

Training in Forensic Audit in the Banking Sector: A Status Report of Banks in Chandigarh

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Abstract

As per a report in Economic Times (Feb 20, 2014) Indian banks lost as much as Rs. 17,284 crore during 2012-13 due to fraud, in a near four-fold jump over the previous fiscal. At a time when the lenders were reeling under burgeoning non-performing assets, 62 banks in India filed a total of 26,598 cases of fraud. This set the authors thinking about the steps being taken by the banking sector to check such frauds. It was found that Reserve Bank of India (RBI), in the year 2009, had issued the circular which fixed the responsibility of fighting the frauds on the Chairman and CEO's of the banks. It also stated that banks need to understand and use the forensic audit techniques. As per RBI, any fraud investigation requires competence in 'forensic audit' and also technical/transactional expertise. In this regard, banks were required to take immediate steps to identify staff with requisite aptitude and give necessary training to them in forensic audit so that such trained staff can be put on the job to investigate banking frauds. In the year 2011, Reserve Bank of India further directed the banks to give the e-tests on the fraud preventions. Therefore, banks are supposed to provide e-tests on various subjects like money laundering, credit card frauds, laws related to banking frauds and such other topics which may be found important by the bankers from time to time. This paper is based on the research carried out to find the kind of preparedness that banks in Chandigarh have to deal with various frauds and the type of systems that they have in place to save them from such eventuality. Forty four banks in Chandigarh were contacted and asked about their technological preparedness to tackle risk and meet compliance requirements, with emphasis on training in forensic audit provided to the identified staff.

Keywords: staff training, forensic audit, banks in India

Introduction

In August this year, replying to a question by the interviewer (Bandyopadhyay, 2014), about the state of affairs in public sector banks, particularly after the arrest of a bank chairman involved in taking bribe; the RBI governor, Raghuram Rajan, mentioned in his answer that he was focusing on forensic accounting training. Earlier in the year, as per a report in Economic Times (Patil, 2014), Indian banks lost as much as Rs. 17,284 crore during 2012-13 due to fraud, in a near four-fold jump over the previous fiscal. At a time when the lenders were reeling under burgeoning non-performing assets, 62 banks filed a total of 26,598 cases of fraud. The report further stated that the total bank frauds in the Indian Banking sector have quadruplicated in one year's time. As per a newspaper report in September (Kumar, 2014), Deputy Managing Director of State Bank of India (SBI) said that forensic audit training would be elementary (sic). With "only a slight nudge in one direction for getting the officers into forensic audit," he was sure that the bank "will be declaring many more people (borrowers) as willful defaulters." Further, a few months ago

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(Merwin, 2014) it was reported that forensic audit was ordered by the government into non-performing assets of the Kolkata-based UCO Bank. Forensic audit was also reportedly being conducted into the accounts of Dena Bank and Oriental Bank of Commerce (OBC) on alleged misappropriation of funds from their fixed deposit customers.

This set the authors thinking about the steps being taken by the banking sector to check such frauds. It was found that Reserve Bank of India, in the year 2009 (RBI, 2009b), had issued the circular which fixed the responsibility of fighting the frauds on the Chairman and CEO's of the banks. It also stated that banks need to understand and use the forensic audit techniques. As per RBI, any fraud investigation requires competence in 'forensic audit' and also technical/transactional expertise. In this regard, banks were required to take immediate steps to identify staff with requisite aptitude and give necessary training to them in forensic audit so that such trained staff can be put on the job to investigate banking frauds.

In the year 2011, Reserve Bank of India further directed the banks to give the e-tests on the fraud preventions (India Forensic, 2011). Therefore, banks are supposed to provide e-tests on various subjects like money laundering, credit card frauds, laws related to banking frauds and such other topics which may be found important by the bankers from time to time.

Therefore, the present authors carried out research with **objective** of finding the kind of preparedness that banks have to deal with various frauds and the type of systems that they have in place to save them from such eventuality. The idea was to ask the banks about their technological preparedness to tackle risk and meet compliance requirements, with primary emphasis on training in forensic audit provided to the identified staff.

Forensic Audit

Even though the primary emphasis of this piece of research is on the 'training' aspect of forensic audit, it would be pertinent to briefly describe the basics of forensic audit.

By definition, 'Forensic Audit' means an examination and evaluation of a firm's or individual's financial information for using as evidence in the court. A forensic audit can be conducted with a view to prosecute a party for fraud, embezzlement or other financial impropriety. Thus, in the context of a bank, all financial transactions and decisions involving finance are analysed with a view to arrive at the truth. Forensic Report can be admitted in a court trial and forensic auditors may directly submit evidence in the court or depose before a judicial authority (Pannvalan, n.d.).

Vasudevan (2004) defines the concept of Forensic Auditing as "a concentrated audit of all the transactions of the entity to find the correctness of such transactions and to report whether or not any financial benefit has been attained by way of presenting an unreal picture". Forensic auditing aims at legal determination of whether fraud has actually occurred. In the process, it also aims at naming the person(s) involved (with a view to take legal action).

As per Singh (2012), forensic audit has been defined as "accounting analysis that can uncover possible fraud that is suitable for presentation in court. Such analysis will form the basis for discussion, debate and dispute resolution."

Review of Literature

The present authors found research and popular literature on different aspects of forensic auditing. Most of the academic studies, Indian as well as foreign, are related with general aspects of forensic audit/accounting, use of forensic investigation to check and detect fraud/corruption, and skill requirement for forensic audit. Very few studies were found specifically about forensic audit in banks. A brief review of literature is presented below.

The research by Islam et al. (2011) in Bangladesh, revealed that forensic accounting as a fraud detection tool has relevance to efforts for combating fraud and corruption. Findings from the study in Kenya (Oyier, 2013), show that fraud detection and prevention increased when forensic accounting services were employed. A research paper by Lohana (2013) concludes that forensic accounting is seen as a suitable tool to offer the highest level of assurance and to add credibility to the financial statements. Biswas et al. (2013) feel that if forensic auditing is made mandatory in financial and corporate sector many of the scams involving thousands of crores can be avoided. Similar views have also been expressed by Yadav & Yadav (2013). Mulsare (2013) found that the forensic auditing departments suffer from multiple challenges, amongst them being the lack of material resources, technical knowhow, interference from management, and unclear recognition of the profession. Types of bank fraud were identified. It was concluded that forensic auditors must be capacitated materially and technically to improve their effectiveness.

In a study on investigation of the necessary skills, education requirements, and training requirements for forensic accountants, Bhasin (2013) recommends fashioning of special training process to give interested accounting graduates an opportunity to acquire these special skills that will make them specialists. The results of the study show that core skills are not enough requirements for FA's to investigate economic and financial crimes in India. It means that some necessary skills from other disciplines, for instance behavioral sciences and law should also be embedded in the curriculum for training FA's. A similar study in Nigeria (Okoye and Jugu, 2010) also shows that special skills are necessary for the work of a forensic accountant hence, the need for educators to develop a curriculum for forensic accounting in their institutions. Another study by DiGabriele (2009) indicates that practitioners and academics agree on the importance of a forensic accountant to move away from a narrow approach and apply a more holistic technique. The findings further illustrate the need in accounting for a more open minded skill set. Wadhwa and Pal (2012) opine that forensic accounting in India has come to limelight only recently due to rapid increase in frauds and the white collar crimes and the belief that our law enforcement agencies do not have sufficient expertise or the time needed to uncover frauds. While majority of CAs have excellent analytical skills, they need to acknowledge that 'forensic' services require 'specialized' training as well as real-life 'practical' corporate experience.

Khanna and Arora (2009), on the basis of survey of 253 bank employees, concluded that the bank employees do not give due importance to the problem of frauds. The awareness level of bank employees regarding bank frauds is not very satisfactory, and majority of them do not dispose favourable attitude towards RBI procedures as they find difficulty in following them due to workload and pressure of competition. Moreover employees are not well trained to prevent bank frauds. Training positively affects the compliance level of employees and improves the attitude towards RBI's procedure.

Thus, we find that there is **need for research** to ascertain the current status of training in Indian banks. This has become all the more important in view of the RBI initiatives to impress upon the banks to train their staff in forensic audit/accounting.

Methodology

As per the most recent published figures available from RBI (2009c), there are 258 bank branches in Chandigarh, with an average population of four thousand served by each branch against an all-India average of fifteen thousand. Thus, Chandigarh is one of the highest banked centres (along with Goa). Instead of taking a sample by using any other method, it was decided to visit the main/local head office of each bank. The most recent figures available from RBI (2009a) show the number of all commercial banks in Chandigarh as 44. For a list of banks, see Appendix.

Thus, a survey was conducted with the help of questionnaire which had questions about opinion on rising bank frauds, bank's experience, reasons for frauds, status of fraud risk management framework, responsibility of fraud risk management, status of training for forensic audit/fraud prevention as per RBI directions, future plans for training, training agents being used, opinion about training being helpful in detecting/reducing fraud, and the efficacy of training in detecting/proving frauds till now. The responses were collected from the head of fraud risk management or key person responsible for managing fraud risk. As no cross-tabulation and hypothesis testing was involved, the data were analysed using percentages. The data have been presented in the form of appropriate tables and charts.

Analysis and Discussion

On the basis of the questions asked in the questionnaire, the data were tabulated and analysed to draw inferences. Analysis and discussion about the data is presented below.

The first question was: Do you think that fraud has been on the rise in the banking industry in the last one year?

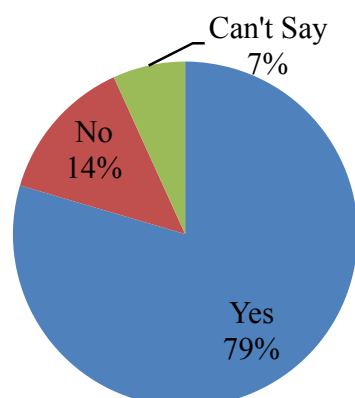


Figure 1. Opinion about rise in fraud in banking industry

From the above figure, we can see that majority of the respondents (79%) feel that there has been an increase in the number of frauds in the banking industry in the previous year.

The second question was about bank's own experience in terms of number of incidents of fraud.

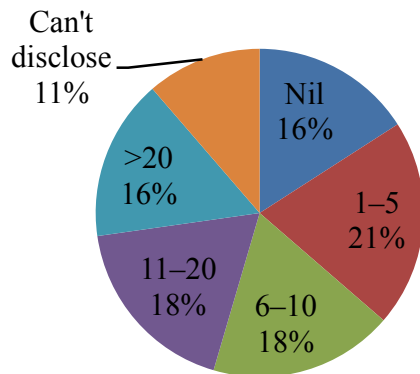


Figure 2. The respondent bank's own experience in terms of number of frauds

We can see that as many as 73% of the respondents said that their bank had experienced more than one incident of fraud in the previous one year, with 52% of them experiencing six or more incidents of frauds. Further research can be done to find differences in case of public and private sector banks and also to find the relationship between size of bank's assets and number of frauds.

The next question was about likely reasons for frauds. Multiple choices were allowed.

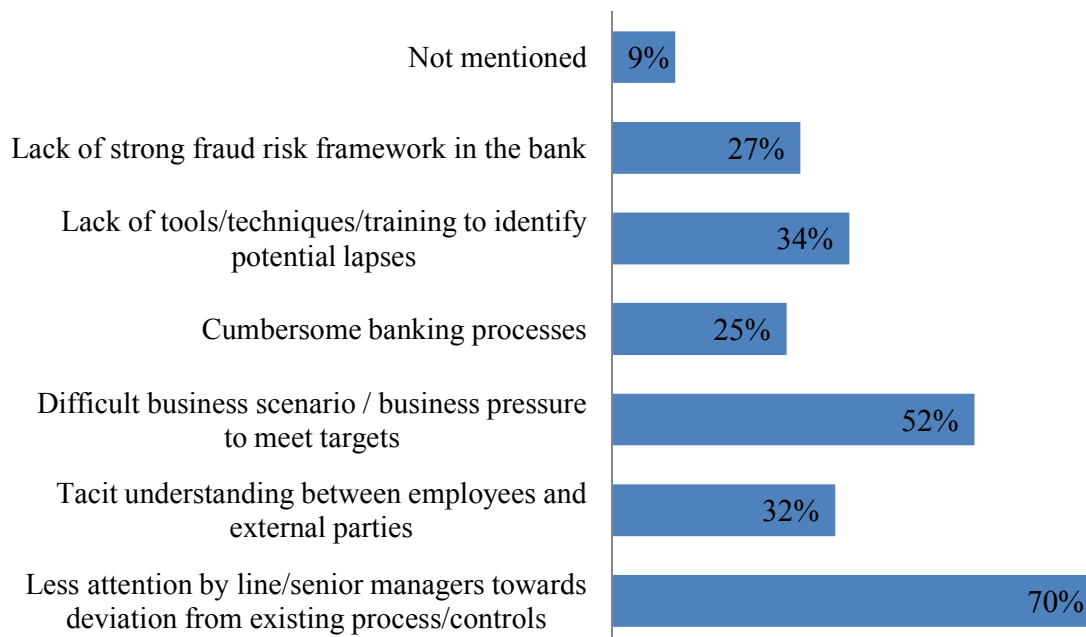


Figure 3. Likely reasons for frauds

From the above figure, we can see that “less attention by line/senior managers towards deviation from existing process/controls” and “difficult business scenario / business pressure to meet targets” were cited by the respondents as the two most significant reasons responsible for frauds. It is interesting to note that apart from the expected “tacit understanding between employees and external parties”, respondents also indicated “lack of tools/techniques/training to identify potential lapses” as another important reason for frauds.

The fourth question was about the possibility of tacit understanding between employee(s) and external parties.

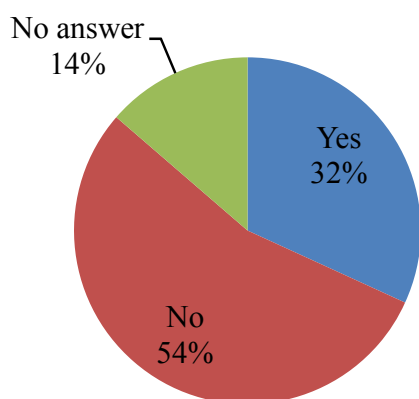


Figure 4. Tacit understanding between employees and external parties

Just 32% of the respondents agreed that there was tacit understanding between bank employee(s) and external parties in case of frauds. As many as 54% of the respondents said that there was no tacit understanding between bank employee(s) and external parties in case of frauds. One must, then, think about the reasons for increase in bank frauds. Is this a pointer towards need for suitable training for the employees to plug the possible lacuna in the banks' internal working and to be more diligent in their work?

Yes, we think that banks should sensitize the employees about their responsibilities and obligations through suitable training. Regular tests and training about specific operational areas, including the identification of possible fraud scenarios, would help the employees to rule out the possibility of frauds. A strong disciplinary system also needs to be put into place to counter any possible temptation. Clear communication and fair implementation of deterrent actions would make the employees more careful and result in reduction/prevention of negligent/fraudulent actions.

The fifth and sixth questions were related to fraud risk management framework in the bank. For tackling the increase in frauds, the Reserve Bank of India introduced guidelines for comprehensive Fraud Risk Management (FRM) system for banks. A fraud risk management system is supposed to include controls that help prevent happening of frauds, detect fraud as and when it happens, and also provide proper mechanism to limit the adverse consequences of fraud. Therefore, the fifth and sixth questions related specifically to existence and implementation of fraud risk management framework.

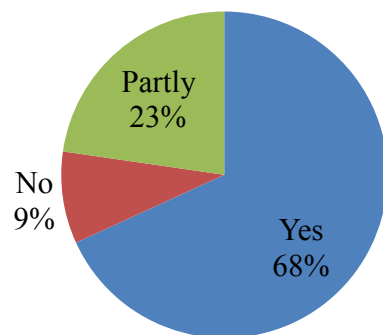


Figure 5. Existence and Implementation Status of Fraud Risk Management Framework

Over two-third of the respondents said that their bank has a formal fraud risk management framework to handle the frauds. This is very encouraging when we see that 23% of respondents have partly implemented a fraud risk management system in their banks. With increasing frauds, it is really surprising that 9% of the respondents said that they have not implemented any formal FRM framework.

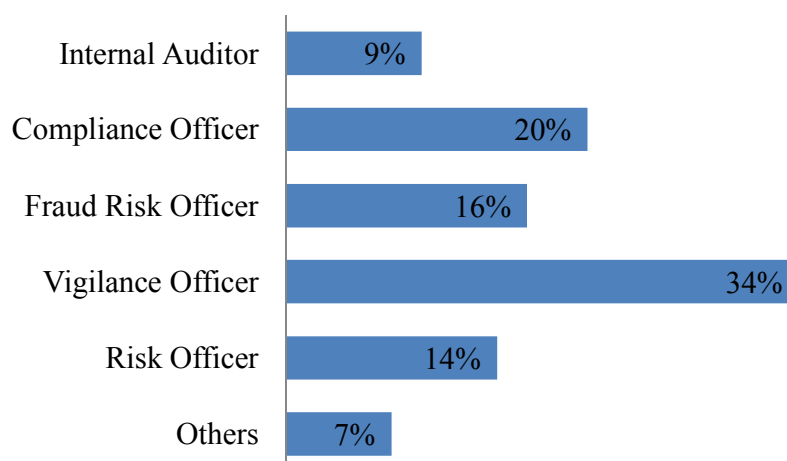


Figure 6. Responsibility for Fraud Risk Management

As per RBI's September 2009 circular mentioned above, the fraud risk management and fraud investigation function must be owned by the bank's CEO, its Audit Committee of the Board and the Special Committee of the Board. Further, they should set up a dedicated outfit to manage this function. To ensure that fraud controls are effective, responsibility for the bank's fraud risk management should be entrusted to a person at the senior level who can interact with different internal departments like internal audit, vigilance and risk management. From figure 6, we can see that the responsibility of fraud risk management is with the vigilance officer as per 34% of the respondents. However, only 16% of the respondents said that there is a separate fraud risk officer to exclusively look after the fraud risk management. Compliance officer was indicated as being responsible for fraud risk management by 20% of the respondents with another 14% of the respondents saying that the responsibility for this activity lies on risk officer.

The next question was about status of training for forensic audit / fraud prevention as per RBI directives.

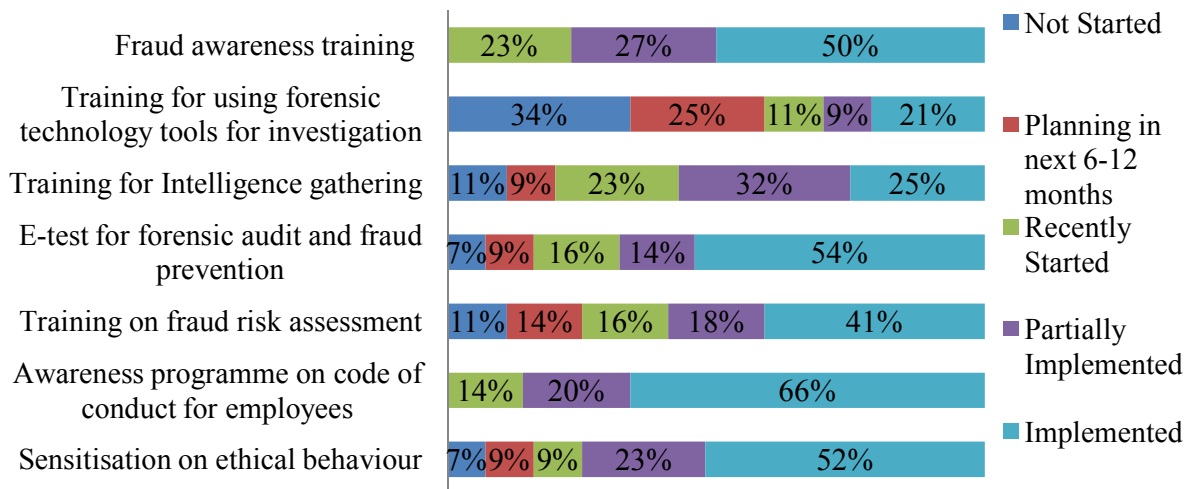


Figure 7. Status of training for forensic audit / fraud prevention as per RBI directives

We can see that fraud awareness training has been implemented by 50% of the respondent banks and others have either partially implemented or started recently. Training for use of forensic technology tools has been completed by only 21% of the respondent, 25% are planning in the next six months and as many as 34% had not yet started. This is an important area which needs to be looked into quickly by the banks. Training for intelligence gathering also needs to be improved as only 25% of the respondents have fully implemented it. E-tests for forensic audit and fraud prevention have been conducted by 54% of the respondent banks. Training on fraud risk assessment is another area where implementation is on the lower side. Awareness programme on code of conduct for employees and sensitization on ethical behavior has also been fully implemented by 66% and 52% of the respondent banks respectively. Thus, three thrust areas for banks, where implementation needs to be improved are: training for using forensic technology tools for investigation, training for intelligence gathering, and training on fraud risk assessment.

The next question was about banks’ plans for training programmes within next 6-12 months.

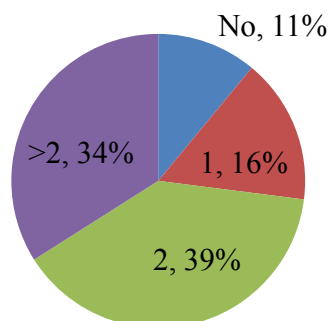


Figure 8. Number of training programmes planned within next 6-12 months

Training is an ongoing activity and the identified bank staff needs to be provided information and training about latest forensic audit techniques and tools. We can see that 90% of the banks had at least one training programme planned during the next 6-12 months.

The next question was about expectations related to cost of fraud awareness and forensic audit training, fraud detection/analytic solutions and setting up or consolidation of fraud detection / forensic audit cell.

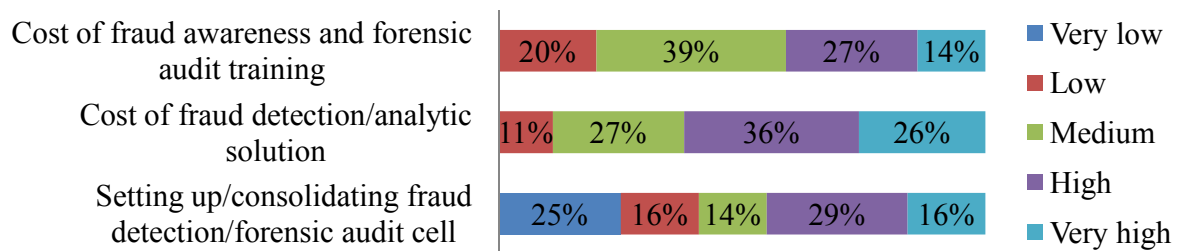


Figure 9. Expectations related to cost of forensic training and related aspects

We can see that a large percentage of respondents feel that cost of fraud awareness/forensic audit training, fraud detection/analytic solutions and setting up or consolidation of fraud detection / forensic audit cell is going to be high. It is obvious that with RBI regularly impressing upon the banks to firm up their infrastructure for fraud detection and forensic auditing, the banks have to make regular efforts to comply with the RBI directives, causing some increase in the cost for the banks.

The last question was: Have the training programmes in forensic audit and fraud detection been useful to detect and prevent frauds?

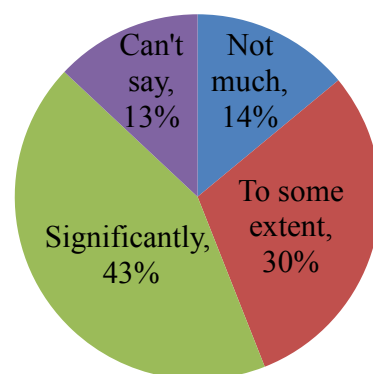


Figure 10. Usefulness of training programmes in forensic audit and fraud detection to detect and prevent frauds?

We can see that majority of the respondents (73%) have positive attitude towards the usefulness of training programmes in forensic audit and fraud detection being useful to detect and prevent frauds. This is really encouraging and there should be no let up in efforts towards providing more and regular training.

Conclusion

From the discussion in the previous section, we can draw the following conclusions:

- Majority of the respondents feel that, in general, there has been an increase in the number of frauds in the banking industry in the previous year.
- As many as 73% of the respondents said that their bank had experienced more than one incident of fraud in the previous one year, with 52% of them experiencing six or more incidents. Further research can be done to find differences in case of public and private sector banks and also to find the relationship between size of bank's assets and number of frauds.
- It was found that "less attention by line/senior managers towards deviation from existing process/controls" and "difficult business scenario / business pressure to meet targets" are the two most significant reasons responsible for frauds. Respondents also indicated "lack of tools/techniques/training to identify potential lapses" as another important reason for frauds.
- Just 32% of the respondents agreed that there was tacit understanding between bank employee(s) and external parties in case of frauds. Still, the present authors feel that there is need for suitable training for the employees to plug the possible lacuna in the banks' internal working and to be more diligent in their work.
- Over two-third of the respondents said that their bank has a formal fraud risk management framework to handle the frauds. With increasing frauds, it is really surprising that 9% of the respondents said that they have not implemented any formal FRM framework.
- Most of the banks do not have a dedicated person for fraud risk management and fraud investigation function.
- Regarding training in fraud detection and forensic audit, the three thrust areas for banks, where implementation needs to be improved are: training for using forensic technology tools for investigation, training for intelligence gathering, and training on fraud risk assessment.
- Training is an ongoing activity and the identified bank staff needs to be provided information and training about latest forensic audit techniques and tools. It is encouraging to see that 90% of the surveyed banks had at least one training programme planned during the next 6-12 months.
- It was also found that a large percentage of respondents feel that cost of fraud awareness/ forensic audit training, fraud detection/analytic solutions and setting up or consolidation of fraud detection / forensic audit cell is going to be high in the next 1-2 years.
- However, majority of the respondents have positive attitude towards the usefulness of training programmes in forensic audit and fraud detection being useful to detect and prevent frauds. This is really encouraging and there should be no let up in efforts towards providing more and regular training.

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Appendix

List of banks included in the survey

Allahabad Bank	Karur Vysya Bank
Andhra Bank	Kotak Mahindra Bank
Axis Bank	Oriental Bank of Commerce
Bank of Baroda	Punjab and Sind Bank
Bank of India	Punjab National Bank
Bank of Maharashtra	South Indian Bank
Canara Bank	Standard Chartered Bank
Catholic Syrian Bank Ltd.	State Bank of Bikaner and Jaipur
Central Bank of India	State Bank of Hyderabad
Citibank Na	State Bank of India
Corporation Bank	State Bank of Indore
Dena Bank	State Bank of Patiala
Dhanlaxmi Bank Ltd	State Bank of Travancore
HDFC Bank Ltd	Syndicate Bank
HSBC	The Bank of Rajasthan Ltd
ICICI Bank Ltd	The Federal Bank Ltd
IDBI Bank Ltd	The Jammu and Kashmir Bank Ltd
Indian Bank	UCO Bank
Indian Overseas Bank	Union Bank of India
Indusind Bank Limited	United Bank Of India
ING Vysya Bank Ltd	Vijaya Bank
Karnataka Bank	Yes Bank