

Forensic Accounting as a Tool for Detecting Fraud and Corruption: An Empirical Study in Bangladesh

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Abstract

Today forensic accounting is a highly talked about topic all over the world and is the fastest growing area of accounting. This paper examines the present status of application of forensic accounting in Bangladesh and recommends steps that should be taken for the enhancement of the utilization of forensic accounting as an effective tool for combating fraud and corruption in Bangladesh. In this study 100 sample size has been taken to reflect the actual scenario regarding the application of forensic accounting in Bangladesh.

Key words: Forensic accounting, corruption, fraud, corporate scandals.

Introduction

“What the use of finger prints was to the 19th century and DNA analysis was to the 20th, forensic accounting will be to the 21st century,” said Gordon Brown, former Chancellor of the Exchequer. The number of fraudulent activities and dubious financial activities has been increasing all over the world. Consequently, businesses are exposed to new risks of fraudulent activities. In such a context, the market for forensic accounting continues to grow especially in the backdrop of the recent rash of corporate scandals, corporate collapses, and business failures. In fact these have prompted business houses to hire forensic accountants to discover through investigation, various types of wrongdoing in one hand and prevent such occurrence on the other. Forensic accounting has established itself as dynamic and strategic tool in combating corruption, crime and frauds through investigations and resolving allegations of frauds and embezzlements. It is fact that recently corporate world is taking more measures to combat fraud and launching new antifraud initiatives and programs by appointing forensic accountant in response to the Sarbanes – Oxley Act of 2002 than to prior years specially because of the occurrence of strong shocking corporate scandals such as Enron (2001), Sunbeams (2001), Dynegy(2002), WorldCom,(2002), Adelphia (2002), etc.

The present study will reveal the current scenario of forensic accounting in Bangladesh and how much it is being introduced and recognized to the professional accountants, Multinational Corporation as well as local organizations and used as a fraud detection tool.

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Objectives of the Study

The main thrust of this study has concentrated on the issues relevant to the current status of the application of forensic accounting in Bangladesh and how efficiently it works as a fraud detection tool. However, the specific objectives of this study are as follows:

- To evaluate the role of forensic accounting for deterring fraud in Bangladesh.
- To recommend some steps to develop forensic accounting practice in Bangladesh.

Methodology of the study

In order to achieve the objectives of the study both primary data and secondary data have been used. To collect primary data a random sample of 35 professional chartered accountants and cost and management accountants, 15 multinational corporations, and 50 local organizations has been chosen for participation in this study. They had filled the questionnaires with 9 questions related to the area of this research. In case of multinational corporations and local organizations the contacted persons were usually chief accountants or executives in account department of the respective organizations. The collected data have been processed manually and report in the present form has been prepared in order to make the study more informative, analytical, and useful for the users. Besides, related books, journals and web sites were also reviewed to prepare this paper.

Literature Review

With the growing complexity of the business environment, fraud, and the growing number of business related investigations, forensic accounting is increasingly used as fraud detection tool in the investigation of financial and business related fraud. Maurice E. Peloubet was probably the first person to coin the phrase “forensic accounting” in 1946. He was a partner in the public accounting firm of Pogson, Peloubet & Co in New York. Peloubet stated that “during the war both the public accountant and industrial accountant have been and are now engaged in the practice of forensic accounting”(Oberholzer,2002). Following the globalization of business in the early 1900s and after the American Stock Market Crash of 1929, auditors shifted their focus from fraud detection to public financial statement reporting. That created an expectation gap between auditors and the users of financial statements, who still viewed auditors as the first line of defence against fraud(Reason,2001).

A forensic accountant can be defined as “someone who is applying financial skills and an investigative mentality to unresolved issues, conducted within the context of the rules of evidence. It encompasses financial expertise, knowledge of fraud and a strong knowledge and understanding of business reality and the working of the legal system”(Thornhill, 1995). 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 (Anwar and Uddin, 2008).

Madan Lal Bhasin finds in his article "Forensic Accounting and Auditing – Perspectives and Prospects" that the services of forensic accountants are in great demand in the areas which include criminal investigation; settlement of outgoing partner; settlement of insurance claims; detection of employee fraud and case relating to professional negligence. The author quotes from William Messier: "A forensic audit's purpose is the detection or deterrence of a wide variety of fraudulent activities."

In the article "Forensic Accounting in Indian Banks", *T R Shastri* observes that while incidence of frauds, detection of frauds and the investigations before and after have been there in India for decades, there is no standardized approach to these investigations. The profession of forensic accountancy has not been recognized as such either in banks or in the financial services industry. The author provides a live example of forensic accounting in banks in India to illustrate how a forensic report formed the basis for handling a case of fraud in a private sector bank.

In 2008, Institute of Chartered Accountants of Bangladesh (ICAB) organized a seminar on "Forensic Accounting – A Dynamic Tool for Combating Corruption in Bangladesh". While speaking in the seminar as Chief Guest Professor Muzaffar Ahmad said, "Corruption poses to destroy the moral of our society and is the number one problem of the country. The threat of corruption in Bangladesh has increased manifold in different segments of government offices and the private sector as well, in wider and alarming scale. To salvage the country from such a deplorable state of affairs, the role of a forensic accountant is extremely important commented. There is an unholy alliance among the corrupt elements of the country, which can be dismantled at least partially, if not fully with the help and assistance of the forensic accountants" (Financial Express, 2008).

Core Concept and Definition of Forensic Accounting

The integration of accounting, auditing and investigative skills yields the speciality known as Forensic Accounting. "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 *Oxford Advanced Learner's Dictionary* explains the word 'forensic' in the following way: "it is used before noun and is connected with scientific tests used by the police when trying to solve a crime." This Dictionary uses the word, 'forensic' with nouns like 'evidence', 'medicine', 'science', 'tests' etc., citing the instances of its usage in the ways like 'the forensic laboratory' and 'a forensic pathologist'. Bologna and Lindquist (1995) in "Fraud Auditing and Forensic Accounting" defined forensic accounting as "the application of financial skills, and an investigative mentality to unresolved issues, conducted within the context of rules of evidence. As a discipline, it encompasses financial expertise, fraud knowledge and a sound knowledge and understanding of business reality and the working of the legal system."

D. Larry Crumbley, Chief Editor of "Journal of Forensic Accounting" and a renowned forensic accountant stated that forensic accounting covers two broad areas: litigation support and investigative accounting. He also Pointed out that forensic accounting is accounting that is suitable for legal review, offering the highest level of assurance, and including the now generally accepted connotation of having been arrived at in a scientific fashion.

Thus, forensic accounting can be defined as the accounting analysis that can uncover possible fraud, which is suitable for presentation in court. Such analysis will form the basis for discussion, debate and dispute resolution. 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.

Typical approach to a Forensic Accounting Assignment

The task of each forensic accounting is unique and different from each other according to nature and status. Accordingly, the actual approach adopted and the procedures performed will be specific to it. However, many Forensic Accounting assignments will include the following steps in general:

Meet with the client: The first step in this typical approach to go through an assignment is to meet with the relevant objects. It is helpful to meet with the client to obtain an understanding of the important facts, players and issues at hand.

Perform a conflict check: Now in this step the concerned forensic accountant critically observe the whole matters. Then a conflict check should be carried out as soon as the relevant parties are established.

Perform an initial investigation: It is often useful to carry out a preliminary investigation prior to the development of a detailed plan of action. This will allow subsequent planning to be based upon a more complete understanding of the issues.

Develop an action plan: This plan will take into account the knowledge gained by meeting with the client and carrying out the initial investigation and will set out the objectives to be achieved and the methodology to be utilized to accomplish them.

Obtain the relevant evidence: Depending on the nature of the case this may involve locating documents, economic information, assets, a person or company, another expert or proof of the occurrence of an event.

Perform the analysis: The actual analysis performed will be dependent upon the nature of the assignment and may involve:

- Calculating economic damages;
- Summarizing a large number of transactions;
- Performing a tracing of assets;
- Performing present value calculations utilizing appropriate discount rates;
- Performing a regression or sensitivity analysis;
- Utilizing a computerized application such as a spread sheet, data base or computer model; and
- Utilizing charts and graphics to explain the analysis.

Prepare the report: Often a report will be prepared which may include sections on the nature of the assignment, scope of the investigation, approach utilized, limitations of scope and findings and/or opinions. The report will include schedules and graphics necessary to properly support and explain the findings.

Data Analysis and Interpretation

For the purpose of analysis, the collected data have been tabulated in eight tables using percentages to show the results of analysis of experts' views. The analysis based on expert opinion survey was aimed at examining whether the experts' views agreed with, or differed from, the information based on literature survey. The table below shows the sample size.

Respondent Groups	Sample Size
Chartered Accountants (CA) and Cost & Management Accountants (CMA)	35
Multinational Corporations	15
Local Organizations	50
Total	100

The study adopted simple random sampling technique to draw the samples from the three groups of respondents as shown in the above table. The overall study sample size is 100. Primary data have been collected by administering a brief questionnaire consisting of only nine questions related to a few relevant issues of forensic accounting for respective three groups. Almost all the questions were in structured form, i.e., in closed form. Each of the respondents filled in the questionnaire as it was administered.

In questionnaire the issues addressed are:

- (1) Whether forensic accounting is known to them,
- (2) Whether forensic accounting has been used in practice to investigate fraudulent/ dishonest acts in that respective organization of Bangladesh,
- (3) Whether forensic accounting is used as a fraud detection tool.
- (4) Whether forensic accounting has impact on Internal Control Systems.
- (5) Whether forensic accounting has impact on External Audit.
- (6) Whether Forensic Accounting is solely enough as a tool to detect suspicious or fraudulent transactions.
- (7) Whether risk assessment process under forensic accounting specifically cover risk of fraud
- (8) Whether they have any pressure to practice Forensic Accounting in your organization

The issues and respondents' opinions are analyzed in the following tables:

Table 1: Responses as to whether they know about forensic accounting

Respondent	Chartered Accountants, Cost and Management Accountants (CMA)	Multinational Corporation	Local Organization	Total
Responses	<i>f</i> (percent)	<i>f</i> (percent)	<i>f</i> (percent)	
Yes	33 (94.29%)	11 (73.33%)	4 (8%)	48 (48%)
No	2 (5.71%)	4 (26.67%)	46 (92%)	52 (52%)
Total	35 (100%)	15 (100%)	50 (100%)	100 (100%)

Note: *f* stands for frequency.

Table 1 shows that a substantial majority of chartered accountants and CMA (94.29% percent), multinational corporation (73.33%) and local organization (8%) that is, overall 49 percent of all the respondents have knowledge about forensic accounting, while only 5.71percent of Chartered Accountants (CA) and Cost and Management Accountants (CMA), 26.67% of Multinational Corporation and 92% of Local Organization have no idea about forensic accounting .It is, therefore, clear that forensic accounting is new on an average to the people.

Table 2: Whether forensic accounting has been used in practice to investigate fraudulent/ dishonest acts in their organization

Respondent	Chartered Accountants, Cost and Management Accountants (CMA)	Multinational Corporation	Local Organization	Total
Responses	<i>f</i> (percent)	<i>f</i> (percent)	<i>f</i> (percent)	
Yes	27 (77.14%)	6 (40%)	1 (2%)	34 (34%)
No	8 (22.86%)	9 (60%)	49 (98%)	66 (66%)
Don't know	-----	-----	-----	-----
Total	35 (100%)	15 (100%)	50 (100%)	100 (100%)

It is evident from table 2 that an overwhelming majority of 'Chartered Accountants' and 'Cost and Management Accountants' (77.14 percent) and 40 percent of Multinational Corporation use forensic accounting to investigate fraudulent/ dishonest acts in their organization. In this respect, only a small proportion of Local Organization (2 percent) use forensic accounting.

Table 3: Whether forensic accounting is used as a fraud detection tool

Respondent	Chartered Accountants, Cost and Management Accountants (CMA)	Multinational Corporation	Local Organization	Total
Responses	<i>f</i> (percent)	<i>f</i> (percent)	<i>f</i> (percent)	
Yes	33 (94.29%)	11 (73.33%)	4 (8%)	48 (48%)
No	-----	-----	-----	-----
Don't know	2 (5.71%)	4 (26.67%)	46 (92%)	52(52%)
Total	35 (100%)	15 (100%)	50 (100%)	100 (100%)

Table 3 shows that quite majority of Chartered Accountants (94.29 percent), Multinational Corporation (73.33percent), and only 8 percent of local organizations think that forensic accounting is strongly used as a fraud detection tool. Those people who have no idea about forensic accounting, they only marked 'Don't know'. But there were no opposite opinions about forensic accounting as fraud detection tool. So undoubtedly we can say forensic accounting is a strong fraud detection tool.

Table 4: Whether forensic accounting has impact on Internal Control Systems

Respondent	Chartered Accountants, Cost and Management Accountants (CMA)	Multinational Corporation	Local Organization	Total
Responses	<i>f</i> (percent)	<i>f</i> (percent)	<i>f</i> (percent)	
Yes	30 (85.71%)	11 (73.33%)	4 (8%)	45 (45%)
No	3(8.57%)	-----	-----	3(3%)
Don't know	-----	4 (26.67%)	46 (92%)	50(50%)
Don't think	2 (5.71%)	-----	-----	2(2%)
Total	35 (100%)	15 (100%)	50 (100%)	100 (100%)

Table 4 shows that greater part of Chartered Accountants (85.71 percent) and Multinational Corporation (73.33 percent) think that forensic accounting has significant impact on internal control system. And the other greater portion of local organization didn't make any comment because they have no sound knowledge about forensic accounting.

Table 5: Whether forensic accounting has impact on External Audit

Respondent	Chartered Accountants, Cost and Management Accountants (CMA)	Multinational Corporation	Local Organization	
Responses	<i>f</i> (percent)	<i>f</i> (percent)	<i>f</i> (percent)	Total
Yes	32 (91.43%)	10(66.67%)	4 (8%)	46(46%)
No	1(2.86%)	1(6.67%)	6(12%)	8(8%)
Don't know	----	4 (26.67%)	40 (80%)	44(44%)
Don't think	2 (5.71%)	-----	-----	2(2%)
Total	35 (100%)	15 (100%)	50 (100%)	100 (100%)

Table 5 shows that 46 percent out of 100 samples believe external audit is influenced greatly by forensic accounting and only 8 percent don't believe that.

Table 6: Whether Forensic Accounting is solely enough as a tool to detect suspicious or fraudulent transactions.

Respondent	Chartered Accountants, Cost and Management Accountants (CMA)	Multinational Corporation	Local Organization	
Responses	<i>f</i> (percent)	<i>f</i> (percent)	<i>f</i> (percent)	Total
Yes	23 (65.71%)	7(46.67%)	2 (4%)	32(32%)
No	5(14.29%)	2(13.33%)	1(2%)	8(8%)
Others	7(20%)	4(26.67%)	1(2%)	12(12%)
Don't know	-----	2(13.33%)	46(92%)	48(48%)
Total	35 (100%)	15 (100%)	50 (100%)	100 (100%)

Table 6 shows that Chartered Accountants, Cost and Management Accountants (65.71%); Multinational Corporation (46.67%) and only 4 percent of Local Organization think that Forensic Accounting is solely enough as a tool to detect suspicious or fraudulent transactions. In opposite side of coin only 8 percent out of 100 didn't believe that. Twelve percent believe moderately and they tried to show something more besides forensic accounting. They think only forensic accounting is not solely sufficient. There should be additional skill and knowledge to find out clueless and most hidden fraud.

Table 7: Whether risk assessment process under forensic accounting specifically cover risk of fraud.

Respondent	Chartered Accountants, Cost and Management Accountants (CMA)	Multinational Corporation	Local Organization	
Responses	<i>f</i> (percent)	<i>f</i> (percent)	<i>f</i> (percent)	Total
Yes	13 (37.14%)	5(33.33%)	1(2%)	19(19%)
No	5(14.29%)	2(13.33%)	2 (4%)	9(9%)
Occasionally	7(20%)	2(13.33%)	1(2%)	10(10%)
Others	10(28.57%)	4(26.67%)	-----	14(14%)
Don't know	-----	2(13.33%)	46(92%)	48(48%)
Total	35 (100%)	15 (100%)	50 (100%)	100 (100%)

Table 7 shows that Chartered Accountants, Cost and Management Accountants (37.14%); Multinational Corporation (33.33%) and only two percent (2%) of Local Organization think that risk assessment processes under forensic accounting specifically cover risk of fraud. Ten percent (10%) respondent out of 100 samples think forensic accounting couldn't cover risk fully. Others fourteen percent (14%) said other variables and situation involved in the particular incidences to cover risk of fraud by the risk assessment process under forensic accounting.

Table 8: Whether they have any pressure to practice Forensic Accounting in your organization

Respondent	Chartered Accountants, Cost and Management Accountants (CMA)	Multinational Corporation	Local Organization	Total
Responses	<i>f</i> (percent)	<i>f</i> (percent)	<i>f</i> (percent)	
Yes	-----	11(73.33%)	-----	11(11%)
No	35(100%)	2(13.33%)	39(78%)	76(76%)
Don't know	-----	2(13.33%)	11(22%)	13(13%)
Total	35 (100%)	15 (100%)	50 (100%)	100 (100%)

It is evident from table 9 that a relatively majority of Multinational Corporation's management (73.33 percent) together agreed that they have corporate pressure to do forensic investigation to dig out while a fraud or fraudulent activities occurred. But professional accountants have no pressure regarding these. I've got a point while I took face-to-face interview. They are not pressurized but they usually do some activities, which were eventually termed as forensic accounting or investigation whatever was used.

Recommendations and Conclusion

It is clear from the foregoing discussion that forensic accounting is the application of a specialized knowledge and specific skills to stumble upon the evidence of economic transactions. Forensic accounting practice is more in developed countries like the UK, the USA, Canada and Australia. The practice and development of forensic accounting are relatively very much lower in developing countries like Bangladesh than those in developed countries. The result that emerges from the analysis of expert views is that formally forensic accounting has not long been in practice in Bangladesh except in a very few multinational corporations.

The research also revealed that forensic accounting as a fraud detection tool has relevance to efforts for combating fraud and corruption in Bangladesh. It is true that in Bangladesh there are no effective tools to measure, detect and prevent fraud and corruption. In such a context forensic accounting now appears as a one of the strategic and dynamic tool for the management of all types of corruption.

In a country like Bangladesh where the unethical aspects of creative accounting are rampant, the practice of forensic accounting (i.e., investigative accounting done by forensic accounting consultants to solve problems in courts) needs to be introduced and recognized. Besides this, it can also be recommended that some courses, related to this issue should be launched by public and private institutions to make the accounting students expert for detecting fraud and corruption. Some workshops, seminars, and symposium can be arranged to make people in corporate sector more familiar with this issue.

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