

# Forensic accounting analysis flashcard



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**FORENSIC ACCOUNTING Abstract** In today's fast growing business world, it is necessary for an organization to evaluate its systems, internal control procedures and to analyze the risks involved to ascertain appropriate implementation and working of its processes. The organization must also identify, record, settle, extract, sort, report and verify past financial data. With increasing number of frauds within organizations, the regulatory framework has also been enhanced with introduction of Corporate Governance, Clause 49, SOX and ISA 240. Companies thus need to use intelligence gathering techniques and accounting / business skills to develop information and opinion on the above due to which Forensic Accounting is gaining more and more importance. Thus Forensic Accounting certainly provides a Value Addition to the business.

This research paper shall discuss the Conceptual Framework which may be followed while dealing with Forensic Audit and the Critical requirements for a successful investigation like Confidentiality, Investigative Expertise, Industry Expertise, Multi Location Considerations, etc. It shall give an insight into the key points that need to be considered while conducting a Forensic Audit like maintaining an attitude of professional skepticism, obtaining information to identify risks, evaluating the entity related controls, designing and performing audit procedures, obtaining written representations from management relating to fraud, communicating with management and the audit committee, etc. It shall also deal with the proposed Fraud Risk Management Strategy along with the Key Areas of Concern like Code of Ethics, Risk Management, Effective Controls and Audit & Fraud Response Plan. **INTRODUCTION:** Forensic Accounting is the use of intelligence

gathering techniques and accounting / business skills to develop information and opinion.

It is the action of identifying, recording, settling, extracting, sorting, reporting and verifying past financial data or other accounting activities. It is basically the use of accounting for legal purposes. BACKGROUND: In February 2002, ASB issued Fraud Exposure Draft. In October 2002 ASB issued SAS 99, Consideration of Fraud in a Financial Statement Audit.

All Big 4 chose to move towards early adoption of new Fraud Auditing Standard (for audits ending after 15 December 2002). Implementation of SAS 99 was made necessary for all organizations seeking an audit opinion under Generally Accepted Auditing Standards (GAAS) as issued by the American Institute of Certified Public Accountants (AICPA). Standards: ? SAS 1 : The auditor has a responsibility to plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error or fraud SAS 99 establishes standards and provides guidance to auditors in fulfilling that responsibility, as it relates to fraud, an audit of financial statements conducted in accordance with generally accepted auditing standards WHAT IS FRAUD? Fraud is an intentional act that results in a material misstatement in the financial statements that are the subject of an audit. . It is generally defined by the courts as an intentional misrepresentation that was properly relied upon by the plaintiff and caused the plaintiff damages. It is a deliberate deceit which is planned and executed to deprive an individual of property, money or any other valuable security.

Fraud must be committed with intent and includes actions of misrepresentations and/or acts of omission. Diagram 1: Fraud and the Fraud Triangle

**MISAPPROPRIATION OF ASSETS:** Misappropriation of assets involves the theft of an entity's assets and is often perpetrated by employees in relatively small and immaterial amounts. Misappropriation of assets can be accomplished in a variety of ways (including embezzling receipts, stealing physical or intangible assets, or causing an entity to pay for goods and services not received); it is often accompanied by false or misleading records or documents in order to conceal the fact that the assets are missing.

**FRAUDULENT FINANCIAL REPORTING:** Fraudulent financial reporting involves intentional misstatements or omissions of amounts or disclosures in financial statements to deceive financial statement users.

Fraudulent financial reporting may involve: Manipulation, falsification (including forgery), or alteration of accounting records or supporting documents from which the financial statements are prepared –

Misrepresentation in, or intentional omission from, the financial statements of events, transactions or other significant information – Intentional misapplication of accounting principles relating to amounts, classification, presentation, or disclosure

Diagram 2: Fraud Characteristics

SAS 99: SAS 99 says “ Fraud is a broad legal concept and auditors do not make legal determinations of whether fraud has occurred”. It categorizes frauds into two types:

- ? Fraudulent financial reporting: Misrepresenting financial information required for management and/or external reporting.
- ? Theft or misappropriation of assets: The embezzlement or misuse of company assets

for personal gain. Other ways in which fraud may be conducted: Internal (e.g. Management, Employees) External (e.

g. Third Parties) Collusive Diagram 3: Schematic representation for enhanced

Regulatory Framework WHAT VALUE ADD DOES FORENSIC ACCOUNTING

PROVIDE? Experience in fraud and misconduct investigations and profiling

fraud and misconduct risk ? Experience in conducting interviews ?

Assessment of regulatory and corporate compliance programs ? Business

ethics, whistle blower policy ? Industry-specific knowledge of occurrence and

indicators of the common frauds ? Higher levels of professional skepticism

CRITICAL REQUIREMENTS FOR SUCCESSFUL INVESTIGATION: ? Confidentiality

? Investigative expertise ? Industry expertise ? Multi-location considerations ?

Execution capabilities Familiarity with court procedures THE KEY POINTS

WHICH NEED TO BE CONSIDERED WHILE CONDUCTING FORENSIC AUDIT: ?

Maintain an attitude of professional skepticism ? Discuss susceptibility to

fraud ? Obtain information to identify risks ? Evaluate the entity related

controls ? Determine overall responses ? Design and perform audit

procedures ? Consider whether identified misstatements are indicative of

fraud ? Obtain written representations from management relating to fraud ?

Communicate with management and the audit committee FRAUD RISK

ASSESSMENT & STRATEGY: It is an innovative service that helps

organizations protect value by effective management of fraud and

misconduct risk. Diagram 4: Fraud Assessment and Strategy Areas of

Concern Tailor Made: ? Designed to fit the precise need ? Ranging from stand

alone workshop through to an in-depth reviews on management of fraud

threat ? Detailed risk assessment, scenario development and sophisticated

data analysis Four Main Phases: ? Planning maximum value ? High level analysis ? In depth analysis ? Reporting and implementation Assessing wider Business Environment: Identify factors in the organisation's business environment that create abnormal levels of risk or seriously undermine current or proposed fraud risk management processes ? Includes culture, ethics, management and reward structure, people profiles, etc Diagram 5: Effective Fraud Risk Management BENEFITS OF USING THIS APPROACH: Quality of Evidence: Effective combination of varied skill sets to bring a higher degree of focus and perspective to the engagement. The team members should have international and cross border experience in conducting investigations.

Skill sets include forensic professionals, IT services professionals, certified fraud examiners, forensic technology specialists, etc In Depth Assessment: ? Fraud risk assessments and investigations ? Liaison with police and other investigation/ regulatory agencies ? Presenting evidence for court purposes CONCLUSION: There is only one thing money cannot buy and that is Integrity. Hence with increasing number of Frauds, it is recommended that the company undertakes extensive Fraud Risk Assessment and Forensic Accounting. REFERENCES: 1. [www. kpmg.](http://www.kpmg.com)

com 2. [www. pwc. com](http://www.pwc.com)