
FORENSIC AUDITING IN CORPORATE FRAUD: ANALYSIS OF THE SATYAM AND PNB SCANDALS IN INDIA

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ABSTRACT

This paper examines the development and implementation of forensic auditing as a multidisciplinary mechanism for detecting and responding to large-scale corporate fraud in India, with a focus on the Satyam Computer Services and Punjab National Bank (PNB) scandals. Through theoretical analysis and profound case study, the paper reveals how forensic auditing differs from typical statutory audits by employing a scepticism-driven, legally sound technique that is capable of exposing purpose, identifying concealment, and reconstructing financial truth. It addresses the central question: *How has forensic auditing emerged as a response to the limitations of traditional audit mechanisms, and in what ways has it operated as a tool of legal and regulatory accountability in major Indian corporate frauds?* Drawing on concepts such as the Policeman Theory and Routine Activity Theory, this paper places forensic auditing in the context of institutional change and structural monitoring. The Satyam case exemplifies promoter-driven financial misreporting, whereas the PNB scam reveals systemic flaws in public banking infrastructure, both demonstrating the critical role of forensic audits in facilitating prosecutions, shaping regulatory responses, and prompting reforms such as auditor rotation and increased investigatory powers. Comparisons with the ongoing financial investigations in India's startup scene highlight its current relevance, as forensic audits are increasingly viewed as crucial to maintaining investor trust and ethical governance. The research suggests that forensic auditing should be considered not only as a reactive post-fraud method, but also as an important component of preventive compliance and regulatory architecture in India's evolving corporate landscape.

Keywords: forensic auditing, corporate fraud, Satyam scandal, PNB scam, statutory audit limitations, corporate governance, regulatory reform, financial transparency.

Introduction

Over the past two decades, both in India and globally, the landscape of corporate finance has been dramatically reshaped by a series of high-profile scandals, that have exposed deep deficiencies in conventional financial oversights. The Enron and Wirecard failures have demonstrated how, while statutory audits are required for financial responsibility, they often fail to identify deeply embedded frauds like managerial collusion, forged documents, and systematic manipulation. In India, the Satyam Computer Services scandal (2009) and the Punjab National Bank (PNB) scam (2018) have severely hampered public trust in corporate governance and regulatory effectiveness. These scandals brought to light that traditional audits, which are focused on materiality requirements, risk-based sampling, and internal confirmations, are inadequate for dealing with sophisticated, large-scale financial fraud.

In response to these challenges, forensic auditing has arisen as a distinct and prime discipline that awaits at the crossroads of accounting, investigative methodology, and legal analysis. It goes beyond discovering financial irregularities to reconstructing the story of intent, concealment, and collusion in a way that meets legal criteria. Forensic auditing has risen as the preferred method for detecting complex frauds and initiating enforcement, owing to technical capabilities such as data analytics, digital forensics, and behavioural modelling. As India's corporate and financial structures become more complex and globally integrated, there is an increase need for regulators, investors, and courts to rely on forensic auditing in order to ensure substantive accountability rather than procedural compliance.

Forensic Auditing: Distinctive Features

Forensic auditing is more than just a more stringent version of traditional auditing; it is a paradigm shift. It adopts an exploratory rather than a confirmatory approach. Unlike statutory audits, which are governed by materiality standards and risk-based sampling, forensic audits have assumed the possibility of fraud and aim to construct an evidence narrative that can possibly withstand judicial examination. It is described as the application of accounting concepts and techniques to legal situations, typically with the goal of giving evidence in a court of law¹. Forensic auditing involves identifying, interpreting, and providing evidence related to

¹ G.S. Smith & D.L. Crumley, *Defining a Forensic Audit*, 4 J. Digital Forensics, Sec. & L. 61 (2009), <https://doi.org/10.15394/jdfsl.2009.1054> (Last visited April 19, 2025).

significant financial and reporting activities. This approach is based on the "Policeman Theory" of auditing, which poses auditors as active enforcers of financial propriety rather than passive record-checkers². Traditional audits main focus is conformity with norms and standards such as the Indian Accounting Standards (Ind-AS) and the International Financial Reporting Standards (IFRS), whereas forensic audits go deeper and investigate the motivating factors behind compliance. They utilize data mining, email forensics, document verification, and behavioural analytics to detect organized deception practices³.

This is particularly significant in the post-IFRS era, as principles-based accounting systems allow for greater managerial flexibility in financial interpretation. While such discretion provides flexibility, it also creates uncertainties that might be misused. Forensic auditing thrives in such murky areas by focusing on the economic substance of transactions, identifying red flags in patterns, and tracing money's origins and destinations. The methodology indicates a hybrid discipline where forensic accountants need to balance financial understanding, legal literacy, and investigative psychology. According to Singleton et al., the forensic auditor must be "part accountant, part cop, and part lawyer"—a profession that is especially suited to uncover financial deceit in today's commercial world⁴.

Institutional Developments and Regulatory Trends in India

While forensic auditing has not yet been incorporated as a statute in India, regulatory authorities have often relied on its approaches to confront corporate malfeasance. Two significant developments to demonstrate this trend are:

In 2021, the Reserve Bank of India (RBI) mandated forensic audits for borrower accounts suspected as fraudulent, with a focus on accounts with exposure over ₹50 crore. This mandate represented a significant departure from the conventional method of passively reading financial figures. Instead, it advocates for a more in-depth review of the borrower's intents and behaviour, with an emphasis on potential deception, fraudulent activities, and the underlying motivations behind financial misreporting⁵. The RBI's approach places a greater importance on identifying the root causes of financial wrongdoing and enforcing accountability at a more

² *ibid.*

³ A.O. Enofe, P. Omagbon & F.I. Ehigiator, *Forensic Audit and Corporate Fraud*, 1 Int'l J. Econ. & Bus. Mgmt. 1 (2015), <https://www.iiardjournals.org/get/IJEBM/VOL%201/55-64.pdf> (Last visited April 19, 2025).

⁴ *ibid.*

⁵ Bhumesh Verma & Himani Singh, *Evolution of Corporate Governance in India*, (2019) PL (CL) November 69.

granular level, signalling a shift towards a more proactive and forensic inspection in the banking and financial sectors.

Second, the Securities and Exchange Board of India (SEBI) has increasingly relied on forensic audits as a key regulatory instrument, particularly under the SEBI (Prohibition of Fraudulent and Unfair Trade Practices) Regulations, 2003⁶. Forensic audit reports have proven essential in discovering and presenting important evidence in cases that involve complicated financial crimes such as insider trading, price manipulation, and financial statement fraud. These audits not only serve to uncover irregularities, but also help build a stronger case for enforcement measures, improving SEBI's ability to regulate and protect the integrity of the securities market. Forensic audits will always continue to play a significant role in SEBI's investigation processes, adding significantly to the transparency and fairness of India's capital markets⁷.

Simultaneously, the Companies Act of 2013⁸ made a significant contribution in forensic auditing by establishing the Serious Fraud Investigation Office (SFIO) under Sections 211 and 212. The establishment of the SFIO marks the Indian government's concerted effort to deal with major corporate fraud and bring about a fundamental change in how corporate malfeasance is handled. The SFIO is responsible for investigating complicated financial scams, and its legislative backing strengthens its ability to undertake rigorous forensic examinations. However, the SFIO's efficiency has been limited by ongoing issues. According to recent literature, SFIO investigations frequently experience significant delays due to a lack of suitable resources, such as qualified personnel and technology infrastructure⁹.

Although organizations such as the Institute of Chartered Accountants of India (ICAI) have produced guidance notes and held training programs, a unified national framework for forensic auditing, akin to the ACFE requirements, remains elusive. The lack of obligatory criteria, consistent certification, and legal regulations has caused dispersed adoption.¹⁰

Satyam Computer Services Scandal

The Satyam scandal of 2009 is India's most notorious case of internal corporate fraud,

⁶ SEBI (Prohibition of Fraudulent and Unfair Trade Practices) Regulations, No. 2, Acts of SEBI, 2003 (India).

⁷ Prashanth Sabeshan & Sindhu V. Reddy, *India's Current Corporate Governance Practices - Impact & Challenges*, (2013) 1.7 JCLG 779.

⁸ The Companies Act, 2013, No. 18, Acts of the Parliament, 2013 (India).

⁹ Kalyani Karnad, *The Role of SFIO With Regard to Corporate Governance*, (2019) 3.1 JCLG 150.

¹⁰ *Id.* at 5.

highlighting severe deficiencies in the country's corporate governance framework. The scandal revolved around Ramalinga Raju, the founder and Chairman of Satyam Computer Services. He admitted to inflating the company's sales by ₹5,000 crores and misreporting cash balances by over ₹5,040 crores. To maintain the appearance of financial health, the company manufactured hundreds of faux employees and modified bank records to paint an overly optimistic picture of profitability¹¹.

Forensic audits, particularly those done by businesses such as KPMG, were essential in exposing the scope of the fraud. These audits revealed a number of fraudulent tactics, such as fake invoices, hidden liabilities, circular transactions, and fabricated documents. The evidence uncovered during forensic investigations was critical in initiating criminal actions against the company's management. The proceedings were initiated under various sections of the Indian Penal Code (IPC)¹², including Sections 420 (cheating), 467 (forgery of valuable security), 468 (forgery for the purpose of cheating), and 477A (falsification of accounts), as well as corporate law violations under the Companies Act of 1956¹³.

This scam exposed some serious procedural lapses on the part of statutory auditors, specifically PwC, who failed to independently verify the company's financial statements. PwC had relied too heavily on internal management representations and failed to acquire essential independent confirmations from banks, allowing the fraud to go undetected for an extended period¹⁴. As a result, the Securities and Exchange Board of India (SEBI) restricted PwC from auditing publicly traded firms for two years, and the Securities and Exchange Commission of the United States (SEC) penalized the firm \$6 million for its role in the incident.

Post Satyam, India's regulatory environment underwent some significant reforms. Where one of the most important legal improvements was the implementation of mandated auditor rotation under Section 139 of the Companies Act of 2013¹⁵, which was intended to limit the risk of audit complacency and conflicts of interest¹⁶. Furthermore, the Serious Fraud Investigation

¹¹ Kalikant Mishra, M. Khalid Azam & S.O. Junare, *Role of Forensic Audit in Controlling Financial Statement Fraud: A Case Study of Satyam Computers*, 58 Psychol. & Educ. 4016 (2021), <https://doi.org/10.17762/pae.v58i2.2672> (Last visited April 19, 2025).

¹² Indian Penal Code, No. 45, Acts of Parliament, 1860 (India).

¹³ *ibid.*

¹⁴ Revati Raman Singh Rathore, *Role of Forensic Accounting in Satyam Scandal*, 11 Int'l J. Creative Res. Thoughts 4024 (2023), <https://ijert.org/papers/IJCRT23A4024.pdf> (Last visited April 19, 2025).

¹⁵ The Companies Act, 2013, §139, No. 18, Acts of the Parliament, 2013 (India).

¹⁶ Bhumes Verma & Sara Jain, *Independent Directors: Role, Responsibilities, Effectiveness*, (2019) PL (CL) July 75.

Office (SFIO) was given increased authority to conduct more thorough investigations into corporate fraud. As a result, the Satyam affair not only triggered these long-overdue regulatory reforms, but it also highlighted the critical role of forensic audits in detecting and addressing deeply rooted financial fraud within organizations.

Punjab National Bank (PNB) Scam

Unlike the Satyam scam, which was the result of internal manipulation, the Punjab National Bank (PNB) scam was a carefully staged example of collusion between corrupt bank personnel's and outside actors. This fraud exploited financial systematic flaws, resulting in the illegal transfer of about ₹14,000 crore. The offenders exploited unlawful Letters of Undertaking (LoUs) issued on the SWIFT platform to circumvent the bank's core banking systems and facilitate these fraudulent transactions¹⁷. Forensic audits were critical in revealing the complicated network of deception that supported this scheme. The forensic investigations yielded the following key findings:

- A network of shell companies, primarily controlled by the main perpetrators, Nirav Modi and Mehul Choksi who acted as fronts for laundering money.
- Persistent failures in the reconciliation of SWIFT messages, which allowed unauthorized LoUs to be issued without detection.
- Repeated violations of Reserve Bank of India (RBI) guidelines regarding foreign credit exposure, which provided the external actors with unchecked access to large sums of money¹⁸.

The forensic audits offered critical evidence that led to legal proceedings under the Prevention of Corruption Act of 1988, which culminated in the issuance of Red Corner Notices against the principal accused. Furthermore, the Fugitive Economic Offenders Act of 2018 was invoked, allowing for the confiscation of both domestic and foreign assets linked to the scam. In reaction to these discoveries, the RBI took quick corrective action, suspending the issuing of LoUs

¹⁷ Akshi Narula, *Financial Crimes in India*, (2018) 5.2 RFMLR 216.

¹⁸ T.C.A. Ramanujam & T.C.A. Sangeetha, *Bringing Absconding Economic Offenders to the Book*, (2018) 409 ITR (Jrn) 14.

entirely, as a preventive move to close the vulnerabilities exploited in the scam¹⁹.

The PNB fraud highlighted how forensic audits might go beyond mere post-crisis analysis and actively push systemic reforms. In this example, forensic audits not only helped reveal the scope of the fraud, but also prompted policy changes in the banking industry. However, this case demonstrated the drawbacks of standard compliance-based traditional auditing methodologies. The fraud was deeply embedded in institutional systems, making compliance checks insufficient to identify the complexities of such a large-scale financial scam. This highlighted the need for more advanced forensic auditing capabilities and a stronger framework for detecting systemic risks within financial institutions.

Comparative Insights: Structural and Legal Implications

Despite their disparities in strategies and scale, Satyam and PNB share a fundamental truth: forensic auditing is the only way to uncover both the mechanics and the motive behind corporate frauds. Traditional audits failed to detect red flags due to materiality thresholds and an overreliance on internal assurances, whereas forensic auditors succeeded by probing whole transaction trails, investigating behavioural patterns, and contextualizing financial abnormalities²⁰. In courtroom proceedings, forensic audit reports served not just as a technical financial document, but as a potent narrative weapon. They meticulously rebuilt the fraud in detail, following the flow of funds, identifying the key actors involved, establishing timelines, and revealing the strategies used to disguise illicit activities. These reports helped bridge the gap between raw data and legal accountability by presenting a cohesive and comprehensible picture of corporate wrongdoing.

However, these high-profile scandals highlighted significant weaknesses in India's enforcement landscape. In the Satyam case, for example, while U.S. investors were able to secure compensation through class action lawsuits under the American legal system, Indian investors had no such recourse. This difference highlights the underdeveloped state of India's private enforcement mechanisms, where aggrieved shareholders have limited options to pursue damages independently. Despite the increasing powers of public regulators like SEBI, the

¹⁹ *ibid.*

²⁰ Predrag Vukadinović, Goranka Knežević & Vule Mizdraković, *The Characteristics of Forensic Audit and Differences in Relation to External Audit*, Finiz Conf. Proc. 202 (2015), 10.15308/finiz-2015-202-205 (Last visited April 19, 2025).

absence of strong private enforcement options weakens the overall legal response to corporate fraud.

Moreover, India's inefficient contract enforcement and lengthy litigation timelines have created an environment of legal ambiguity, prompting many investors to seek arbitration in international jurisdictions such as Singapore and London. This tendency suggests a general lack of trust in the domestic conflict resolution system. Scholarly analyses have found that meaningful reforms, such as creating dedicated commercial seats in courts, implementing fast-track procedures for financial fraud cases, and improving coordination between regulatory and investigative bodies, could significantly improve forensic audits' deterrent and remedial capacity. Strengthening these structural components would ensure that forensic findings translated into fast and effective legal solutions, hence increasing both investor trust and corporate accountability.

Integration into Broader Governance Structures

The introduction of forensic audits into India's corporate governance ecosystem is a structural demand rather than a technical one. Academic literature has long criticized Clause 49 of the SEBI Listing Agreement for adopting a symbolic rather than substantive approach. While it encourages whistleblower frameworks but it does not compel them. This is significant because whistleblower disclosures are frequently the initial lead in fraud investigations. Furthermore, the effectiveness of audit committees is inconsistent. These panels are ineffective gatekeepers because they lack adequate independence and knowledge. According to recent industry interviews, even Indian private equity investors are increasingly requiring pre-investment legal and forensic due diligence—an emerging best practice that should be implemented across all high-risk sectors. India's enforcement system must also mature²¹. Regulatory entities such as SEBI and SFIO must work with tax authorities, the RBI, and the Enforcement Directorate to ensure that the insights gained from forensic audits are translated into cross-agency enforcement. Without such coordination, evidence may fall through institutional silos.

As a law student, I find the evolution of forensic auditing especially useful in understanding how regulation, finance, and legal accountability connect. It shows that corruption is rarely the product of single malfeasance, but rather a systematic failure assisted by ineffective oversight,

²¹ *Id.* at 7.

weak institutions, and regulatory lethargy. If we consider the ongoing investigation of a prominent Indian ed-tech business suspected of revenue overestimation and aggressive accounting practices. While the matter remains under investigation, there is a sudden societal dependence on forensic audits to validate financial integrity, particularly in startups that scale rapidly and attract global capital. In an environment where investor trust and public reputation are constantly changing, forensic auditing is no longer a reactive process, but rather the de facto standard for truth verification. In my opinion, the institutionalization of forensic auditing represents a philosophical shift in corporate governance. It represents a transition from procedural formality to substantive honesty. It empowers stakeholders, exposes complicit gatekeepers, and fosters an accountable culture.

Conclusion

The Satyam and PNB crises are not isolated incidents; rather, they point to deeper systemic weaknesses in a still-developing regulatory framework. Both incidents reveal an important truth: corporate fraud is a recurring systemic issue that requires continual monitoring. In this scenario, forensic auditing has a transformative effect. It reflects a "jurisprudence of suspicion", a worldview that prioritizes the detection of disguised wrongdoing and transforms corporate governance from a reactive paradigm focused on demonstrating malfeasance to a proactive framework focused on ensuring transparency and integrity²².

To meet the needs of a complex and globalizing economy, forensic auditing cannot be viewed as an optional or post-crisis intervention. It should be regarded as a vital component of corporate governance, mandated at critical financial thresholds, triggered by red flags, and supported by a strong legal framework. This includes establishing whistleblower protections, forming specialist enforcement authorities, and increasing judicial receptivity to forensic findings. Most importantly, forensic audit findings must result in tangible outcomes such as criminal prosecutions, regulatory penalties, or restitution for damaged stakeholders, rather than simply serving as symbolic headlines with no follow-through²³.

As India's corporate and financial landscape becomes more intertwined with global markets,

²² *Id.* at 17.

²³ Katerina Mircheska et al., *The Importance of Forensic Audit and Differences in Relation to Financial Audit*, 54(2) Int'l J. Sci.: Basic & Applied Res. (IJSBAR) 190–200 (2020), <https://core.ac.uk/download/pdf/337387666.pdf> (last visited Apr. 21, 2025).

and as frauds increasingly transcend national and digital boundaries, the regulatory toolkit must evolve accordingly. Forensic auditing, which combines legal experience, financial analysis, and investigative strategies, is an effective means of not just discovering fraud but also constructing a future-proof regulatory architecture²⁴. It ensures that the pursuit of accountability is evidence-based, procedure-driven, and unwaveringly committed to corporate integrity.

²⁴ *Id.* at 20.