



Use of Forensic Accounting in Detection and Prevention of Financial Frauds

Singh A^{1*} and Gaur JR²

¹Ph.D., Research Scholar and Teaching cum Research Officer, Rashtriya Raksha University, India

²Life Time Professor, Rashtriya Raksha University, India

*Corresponding author: Anshu Singh, Ph.D., Research Scholar and Teaching cum Research Officer, Rashtriya Raksha University, Dist- Gandhinagar, Gujarat, India, Email: anshu.singh@rru.ac.in

Received Date: December 17, 2024; Published Date: January 10, 2025

Abstract

This paper highlights the gravity of financial fraud in recent years. It also explores as to whether financial frauds can be detected and prevented by Forensic Accounting. What is the situation of financial frauds in India and the global impact of the same on the economy? The role of forensic accountants in contemporary society today and in future has also been analysed and discussed vis a vis ever increasing financial crimes. How global embracement of new technologies is affecting the economic scenario, has been mentioned.

Keywords: Financial Frauds; Forensic Accounting; Contemporary Society; New Technologies; Economic Scenario

Abbreviations

BSE: Bombay Stock Exchange; SEBI: Securities and Exchanges Board of India; PNB: Punjab National Bank; INTERPOL: International Criminal Police Organization; NCRB: National Crime Records Bureau; RBI: Reserve Bank of India; CBI: Central Bureau of Investigations; ED: Enforcement Directorate; IT: Income Tax; AI: Artificial Intelligence; ML: Machine Learning; NGO: Non-governmental organization; KYC: Know Your Customer; NCIIPC: National Critical Information Infrastructure Protection Centre; CERT-In: Indian Computer Emergency Response Team.

Introduction

In literal terms, fraud can be defined as a deliberate act of cheating somebody in order to get money or benefits by illegal means. In other words, fraud is a deliberate act of deception or concealment intended to gain an unfair advantage over another person or an institution. It is in

fact forgery, computer manipulation, fraudulent financial reporting, misappropriation of assets, obtaining payment for the services not provided, getting illegal remuneration or salary and by getting false insurance claims and other crimes. It causes conflict of interest and violation of ethics.

Frauds can be committed in Banks, Financial Institutions, Insurance Companies, Government Departments/ Companies, and Stock Exchanges with public who are depositors or investors. In the 20th century frauds were mostly committed through physical mode that is by additions and alterations in the bank documents, agreement deeds or by printing and circulating fake currency selling of spurious precious metals like gold and silver and the jewellery has also not been uncommon. However, in the 21st century frauds are more often being committed by the use of technology. It may be online or offline. Even then it is very difficult to demarcate their occurrence as crime can be committed anywhere and in any manner.

Magnitude of the Problem

The magnitude of the financial frauds has ever been increasing thereby affecting the world economy and the society adversely. The fraudsters through their acts have always taught us lessons for the future. In other words, these ghastly and deplorable acts have made society, the banking system and the financial institutions more vigilant and careful in the future and permitted for plugging the loopholes in the system to make it more robust for the future.

India has witnessed several financial scams and scandals in the past which have drawn the attention of the whole world and left everybody stunned.

Harshad Mehta Scam: This case is also known as Indian Security Scam. Harshad Shantilal Mehta was an Indian stock broker who was involved in the particular scam in the year 1992. It was a fraud to the tune of rupees 30,000 crores and was committed through Bombay Stock Exchange (BSE). He gained infamy for market manipulation. Bombay High Court and the Supreme Court of India convicted Mr. Mehta for five years. However, he died of a heart attack in 2001. This scandal has exposed the ambiguities in the Indian Banking System and the Bombay Stock Exchange. The Securities and Exchanges Board of India (SEBI) has introduced new rules to cover these loopholes [1].

Abdul Karim Telgi Scam: The case is also known as Stamp Paper Scam. Mr. Telgi earned money printing and selling counterfeit stamp paper in India. He has in fact run a parallel business to the government. The size of this scam was estimated to be around rupees 3000 billion (US \$36 billion). Telgi and others were convicted from 13 to 30 years of rigorous imprisonment in the years 2006 and 2007. Mr. Telgi died in October 2017 [2].

Mr. Vijay Mallya Case: Mr. Vijay Mallya an ex-Rajya Sabha member of India, ex-chairman of several other companies, and whose name is closely associated with defunct. Kingfisher Airlines launched by him in the year 2005 in India, owes about rupees 9000 crores to 17 Indian banks. He fled to United Kingdom (U.K) in the year 2016. The Indian government and the investigating agencies are trying their level best for his extradition from the U.K but he is fighting against it through the U.K courts for not to be sent back to India. This person has ditched several banks in India and has fraudulently drawn money and loans [3].

Mehul Choksi and Nirav Modi Scam: It is also known as the Punjab National Bank (PNB) Scam. Mehul Choksi was a fugitive businessman in India, and owner of Gitanjali Group of Companies, a retail jewellery firm with about 4000 stores

in India. He along with his nephew Nirav Modi defrauded PNB for rupees 14000 crores. Mr. Mehul fled India from India after the scam and is living in Antigua and Barbuda where he holds citizenship. A special PMLA court in India issued non-bailable warrants against him in March 2018. He did the biggest fraud perhaps in Indian banking history [4].

Recent Statistics

The World Economic Forum reported on April 10, 2024, that, according to INTERPOL, in 2023, scammers stole over one trillion dollars from victims around the world. Financial fraud is increasing! Further, it states that digital scams, including investment fraud and people trafficking deceptions, are on the rise. The increase is partly due to the global embrace of new technologies, crypto currency, and Artificial Intelligence [5].

The perusal of Indian data on cybercrimes and the frauds revealed that the amount of money lost due to cyber fraud in India has more than doubled from rupees 69.68 crores in the financial year 2023 to rupees 177.05 crores in the financial year 2024. National Crime Records Bureau (NCRB) reported 4850 cybercrime cases in 2023, resulting in a loss of 66.66 crores of rupees [6]. In fiscal year 2024, the Reserve Bank of India (RBI) reported bank frauds amounting to more than 139.3 billion Indian rupees. This was a decrease from over 302 billion rupees in 2023 [7]. In Tamil Nadu, from January to September 2024 cyber financial frauds resulted in the losses of rupees 1100 crores [8].

According to a report published from Ahmedabad (Gujarat) India on May 06, 2023 in the daily Newspaper Rajasthan Patrika, the fraudsters duped more than 14000 people in one year by getting information about their debit and credit cards. In total 14775 people were victimized alone in Gujarat in one year [9]. In the cybercrime cell, 14725 complaints were registered. Out of these complaints 3997 were registered in Ahmedabad, 2197 in Surat, 1339 in Vadodara and 612 in Rajkot [10]. People lost one thousand to three lac rupees in different cases. According to another report in the same newspaper from Mumbai, a mastermind cyber fraudster was arrested by police. He operated for three-four years and was able to commit cyber fraud of rupees 4 to 5 cores daily. He has a group of five persons operating in different cities in India and had links with Chinese fraudster gangs. He has 40 bank accounts which were frozen by police. He used to deposit fraud money earned from India in Chinese bank accounts. On December 16, 2023, The Hindustan Times reported that as per police as person aged 88 years and his wife living in sector 46, Chandigarh were duped by the fraudsters of rupees 75 lakh for getting their relative released from jail in Canada. A case under section 406 (Criminal Breach of Trust), 420 (Cheating), and 120-B (Criminal Conspiracy) of the Indian Penal Code had been registered at the cybercrime

police station, in Chandigarh [11]. In fact, not a single day passes now when we don't come across the news of cyber financial fraud in the print and electronic media not only in India rather all over the world.

Role of Forensic Accounting

The role of audit and accounting has always been of paramount importance in banks, financial institutions, and government departments. The internal and external audits were conducted to detect embezzlement, misappropriation, and fraud. The education and training in forensic accounting are producing manpower of specialists or forensic accountants. These specialists are able to dig out deeply the financial frauds, scams, and scandals while working with the law or the investigating and enforcement agencies like the Central Bureau of Investigations (CBI), Enforcement Directorate (E.D) and Income Tax (IT) and other government departments [12].

They can better calculate the disproportionate assets than the known sources of income. They can better produce financial evidence in the court of law during trial of cases and give authentic testimony with financial facts and figures. These specialists are also working in multinational and private companies, insurance companies to prevent financial losses through frauds and misdeeds of insiders. They suggest different measures for financial security physically and online. Thus, financial accounting is playing a great role in the detection and prevention of frauds through its investigative and deterrent methods today and will also be having an excellent future.

Artificial Intelligence and Machine Learning in Finance

Artificial Intelligence (AI) and Machine Learning (ML) are playing a key role in prevention and mitigation of financial frauds. With the help of advanced tool and technologies we can now detect and prevent financial frauds in real time. In order to detect fraudulent behaviours like unusual transactions, we have machine learning algorithms which recognize patterns from historical data (for example- MasterCard's AI powered security system). AI has also extended its arms by introducing two important elements like authentication factors and identity verification to improve the security measures, one example could be the fido alliance's password free authentication using biometric data. Credit Card companies can now by analysing card holder's transaction history can prevent unauthorized charges. Experts have designed algorithms in way that AI can now detect phishing emails by analysing language patterns and sender's history, one such example being the PayPal's fraud prevention system. Even the crypto currency related frauds can be analysed and

prevented to some extent with the help of AI. It can track and monitor large crypto currency transactions across various block chains with the help of techniques like chainalysis and elliptic [13]. With these emerging technologies AI and ML are helping financial institutions stay one step ahead of manipulators and fraudsters [14].

Professional Investigations for Data Collection

We have carried out professional investigations for the data collection for this research work in 19 banks and several financial institutions in accordance with the approval and directions of the ethical committee of the Rashtriya Raksha University. The detailed results will be reported in the PhD thesis. We have also organized public camps for providing awareness for safeguarding the public at large from financial cyber frauds. We also collected data from the public through interviews at these camps. For the purpose of this publication our investigations and observations facilitated us to draw following inferences:

1. We have more robust systems than earlier in the banks and financial institutions, which are capable of preventing financial frauds. Multi layered cyber security has been provided to secure the accounts of the depositors and investors from frauds. Even the employees of the banks and financial institutions can't have access to these accounts singly. Two to three officers and the investors themselves get information/messages of the account has been fiddled with. There is always a security alert message.
2. Literate person using net banking are more prone to cybercrime or financial frauds in comparison to non-net banking users, semi-literate or illiterate persons.
3. The awareness against financial frauds being provided to the depositors and investors by the banks, financial institutions, NGO's, think tanks in the research institutions and the government are playing a crucial role in the prevention and mitigation of financial frauds.
4. Social media and the like platforms are also positively contributing against the financial frauds.
5. All age groups are prone to financial and cyber frauds though in carrying degrees not in kinds.
6. The financial fraudsters have global links for information sharing for the commission of financial and cyber frauds.
7. In the detection and prevention of financial frauds forensic accountants are also creating awareness in their institutions where they are working.

Discussion and Conclusion

Mr. Dennis Blair, former director of national intelligence of United States stated, "Nothing is more important to national security and the making and conduct of good policy than timely accurate, and relevant intelligence". Likewise, our

national security in India is paramount [15]. The major component of the national security is financial security, for which we should make and conduct good policy. From time-to-time Reserve Bank of India and Securities Exchange Board of India are making policies and giving guidelines to the public for the prevention and mitigation of financial frauds and are being of great help to the nation to streamline the matters related to finance and frauds. RBI's guidelines on Know Your Customer (KYC) and Cyber security had been of great help in protecting the customers finances and prevented them from falling prey of various scams like phishing attacks and bank frauds. SEBI's regulations for Prohibition of Insider Trading and mutual fund operations are also ensuring transparency, fairness, and investor protection thus preventing financial frauds. In the matters if cyber security also, India is second to none in the world. It has demonstrated commitment towards cyber security through technological advancements by coming up with National Critical Information Infrastructure Protection Centre (NCIIPC), CERT-In (Indian Computer Emergency Response Team), Cyber Swachhta Kendra (Botnet Cleaning and Malware Analysis Centre) to name a few. For the ever-increasing financial frauds with the use of new technology, artificial intelligence and crypto currency, we have to be ahead of the criminal's using technology for the commission of crime. We need national policy for making the best use of forensic accounting in the investigations of crime and the administration of justice. This can provide better financial security environment in the country.

Recommendations

- Investigation agencies should use Forensic Accountants in their teams during investigation.
- Investigative agencies should even invest in a few specialized trainings for their staff, equipping them with forensic accounting skills and techniques.
- Complex financial data should be analysed using the forensic accounting tools.
- Forensic accounting principles should be embedded in the internal audit systems.
- Financial institutions, Banks and Insurance companies should create dedicated forensic accounting departments tasked with investigating suspicious transactions and protecting against fraud thus, enhancing compliance with regulatory requirements.

Thus, it is concluded that-

- The use of forensic accounting can detect and prevent

financial frauds. It can provide better financial security in future.

- The global embracement of new technologies is giving rise to more complex crimes. So, for apprehending the criminals causing financial frauds by the use of technology, the investigating agencies all over the world need to have better combat technologies all the times.
- Adoption of new technologies should always be followed for imparting trainings to all the stakeholders in the criminal justice system so that the technological testimony is appreciated by all in the legal system and the judiciary.

References

1. (2023) Clear Tax. Defmacro Software Pvt. Ltd.
2. Mukherjee V (2023) Business Standard.
3. (2024) The Hindu. Hindu News.
4. (2022) Economic Times, India Times.
5. Wood J (2024) World Economic Forum.
6. Chadha S (2024).
7. (2024) Statista.
8. Vaitheeswaran (2024) The Times of India.
9. (2023) The Times of India.
10. (2023) ETNOW.
11. (2024) Hindustan Times.
12. Alkhalaileh R, Alshurafat H (2024) The impact of external auditors with forensic accounting competencies on auditee firm performance. *Heliyon* 10(11).
13. ELLIPTIC Elliptic Enterprises Limited.
14. Subudhi S (2024) Financial Frauds – How to Alleviate Customers Greivences. *J Indian Institute of Banking & Finance*, pp: 24-33.
15. Gaur J, Kathane P, Prakash S, Singh A (2023) Forensic Science & the Making of Safer Planet, in *Technology & Analytics for Law & Justice*. Haryana, Oak Bridge, pp: 153-170.