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FORENSIC ACCOUNTING AND AUDIT TO STRENGTHEN CORPORATE GOVERNANCE

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Abstract

Forensic accounting is a distinct specialized field of accounting. It is described as a dynamic and all-encompassing instrument for investigating financial fraud that includes a thorough review of records to support financial fraud and serves as supporting documentation in legal proceedings. It involves applying scientific knowledge to legal proceedings and tries to use accounting reports for legal reasons to survive legal scrutiny for criminal prosecution. It has been determined that internal and statutory audit systems are insufficient to prevent frauds, and it is urgently necessary to redefine the function of auditors. As a result, forensic audit is expected to grow dramatically.

This paper is descriptive and qualitative in nature and is based on secondary sources of data. It clarifies the idea and application of forensic accounting and recognises its significance in corporate governance. The Forensic Audit Investigation Methodology has been discussed and the regulatory stance on Forensic Audit in India has been elaborated. It also identifies the difficulties in implementing Forensic Accounting in India.

The use of forensic auditing as a preventative measure has given management and regulators access to intricate financial concealment. Since stakeholders have grown to comprehend the significance of forensic audit and recognise its relevance, a regular procedure is now employed to preserve an entity's operational accuracy and managerial effectiveness. The forensic audit should be made mandatory in order to stop scams before they start and increase security awareness to fight fraud. India's financial sector reforms are intended to increase its versatility, efficiency, and competitiveness.

Keywords: *Forensic auditing, forensic tools, fraud, accounting, techniques, Corporate Governance.*

1. INTRODUCTION

The creation of forensic accounting to expose all fraudulent practises has been prompted by the rise in regulatory compliances, the unceasing quantity and aggressive accounting techniques were used to commit complicated business frauds and economic crimes. Forensic Accounting is a comprehensive and dynamic field encompassing accounting, financial, auditing and investigative skills, to withstand legal scrutiny for criminal prosecution. In an effort to include both litigation assistance and investigative accounting, a new field of accounting called "Forensic Accounting" was created. (Zysman, 2004).

Forensic accounting assists companies to avert frauds and also aids in attaining the goals to enhance risk management, control, and governance processes in a systematic and logical manner. In the field of accounting, forensic accounting is expanding quickly. It focuses with combining "accounting, auditing, and investigative skills" to deal with locating or preventing financial fraud and white-collar crimes. It is known as a financial fraud assessment tool and includes a careful examination of documents to prove financial fraud. It also acts as supporting evidence in court cases. It entails the use of scientific knowledge to legal proceedings with the goal of employing accounting reports for legal reasons that will withstand legal scrutiny for criminal prosecution.

2. REVIEW OF LITERATURE

In light of the growing incidence of corporate crises and frauds, several authors have discussed the range and role of forensic accountants in fraud examination.

According to **Bhasin's** research (**2017)**, "Forensic experts should possess auditing abilities, decisive deliberation, systematic proficiency, legal knowledge, flexible troubleshooting, and investigative adaptability." **Ngozi Ijeoma (2015)** in her study showed that robust evidence exists on the effectiveness of the practices, tools and techniques applied by forensic fraud accountants which help to control the issue of creative/innovative/aggressive accounting. The outcome demonstrated the existence of substantial proof that forensic accountants' productivity increases with time. Additionally, it was discovered that the rise of forensic investigative accountants increased public trust in business firms' reliability and their report. **Luke (2013)** considered Forensic Accounting as an effort which is providing support to statutory/financial audit and exhibits the potency and strength of the audit report. **Sowjanya and Jyotsna (2012**) depicted data mining methods by applying fuzzy set theory. They recommended that using only financial statements data may be inadequate for detection and prevention of fraud without applying data mining techniques. **Stanbury and Paley-Menzies (2010)** "discovered that the practise of forensic accounting entails obtaining, compiling, and presenting financial data in a way that makes it admissible in court against criminals." **Owolabi, Dada, and Olaoye (2013)**, "advised that forensic accounting is acceptable for legal examination, as it incorporates it in a scientific manner and lays out the findings in resolving disputes, contributing to the highest level of confidence." **Okunbor and Obaretin (2010)** stated that "Forensic accounting aids in settling factual disputes in commercial litigation." **Dhar and Sarkar (2010)** argued that "Forensic accounting has jurisdiction over tax evasion, bankruptcy, and accounting rule violations." The American Institute of Certified Public Accountants (AICPA), in 2010, noted that "Forensic accounting requires the application of technical and professional knowledge as well as the investigative abilities that Certified Public Accountants possess." **Singleton and Singleton (2010)** suggested that "Forensic accounting must focus on preventing fraud and examining antifraud measures using non-financial information." **Arokiasamy and Cristal (2009)** claimed that by carefully reviewing financial data, forensic accountants can identify illicit transactions. **Ozkul and Pamukc (2012)** suggested that **"**prior to initiating the legal procedure, it is advised that forensic accountants provide accounting data to ascertain the facts needed to resolve the dispute**." Huber (2012)** asserted that "scandals, frauds, and other incidents have lead users of financial statements to have trust in forensic accountants."

3. STATEMENT OF THE PROBLEM

Forensic audit was deemed necessary for the reasons listed below.

- Forensic audits for corporations and banks are required due to gaps in traditional audit mechanisms that make it difficult to identify and evaluate fraud because of their narrow scope for opinion-forming.
- In the absence of concrete proof, the evidence gathered during traditional audit is compliance-based and may not be acceptable in court. Forensic audit fills this gap because the evidence it produces is conclusive and the outcome of a thorough investigation.
- As businesses get more sophisticated and technology is used more frequently, forensic auditors are required to find and pinpoint probable fraud areas since nowadays, frauds are carried out through a variety of technological resources.
- Since skilled individuals rather than incompetent ones commit the majority of white collar and occupational frauds, we require a specialist who not only comprehends finance, accounting, and audit but also employs professional scepticism, unconventional thinking, and inventiveness to deter fraud.
- A forensic lens view would make it possible to determine whether the individual, authorities, or service providers are carrying out necessary verification and investigation exercises as required by the circumstances because a rigid auditing method would not yield results.
- The importance of forensic audit is highlighted by the increased demand for accountability and transparency in a positive company culture.
- The commissioning of forensic audits on a voluntary basis builds stakeholder confidence and gives them a sense of satisfaction and security that their interests are protected.

Thus, it is anticipated that forensic accounting will be essential in preventing financial crimes, fraud, and other types of mismanagement that are viewed as occurring in most industries.

4. SCOPE OF FORENSIC ACCOUNTING

The business world has changed and advanced, both domestically and globally, and forensic accounting is a strong profession that has moved with it.. Subfields of Forensic Accounting include securities and tax fraud- investigating and analysing financial evidence, Business valuations, computer/cyber/digital forensics-recovering and investigating the digital data, electronic discovery, Royalty Audits, economic damage computation- fraud and economic loss quantification, bankruptcy and insolvency, financial surveillance, Anti money Laundering Programs and due diligence assignments.

5. OBJECTIVES OF THE STUDY

This study aims to achieve the following objectives

- Reviewing literature on Forensic Accounting
- Recognizing scope of Forensic Accounting

- Cognizing impact of Forensic Accounting in Corporate Governance
- Understanding Forensic Audit Investigation Methodology
- Discussing the regulatory stance on Forensic Audit in India
- Identifying the difficulties in implementing Forensic Accounting in India
- Attaining meaningful conclusions of the study

6. RESEARCH METHODOLOGY

The study uses secondary data sources and is descriptive and qualitative in character. According to the needs of the study, the researcher has logically researched and collated a variety of data and figures from reputable sources, including websites, news stories, journals, and working papers.

7. THE IMPACT OF FORENSIC ACCOUNTING ON CORPORATE GOVERNANCE

In the modern world, a forensic accountant plays a critical function. This is due to forensic accountants who examine and record frauds. The effectiveness of the practises, methods, and procedures employed by forensic accountants in assisting in the eradication of the problem of inventive accounting is clearly demonstrated by the available evidence. Through forensic accounting and investigation paired with fraud detection, an effective internal control system, and high-quality financial reports, the corporate governance mechanism will be able to carry out its role of achieving company goals.

Therefore, through enhancing management responsibility, internal control, and financial reporting systems, forensic accounting and investigation will successfully affect corporate governance. Additionally, it will aid in minimising company failure and investor destitution, both of which can hinder corporate success and expansion. So, by using accounting ideas, auditing techniques, and investigative procedures to deal with legal issues, the investigation of financial frauds is aided by forensic accountants working with attorneys, judges, regulatory bodies, and other organisations.

8. FORENSIC AUDIT INVESTIGATION METHODOLOGY

In order to quantify the level of corruption, compute it, and arrange to put the results through computerised audit processes and methodologies, forensic accountants employ scientific and systematic technology to collect, classify, and analyse large volumes of data as part of fraud investigations. Forensic investigation is the use of specialized, technical, specific and unique accounting skills which are crucial in executing an inquiry and to ensure that the result will have application to legal proceedings.

Umeraziz (2014) stressed upon the methodology which is to be applied by forensic auditors. He suggested that the investigation for financial fraud could be examined from all the ways of occurrence of fraudulent act or not. The methodology is as follows:

1. Examining the data that is already accessible
2. Formulating a hypothesis in light of such data
3. The hypothesis is tested
4. Developing and changing the premise

Techniques for Investigation

In a forensic audit, the following are a few methods and approaches used to gather evidence:

1. Substantive techniques, such as document reviews, reconciliations.
2. Analytical methods are employed to compare patterns across a given time period or to compile comparable data from several locations.
3. Techniques for auditing that are assisted by computers, such as software that can spot fraud
4. To find the faults that made it possible for the fraud to be committed, internal controls must be understood and put to the test.
5. Interviews and interrogations: To elicit comments and reactions from the accused, interviews and interrogations are two essential investigative techniques. The interrogator does not have the authority to convict the prisoner in court. In order to prove or disprove a course of action in a particular circumstance, it is his responsibility to gather the relevant evidence. (John, Fred, Joseph, and Brian; Oyedokun, 2014)

Tools for Investigation

1. Forensic fraud examiners employ the following seven methodologies and methods of investigation: (Richard 2013)
2. Background checks and assessments of publicly available documents
3. Interviews with informed individuals (the witness and the accused)

4. Privileged informants and sources
5. Examination of physical and electronic evidence in a laboratory
6. Document dating, fingerprint analysis, ink sample, and simulated forgery of signature analysis are all part of physical forensic examination.
7. Computer forensics encompasses several different tasks, including hard disc imaging, email analysis, file recovery, examining the use of, and potential abuse of, company computers for personal use, as well as ensuring digital evidence's chain of custody.
8. Both physical and electronic surveillance
9. Operations conducted covertly
10. Approaches for analysis using horizontal and vertical analysis, ratio analysis, trend or time series analysis, and use of work-back ratios techniques for analysing financial statements.

9. REGULATIONS GOVERNING FORENSIC AUDIT IN INDIA

The rise in financial and cyber fraud as well as the inadequacy of authorities to monitor security schemes necessitate a forensic audit. Forensic audits have been mandated by the Reserve Bank of India for sizable advances and account reorganisation. The Serious Fraud Investigation Office (SFIO) and the Enforcement Directorate (ED) have emphasised the significance of forensic audit in light of the rise in money laundering and willful default cases that are impacting the banking sector.

The Benami Transactions (Prohibition) Amendment Act has made forensic audits even more vital in the fight against financial criminals. Section 3 of Prevention of Money-Laundering Act 2002 defined money laundering "as the involvement of a person in any activity involving the proceeds of crime and displaying it as untainted property, where it is clear that incorporating forensic audits is necessary." Using a forensic auditing technique, it has been possible to look into the placement of cash and other assets, layering and structuring them, integrating them, and finally transporting them to other countries that serve as tax havens.

Master Directions on Frauds are provided by the Central Fraud Registry (CFR), which was established by the RBI by notification RBI/DBS/2016-17/28 on July 1, 2016, and is based on the Fraud Monitoring Returns. Banks can access the CFR using user names and passwords. Searchable CFR, a web-based database. CFR was formed to evaluate real-time risks linked with certain payment operators and frauds related to digital payments in an effort to boost client confidence. The RBI started a self-conducted forensic investigation of the top 12 defaulters in addition to the bank audits to determine if the banks authorised these loans in conformity with the policies and guidelines in place at the time. The RBI also included Early Warning Signals, a list of dubious transactions, in the same press release. "High value RTGS payments to unrelated parties, frequent changes in the scope of the project the borrower is undertaking, foreign bills that are outstanding with the bank for a long time and a tendency for bills to remain overdue, default in undisputed payment to the statutory bodies as declared in the Annual Report, inability to produce original bills for verification upon request, Significant changes in receivables, a disproportionate change in current assets, a significant increase in working capital borrowing as a percentage of turnover, a significant increase in fixed assets without a corresponding increase in long-term sources, and a significant increase in borrowings despite a sizable amount of cash and cash equivalents on the borrower's balance sheet frequent changes to accounting procedures, project costs that are significantly higher than average project installation costs, claims that are not acknowledged as high debt, and a significant annual growth in unbilled revenue, extensive related party transactions, numerous transactions with interconnected companies, material inconsistencies in the annual report, significant discrepancies within the annual report between different sections, inadequate disclosure of materially adverse information and no qualification by the statutory auditors, raid by income tax, sales tax, or central excise duty officials, and a significant decrease in the promoter's stake are just a few of the issues."

The Central Government has the authority to look into the business dealings of corporations thanks to Section 210 of the 2013 Companies Act. In accordance with Section 212(1) of the Companies Act of 2013, a probe may be launched based on the data in the inquiry report from the Registrar of Companies, which serves as the foundation for a forensic audit by the relevant regulators to find suspected fraud.

To maximise asset value and boost investor confidence in handling business failures, the Bankruptcy and Bankruptcy Code 2016 aims to perform bankruptcy and liquidation proceedings in a timely and effective manner. According to the Code, insolvency professionals (IPs), who would perform a variety of tasks throughout the procedures, would be the primary force behind the bankruptcy resolution process. Avoidance transactions, fraudulent trade, and preserving business value during the insolvency process are all prohibited by the IBC. IPs must also recognise and reveal transactions with a dubious history. They must therefore be skilled in forensic techniques in order to conduct forensic examinations of claims and adjudication (as required by Sections 18 and 35), evaluate the validity of proofs, conduct liquidation analyses, and supervise the distribution of funds in accordance with Section 18 of the IBC. IPs and liquidators are required to register avoidance of certain transactions with the adjudicating body within two years of the insolvency commencement date in line with Sections 43-51 and 66 of the Code. These transactions include those that are exorbitant, preferential, or undervalued, as well as illegal or fraudulent conduct taken with the intention of misleading creditors.

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undervalued, as well as illegal or fraudulent conduct taken with the intention of misleading creditors. In an effort to deter and stop capital market fraud, the Capital Market Regulator has frequently used this power. Some of the most significant fraudulent practises that call for SEBI engagement include Round-trip trade, swaps, insider trading on the stock market, Ponzi or Pyramid schemes, and the eight-ball model are all examples of unethical money movements. After obtaining the Ministry of Corporate Affairs' list of 331 shell companies in 2017, SEBI instructed the stock exchanges to identify the companies listed on their trading platforms and begin monitoring steps, such as prohibiting trading in their shares. By engaging an independent auditor to perform a forensic investigation of these enterprises, stock exchanges also started the process of proving the legitimacy of these corporations. According to Section 33 of the Insurance Act of 1938, IRDA has the power to ask anyone (the Investigating Authority) to look into the financial problems of any insurer. The provisions of this section have been amended to require all insurance firms to fully investigate the claimant's intentions in the case that a suspected false claim exists. In the general insurance sector, fake official documents such FIRs (police reports), licences, and medical bills are used in the majority of fraud cases. Forging these documents is not a concern for fraudsters. One of the largest fraud threats that insurance firms face is claims of fraud. Investigations into any surveyor, intermediary, client, or employee involvement in inflated or fraudulent claims are necessary to validate the facts, look for supporting documentation, pinpoint the method of operation, and assign blame. Only forensic audit will allow for this, the statutory and internal audit are still infrequently able to take the proper action at the proper time. Despite the strict revisions made to the appointment, resignation, and audit procedures under the SEBI Listing Obligations and Disclosure Requirements 2015 and the Companies Act, 2013, these processes continue to be problematic. Hiring forensic auditors will soon become common company practise for proactive fraud audit check-ups and for achieving improved and transparent corporate governance practises in the organisation. Additional laws that support the forensic auditors' conclusions can be found in Sections 45 and 47 of the Indian Evidence Act of 1872. Questions to Ask Companies About Forensic Audit A forensic audit is frequently requested by regulatory agencies when there is a reasonable suspicion that funds are being misused or to locate and gather proof of frauds, embezzlements, or other white-collar crimes. Therefore, regulatory body's order approving the Forensic Auditor's employment shall serve as the basis for his mandate.

10. DIFFICULTIES IN IMPLEMENTING FORENSIC ACCOUNTING

- India severely lacks qualified fraud examiners with adequate specialised knowledge on forensic issues.
- Accounts and audit trails are difficult to manage as a result of the digitization of records.
- The judicial and political systems are intertwined, which makes it difficult to acquire records.
- A model for detecting and preventing fraudulent activity needs to be developed.
- There is a lack of an efficient internal financial control system.
- The government should work with regulatory organisations to set the necessary rules to control forensic activities.
- The importance and significance of forensic accounting are still not widely understood by businesses.

11. CONCLUSIONS AND RECOMMENDATIONS

The future of forensic accounting is really bright. It has been determined that internal and statutory audit systems are insufficient to prevent frauds, and it is urgently necessary to redefine the function of auditors. As a result, forensic audit is expected to grow dramatically.

As the demand for fairness, integrity, and openness in reporting is exponentially increasing, forensic audits and company secretaries are often employed techniques to identify fraud. As his function expands and becomes more important during forensic audit, the Company Secretary who also serves as the The corporate compliance manager ought to get knowledgeable about the practical nuances of forensic audit. Through a consultant, advisory company, or investigator company, he might support a forensic audit. The most crucial attitude in any audit is professional scepticism, which includes having an open mind and assessing audit data critically. Instead of assuming management is dishonest or presuming unquestionable honesty, auditors should use a professional approach to planning, acquiring data, obtaining accurate information, executing the audit, and writing the report. The burgeoning field of forensic audit offers opportunities for company secretaries to join and excel in.

Additionally used as a preventive measure, forensic auditing, brings complex financial concealment within the management's and regulators' control. Now that stakeholders are aware of its value, forensic audits are used frequently to uphold an organization's operational accuracy and managerial effectiveness. To prevent scams from happening in the first place and to increase security awareness in the fight against fraud, forensic auditing should be made mandatory. India's financial sector reforms are intended to increase its versatility, efficiency, and competitiveness.

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