

Forensic Accounting vs Forensic Audit

Accounting analysis that is acceptable for use in judicial proceedings is performed through forensic accounting. Accounting, auditing, and investigative abilities are all used in forensic accounting to look into a person's or company's records. There is still considerable confusion over whether this accounting discipline is called "forensic accounting" or "forensic audit." Even though the global perception of this financial fraud analysis domain is called forensic accounting by various regulatory bodies, the Indian perspective labels any financial examination as an audit.

The article attempts to examine the various definitions by global regulatory bodies of forensic accounting or forensic audit.

Definitions of Forensic Accounting

According to the **Association of Certified Fraud Examiners (ACFE)**, the world's largest anti-fraud organisation, forensic accounting is defined as *"An integration of auditing, accounting, and investigative skills, and presents an accounting evaluation; that is appropriate and acceptable to the court; which will then establish the basis for discourse, debate, and the settlement of arguments."*

It further states, *"A forensic accountant can provide various services, including audits; accountant performance reviews; and examinations of financial documents for fraud, misconduct, or industry-standard violations. Moreover, these experts can mine and analyse large amounts of data to identify potentially irregular transactions and high-risk relationships."*

Bologna and Lindquist (1985) define forensic accounting as *"The application of financial skills, and an investigative mentality to unresolved issues, conducted within the context of rules of evidence. As an emerging discipline, it encompasses financial expertise, fraud knowledge, and a sound knowledge and understanding of business reality and the working of the legal system."*

The forensic accounting terminology has been explained by the **Association of Chartered Certified Accountants (ACCA)** as the application of accounting skills and knowledge to situations with legal implications, the most well-known of which is the investigation of alleged fraudulent activities. The phrase used to characterise this type of engagement also refers to the entire process of conducting a forensic investigation, including writing an expert report or witness account and sometimes testifying as an expert witness in court.

The **AICPA** (1993) defines it as *"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."*

Since forensic assignments are by definition associated with a legal or semi-legal dispute determination, a fundamental understanding of the material statute and legal principles, the law of confirmation, and the law of methodology are required of the forensic expert.

Definitions and/or references to the term; Forensic Audit

The term 'Forensic Audit' is often used interchangeably with the term 'Forensic Accounting.' However, multiple accounting bodies define and differentiate both of these terms.

The ACCA defines forensic audit as *"The application of traditional auditing procedures and techniques in order to gather evidence as part of the forensic investigation."*

The Black's Law Dictionary defines, "*A forensic audit is a process of reviewing a person's or company's financial statements to determine if they are accurate and lawful.*" The legal dictionary further states that forensic audits are utilised when an entity's finances are a legal concern. For example, it is used to investigate alleged embezzlement or fraud, to evaluate tax liabilities, to probe a spouse during divorce processes, and to investigate bribery charges, among other things.

In the Indian context, the ICSI and ICAI refer to a forensic audit as "*an examination of evidence regarding an assertion to determine its correspondence to established criteria carried out in a manner suitable to the court.*"

The ICAI states, "*Forensic Auditing has established itself as a dynamic and strategic tool in combating corruption, financial crimes and frauds through investigations and resolving allegations of fraud and embezzlement.*" Also, the ICAI refers to a forensic auditor as someone who is "*retained to analyse, interpret, summarise and present complex financial and business-related issues in a manner which is both understandable and properly supported.*"

The Concept of Watchdog and Bloodhound

Auditors are intended to be watchdogs and, at most, sniffer dogs, not bloodhounds. The decision in Kingston Cotton Mills Co. (1896) shaped the concept of an auditor's responsibility in terms of detecting and preventing frauds and errors. "*Auditor is a watchdog, not a bloodhound,*" the judge said, summarising the auditor's role. Through discussions with many stakeholders, including the government and investigative agencies such as the Serious Fraud Investigation Office (SFIO) and the Economic Offences Wing, the ICAI has attempted to raise awareness about the difference between audits and investigations.

The ACFE notes in its 2018 Report to the Nations that tip-offs are the most common early detection method for occupational fraud, accounting for 40% of all detections. Internal audit (15%), management review (13%) and "by accident" are the next three categories at 7%. External audit, at 4%, appears to be slightly over half as successful as pure luck.

In light of this, and with organisations globally losing an estimated 5% of their revenue to fraud each year, there is a strong demand for forensic accountants and fraud investigators. Because of the breadth and scope of the global fraud problem, no forensic accountant, regardless of how skilled, can ever guarantee a successful outcome in terms of fraud prevention or detection. The proper utilisation of forensic accounting and investigation knowledge of the situation, on the other hand, increases the possibilities of success. In a world full of watchdogs, a bloodhound is sometimes required. As a result, it is the need of the hour to differentiate and define the forensic accounting domain in order to specify its nature and scope in fraud detection and prevention.

References

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