

**Lecture note on**

## **Forensic Accounting**

(For MBA 1<sup>st</sup> semester)

### **Subject-Accounting and Financial Analysis**

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# Forensic Accounting



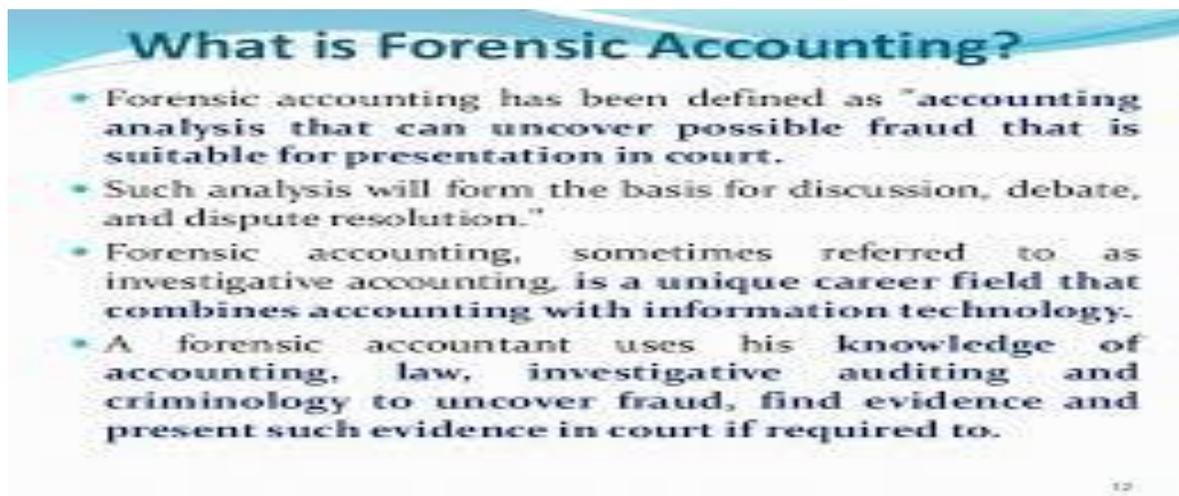
## 1. Concept of Forensic Accounting

Forensic Accounting (FA) is the combination of the Accounting, Auditing and Investigation skills. The term "forensic accounting" was first used in 1946 by Maurice E. Peloubet; a partner in a New York based accounting firm. The word forensic is derived from the Latin word '*forensis*', meaning thereby belonging to the forum (*the site for public discussion and debate in ancient Rome*). It refers as assistance in disputes regarding allegations or suspicion of fraud. Which are likely to involve litigation, expert determination and enquiry by an appropriate authority and investigations of suspected fraud and irregularity, which could potentially lead to civil, criminal or disciplinary proceedings.

The term "Forensic", according to the Webster's Dictionary means, "Belonging to, used in or suitable to courts of judicature or to public discussion and debate." The word accounting is defined as "a system of recording and summarizing business and financial transactions and analyzing, verifying, and recording the results."

According to George A. Manning, "Financial Investigation and Forensic Accounting" defines Forensic Accounting as the science of gathering and presenting financial information in a form that will be accepted by a court of jurisprudence against perpetrators of economic crimes.

## 2. Meaning of forensic Accounting



**What is Forensic Accounting?**

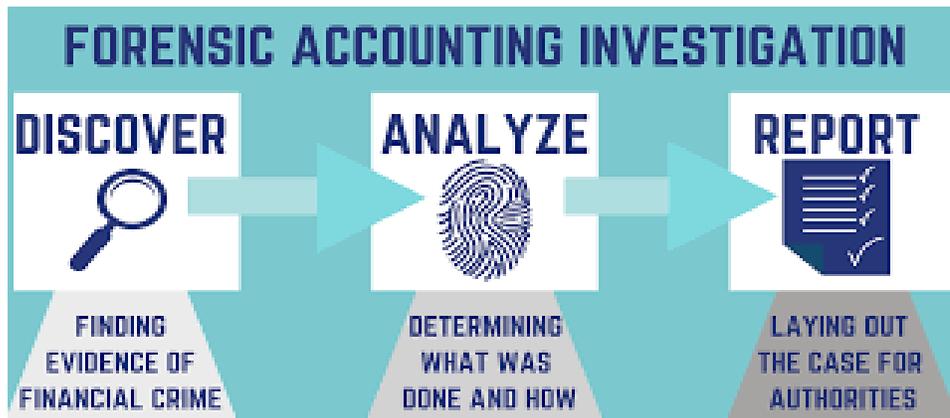
- Forensic accounting has been defined as "accounting analysis that can uncover possible fraud that is suitable for presentation in court."
- Such analysis will form the basis for discussion, debate, and dispute resolution."
- Forensic accounting, sometimes referred to as investigative accounting, is a unique career field that combines accounting with information technology.
- A forensic accountant uses his knowledge of accounting, law, investigative auditing and criminology to uncover fraud, find evidence and present such evidence in court if required to.

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According to AICPA ( American Institute of Certified Public Accountants ),(1993):  
"Forensic accounting is the application of accounting principles, theories, and discipline to facts or hypotheses at issues in a legal dispute and encompasses every branch of accounting knowledge."

The system of financial reporting and the accounting and auditing profession are often accused because of the appearance of frauds and the loss of trust in the reliability of financial information. Great financial frauds at the end of the past and the beginning of this century have imposed the need for deeper investigation of irregularities in the area of financial reporting. Forensic Accountants are related with deterring, detecting and investigating frauds in financial reporting.

Forensic accounting, sometimes called investigative accounting is the application of an expert knowledge and specific skills to spot transactions which are not authentic. It is used for fraud examination and fraud examination covers fraud allegations from inception to disposition, including obtaining evidence, interviewing, writing reports and testifying.



**Forensic Accounting assists an organization in legal matters in two ways –**

**i) Investigative Accounting** deals with the investigation of criminal matters relating to employee theft, securities, fraud, insurance fraud etc. and also includes provisions and suggestions regarding possible courses of action.

**ii) Litigation Support** involves the quantification of the amount of economic damages and also providing accounting assistance in litigation matters.

**Forensic accounting may consists of the following two major components:**

1. In case of court case, investigative skills of forensic accountant are used in two ways, he can be called upon to give his expert opinion based on his investigation and may require possible courtroom evidence.
2. Forensic accountant's investigative skills are required for collecting, analyzing, and evaluating financial evidence, as well as the ability to understand and communicate findings.

Today, a mechanism to detect and prevent corporate frauds and scams, forensic accounting has emerged as relatively new and effective tool in the hands of accountants to find out mistakes and malpractices in accounting . Forensic accountants are recruited by law firms, corporations, banks, government agencies, insurance companies and other organizations to analyze, interpret, summarize and present complex financial and business related issues in a simple and concise manner. Forensic accountant may apply certain examination and evaluation techniques similar to those used in financial audits but the objective of these procedures is quite different.

### **3. Scope of forensic accounting is to:**

1. To find the evidence of unusual development in the accounting and financial systems.
2. To design proper accounting processes for verifying important premises and data and develop skills in identifying possible fraud.
3. Perform audit type processes on a routine schedule in order to reduce transaction processing risks.
4. To cover a broad range of businesses and locations that requires customary or continuous surveillance of all transaction processing systems.

### **4. FORENSIC ACCOUNTING - INDIAN SCENARIO**

Recently, forensic accounting has become an indispensable tool for investigation in India due to rapid increase in corruption and our law enforcement agencies do not have the expertise or time to uncover such stock market fraud or bank fraud or cyber fraud. Scams like Satyam (2009), 2-G Spectrum (2010), Commonwealth games (2010), Railgate scam (2013), Tatra Truck scam (2011) and most recently coal block allocation scam (2012) and Chopper scam (2013) in India had improves the scope for forensic accounting in India. According to the Corruption Perception Index 2016 Report released by Transparency International, India's rank is 79<sup>th</sup> among 176 countries affected with corruption. However, in 2019 their Corruption Perception Index, ranked the country 80th place out of 180, reflecting steady decline.