

*In the world of financial frauds,  
the fraudster is an artist,  
the investigator a critique.*

# Forensic Accounting Insights

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# Agenda

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- What is Fraud?
- Types of Frauds
- The most common and the most expensive frauds
- Case study on detecting fraud
  - Profits are Overstated.
  - Violation of provisions of Companies Act w.r.t Loans taken.
  - Violation of provisions of Companies Act w.r.t Loans given.
  - Directors have underreported their income.
  - GST - Input Tax Credit (ITC) Fraud.

# What is 'Fraud'

"Fraud is any **intentional or deliberate act** to deprive another of property or money through **deception or other unfair means**"

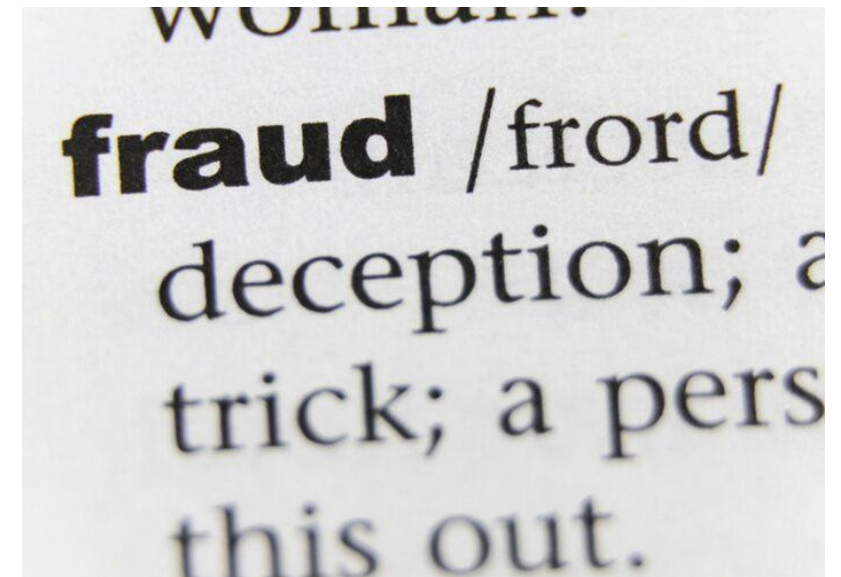
- Para 3.3.4 Framework governing forensic accounting and investigation standards - ICAI

"A **knowing misrepresentation** of the truth or **concealment of a material fact** to induce another to act to his or her detriment."

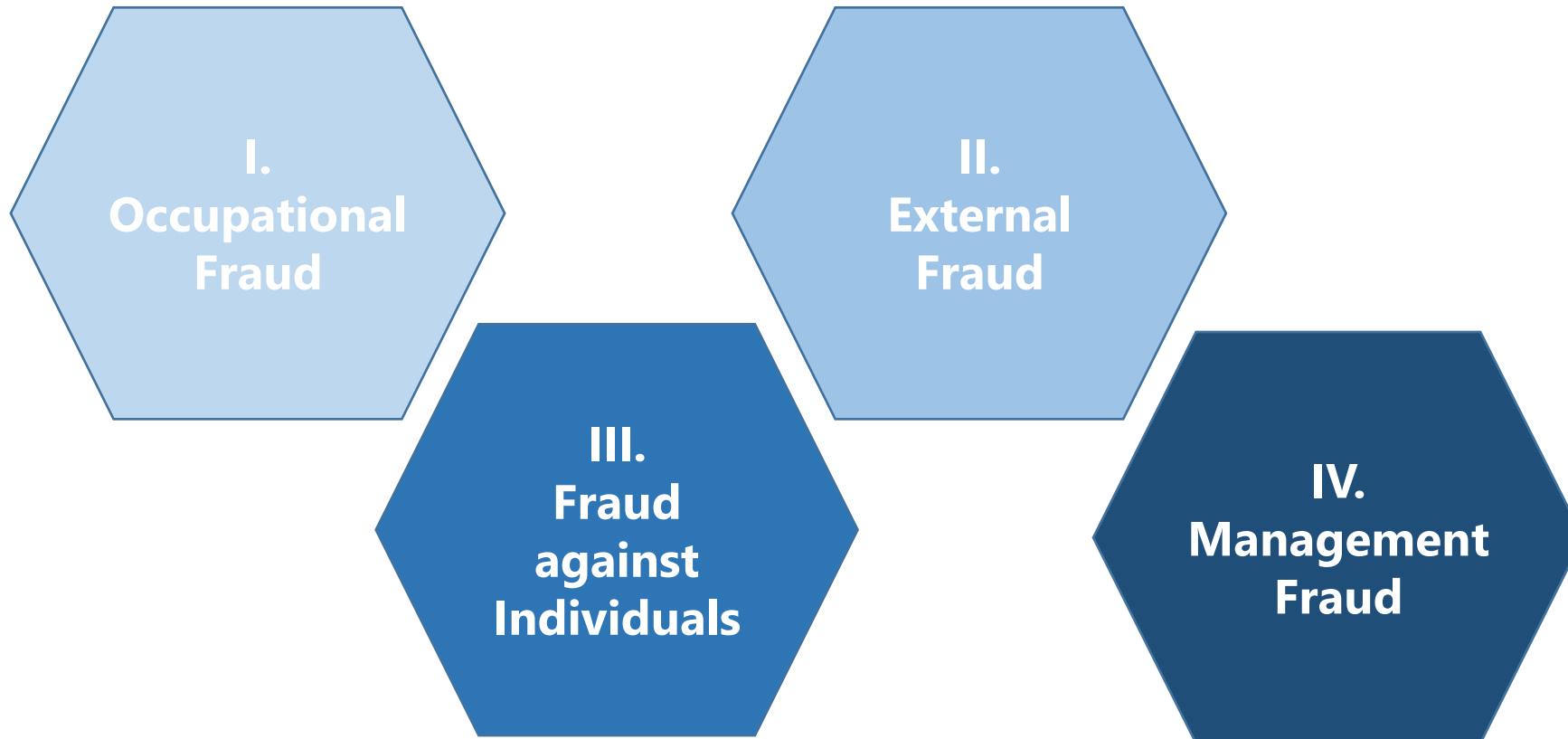
- Black's Law Dictionary

In other words, fraud is a deceitful activity used to gain an advantage or generate an illegal profit.

Also, the illegal act benefits the perpetrator and harms other parties involved.



# Types of Fraud – From an Investigation perspective



*A typical organization loses 5% of its revenues to fraud each year  
ACFE's Report to the Nations, 2020*

# Types of Fraud – From an Investigation perspective

## ***I. Internal Fraud***

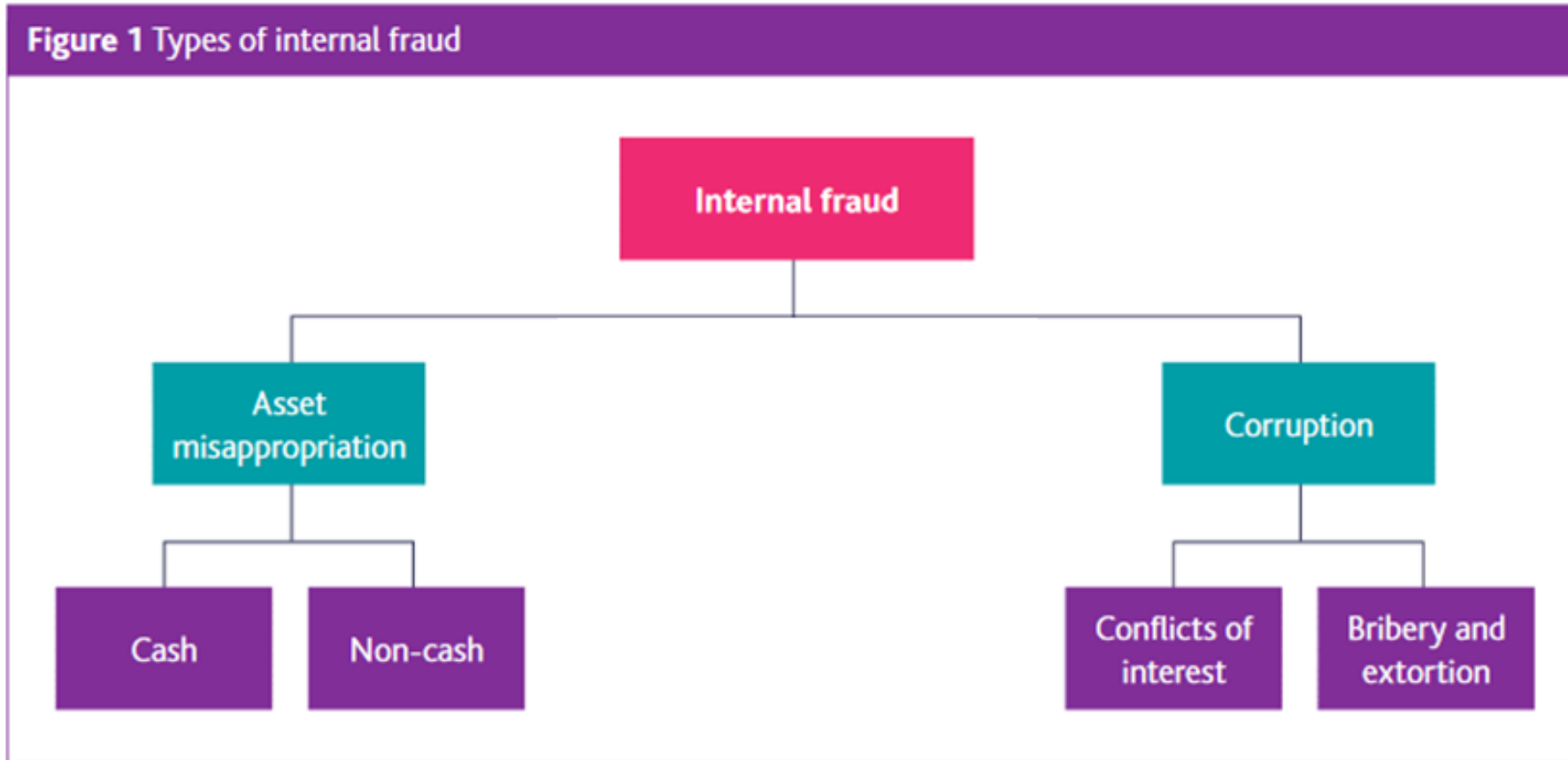
*Internal fraud, also called **occupational fraud** is: “the use of one’s occupation for personal enrichment through the deliberate misuse or misapplication of the organization’s resources or assets.”*

Simply stated, this type of fraud occurs when an employee, manager, or executive commits fraud against his employer.



I.  
Occupational  
Fraud

# Classification of Occupational Fraud

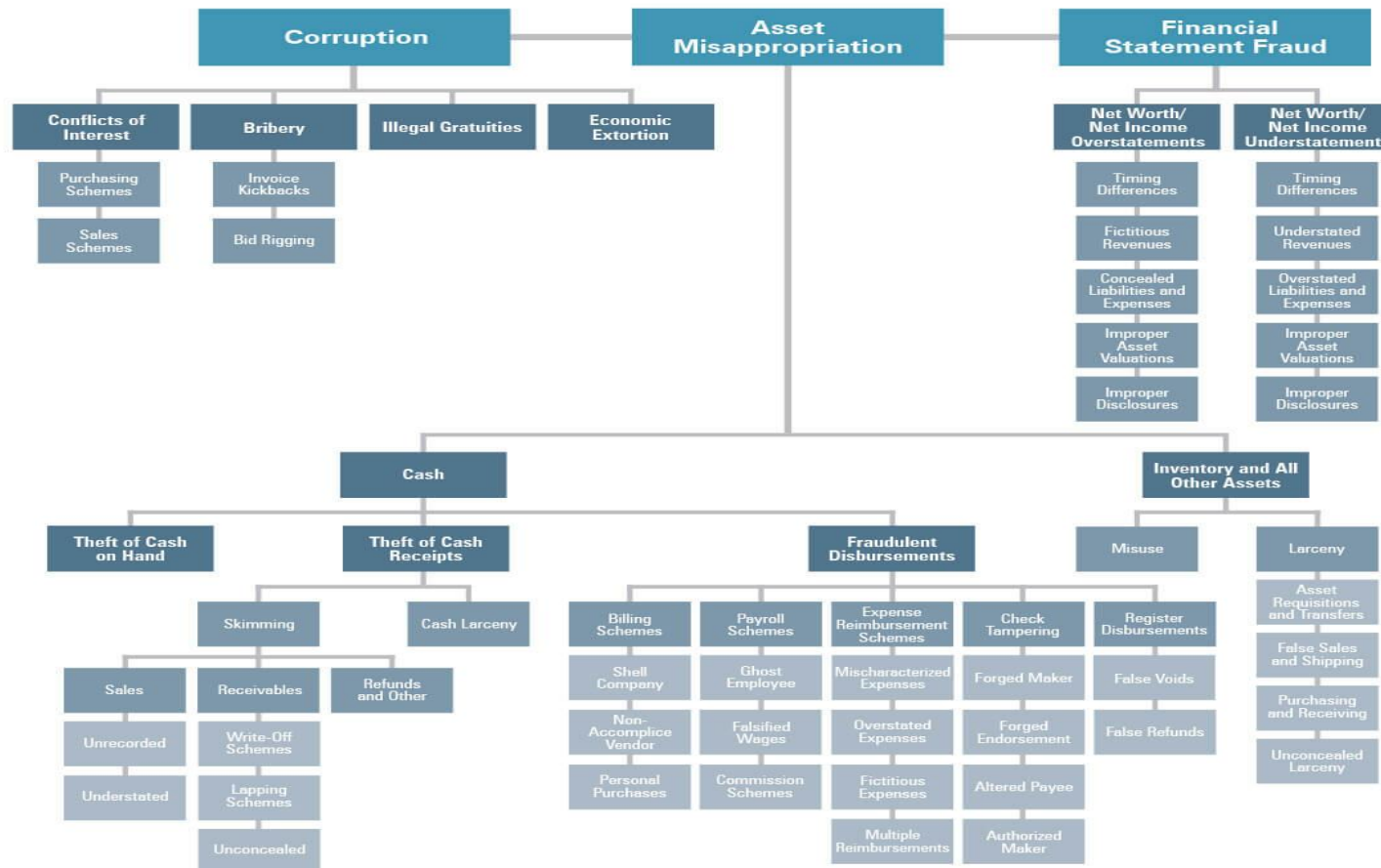


I.  
Occupational  
Fraud

Source – Fraud Risk Management – A guide to good practice  
Chartered Institute of Management Accountants (CIMA)

# Classification of Occupational Fraud

## THE FRAUD TREE OCCUPATIONAL FRAUD AND ABUSE CLASSIFICATION SYSTEM



I.  
Occupational  
Fraud

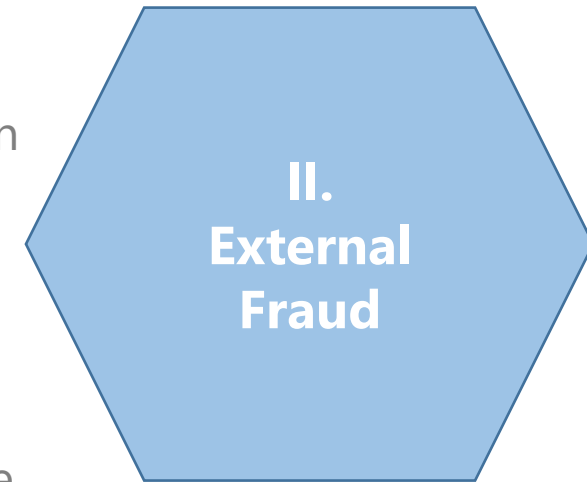


# Types of Fraud – From an Investigation perspective

## ***II. External Fraud***

External fraud against a company covers a broad range of schemes.

- ✓ **Dishonest vendors** might engage in bid-rigging schemes, bill the company for goods or services not provided, or demand bribes from employees.
- ✓ **Dishonest customers** might submit bad checks or falsified account information for payment, or might attempt to return stolen or knock-off products for a refund.
- ✓ Security breaches and thefts of intellectual property perpetrated by unknown third parties.
- ✓ Hacking, theft of proprietary information, tax fraud, bankruptcy fraud, insurance fraud, healthcare fraud, and loan fraud.



# Types of Fraud – From an Investigation perspective

## ***III. Fraud Against Individuals***

Numerous fraudsters have also devised **schemes to defraud individuals**.


Identity theft, Ponzi schemes, phishing schemes, and advanced-fee frauds are just a few of the ways criminals have found to steal money from unsuspecting victims.`

## ***IV. Management Frauds***

Management fraud, conducted by one or more top-level managers within the company, is **usually in the form of fraudulent financial reporting**.

The CEO or the CFO may perpetrate fraud by misstating the financial statements through elaborate schemes or complex transactions. Management fraud may involve:

Overstating revenues and assets, understating expenses and liabilities, misapplying accounting principles, or any combination of these.



**III.  
Fraud against  
Individuals**



**IV.  
Management  
Fraud**

# The most common and the most expensive frauds



# Management Fraud – Case Study

## ***Allegations Levelled against the Company***

- Profits are Overstated.
- Company has violated provisions of Companies Act w.r.t Loans taken.
- Company has violated provisions of Companies Act w.r.t Loans given.
- Directors have underreported their income.
- GST - Input Tax Credit (ITC) Fraud.

# Level 1 Observations

## ➤ Debtors Verification:

### 13 . Trade receivables

In □ (Rupees)

Particulars	as at 31-Mar-2020	as at 31-Mar-2019
Outstanding for less than 6 months from the due date		
Unsecured, considered good	21,44,716	6,60,18,275
Outstanding for more than 6 months from the due date		
Unsecured, considered good	10,34,83,226	3,55,92,047
<b>Total</b>	<b>10,56,27,941</b>	<b>10,16,10,323</b>

### **Possible Reasons (Page 3 & 4 of Material):**

1. Customers not assessed properly against the Credit policy.
2. Fictious Assets – Amounts due from customers (debtors) that cannot be realized.
3. Sales Overstatement – Sales booked only with an objective to show a fat top line.
4. Round Tripping

# Level 2 Observations

## ➤ Window Dressing

### 17 . Revenue from Operations

In □ (Rupees)

Particulars	1-Apr-2019 to 31-Mar-2020	1-Apr-2018 to 31-Mar-2019
<b>Sale of Products</b>	<b>54,78,23,889</b>	<b>72,15,48,612</b>
Export Sales	-	7,72,41,027
Local Sales	53,16,80,279	59,08,90,535
High Sea Sales	1,61,43,610	5,34,17,050
<b>Other Operating Revenues</b>	<b>1,32,00,175</b>	<b>61,95,914</b>
Rebate	(3,54,845)	47,32,127
Currency Fluctuation Gain/Loss	47,60,366	13,10,527
<b>Commission Income</b>	<b>83,12,139</b>	<b>-</b>
Insurance Claim	4,82,515	-
Interest on Late Payment From Debtors	-	1,53,260
<b>Total</b>	<b>56,10,24,063</b>	<b>72,77,44,526</b>

### Possible Reasons (Page 5 of Material):

1. Booked Commission Income to show profits to Financial Institutions.

# Level 2 Observations

## ➤ Loans **from** Shareholders:

### 3 . Long-Term Borrowings

In □ (Rupees)

Particulars	as at 31-Mar-2020	as at 31-Mar-2019
<b>Secured</b>		
Term Loans from Banks*	4,61,58,000	-
<b>Unsecured</b>		
Loans and Advances from Shareholders	8,50,00,000	8,50,00,000
<b>Total</b>	<b>13,11,58,000</b>	<b>8,50,00,000</b>

### 5 . Short-Term Borrowings

In □ (Rupees)

Particulars	as at 31-Mar-2020	as at 31-Mar-2019
<b>Secured</b>		
Other Loans and Advances from banks*	3,49,92,787	3,12,63,915
<b>Unsecured</b>		
From Shareholders	26,09,499	1,42,42,389
<b>Total</b>	<b>3,76,02,286</b>	<b>4,55,06,304</b>

# Level 2 Observations

## ➤ Loans **from** Shareholders:

### Check for possible irregularity/non-compliance (Page 6 of Material):

1. Section 179 of Companies Act, 2013 – Prior Consent of BOD.
2. Section 180 of Companies Act, 2013 – Prior Consent of Members by way of special resolution if Money already Borrowed + Money proposed to be Borrowed > Aggregate of its paid up share capital, FR & Securities premium.
3. Director or the relative of director to furnish a declaration that loans that have been given are out of own funds.
4. Check Compliance with THE BANNING OF UNREGULATED DEPOSIT SCHEMES ACT, 2019.
5. Every Company shall disclose by way of notes amount received from directors or relative of directors.



# Level 2 Observations

## ➤ Loan to Directors:

15. Short-Term Loans and Advances			In □ (Rupees)	
Particulars		as at 31-Mar-2020	as at 31-Mar-2019	
<b>Other Loans and Advances (Unsecured, considered good)</b>				
Advance to Suppliers		24,32,358	1,15,50,033	
Balance with Government Authorities		49,01,868	72,64,432	
Loan to Directors/Entities in which director are Interested		2,08,56,900	-	
Deferred Premium Expense		1,75,983	13,15,887	
Deposits		1,86,04,270	55,71,585	
Forward Contract Amount Receivable		2,73,92,701	17,08,42,735	
Prepaid Expenses		2,00,701	5,265	
<b>Total</b>		<b>7,45,64,782</b>	<b>19,65,49,936</b>	

### Check for possible irregularity/Non-Compliance (Page 6&7 of Material):

1. Check Compliance of Sec 185 of Companies Act, 2013.
2. Whether the Loan is given to Managing Director or Whole Time Director in their capacity as an employee.
3. Section 185 of Companies Act, 2013 is not applicable to certain companies such as Government Company, company in the business of money lending and private companies subject to certain conditions.

# Level 2 Observations

## ➤ Loan **to** Directors (From Income Tax perspective):

According to Section 2(22)(e), when a company in which the public are not substantially interested\*, extends a loan or an advance to: a. any of its shareholders who has more than 10% voting power in the company or b. to any concern in which such shareholder is substantially interested or c. for the individual benefit of such shareholder or d. on behalf of such shareholder **to the extent the company has accumulated profits**, such payment would be deemed as a dividend under Section 2(22)(e). \*a company in which public is not substantially interested is otherwise called a closely held company.

Check for possible irregularity/non-compliance (Page 7&8 of Material):

1. Directors have disclosed the same as dividend income.
2. Company has paid DDT?
3. If said loan is towards procurement of goods or service, please examine the underlying records.

# Level 3 Observations

## ➤ GST Law Viewpoint:

### 6. Trade Payables

In ₹ (Rupees)

Particulars	as at 31-Mar-2020	as at 31-Mar-2019
Creditors for Local Purchase	2,83,73,373	36,68,838
Outstanding for Import Purchase	3,48,34,972	3,60,97,314
Outstanding for Expenses & Others	57,11,191	33,38,681
<b>Total</b>	<b>6,89,19,536</b>	<b>4,31,04,833</b>

### Check for possible irregularity/non-compliance (Page 9 of Material):

1. Whether the Company has reversed amount of ITC availed in case of non-payment of dues for expenses beyond 180 days? Note: The New Disclosure Requirements for Financial Statement as per Schedule III of Companies Act, 2013 w.e.f. 1<sup>st</sup> April 2021 require **Trade Payable Ageing Schedule** to be disclosed Check: [https://mca.gov.in/Ministry/pdf/ScheduleIIIAmendmentNotification\\_24032021.pdf](https://mca.gov.in/Ministry/pdf/ScheduleIIIAmendmentNotification_24032021.pdf)
2. Whether company is involved in availing ITC through bogus invoices?

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# Cash Flow Statements:-

## ➤ Observations (Page 12 of Material):

1. The Company is relying heavily on borrowed funds.
2. Company is using most of borrowed funds for operating activities instead of investing in expansion activities.
3. The company is in need of strategic transformation to generate cash flows in order to continue for foreseeable future.

Kingfisher Airlines					
Cash Flow	in Rs. Cr. ----				
	Mar 13	Mar-12	Mar-11	Mar-10	Mar-09
<b>Net Profit/Loss Before Extraordinary Items And Tax</b>	<b>-4,301.12</b>	<b>-3,446.09</b>	<b>-1,520.78</b>	<b>-2,417.92</b>	<b>-2,155.21</b>
Net Cash Flow from Operating Activities	-1,390.86	-885.55	2.23	-1,665.09	-645.78
Net Cash Used In Investing Activities	-69.72	-387.57	-38.05	235.13	206.63
Net Cash Used From Financing Activities	1,297.36	1,203.02	81.72	1,464.55	290.11
<b>Net Inc/Dec In Cash And Cash Equivalents</b>	<b>-163.22</b>	<b>-70.1</b>	<b>45.9</b>	<b>34.6</b>	<b>-149.04</b>
Cash And Cash Equivalents Begin of Year	182.27	252.36	206.47	171.87	320.91
Cash And Cash Equivalents End Of Year	19.05	182.27	252.36	206.47	171.87

# Ratio Analysis:-

## ➤ Overview:

Ratio analysis is the comparison of line items in the [financial statements](#) of a business. Ratio analysis is used to evaluate a number of issues with an entity, such as its [liquidity](#), [efficiency](#) of operations, and [profitability](#). This type of analysis is particularly useful to analysts outside of a business, since their primary source of information about an organization is its financial statements.

## ➤ Types of Ratios (Page 13 of Material):

Types of Ratios	Formulas
a. Liquidity Ratio	Current Ratio: Current Assets/ Current Liabilities
b. Working Capital Ratio	Debtors Turnover Ratio: Total Sales/ Debtors Creditors Turnover Ratio: Credit Purchase/ Creditor
c. Capital Structure Ratio	Debt Equity Ratio: Long Term Debt/ SH Funds Capital Gearing Ratio: Equity Share Capital/ Fixed Interest Bearing Funds