

TECHNIQUES OF FRAUD INVESTIGATION

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- » **BASIC PRINCIPLES OF FRAUD INVESTIGATION**
- » **INITIAL ASSESSMENT OF FRAUD**
- » **CONFIDENTIALITY IN INVESTIGATION**
- » **CHAIN OF CUSTODY**
- » **LEGAL CONSIDERATION OF INTERVIEW**
- » **EXAMPLES OF DOCUMENT VERIFICATION**
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1.

Fraud Investigation

Basic Principles of the Fraud investigation process



The term Fraud Examination / Investigation refers to the process of resolving allegations of fraud from inception to disposition. Whereas, Forensic Accounting means use of professional accounting skills in matters involving potential or actual civil & criminal litigation.

- » Assume Litigation will Follow
- » Act on Predication
- » Dual Approach Investigation
- » Move General to Specifics
- » Use Fraud Theory Approach

Principle

Each Fraud Investigation should be conducted with assumption that at closure of investigation a litigation will follow

Background

This ensures that the person conducting the fraud investigation will follow appropriate legal guidelines and will document the evidence appropriately.

EXAMPLE

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In a case of employee expense fraud, fraud investigator, based on a tip received, investigated an employee for submission of fake expense claim. In investigation, the person was interviewed and he agreed that he has committed the fraud. On the basis of his statement, appropriate action was taken against him by the company.

Post which he filed a suit against the company's action on the grounds that the action being discriminatory in nature. The statement he made during the interview was not documented anywhere neither any formal report was made for this investigation.

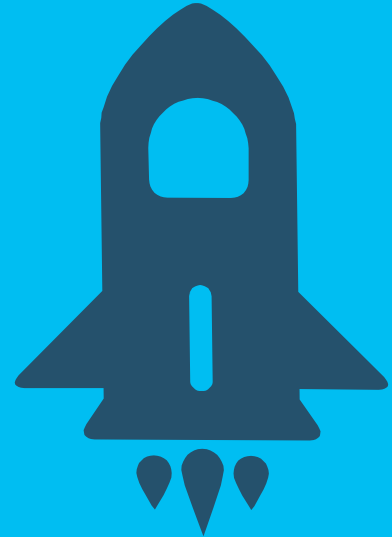
As an Fraud Investigator what will you do?

INVESTIGATION MUST BE DOCUMENTED

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If an Investigation is not appropriately documented including all the evidences then it may happen that the company or client, at a later stage, may unable to prove that the appropriate action which has been taken is legitimate.

IF INVESTIGATION IS NOT DOCUMENTED... THEN
INVESTIGATION IS NOT DONE...



Principle

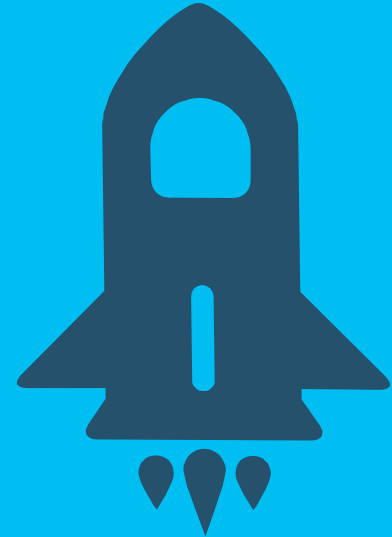
Predication is the all circumstances that would lead a fraud investigator to believe that a fraud has occurred or it can occur. It means the base on which investigation is done.

Background

If a fraud examination is not done on the basis of Predication then it can expose the employer or clients to the huge liabilities.

Evaluating Predication is a continuous process. Fraud investigator needs to evaluate at every stage after getting every new information in the Fraud investigation.

IF NO PREDICATION... THEN NO INVESTIGATION...



EXAMPLE

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Based on a tip received for fake expense claim about an employee, the fraud examiner started the investigation. In the initial phase, it was found that the employee's expense claim is thrice compared to normal employee at the same level (Field Engineer).

However, upon extracting additional details about his assignments, it was identified that usually a normal employee used to handle 10 to 12 assignments monthly whereas, the employee under suspect has complete more than 30 assignment monthly on an average. Also, upon understanding the nature of expense they incur, it was identified that expense incurred are directly proportionate to the number of assignments they complete. Would you still move for investigation?

Principle

Fraud Investigator should always investigate from two perspectives i.e. 1) Fraud has occurred and 2) Fraud has not occurred. The way to prove fraud has occurred is to prove that fraud has not occurred and vice versa.

Background

This ensures the objectivity of the fraud examiner is intact and he is not biased to any of the side. This helps in establishing the guilt behind the fraud i.e. presence of Mens Rea (Guilty Mind).

Principle

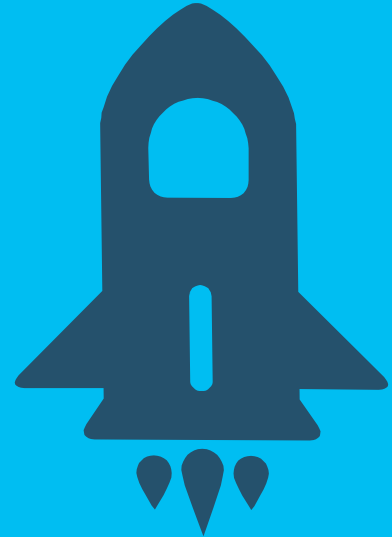
Fraud Investigator should always move from general to specific details. He should start at periphery, and then he should move to the center of the matter.

Background

This ensures that all the details are available with the fraud investigator when he finalizes and reports a case, no matter whatever small detail it is. Each and every detail and evidence is necessary to decide the outcome of the case.

If Fraud Examiner directly investigates the centre, then there are huge chances that he will investigate with limited knowledge but more with perspective.

Fraud Examination should be based on more of INFORMATION and less of PERSPECTIVE.



FLOW OF INVESTIGATION

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Firstly, the natural third person is investigated and minute details about the matter are gathered

Secondly, the person suspected of complicity is investigated, starting with least culpable person

Lastly, the prime suspect and by this time major information is available for prime suspect

Principle

Fraud Investigator should follow the fraud theory approach to investigate the allegations. Fraud theory approach is :

- 1) Analyzing Available Data
- 2)Creating Hypothesis
- 3)Testing Hypothesis
- 4)Refining Hypothesis.

Background

Fraud Theory Approach is a tool kit which helps in understanding the situation and scenario. It also helps in guiding the investigation.

Under this approach, the investigator first analyze the data which is in the hand. Then builds a hypothesis based on the available data. Hypothesis is nothing but a supposition or proposed explanation made on the basis of limited evidence as a starting point for further investigation. Then he test the hypothesis by collecting new data through various techniques and analytics. Once the additional data is available then the fraud examiner should verify whether his existing hypothesis is valid or not i.e. whether it is provable or not. Based on that he should amend his hypothesis and he should continually revise and test his theory until the fact becomes provable or they conclude that there is no fraud or fraud cannot be proved.

EXAMPLE

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Mr. A, Forensic Auditor of X Limited received a call, from an unknown person, that Mr. P the purchasing manager of the company is favoring certain purchasers who are paying him some kickbacks.

How Mr. A should move forward in this case?

EXAMPLE

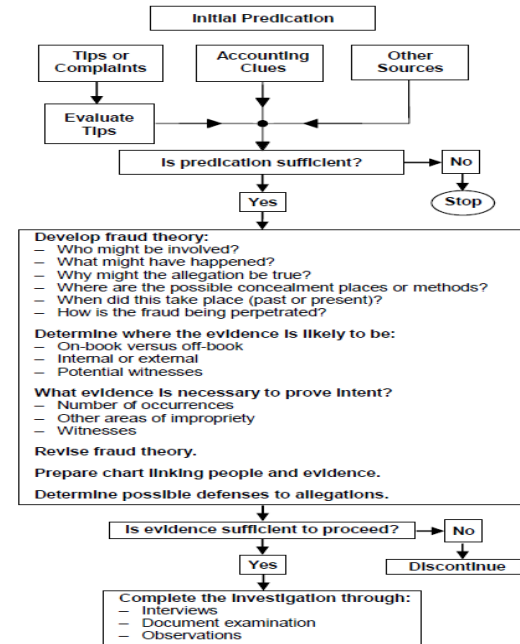
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Mr. A, should first analyze the data available on the hand, in the current case the allegation is Mr. P is receiving kickbacks for supply purchase contracts to certain vendors. Then Mr. A should build a hypothesis, that it might be possible or the call was hoax (Dual Approach). Then he should test the hypothesis by collecting the additional data. Additional data can be procurement records, supplier master data, material quality reports, etc. Then he should revisit his hypothesis based on the additional data. For example, if Mr. A found that the orders are processed based on the lowest quotation and they are awarded not only to one vendor but to multiple vendors then he needs to change his hypothesis.

Flow Chart for the Fraud Theory Approach

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First based on the source, FE builds the initial predication. Then he evaluates the initial predication. If sufficient, then he proceeds to develop a hypothesis. Then he collects the additional information to test the hypothesis. If sufficient evidence is found then he will complete his investigation through various techniques. Otherwise, he will stop or discontinue.



2.

Initial Assessment of Fraud

How to perform initial fraud investigation process



When usually fraud arises there are not enough evidence known and facts present to carry a formal investigation. An initial assessment tests the allegation and verifies the need of formal investigation process. Initial Assessment should be quick and limited to fact finding process unlike formal investigation which requires a detailed plan.

- » Understand the Context
- » Review the Policy & Procedures
- » Investigate the Allegations
- » Contacting the Source
- » Document the Initial Response

- » Before proceeding one should focus on understanding the allegation made. Understanding the allegation is the prime most factor and deciding factor of any fraud investigation.
- » Then comes the manner in which the allegation was known, then the date of allegation, period of allegation (fraud), source of information, and areas and person involved.
- » This will provide the appropriate direction to all the subsequent activity.

EXAMPLE

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Mr. A, Forensic Auditor of X Ltd received a call, from an unknown person, that Mr. P the purchasing manager is favoring certain purchasers.

What Favoring means, It can mean kickbacks, it can mean that purchasers are at good terms with Mr. P or it can mean that the purchasers are related party to Mr. P.

Hence understanding the allegation is prime most important step in any fraud investigation.

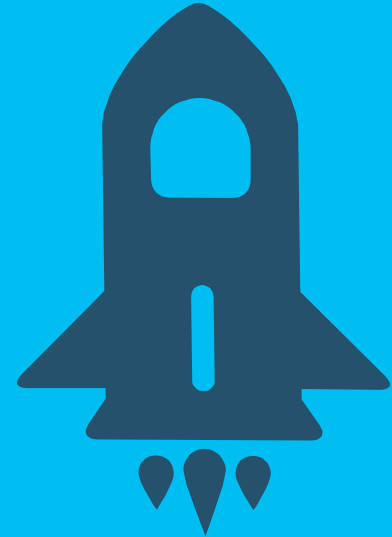
- » After understanding the context, one should review the policy and procedure of the company. Most of the companies have specific reporting policy when such allegations are received.
- » It may happen that the company might already have a procedure defined for handling such allegations if any received by the fraud investigator.

- » Initial assessment should be limited to fact finding and it should focus on investigating the specific allegation received. Various questions he should ask related to allegations like
- » Whether the allegation are appropriate, how they are related to company, which department is affected the most, is the fraud ongoing or it was at one point in time, what level of employees are involved, whether any third party are involved, whether any government officer or authority is involved, is it possible that it might larger than it appears, whether any such previous incident reported or investigated, etc.

- » If the person who has provide the information is traceable then contacting the source will become utmost important as the following question answered by him or her will give additional key information to procedure further:
- » What does he know more, from where he received the information, whether he was involved at any point in time, when did he come to know, what are the dates he is aware of, Is he witness to the allegations, who else has the information, Why he is raising question what is his motive, etc.

If an Investigation is not appropriately documented including all the evidences then it may happen that the company or client, at a later stage, may unable to prove that the appropriate action which has been taken is legitimate.

IF INVESTIGATION IS NOT DOCUMENTED... THEN
INVESTIGATION IS NOT DONE...



3.

Confidentiality in Investigation

Why Confidentiality is required in fraud investigation process

- » If the confidentiality is not maintained then:
 - » Information will become public compromising the investigation (alerting the suspect)
 - » Employees might not report the future events or might not provide the details of current issue
 - » If suspicion comes as false then it might damage the reputation of the person on whom allegation was made

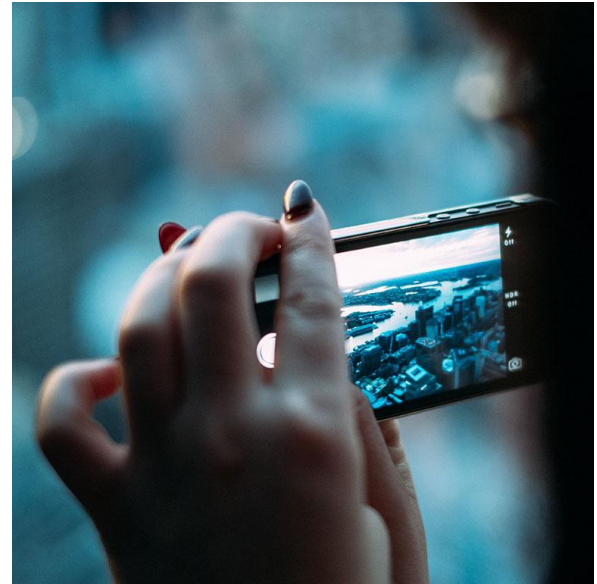
- » Never alert the Suspect;
- » Request participants' confidentiality;
- » Protect the information of case;

- » If the suspect is alerted then:
 - » He might try to destroy the evidence available, he might try to alter or fabricate the evidence.
 - » If allegation is for any on going activity then he might stop performing the same.
 - » There are chances that he might try to flee or leave organization as soon as possible.

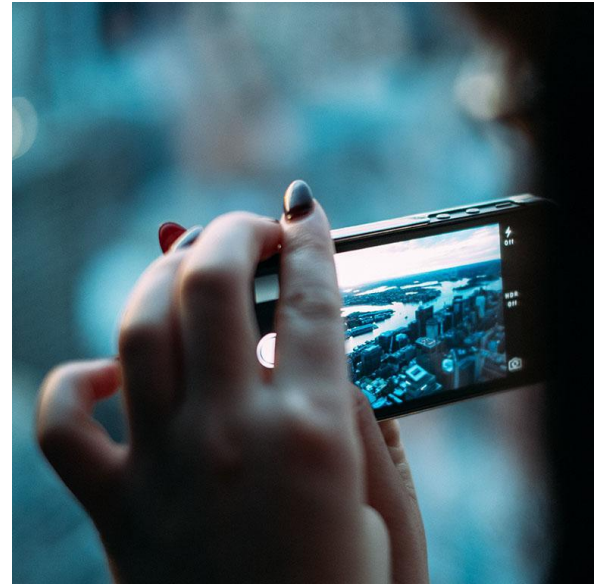
REQUEST PARTICIPANTS' CONFIDENTIALITY

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- » When possible as per policy and law, management must ask the employees involved in the initial phase of investigation to refrain from discussing investigation information with anyone.
- » If possible, management may require employees to sign an confidentiality oath vowing to divulge any information regarding investigation.



- » At most care should be taken with data privacy.
- » All the relevant data must stored safely and should not be circulated to persons who need not to know
- » Access restriction should be used for the places where data is stored (Physical and Virtual both).



- » Following are the basic measures that one must take:
 - » Know who is under suspicion and what accesses he has.
 - » Limit the discussions in public places or common areas.
 - » Inform only those who need to know.
 - » Investigate without disrupting the office normal course of business.
 - » Investigate fast as time is crucial factor.
 - » Investigate in non-business hours.

4.

Chain of Custody

What is Chain of Custody and why it is important

- » From the moment evidence is received a chain of custody log should be maintained.
- » Chain of custody is a process and a document both wherein it is enumerated that who had the possession of the documents at what time frame and what procedures were performed by him over the documents.
- » Establishing chain of custody is utmost important for proving the credibility and authenticity of the evidence.
- » It proves that the evidence has not been altered since it was gathered for the case.

5.

Legal Considerations of Interview

What to be taken care of while conducting interviews

- » Conducting Interviews and investigation with people and employees can result in liabilities and ramification for the fraud investigator and the company. For eg: harassment, discriminatory proceedings, favoritism, etc.
- » In a fraud investigation, rights of people involved varies from level to level and hence it becomes crucial to consider the legal aspects of the same.
- » For eg: In a bribery fraud, where a government officer is also involved, can the company's fraud investigator interview or question that government official?

- » First of all, we need to see whether we are legal authorized to conduct the investigation or interview.
- » Whether the company's policy and procedure allows us to move ahead and conduct the interviews and investigation.
- » Whether conducting an interview is will result in breach of any fundamental rights of that person.
- » For eg: In a bribery fraud, where a government officer is also involved, can the company's fraud investigator interview or question that government official?

- » Imprisonment is means restraining a person of the physical liberty. False imprisonment means restraining a person without his consent and legal justification
- » Like locking the doors of interview rooms, standing in front of the doors, refuse to allow exit to the person, etc.
- » False imprisonment can cause huge ramifications upon the fraud investigator or the company.
- » For Eg: What if any employee files a suit of workplace harassment against the company for discriminatory behavior due to cast or religion?

- » Section 339 & 340 of Indian Penal Code Wrongful Restraint and Wrongful Confinement are punishable offence.
- » As per section 341 and 342 the punishment for the same is imprisonment ranging from one month to one year with various fines.

- » Use of deception in interviews and investigation with people can cause legal suits of fraud upon the company and investigator.
- » At times evidences obtained through deception are not legally admissible in the court of law
- » Over and above to that it may happen that a legal suit for cheating under section 415 of the Indian Penal Code.
- » The punishment for the same can range from one month to one year with fine.

- » Recording call, interviews, meetings or conversation without the consent of the person is illegal in various jurisdiction.
- » The General Data Protection Regulation (GDPR) in the European Union mandates that call, meetings, interviews or conversation should not be recorded with the consent
- » Doing so, it may attract legal liabilities for us.

6.

EXAMPLES FOR DOCUMENTS

Certain examples as to which documents can be investigated

- » Contracts allotted to vendor, quotations from other vendors, vendor enrollment procedure, Vendor Master data, Vendor Relation with employees.
- » Quality report of vendor's raw material, verification of price escalations, quantum of raw material reject, etc.
- » To ensure Kickbacks, Bank accounts and credit card statement of employee, unusually spending by the employee, etc.
- » Segregation of Duties, Controls & Internal Checks on place.
- » Review Reports by supervisors.

- » Monthly Payroll Statement, Employee Master Verification, Duplicate Master Check, Duplicate Bank Details Check, etc.
- » Monthly working hours statement, Attendance Sheets, Pay Rate Register, etc.
- » Leave Calculation records, payroll calculations and deduction statement, etc.

- » Sales Register, Monthly Sales Trend, Goods Return Details, sale to customer quantum, Sale report agent wise, good return report agent wise, etc.
- » Commission records, Price register, Bad-Debt trend and customer wise analysis, etc.

- » Employee Expense Reports, Quantum of expense claimed, allowable limit of expenditure for that employee, type of expenses claimed, mode of expenditure and claim.
- » Appropriate approvals for expense claim, period of claim and date of submissions, listing of supporting's for expense, etc.

Questions ?

THANK YOU!