Audit of Fraud
Fraud Detection Techniques & Forensic Audit

Misappropriation of Funds
- A Case Study

Indian Audit & Accounts Department
Regional Training Institute
26/1, Civil Lines, Nagpur
E-mail address: rtiaadrn_ngp@sancharnet.in
Phone: (0712) - 2545420, 2545816, 2545829
Fax: 0712-2562577
From PD’s Desk

As a part of our pursuit towards excellence in training in the area of “Audit of Fraud, Fraud Detection Techniques and Forensic Audit”, we bring out series of cases of frauds reported in the audit reports of Comptroller and Auditor General of India, as case studies. Simultaneously, we also endeavor to consolidate the approach and methodology followed by fraudsters in committing them as well as the manner in which they were prevented/detected.

This case study “Misappropriation of Funds” has been prepared based on the material reported under para 4.1.2 of the report of the Comptroller and Auditor General of India for the year ended March 2007(Civil) Government of Assam.

I take this opportunity to extend my sincere thanks to Ms. Y. Ray Chaudhari, Accountant General (Audit), Assam, Guwahati who made us available all relevant documents of the case whenever requested for. I am also thankful to him for arranging for validation of the facts reported and conclusions drawn in the case study.

I commend the efforts of Shri K. G. Hatwar, Sr. Audit Officer/Core Faculty in preparing this case study on the lines directed from time to time.

I hope that the readers would benefit from this. The suggestions, if any, would help us in future such attempts.

RTI, Nagpur
June, 2010

(S. Snehalatha)
Principal Director
### CONTENTS

<table>
<thead>
<tr>
<th>Sr. No.</th>
<th>Topic</th>
<th>Page No.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Background</td>
<td>1</td>
</tr>
<tr>
<td>2</td>
<td>Fraud Environment</td>
<td>1</td>
</tr>
<tr>
<td>3</td>
<td>Opportunity to prevent Fraud</td>
<td>1</td>
</tr>
<tr>
<td>4</td>
<td>Act of Fraud</td>
<td>2</td>
</tr>
<tr>
<td>5</td>
<td>Opportunity to detect and proving the Fraud</td>
<td>2</td>
</tr>
<tr>
<td>6</td>
<td>Red flag indicators</td>
<td>3</td>
</tr>
<tr>
<td>7</td>
<td>Lessons learnt — Preventive Controls/ Detective Controls</td>
<td>3</td>
</tr>
<tr>
<td>8</td>
<td>List of key documents</td>
<td>4 - 35</td>
</tr>
</tbody>
</table>
Misappropriation of Funds

1. Background

In the O/o The Commandant 3rd Assam Police Battalion and Director General of Police, Titabar, due to failure of Internal controls including budgetary control, Government Money to the tune of Rs. 19.07 crore was mis-appropriated by fraudulent drawal of fund.

2. Fraud Environment

Assam Financial Rule – clause 95 prescribed that, the head of office is personally responsible for accounting all moneys received and disbursed. It was however observed that no check was ever exercised by the DDO to see the actual requirement of money for payment of salaries to the staff of the unit nor any check was exercised on the A/Roll received with reference to Personal Cheques (PCs) issued. Thus failure of budgetary Control, Manpower Management Control and Internal Control System at DDO’s level and Controlling Officer’s level led the door open for mis-appropriation of Government Money.

3. Opportunity to prevent Fraud

The act of fraud explained separately could have been avoided through the following Internal Controls.

(a) Had a comparative study of the expenditure on salary of 3rd APBn been made with the expenditure of other similar Unit/Battalion having similar manpower strength, the reason of such huge excess expenditure could have been detected.

(b) According to Budget Manual, the actuals of previous years and the revised estimates ordinarily form best guide in framing budget estimates, but the said principles were never followed and the estimates were prepared (in ‘L’ form) on the basis of the sanctioned strength taking all vacant posts into account year after year though
manpower particularly in respect of constables were decreasing with
the retirement every month/year.
(c) Vacant posts were not filled up since long time but fund was provided
as per demand in some years in excess of the demand. Had, this aspect
been considered, the occurrence of mis-appropriation could have been
avoided.
(d) Verification of the supporting documents vis-a-vis the amount
claimed.
(e) Adherence to the norms stipulated in the codal provisions on
delegation of financial powers.
(f) Failure of internal/budgetary controls.

4. Act of Fraud

<table>
<thead>
<tr>
<th>Name of the Office</th>
<th>Act of Fraud in Brief</th>
</tr>
</thead>
</table>
| O/o Commandant, 3rd Assam Police Battalion, Titabar and the office of the Director General of Police (DGP) | (i) The annual budget estimates prepared included funds for the vacant posts in the unit, which were allocated.  
(ii) The DGP allocated funds in excess of that requisitioned by the commandant during the years 2001-2005.  
(iii) In disregard of financial discipline and rules neither the funds allotted in excess were refunded, nor were saving surrendered to the government.  
(iv) The surplus was shown as utilized.  
(v) No steps were also taken by the O/o the DGP to ascertain the whereabouts of the surplus funds at any level.  
(vi) Excess pay & allowances were drawn through the pay bills by inflating the number of employees, especially constables.  
(vii) The amount so drawn were disbursed to several officials through pay-cheques for onward disbursement to the battalion personnel (platoon wise) stationed at Battalion headquarters and field units. |
manpower particularly in respect of constables were decreasing with the retirement every month/year.

(c) Vacant posts were not filled up since long time but fund was provided as per demand in some years in excess of the demand. Had, this aspect been considered, the occurrence of mis-appropriation could have been avoided.

(d) Verification of the supporting documents vis-a-vis the amount claimed.

(e) Adherence to the norms stipulated in the codal provisions on delegation of financial powers.

(f) Failure of Internal/budgetary controls.

4. Act of Fraud

<table>
<thead>
<tr>
<th>Name of the Office</th>
<th>Act of Fraud in Brief</th>
</tr>
</thead>
</table>
| O/o Commandant, 3rd Assam Police Battalion, Titabar and the office of the Director General of Police (DGP) | (i) The annual budget estimates prepared included funds for the vacant posts in the unit, which were allocated.  
(ii) The DGP allocated funds in excess of that requisitioned by the commandant during the years 2001-2005.  
(iii) In disregard of financial discipline and rules neither the funds allotted in excess were refunded, nor were saving surrendered to the government.  
(iv) The surplus was shown as utilized.  
(v) No steps were also taken by the O/o the DGP to ascertain the whereabouts of the surplus funds at any level.  
(vi) Excess pay & allowances were drawn through the pay bills by inflating the number of employees, especially constables.  
(vii) The amount so drawn were disbursed to several officials through pay-cheques for onward disbursement to the battalion personnel (platoon wise) stationed at Battalion headquarters and field units. |
The details in brief was as given below:

<table>
<thead>
<tr>
<th>Sr. No.</th>
<th>Name of the Officials to whom paid for disbursement</th>
<th>Amount paid (Rs.)</th>
<th>Amount for which A/Roll received</th>
<th>Balance (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Sri Dadul Borah, MTO/AbSI</td>
<td>24,32,96,165/-</td>
<td>8,39,00,529/-</td>
<td>15,93,95,636/-</td>
</tr>
<tr>
<td>2</td>
<td>Sri Nripen Sarma, J. A.</td>
<td>3,21,10,549/-</td>
<td>1,80,99,863/-</td>
<td>1,40,10,682/-</td>
</tr>
<tr>
<td>3</td>
<td>Sri Gunin Gohain, W/c</td>
<td>7,53,70,924/-</td>
<td>5,29,95,275/-</td>
<td>2,23,75,647/-</td>
</tr>
<tr>
<td></td>
<td>Total:</td>
<td>35,07,77,638/-</td>
<td>15,49,95,673/-</td>
<td>19,57,81,965/-</td>
</tr>
</tbody>
</table>

5. Opportunity to detect and proving the fraud

The Audit party of the Principal Accountant General (Audit) Assam conducted the audit of the records of the O/o the commandant, 3rd Assam Police Battalion, Titaban and the O/o The DGP in November, 2006 found that due to failure of internal controls including budgetary control, Govt. money to the tune of Rs. 19.07 crore was misappropriated by fraudulent drawal of fund. The following red-flags helped the audit team in substantive testing of the transactions.

6. Red Flags Indicators

(a) Lack of evidence of exercising mandatory pre checks at the DDO level
(b) Non-reconciliation between Treasury Account & DDO’s Accounts.
(c) Lack of evidence exercising manpower management control
(d) Non-submission of complied expenditure statement to finance department
(e) Lack of evidence to scrutinize the expenditure at controlling officers level.

7. Lessons leant – Preventive Controls/Detective Controls

(a) failure of Drawing & Disbursing officer to compare the ‘Men in Position’ render all the preventive controls in the system ineffective.
(b) Making payments by Personal Cheques without proper receipt and record create scope for embezzlement.

c) Lack of evidence to exercise budgetary control by Finance Department/ DDO & Controlling Officer.

8. List of key documents


(ii) Statement showing non-receipt of APRs (Acquittance Roll) against payment made during the period from 2001-02 to 2006-07.

(iii) Copy of Finance Department, Budget Branch’s directive – regarding strict observance of financial rules and procedure etc.

(iv) Copy of Inspection Report – Part –II-A – Para 1(A) and (B)
Lack of monitoring and supervision by the Deputy Commissioner, Nagaon in procurement and distribution of rice among the flood-affected people resulted in short/non receipt of rice and consequent loss of Rs.52.11 lakh.

Scrutiny (November-December 2005) of records of the DC, Nagaon revealed that 13,354.53 quintals of rice were procured (July-October 2004) from Nagaon wholesale consumers co-operative stores by the DC and shown as issued (20 July 2004 to 17 October 2004) to six Circle Offices (CO’s) for distribution as relief to the people of the district affected in the floods during July/October 2004. But the records of the concerned six CO’s showed receipt of only 8,082.54 quintals of rice. While two of the COs received their full quantity of rice short/non receipt of 5,271.99 quintals of rice valued at Rs.52.11 lakh was detected in the stock account of the remaining four COs (Appendix-4.1).

It was observed that the distribution of rice was not monitored by the district administration at any level, which resulted in short/non receipt of 5,271.99 quintals of rice valuing Rs.52.11 lakh. Inspite of pointing out by audit, the loss was neither investigated, nor was any responsibility fixed.

The matter was reported to the Government in July 2007; reply had not been received (September 2007).

Due to failure of internal controls including budgetary control, Government money to the tune of Rs.19.07 crore was mis-appropriated by fraudulent drawal of fund.

Test-check (November 2006) of records of the Commandant, 3rd Assam Police Battalion, Titabar and the Office of the Director General of Police (DGP), revealed that the annual budget estimates prepared by the Commandant included funds for the vacant posts in the Unit, which were allocated. In addition, the DGP allocated funds [in excess] of that requisitioned by the Commandant during the years 2001-05, as shown below:

---

1 Sadar, Rupahi, Dhing, Raha, Kamalpur and Samaguri Circles.
2 Sadar, Rupahi, Raha and Kampur Circles.
Audit Report (Civil) for the year ended 31 March 2007

Scrutiny of the records of the unit revealed that in disregard of financial discipline and rules, neither the funds allotted in excess were refunded, nor were savings surrendered to the Government. The surplus was shown as utilised. No steps were also taken by the Office of the DGP to ascertain the whereabouts of the surplus funds at any level. It was noticed that excess pay and allowances were drawn through the pay bills by inflating the number of employees, especially constables. The amounts so drawn were disbursed to several officials through pay-cheques for onward disbursement to the Battalion personnel (platoon wise) stationed at Battalion headquarters and field units. Audit analysis of actual requirement of money for disbursement of salaries based on the actual strength maintained on roll, pay chart, pay record register etc. with pay bills/pay bill copy book and amount drawn from treasury, disclosed that Rs.19.07 crore was drawn in excess over a period of 75 months between April 2000 and June 2006 (Appendix-4.2). The actual payee receipts in support of disbursement of the amount could not be shown to audit.

Thus, due to failure of internal controls including budgetary control, Government money to the tune of Rs.19.07 crore was mis-appropriated by fraudulent drawal of fund.

The Commandant stated (27 April 2007) that the case has been referred to Police after being pointed out by audit and that it was being investigated by the State CID. He further confirmed that an amount of Rs.14.35 lakh was recovered (April 2007).

Government reply, had however not been received (September 2007).

<table>
<thead>
<tr>
<th>Year</th>
<th>Budget provision</th>
<th>Additional allotment</th>
<th>Total Allotment</th>
<th>Expenditure</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001-02</td>
<td>8.28</td>
<td>0.72</td>
<td>9.00</td>
<td>9.00</td>
</tr>
<tr>
<td>2002-03</td>
<td>10.15</td>
<td>0.65</td>
<td>10.80</td>
<td>10.80</td>
</tr>
<tr>
<td>2003-04</td>
<td>10.04</td>
<td>1.01</td>
<td>11.05</td>
<td>11.05</td>
</tr>
<tr>
<td>2004-05</td>
<td>11.43</td>
<td>0.57</td>
<td>12.00</td>
<td>12.00</td>
</tr>
<tr>
<td>2005-06</td>
<td>12.75</td>
<td>--</td>
<td>12.64</td>
<td>12.64</td>
</tr>
<tr>
<td>2006-07</td>
<td>13.03</td>
<td>--</td>
<td>11.04</td>
<td>11.04</td>
</tr>
<tr>
<td>Total</td>
<td>65.68</td>
<td>2.95</td>
<td>66.53</td>
<td>66.53</td>
</tr>
</tbody>
</table>

Source: Departmental records

Public Works Department

4.1.3 Loss of bitumen

Non-reconciliation of bitumen transferred by EE, Guwahati Rural Road Division to 21 consignee divisions for more than 2 years facilitated non-receipt/short receipt of bitumen worth Rs.55.20 lakh by 13 consignee divisions.

According to normal practice, bitumen is generally procured by the CE, Public Works Department (PWD), (Roads), Assam from the Indian Oil Corporation (IOC)/Hindustan Petroleum Corporation Limited (HPCL) on the basis of indent/requirement from the executing Divisions against advance payments. The
Statement showing non-receipt of APRs (Acquittance Roll) against payment made during the period from 2001-02 to 2006-07

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount paid to</th>
<th>Amount for which A.R submitted in respect of</th>
<th>A.R not submitted</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Shri Dodul Borah, MTP/ABSI</td>
<td>Shri Nripen Sarmah, J.A</td>
<td>Shri Gunin Gohain, W/C</td>
</tr>
<tr>
<td>2001-02</td>
<td>18865967</td>
<td>27665788</td>
<td>15723328</td>
</tr>
<tr>
<td>2002-03</td>
<td>41537324</td>
<td>4161240</td>
<td>14982428</td>
</tr>
<tr>
<td>2003-04</td>
<td>52886454</td>
<td>-</td>
<td>12639065</td>
</tr>
<tr>
<td>2004-05</td>
<td>5,9746447</td>
<td>-</td>
<td>16575730</td>
</tr>
<tr>
<td>2005-06</td>
<td>64485132</td>
<td>-</td>
<td>13425655</td>
</tr>
<tr>
<td>2006-07</td>
<td>10008561</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>TOTAL</td>
<td>24,75,29,887</td>
<td>7,33,46,206</td>
<td>35,27,03,119</td>
</tr>
</tbody>
</table>

Shri Dodul Borah: MTP/ABSI
Shri Nripen Sarmah: J.A
Shri Gunin Gohain: W/C
Statement showing non-receipt of APRs (Acquittance Roll) against payment made during the period from 2001-02 to 2006-07.

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount paid to</th>
<th>Amount for which A.R. submitted in %</th>
<th>A.R. not Submitted</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001-02</td>
<td>1,88,65,967</td>
<td>2,76,65,788</td>
<td>1,57,23,328</td>
</tr>
<tr>
<td>2002-03</td>
<td>4,15,37,324</td>
<td>41,61,240</td>
<td>1,49,82,442</td>
</tr>
<tr>
<td>2003-04</td>
<td>5,28,86,454</td>
<td>-</td>
<td>1,26,30,065</td>
</tr>
<tr>
<td>2004-05</td>
<td>5,97,46,447</td>
<td>-</td>
<td>1,65,75,730</td>
</tr>
<tr>
<td>2005-06</td>
<td>6,44,85,132</td>
<td>-</td>
<td>1,34,26,555</td>
</tr>
<tr>
<td>2006-07</td>
<td>1,00,08,561</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Total</td>
<td>24,75,29,885</td>
<td>3,18,27,028</td>
<td>7,33,46,206</td>
</tr>
</tbody>
</table>

Leaves taken: 87, 83, 82, 77, 81, 78, 77, 80

1296, 97 & 98

C/26° - 35°
C/2l° - 26°
Government of Assam
Finance Department, Budget Branch

No. BR 90/78/12, Dated Dispur, The 15th June, 1978

All Secretaries to the Government of Assam in Administrative Departments, including Public works, Irrigation and Flood Control Department,

Sub:-Strict observance of financial rules and procedure.

Sir,

I am directed to say that under the Assam Rules of Executive Business and Budget Manual Finance Department is to report to the Cabinet by the 1st week of December of every year the overall budgetary position showing anticipated receipts and expenditure for preparation of next year’s Budget and for taking a proper view on new development plans and programmes for the next year. Therefore, a constant review of the Budget, control of expenditure, timely verification of departmental figures of receipts and expenditure with those booked in the office of the Accountant General, watching the progress of revenue collection and also observance of Budget time-table by the Controlling Officers, Heads of Departments and Administrative Departments from the beginning of the financial year are essential. But it has been noticed that this is not done generally and there is no proper phasing of expenditure for implementation of schemes and utilisation of funds for the purpose for which it has been provided in the Budget. As a result there is always a last hour rush for sanction, diversion of funds, etc. These make it difficult for Finance Department to get a correct and comprehensive picture of financial liability, etc. at any time. The Finance Department also do not get sufficient time to examine the schemes, etc. properly. Verification of departmental figures of receipts and expenditure with those booked in the Office of the Accountant General and reconciliation of the discrepancies are also get delayed.