

# ESG Audit: Concepts, Global Perspectives and Emerging Trends

Environmental, Social, and Governance (ESG) audit has become a cornerstone of modern corporate accountability, driven by growing demands for sustainability and transparency in business operations. As organizations worldwide face increasing scrutiny from investors, regulators and stakeholders, ESG audits serve as a vital tool for assessing and verifying non-financial performance, ensuring alignment with ethical and sustainable practices. This article delves into the concept of ESG auditing, historical genesis, the evolving scenarios in India, the European Union (EU), the United Kingdom (UK), and the United States (US). It also examines the role of auditors, benchmark frameworks, and key trends shaping the future of ESG auditing.



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## INTRODUCTION

**E**SG audit is a structured process to evaluate an organization's Environmental, Social and Governance practices against established standards or frameworks. Unlike traditional financial audits, which focus on monetary metrics, ESG audits assess non-financial factors that influence a company's long-term sustainability and societal impact. The three pillars of ESG are:

Environmental	Social	Governance
Focuses on a company's environmental footprint, including carbon emissions, energy use, waste management and climate risk mitigation.	Evaluates labor practices, diversity, equity, inclusion (DEI), human rights, and community engagement.	Examines corporate leadership, transparency, anti-corruption measures, executive compensation and shareholder rights.

The primary objective of an ESG audit is to ensure that a company's reported ESG performance is accurate, reliable, and compliant with relevant standards. It enhances stakeholder trust, mitigates risks, and supports informed decision-making for investors and regulators. ESG audits can be conducted internally to improve processes or externally for third-party assurance, providing credibility to ESG disclosures.

## EVOLUTION OF ESG AUDIT

The concept of ESG audit evolved from the broader movement toward Corporate Social Responsibility (CSR) and sustainable investing in the 1980s. Early efforts focused on environmental reporting, driven by public concerns over pollution and resource depletion. The 1990s saw the rise of social responsibility standards, such as SA8000, addressing labor practices. Governance gained prominence in the 2000s following corporate scandals like Enron, emphasizing transparency and accountability.

The term "ESG" was coined in 2004 in the United Nations "Who Cares Wins" report<sup>1</sup>, which urged integrating environmental, social, and governance factors into financial markets. This catalyzed the development of ESG frameworks like Global Reporting Initiative (GRI) and Sustainability Accounting Standards Board (SASB). The 2015 Paris Agreement and the UN Sustainable Development Goals (SDGs) further accelerated demand for ESG reporting and auditing, as regulators and investors sought standardized metrics.

ESG audit emerged as a distinct practice in 2010, driven by the need for assurance over voluntary ESG disclosures. The lack of uniform standards initially led to inconsistent reporting, prompting calls for mandatory frameworks. Today, ESG audit is a critical component of corporate governance, with regulators worldwide introducing disclosure mandates.

## EMERGING SCENARIO IN INDIA FOR ESG AUDIT

In India, ESG audit is gaining traction amidst increasing regulatory and investor focus on sustainability. The Securities and Exchange Board of India (SEBI)<sup>2</sup> introduced the Business Responsibility and Sustainability Reporting (BRSR) framework in 2021, mandating the top 1000 listed companies to disclose ESG performance. The BRSR aligns with global standards like GRI and SASB, requiring assurance for key metrics by 2026.

## KEY DEVELOPMENTS

SEBI has formulated a glidepath for implementation of BRSR, BRSR Core and its assessment/ assurance. The following table summarizes the SEBI requirement and the glidepath:

Requirement	Applicable To	Effective From (FY)
BRSR Comprehensive annual reporting	Top 1000 listed entities by market cap	2022-23
BRSR Core disclosures + “assessment or assurance”	Top 150 listed entities	2023-24
BRSR Core disclosures + “assessment or assurance”	Top 250 listed entities	2024-25
BRSR Core disclosures + “assessment or assurance”	Top 500 listed entities	2025-26
BRSR Core disclosures + “assessment or assurance”	Top 1000 listed entities	2026-27
Value-Chain ESG disclosures (voluntary; ‘comply-or-explain’)	Top 250 listed entities	2025-26
Value-Chain ESG disclosures + “assessment or assurance”	Top 250 listed entities (same group)	2026-27
Standardized BRSR Core templates & industry-specific guidance	All listed entities (subject to BRSR Core mandate)	2024-25 onwards

## REASONABLE ASSURANCE CONCEPT IN THE SEBI BRSR FRAMEWORK

The Business Responsibility and Sustainability Reporting (BRSR) framework, introduced by the Securities and Exchange Board of India (SEBI), mandates ESG disclosures for listed companies to enhance transparency and accountability. A critical aspect of this framework is the “reasonable assurance” requirement, which ensures that reported ESG data is credible and reliable. This concept aligns with global ESG reporting trends, where third-party assurance enhances stakeholder confidence.

Reasonable assurance under the BRSR framework involves an independent evaluation of a company’s ESG disclosures to ensure they are free from material misstatements. Unlike limited assurance, which provides a moderate level of confidence, reasonable assurance offers a higher degree of scrutiny, akin to financial audits.

Key aspects covered under reasonable assurance include:

- Accuracy of ESG metrics (e.g., carbon emissions, energy consumption, diversity ratios).
- Compliance with SEBI’s disclosure requirements (Principle-wise and Leadership Indicator disclosures).
- Verification of qualitative statements (e.g., policies on human rights, anti-corruption, and sustainable sourcing).

## RAMIFICATIONS FOR LISTED COMPANIES

Assurance requirements prescribed by SEBI will have following ramifications for listed companies in India.

### Enhanced Credibility & Investor Confidence:

Assurance enhances the credibility of ESG disclosures for Indian listed companies by ensuring data accuracy

and compliance with global standards like ISSB and SEBI’s BRSR framework. Reliable, third-party verified reports build trust among ESG-focused investors, both domestic and international, who prioritize transparency. As India integrates with global markets, assured ESG disclosures align with cross-border

regulatory expectations, easing compliance for Indian firms seeking foreign capital. For instance, companies with assured BRSR reports can attract sustainability-linked investments from ESG funds in the U.S. or Europe. This alignment not only boosts investor confidence but also positions Indian firms competitively in the global ESG ecosystem, fostering sustainable growth.

### Operational & Compliance Challenges:

For Indian listed companies, implementing robust ESG data collection systems and third-party assurance involves upfront costs, but delivers long-term benefits. The SEBI BRSR mandate requires accurate disclosures, and unreliable reporting risks regulatory penalties (like suspension or fines) and reputational damage. For example, discrepancies in carbon emissions or diversity data could trigger SEBI scrutiny or investor lawsuits. While assurance engagements increase compliance costs (by 15-25% for large caps), they prevent costly violations and build market trust. Companies like Tata Steel and Infosys, which invest in assured ESG reporting, gain easier access to global ESG funds and avoid losses from non-compliance. Thus, assurance acts as both a safeguard and strategic investment.

## SEBI’S REQUIREMENT OF ASSURANCE PROVIDER

SEBI has in its Master Circular dated November 12, 2024, specifically provided for the qualifying criteria with respect to the assurance provider.

- The Board of the listed entity shall ensure that the assurance provider of the BRSR Core has the necessary expertise, for undertaking reasonable assurance.
- The listed entity shall ensure that there is no conflict of interest with the assurance provider appointed for assuring the BRSR Core. For instance, it shall be

ensured that the assurance provider or any of its associates do not sell its products or provide any non audit / non assurance related service including consulting services, to the listed entity or its group entities.

- The reasonable assurance mandate under SEBI's BRSR framework marks a significant step toward standardized and reliable ESG reporting in India. While it imposes additional compliance burdens, it also enhances corporate accountability and aligns Indian markets with global sustainability reporting norms. As ESG audits gain prominence, companies must proactively strengthen their data governance and assurance mechanisms to meet evolving regulatory expectations.

### RBI'S REGULATORY ROADMAP: INTEGRATING CLIMATE RISKS INTO INDIA'S FINANCIAL SYSTEM

The Reserve Bank of India (RBI) released a discussion paper to integrate climate-related risks into India's financial stability framework.<sup>3</sup> It highlights how climate change poses physical risks (e.g., extreme weather disrupting assets) and transition risks (e.g., policy shifts impacting carbon-intensive sectors), which could destabilize banks and financial institutions. The paper proposes:

1. **Disclosure Mandates:** Aligning with global standards like TCFD, RBI recommends mandatory climate risk disclosures for regulated entities (banks, NBFCs), focusing on governance, strategy, and risk management.
2. **Risk Assessment:** Financial institutions must adopt climate stress testing to evaluate exposure to vulnerable sectors (e.g., agriculture, energy) and build resilience.
3. **Sustainable Finance Incentives:** RBI suggests green deposit frameworks, preferential risk weights for ESG-aligned loans, and liquidity facilities for green bonds to channel capital toward low-carbon projects.
4. **Capacity Building:** Banks need internal expertise to quantify climate risks, aided by RBI's proposed guidelines and training programs.

The paper seeks stakeholder feedback on implementation challenges, including data gaps and sector-specific transition pathways. By embedding climate considerations into financial regulation, RBI aims to safeguard India's economy while supporting its 2070 net-zero goal.

### SCENARIO IN THE EU FOR ESG AUDIT

The European Union is a global leader in ESG regulation, with the Corporate Sustainability Reporting Directive (CSRD)<sup>4</sup> setting a high standard for ESG audit. Effective from 2024, the CSRD mandates over 50,000 companies to report audited ESG data, covering environmental impact, social responsibility, and governance practices.

The CSRD entered into force on January 5, 2023, with phased implementation starting in 2024 and extending through 2029. Companies initially in scope must start collecting data in 2024 to be prepared for reporting in 2025.

### KEY ASPECTS OF THE CSRD

The following table gives a bird's eye view about the key aspects of the Corporate Sustainability Reporting Directive

<b>Mandatory ESG Reporting</b>	The CSRD requires companies to report detailed ESG data, including information about their operations and supply chains, governance structures, and sustainability practices.
<b>Double Materiality</b>	Companies must assess both the impact of sustainability issues on their financial performance and the impact of their business on the environment and society.
<b>Standardized Reporting</b>	The CSRD promotes standardization in sustainability reporting through the use of digital formats, allowing for easier comparison of metrics across different organizations.
<b>Mandatory Assurance</b>	The CSRD requires limited assurance for ESG disclosures, with plans to transition to reasonable assurance by 2028. Third-party auditors, including traditional audit firms and sustainability specialists, play a critical role.

### WHO MUST COMPLY WITH THE EU CSRD?

Mandatory CSRD compliance depends on a company's size and financial revenue. In February 2025, the European Commission released the EU Omnibus proposal updating the minimum qualifying criteria. The proposed rules now only affect companies operating in the EU with a minimum of 1000 employees with an exemption given to Small and mid-sized organizations. Instead, they follow the Voluntary Sustainability Reporting Standard (VSME). This focuses regulation efforts on entities with the largest social and environmental impact.

### ESG AUDIT SCENARIO IN THE UK

The UK has emerged as a leader in mandatory ESG reporting and assurance, driven by stringent regulations and growing investor demand for transparency. Key frameworks such as the Task Force on Climate-related Financial Disclosures (TCFD), UK Sustainability Disclosure Standards (UK SDS), and Corporate Sustainability Reporting Directive (CSRD) for UK-based EU companies shape the ESG auditing landscape.

The IFRS S1 and S2, developed by the International Sustainability Standards Board (ISSB), are global sustainability disclosure standards designed to provide consistent, comparable ESG reporting for financial markets.

## 1. IFRS S1: General Sustainability Disclosures

- Governance: How sustainability risks are managed at board level.
- Strategy: Business model resilience to sustainability risks (e.g., climate, human rights).
- Risk Management: Processes for identifying and mitigating ESG risks.
- Metrics & Targets: Performance indicators (e.g., carbon footprint, diversity ratios).

## 2. IFRS S2: Climate-Specific Disclosures

- Scope 1, 2 & 3 Emissions: Mandatory GHG reporting (with phased compliance for Scope 3).
- Climate Resilience: Scenario analysis for different warming pathways (1.5°C, 2°C+).
- Transition Plans: How the company aligns with net-zero goals.

These standards mark a shift from voluntary ESG reporting to regulated, investor-grade disclosures.

The UK has adopted these as the basis for its Sustainability Disclosure Standards (UK SDS), mandatory from 2025 for listed companies.

The IFRS S1 (General Sustainability Disclosures) and IFRS S2 (Climate-related Disclosures) standards do not explicitly mandate third-party assurance as part of their requirements.

## USA- ENHANCED CLIMATE DISCLOSURES: NUANCES AND KEY FEATURES

In the USA, ESG audit is evolving amidst a fragmented regulatory landscape and growing investor demand. The Securities and Exchange Commission (SEC) introduced climate disclosure rules in 2024, requiring large public companies to report Scope 1 and 2 emissions, with limited assurance mandatory by 2029.

The SEC's newly adopted climate disclosure rules mark a significant shift toward standardized, investor-grade environmental reporting. Public companies must now disclose material climate-related risks, including how they impact business strategy, financial performance, and operational resilience. A critical nuance is the phased implementation—larger firms (accelerated

filers) must comply earlier, while smaller companies get extended timelines. The rules also introduce stringent requirements for GHG emissions reporting, with Scope 1 and 2 disclosures mandatory for many firms, though Scope 3 emissions were notably excluded due to industry pushback. This tiered approach balances transparency with practicality, acknowledging varying corporate capacities while ensuring consistent, comparable data for investors.

The SEC's primary goal is to equip investors with reliable, decision-useful climate data to assess long-term risks and opportunities. By mandating disclosures aligned with the TCFD framework, the rules aim to curb greenwashing and promote apples-to-apples comparisons across firms. Another key objective is enhancing corporate accountability—companies must detail their climate risk management processes, governance oversight, and transition plans (if any). While the rules stop short of requiring full net-zero commitments, they incentivize proactive climate strategies by making such efforts visible to stakeholders. Ultimately, the SEC seeks to foster market stability by reducing information asymmetry and ensuring climate risks are priced accurately into securities.

Assurance providers are no longer optional but essential actors in the ESG ecosystem. By ensuring transparency, compliance, and continuous improvement, they empower companies to build stakeholder trust, secure investment, and achieve long-term sustainability goals.

The rules apply to all SEC-registered public companies, including foreign private issuers, but with scaled requirements based on firm size and filing status. Notably, smaller reporting companies (SRCs) and emerging growth companies (EGCs) are exempt from Scope 1 and 2 emissions reporting, reflecting cost-benefit considerations. High-impact industries (e.g., energy, transportation) face heightened scrutiny due to their exposure to physical and transition

risks. The rules also carve out a “safe harbor” provision for forward-looking climate statements, shielding firms from liability if projections are made in good faith.

## FROM COMPLIANCE TO COMPETITIVE EDGE: HOW ESG AUDITS STRENGTHEN VALUE PROPOSITIONS FOR LISTED FIRMS

The findings of a seminal study<sup>1</sup> indicate how ESG practices of the firm significantly influence economic performance and robust ESG disclosures enhance firm valuation and investor confidence. In today's interconnected global economy, stakeholders increasingly view ESG practices as critical drivers of corporate performance and long-term resilience. Studies demonstrate that proactive ESG management fosters organizational integrity, strengthens stakeholder trust, and cultivates a culture of sustainable growth. Companies that transparently disclose their ESG

<sup>1</sup> “The Impact of Environmental, Social and Governance Practices (ESG) on Economic Performance: Evidence from ESG Score”, Tarmuji, I., Maelah, R., & Tarmuji, N. H. (2016)





commitments, particularly through standardized reporting frameworks, often reap significant benefits, including enhanced reputational equity, greater investor confidence, optimized resource efficiency, and sustained competitive advantage.

Another seminal study<sup>2</sup> provides critical evidence on how ESG data shapes investment decisions. Through a comprehensive survey of global investors, the authors found that audited ESG disclosures significantly influence capital allocation, with 73% of respondents relying on verified ESG metrics to assess long-term risks and opportunities. The study underscores how assurance transforms ESG data from aspirational claims into actionable intelligence, bridging the trust gap between corporations and stakeholders. For listed companies, this translates to tangible benefits: lower cost of capital, higher valuation premiums, and preferential inclusion in ESG indices. As regulatory frameworks like SEBI's BRSR mandate stricter disclosure norms, Amel-Zadeh and Serafeim's work reinforces why Indian firms must treat ESG audit as a strategic imperative, not just compliance.

## THE CRITICAL ROLE OF ASSURANCE PROVIDERS IN ESG REPORTING

In an era where Environmental, Social, and Governance (ESG) factors significantly influence investment decisions and corporate reputation, the role of assurance providers has become indispensable. Assurance providers, including auditing firms, certification bodies, and specialized ESG verifiers, serve as critical intermediaries that enhance the credibility, accuracy, and reliability of ESG disclosures. Their involvement ensures that reported data meets regulatory requirements and stakeholder expectations, thereby fostering trust and transparency in corporate sustainability claims.

One of the primary functions of assurance providers is to validate the accuracy of ESG disclosures, protecting against greenwashing—a practice where companies exaggerate or misrepresent their sustainability efforts.

<sup>2</sup> Amel-Zadeh and Serafeim, (2018), "Why and How Investors Use ESG Information: Evidence from a Global Survey" *Financial Analysts Journal*, Vol. 74, Issue 3, pp. 87–103.

By conducting independent audits, assurance providers verify metrics such as carbon emissions (Scope 1, 2, and 3), workforce diversity, and supply chain ethics. For instance, under frameworks like SEBI's Business Responsibility and Sustainability Reporting (BRSR) in India or the EU's Corporate Sustainability Reporting Directive (CSRD), third-party assurance is increasingly mandated to ensure compliance. Without such verification, companies risk regulatory penalties, investor skepticism, and reputational damage.

Assurance providers are no longer optional but essential actors in the ESG ecosystem. By ensuring transparency, compliance, and continuous improvement, they empower companies to build stakeholder trust, secure investment, and achieve long-term sustainability goals. As ESG regulations tighten globally, their role will only grow in significance, making them indispensable partners in the transition to a more accountable and sustainable corporate world.

## CONCLUSION

ESG auditing is transforming corporate accountability, bridging the gap between sustainability goals and stakeholder expectations. From its origins in CSR to its current prominence, ESG auditing reflects a global shift toward responsible business practices. While India, the EU, the UK, and the US adopt distinct approaches, common challenges like standardization and auditor expertise persist. Benchmark frameworks and technological advancements are driving progress, with auditors playing a critical role in ensuring transparency and trust. As regulatory mandates tighten and investor scrutiny intensifies, ESG audit will remain a cornerstone of sustainable growth, shaping a future where businesses thrive while prioritizing people and the planet.

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# Are Financial Shenanigans becoming the triggers for implementation of Forensic Audit?

The shenanigans are the red flags which lie under the bed rocks of the financial statements and cause the damage to the health and wealth of the company. These shenanigans can be unearthed by the implementation of the Forensic Audit. Company Secretary, being a governance watchdog is responsible for the detection of the scams and scandals committed intentionally or unintentionally by the shenanigans and also to enable the forensic auditors to exercise their expertise in generating a true audit report.



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## INTRODUCTION

The art of presenting the financial information comes true when the statement of accounts and income statement of the company is produced before the stakeholders. The need to prepare financial statements is said to be of utmost importance as the decision of the future investment is entrusted majorly on that. The truthfulness of the same is always doubted as the real-time difficulty exists in fathoming its intrinsic value. The researchers, academicians, investors and various other segments of stakeholders always depend on these volumes of information as they believe to build their blocks by nurturing the available information in the public domain. This practice is always tested and questioned as information presented before the table is distorted intentionally with a target of developing reservoir of void

surplus or unintentionally as it becomes an inherited norm. Financial scandals and scams are outcomes of the age-old deliberate exaggeration of the financial transactions made by the top level management. Sometimes the financial reporting of the companies are done with tricks and gimmicks with the intention to portray a rosy picture before the investors. These manipulative approaches in the name of accounting tricks and strokes are known as Financial Shenanigans.

Approximately 50000 frauds have hit the banks in India during FY2009-2019. RBI Report (2019) affirms that in India bank frauds went up to ₹ 2.05 trillion in the last 11 years and this lead to the sarcasm of creating more financial troughs instead of financial peaks. The birth of Auditing and Auditing techniques and rebirth of Audit in the name of Forensic Audit as a post mortem analysis could not completely arrest its accelerating trend but was instrumental in doing some deeper analysis with an objective of revealing the truth for future safety and security.

## CONCEPT AND TYPE OF FINANCIAL SHENANIGANS

Financial shenanigans are the art and architecture of creating hype in the financial status of the company by window dressing the balance sheet, income statement, cash flow statement and statement of showing changes in equity and in addition also the notes to account and other annexures. It is the deceptive mechanism of presenting willfully the stretched statistics of the financial transactions before the investors' community by adopting some unethical yet creative and unusual techniques.

## TYPES OF SHENANIGANS

The intention of defeating the investors and eroding their confidence mainly exist in the form of hiking losses to save taxes, booking unrealized profits in the dull period, not writing off the necessary fictitious assets, recording unsound liabilities under mining the sale of assets and typically misclassifying the expenses. In the name of accounting flexibility the financial shenanigans are used and their dubious incorporation in the financial statements results in drainage of shareholders' wealth. There are restricted few financial shenanigans that are not illegal and do not do away with the requirements of the GAAP but majority of them are introduced to mask the truthfulness of the financial statements.

The types of Shenanigans are tabularized as follows. The items with \* are explained below the table.

**Table No 1: Types of Shenanigans**

Earning Manipulation	Erroneous Classification of items	Related Party Transactions	Asset Manipulation	Window Dressing	Siphoning of Funds	Insider Trading & Stock Manipulation
Hiking Revenue	Capitalizing expenses	*Round Tripping	Over valuation of Assets	Short term Borrowing	Fund Diversion	*Pump & Dump
Postponing expenses	*Off- Balance Sheet Items	Over Invoicing	*Ghost Assets	*Temporary Boost	*Loan ever greening	*Insider Trading
*Cookie Jar Reserves		Under Invoicing				

\*Cookie Jar Reserves refers to the process of building a reserve/s in good year/s and releasing the same in the year of losses.

\*Off- Balance Sheet Items means the process of keeping away the liabilities or losses from the Balance sheet by suing the Special Purpose Vehicle.

\*Round Tripping is the process of creating fake sales by routing funds through related entities.

\*Ghost Assets are the non existing assets but they are placed artificially in the balance sheet.

\*Temporary Boost is the one time sale or financial gimmick at the end of the year.

\*Loan ever greening is the process of lending new loans to the defaulters to shadow their NPAs.

\*Pump & Dump is the deliberate increase in the stock prices by capitalizing the false information and then selling at a profit.

\*Insider trading is the trading done by using the sensitive but unpublished information.

Anomaly Detection, Text Analysis, Predictive Models, Forensic Accounting Tools are some of the key applications of the AI in detecting financial shenanigans.

the health and wealth of the company. These shenanigans willfully deceive the stakeholders of the company and the same can be unearthed by the implementation of the powerful audit named as Forensic Audit-the audit that follows untraditional route to excavate the causes of the loopholes in the financial statements. The frauds which are

common in the corporate corridor often go unnoticed and non indicative in the spectrum of statutory audit but comes to the knowledge of the community by the deep rooted searching of the super investigative wings of the forensic audit.

## THEORIES OF FORENSIC AUDIT

The theories which developed gradually in the field of forensic audit are namely

Fraud Triangle Theory, Fraud Diamond Theory, Fraud Pentagon Theory, and Fraud Scale Theory. These theories evolved within the period from 1950 to 2016. The basic theory is the Fraud Triangle theory of Dr. Cressey resting on the pillars of Pressure, Rationalization and Opportunity which compel the fraudsters to commit the fraud. The theories that got established later also trusted significantly these pillars and introduced the additional pillars to strengthen the viability of the theory. The Fraud Diamond theory of Wolf & Hermanson brought the fourth pillar in the name of "Capability" which indicates that the fraudster not only hunts for a right opportunity, not only get the impulse out of pressure and the power to rationalize the actions committed but also needs the capability to execute the same. Further to this theory came the Crowey's Fraud Pentagon theory which added the pillar Arrogance as a triggering competency to commit the fraud. In case of Fraud Scale theory the pillar named as "Rationalization" of Fraud Triangle theory is replaced with the term "Personal Integrity" keeping other pillars constant. This model was developed by W. Steve Albrecht and emphasised on the personal integrity as one of the unavoidable aspect in committing frauds especially in the context of financial fraud reporting.

## TYPES OF FINANCIAL SHENANIGANS AND FORENSIC AUDIT

The companies who are blamed for using the financial shenanigans are of the following types:

## REASONS FOR THE EXISTENCE OF SHENANIGANS

Some of the prominent reasons as why the shenanigans exist:

- Greed factor
- Fear factor
- Need for finance
- To turn off the negative market sentiment
- To support the company's financing covenants

## INTERCONNECTION BETWEEN FINANCIAL SHENANIGANS AND EMERGENCE OF FORENSIC AUDIT

The above mentioned reasons are further corroborated by the theoretical framework of Forensic Audit. The shenanigans are the red flags which lie under the bed rocks of the financial statements and cause the damage to



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- Companies with narrow or zero focus on checks and balances.
- Companies who are comfortable with camouflaging the financial metrics for the short run benefit.
- Companies who are having incompetent members in the Board of Directors.
- Companies who lack control in Corporate Governance.
- Companies who do not hesitate to compromise financially in the context of recruiting the professional and ethical auditors.
- Companies whose Vision and Mission statements are at a questionable stake.
- Companies such as newly incorporated public companies, privately held ones and basket case companies are highly prone to commit accounting frauds.

### HOW TO DETECT FINANCIAL FRAUDS IN FINANCIAL REPORTS: HOWARD M SCHLITZ'S 7 FINANCIAL SHENANIGANS

- Recording revenue too soon.
- Recording bogus revenue.
- Boosting income with one-time gains.
- Shifting current expense to a later period.
- Failing to disclose liabilities.
- Shifting current income to a later period.
- Shifting future expenses to a current period.

### FINANCIAL SHENANIGANS IN US AND INDIA

Financial Shenanigans are not only accounting gimmicks or tricks but also refers to financial misconduct, regulatory mishaps, corporate failures and such other significant financial dilapidations.

The table below shows the list of US and Indian companies who have embroiled themselves in various tumultuous financial, regulatory and systemic damages.

**Table No 2: Year and name of companies with its origin that used Financial Shenanigans**

Year	Name of the US based Company	Type of Shenanigans
2001	Enron Corporation	Off Balance-sheet Financing
2002	WorldCom	Expense Capitalization
2008	Lehman Brothers	105 Repo Transactions
2019	General Electric	Misclassification of expense and under reporting of risks

2024	Archer Daniels Midland Investigation	Securities fraud related to accounting practices
2024	Supermicro Accounting Violations	Accounting Violations
Year	Name of the Indian Company	Type of Shenanigans
2009	Satyam Computers	Misappropriation of revenue and cash balances.
2010	Sahara Group	Illegal Optionally fully convertible debentures issued for ₹24000 crore without regulatory approval.
2013	Sharada Chit Fund	Exposure of ₹2500 crore ponzi scheme slash in financial cash flows.
2018	Dena Bank and Oriental Bank of Commerce	Embezzlement of cash of ₹257 crore in Dena bank and ₹180 crore misappropriation from Fixed deposits in Oriental Bank of Commerce.
2018	ILFS	Ever greening of loans and subduing the debt.
2019	Punjab National Bank and Nirav Modi	Fake LOU of ₹127000 crore.
2020	Yes Bank	Under reporting of Toxic assets or loans.
2023	Adani Group	Brazen stock manipulation.
2025	BluSmart and Gensol Engineering	Fund diversion.
2025	IndusInd Bank Microfinance Irregularities	Discrepancy in reporting of bad loans.
2025	TASMAC scam	Manipulation of tender, inflation of expenses and illegal transactions.

The companies conducted forensic audit as the above shenanigans washed out the financial profits, made injudicious use of systems and procedures and tarnished the corporate image. Forensic audit was instrumental in the case of above companies to unfold the true facts.

### ROLE OF ARTIFICIAL INTELLIGENCE (AI) IN DETECTING FINANCIAL SHENANIGANS

The role of AI is in experimental stage in detecting the financial shenanigans. Though the world around us is reeling under the wheels of AI, with special mention to Machine Learning (ML) and Natural Language processing (NLP), Still AI can perpetuate frauds in financial reporting.



Some of the key applications of the AI in detecting financial shenanigans are:

- **Anomaly Detection:** AI can locate unusual frauds in the financial statements; can identify the unnatural patterns and movements.
- **Text Analysis:** NLP can examine annual reports, earning calls, MD & A sections to detect deceptive language or obfuscation.
- **Predictive models:** Machine Learning can predict the likelihood of fraud based on historical patterns.
- **Forensic Accounting Tools:** AI driven tools and supports are used by the auditors and regulators to conduct real time financial scrutiny.

The companies are heavily dependent on the use of AI to detect the frauds but the challenges are also unavoidable.

- **Duplication of data:** Generative models sometimes give birth to some artificial transactions.
- **Fake Financial Reports:** Generative models would bring in highly convincing earning reports or investors' presentation.
- **Algorithm bias:** Unethical actors might exploit AI system's blind spots to manipulate financial outcomes.
- **Dark AI Models:** Proprietary AI used in Fintech or trading platforms could be made to hide the losses or to exaggerate the performance.

## ROLE OF COMPANY SECRETARY IN UNLEASHING THE FRAUDS COMMITTED BY THE FINANCIAL SHENANIGANS AND FACILITATING THE CONDUCT OF THE FORENSIC AUDIT

Company Secretary, being a governance professional is responsible for the detection of the scams and scandals committed intentionally or unintentionally by the shenanigans and also to enable the forensic auditors to exercise their expertise in generating a true audit report. The four-fold role of a Company Secretary is highlighted below in a tabular form.

**Table No 3: Four-fold role of Company Secretary**

Phase	Role
Preventive	Can take active participation in ensuring smooth compliance procedure as per Companies Act, 2013, SEBI Listing Obligations, fulfilling statutory and filing requirements. Also can emphasize on the proper disclosure of financial data, related party transactions and documents reflecting board decisions.
Early Warning Signals	Can identify through the irregular board resolutions, unusual disclosures, filing gaps.  Can take due care of whistle blower policy to protect the organization.

Support in conducting forensic audit	Acts as a liaison between the boards, audit firm and the regulators.  Providers of various company's documentation.
Governance compliance and post audit support	Keep up the role of a reporter in post audit scenarios to the shareholders, regulators.  Maintain ethical policies intact. Trainers for the directors and members.
Case based Resolution	Handles queries from regulators such as SEBI, MCA. Provider of information specific to the company data to the forensic auditors.  Maintains compliance with investigative procedures.

## CONCLUSION

Financial shenanigans are the weapons used in distorting and depicting willfully the financial picture of the organization. These shenanigans can be unearthed by the collaborative efforts of the Forensic Auditors and meticulous support from the Company Secretary for maintenance of adequate governance and compliance mechanisms.

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