Fraudulent firms' revenue grew during slowdown

The study found that promoters have been involved in most cases of fraud

TRITHESH NANDAN | NEW DELHI | JUNE 25 2013

The financial crisis in 2008 hit the revenues of many companies in the world. But this was no deterrent on the revenue generation of the Indian companies which were indulging in fraudulent practices. A new study finds there has been a spurt of fraud cases and a corresponding increase of revenue generation of such companies since 2009.

“The average revenue of the companies involved in fraud after 2009 is Rs. 1,538 crore, significantly higher than before 2009, exposing the interests of a larger number of stakeholders to risks of corporate failure,” says the study done by Global Compact Network India and Thought Arbitrage Research Institute (TARI).

The study adds that revenue from fraudulent practices have seen an increase of five times since 2009. “The average size of fraud detected pre-2009 was around Rs. 200 crore whereas this was around Rs. 1,040 crore in the post-2009 data set which reflects an almost 5 times increase,” notes the study which is based on the analysis of 100 cases of corporate frauds from 2007-2012. The data has been collected after studying information gathered from the cases which are under investigation with the Serious Fraud Investigation Office (SFIO), Central Bureau of Investigation (CBI), income tax department, ministry of corporate affairs (MCA) and enforcement directorate (ED).

Most of the fraud has been happening with the blessings from the promoters or the top management. The study says that 36 percent of the involvement in fraud takes place either promoters or top management. “Significant motivator for fraud is personal enrichment at the cost of all other stakeholders,” the report highlights. It noted that 13 percent of the bilking companies were involved in the defrauding the government.

Thirty two percent companies were involved in falsifying assets. The study observes, “Inappropriate disclosures and disregard to prudent revenue recognition norms has gained prominence detected after 2009.”

The study blames the big auditing firms (Deloitte Haskins & Sells, Ernst & young, KPMG and PricewaterhouseCoopers) for aiding fraud
“Companies audited by the Big 4 audit firms accounted for 57 percent of the total fraud amount in the sample, suggesting that a Big 4 audit firm contributed to a significant amount of the fraud if not the number of fraud companies,” according to the study.

The number of big audit firms audited 24 percent of the companies while rest was done by the small or medium sized audit firms.

The public limited companies have been involved more in the fraud than the private limited companies. “In the sample data 57 percent of the public limited and 43 percent of the private limited companies had registered cases of fraud. Every sector of the economy is equally affected by fraud,” the report points out.

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The study found that the manufacturing sector is involved in maximum instances of fraud followed by the real estate companies and information technology sector.

But the penalty mechanism imposed has little effect on companies in stopping them from indulging in fraudulent methods. “Nearly 80 percent of the criminal prosecution cases filed by SEBI do not result any sentencing and 18 percent resulted in a sentencing of less than six months.”

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