

Success of Forensic accounting over traditional auditing

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ABSTRACT

Forensic accounting is the practice of utilizing accounting, auditing, and investigative skills to assist in legal matters. It encompasses two main areas – litigation support and investigation. It is a new area where various stakeholders, like banks, insurance companies and even public have increased taking the help of forensic accountants. In the emerging economic scenario, forensic accounting is an essential tool for uncovering or inquiry of financial crime and the direction of justice, providing decisive information about the facts found related to financial crime. Since the scope of Forensic Accounting has been growing steadily, it is also important to make sure that a company's finances are being kept safe. The increase in white collar crime and the difficulties faced by law enforcement agencies in uncovering fraud have also contributed to the growing need of forensic accounting. While many companies have always had in-house accountants to monitor and minimize any irregularities or complications that arise over the course of regular business, there are still instances of fraudulent activity. While the numbers may be balancing out in the end, businesses are still finding cleverly masked fraudulent activity when they go through the books. The paper focuses on the concept of forensic accounting and its importance and challenges. It also enumerates the differences between traditional auditing and forensic accounting. i.e., how the forensic accounting is proved to be an effective tool in detecting and preventing the white collar crime.

Keywords: Forensic Accounting, Auditing, detection and investigation of Fraud and effective tool.

I. INTRODUCTION

Forensic accounting is a specific area of accounting which utilizes accounting, auditing, and investigative skills to investigate fraud and analyse financial information that can be utilized in legal trials. It helps to resolve legal issues. Forensic accounting is judicious mix of accounting, auditing and investigative skills to perform investigations of financial frauds. It is helpful for legal action and analytical Accounting.

According to the Journal of Forensic Accounting, "Forensic accounting is sufficiently thorough and complete so that an accountant, in his/ her considered independent professional judgment, can deliver a finding as to accounts, inventories, or the presentation thereof that is of such quality that it

would be sustainable in some adversarial legal proceeding, or within some judicial or administrative review.”[CITATION Fra03 \l 1033]

1.1 Objectives of Forensic Auditing

1. To use the forensic accountant's conclusions to facilitate a settlement, claim, or jury award by reducing the financial component as an area of continuing debate
 2. To avoid fraud and theft
 3. To restore the downgraded public confidence
 4. To formulate and establish a comprehensive corporate governance policy
 5. To create a positive work environment
- Techniques and tools of forensic audit

1.2 Need for Forensic Accounting

Forensic Accounting is needed due to the following reasons:

- People and corporates are increasingly going for court action to resolve their problems,
- Trade transactions are increasing and getting more complex,
- People and corporates are having more problems with government,
- Employees involving with fraud is increasing and it is getting harder to unveil and prevent them,
- There have been increasing fraud with financial tables of companies and this led to increasing harm to society,
- It has come out that there has been increasing number and amounts of unsuccessful companies,
- Lawyers and courts need more support from specialists in the different areas of fraud,
- There has been increasing fraud in the virtual environment and the necessity of experts to fight against these.

II. LITERATURE REVIEW

Bhasin (2016) deals that while framing the accounting policy the help of expert should be taken as this will help in reducing fraud. Recent fraud (WorldCom, Satyam) was due to failure of Corporate Governance. Therefore paper discussed the key role of Forensic Accounting professional to have strong internal controls.

Yadav & Yadav (2013) has discussed the basic of forensic accounting and its application to detect fraud in the industries article further discussed the use of experts in the field of book keepings so that all kind of the case in the court of law can be handled by them. This article also discussed the various fraud cases of India in short.

Chakrabarti (2014) Forensic accounting has been in limelight after Satyam case, which urges a need of forensic accounting professional to detect and prevent fraud on time so as to control the white collar time. The study focus on the challenges to be handled in future as an expert in this profession.

Research gap: The past studies focussed on the importance of forensic accounting. The gap lies between how forensic accounting is superior to traditional auditing.

III. RESEARCH DESIGN

3.1 Statement of the Problem

The study has been undertaken to study the emerging trends of forensic accounting. Even though the need of Forensic Accounting has been steadily growing, its scope is still limited in India due to lack of awareness and its own problems in adoption. The paper also offers some suggestions to overcome the challenges in carrying adopting Forensic Accounting.

3.2 Objectives of the Study

- To understand the concept of Forensic Accounting
- To understand the differences between Auditing and Forensic Accounting

- To know the benefits and challenges in adopting Forensic Accounting
- To know how Forensic Accounting is an effective tool over Auditing

3.3 Scope of the Study

- The study focuses on importance of Forensic Accounting
- The study covers the basic concepts, challenges, advantages and it also shows how it is different from traditional auditing

3.4 Limitations of the Study

- The accuracy of the paper depends upon the accuracy of secondary data collected for the purpose.
- The paper's scope is limited as it enumerates much on the differences between auditing and forensic accounting.

IV. METHODOLOGY

4.1 Data Collection Method

Secondary data- The data for the study has been collected from various websites by accessing to e-books, e-journals and e-newspapers.

Research Type: The study is exploratory/analytical in nature.

4.2 Data analysis and Interpretation

Forensic Accounting Vs. Traditional Auditing

An audit is a set of tests and procedures carried out according to generally accepted auditing standards. Those standards require that the auditors plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

The goal of the audit is to provide an opinion on the financial statements. That opinion is in the form of a letter and almost always in an unqualified opinion. It is important to note the goal of the audit is not to detect fraud but to ensure that the financial statements are free of material misstatement

Forensic Accounting is defined as the use of accounting skills to investigate fraud or embezzlement and to analyze financial information for use in legal proceedings.

Forensic accounting is typically used in the course of an investigation. The goal of which would be to detect fraud and provide evidence which can be used in a court of law. The proceedings are not always criminal but often times civil and also require a valuation of assets (as in a divorce case).

- a. Forensic accounting is the use of accounting skills to investigate fraud or embezzlement and to analyze financial information for use in legal proceedings. Where traditional accounting deals in the assessment of a business' funds and properly conveying that information to investors and management, a forensic accountant is called upon to investigate the flow of funds through a business to evaluate the path it takes and determine whether illegal transactions have occurred.
- b. A forensic accountant investigates a wide range of different crimes that relate to fraud, such as corporate, health care, mass marketing, hedge fund, and securities fraud. They also investigate other crimes such as contract disagreements, money laundering, and embezzlement. And traditional Auditing is not.
- c. While the duties of a forensic accountant mainly leads them to investigating and analyzing, they are also commonly called on as an expert witness during a trial, due to the combination of experience and knowledge required to enter the field.

- d. There are also instances in which the skills forensic accountants employ are used in more personal matters. The dissolution of a marriage, for instance, is an event during which a forensic accountant will review the financial situation of both parties as well as their spending to further the settlement process or to assist attorneys with accurate information to use in court. Forensic attorneys are able to trace assets through the various investments and accounts as well as identify any hidden income or assets.
- e. **Forensic accounting** refers to a strategic approach whereby financial data and non-financial information are gathered, monitored, studied and analysed for fraud-prevention purposes. While the standard accountant focuses on balancing books and maintaining records, the forensic accountant intensively investigates financial activity for evidence of misconduct.

4.2 Benefits of Forensic Accounting

- **Minimised Losses:** The primary benefit of strong forensic accounting is the way in which it can help minimise and prevent unnecessary loss. Fraudulent activity and general financial discrepancies cost the business community extraordinary sums of money, every hour of every day. The forensic accountant ensures this isn't allowed to happen.
- **Improved Efficiency:** Forensic accountants play a key role in examining and investigating current financial processes and standards, which can help in the identification of more effective and efficient solutions. The whole process is one of detecting problems and areas of improvement for the benefit of the business.
- **Reduced Exploitation Risk:** By proactively patching any obvious 'gaps' in current financial operational standards, the forensic accountant can ensure that risk of future exploitation is significantly reduced. It's a case of protecting the best interests of the business before fraudulent activity can take place.
- **Avoidance of Legal Problems:** Dealing with instances of fraud (internal or external) can be spectacularly disruptive and costly for the business. In an ideal situation, forensic accountancy can be used to avoid such scenarios from ever occurring by both preventing fraudulent activity and nipping any problems detected in the bud.
- **Improved Brand Reputation and Authority:** A brand that leaves itself wide open to manipulation and fraud is a brand that is very difficult to respect, trust and work with. Fraud can do the kind of reputational damage that is borderline impossible to repair – hence the importance of thorough and on-going forensic accountancy.
- **Fraud Identification and Prevention:** Fraud is quite common in big organizations where the number of daily financial transactions is huge. In such an environment, an employee can easily undertake fraudulent activities without being caught. **Forensic accounting** helps in analyzing whether the company's accounting policies are followed or not, and whether all the transactions are clearly stated in the books of accounts. Any deviation observed in the books of accounts can help in identifying fraud, and necessary measures can be taken to prevent it in the future.
- **Making Sound Investment Decisions:** As forensic accounting helps in analyzing the financial standing and weaknesses of a business, it provides a path for investors to make thoughtful investment decisions. A company dealing with fraud is definitely not a good option for investment. Therefore, the reports of forensic accountants act as a guide for potential investors of a company. Many organizations also apply for loans from various financial institutions. By performing an analysis, such institutions can come to a decision on whether they would like to fund a company or not.
- **Formulation of Economic Policies:** Various cases of fraud that become evident after forensic analysis act as a reference for the government to formulate improved economic policies that

would be able to curb such fraudulent activities in the future. By doing so, the government can strengthen the economy and prevent such illegal activities in the country.

- **Rewarding Career Opportunity:** As a career, forensic accounting is extremely rewarding, as it not only involves regular accounting activities, but also involves identification, analysis, and reporting of the findings during an audit. The acceptance of reports generated by a forensic accountant by the court of law, gives them an upper hand as compared to other accountants. Good forensic accountants are in high demand and can easily draw a starting salary between \$30,000 and \$60,000 per annum.

4.3 Problems or challenges in implementing Forensic Accounting in India

- Forensic accounting is developing field of financial fraud detection. There is acute shortage of qualified accountants with adequate technical knowledge of forensic issues in India.
- In India, most of the financial fraud cases involved politicians, so it is crucial to find evidences against them.
- Indian judicial system still follows age old British judicial system. It is expensive to bring the matter to court and hire expert advocates.
- **Expensive:** Because of the lengthy period of time needed, forensic accounting can turn out to be expensive. This isn't a problem for huge corporations that have more than enough funds, but it can be an issue for smaller businesses that have limited budgets. Forensic accounting can be an expensive affair because the procedures which accountants use involve high-end accounting software.
- Due to liberalization and fast moving economy, more and more investors from foreign countries invest in India and so, it is difficult to sue financial fraudster from other countries.
- Because of continuous adoption of new techniques of Information and Technology by fraudster, it is difficult to Forensic Accountant to cope up with them.
- Forensic accounting is an expensive field compared to other investigative fields.
- It is not mandatory for companies to appoint forensic accountant in companies.
- There is no specific guideline or act on forensic accounting in India.
- **Time consuming:** It requires accountants to go through every piece of document to ensure that their investigation is complete and that they'll uncover every evidence that will solve the case. This can take many days and can even stretch to many weeks or months, depending on the magnitude of the case, the size of the organization involved, and the number of documents to review.
- **Distracting:** Forensic accounting can cause a distraction among employees, particularly when outside accountants are brought in. The process can disrupt the staff's normal routine and cause their productivity and efficiency to suffer.
- **It can affect employee morale:** Forensic accounting can cause employees to feel like their integrity is doubted, which can lead to lower staff morale. It's the responsibility of managers and business owners to make their people understand that forensic accounting is done not as a sign of distrust but as a way to improve business efficiency.
- **Confidentiality Issue:** Since the scrutiny of a company's financial records is done by an external forensic accountant, the chances of leakage of confidential matter is always there. It is true that their code of ethics clearly mentions that forensic accountants and other members involved in the scrutiny must not engage in disclosing confidential data to outsiders, but the possibility of disclosure cannot be nullified.
- **Increased Chances of Threats and Negative Publicity:** If the analysis of a company's financial statements points out the involvement of a particular person in fraudulent activities,

there is a significant chance that the person will try to threaten the company to safeguard himself from the trial. Also, any trial that confirms a fraud happening in the company comes under public eye and gains negative publicity, which directly affects the reputation and investor relations of the company.

- Despite the disadvantages associated with forensic accounting, it is, and will continue to be an important part in the world of business. This is because it helps organizations and individuals to figure out whether their financial accounts are accurate or fabricated to hide illegal activities going on within the organization.

4.4 Different tool and techniques used for Forensic Audit are:

- **Benchmarking** – comparison of financial result of one period with another or the performance of one cost centre, or business unit, with another and overall business performance with its pre decided standards.
- **Ratio analysis** – to identify any abnormal trends and changes.
- **System analysis** – to examine the systems in place and identifying any weaknesses which could be opportunities for the fraudsters.
- **Specialist software**- like audit tools for data matching analysis.
- **Exception reporting** –Generating automatic unchangeable reports that to find out deviation from the norms.

V. FINDINGS

- From the above study it has been discovered that forensic accounting helps in:
- Developing digital or computerized applications to support in the investigation as well as representation of the financial evidence.
- Playing a major role while assisting in legal proceedings that includes testifying in the courtroom as an expert witness and then making visual aids in order to support the trial evidence.
- Interconnecting the findings in terms of the reports, a collection of documents as well as exhibits.
- Help in evaluating and investigating the financial evidence.
- Forensic accounting is also useful in engaging in public practice or it may be integrated by the insurance organizations, police forces, financial institutions like banks, government agencies and many others.

VI. SUGGESTIONS

The organisations should follow forensic accounting in preventing white collar crime. So they should adopt forensic accounting. There is huge requirement for honesty, fairness and transparency in Indian Corporate reporting. Therefore, The Institute of Chartered Accountants of India (ICAI) started a course on forensic accounting for only its members. It is “Certificate Course on Forensic accounting and Fraud Detection using IT and CAATs”. At present, very few academic institutions are offering courses (full time or part time) on forensic accounting. Indian universities are lagging behind in this area as compared to other foreign universities. Some leading organization such as India forensic (Pune, Maharashtra) started certificate Course in Bank Forensic Accounting (CBFA), Certified Forensic Accounting Professional (CFAP). Institute of Chartered Financial Analyst of India (ICFAI) University also started Postgraduate Diploma in Forensic Accounting.

VII. CONCLUSION

The Association of Certified Fraud Examiners (ACFE) described **forensic accounting** as “the application of accounting skills to provide quantitative financial information about matters before the courts.” One of the vital elements of forensic accounting is the pursuit to recreate or reestablish previous event or events, through financial information where remaking or reestablishing is expected to be utilized in certain judicial proceedings — deposition, arbitration, civil or criminal court, plea bargaining, etc.

The forensic accounting is proved to be an effective by analyzing its benefits. The Traditional Auditing checks only the arithmetical accuracy of books of accounts and finds out the deviations there from. But forensic accounting is beyond this.

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