

# *Forensic Auditing - A Fraud Detecting Mechanism*

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## **1.1 Introduction**

Financial frauds have from time immemorial affected all establishments as no one is immune to frauds, but they often go undetected due to inadequacies in the system. Recent happenings in most parts of world has exposed the growing greed of human being and art of camouflaging of accounting facts through deception by indulging in fraud and manipulation, depending upon the position that one holds. It is estimated that the average organization loses about six percent of its total revenue to fraud and abuses by its own employee, which runs over to hundreds of crore of rupees. Large number of times the managing director and CEO had no clue of deep rooted white-collar crime that have perpetrated as well planned strategy. White-collar crimes have been increasing at an alarming pace, as the fertility of man's invention in devising new scheme of fraud is unlimited.

To sniff out financial frauds is highly specialized job and statutory audit as such has inherent limitation as a means to detect fraud. At the same time the new business methods and technology dependency, which are making business dynamic, are also making them vulnerable to financial fraud. To cope with the complications and to understand the implications of new business methods and technology, the internal auditor can no more limit to its traditional position, revolving around control and compliance. The profession of internal audit does not remain with in the perimeters of accounting records; in fact it only begins there. Internal auditor is no more just an accountant; he has to have the complete knowledge of the business and ability to link data, knowledge, and insight together to prevent potential wrongdoings. Unfortunately the corporate still has to accept internal auditor in its new role, at the same time internal auditor as an employee of the corporate is not even equipped to take on the new role. Alarming increase of financial fraud, inability of internal audit and limitation of statutory audit to sniff out the financial fraud has given rise to new profession known as Forensic audit.

The concept of Financial Auditing may be defined as "a concentrated audit of all the transactions of the entity to find the correctness of such transactions and to report whether or not any financial benefit has been attained by way of presenting an unreal picture".

Forensic auditing aims at legal determination of whether fraud has actually occurred. In the process, it also aims at naming the person(s) involved (with a view to take legal action). Forensic audit involves examination of legalities by blending the techniques of propriety (VFM audit), regularity and investigative and financial audits. The objective is to find out whether or not true business value has been reflected in the financial statements and in the course of examination to find whether any fraud has taken place.

## **1.2 History of forensic audit-**

In a global review conducted by Ernst & Young, on the question of auditors' responsibility, in 1996, the finding was:

"Over seven out of ten of the respondents believed that auditors should have the responsibility to detect substantial fraud. Of these eight out of ten believe that this should be