



The most common examples of financial fraud in Bosnia and Herzegovina - A PRACTICAL INSIGHT –

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Abstract

The aim of this paper is to shed light on the two most common examples of financial fraud, which occur in most businesses in Bosnia and Herzegovina. The causes and consequences of the mentioned financial frauds will be analyzed, as well as the reasons why they were not procedurally discovered in time. The first example is related to the inflow of money from abroad, which creates doubts about merits, while the second example is related to the presentation of operating losses and reduced tax liabilities of related legal entities. Each of the examples will be analyzed in detail in terms of the causes of financial fraud, the manner of their implementation, the relevant accounting records, and finally the manner of their detection.

Keywords: financial fraud, examples of financial fraud, forensic accounting, Bosnia and Herzegovina

Paper type: Non-research article

Received: November 22, 2021

Accepted: December 20, 2021

Citation: Lalić, S., Jovičić, Ž., Bošnjaković, T. (2021), “The most common examples of financial fraud in Bosnia and Herzegovina: a practical insight”, Journal of Forensic Accounting Profession, Vol. 1, No. 2, pp. 80-88.

DOI: <https://doi.org/10.2478/jfap-2021-0010>

The analysis of the mentioned financial fraud will give us an insight into the less frequent abuses that occur in practice, and the way of their detection. A critical review of forensic accounting methods and techniques that can be used in the context of detecting analyzed financial fraud in practice will be made.

1. Introduction

One of the three pillars of every society, in addition to the culture and the military, is the economy. The economy needs to be healthy and stable in order to ensure economic growth and development. Today's trends show that these three pillars are stable only in developed countries, while countries in transition, such as Bosnia and Herzegovina, generally face difficulties in sustainable economic development. Moreover, many macroeconomic indicators point to the fact that Bosnia and Herzegovina's economy is no longer sustainable, and therefore not competitive. All this has a negative effect on the position in which primarily public companies, and partly private companies, are today. High fiscal burdens of legal entities and entrepreneurs in Bosnia and Herzegovina contribute to the gray economy and the efforts to ensure that at least parts of business transactions are not officially recorded.

The ultimate goal is to reduce tax payments. The current legislation related to external audits has also contributed to this situation, as it currently does not have the instruments to achieve change in the current situation, but has its work exclusively reduced to giving opinions and recommendations; ie. it has only an advisory role as well as internal audit. Therefore, it happens that the external audit gives a negative opinion as part of its findings as the final phase of the audit procedure, after which no one takes responsibility and nobody reacts to the audit recommendations. No investigative actions and analyzes are carried out to determine the validity of a negative opinion, nor are any sanctions implemented to provoke such negative business in the company. Due to all the above, we will point out the importance of forensic accounting and auditing in the process of detecting, reporting, investigating and prosecuting financial fraud, all for the purpose of protecting the domestic economy.

The aim of this paper is to use forensic accounting methods and techniques to shed light on the most common types of financial fraud in Bosnia and Herzegovina, which have been exposed in detail in the media. Through the examples that will be processed, we will shed light on the ways of conducting financial fraud and the reasons why they are procedurally difficult to detect. Selected examples from the practice of Bosnia and Herzegovina are represented in all spheres of the economy, which means that approximately 80-90% of economic entities, whose business was the subject of external financial audit, encountered similar situations.

2. Inflow of money from abroad that creates doubts about the merits - individuals and entrepreneurs

The current practice is reflected in the fact that individuals (freelancers) and entrepreneurs who earn income abroad, via the Internet, such as: translation services of documents into foreign languages, consulting services - bookkeeping, analysis, interpretation, software support, web application development, maintenance, virtual money, etc., receive payment directly to their existing bank account, but do not report it for tax purposes.

Taxpayers have not yet been informed what they should do to report that type of income. Inflows from abroad are especially suspicious to individuals in Bosnia and Herzegovina because there is no clear evidence of their origin. Until investigative actions are carried out, the exact purpose of the transfer of money from abroad is not known. There are opportunities to use this money to finance arms trafficking, drugs, terrorism and other criminal activities.

The Law on Income Tax of the Republika Srpska (Official Gazette of the Republika Srpska No. 60/15, 5/16, 66/18, 105/19, 123/20 and 49/21) has clearly defined that all these activities fall under other income and that natural persons and entrepreneurs are legally obliged to submit an annual tax return for Income Tax (Form 1004), no later than March 31. current year for all inflows from the period 01.01. - 31.12. previous year, pursuant to the Law on Income Tax of the Republika Srpska (Official Gazette of the Republika Srpska No. 60/15, 5/16, 66/18, 105/19, 123/20 and 49/21) and thus state the realized other income in order to calculate tax on other income. Necessary

techniques and methods of forensic accounting would in this case be reflected in the verification of form 1004 with the balance on the current accounts of individuals and verification of the merits of the inflow. In the future, a draft of the Law on the Origin of Property is being created, and will be closely related to the forensic activities mentioned above, with special emphasis on the origin of inflows from all sources for individuals and their legal basis. The goal of forensic accounting would be to detect the origin of money, the final destination of money transfers and to put the income from this type of transfer within the legal framework.

3. Statement of operating losses and reduced tax liabilities of related legal entities

3.1. Example of incorrect presentation of data in tax records

The current practice is that a large number of legal entities in Bosnia and Herzegovina have established parent companies abroad or entrepreneurial activities in Bosnia and Herzegovina with which they perform from 90% to 100% of the turnover in the books, which makes it difficult to determine tax liabilities, profit and income tax for legal entities and entrepreneurs registered in Bosnia and Herzegovina. Legal entities knowingly create business books and in most cases report losses in operations in the territory of Bosnia and Herzegovina, which results in non-calculation of the real value of tax liabilities. Entrepreneurs consciously, especially those engaged in agricultural production activities, open several entrepreneurial entities in Bosnia and Herzegovina, which operate with the parent legal entity. The cost of production is difficult to prove while the turnover reported between these legal entities is from 90% to 100%, thus increasing costs and reducing income tax. In the case of legal entities, the suspicion is that there is clear evidence that in most cases they withdraw funds from companies in Bosnia and Herzegovina, while at the same time showing operating losses. Also, it often happens that there are several related legal entities abroad and it is not uncommon for the parent company in Bosnia and Herzegovina to provide unjustified financing of these related parties abroad. It should be noted that in 99% of situations, no study on transfer prices, to be created in the business books of the parent company, is made as the study is an integral part of the annual income tax return (form 1101). The accountant in the interest of management, as practice has shown, misinterprets the reason for the study (should take into account the complete turnover of related parties and obligations and receivables, while in reality looks only at the obligations and therefore does not prepare the study). In the case of

entrepreneurs who do business with their parent company in Bosnia and Herzegovina, it happens that both the entrepreneur and the legal entity show losses, which is especially difficult to prove when it comes to agricultural production, namely the entrepreneurs who buy agricultural raw materials through purchase blocks. With this procurement, the related parent company is fully indebted and the payment under these transactions is made 100% of the process through compensations that are not legally regulated in detail. When preparing an annual income tax return for an entrepreneur who did business with his affiliated parent legal entity, it is difficult to prove the calculation of production that they reported through redemption blocks, while the reported income is problematic in most cases because the actual inflow of money to the entrepreneur's bank account did not happen, and debts are closed with compensations. Law on Profit Tax of the Republika Srpska (Official Gazette of the Republic of Srpska No. 51/01, 91/06, 57/12, 94/15, 1/17 and 58/19) and Rulebook on the Application of the Law on Profit Tax of the Republic of Srpska (Official Gazette of the Republika Srpska No. 70/01, 129/06, 110/07, 114/07, 62/08, 9/09, 122/10, 73/11, 17/13, 21/13, 99/13) clearly regulates the definition of related parties and the obligation to prepare a study on transfer pricing between related parties. The Law on Income Tax of the Republika Srpska and the Rulebook on the Application of the Law on Income Tax also regulate the definition of related parties. The necessary techniques and methods of forensic accounting in this case would be reflected in the verification of form 1104 and form 1101 with related parties and entrepreneurs. It is necessary to perform an in-depth analysis of the realized income of the entrepreneur, the amount of turnover through compensations and determine the exact procedure for calculating the cost of production with the entrepreneur (based on a sample of purchase blocks, take statements from individuals and determine whether the purchase was actually made in that amount and compare it with the development capabilities of the entrepreneur). Additionally, check the manner in which the legal entity made a study on transfer pricing, which it was legally obliged to do in order to submit form 1101. The goal of forensic accounting would be to detect large transactions with related parties, to monitor legislation and its application in the business of these related persons and to put the real realized income into the legal framework.

3.2. Example of transfer pricing

The current practice is that a large number of legal entities in Bosnia and Herzegovina have established their parent companies abroad, with which they perform a larger volume of turnover in the business books, making it difficult to determine corporate income tax and income tax liabilities for registered legal entities in Bosnia and Herzegovina. Most of these economic entities do not respect the legal provisions and do not compile a study on transfer prices, which should be an integral part of the tax balance that is submitted to the tax records. Business entities intentionally hide the turnover between related parties and express only the part according to which the reported turnover does not have to be a study on transfer prices, all with the aim of hiding the total turnover between related parties. It is not uncommon for legal entities from abroad to transfer funds to Bosnia and Herzegovina through various sales contracts in order to legally comply with tax records in their home country, and return the same money transferred to Bosnia and Herzegovina through loans from their affiliate to their home country. It also happens that large amounts of credit funds are taken from commercial banks through a related party in Bosnia and Herzegovina, although the related party operates at a loss and the same money is again transferred to the home country of the home entity (company). It is a very common situation that the parent company has its affiliates in several countries, so the transfer of money between them is very difficult to monitor. They often show negative business in related parties or a dependent entity (company) in order to be in the main place of business, ie. in the home country, reported a profit and paid tax liabilities. The Law on Profit Tax of the Republika Srpska and the Rulebook on the Application of the Law on Profit Tax of the Republika Srpska clearly regulate the definition of related parties and the obligation to prepare a study on transfer prices between related parties. The Law on Income Tax of the Republika Srpska and the Rulebook on the Application of the Law on Income Tax also regulate the definition of related parties. The necessary techniques and methods of forensic accounting in this case would be reflected in the verification of form 1101 with related parties. It is needed to perform an in-depth analysis of the realized income and complete turnover with related parties, both liabilities and receivables, because all in all it represents the basis for recording turnover between related parties that should be included in the study on transfer pricing. The goal of forensic accounting would be to detect large transactions with related parties, to monitor legislation and its application in the business of these related parties, and to put the real revenues and complete turnover between related parties within the legal framework.

Conclusion and recommendations

The subject of this paper was the analysis of the most common financial fraud in Bosnia and Herzegovina, the causes and consequences of the lack of their timely detection, reporting, investigation and prosecution. In this regard, it was mentioned that forensic accounting has the most accurate techniques for detecting financial fraud. Adequate application of forensic accounting and auditing would minimize this problem, and the process of controlling and sanctioning non-compliance with audit recommendations would be completed. New steps would be introduced by applying forensic accounting and detecting those responsible for causing business irregularities, bringing them to court and conducting investigative actions and gathering evidence to prove guilt and responsibility, which would greatly contribute to protecting Bosnia and Herzegovina's economy from the gray economy. A prerequisite for the application of forensic accounting and auditing in Bosnia and Herzegovina is well-regulated legislation in the field of accounting and auditing that recognizes the profession of forensic accountant at the state level, and updated other relevant laws and regulations accordingly. Namely, forensic accounting in the profession is currently only recognized in the Law on Accounting and Auditing of the Republika Srpska (Official Gazette of the Republic of Srpska No. 67/05, 36/09, 52/11, 94/15 and 78/20). The procedure for hiring a forensic scientist in accounting and auditing is not clearly defined, while the procedure for hiring a certified accountant and a certified accounting technician is clearly defined. Legal non-recognition of the engagement of a forensic accountant and auditor is a major limitation in its application. Due to this restriction, there has been a lot of space for various types of manipulations and criminal acts. Legal recognition of a forensic accountant and forensic auditor would improve and expand the process of existing auditing practice with an additional two steps. Thus, after giving the auditor's opinion, the procedure of detecting economic crime would be started, detecting the persons responsible for the newly created negative situation and bringing them before the court in order to determine guilt and responsibility. Finally, with the application of a well-defined legal framework, it is necessary to include in this practice other competent institutions such as the Ministry of Finance, the Ministry of Interior, the Tax Administration, the Indirect Taxation Authority and others.

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Sažetak

Cilj rada je da rasvijetli dva najučestalija primjera finansijskih pronevjera, koji se dešavaju u većini privrednih subjekata u Bosni i Hercegovini. Analizirat će se uzroci i posljedice pomenutih finansijskih pronevjera, te razlozi zbog kojih se one proceduralno nisu otkrile na vrijeme. Prvi primjer veže se za prilive novca iz inostranstva, koji stvaraju sumnju u osnovanost, dok se drugi primjer veže za iskazivanje gubitaka u poslovanju i smanjene poreske obaveze kod povezanih pravnih lica. Svaki od primjera će biti detaljno analiziran u pogledu uzroka nastanka finansijskih pronevjera, načina njihovog sprovođenja, relevantne knjigovodstvene evidencije, te konačno načina njihovog otkrivanja. Analiza pomenutih finansijskih pronevjera dat će nam uvid i u manje česte zloupotrebe koje se dešavaju u praksi, te način njihovog otkrivanja. Napravit će se kritički osvrt na metode i tehnike forenzičnog računovodstva koje mogu biti korištene u kontekstu otkrivanja analiziranih finansijskih pronevjera u praksi.

Ključne riječi: finansijske pronevjere, primjeri finansijskih pronevjera, forenzično računovodstvo, Bosna i Hercegovina