

THEORETICAL DEFINING OF FORENSIC ACCOUNTING AND FORENSIC AUDIT AS NEW DISCIPLINES IN THE MODERN WORLD

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Abstract: *Globalization of the markets, economic pressures of the surrounding, and development of technology obstruct the world in its dealing with the new forms of fraud, embezzlement and deception. Accounting and audit cannot deal with such offence. Thus, the need to show a new method of acting and discovering crime, fraud, and all unlawful actions in economy matters appeared.*

This paper aims to analyze the history and the theoretical conditions for forensic accounting and forensic audit. In this sense, there is no a standardized definition of these terms. Some scientific papers say that the beginnings were in Spain and other that they were in Scotland at the end of the 19th century.

If we analyze the phenomenon of the two concepts, we can extract the definition of both terms using historical and logical method. Facing the biggest world frauds such as Enron in the United States or Parmalat as the largest European fraud, we can deduce the need for forensic accounting and auditing.

Through the analysis, we come to the possibility of defining the responsibilities of forensic accounting and forensic audit. As a conclusion, it appears that besides the respect of the highest international accounting rules, there is the need of a secular institution that conducts training and has its agencies worldwide.

Keywords: accounting, auditing, forensic accounting, forensic audit, fraud.

1. INTRODUCTION

Looking back into history, we can say that frauds are as old as the human race. The issues of frauds and penance were pointed out even in the Code of Hammurabi, the well-preserved Babylonian Law (1800 BC). In Greek mythology, the symbol of frauds, stealth, lies and thefts is the God Hermes, the son of Zeus. The first known case of engaging an independent accounting expert to investigate the entrepreneurial books and confirmed irregularities dates from 1721. Charles Snell, after the audit of the entrepreneurial books of the “South Sea Company” related to the scandal with the stocks, named “South Sea Bubble”, submitted a report in which he described the “corruption between the managers of the company and the power structures” [1]. Frauds are defined by the International audit standard 240 on the responsibilities of the auditor related to frauds in the audit of financial reports (International audit standards, further; IAS 240). In accordance with the decisions from point 4 of the IAS 240, fraud implies to intentional actions for acquiring

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unjust and illegal advantage by cheating, performed by one or more members of the management, members of the supervisory board, other employees, or a third party. The financial crisis of 2008, the development of the global economy, the international markets, the development of financial instruments, as well as the need to be in the first place in the competition of the global markets by higher incomes, through the improper corporative working, etc. have all brought up to vulnerability of the global economy from the aspect of frauds, corruption, and abuse. Frauds or abuse are clearly recognized in the financial reports, regardless of whether we are talking about fictional incomes, false financial paperwork, capitalization of the expenses, abuse of the accounting standards, concealment of the facts, intentional omissions in the presentation of the transactions, violation of the fiduciary duties, etc. All types of fraud are done in the financial reports. The question here is: who can discover the fraud? Accountancy documents and accountancy reports are the main evidence of the property and the financial state, and the business and entrepreneurial pecuniary successfulness of the economic subject [2]. The auditors of the financial reports express their opinion on whether the financial reports of the clients are truthful and fairly presented in all financially significant aspects. The audit of the financial report is an insufficient protection from abuse of the creative accounting.

2. METHODOLOGY

Methodologically, through the solving of the logical problem and through the historical method, in this paper we will make an effort to define forensic audit and accounting. Using these two methods, we will come to the definition of the both concepts. Analyzing all definitions elaborating these two sciences and observing the logical structure and the literature which we have on disposal, we should give the definition of the forensic accounting and forensic audit. Traditionally, forensic economists have referred to the application of economics to the detection and quantification of harm from behavior that has become the subject of litigation, and has been practiced by experts who are paid by the court or one of the parties. [3]

Forensic accounting as a concept was mentioned for the first time in 1824 in Glasgow, Scotland, and its implementation in practice has been especially present in the recent years. [4] So, it is not a new concept. Although its roots were traced far back, it remained relatively unknown until the plethora of high-profile corporate scandals and stricter reporting and internal control regulations which brought to light its importance to the business world. [5] The name Forensic Accounting was not even coined until 1946 implying that this specialty career path was not especially common. Even the first forensic accounting book did not come out until 1982 ("Introduction to Forensic" 2011). The popularity and need for the services forensic accountants provide has steadily and more rapidly grown in the past few decades. [6] Forensic accounting can, therefore, be defined as accounting that is used in a court of law, including, but not limited to the application of accounting theory, principles, and calculations to actual or to hypothetical issues in legal proceedings. The term is broad enough to include the many procedures that an accountant or auditor applies in a fraud investigation. Webster's Dictionary defines forensic as "belonging to, used in, or suitable to courts of judicature or public discussion and debate". [7] The AICPA Forensic and Litigation Services Committee (2006, 2) in its report on Forensic Procedures and Specialists articulated, "forensic accounting services

generally involve the application of special skills in accounting, auditing, finance, quantitative methods, certain areas of the law and research, and investigative skills to collect, analyze, and evaluate evidential matter and to interpret and communicate findings, and may involve either an attest or consulting engagement.” Bologna and Lindquist (1995) for forensic accounting is “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.” According to the financial dictionary, forensic accounting integrates an understanding of accounting principles with investigative techniques to determine whether the actions behind financial records and statements are suspicious. This process consists of many steps such as identifying, recording, settling, extracting, sorting and reporting exceptions, oddities, irregularities and suspicious transactions, and verifying digital financial data and other accounting activities, with the purpose of making a firm evidence for legal processes. [8]

Traditional auditing has its focus on error identification and prevention (Gray, 2008). In the regular financial auditing process, the focus is on a sample of transactions, accuracy and reliability of the financial statements, and making remarks in the auditing report in case of deviation, error, unusual exaggeration, etc. [9] Forensic auditing according for Tommie W. Singleton represents “a specialized approach and methodology for detecting of fraud or an audit by which proofs on fraud are gathered, i.e. an entire investigation of frauds which includes revision of the accounting records in direction of proving or denying a suspicion of existence of fraud”. [10] According to Rezaee, forensic audit is: “(1) consulting services for support of legal procedures, (2) testifying in court, (3) investigation of fraud”. [11] Forensic audit “implies to a contract with the auditing company and an auditor who completed a special training and experience in the prevention and detection of criminal activities”. [12]

Taking into consideration the big number of definitions, forensic audit can be defined as a special department for auditing of the revised financial reports by application of the financial standards and the auditing skills and detailed auditing procedures, with the unique aim of detecting of the criminal activities and presenting them in a way acceptable to the court procedure. [13] The difference between the regular audit and the forensic audit is that the regular audit aims to prevent, to detect the action, whereas forensics aims to investigate, solve, and at the end to bring to the court the perpetrator. [14]

3. RESULTS

According to the analysis of the literature, mutual features of all definitions of forensic accounting are:

- Providing of evidence (physical, documented, interviews)
- Forensic accountant as a person with special skills or knowledge in economy, transactions and finance (accounting)
- Litigation support
- Investigative aspect

Mutual features of all definitions on forensic audit are:

- Detecting fraud
- Supporting legal procedures or litigation support
- Estimation of the degree of risk from the stated irregularities (intentional, unintentional, high or low level of irregularities, high or low risk of conducting frauds, etc.)
- Financial reports
- Transactions
- Evidence

In order to observe the situation in the Republic of Macedonia related to the perception about the knowledge of the forensic accountant and the forensic auditor, a survey research was conducted on 25 accountants and 37 auditors on the territory of the Republic of Macedonia. The recognizing of the two concepts according to the research carried out in the Republic of Macedonia, has the following result: 93% of the accountants are familiar with the term of forensic accounting, while 7% are not. 97% know about trainings or bodies which conduct trainings of forensic accountants, 3% do not know. To the question of whether they see the difference between forensic accountants and forensic auditors, 74% see, and 5% do not, while 11% do not know. All 100% of the accountants consider that there should be a special training for forensic accountants.

As to the profession of forensic auditor, 99% of the auditors in the Republic of Macedonia had heard about the existence of this profession and they know their work tasks, while 1% had never heard of it. All 100% have never heard about special trainings or a body which conducts trainings on the territory of the Republic of Macedonia. To the question of whether they see the difference between forensic accountants and forensic auditors 91% see the difference, 5% do not see the difference, while 3% do not know.

4. DISCUSSION

The theoretical determination of the profession of forensic accountant and forensic auditor is identified by its definition. According to the reviewed literature, we can deduce the definition on forensic accountant and forensic auditor.

Many authors do not see the difference between the two concepts, i.e. they equalize them. If we compare the definitions of the two concepts, we will notice that there are many similarities.

Forensic accounting is an advanced accounting conducted by a competently trained person by knowledge of finances and economy, discovering a fraud or a crime through investigation of the accounting paperwork, and in service of a legal support in criminal charges or a judicial trial.

Forensic audit is an audit above audits carried out by a forensic auditor trained for conduction of investigation for the sake of prevention and discovery of frauds especially in the financial reports, as well as estimation of the risk of financial frauds, and it should provide the evidence for the court procedure.

From the investigation conducted in the Republic of Macedonia we can conclude that these two disciplines are new in the modern world, full of frauds and crime. The auditors possess more knowledge in forensic audit than the accountants do in the accounting audit. There is a need of training for promotion of these two professions as well as forming of a special body which will be part of the international association of investigators of financial crime or certified investigators of frauds.

5. LITERATURE

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