

FORENSIC ACCOUNTING: A CASE IN POINT FOR COMBATING FINANCIAL CRIMES OF BANGLADESH

Sanjida Ahmed
Mohobbot Ali

¹Senior Accounting Teacher Maple leaf International School (E-mail : Sanjida.ahmed.nsu@gmail.com)

²Professor University of Dhaka Department of Accounting and Information Systems
(E-mail: Mohobbot70@yahoo.com)

Accepted date: 25-09-2019

Published date: 13-10-2019

To cite this document: Ahmed, S., & Ali, M. (2019). Forensic Accounting: A Case in Point for Combating Financial Crimes of Bangladesh *International Journal of Accounting, Finance and Business (IJAFB)*, 4(22), 1 - 8.

Abstract: *Today, many countries around the world have recognized the necessity of forensic accounting and also many organizations retained forensic accountants in their organization to combat and prevent potential financial crimes. Bangladesh is not an exception to the rest of the world, where the country is losing billions of Taka in financial crimes each year. Looking into the history of fraud cases of Bangladesh, from institutional fraud like Destiney2000, Hallmark-Sonali Bank scam, Bangladesh Bank reserve heist to liquidation of People's leasing, all these incidents raised a question in the minds of common run of people as to how the fraudsters could get away with the misappropriated money in presence of regulatory bodies? A question arises as to whether the auditors in Bangladesh are already empowered to detect such incidences ahead of time but not really motivated to do so or they are not adequately empowered to dig deeper into such occurrences due to some glass-doors. Is it right to hold auditors solely responsible for identifying the ongoing anomalies within organization? This paper scrutinizes the loopholes of existing system of Bangladesh and how forensic accounting plugs in the loopholes to combat financial crime.*

Keywords: *Forensic Accounting, Financial Crime, Misappropriation*

Introduction

Bangladesh has already met all the criteria and waiting to be officially called as developing nation of the world. Indeed, the pace of prosperity of the country is hindered by corruption, unethical activities and financial crimes that occur in both, public and private sectors firms. Financial crime has just followed in the footsteps of corruptions that was evident in the country for many years and took a more severe form. For the past few years one after another large scale financial crimes are taking place and engrossing attention of the mass people of the country. Necessary actions and interventions by the regulatory bodies' are falling apart to combat such crimes. Lost financial resource in financial fraud might not enter into the proper financial

channel of the country resulting in loss of potential future earnings for the government and also for the organization and economy. According to a report of the Centre for Policy Dialogue, scams in 14 banks cost tk 225.02 billion in the past decade, which is about fourth-fifths the project cost of Padma-bridge and two-fifths that of Sonadia deep-sea port. According to Association of Fraud Examiners' report, half of the money lost in financial crime could never be recovered. Thus to reduce and prevent financial crime, many countries in the world have recognized the importance of forensic accounting. Bangladesh should also incorporate Forensic accounting in the corporations to fight and protect the organization and the economy as a whole against those financial frauds perpetrated by the employee or by the organization itself.

Problem Statement

Bangladesh is losing billions of taka in financial crimes each year. As mentioned earlier one after another colossal level financial crimes are taking place in this country. Existing regulatory bodies of the country alone are failing every time to fight against these frauds. Thus the organizations and the economy as a whole are under great threat of such crimes.

Objective of the study:

This is an observational study to critically identify the loopholes of the existing regulatory system of Bangladesh and practices of the organization. The report also identifies the importance of forensic accounting in combating financial crime of Bangladesh. Moreover how forensic accounting, utilizing its specialized attributes which is different from auditors, can plug in the loopholes of the existing regulatory system is also discussed in this report.

Methodology

This paper is an observational study on necessity of incorporating forensic accounting as an investigator and preventer of financial crime of Bangladesh. Daily newspapers of different time frames, for example the news reports regarding each financial crime came to light before the public through print media, were collected. For the analysis purpose news reports of the entire month of August 2012, August 2016 and July 2019 were collected. Along with newspaper articles, internet has been used as a secondary source of data collection. Different websites of Regulatory bodies of Bangladesh, like Registrar of Joint stock Companies and Firms (RJSC&F), Dhaka Stock Exchange (DSE), and The Company ACT 1994 have been used as a source of information. Interviews conducted on different employees of different public limited companies to be appraised of the current accounting and fraud detection practices.

Literature review

In 1946, Maurice E. Peloubet first introduced the term forensic accounting in his essay "Forensic Accounting: Its Place in Today's Economy." Forensic accounting is a specialized branch of accounting that is investigative in nature. Forensic accounting is identified as a certain type of accounting profession that is endowed with special characteristics and requires a formal certification in the subject matter (Williams, 2002). "Forensic" means "suitable for use in a court of law," and it is to that standard and potential outcome that forensic accountants generally have to work (Crumbley, Heitger and Smith, 2005). Forensic accountants are specially designated to work in these two area- investigative accounting and litigation support. Investigative accounting is not only limited to numbers and documents of a company, but understanding the business environment as well. (Moncliff, 2005). Forensic accounting got popularity due to rapid increase in financial frauds and white-collar crimes. The scope of the profession growing enormously,

they are retained by insurance companies, banks, police forces, government agencies, etc. (Bhasin, 2007). Numerous cases of corporate scandals and failure in their ability to anticipate the fraudulent activities have created a need for these special professional accounting bodies that goes beyond statutory audit and in some cases even the trend of corporate governance. Owajori, A.A and T. O. Asaolu (2009). Forensic professional accountants are expected to identify the signs of fraud where all other accountants (cost and management accountant, and financial accountant, auditors) have limitation in doing so. Forensic accountants while conducting their investigation may examine internal databases and court records. Fraudsters must have concealed the evidence of their crimes, forensic accountants with their skeptic eye must look beyond the numbers and foresee criminal actions. (Bobby Waldrup, Kim Capriotti and Seth C. Anderson, 2009). General activities of forensic accountants might include analyzing the financial considerations of a lawsuit, preparing a damage report, and testifying as an expert witness. Along with these activities forensic accountants may also help to prepare deposition questions by anticipating opposition's move (Fenton and Isaacs, 2012). The concern of forensic accounting investigator is much more granular in nature, with the extensive development of factual information, gathered from both documentary evidence and testimonial evidences. The evidences addresses the questions like who, what, when, where, how, and why regarding the suspected fraud. The forensic accounting investigators are comparable to detectives known as fraud investigator (Gerson, Brolly and Skalak, 2015). Another research found irrespective of public or private sector firms, contribution and importance of Professional Forensic Accountant is enormous (Okoye and Gbegi, 2013). The business world is unethical and fraud activities are evident in this business world. However, to protect industries and economies against such fraudulent activities anti-fraud scheme exists known as forensic accounting (Rizk, 2014) Financial statement fraud is considered to be deliberate misrepresentation of organization's financial health through the deliberate misstatement or omission or disclosures in the financial statements to mislead financial statement users (ACFE Fraud Examiners Manual 2018). Forensic accounting possessing special attributes is proven to be effective in discovering fraud (Hamdan, 2018). Forensic accountants are considered to be fraud detection expert who plays a significant role in the prevention of financial crime and corruption in the selected micro finance institutions of Calabar (Basseyy, 2018). Similarly, another article revealed that there is a positive impact on detection and prevention of fraudulent activities after adaptation of some Forensic accounting practices in Nigerian banking industry (Ogundana, Okere, Ogunleye and Oladapo, 2018).

Financial fraud:

According to Federal Bureau of Investigation (FBI) fraud is defined as "Lying, cheating, and stealing. That's white collar crime in a nutshell. The term reportedly coined in 1939- is now synonymous with the full range of frauds committed by business and government professionals. It's not a victimless crime. A single scam can destroy a company, devastate families by wiping out their life savings, or cost investors billions of dollars (or even all three, as in the Enron case). Today's fraud schemes are more sophisticated than ever, and we are dedicated to using our skills to track down the culprits and stop scam before they start" (Howard Silverstone, 2012)

Existing Regulations and Practices of Bangladesh to combat financial crime:

Organizations, both public sector and private sector firms, have to cross several check points put in place by regulatory agencies to make the organization work for cumulative benefit of the

stakeholder's of the organization, avoid agency problem, and also to ensure true and fair representation of financial statements

Corporate Governance

To safeguard interest of general investors and avoid agency problem within organization Corporate Governance code was formulated. In 2006 Corporate Governance Code was first adopted by Bangladesh Securities and Exchange Commission. After every 6 years it is updated to incorporate and fix the ongoing problematic area that might give a chance to the organization to practice creative accounting and perpetrate fraud. Corporate Governance specifies the overall structure, policies, responsibilities of Board of Directors & chairman, policies and procedures in preparation of financial statements and certain mandatory practices (External and internal audit) to be followed by listed companies as required by the regulatory authorities like Bangladesh Securities and Exchange Commission (BSEC), Registrar of Joint stock Companies and Firms (RJSC&F) and so on.

Internal Audit

Internal audits are carried out by the organizations to achieve corporate objectives by keeping tabs on the consistency of internal business practices. The objective of an internal audit is to ensure that organizational policies and procedures are followed and to raise red flag in case of management gaps in policy compliance, anomalies and misappropriations by the employees. In case of financial institutions internal audit is a mandatory requirement by Bangladesh Bank.

External Audit

Code of Corporate Governance formulated by Bangladesh Securities and Exchange Commission (BSEC) also specifies the specific guidelines which must be followed in case of External Audit. According to Company Act 1994, listed Companies' financial statements must be audited by External auditors. External auditors have to be the member of The Institute of Chartered Accountants of Bangladesh (ICAB). Every year audited financial statements along with audit report and proper disclosures must be disclosed to public in case of public limited companies. This is a requirement by regularity bodies to ensure true and fair representation of the financial affairs of the respective companies.

Credit Rating

Credit rating agencies are the organizations that are responsible for assessing the creditworthiness of the borrower. External credit assessment institution accredited by Bangladesh Bank., allows the company's rating to be used by banks and financial institutions for capital adequacy reporting under Basel 11 and Basel 11I accord. Provided that the credit rating agencies exercise the due diligence while carrying out their rating assignments, they can also use their access to the privileged information in unearthing probable financial crimes and reflect the same in award of their rating.

Loan Disbursement Policy in case of financial Institution

Loan disbursement policy varies from financial institution to financial institution. The loan proposal along with credit appraisal and other documents are assessed by management then the board decides on whether the loan should be given out to the prospective clients or not. Being a fiduciary responsibility, all kinds of lending activity in a financial institution should be at arm's

length basis on the part of both board of directors and management. An effort must be made consciously to avoid existence of any possibility of “daisy chain” in the lending.

Whistle blowing

In any organization it is claimed that they encourage whistle blowing along with other mandatory procedure to identify fraud or misappropriation within organizations. Whistle blowing refers to the raising of red flag by any stakeholders of the organization in case of any suspicious matter.

Forensic Accounting

To overcome the shortcomings, a specialized field of accounting integrating auditing, accounting, law and investigation surfaced. Forensic accounting deals primarily with fraud prevention and fraud investigation. Different scholars have defined forensic accounting in different ways. Kranacher, Riley, and Wells defined forensic accounting as:

Financial forensic is the application of financial principles and theories to fact or hypotheses at issue in a legal dispute and consists of two primary functions:

1. Accounting expert or consultant.
2. Investigation services, which makes use of the financial forensic professional’s skills and may or may not lead to courtroom testimony.

Financial forensic is the intersection of financial principles and the law and therefore, applies the, (1) technical skills of accounting, auditing and finance, quantitative methods, and certain areas of law and research: (2) investigative skills for the collection, analysis and evaluation of evidentiary matter: and (3) critical thinking to interpret and communicate the results of an investigation. (Howard Silverstone, 2012)

Forensic accounting as a specialized branch of accounting started getting more spotlight at recent times when it is being increasingly evident to all that financial crimes have been taking a heavier toll on the financial resources of all countries than any time before. This may partly be attributable to universal trend towards loss of moral values and unbridled pace of technological adoptions. Nevertheless the field was identified by Maurice E Peloubet in late 1800s. Application of this profession is much needed in today’s complex financial condition of any country including ours in particular.

Scope of Forensic Accounting:

Fraud prevention and mitigation is major broad area of application, however application of forensic accounting also includes the following areas:

Fraud Prevention, Detection and Response

Forensic accounting primarily focuses on detecting fraud that has already been committed and also in preventing fraud where they are likely to be committed. Forensic accounting has its role to play in assisting owners and organizations to ensure better controls and procedures in response to fraud that has taken place. Forensic accountants, if retained by the organization, thus can proactively evaluate its internal control, financial policies and accounting procedures before occurrence of such financial fraud. They can also identify the specific fraud areas where red flags are not even raised by the auditors or no indications of fraud exist. Moreover, if fraud is identified, then forensic accountants with their investigative eyes can also dig down the period of

anomalies and can also find the perpetrators to take them to the court by taking appropriate actions.

Bankruptcy, Insolvency and reorganization

Organizations can employ forensic accountants on behalf of debtors or creditors where organization is already or contemplating on bankruptcy. Forensic accountants assist the trustee in managing financial affairs, searching for hidden assets, identifying pre-bankruptcy transfers, recovering funds and assets to be used to satisfy creditors, or performing business valuations to be used in resolving the bankruptcy filing.

Computer Forensic Analysis

Technological advancement has made the information to be kept not only in computers and server hard drives but also in clouds. The physical location of the information thus had gone away from the business location. The two major application of computer forensics are preservation and recovery of electronic information for evidence purpose, and electronic litigation support.

Economic Damage Calculation

Damages are known as calculated loss suffered from causation. Forensic accountant could be hired to calculate losses in many contexts, including lost earnings, lost profit, lost business and the physical loss of property (flood, fire, theft). Forensic accountants could be hired by either parties-plaintiff or defendant. However, they are entrusted to advocate for the truth, by being subjective and unbiased. Two common instances where damage calculation is necessary are litigation and insurance claim. Forensic accountants are also called upon to prepare and also review and refute submitted damage calculation in the cases, litigation and insurance claim.

Family Law

The forensic accountant has a number of roles to play in marital dissolution (divorce and post-divorce). Due to very nature of these personal and highly emotionally charged matters, fraud and nondisclosure are both common. The forensic accountant may work with counsel to uncover hidden or undisclosed sources of income or assets that should have been appropriately included on a party's financial affidavit. Earnings and expenses of each party, along with earning potential, will come into play in calculating alimony and child support.

Financial Statement Misrepresentation

Forensic accountants can be employed to examine the financial statements and disclosures of publicly traded and privately held entities. The forensic accountants can identify the anomalies of the financial statements, such as understatements, overstatement, omissions and improper accounting treatments. The forensic accountant also looks after the standards, rules, procedures and regulations that were violated and also reveal the underlying motives for intentional misrepresentations.

Business Valuation

Forensic accountants are hired to conduct business valuations in a number of instances. The valuation is done in cases like dividing assets in a divorce, shareholders dispute, purchase and sales of companies, shareholder buy-ins and partner buy-outs, the value of the business.

How Forensic accounting differs from auditing?

According to The Companies Act 1994, as applicable in Bangladesh requires the financial statements of the public limited companies to be audited by the members of Institute of Chartered Accountants of Bangladesh (ICAB). The responsibility of auditors is to evaluate whether the financial statements prepared by the management of the company are stated in all material respects in accordance with general accounting principles. Thus the audited reports reflect the opinion based on tests, evidence supporting accounts and disclosures in the financial statements. Taking into consideration the main objective of auditor (internal or external), we can conclude that they fail to trace the deliberate misstatement and potential fraud crime. This is because the nature of the profession is not investigative as the act of concealment is involved with fraud.. Auditors reply on sampling techniques, given their limitation in time and resources, to ensure fairness and accuracy of financial statements. At times, falsified, altered or forged documents which are indistinguishable from the original ones are supplied to auditors. Given the scope of auditor it is next to impossible to go as far as to detect the genuineness of documents Nevertheless, auditors may still raise the red flag on doubtful issues but have limitation in undertaking the issue further or fail to provide litigation support. However, Forensic accounting is investigative in nature and also able to provide litigation supports. Forensic accounting scrutinizes the red flagged issues and skeptic features of the profession can also unearth fraud even where no red flags were raised or indication was evident.

Table 1: Attributes of Auditing & Forensic Accounting

	Auditing	Forensic accounting
Error identification	Yes	
Error prevention	Yes	
Fraud identification		Yes
Litigation support		Yes
Evidence gathering		Yes
Economic Damage calculation		Yes
Finding fraudster		Yes
Material misstatement	Yes	Yes
Disclosures and accounting procedures	Yes	

Conclusion and Recommendation

Forensic accounting is an emerging discipline and inclusion of forensic accounting in the corporate world of Bangladesh in necessary. Around the globe forensic accounting has already got its recognition as an individual discipline. Since financial crime pervaded the corporate landscape of Bangladesh as admitted on all hands, forensic accountant should be hired by the organizations which are genuinely sincere to do away with all forms of overt and covert frauds. Retaining forensic accountants within the organization can help identifying the fraud beforehand. In order to bring out trained forensic accountants Universities should offer full-length bachelors and masters programs in forensic accounting. The prospect of forensic accounting is enormous and far-reaching. There is a saying “accountant (normal) acts like a watchdog, but a forensic accountant must be trained to act like a bloodhound.’ Thus, it is high time that Bangladesh

recognized the importance of forensic accounting as a discipline and should train regular accountants into forensic accountants to prevent and mitigate financial crime.

References

- (n.d.). Retrieved March 20, 2019, from Association of Certified Fraud Examiners: <https://www.acfe.com/fraud-resources.aspx>
- O. Enofe, P. O. (2013). The Impact of Forensic Accounting on Fraud Detection. *European Journal of Business and Management* .
- Code of corporate Governance*. (2018, 06 03). Retrieved 07 20, 2019, from Bangladesh Securities and Exchange Commission: http://www.sec.gov.bd/slaws/Corporate_Governance_Code_10.06.2018.pdf
- Emerging Fraud: Fraud Cases from Emerging Economies*. London: springers.
- Fasua Henry Kehinde, I. L. (2016). Basic Issues in Forensic Accounting and Auditing. *International Journal of Scientific & Engineering Research* .
- forensic accounting*. (n.d.). Retrieved 06 2019, 30, from wikipedia: https://en.wikipedia.org/wiki/Forensic_accounting
- Godwin Emmanuel, E. P. (2019). Integrity of financial statements and forensic accounting techniques. *Journal of Forensic Accounting and Fraud Investigation* .
- Huber, W. D. (2014). Forensic Accountants, Codes of Ethics and Forensic Accounting Corporations. *Journal of Forensic & Investigative Accounting* .
- The Company Act 1994*. (n.d.). Retrieved 07 17, 2019, from https://www.iiiiglobal.org/sites/default/files/companiesact_0.pdf
- 51 indicted in Destiny scam cases. (2016, August 25). *The Daily star* .
- Bangladesh Bank Robbery*. (n.d.). Retrieved from Wikipedia: https://en.m.wikipedia.org/wiki/Bangladesh_Bank_robbery
- Hallmark loan scam under ACC probe . (2012, August 14). *The Daily Star* .
- Hasan, M. (2019, 07 10). People's leasing liquidation move leaves depositors worrying. *Dhaka Tribune* .
- Howard Silverstone, S. P. (2012). *Forensic Accounting and Fraud Investigation*. USA: John Wiley & Sons Inc.
- THOMAS W. GOLDEN, S. L. (2006). *A Guide to forensic investigation*. New Jersey: John Wiley & Sons, Inc.
- Uddin, A. Z. (2019, 07 19). Peopl'e leasing faces liquidation. *The Daily Star* .
- Bassey, B. E. (2018). Effect of forensic accounting on the management of fraud in microfinance institutions in Cross River States. *Journal of Economics and Finance* , 79-89.
- MW, H. (2018). The role of forensic accounting in discovering financial fraud. *International Journal of Accounting Research* .
- Peterson, O. K. (2015). Forensic Accounting and Fraud: A Review of literature and Policy Implications. *International Journal of Accounting and Economic Studies* , 63-68.
- Safiyanu Sule, S. S. (2019). The Effect of forensic accounting investigation in detecting financial fraud: A study in Nigeria. *Internation Journal of Academic Research in business and Social science* , 545-553.
- Temitope, O. A. (2014). The effect of forensic accounting on the financial performance of Commercial Banks on Nigeria. *Research Journal of Finance and Accounting* .