

FORENSIC ACCOUNTING



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Forensic Accounting Beginnings

The term "forensic accounting" was first used in 1946 by Maurice E. Peloubet, a partner in a New York accounting firm. He wrote about the use of accounting in courtroom proceedings as part of testimony, but acknowledged that investigation was becoming more prevalent for accountants due to the increase in government agencies that regulated financial practices. Journals began to publish articles about the connections between law and accounting. In 1953, a New York lawyer named Max Lourie claimed that he invented the phrase "forensic accounting," although Peloubet wrote about it first. Lourie stressed the need for forensic accounting literature and training.

Forensic accounting service has been the growth industry in the 1990s. Called the private eyes of the corporate culture, forensic accountants must have an investigative mentality. A normal accountant acts like a watchdog, but a forensic accountant must be trained to act like a bloodhound. They look behind the

facade and do not accept financial records at their face value.

Forensic Accounting

"Forensic" means "suitable for use in a court of law", and it is to that standard and potential outcome that forensic accountants generally have to work.

“Forensic accounting” is the practice of utilizing accounting, auditing, and investigative skills to assist in legal matters. Forensic accounting is the specialty practice area of accountancy that describes engagements that result from actual or anticipated disputes or litigation.

Forensic accounting is the application of accounting principles, theories, and disciplines to facts or hypotheses at issue in a legal dispute, and encompasses every branch of accounting knowledge.

There are two major aspects within forensic accounting practice -

1. *Litigation support services* that represent the factual presentation of economic issues related to existing or pending litigation. In this capacity, the forensic accounting professional quantifies damages sustained by parties involved in legal disputes and can assist in resolving disputes, even before they reach the courtroom. If a dispute reaches the courtroom, the forensic accountant may testify as an expert witness.
2. *Investigative services* that make use of the forensic accountant's skills, which may or may not lead to courtroom testimony. It is the act of determining whether criminal matters such as employee theft, securities fraud (including falsification of financial statements), identity theft, and insurance fraud have occurred. As part of the forensic accountant's work, he or she may recommend actions that can be taken to minimize future risk of loss. Investigation may also occur in civil matters. For example, the forensic accountant may search for hidden assets in divorce cases.

An important criterion is the ability to respond immediately and to communicate financial information clearly and concisely in a courtroom setting. A forensic accountant must be open to examining all alternatives, scrutinising the fine details and at the same time seeing the big picture.

Forensic accounting can involve the application of special skills in accounting, auditing, finance, quantitative methods, certain areas of the law and research, and investigative skills to collect, analyze, and evaluate evidential matter and to interpret and communicate findings.

Application of Principles of Forensic Accounting to an organisation

- One premise of forensic accounting is to look for indications of abnormal occurrences in the accounting and financial reporting systems.
- Having a forensic accounting orientation to designing the accounting processes will provide an opportunity to design in steps for verification of key assumptions and data while also providing the opportunity for identifying possible fraud.
- The related area of forensic auditing can help in reducing the transaction processing risk by helping to perform audit type procedures on a routine schedule.
- Timely performance of audit type procedures can help management and internal audit function be more effective by helping to identify and resolve potential internal control breakdowns quickly and thoroughly. It can reduce external audit costs by regularly completing testing procedures that are part of the annual certified audit.
- In instances where information processing systems cover a broad array of businesses and/or locations establishing routine or continuous monitoring of all transaction processing systems, it can be considered as a type of forensic accounting.

Some of the areas that the principles and activities of forensic accounting can apply in an organization include:

- Reviewing operational transactions for compliance with standard operating procedures and approvals.
- Completing analysis of financial disbursement transactions in the accounting system to determine if they are normal or outside company policy and, thus, possibly fraudulent.
- Reviewing general ledger and financial reporting system transactions for possible improper classification or manipulation of data or accounts and its impact on the resulting financial reports.
- Examining warranty claims or returns for patterns of fraud or abuse.
- Helping estimate the economic damages and the resulting insurance claims that stem from calamities such as fires or other natural disasters.
- Evaluating or confirming business valuation in mergers and acquisitions.

Forensic Accountants - The Bloodhounds of Book-keeping

Forensic accounting requires the most important quality a person can possess: the ability to think.

There is no book that tells you how to do a forensic investigation. It is about solving a puzzle or peeling an onion. It takes creativity.

All of the larger accounting firms, as well as many medium-sized and boutique firms, have specialist forensic accounting departments. Within these groups, there may be further sub-specializations: some forensic accountants may, for example, just specialize in insurance claims, personal injury claims, fraud, construction, or royalty audits.

Forensic accountants may be involved in recovering proceeds of crime and in relation to confiscation proceedings concerning actual or assumed proceeds of crime or money laundering. In the United Kingdom, relevant legislation is contained in the Proceeds of Crime Act 2002. In India there is a separate breed of forensic accountants called Certified Forensic Accounting Professionals.

Some forensic accountants are also Certified Fraud Examiners, Certified Public Accountants, or Chartered Accountants.

Forensic accountants utilize an understanding of business information and financial reporting systems, accounting and auditing standards and procedures, evidence gathering and investigative techniques, and litigation processes and procedures to perform their work. Forensic accountants are also increasingly playing more proactive risk reduction roles by designing and performing extended procedures as part of the statutory audit, acting as advisers to audit committees, fraud deterrence engagements, and assisting in investment analyst research.

The forensic Accountant is a bloodhound of Bookkeeping. These bloodhounds sniff out fraud and criminal transactions in bank, corporate entity or from any other organization's financial records. They hound for the conclusive evidences. External Auditors find out the deliberate misstatements only but the Forensic Accountants find out the misstatements deliberately. External auditors look at the numbers but the forensic auditors look beyond the numbers.

Forensic accountant takes a more proactive, skeptical approach in examining the books of Accounting. They make no assumption of management integrity (if they can assume so then there is no need for their appointment) show less concerns for the arithmetical accuracy have nothing to do with the Accounting or Assurance standards but are keen in exposing any possibility of fraud.

In addition to the specialized knowledge about the techniques of finding out the frauds one needs patience and analytical mindset. One has to look beyond the numbers and grasp the substance of the situation. It is basically the work of the intelligent accountants. He needs to question seemingly benign document and look for inconsistencies. He searches for evidence of criminal conduct or assists in the determination of, or rebuttal of, claimed damages.

Who needs Forensic Accountants

Forensic accountants are more than just number crunchers who happen to work on criminal or civil disputes -- these accountants possess additional skills. They must conduct investigations, know how to use a variety of computer programs and communicate well. Some forensic accountants specialize in specific industries that are susceptible to fraud, such as insurance or banking, and learn the business practices associated with those fields.

Forensic Accountants work in most major accounting firms and are needed for investigating mergers and acquisitions, and in tax investigations, economic crime investigations, all kinds of civil litigation support, specialized audits, and even in terrorist investigations.

Forensic Accountants work throughout the business world, in public accounting, corporations, and in all branches of government.

Forensic Accounting in India

Forensic accounting is unique in that it combines accounting with investigation. These bloodhounds – as opposed to the watchdogs that are auditors – attempt to sniff out fraudulent transactions from the financial records of banks and companies.

Sherlock Holmes was probably the most famous practitioner But Kautilya was the first economist who openly recognized the need of the forensic accountants. He mentioned forty ways of embezzlement centuries ago.

The Opportunities for the Forensic Accountants are growing at the rapid speed. Collapse of Enron and World Trade Centre twin towers have blessed the American Forensic Accountants with the opportunities.

Forensic accounting is still nascent in India. However, the nature of fraud in India has undergone a change. Reserve Bank of India has made forensic accounting audit compulsory for banks in India. However banks are hesitant in

approaching certified fraud examiners, and are mostly dependent on their internal auditors.

In India the formation of Serious Fraud Investigation Office is the landmark creation for the Forensic Accountants. Growing cyber crimes, failure of regulators to track the security scams, series of co-operative banks bursting - all are pinpointing the need of forensic accounting, irrespective of whether we understand the need or not.

In the Indian context the Forensic Accountants are the most required in the wake of the growing frauds. After the Satyam scam, forensic auditors are much in demand as many companies want to understand what could be the initial warning signals of a Satyam kind of fraud in other Indian companies. Even the government's Serious Fraud Investigation Office (SFIO) has sought the help of forensic accountants to get to the root of the financial fraud at Satyam.

How to become a Forensic Accountant

Commerce graduates can easily take up forensic accounting as a career. You need to become a chartered accountant and then specialise in forensic accounting. The forensic accountants prior audit and accounting experience will be of tremendous assistance. But ultimately, it is only through working with experienced forensic accountants on various cases that one can learn the skills necessary to become a capable forensic accountant.

There are several organizations that provide training and additional certification for forensic accountants. Each organization requires that its members possess varying degrees of education and experience, and they must sit for additional exams. These certifications show that a forensic accountant has training and experience beyond that of a standard accountant.

Some places where one can study and/or obtain certifications as Forensic Accounting Professional are:

- Institute of Chartered Accountants of India, New Delhi
- Association of certified fraud examiners (ACFE), USA
- Indiana University, Bloomington, USA

- British Columbia Institute of Technology, Canada
- Charles Stuart University, New South Wales, Australia

Some forensic accountants take courses in:

- Sociology
- Psychology
- Law enforcement
- Criminal law
- Business law
- Business and finance
- Information systems
- Communication

Conclusion

Forensic accountants are trained to detect evidence of frauds. Forensic accounting is about more than legal matters and financial numbers. There is an acute shortage of forensic accounting skill sets in India. A huge demand for forensic accountants has come up in the wake of the requirements from the investors after the Satyam fiasco. There are only about 400 forensic accountants in the country though India loses approximately \$40 billion because of frauds.

About the Author

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Mr. Rajkumar S Adukia is an eminent business consultant, academician, writer, and speaker. A senior partner of Adukia & Associates he has authored more than 34 books on a wide range of subjects. His books on IFRS namely, "Encyclopedia on IFRS (3000 pages) and The Handbook on IFRS (1000 pages) has served number of professionals who are on the lookout for a practical guidance on IFRS. The book on "Professional Opportunities for Chartered Accountants" is a handy tool and ready referencer to all Chartered Accountants.

In addition to being a Chartered Accountant, Company Secretary, Cost Accountant, MBA, Dip IFR (UK), Mr. Adukia also holds a Degree in Law and Diploma in Labor Laws. He has been involved in the activities of the Institute of Chartered Accountants of India (ICAI) since 1984 as a convenor of Kalbadevi CPE study circle. He was the Chairman of the Western Region of Institute of Chartered Accountants of India in 1997 and has been actively involved in various committees of ICAI. He became a member of the Central Council in 1998 and ever since he has worked tirelessly towards knowledge sharing, professional development and enhancing professional opportunities for members. He is a regular contributor to the various committees of the ICAI. He is currently the Chairman of Committee for Members in Industry and Internal Audit Standard Board of ICAI.

Mr. Adukia is a rank holder from Bombay University. He did his graduation from Sydenham College of Commerce & Economics. He received a Gold Medal for highest marks in Accountancy & Auditing in the Examination. He passed the Chartered Accountancy with 1st Rank in Inter CA & 6th Rank in Final CA, and 3rd Rank in Final Cost Accountancy Course in 1983. He started his practice as a Chartered Accountant on 1st July 1983, in the three decades following which he left no stone unturned, be it academic expertise or professional development. His level of knowledge, source of information, professional expertise spread across a wide range of subjects has made him a strong and sought after professional in every form of professional assignment.

He has been coordinating with various professional institutions, associations' universities, University Grants Commission and other educational institutions. Besides he has actively participated with accountability and standards-setting organizations in India and at the international level. He was a member of J.J. Irani committee which drafted Companies Bill 2008. He is also member of Secretarial Standards Board of ICSI. He represented ASSOCHAM as member of Cost Accounting Standards Board of ICWAI. He was a member of working group of Competition Commission of India, National Housing Bank, NABARD, RBI, CBI etc.

He has served on the Board of Directors in the capacity of independent director at BOI Asset management Co. Ltd, Bharat Sanchar Nigam Limited and SBI Mutual Funds Management Pvt Ltd. He was also a member of the London Fraud Investigation Team.

Mr. Rajkumar Adukia specializes in IFRS, Enterprise Risk Management, Internal Audit, Business Advisory and Planning, Commercial Law Compliance, XBRL, Labor Laws, Real Estate, Foreign Exchange Management, Insurance, Project Work, Carbon Credit, Taxation and Trusts. His clientele include large corporations, owner-managed companies, small manufacturers, service businesses, property management and construction, exporters and importers, and professionals. He has undertaken specific assignments on fraud investigation and reporting in the corporate sector and has developed background material on the same.

Based on his rich experience, he has written numerous articles on critical aspects of finance-accounting, auditing, taxation, valuation, public finance. His authoritative articles appear regularly in financial papers like Business India, Financial Express, Economic Times and other professional / business magazines. He has authored several accounting and auditing manuals. He has authored books on vast range of topics including IFRS, Internal Audit, Bank Audit, Green Audit, SEZ, CARO, PMLA, Antidumping, Income Tax Search, Survey and Seizure, Real Estate etc. His books are known for their practicality and for their proactive approaches to meeting practice needs.

Mr. Rajkumar is a frequent speaker on trade and finance at seminars and conferences organized by the Institute of Chartered Accountants of India, various Chambers of Commerce, Income Tax Offices and other Professional Associations. He has also lectured at the S.P. Jain Institute of Management, Intensive Coaching Classes for Inter & Final CA students and Direct Taxes Regional Training Institute of CBDT. He also develops and delivers short courses, seminars and workshops on changes and opportunities in trade and finance. He has extensive experience as a speaker, moderator and panelist at workshops and conferences held for both students and professionals both nationally and internationally.. Mr. Adukia has delivered lectures abroad at forums of International Federation of Accountants and has travelled across countries for professional work.

Professional Association: *Mr. Rajkumar S Adukia with his well chartered approach towards professional assignments has explored every possible opportunity in the fields of business and profession. Interested professionals are welcome to share their thoughts in this regard.*