

# FORENSIC ACCOUNTING

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**Abstract :** The system of financial reporting and the according and auditing profession are often accused because of the appearance of frauds and loss of trust in the reliability of financial information on the part of the users and makers of economic decisions. Great financial frauds at the end of the past and beginning of this century have imposed the profession, the Enron scandal lead towards formation of a new regulative bodies and the appearance of a new profession is called Forensic Accounting. Investigation or simply Forensic Accounting (FA). It is the consolidation of the Accounting, Auditing and Investigation skills. Forensic Accounting ae related with deterring, detecting and investigating frauds in financial reporting. Initially, forensic accountants were used by government agencies, to uncover and investigate uncover fraudulent financial reporting and misappropriated assets. Forensic Accounting in India, of late has come to lime-light recently due to increase in white-collar crimes in business. This research paper discusses on the prospects and problems of forensic accounting, as profession in India on the basis secondary data collected from various sources.

**Keywords:** Financial Reporting, Auditing, Frauds, Forensic Accounting, Accounting, Fraudulent, White-Collar crimes.

## I. INTRODUCTION

### II. What is Forensic Accounting?

The use of accounting skills, to investigate the fraud and theft and to analyse the financial information for use in the legal proceedings.

It provides analysis on accounting which is suitable to the court which will form the basis for discussion, debate and ultimately dispute resolution.

“Forensic” means the “evidence used to present in the court of law” and it is to that standard and potential outcome that forensic accountants generally have to work.

It encloses both Litigation Support and Investigate Accounting. Forensic Accountants utilize auditing, accounting and investigate skills while conducting an investigation. It is the ability of forensic accountants to react immediately and to communicate financial information clearly and expressing in a courtroom setting.

Forensic Accountants are well trained to deal with the problem and look into day to day business reality.

Forensic accountants might asses in looking for hidden assets in divorce cases or offer their services for different civil matters like breach of contacts, breach of guarantee etc.

### **OBJECTIVES OF THE STUDY:**

- It highlights the problems and prospects of Forensic accounting in India in the context of growing various frauds.
- To understand the basic techniques used by forensic accountants.
- To determine the differences between forensic accounting and financial audit.
- .To understands the importance of forensic accounting and accountants in a business or a company.
- To determine various measures taken by forensic accountants to prevent the fraud

### • **HISTORY:**

Maurice E. Peloubet was the man who came up with the word ‘forensic accounting’ in 1946. By the start of 1800’s both accountancy and legal profession started going hand in hand. Like any different field forensic accounting has evolved with the perpetual changes in technology, society and also the economy. Previously, the use of forensic accounting was not recognized as a separate practice area distinct from auditing. Over the decades, the auditing function separated itself from fraud detection. As occurred, forensic practice began to develop, and fraud investigation and litigation services began to be offered. As forensic practices followed their own separate path, the services provided changed into those of an investigation nature. Today, with the rash of cybercrimes being committed against every business connected to the internet, the nature of forensic practice is poised to expand into new territory. This article tells us the history of forensic accounting, and makes predictions about what the future holds for this practice area.

(In the fall of 2000 ) Enron's case- the corporate company would build a plant, and instantly claim the projected profits on its books although , it hadn't made any real money from it. If the revenue from plant were less than the projected amount, rather than taking the loss, the company would then transfer these assets to an off-the-books corporation like chewco \*(which was fake) , where the loss would go unreported. this kind of accounting enabled Enron to write off losses without damaging the company’s reputation .The securities exchange board investigated only to find that they were in debt of 6billion dollars.

But in Indian context history of forensic accounting goes back to Mauryan Times where Kautilya was the first person to publicize the famous forty ways of fraudulent practices in his renowned KautilyaArthashastra. Chartered accountants have monopoly over this fraud examining space crediting to their experience in accountancy. Although India’ chartered Accountants unit is well known to take up investigative assignments only a few companies having a department of finance have fraud examination as separate apply. However, the enormous space is dominated by the four big companies like Deloitte, KPMG, price water House Coopersand Ernst and Young. In India the formation of significant Fraud Investigation serves as a landmark for the creation of

forensic Accountants. Growing cyber-crimes, failure of regulators to trace scams, etc. are pinpointing to the requirement of forensic accountants, regardless of whether or not we understand the requirement or not.

#### ❖ **TECHNIQUES:**

The Direct technique is additionally referred to as transaction technique. When Direct technique of forensic accounting is used, the accountant examines canceled cheques, contracts, agreements, public records and notices etc. The accountant might also interrogate the management and staff. The Cash T Method, The Source and Application of Funds Method, The Net worth Method and The Bank Deposit Method come under Indirect technique.

The Cash T technique - It is typically utilized once a company's books and records don't clearly show their financial gains resulting in a suspicion that they would have omitted an amount of their earnings for a selected period of time.

The Source and Application of Funds Method - The Source and Application technique measures standard of living (lifestyle) against cash spent on assets and investments to ascertain if any noticeable discrepancies exist. It is the side of measurement incoming expenditures that make these two strategies usually comparable.

The Net Worth Method - Under this methodology, the whole net value of a person is evaluated from the start to the end of a stipulated period of time, The resultant number represents net worth which is compared to reported incomes over many periods. Any variations in the amount, a forensic accountant may pursue the investigation.

Bank Deposit Method - Bank deposits are tallied against entire expenses during a given year. This number is compared to funds from known sources to determine the total funds from unknown sources. A forensic accountant then will investigate these unknown sources further by interrogating individuals who are responsible and trace information, about those particular amounts.

#### ❖ **STEPS OF FORENSIC INVESTIGATION:**

1. **ACCEPTING THE INVESTIGATION:** The work done by forensic investigators requires specialization, detailed knowledge of the techniques of investigation and the legal frame work. The specialization of investigators include training in interrogation techniques, to maintain the safety of evidence other considerations include it or not the process is being requested by an audit client if there may be a chance of them being ethically questioned as the firm would be potentially exposed to threats the firm should avoid providing services to the same client without any robust safeguards.

2. **PLANNING THE INVESTIGATION:** The investigator's aim should only be to achieve what they have been asked to do and plan what they need to do accordingly. Primarily should be:

To know for how long this fraud has been operating for,

- a) The nature of fraud that has been carried out and
- b) In the financial loss that they have incurred.

The first step of planning investigation is to consider the best way to gather evidence including computer based audit techniques

3. **GATHERING EVIDENCE:** To gather evidence all the details regarding the fraud need to be gathered which includes understanding the type of fraud carried out and how it has been committed. The gathered evidence should be able to identify the fraudster's mechanism of their scheme, and the financial loss incurred. The team should be professional and trained in collecting evidence that needs to be presented in court. The evidence so provided needs to be linked without any gaps in the chain if not the evidence can also become inadmissible. Documents provided should neither be falsified nor should it be tampered with.

4. **REPORTING:** A report on what has been found, the summary of what went wrong, the techniques used by the fraudsters etc should be presented to the client. This is to keep them informed and be protected against any such fraudulent practices.

5. **COURT PROCEEDINGS :** Once the evidence is collected and when proves are concrete enough to present it in court both the parties are summoned to the court to present their findings and explain why or how the criminal act took place. Although the forensic accountants are expected to present their work professionally they also need to simplify complex accounting issues for everyone to comprehend the evidenc and its implications.

#### ❖ **DIFFERENCES BETWEEN FORENSIC ACCOUNTING AND FINANCIAL AUDIT**

FORENSIC ACCOUNTING	AUDIT
1.It focuses on-Fraudulent accounting/reporting.	1.Performs in accordance with usually accepted auditing standards (GAAS).
2. It seeks to verify and check the existence of specific issues or allegations ,extent and cause.	2.Provides opinion on monetary statements for general or restricted use.
3. It usually has few preset boundaries and greater access to executive management.	3.Conducts procedures in accordance with associate accepted methodology and procedures with materiality levels.
4. The analyst uses methods which include completeness and integrity.	4.An audit's objective is to provide assurance, to the intended user, that the information contained in those financial statements is a fair and accurate representation of the organization.
5.Forensic accounting services are usually necessary when there is a dispute or lawsuit already in place.	5.Audits often fail to detect fraud that is below the materiality level established by the auditor performing the engagement.
6. A forensic accounting engagement is designed to analyze a specific set of transactions or to search for misappropriated assets.	

#### ❖ **ADVANTAGES:**

- a. Review:The information is useful for legal reviews or public debates with the aim of resolving disputes.
- b. Valuable Contributions to an Economy: the information is analyzed and is helpful in formulating policies in an economy.

c. Detection of Fraud: forensic accounting ensures that accounting policies and systems are followed to the book -- where any activity which is different from the normal is detected.

d. Career Opportunity: it not only involves basic accounting activities, but also involves discovery of evidences presentable at the court of law. The acceptance of evidence generated by a forensic accountant by the judiciary, leaves them at a higher position when compared to others accountants.

❖ **DISADVANTAGES:**

- a. Costly : forensic accounting involves the utilization of the newest software system and skills, which proves to be very costly.
- b. Risk: Forensic accounting involves detection of fraudulent activities and presentable at the court of law. The forensic accountants might be black mailed, extorted or terrorized due to their involvement.
- c. Confidentiality: forensic accountants are employed from outside the business to analyses its monetary records, thereby exposing its money dealings to outsider scrutiny. However, the code of ethics of the Institute of Certified forensic Accountants states that "members must always observe confidentiality unless specific authority has been given to disclose information or there's a legal duty to disclose.
- d Losing worker' Trust : It is quite obvious for workers to be offended when their work is being scrutinized by a 3rd party. Lack of trust can also lead to inefficiency at work .

❖ **MAJOR SCAMS:**

- XEROX CORP
- SUNBEAM
- FIVE PROMINENT BANKS IN NIGERIA DECLARED INSOLVENT
- CADBURY

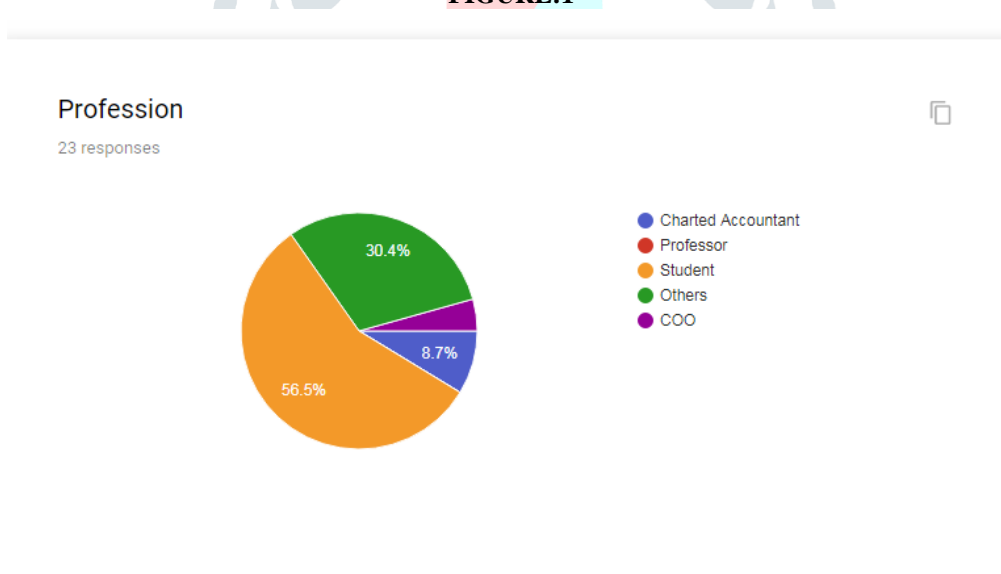
➤ **About The Methodology:**

The Survey has been conducted and analysed in three ways .i.e., from the point view of Chartered Accountant, Students, Professors and others.

The analysis was done on the form of a questionnaire which contained questions associated with the- Support of people for the move, their views, benefits and difficulty faced by them by Forensic Accounting and the assistance provided by Forensic Accountants.

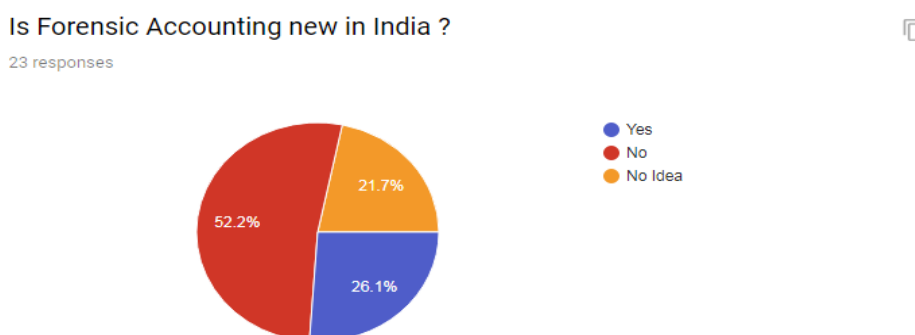
The analysis was done with a sample size of 23 numbers of respondents

**FIGURE:1**



Source: Own Computation Primary Data.

**FIGURE:2**

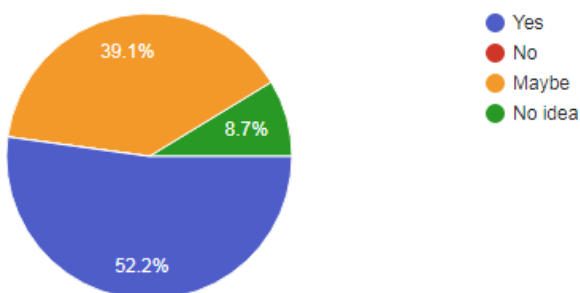


Source: Own Computation Primary Data.

**FIGURE: 3**

Is there as need for the service of a forensic accoun

23 responses

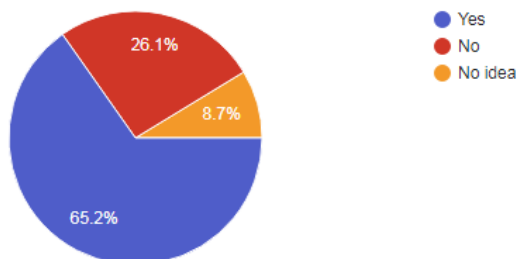


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**FIGURE: 4**

Are you aware of what is forensic Accounting is ?

23 responses

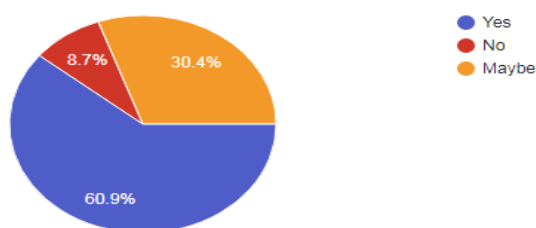


Source: Own Computation Primary Data.

**FIGURE: 5**

Should the topic Forensic accounting be implemented in students day to day curriculum ?

23 responses

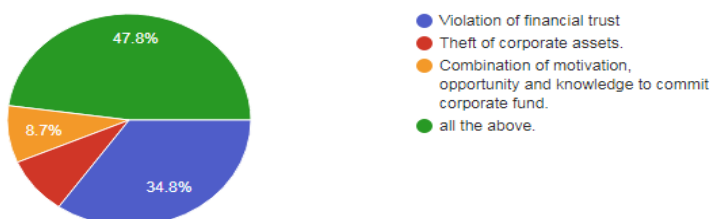


Source: Own Computation Primary Data.

**FIGURE: 6**

According to your point of view what is white-collar crime ?

23 responses

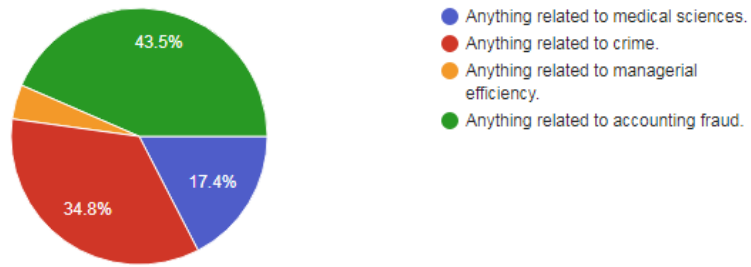


Source: Own Computation Primary Data.

FIGURE: 7

What do you understand by the term "Forensic"?

23 responses

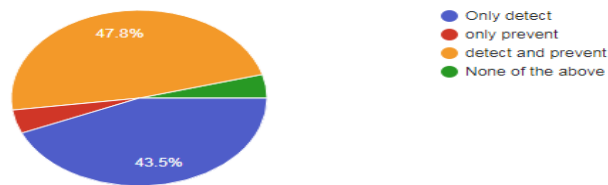


Source: Own Computation Primary Data.

FIGURE: 8

Can forensic accounting be used to detect and prevent the white-collar crimes ?

23 responses

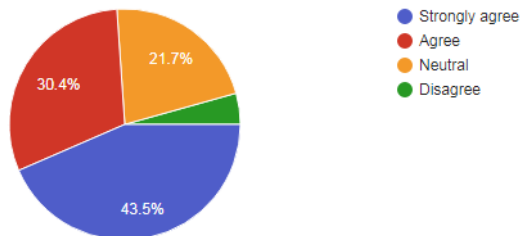


Source: Own Computation Primary Data

FIGURE: 9

Will the 'forensic accountants examine financial records and transactions closely to identify and stop frauds?

23 responses

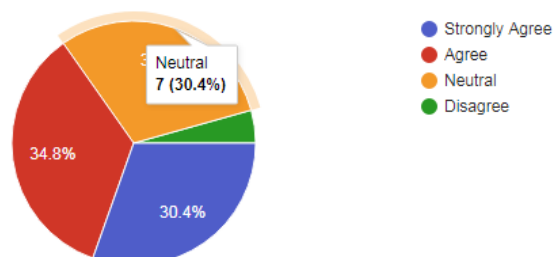


Source: Own Computation Primary Data

FIGURE: 10

The forensic accountant in India is up to a hard job because of the high rate of dis-honesty in the country?

23 responses

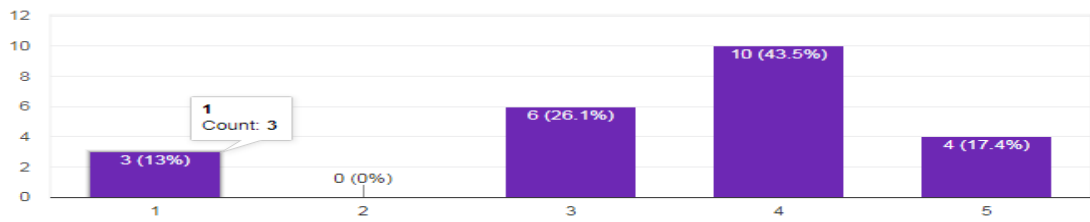


Source: Own Computation Primary Data

FIGURE: 11

How would you rate a company/business in which a forensic accountant is part of the organization?

23 responses

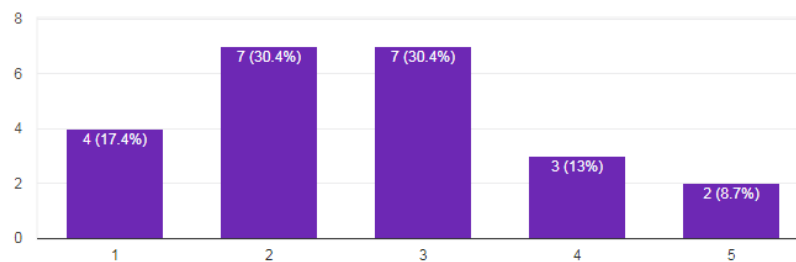


Source: Own Computation Primary Data

FIGURE: 12

How would you rate a company/business in which a forensic accountant is NOT part of the organization?

23 responses

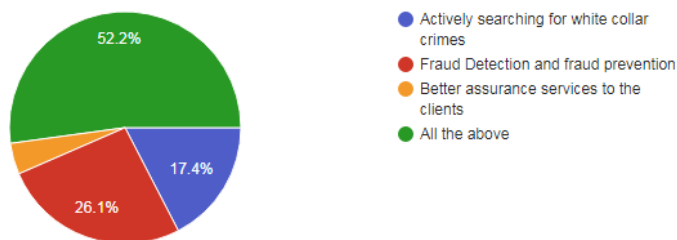


Source: Own Computation Primary Data

FIGURE: 13

What is the aim of Forensic Accounting ?

23 responses

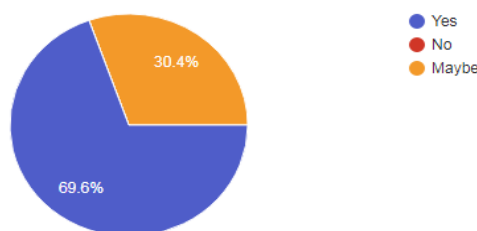


Source: Own Computation Primary Data

FIGURE: 14

Do you believe employing a forensic accountant would make some positive impact on the detection and prevention of fraud in your organization?

23 responses

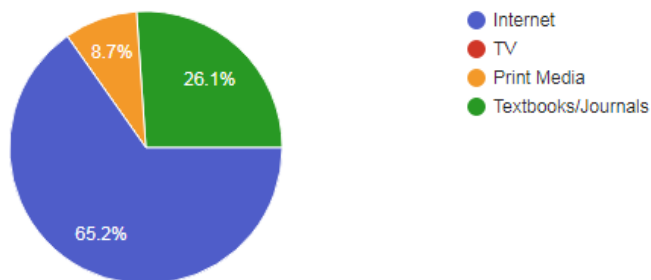


Source: Own Computation Primary Data

FIGURE: 15

## How did you hear about forensic accounting?

23 responses

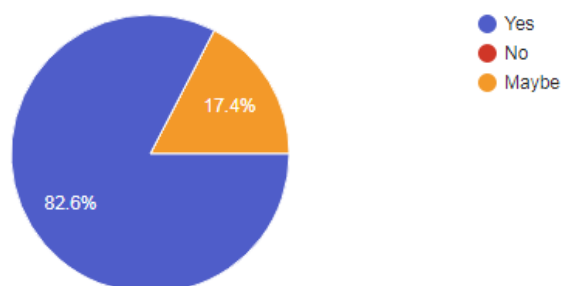


Source: Own Computation Primary Data

FIGURE: 16

## Knowledge of forensic accountant and auditors in your organization will make some impact on the nations fight against fraud and theft of assets?

23 responses



Source: Own Computation Primary Data.

❖ **LIMITATIONS OF THE STUDY:**

- Time constraint was one of the major limitations during the study.
- Increased chances of threats and negative publicity.
- Very Expensive-Costs a lot of money.
- Time Taking process.
- It affects the employees' morale.

❖ **CONCLUSION:**

As the government is trying to get awareness about forensic accounting in the colleges and in the companies too. As it is not in a regular use but should make a mandatory subject so that people will know the importance of forensic accounting, about the forensic accountants, thefts and frauds which are taking place in the companies. So that the measures are taking from starting to prevent theft, misappropriation of assets, and fraud.

❖ **BIBLIOGRAPHY.**➤ **BOOKS:**

- Forensic accounting and fraud investigation for non-experts- 3<sup>rd</sup> edition.
- Detecting accounting fraud.
- Financial forensics body of knowledge.

➤ **LINKS:**

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