

FORENSIC ACCOUNTING

DEFINED AND DE-MYSTIFIED

PART 1

theSun Insights now focuses efforts on a series of articles exploring specialised practices in the accounting arena. Using simple language and graphics to empower both lay readers, lawyers and other professionals with carefully structured analysis providing explanation and insights, which help explain the importance, relevance and scope of such work.

theSun CMO, Prashun Dutt, pursued hours of research, punctilious interviews, plus expert inputs by **Prabhat Kumar**, a prominent Malaysia-based Investigative and Forensic Accountant. He is a reputed international expert in this subject.

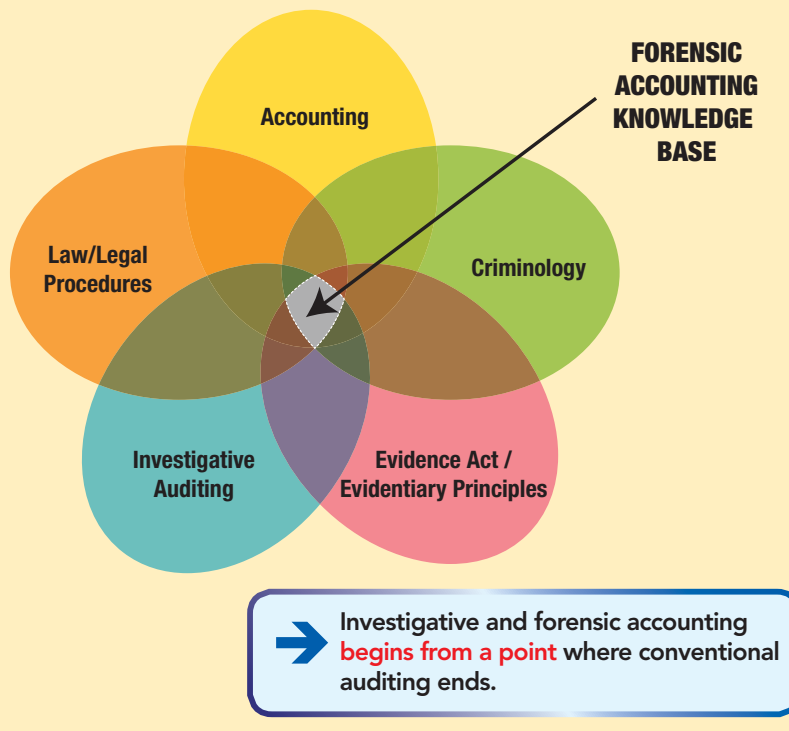
FORENSIC Accounting and financial forensics involve a specialty practice area of accounting. It should NOT be considered a simple extension of audit or special audit, pursued with broader, deeper investigation. **Forensic accounting requires a different approach and mindset. It is now firmly established as a specialised profession.**

SCOPE OF WORK

Following the dictionary definition: "pertaining to, connected with or used in courts of law", the term Forensic Accounting was coined by Canadian accountant Robert Lindquist to explain the special combination of skills required for examining, reviewing and analysing financial records/evidence, resulting from actual or anticipated disputes, investigation, litigation and evidentiary needs.

Forensic accountants are often

Figure 1: Forensic Accounting - Required Knowledge Base



cycles, financial, banking and insurance procedures, besides clarity in communication, competence in writing reports and experience in working with other enforcement agencies and legal counsel (see Figure 1).

Some forensic accountants also develop sub-specialisations and focused expertise, including

- ▶ insurance claims/fraud;
- ▶ money laundering;
- ▶ construction and real estate;
- ▶ royalty audits;
- ▶ forensic financial due diligence;
- ▶ economic damage calculations, whether suffered through tort or breach of contract;
- ▶ post-acquisition disputes such as earn-outs or breaches of warranties;
- ▶ asset analysis for divorce settlements and partnership dissolution;
- ▶ bankruptcy, insolvency, reorganisation and restructuring;
- ▶ securities fraud, theft of stock, fidelity, bond;
- ▶ tax fraud;
- ▶ arson for profit;
- ▶ purchase and procurement fraud;
- ▶ business valuation;
- ▶ economic damage quantification for recovery of loss;
- ▶ internet fraud.

INCREASING DEMAND FOR FORENSIC ACCOUNTANTS

With enormous sums of money, assets and opportunities being involved, the last decade reflects increasingly higher incidences of fraud and irregularities among executives and senior personnel.

Large to medium corporations, SMEs and NGOs are susceptible to creative accounting practices, often engineered by management, directors, promoters and stakeholders. Upon suspicion/discovery, urgent review and adjustments are required along with



called to give expert evidence during court proceedings and formal inquiry commissions, besides working for business corporations, lawyers, government agencies including excise, tax, revenue departments and the police.

Consequently, they are particularly tasked to conduct inquiries, examination and evaluation in an objective, unbiased and professional manner, such that judges, arbitrators and lawyers clearly understand:

- ▶ the complexities involved in the dispute;
- ▶ purpose, manner and modus operandi of the irregularities;
- ▶ professional negligence, extent

and implications;

- ▶ nature and extent of the damages/losses incurred;
- ▶ roles played by various (involved) individuals/parties;

...empowering them with transparent and firm decision-making inputs.

DISTINCT PRIORITIES

Proficient forensic accountants are much more than just fraud auditors. Building on the basic foundation-knowledge of accounting and auditing principles, their role requires operational familiarity with the law, relevant legal torts and evidentiary procedures, criminal investigation process, corporate governance, business and purchase

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verification plus re-statement of previous annual financial reports.

In today's borderless society, business, trade and financial dealings have become more complex and digitalised. Simultaneously postulating an even wider range of opportunities for irregularities, creative accounting, financial manipulation, illegal asset acquisition, investment fraud, computer/internet-fraud, tax/duty evasion and money laundering across markets and continents.

These complexities have escalated the demand for specialised or independent forensic accountants with such expertise.

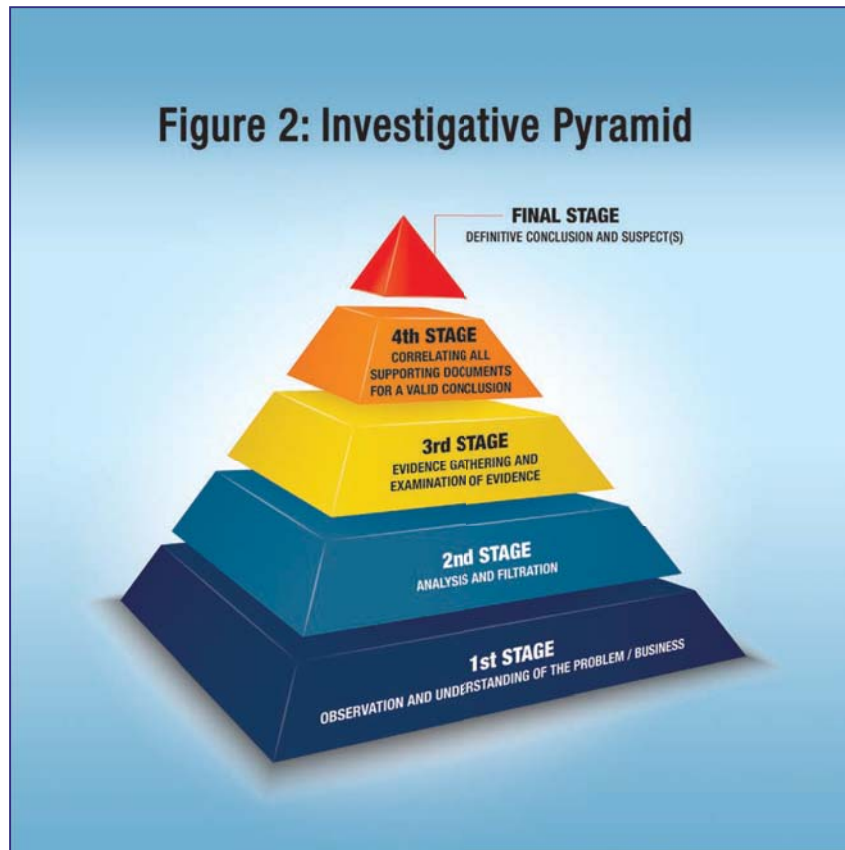
FORENSIC ACCOUNTANT: REQUIRED TRAITS

By virtue of education, training, skills and experience, an aspiring general accountant can also become a specialist forensic accountant. Along with domain-knowledge, these 10 traits are considered necessary:

- 1) Investigative mind set;
- 2) an eye for punctilious, detail;
- 3) persevering and persistent;
- 4) professional scepticism;
- 5) well-developed analytical skills;
- 6) determination to overcome obstacles;
- 7) remaining steadfast despite threats and bribes;
- 8) independence, objectivity and integrity;
- 9) ability to craft/write reports with probative value; **plus**
- 10) effective communication and presentation skills

METHODOLOGY: INVESTIGATIVE PYRAMID

To ensure their reports are **admissible in court**, preferably



having the **required probative value**, forensic accountants tend to **pursue a structured approach** and some preferred techniques. This is pragmatically detailed in the Pyramid [see figure 2].

- Ideally initiating the investigation across a broader-base area, where he/she assesses all potential possibilities with an unbiased open mind.
- With increasing familiarity/knowledge of the operational

structure, process, intricacies and nuances, forensic accountants move up this proverbial pyramid in a systematic manner.

- Narrowing the options through careful filtration;
- Focusing on specifics, tracking/tracing the leads;
- Collating the references/material and pursuing the required examination, evaluation;

- Continuously assessing the crucial factors, discarding the irrelevant facets/red-herrings;
- Ultimately reaching the appropriate, convincing conclusion.

Forensic accountants **MUST** first acquire a comprehensive understanding of the business and all the relevant dynamics. This helps them **catch the nerve of the issue leading on to development of the possible hypothesis**. It is vital that the accountant does not lose track of the crucial, relevant issues, while discarding the irrelevant and non-essential.

In the second stage, the investigation area becomes narrow and focussed. The forensic accountant now has a comprehensive understanding of the business, the issues involved and begins developing clarity with conviction about the actual irregularities, factors which precipitated the economic loss and

the clues/evidence which need to be pursued.

Investigators must ascertain the most appropriate operational procedures and cycles, to establish the standard operating procedure, obviously acknowledging the credible arc/range of deviation coerced by practical business/revenue considerations.

After understanding the business cycle, operational process and filtration, forensic accountants:

- pursue microscopic examination
- of each phase and sub part;
- identifying the areas where illogical deviation and irregularities have occurred;
- mode and timing of those anomalies;
- plus the most likely individual and parties involved;
- collating appropriate facts, references and evidence, confirming that all needle point in the same direction.

This is critical, for cases are won (or lost) when judges remain dissatisfied or unconvinced about the logical reasons for such deviations/anomalies. Figure 3 details the sequential stages and flow of such a "Procurement Cycle" which forensic accountants micro-examine.

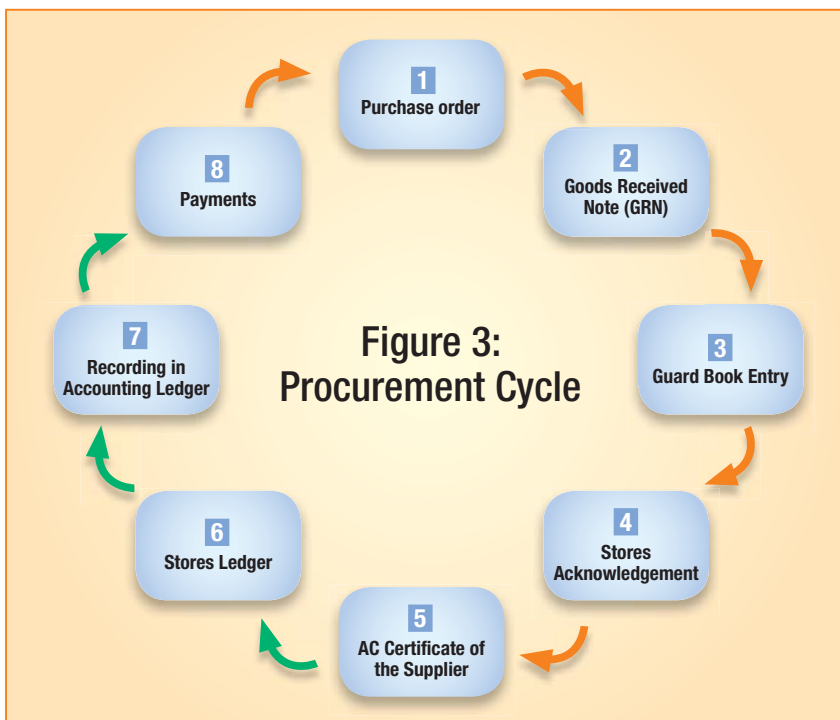
DIFFERENTIAL MIND-SET, SKILL-SETS

Forensic and investigative accounting is very different from conventional accounting practices. The auditors' approach rests on the key concept of good faith of the client. Further, they are governed by the concept of materiality. If deviation from the norm is not material, most likely it will not be examined or tested further.

The mind of an investigative and forensic accountant harbours scepticism as the basic quality. They investigate without having any pre-determined notion. Further, at the start, all clients and investigation-subjects are neither in good or bad faith.

Their core strength lies in the determination and ability to sift through mountains of material, data and files, extracting information, facts and insights. With the purpose of correlating these facts and evidence to present a big picture. Even in routine situations forensic accountants pay rigorous attention to detail and precision such that even minor hairline cracks catch

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FORENSIC ACCOUNTING PART 1



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their attention.

Forensic accountants consciously avoid pre-conceived notions, as this compromises their wider-ambit search for all potential possibilities. The **core mantra** lies in discounting all other possibilities. This essentially allows them to confirm that there was no plausible cause for the irregularity or event, other than the facts, causes and conditions identified by the investigator.

Such investigation and reports are prone to serious challenges by opposing lawyers, defendants and even media. **Forensic investigation reports should thus postulate a definite conclusion, duly considering the entire scenario and leaving zero scope for reaching any other alternative hypothesis.**

The entire purpose stands defeated if defendants and lawyers are successful in creating the slightest doubt in the judge's mind regarding other possibilities and options which were not pursued by the investigating accountant.

Such forensic reports, for instance, should detail with corroborating evidence: the role, authority and responsibilities of the suspect(s), possibility of others' participation or involvement in the irregularity, level of authority, control exercised by the person at various phases of an accounting cycle, existing internal control and its weaknesses. Besides the possibility of external and/or multiple party collusion.

Forensic accountants thus need to constantly evaluate their own work to confirm that **a given mandate has been accomplished in a manner which opposing lawyers and defendants will find difficult to challenge.**

COMMUNICATION AND PRESENTATION

Since forensic accountants compile complex financial evidence, they are also tasked to structure the information and communicate their findings in reports, presentations and visual aids. Such that issues come forth **in a logically structured, unbiased, objective manner empowering courts, judges, lawyers and other**

enforcement agencies with transparent and definitive decision-making inputs.

In complex business and financial investigations entailing tracing of funds, asset identification, asset recovery and due diligence reviews must be presented through

- Well-structured, skilfully crafted reports,
- Animated flow-charts, and
- Appropriate audio-visual presentations

... to generate higher impact and convincing testimony.

Due to their familiarity and high involvement with legal issues and the judicial system, some competent forensic accountants also pursue additional training in **alternative dispute resolution (ADR).**

COMPUTER-DRIVEN FORENSIC INVESTIGATION

Forensic and investigative accountants increasingly require the support of computer, software and mobile forensic expertise, data analytics, handwriting specialists and experts in other fields beyond conventional accounting.

In earlier times, it was relatively easier to ensure the integrity and reliability of (non-digital) evidence. Seized in the form of printed records, files and packages, they were sealed and transported in appropriate manner confirming the chain of custody.

In today's digitalised world most sensitive documents and records are created and stored in computers and as soft-copies. Computer/software expertise is thus required for extraction of data which is often vulnerable and prone to contamination if not retrieved and imaged properly.

Digital evidence differs substantially from traditional forms of evidence. When a laptop is seized, the evidence is not apparent like bundles of seized cheques. The real value of the evidence accrues only after the computer is turned-on and investigators are able to plough through passwords/ coded files to access the details. Any mistake here which causes files to be erased or lost may cause irreparable damage to



Prabhat Kumar explaining critical forensic accounting issues to theSun CMO Prashun Dutt .

STOPPAGE ORDER

STOPPAGE ORDER are imposed on individuals who will be leaving Malaysia without paying all his tax, sums and debts payable or company directors who will be leaving Malaysia without paying company tax and debts or monthly tax deduction (MTD) of employees.

Issuance of Certificate

Certificate issued to the last known address of taxpayer through registered mail

Revocation of Stoppage Order Certificate

Full payment as stated in the certificate by cash via ByrHASIL or other payment methods stated in LHDNM's Official Portal

Application for Temporary Release of Stoppage Order

If a taxpayer fails to pay in full, he can still apply for temporary travelling release by making payment of at least 50% of outstanding tax amount



Prabhat Kumar, investigative and forensic accountant.

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the investigations.

Further, forensic accountants nowadays deal with mammoth data files, multi-tier records and pursuit of investigative leads across countries and jurisdictions. Such as tracking a company's records across 30 terminals and five servers; or matching of a suspect's financial transactions across several years and multiple bank accounts.

To handle such large data and manage efficient searching and matching tasks, forensic accountants now utilise analytical software like IDEA or ACL, using specialised skills to execute these tasks.

Special proficiency, expertise and persistence are necessary for identifying, seizing, acquiring, extracting, filtering and processing the required evidence. Ensuring the entire plethora of relevant material sitting in multiple storage devices/servers are retrieved (and preserved for reference) without distortion. Figure 4 details the computer forensic process.

FORENSIC ACCOUNTANT AS A STRATEGIC PARTNER

Investigative and forensic accountants provide much more than just a back-room material collation and fine-tuned accounting or auditing services.

Besides the required expertise, they can function as a vital strategic partner to the legal team, an amicus curiae for the court and presiding judge, while accelerating the entire investigation and trial process with precision guidance at various stages of the proceedings. Plus well-

structured reports which postulate definite conclusions.

Following initial investigation, forensic accountants can even advise lawyers regarding the various facets of the case which need to be pursued, including grounds for leveraging two *nuclear weapons* in the legal armoury: **Asset Freezing/Mareva Injunctions** and **Anton Piller Orders**.

Asset Freezing/Mareva Injunctions and **Anton Piller Orders**.

a) Asset freezing is an *ex parte* legal process which prevents a defendant (usually an apparent fraudster) to an action preventing dissipation of their assets from beyond the jurisdiction of a court so as to frustrate investigation and potential judgment.

b) These are often combined with an **Anton Piller order** which provides the right to search premises and seize evidence, including financial transactions, revenue records and bank details, without prior warning.

- This is intended to prevent the destruction of relevant evidence.

- While it is not an open search warrant, this order does put defendants under huge pressure to give permission for pursuing and seizing of relevant documents. Else they would be **in contempt of court**.

c) The cumulative effect of these orders can even destroy the ability of the defendant to fund legal costs; may even help

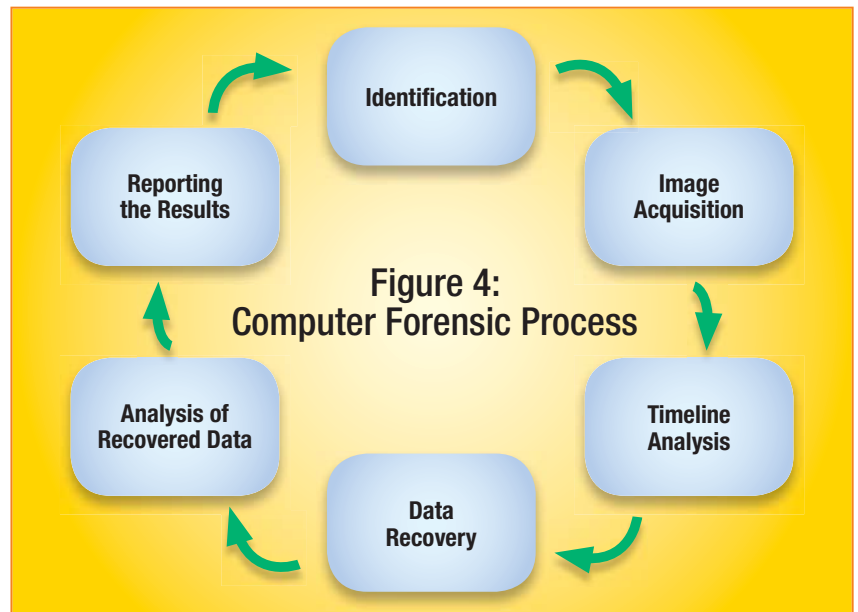


Figure 4:
Computer Forensic Process

precipitate or reveal important self-inflicting evidence to prove the crime and his involvement.

Pursuing such a comprehensive, thorough investigative (pyramid) process, competent forensic accountants provide lawyers, judges and all investigating authorities with **definite non-ambivalent conclusions, empowering firm decision-making and judgment.**

ACKNOWLEDGEMENT

- Prominent investigative and forensic accountant, **Prabhat Kumar**, founded his specialized practice in 2006. Alliance IFA provides clients with a wide range of investigative and forensic accounting services, including expert help in fraud risk assessment, forensic due diligence, restructuring, loss/damage quantification and litigation support.
- A member of the Malaysian Institute of Accountants, he is a qualified Chartered Accountant with a Diploma

in Forensic Accounting (Toronto, Canada), besides being a Certified Fraud Examiner (Texas, USA).

- He contributes expert articles on this subject to international publications and shares this unique experience at seminars and specialized courses.
- *theSun* CMO, **Prashun Dutt**, pursued hours of research, interviews and interaction with experts to collate and co-write this feature.
- Creative visualisation, art and design by **Ashley Seow**.



Alliance IFA Forensics Services Provided

Management Consultancy & Digital Forensic Services

- Management information system review & restructuring
- Insurance claim which are under disputes
- IT Audit, Infrastructure & Cyber Security
- Business Process Improvement
- Business Restructuring
- Acquisition & retrieval of lost data
- Computer / Mobile Forensic Analysis
- All types of digital crime forensic analysis

Risk Management Services

- Investigative & Forensic Accounting Services
- Fraud Risk Analysis
- Fraud Risk Assessment
- Fraud Awareness Training
- Damage Quantification
- Expert Witness
- Litigation Support Services

Financial Services

- Forensic Due Diligence
- Solutions to complex disputes for individuals / companies
- Review & analysis of financial statements
- Forecasting
- Internal audit & assessment of weaknesses in the system
- Reconstructing accounts where documents are partially or totally destroyed

Panel of Experts include:

- Tan Sri Dato' Setia (Dr.) Haji Ambrin Bin Buang
- Prabhat Kumar
- Bhavesh Lalwani
- Prakash Chetwani

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