

Forensic Accounting: A Tool to Alleviate Creative Accounting.

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Abstract:

A Forensic Accounting is the domain of Accounting which curbs the irregularity of accounting practices as created by Creative Accounting. Forensic Accounting includes the special knowledge and vigilant skills that are utilised to combat the financial frauds and check upon the deliberate practices in the books of accounts maintained under the loopholes of accounting principles.

This paper undertakes the research to investigate the dimension of forensic accounting and its measures. Paper also emphasis on the creative accounting practices in India, envisage the problem and provide the needed solution through Forensic accounting. This research article discusses the concept of forensic accounting and its vital role in corporate organisation.

Keywords: Forensic Accounting, Creative Accounting, Financial frauds, White collar crime

Introduction:

Creative Accounting is a referred as a deliberate attempt to make smoothening of income by manipulation of items of Financial Statement which may prove detrimental in long-run (Merchant and Rockness, 1994). Creative accounting is a purposeful intervention of management in the financial reporting process (Schipper, 1989) using choice of accounting methods, estimates and other practices allowed under accounting principles. The driving force behind the creative accounting is existence of tax levies based on the income, confidence by shareholders and workers in management that management is efficiently performing and have stable income and coping with other psychological expectations related to increase or decrease in anticipated income (Hepworth, 1953). In general, creative accounting practice is deceitful and undesirable, this arises the urgent need for a expert or accounting skilled personnel who can investigate and give opinion about law-suits related to misrepresentation and fraudulent accounting practices, which is referred as Forensic Accounting. It is the branch of accounting that deals with in-depth knowledge of accounting and scrutinising the financial reports to check their authenticity and transparency.

Objective of the Study:

This research articles is focused on the understanding of Forensic Accounting and its relation with Creative Accounting. The study is basically exploratory in nature, and various facts and contents has been taken from published Journals, Websites , other related agencies and other online sources of information. The main objective of the study are:

1. To develop the insight about Forensic Accounting.
2. To understand the relation of Creative Accounting with Forensic Accounting.

3. To evaluate need of Forensic Accounting and its dimension in India.
4. To analyse method of Forensic Accounting and its role in fraud examination.
5. To conclude the understanding and needed action for Forensic Accounting practices in India.

Literature Review:

Ogutu and Ngahu (2016) studied that, proficiency of accounting personnel and their training is guaranteed improvement against fraud. The study suggested traits of forensic accountant like, analytical skills, ethical traits, and confidence, beside this; accountant should have auditing skills, investigating skills, and legal knowledge.

Ibidunni, Okere and Aro (2018) studied the background of failure of anti-corruption agencies and various reforms and required forensic accountants to deal with growing corruption in Nigeria. The finding suggested that Government financial statements should be studied thoroughly for their reliability and authenticity.

Imoniana, Antunes and Formigoni (2013) differentiated forensic accounting with auditing, and established forensic accounting as a specific career option in progressive nations. The emphasis of the study was to align practices of forensic accounting with international practices. These practices will explore the doubtful and fraudulent transactions. The study also reveals that weak internal control and regulations lead to corrupt management practices.

Bhasin (2015) studied the practice of creative accounting is prerequisites to achieve unethical benefits for accountants, administrators or organisations. Study recommended a strict action against practice of creative accounting like efficient regulation of auditing, accounting and corporate governance actions to prevent creative accounting practices.

Zeid, Younis and El-Mousawi (2020) Studied the inverse relationship between forensic accounting and creative accounting, and suggested that Integrated Audit method one of the method of forensic accounting is the most efficient way to curb creative accounting and recommended to add Forensic Accounting as a Master Certificate course and training sessions should be arranged to learn in depth about changing accounting practices in the business scenario.

Creative Accounting Practices:

Creative accounting relates to the presentation of financial numbers, based on cognitive reference point. It is the manipulation in balance sheet to reclassify the liabilities to reflect smoothening of liquidity position and sound leverage ratios (Gramlich 2001)

Practices of creative accounting are done in Income Statement, Balance Sheet and Cash flow Statements (Remenarić, Kenfelja, & Mijoč, 2019). Some of the techniques are elaborated as follows:

- Inflating the expenses like depreciation on fixed assets.
- Charging current year expenses to later or previous year.
- Exaggeration in the valuation of intangible assets.
- Paying bogus expenditure.
- Manipulating inventory value.
- Depleting the value of fixed assets by charging high rate of depreciation.
- Readjusting exchange rates in case of Balance sheet for foreign firms.
- Manipulating cash flow to evade tax.
- Over and undervaluing the Inventory and underpricing scrap.

- Creating ghost employees and deriving salaries and wages in their name.
- Manipulating the financial ratios, etc.

Thus potential for creative accounting can be summarised in six guiding principles; Regulatory flexibility, no common regulation, wider scope of managerial discretion regarding reserves and provisions, timing of transactions, reclassification and presentation of financial numbers, these all basic principles prepare financial reports in such a way to achieve a desired goal for managerial frauds and income smoothening. This became a breeding ground for many financial scams and various techniques for asset misappropriation, defined as White Collar Crime. This needed for a branch of accounting to detect such unethical practice in books and it evolved the term 'Forensic Accounting'.

Need for Forensic Accounting:

Black (2010) stated that, financial fraud is one of the major contributors to the financial crisis and endangering the regulation, liquidity and safety of capital market. It increases the volatility and uncertainty in the market which disturbs the sentiments of investors worldwide and effect the economy in total. Increase in financial frauds prompted for development of new branch of accounting , which investigate and disclose all the material facts related to the financial reports and disclose the White Collar crimes in the practice of creative accounting. Thus Forensic Accounting rose to be prominent accounting practices to detect and disclose the hidden truths of the books of accounts.

Methods of Forensic Accounting:

There has been two possible method developed to aid forensic accounting, Reactive Auditing and Proactive Auditing.

1. **Reactive method:** this method detects the illegal or doubtful activities to know whether fraud exist or not. This method also collects the evidence that support the fraud and the find out the person responsible for the fraud. This method requires recognizing, protecting, gathering, examining, and generating the final survey. The procedures used in detecting frauds includes
 - 1.1 Genetic Chart this present a personal relation among parties directly or indirectly involved in the investigation (Crumbley 2009)
 - 1.2 Tracking chart is use to show cash flow to and from bank or from stock of company to another company.
 - 1.3 Data mining use computer system to search for hidden data(Mehta and Mathur 2007)
 - 1.4 Auditing the process of delegation of authority and the person involved in the authority making.
 - 1.5 Checking the authenticity of books of accounts.
 - 1.6 Sequencing the occurrence of disputes and analysing all the details relevant to the case. It is summarizing the investigation.
 - 1.7 Examine the expenditure nature whether it is rightfully capital or not, and checking the diversion of funds from one organization to another.

2. Proactive Auditing:

Statutory Auditing is a type of proactive auditing, as it evaluate internal control system and ensure protection of interest of various stakeholders. It is a 'diagnostic tool' to analyse the risk resulting from fraud. Proactive auditing includes organized and transparent accounting records to ensure ethical accounting practices in an organization (Nieto, 2018).

Forensic Accounting in India:

Forensic Accounting was developed early in 1995 in USA, but rise steadily in India, a few years before. The Institute of Chartered Accountants of India (ICAI) is providing 100 hours certificate course for training Chartered Accountants to become Certified Forensic Accountants (CFAs).

Government of India has establish agencies to combat financial frauds,

1. Serious Investigation Fraud Office (SIFO) is established under Ministry of Corporate Affairs of India to look over fraud in the area of Income tax, FEMA, RBI etc.
2. Central Vigilance Commission (CVC) to combat corruption. A special “Forensic Cell” is develop to look over Banking Frauds supervised by RBI and Financial nature Frauds supervise by SEBI.
3. Central Bureau Of Investigation(CBI) deals with financial frauds refer as “Economic Offence Wing”

In addition to these, many Private entities are also providing services for Forensic Accounting in India.

Conclusion:

Today there have been tremendous cases of corporate fraud and scams resulting into white collar crimes which are hard to crack down. In this Forensic accounting plays a beneficial role as it deals with the issues related to quantification of economic damages resulted from this financial fraud. A new dimension of cyber fraud is rising up in the country with it many corporate scams will raise; hence in order to curb such malpractices in the books of accounts, therefore a strong legislation framework for Forensic Accounting must be created. A specialised course should be designed for Forensic the understanding and implementing the techniques of Forensic accounting. Forensic Accounting is at a nascent stage, developing the framework for working of Forensic accounting today will save many future frauds and errors. This will provide benefit and protection to various stakeholders and will retain their trust in Intangible existence of the corporate entity. Various research studies proved that, audit serve as a measure to check upon Forensic Accounting but it is needed to explore more areas in data mining and other computer tools to assist the forensic accounting.

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