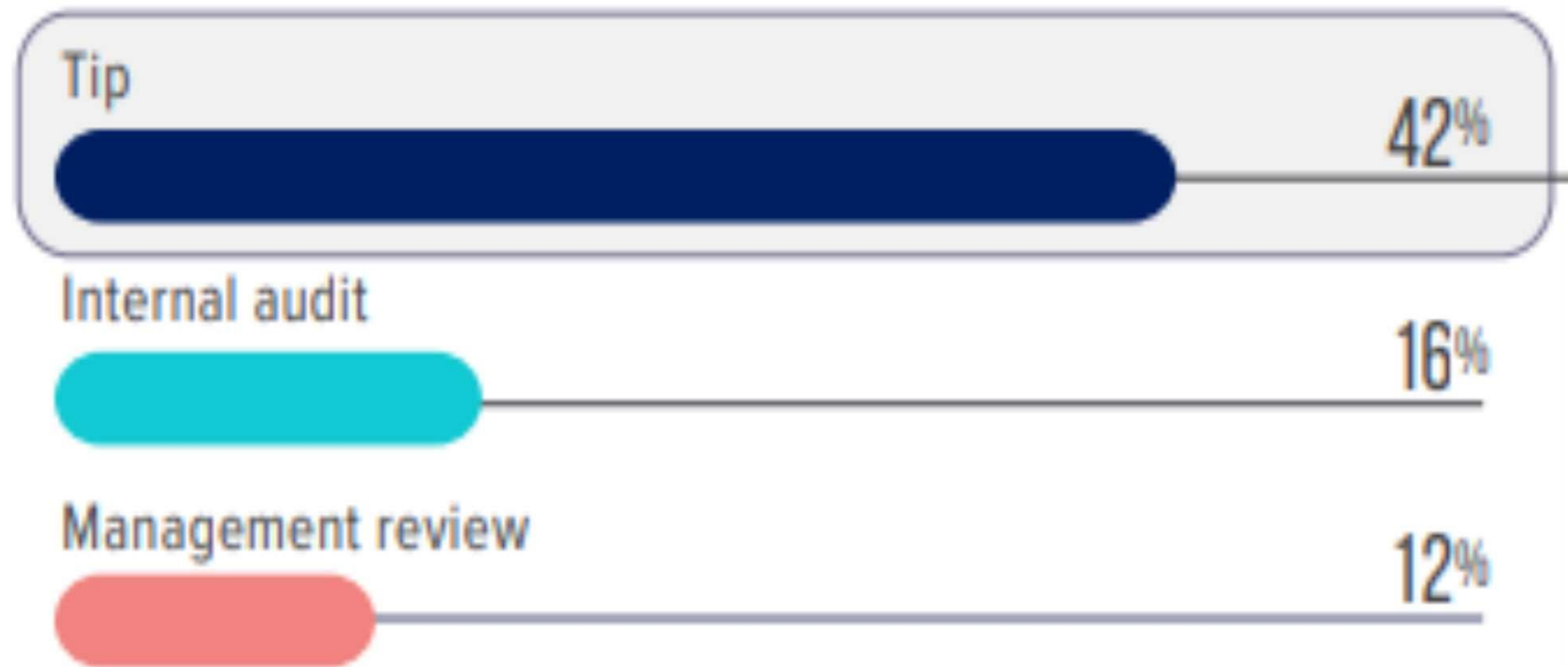
Artificial Intelligence

- Data Mining
- Neural Networks
- Machine Learning
 - Supervised Learning
 - Unsupervised Learning
- Pattern Recognitions

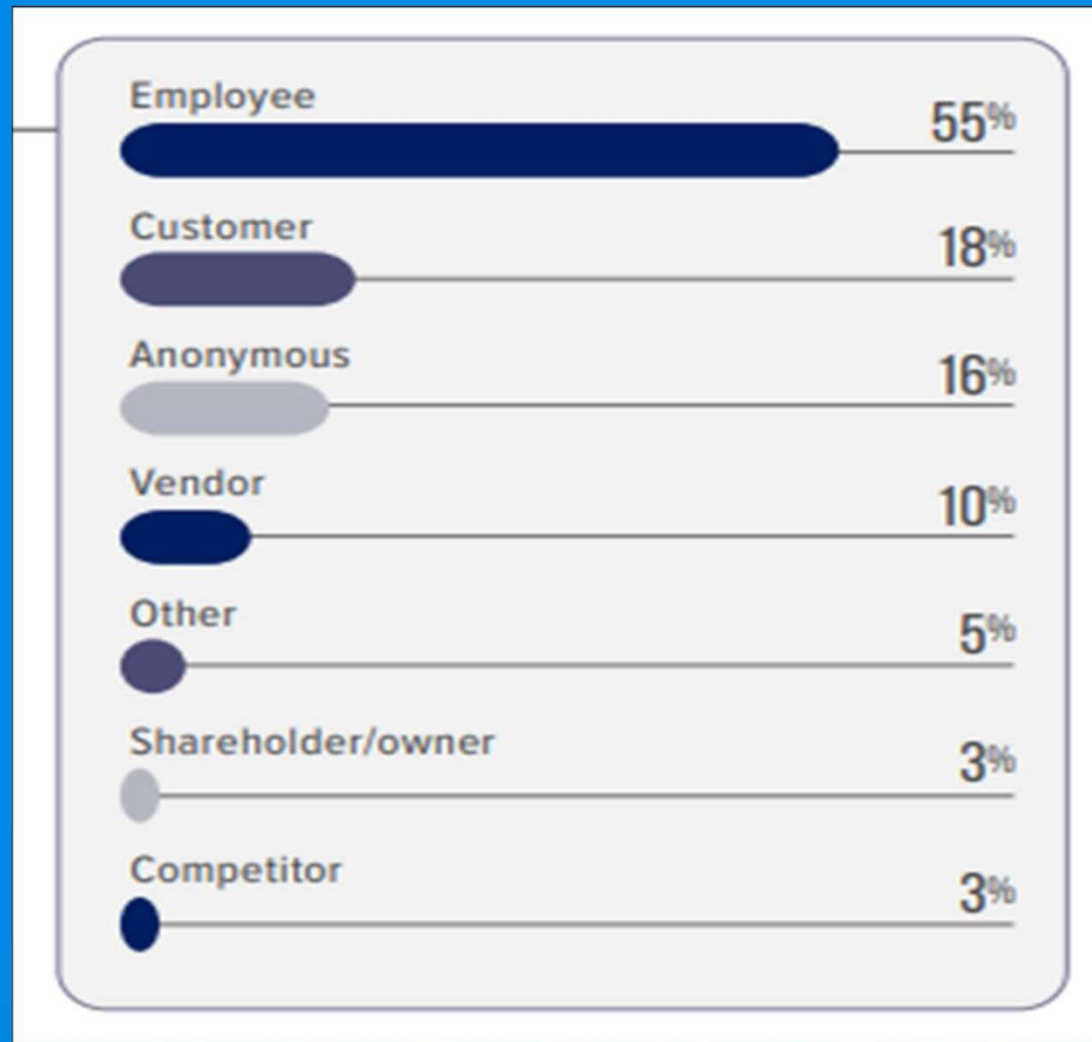
Techniques used



Fraud Detection



Fraud Detection (Cont'd)



Fraud Detection (Cont'd)

In 2022

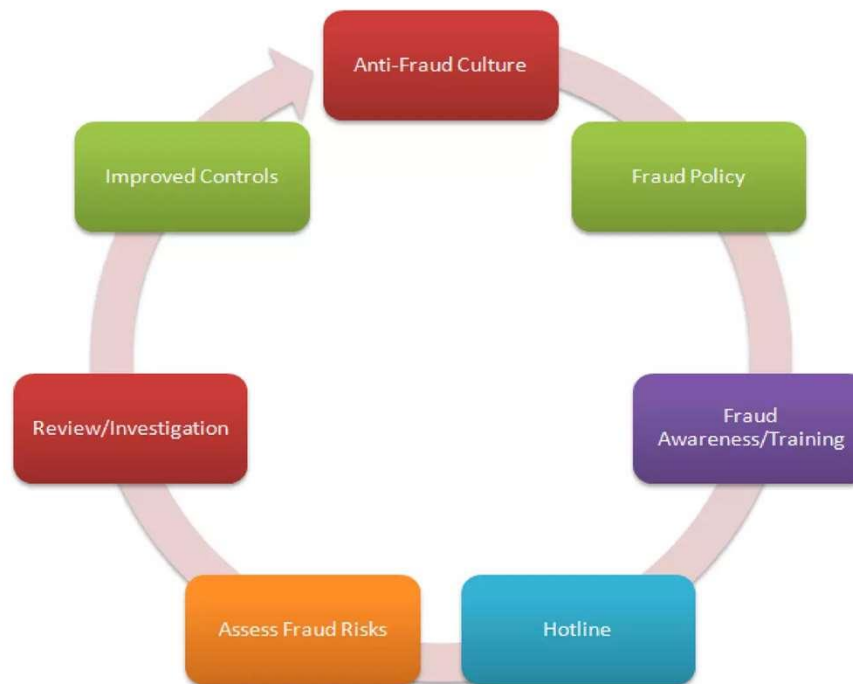
- 54% of fraud cases were discovered by tips or during routine reviews by management.
- 87% of fraudsters had no prior criminal history.
- 83% of fraudsters had no prior employment issues related to fraud.

Fraud Prevention

- Anti Fraud Culture
- Fraud Policy
- Fraud Awareness / Training
- Hotline
- Assess Fraud Risks
- Review / Investigations
- Improved Controls

Fraud Prevention

7 Keys to Fraud Prevention



Disclaimer

➤ The above presentation is compiled with data inputs and support from

- CA Mayur Joshi, Chairman, Risk Pro Research Centre.
- India Forensic Research Centre, Pune
- Wikipedia, the free encyclopedia
- Fraud Examiners Manual by ACFE, USA
- www.fraudaccounting.com
- www.corporatefinanceinstitute.com
- Investopedia.
- The Journal of Forensic Accounting

And ideas and inputs from various writers, friends and well wishers

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