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## A Study on Forensic Accounting

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### ABSTRACT

*The importance of financial accounting has increased due to rapid increase in corporate and public sector. India which is a developing economy with expanding rates of business deals. Due to the fact that few companies are still new and inexperienced in managing business and its accounts this has created undetected loopholes for accounting fraud committers. This has also created bad perceptions among the public regarding the various fraudulent activities that emerge in the country.*

*Fraud detection that plays a vital role in business growth .This article maps the importance of fraud detection to strengthen the business in this competitive world.*

*Forensic accounting is the special area which talks about various cases investigated and solved by forensic accountants. Fraud examination in forensic accounting is different from that of traditional accounting it has the intuitive ability to analyze fraud. The aim of the paper is to identify the role of forensic accounting in fraud investigations.*

**Key Words:** *Fraud, Forensic Accounting, Investigation.*

### INTRODUCTION

Forensic accounting is an investigation of accounting ,auditing and investigative skills. It is a specialized accounting method where accounting skills are used to investigate fraud or embezzlement, manipulation and to analyze financial information for the use in legal proceedings. The accounting analysis provided by the forensic accountants is more appropriate to the court as an evidence and which can be up for discussion and ultimately dispute resolution. Forensic accountants conjointly stated as forensic auditors or investigator auditors usually need to provide knowledgeable proof and an evidence which is concrete at the ultimate trial.

Along with visual aids to support trial proof a forensic accountant should also testify in court. For business investigations forensic accounting entails the utilization of tracing fund, identification , recovery and due diligence reviews. Forensic accountants may get in various disputes resolutions (ADR) thanks to the involvement in legal problems and familiarity with the judicature.

Forensic accountants analyze, interpret and summarize complicated monetary and business matters. They'll be used by insurance corporations , banks ,police forces ,government agencies or public accounting corporations. Forensic accountants compile monetary proof, develop the information collected and present their findings.

Forensic accounting conjointly encompasses the determination of whether or not criminal matters occurred. Such crimes might embody worker larceny, securities fraud, falsification of monetary statement data, insurance fraud. Forensic accountants might assist in looking for hidden assets in divorce cases or offer their services for different civil matters like breach of contracts, tort, disagreements about company acquisitions, breaches of guarantee or business valuation disputes.

### OBJECTIVES:

- a. To understand what is Forensic Accounting and its History
- b. To understand the basic techniques used by forensic accountants.
- c. To determine the differences between forensic accounting and financial audit.

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## HISTORY

Maurice E. Peloubet was the man who came up with the word 'forensic accounting' in 1946 "Forensic Accounting: Its Place in Today's Economy." Archeological findings reveal that, during 3300-3500 B.C itself the accountants that were present in those days in Egypt, were very much into the detection of fraudulent practices. 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. Because the frauds in several sectors like financial frauds, crimes over the web, concealment of real amounts and lots of different economic crimes etc. were the reasons that arose the need for forensic accounting.

In 1930's America Eliot Ness. (He was most likely to be America's 1st high-profile forensic accountant) was attributable for bringing down a criminal named Al Capone who earned money through embezzlement, means of wagering, and also by other illegal and unlawful methods.

(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 6 billion 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 Kautilya Arthashastra. Chartered accountants have monopoly over this fraud examining space crediting to their experience in accountancy. Although India's 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 Coopers and 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 specialisation, detailed knowledge of the techniques of investigation and the legal frame work. The specialisation of investigators include training in interrogation techniques, to maintain the safety of evidence other considerations include if or not the process is being requested by an audit client if there maybe 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 evidence and its implications.

### DIFFERENCES BETWEEN FORENSIC ACCOUNTING AND FINANCIAL AUDIT

FORENSIC ACCOUNTING	AUDIT
<ol style="list-style-type: none"> <li>1.It focuses on-Fraudulent accounting/reporting.</li> <li>2. It seeks to verify and check the existence of specific issues or allegations ,extent and cause.</li> <li>3. It usually has few preset boundaries and greater access to executive management.</li> <li>4. The analyst uses methods which include completeness and integrity.</li> <li>5.Forensic accounting services are usually necessary when there is a dispute or lawsuit already in place.</li> <li>6. A forensic accounting engagement is designed to analyze a specific set of transactions or to search for misappropriated assets.</li> </ol>	<ol style="list-style-type: none"> <li>1.Performs in accordance with usually accepted auditing standards (GAAS).</li> <li>2.Provides opinion on monetary statements for general or restricted use.</li> <li>3.Conducts procedures in accordance with associate accepted methodology and procedures with materiality levels.</li> <li>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.</li> <li>5.Audits often fail to detect fraud that is below the materiality level established by the auditor performing the engagement.</li> </ol>

**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 terrorised due to their involvement.
- c. Confidentiality: forensic accountants are employed from outside the business to analyse 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

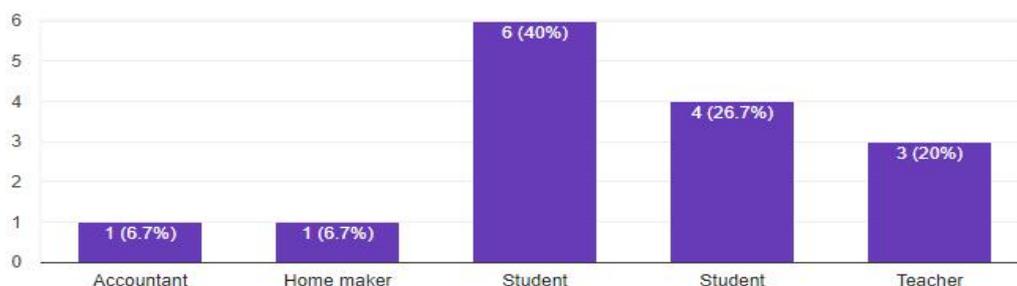
CADBURY

**METHODOLOGY :SECONDARY DATA**

Profession:

Profession :

15 responses



### What According to you is White-Collar Crime ?

What according to you is White-Collar Crime ?

15 responses



As Seen in the chart According to the majority :

40%- Says Theft or Embezzlement off corporate assets .

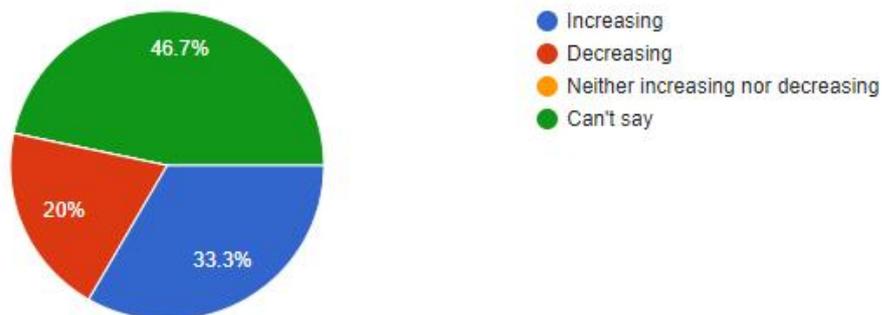
26.7%- Violation of Financial Trust.

13.3%- Combination of Motivation Opportunity and Knowledge to commit Corporate Fraud

20%- say It's All the Above .

Incidence of white-collar crime over the period 2002-2006 is :

15 responses



**The Pie Chart Says :-**

**46.7%- Says that the incidence of white-Collar crime over the period of 2002-2006 is not assessed properly .**

**33.3%- Says that the incidence of White-Collar crime over the period o White-Collar Crime have Increased.**

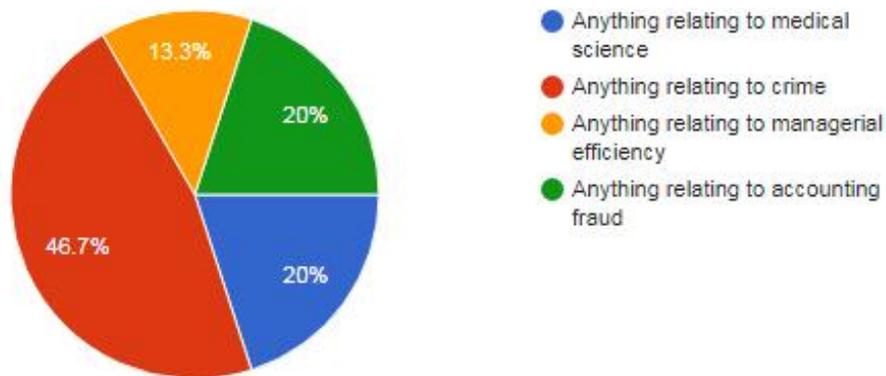
**20%- Says that the incidence have Decreased over the period.**

**What do you understand by the Word 'Forensic' ?**

What do you understand by the word ' Forensic' ?



15 responses



The Sound of Forensic Accounting in India

**This time Pie Chart Speaks about what people know about Forensic in India:-**

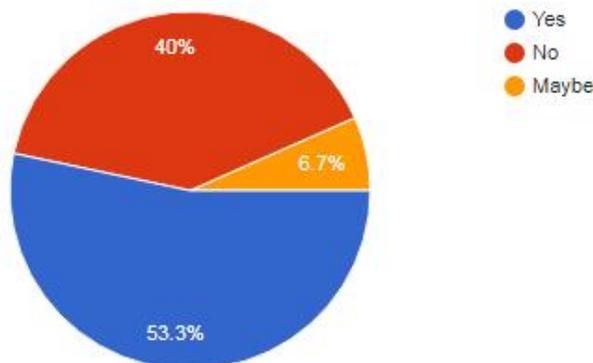
**46.7%- People in India Thinks Forensic means anything Related to Crime .**

**20%- Says it's Something Related to Medical Science or Anything relating to accounting fraud.**

**13.3%- Says it's Something related to managerial efficiency .**

Have you head of the Term " Forensic accounting" ?

15 responses



**The Term Forensic Accounting is Pretty Audible in India But doesn't have much Impact or have not got the Spot light.**

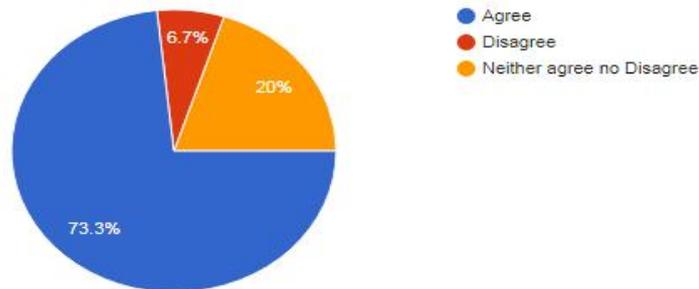
**53.3%- Respondents says they have heard about this term.**

**40%- Respondents says they have not Heard about this Term.**

**6.7% - Are confused if they have heard about the Forensic Accounting or the Forensics from CID.**

**Existing criminal law in India already covers regulation with respect to white collar crime .**

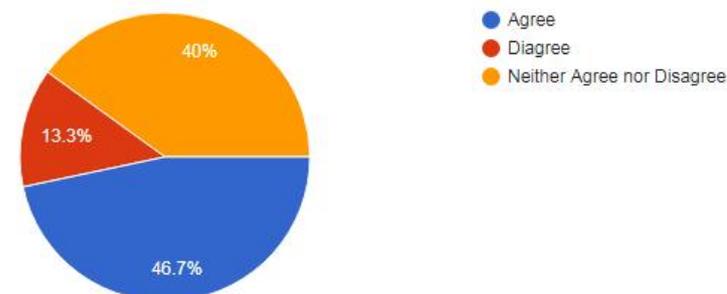
15 responses



**Can Forensic Accounting be used to detect and prevent while collar Crime ?**

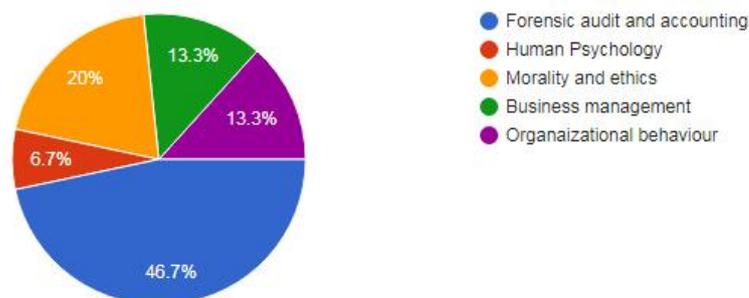
There is no Legal Provision in India to prevent white-collar crime, So new tool like forensic audit is on the threshold.

15 responses



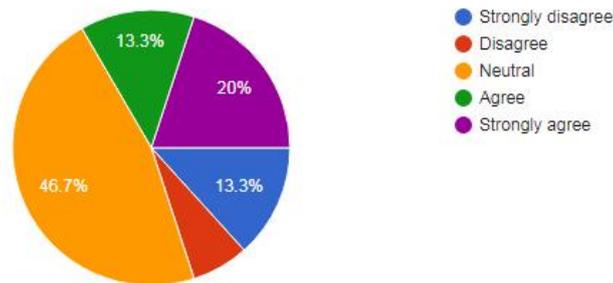
In order to practice fraud audit, law professionals will require additional skills apart from their conventional training in respect to which of the following field of

15 responses



Forensic auditors should be allowed to make formal public appearance in court of law to present available audit evidence in support of white-collar crime.

15 responses



## CONCLUSION

A lot of firms around the world believe the market is sufficiently large to support independent unit devoted strictly to forensic accounting. All of the larger accounting companies, as well as several medium sized have recently created forensic accounting department because forensic accounting is comparatively a brand new space of study, a series of working definition and sharing of company experience that ought to be undertaken encouraged to ensure a common understanding. Indeed there's beneficial future for forensic accounting as a separate "niche" consulting. Forensic accountants are solely handling money implications of the case entrusted to them and not participating in auditing exercise. On account of world competition the accounting profession should persuade the market place that has the "best-equipped" professionals to perform such services. While majority of CA's have professional analytical skills they have to acknowledge that "forensic" services need 'specialised' coaching yet as real life 'practical' company expertise.

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