

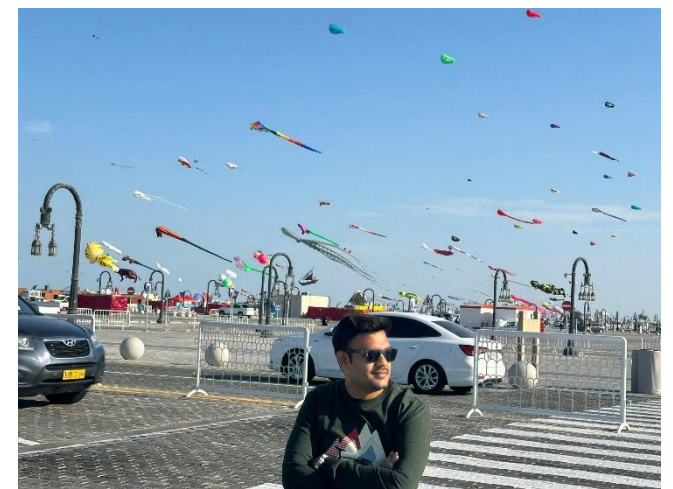
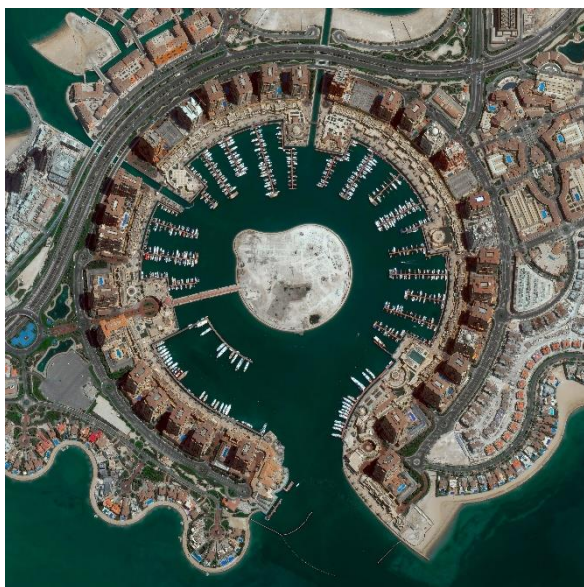


# Approach to Forensic Investigation

*ICAI Ahmedabad*

Sharing of experiences by CA Arpit Kabra, CCM Elect







# Collaborative Aggregators

Hello!



Please feel free to post your questions

All ~~stupid~~ questions are welcome

Keep making notes for  
reference...



*Green Flag*  
*Red Flag*

*Keep checking for these flags, its all about it ...*

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Forensic Audit and  
Frauds**



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**Background**



# Background - Forensic Audit

“Forensic” means “suitable for use in the court of law”.

It is the application of financial skills and investigative mentality to unresolved issues, conducted within the context of the rules of evidence.

As an emerging discipline, it encompasses financial expertise, fraud knowledge and a sound knowledge and understanding to business reality and the working of legal system. Simply stated, Forensic Auditing includes use of accounting, auditing and investigative skills to assist in legal matters

Forensic audit can be conducted in order to prosecute a party for fraud, embezzlement or other financial claims.

In addition, an audit may be conducted to determine negligence

A forensic audit is an examination of a firm's, entity's or individual's financial information for use as an evidence in court.

# Standards on Forensic Accounting and Investigation

Understanding the Nature of Engagement 110  
Understanding Fraud Risk-120  
Laws and Regulations 130  
Applying Hypotheses 140  
Engagement Acceptance & Appointment 220  
Using the Work of an Expert 230  
Engagement Objectives - 210  
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# Types of Audit

Basis of Distinction	Other Audits	Forensic Audits
Objectives	Express an opinion as to 'True & Fair presentation	Whether fraud has taken place in books
Techniques	Substantive & Compliance. Sample based	Investigative, substantive or in depth checking
Period	Normally for a particulars accounting period	No such limitations
Verification of stock, Estimation realisable Value of assets, Provisions, liability etc.	Relies on the management certificate / Management Representation	Independent/verification of suspected/ selected items where misappropriation is suspected
Off balance sheet items (like contracts etc.)	Used to vouch the arithmetic accuracy & compliance with procedures	Regulatory & propriety of these transactions/ contracts are examined

# Fraud as per various Statutes

Companies Act, 2013	• Section 447 of the Companies Act. 2013
Criminal Procedure Code, 1973 / Indian Penal Code, 1860	• Section 25 of IPC defines what amounts to fraudulently
Indian Contract Act, 1872	• Section 17
SEBI	• Regulation 11C empowers to investigate
Information and Technology Act, 2000	• Section 43 and Section 44 of IT Act
PMLA	• Section 3
Insurance Act, 1938	• Section 33
Income Tax Act, 1961	• Section 68, 69, 69A, 69B, 69C, 69D
RBI	• 35A of the Banking Regulation Act , Notification dated 1 July 16

# Corporate Frauds

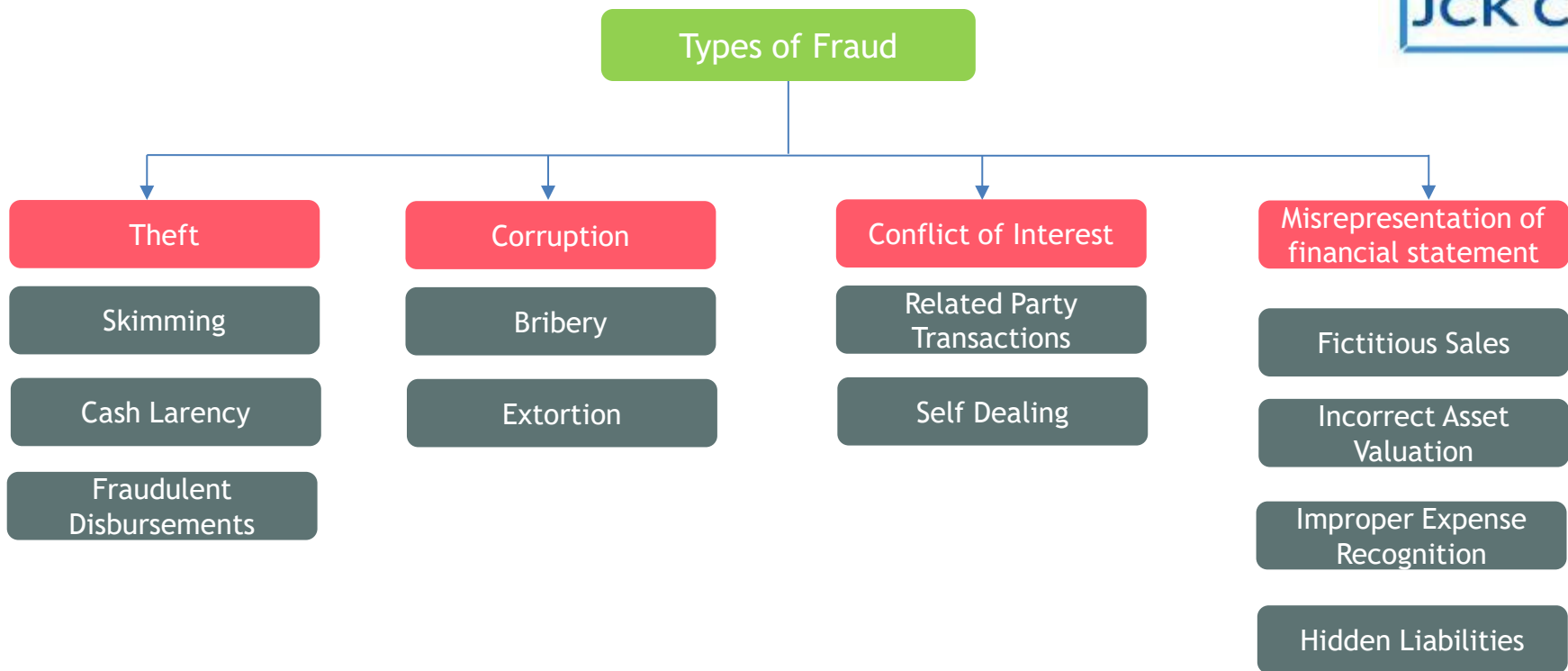


## Financial statement falsification

- ▶ Extending the depreciation period to delay depreciation recognition
- ▶ Shifting debt to special purpose entities.
- ▶ Accelerate the recognition of revenues and delay the recognition of expenses
- ▶ Capitalize expenses
- ▶ Counting non-existent inventory, which reduces the cost of goods sold

*Corporate fraud can be extremely difficult to contain and is essentially impossible to stop if senior management is willing to engage in it. In such cases, even the most robust control system can be breached.*





With an aim to promote better fraud risk management systems and framework in Regulated Entities (REs), on **15 July 2024**, the Reserve Bank of India (RBI) has issued three revised master directions on fraud risk management, which are applicable to banks, Non-Banking Financial Companies (NBFCs)

Instructions Issued by RBI\_using the powers u/s 35A of the Banking Regulation Act, “Master Directions on Frauds - Classification and Reporting by commercial banks” dated 01-07-2016

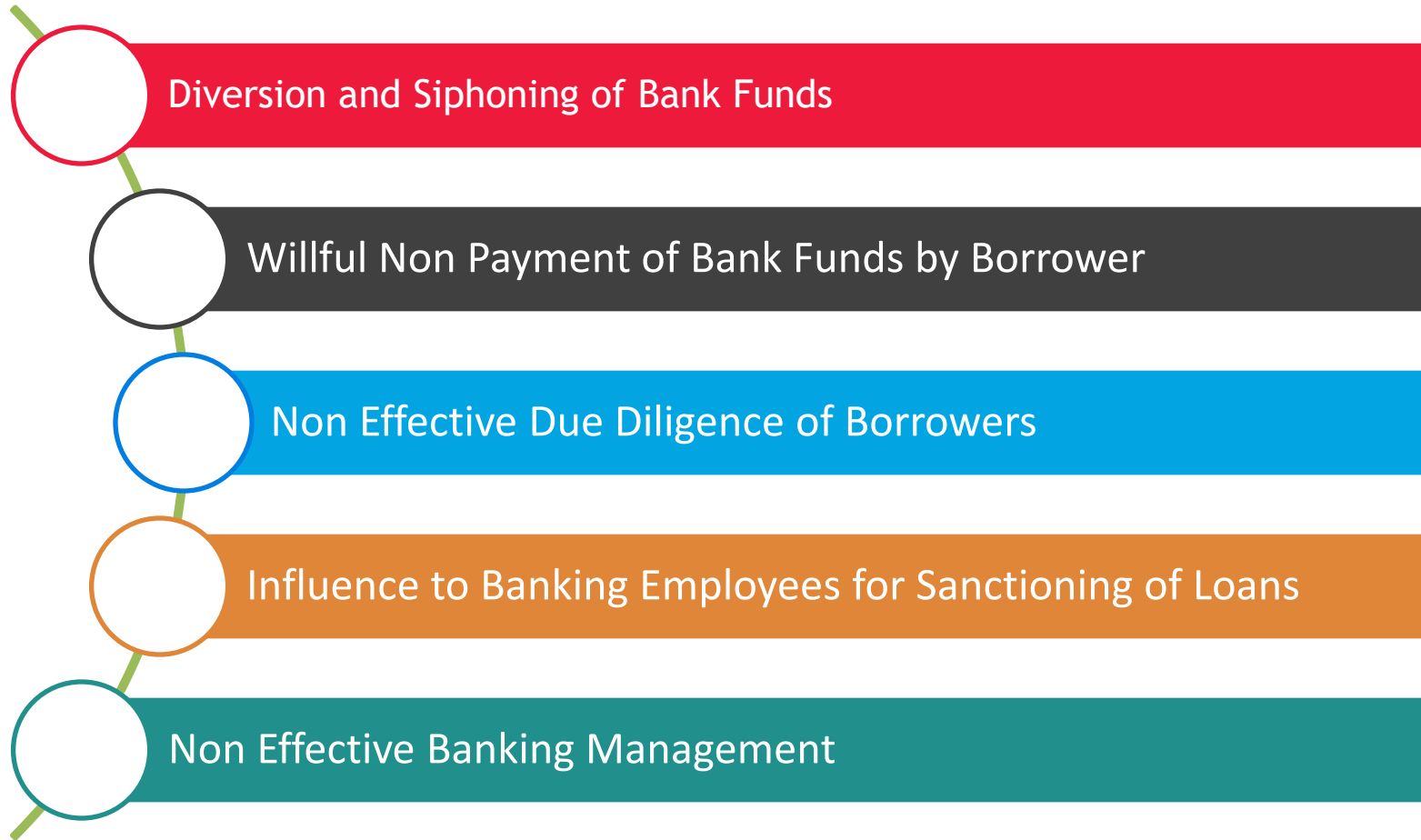
Master Directions on Frauds:

*“These directions are issued with a view to providing a framework to banks enabling them to detect and report frauds”*

# FRAUD RISK PRONE AREAS



# KEY REASONS FOR RISE IN BANK FRAUDS & NPA





# Ingredients for Fraud or *mischief*





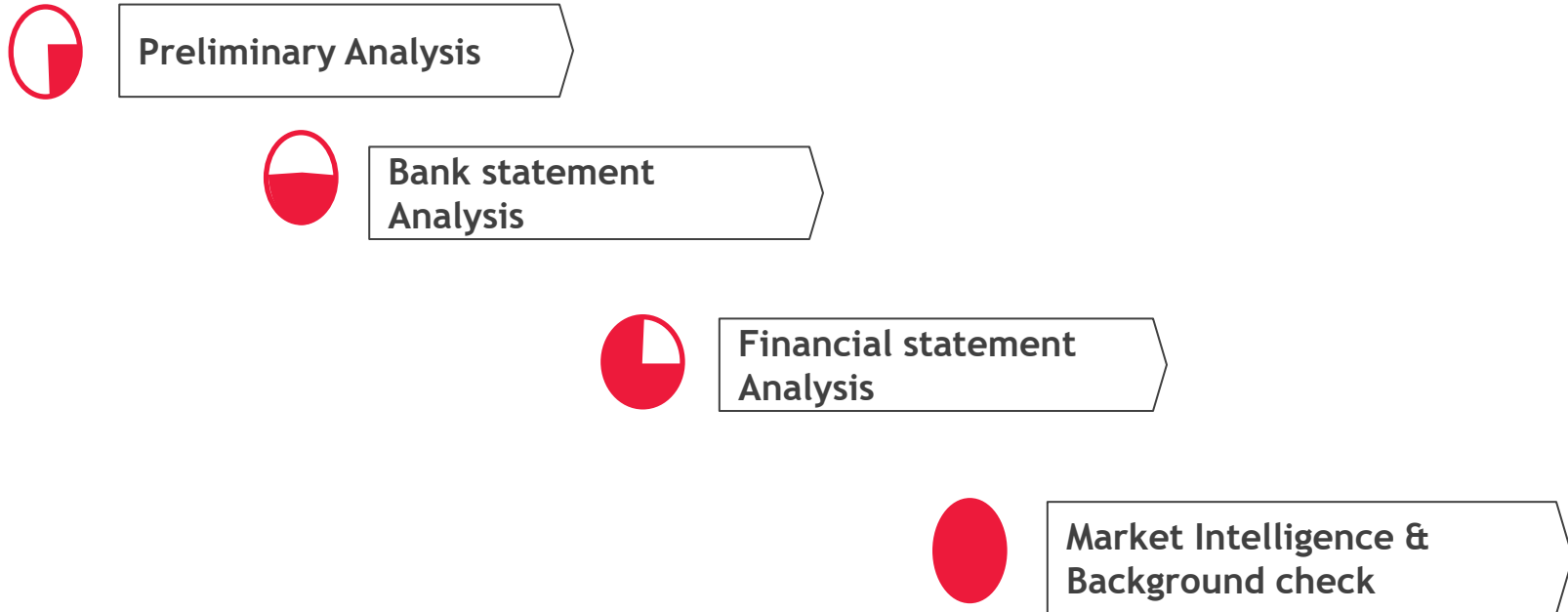
# **Approach to Forensic Accounting**

# Steps in Forensic Audit





# Bird eye view of Approach



## Typical results / outcome of the review



# 1. Initial Steps- Characters of the Story



## Company Profiling

- Company registration information
- Details of registered office
- Line of business
- Details of related companies/ associate co./subsidiary co.
- Various factory Location
- Shareholding pattern of the company
- Past and current directors of the company

## Preliminary Analysis

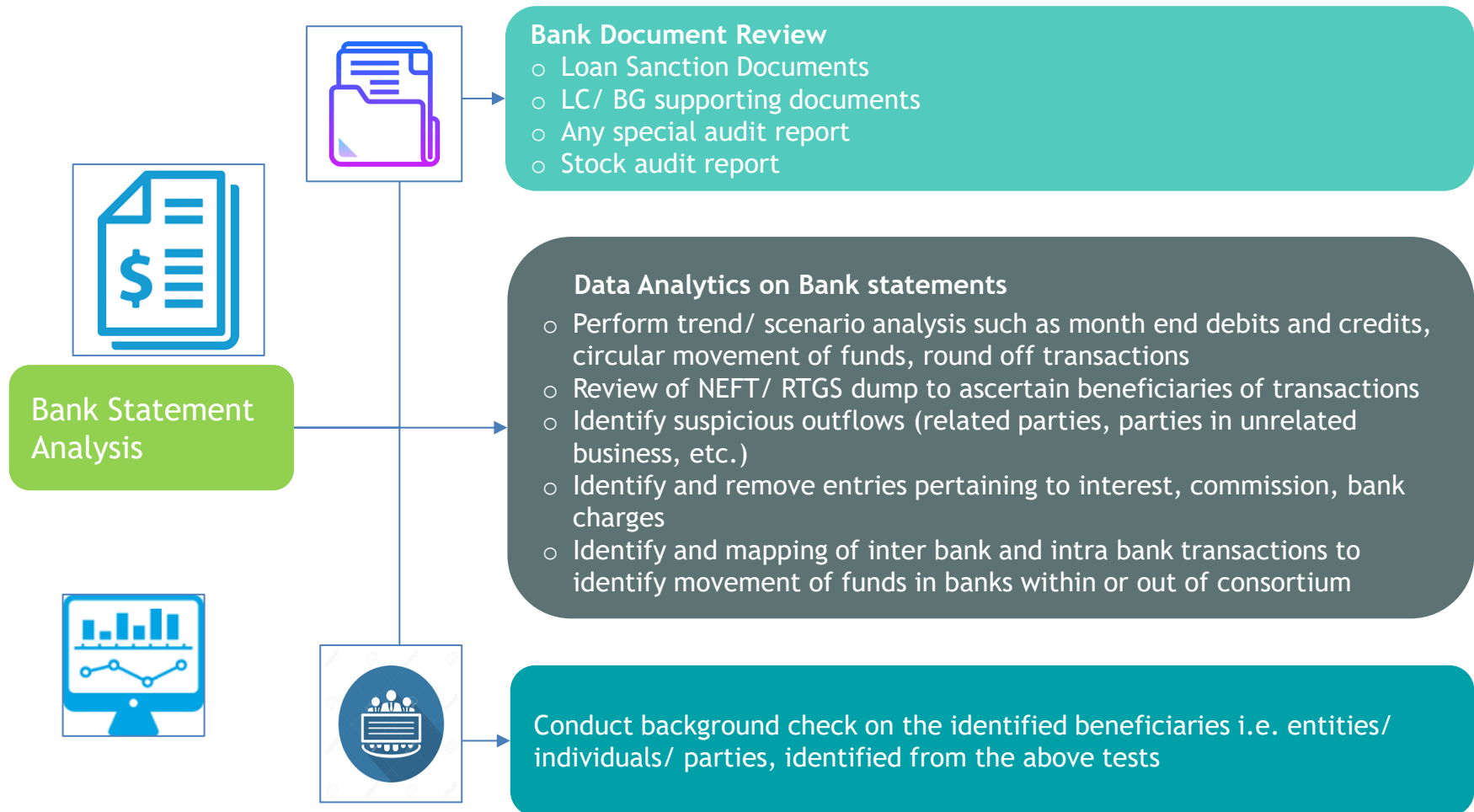


## Promoter - Promoter group & Directors Profiling:

- Preparation of family tree of promoter group
- List of the directorships held by the promoters group
- Basic background information of the companies in which the promoters hold directorship i.e.
  - ✓ company name,
  - ✓ registered address,
  - ✓ other directors of that company,
  - ✓ shareholders of that company and
  - ✓ details of related parties

This will lead to identification of key individuals and companies and set the tone of Characters in the Story !

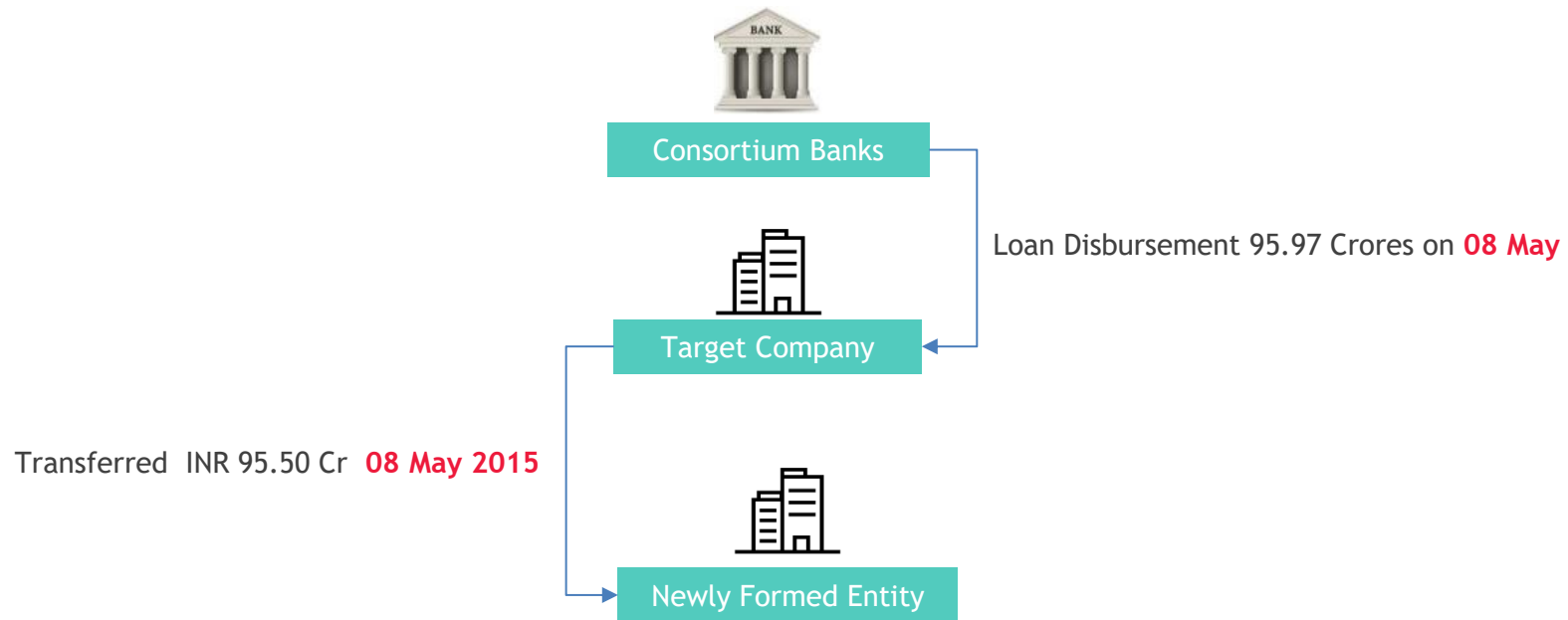
## 2. Beginning the Analysis- Bank st





# Bank st analysis

Bank statement analysis of the target company revealed that the funds disbursed by the bank on 8 May were immediately transferred to a newly formed entity having unrelated Line of Business



1. Incorporated in March 2015 with paid up capital of INR 1 Lakh
2. Incorporated just 2 months before the Bank Loan transaction date.
3. Directors of Newly formed entity are director A and B.
4. Registered Address same as Target company.

# 3. Financial statement Analysis

## Financial Statement Analysis

### Revenue & Debtors

- Growth % of debtors vis a vis revenue
- Export sales made to customers who have very less existence on public domain
- Domestic sales made to small proprietorship / partnership firms
- Perform analysis on Sales register to check concentration of sales.
- Mapping of transactions with related parties
- Identify major, long overdue and written off customer accounts from receivable data for the review period
- Find out Top 10 parties and check their credentials

### Purchases & Creditors

- Recurring purchases from single vendors without obtaining comparative quotations
- Sudden increase in expenses without corresponding change in revenues
- High amount of purchases from without credentials
- Machinery / Raw materials purchased which is relatively higher from market prices
- Plot Top 10 vendors
- Check their relationship with Debtors, indicating mere book entries etc
- Loans and Advances given to such Creditors

### RPT

- Related Party Transactions
- Review list of disclosed related parties/group companies
- Ascertain whether transactions have been entered at arms length
- Details of substantial debts raised in sister/associate/group companies Mapping of year on year unsecured loans given/ taken with actual receipts/ payments as per bank statements

### Cash & Bank

- Bank reconciliations have regular open items of same nature
- Large cash payments to contractors / vendors
- Large transactions of round amounts for movement of funds within different bank accounts

## 4. Public Domain Research and Investigation



### Market Intelligence & Background check

#### Discreet Source Inquiries

Gather information on business operations of target companies:

- vendors
- customers
- Current employees
- Ex-employees
- Factory Labour
- Identify ex employees, personnel connected with the company, relatives in the Industry line, known auditors and their employees, other CAs worked

#### Public domain Searches

To identify possible nexus between vendors, customers, employees and promoters identified from preliminary analysis, bank statement analysis and financial statement analysis to identify:

- Company registration details through MCA
- Line of business of these entities
- Relationship between the key personnel's of these entities and the target company
- Financial status of these entities through review of financial statement to identify following:
  - Net worth
  - PAT
  - Sales and purchases
  - Investments
  - Related party transactions

# Must do to learn about Forensic Accounting

learning.icaai.org/iDH/icaai/home

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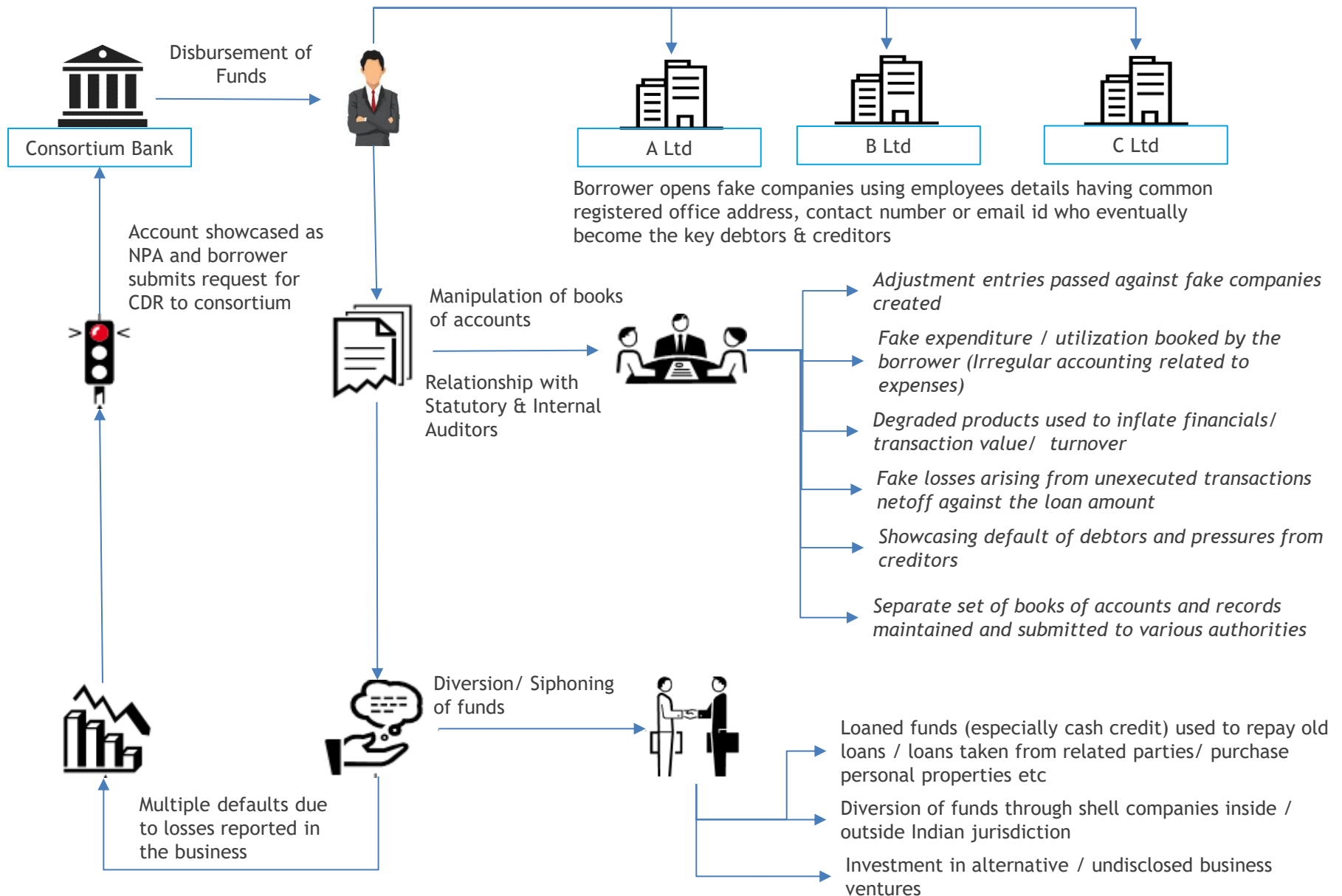
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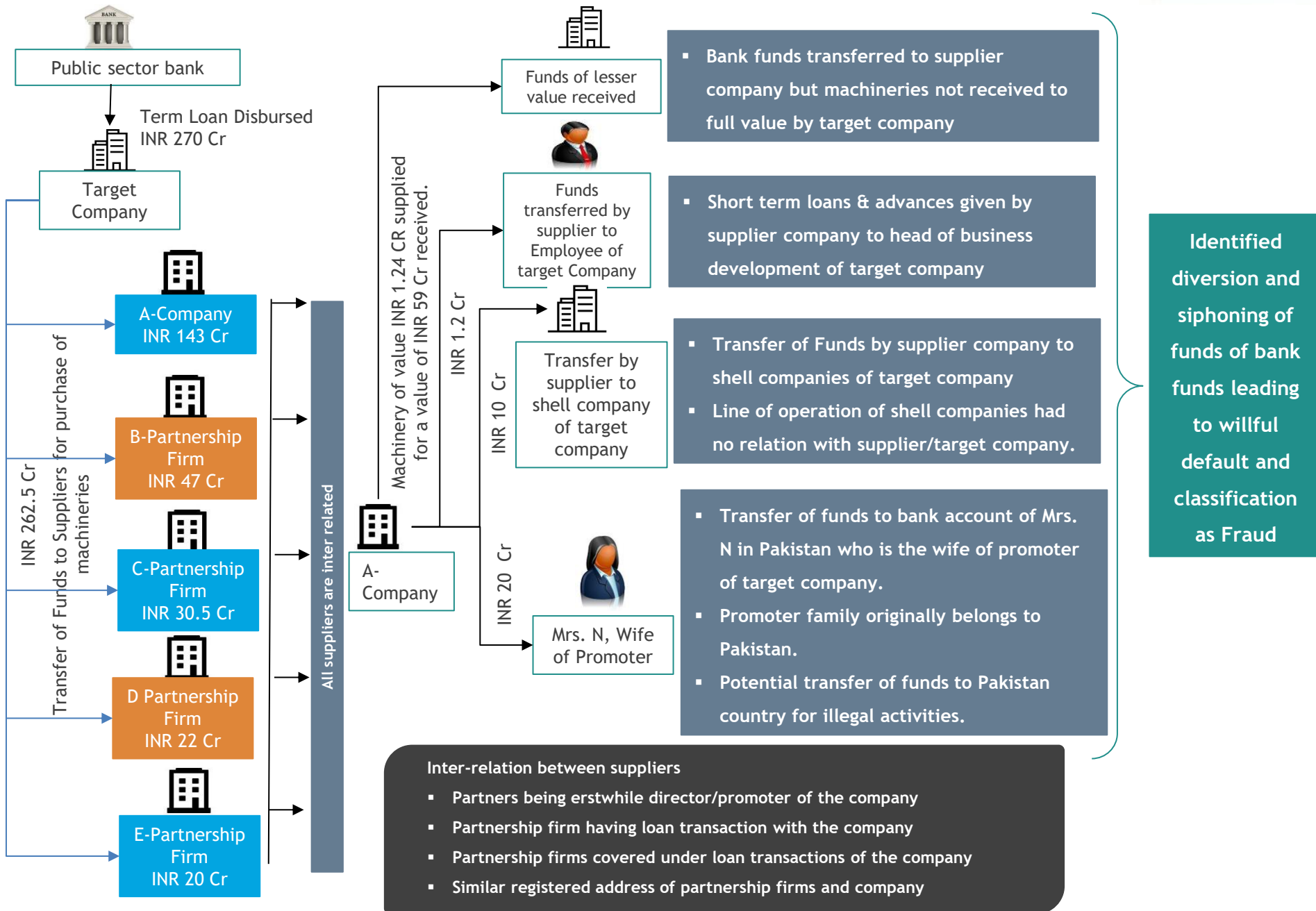
**How is it  
done ?**



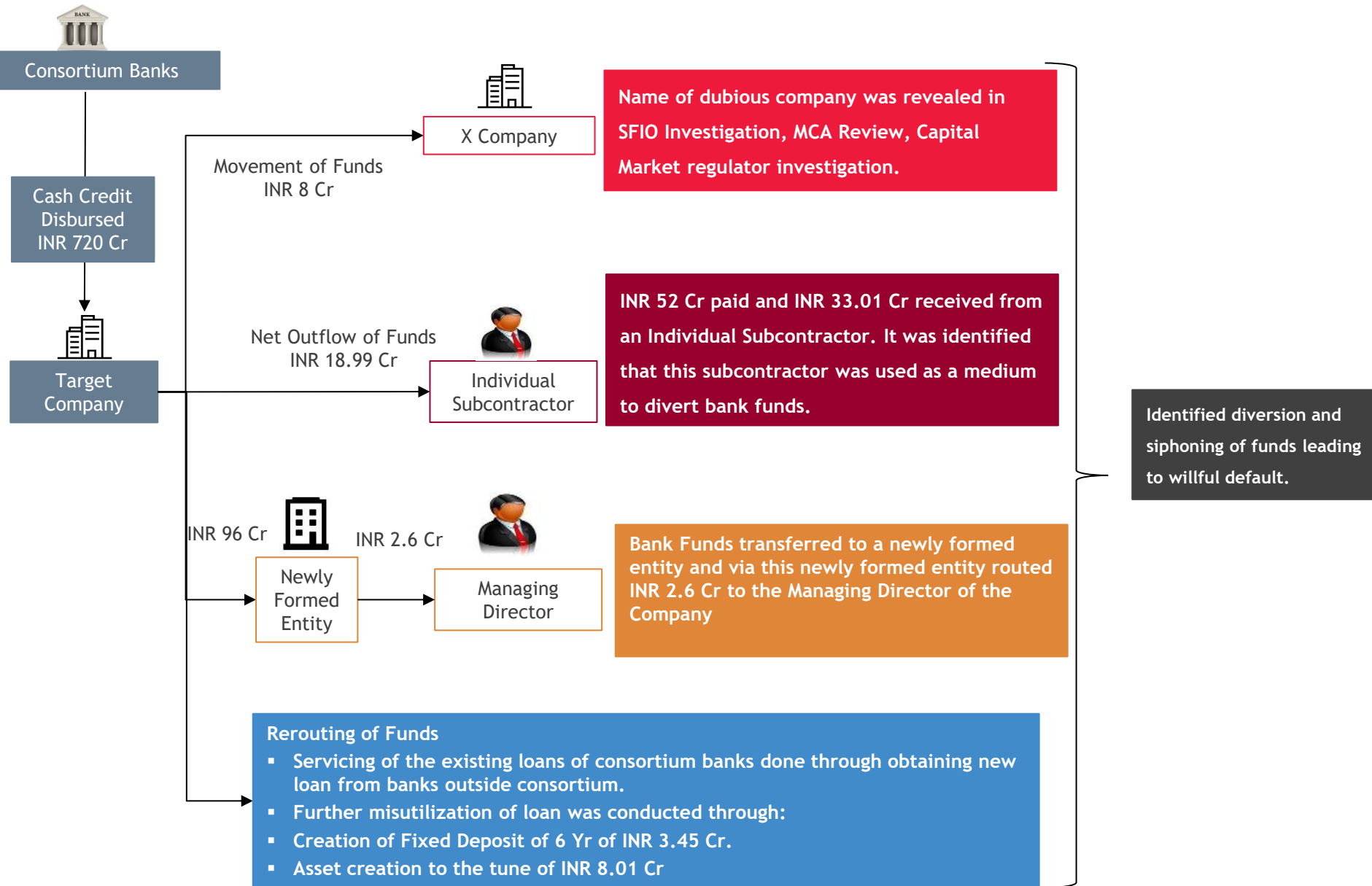
# Illustrative Modus Operandi



# Case study: Fact finding exercise for identifying diversion and siphoning of bank funds by a energy from waste company



## Case study: Fact finding exercise for identifying diversion and siphoning of bank funds by an Infrastructure company





**Key take  
aways !**

## Key- take aways\_ Accounting

- a) **Going beyond the confines of definitions:** In identifying an RP and an RPT, one needs to go beyond the confines of the regulatory definitions and apply the ‘**substance over form**’ principle by looking at the spirit of the regulations. (this we need to understand very well)
- b) **Unmasking:** Special attention may be paid to unravel:
  - i. Arrangements for providing free usage of assets, facilities and resources to certain parties;
  - ii. Unusual, uncharacteristic arrangements that do not reflect usual contractual acumen, as RPTs may be masked therein;
  - iii. Terminations and modifications of approved RP transactions / contracts on terms favourable to the RP.
- c) **Questioning purpose and legitimacy:** Review of RPTs needs to go beyond the disclosures and reporting protocols and must extend to questioning the legitimacy and the purpose of entering into such transactions.
- d) **Going beyond the obvious:** Internal Auditors may periodically consider special audits like an asset usage review, people deployment review, etc., to identify potential redundancies and misuse, including violation of regulations pertaining to RPs.
- e) **Engaging with the staff:** One must create opportunities for direct, periodic interactions with the relevant staff members in the normal course. Reporting on issues related to RPs and RPTs is sensitive and requires tactful communication. (Diplomatic and absolutely professional).
- f) **Good Cop and Bad Cop :** Play the game to make the auditee believe and provide real information



## Bottom Line



Data Analytics allows you to do more with less.

If you think that there must be a better way then there probably is!

Get into a Investigative Mind set with presumption that Fraud has been done unless otherwise proved

Don't rely on the work of experts unless you have exhausted all the ways of ascertaining information

A non cooperative borrower is better than a Very cooperative one !

Don't rely on hear say and see Too good to be True scenario

# Maun - The Best weapon and Strategy !

*'Maun' in Sanskrit means silence. The above is a Sanskrit proverb meaning everything can be achieved through silence. It is a sign of control and tolerance. An underlying meaning of the proverb is to exercise the wisdom to understand and comprehend when to speak and when to be silent, given a particular situation.*

- ▶ When wisdom speaks, be silent. Do not waste your candle when the sun is there
- ▶ Let silence be the art you practice
- ▶ The most important thing in communication is what is not said
- ▶ Work hard in silence; let your success make the noise
- ▶ Be silent in two situations:  
When you feel one can't understand your feelings from words, and  
When one can understand without any words
- ▶ The quieter you become, the more you can hear
- ▶ Fools multiply when wise men are silent
- ▶ Silence is one of the hardest arguments to refute

## Cosmos Bank fraud - Heist of 94 Crore (Lazarus Group)

[https://www.securonix.com/wp-content/uploads/2021/07/Securonix\\_Cosmos-Bank-Report.pdf](https://www.securonix.com/wp-content/uploads/2021/07/Securonix_Cosmos-Bank-Report.pdf)

## The Ranbaxy Fraud - Dinesh Thakur (244 Crore)

<https://www.cbsnews.com/news/ranbaxy-whistleblower-reveals-how-he-exposed-massive-pharmaceutical-fraud/>

## The ONGC Fraud - 197 Crore

<https://indianexpress.com/article/business/companies/identity-theft-ongc-falls-prey-to-cyber-fraud-loses-rs-197-crore/>

## AMPL Fraud

***Try Try .... Never say Die !***

डुबकियां सिंधु में गोताखोर लगाता है,  
जा जा कर खाली हाथ लौटकर आता है।  
मिलते नहीं सहज ही मोती गहरे पानी में,  
बढ़ता दुगना उत्साह इसी हैरानी में।  
मट्ठी उसकी खाली हर बार नहीं होती,  
कौशिश करने वालों की कभी हार नहीं होती।

असफलता एक चुनौती है, इसे स्वीकार करो,  
क्या कमी रह गई, देखो और सुधार करो।  
जब तक न सफल हो, नींद चैन को त्यागो तुम,  
संघर्ष का मैदान छोड़ कर मत भागो तुम।  
कछ किये बिना ही जय जय कार नहीं होती,  
कौशिश करने वालों की कभी हार नहीं होती।



# Thank you

Breathe well... and Meditate !  
For any feedback /clarification, please reach out

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