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Forensic Audit: A Tool for Detection and Prevention of Fraud in the Specific Sector

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ABSTRACT

The press is constantly revealing new financial frauds and scandals. As a result, the accounting profession's traditional methods of monitoring corporate financial activities are being scrutinized. Simultaneously, it is acknowledged that the principles-based GAAP of the International Accounting Standards Board will become the recognized standard in the United States. According to the authors, as investigators adapt accounting techniques into a forensic audit engagement model, these two factors will change the practices used to combat corporate malfeasance.

Internal controls are required to successfully exercise good corporate governance, and financial oversight is one of these controls. Unfortunately, the number of consistent financial frauds committed within US companies raises serious concerns about the effectiveness of traditional financial controls. "Does the traditional audit model continue to play a role in providing financial oversight?" Today's response could be, "not very well, but what other options do you have?" Concerns about the audit-reporting model's ability to provide reasonable financial oversight, as well as broader acceptance of principles-based accounting methods, have the potential to usher in a new approach to risk assurance. According to this paper, forensic auditing, which is based on forensic accounting practices.

It is argued that it is appropriate to consider alternatives, such as forensic audits, to help stakeholders gain confidence in a company's financial risks. This action is especially important as the United States transitions from a GAAP system based on regulations to one based on accounting principles.

Keywords: Forensic accounting, financial fraud control, Internal control quality, financial reporting credibility, Forensic auditing

Introduction

The number of fraudulent and ambiguous financial activities is growing globally. As a result, companies are more vulnerable to fraud. Recent corporate accounting scandals at Parmalat, Xerox Corporation, and Satyam Computer Services, as well as high-profile corporate frauds at Enron, WorldCom, and HealthSouth, followed by Bernie Madoff's massive ponzi scheme, have transformed Forensic Accounting and Forensic Auditing into a thriving industry.

"Forensic" means "suitable for use in the court of law". It is the application of financial skills and an investigative mindset to unresolved issues while adhering to the rules of evidence, according to Bologna. As a developing discipline, it necessitates financial expertise, knowledge of fraud, and a solid knowledge and understanding of business reality and the operation of the legal system.

A survey was conducted, and data from public sector organizations were gathered. The credibility of forensic accounting and financial reporting contributes to the effectiveness of forensic auditing. Controlling corruption and fraud would improve the performance of publicly owned entities in the long run. As a result, this study provides important insights for practitioners developing anti-corruption and anti-fraud strategies.

Fraudulent activities in government organizations have a significant impact on organizational performance. Every year, fraud and corruption cost businesses and economies hundreds of billions of dollars, and they have the potential to harm an organization's reputation. Fraud and corruption are prevalent in both private and public organizations; however, these activities are more dangerous in the public sector. The situation in Pakistan's public sector is particularly dire. The primary causes of poor public-sector business performance are corruption and fraud.

In the current decade, corporate/white-collar crime scandals have slowed the pace of economic growth, as well as caused the collapse of some of the world's most well-known and large-scale companies, including WorldCom, Enron, Tyco-mart Corp, and Global Crossing, as well as wiping out billions of dollars in shareholder value and eroding investor and public confidence in financial markets. Since Edwin Sutherland coined the term "white-collar crime" in 1940, it has been frequently used to depict meticulous types of offence in various scholarly works and textbooks on the subject. According to Enterprise Surveys 2015, the extent and severity of white-collar crime in developing countries, particularly in Pakistan, has reached an all-time high.

Research Problems

According to Williams (2002), forensic accounting is recognized as a distinct type of professional expertise with distinguishing characteristics such as rationality, neutrality, and independence. Forensic accountants have a unique social recognition, which is critical in translating economic issues into symbolic displays of trust. The symbolic capacity through which the translation is realized is the critical social value that forensic accountants possess.

Forensic accounting serves as a cultural link between economic and political logics (Williams, 2002). These events precipitated and exacerbated the Great Recession, and they had a significant impact on the efficient operation of free market capitalism. Some of which were made possible by public accountants (cf. Enron and Arthur Andersen). The scandals, frauds, and failures have eroded financial statement users' trust in public accounting's ability to provide viable solutions to financial problems, fueling the rise in demand for forensic accountants.

In reality, very little has been written in this field. Based on the problem stated above, this research focuses on the impact of forensic accounting on fraud detection.

Forensic Accounting and Financial Fraud

Fraud is a legal term that refers to the intentional misrepresentation of the truth in order to manipulate or deceive a company or individual. Senior management may be involved in fraud when a company experiences severe financial difficulties and declares bankruptcy. Accounting fraud may be used by company executives to recover losses or meet earnings expectations from shareholders or the general public. The forensic accounting specialization combines accounting, auditing, and investigative skills (Crumbley, 2008). Forensic accountants are expert auditors, accountants, and investigators of legal and financial records hired to examine probable allegations of fraud within a corporation; or engaged by a firm to simply prevent fraud from occurring (McKittrick, 2009).

Though forensic accounting is not yet extensively employed in Nigeria, the recent wave of financial irregularities in Nigeria, notably in the banking sector, has underlined the necessity for the employment of forensic accounting techniques. Sanusi (2010) delivered a presentation on the current situation of various banks' operations, revealing some of the institutions' hidden secrets. After it was shown that five big banks had largely degraded their shareholders' capital and almost broke all banking ratios, they were deemed technically insolvent and chronically illiquid. The Central Bank of Nigeria (CBN) issued a list of debtors, which includes corporations and their directors that received loans worth N747 billion from the impacted banks.

Surprisingly, Price Waterhouse Coopers and Akintola Williams Delliote are the auditors for the five struggling institutions. Aside from problems concerning the specifics of company governance, concerns were raised about their accountant's competence and honesty. Prior to the CBN's announcement of its findings on the five banks' conditions and operations in the EDW, their auditors were unable to adequately evaluate and bring to light the real situation of these reports, including their loans portfolio, which the CBN currently estimates to be worth N2.8 trillion. Almost all of the defects and challenges found in Nigeria's post-consolidation banking sector, as well as the ensuing criminal investigations and prosecutions, are forensic accounting issues.

Furthermore, bringing the concerns to court and requiring expert witness would be highly costly. As a result, to avoid the high expenses and the danger of unfavorable publicity on their corporate image, most corporations choose to resolve the disagreement outside of court. (vii) Forensic accounting is a recent phenomenon, especially in developing countries. As a result, accountants with sufficient technical expertise of forensic issues are in short supply.

Research Questions:

The study is expected to answer the following questions:

1) To what extent does forensic accounting influence fraud detection?

2) To what extent does forensic accounting prevent fraudulent activities in a company?

Research Objectives:

The main objective of the study is to examine the impact of forensic accounting on fraud detection. The specific objectives are to:

1) Determine how forensic accounting affects fraud detection.

2) Determine whether forensic accounting will reduce fraudulent activity.

Hypothesis:

The following hypothesis will be tested:

Forensic accounting has no effect on fraud detection.

H02: Forensic accounting cannot prevent fraudulent behavior.

Fraud Detection:

Both defining and recognizing fraud are challenging tasks. As a general rule, it is impossible to define fraud since it encompasses all unexpected, sneaky, devious, and unjust methods that someone might be taken advantage of. The deliberate misrepresenting of the facts in order to influence or defraud a company or a person is referred to as fraud in law. Fraud is when someone is persuaded to enter into a contract by using false information. It involves surreptitiously decreasing an asset's value or worth in order to profit oneself on purpose. Senior management may be complicit in the deception when a firm experiences serious financial issues and files for bankruptcy.

The definition of fraud is equally as challenging as the detection of it. Since fraud encompasses all unexpected, sneaky, crafty, and unjust methods that someone is taken advantage of, there is no clear-cut norm that can be established as a general principle. In order to mislead or fool a corporation or an individual, it is permissible to intentionally distort the facts. This practice is known as fraud. Fraud is when someone is persuaded to enter into a contract by using false information or maintaining a false impression. It comprises surreptitiously decreasing an asset's value or worth in order to purposely profit oneself. Senior management could be complicit in the deception when a business experiences serious financial problems and files for bankruptcy. This issue needs special attention for fraud protection since the business might have a big influence on the opportunity factor. The establishment of defensive mechanisms by the fraudster to support their conduct is the third element of the fraud triangle. Some of the explanations and justifications used by the fraudsters include: (a) I borrowed the money and would pay it back; (b) this is in compensation for my work on behalf of the business; (c) No one has been harmed as a result of this; and (d) I took the money for a worthy cause. Businesses should teach ethical principles to employees and warn them that fraudsters will surely suffer repercussions in order to combat these reasons.

Additionally, fraud must be discovered before it can be eradicated, regardless of its appearance or method of concealment. The best group to conduct the duty of identifying fraud on their own is not necessarily the auditors. By implementing suitable fraud prevention procedures inside its business, the corporation may identify and stop non-management fraud. A rising number of studies look into the elements, such strong CEO incentives and a flimsy board structure, that entice firms to commit fraud. On the other hand, companies with the biggest defense contracts had lower negative anomalous returns than those with lesser contracts.

Forensic Accounting and Fraud Detection

Ramaswamy (2005) claims that inadequate company governance and accounting failure are two reasons why fraud cases occur. This is so that one individual or a group of persons with similar interests may take advantage of it and engage in fraudulent activities within the corporation due to inadequate corporate governance. He also asserts that a lack of properly executed corporate governance standards is to blame for issues with the corporate reporting system. Top-level management following corporate policies can reinforce this and improve business performance. The problem is caused by the disinterest of some corporate executives in the policies.

Although it is understandable that an auditor does not have a legal obligation to find fraud, they should nonetheless report information fairly and accurately to safeguard the interests of the general public and their staff. By adhering to forensic accounting rules, auditors can take on the role of forensic accountants in situations when fraud or criminal conduct in a business is suspected. According to the author, a subpar management system cannot be improved by an ineffective and inefficient internal control system.

Management will continue to have the largest influence over implementation even if a business installs effective internal control mechanism. Since forensic accounting may be the next best choice for addressing issues, businesses should think about new strategies rather than keeping with the existing quo.

In response to the Sarbanes-Oxley Act of 2002, more businesses are initiating new anti-fraud efforts and programmed, reporting more recent fraud incidences than in prior years, and implementing anti-fraud measures. (KPMG 2003). In 50 nations, 37% of respondents to PricewaterhouseCoopers' (PWC) 2003 Global Crime Survey reported serious economic crimes, with an average loss per firm of $2,199, 930. (PWC 2003). These survey results demonstrate the value of forensic accounting training and practice.

The US General Accounting Office (GAO) (1996) asserts that fraud detection and prevention are now given top priority during statutory audits. In reality, the United States and other countries that set standards have strengthened the obligation on auditors to take fraud risk into account while doing financial statement audits. Even higher forensic abilities are required of people who carry out these audits, according to others. Enyi (2009) agrees, contending that all regular statutory audits should incorporate certain aspects of forensic inquiry since it is simple to find evidence of fraudulent actions if the effectiveness and compliance of the internal control system are carefully examined. All of them are meant to stop and catch fraud.

However, an auditor might be unable to do this without some familiarity with forensic accounting techniques (Efiong, 2012). According to KPMG's Fraud Survey (2003), more businesses are establishing new anti-fraud efforts and programmed in response to the Sarbanes-Oxley Act of 2002, experiencing fraud occurrences more recently than in prior years, and implementing anti-fraud measures. (KPMG 2003). In 50 nations, 37% of respondents to PricewaterhouseCoopers' (PWC) 2003 Global Crime Survey reported serious economic crimes, with an average loss per firm of $2,199, 930. (PWC 2003). The results of this poll demonstrate the value of forensic accounting practice and instruction.

Methodology

The purpose of the current study is to address this topic and ascertain if fraud detection and forensic accounting are related. In order to get enough primary data for this study, the survey approach was employed. Chi-square statistical software and OLS regression analysis are used to evaluate the data, and the findings are utilized to confirm or refute the hypothesis. The conclusions will be discussed in light of the findings.

Summary of Findings

It is useless for publicly listed firms in Nigeria to utilize forensic accounting services to fight fraud. Forensic accounting services are not effectively used by business entities in Nigeria, which has major consequences for good corporate governance. As most anti-corruption activists predicted at the beginning of the 2000, the introduction of e-business and its growing complexity hasn't done much to lessen unethical behaviors in Nigeria. In an effort to stampede the monster, policymakers from all over the world have established regulations, some of which have taken the shape of legislation. However, nothing seems to be working.

Conclusion and Recommendation

Based on this discovery, the article draws the conclusion that forensic accounting services give businesses the resources they need to thwart fraud but do not actually stop it. Introduce and modify forensic accounting as a financial tactic to fight economic and financial crime in order to reduce the gap:

• Forensic Accounting will provide litigation support services in the law courts, as well as appropriate professional services. They are able to access the system of the company and go through the books legally.

• Economic and financial crime have damaged Nigeria's reputation abroad and deterred foreign direct investment. Development, employment, and peoples' standards of life are all impacted by this.

• The profession of forensic accounting developed from the identification and prevention of corruption. The eradication of economic and financial crime in the system via the application of forensic accounting would enhance the reputation of the businesses under evaluation. Therefore, the most crucial action that businesses should take in regards to fraud is to stop the crime from happening.

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