



**THE INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS OF
PAKISTAN (ICPAP)**

(Suggested Solution)

Stage	Specialization	Course Code	SP-611
Examination	Summer-2012	Course Name	Forensic Accounting
Time Allowed	03 Hours	Maximum Marks	100
NOTES: 1) All questions are to be attempted. 2) Answers are expected to be precise, to the point and well written. 3) Neatness and style will be taken into account in marking the papers.			

Question No 1:-

a. What does a Forensic Accountant do?

Answer:-

A Forensic Accountant is often retained to analyze, interpret, summarize and present complex financial and business related issues in a manner which is both understandable and properly supported.

Forensic Accountants can be engaged in public practice or employed by insurance companies, banks, police forces, government agencies and other organizations.

A Forensic Accountant is often involved in the following:

- Investigating and analyzing financial evidence;
- Developing computerized applications to assist in the analysis and presentation of financial evidence;
- Communicating their findings in the form of reports, exhibits and collections of documents; and
- Assisting in legal proceedings, including testifying in court as an expert witness and preparing visual aids to support trial evidence.

In order to properly perform these services a Forensic Accountant must be familiar with legal concepts and procedures. In addition, a Forensic Accountant must be able to identify substance over form when dealing with an issue

b. How can a Forensic Accountant be of assistance?

Answer:-

A Forensic Accountant can be of assistance in various ways, including:

Investigative Accounting

- Review of the factual situation and provision of suggestions regarding possible courses of action.
- Assistance with the protection and recovery of assets.
- Co-ordination of other experts, including:
 - o Private investigators;
 - o Forensic document examiners;
 - o Consulting engineers.
- Assistance with the recovery of assets by way of civil action or criminal prosecution.

Litigation Support

- Assistance in obtaining documentation necessary to support or refute a claim.
- Review of the relevant documentation to form an initial assessment of the case and identify areas of loss.
- Assistance with Examination for Discovery including the formulation of questions to be asked regarding the financial evidence.
- Attendance at the Examination for Discovery to review the testimony, assist with understanding the financial issues and to formulate additional questions to be asked.
- Review of the opposing expert's damages report and reporting on both the strengths and weaknesses of the positions taken.
- Assistance with settlement discussions and negotiations.

- Attendance at trial to hear the testimony of the opposing expert and to provide assistance with cross-examination.

c. Who retains a Forensic Accountant?

Answer:-

Forensic Accountants are often retained by the following groups:

- Lawyers;
- Police Forces;
- Insurance Companies;
- Government Regulatory Bodies and Agencies;
- Banks;
- Courts; and
- Business Community

What should I consider when retaining a Forensic Accountant?

The following issues should be considered on retaining a Forensic Accountant:

- The experience and qualifications of the Forensic Accountant;
- A Forensic Accountant should be retained as early as possible in order to obtain maximum benefit. The assistance that a Forensic Accountant can provide early in the process can be significant in reducing the overall cost and maximizing the benefit. If retained early, a Forensic Accountant can assist with the Examination for Discovery, identify additional areas of damages, assist with settlement negotiations and provide a preliminary assessment of the quantum of damages;
- If a Forensic Accountant is engaged as an expert witness then he or she should be given access to all of the relevant documentation. If restrictions are imposed upon the scope of the investigation there may be an impact upon the acceptance of the findings; and
- In situations where counsel is involved, the Forensic Accountant should be retained by counsel so that the privilege which exists between the client and counsel will be extended to the work product of the Forensic Accountant.

Question No 2:-

a. How Should the Investigation Objectives Be Defined?

Answer:-

How Should the Investigation Objectives Be Defined? Investigation either proposed or performed. As an example of a detailed issue pertaining to scope, in some investigations e-mail is obtained by “copying” the relevant server files. The audit firm’s forensic team might suggest that hard drives found on personal computers, portable mass storage devices like pen drives, personal digital assistants, and the like be imaged instead of simply copied, so that files not retained on the servers as well as deleted files are captured.

Audit partners may use their firm's forensic accounting investigators to assist in a variety of ways, including:

- Receiving detailed reports of questions and facts discovered by 10A counsel:

Attending selected interviews with 10A counsel and/or counsel's forensic accounting advisers may be appropriate in some situations as well. Expanding the audit tests of certain accounts

- Attending updates meetings called by 10A counsel to advise on the progress of an investigation

If the forensic accounting investigators are from the audit firm, the firm may expect to be involved in the procedures and findings at every stage. Some counsel and boards view this as a barrier to hiring the audit firm's forensic accounting investigator to conduct the investigation; however, no matter who completes the investigation, critical information must still be communicated to the auditors.

Stockholders may become concerned once suggestions of financial impropriety surface. They may file a class-action lawsuit with the objective of extracting the largest possible settlement from the company and other parties, including the external auditors.

The company's lenders are likely to be concerned about their exposure to losses. The investigation may take place during a period of financing negotiations and may therefore need to address the lenders' objectives.

The public at large may feel some degree of vested interest in the investigation, particularly if the entity is a public, quasi-public, or charitable organization or if it is a significant regional employer. These concerns are often reflected in and fed by media attention, and they create pressure to "get to the bottom quickly."

HOW SHOULD THE INVESTIGATION OBJECTIVES BE DEFINED?

Forensic accounting investigators should develop a plan that offers the client investigative alternatives. The investigation should obviously focus on the facts that cause concern, with the ultimate objective of determining if an illegal act has been committed. In their quest to achieve the objectives of the investigation, forensic accounting investigators must be mindful that they are governed by the ethical principles and other guidelines of the authoritative professional organization(s) to which they belong—be it the American Institute of Certified Public Accountants, the Association of Certified Fraud Examiners, or both.

The forensic accounting investigator should recognize that auditors may be apprehensive when confronted with issues of fraud—and appropriately so. Sensitivity to auditors' concerns will go a long way toward easing their natural disquiet when it is determined that the company has begun an investigation to evaluate allegations of fraud. Keeping auditors

informed in an appropriate manner, agreed to by the client, will help ensure the efficiency of the financial statement audit.

In earlier chapters of this book, the issue of financial statement materiality has been raised more than once. In the course of an audit, numerous immaterial variances and adjustments are identified, documented in the working papers, and never adjusted on the books and records of the company. This is appropriate and consistent with auditing standards. Materiality is a filter that allows the auditors to work efficiently and effectively. In the course of a financial investigation, however, a small fact, immaterial under normal circumstances, may have a critical bearing on the overall investigation

b. WHO SHOULD DIRECT THE INVESTIGATION AND WHY?

Answer:-

A ship has but one captain and, generally, a company's audit committee must proactively lead the investigation. Forensic accounting investigators follow the evidence wherever it leads and communicate their findings to the audit committee or to the committee's designee, such as counsel, whose decisions direct the conduct of the investigation. While the external auditors must be satisfied that the audit committee has directed a proper investigation, they neither direct the investigation nor decide what remedial actions are required by the circumstances.

Financial crime investigations are fraught with uncertainty, and a wrong move can produce harmful results. Audit committees recognize the value of consulting with a competent team of advisers, including counsel and forensic accounting investigators. A forensic accounting investigator working for an audit committee that does not seek advice or that interferes with the investigation would be well advised to resign the assignment.

In the course of an investigation, a time may come when the forensic accounting investigator is alone in advocating a certain course of action or series of procedures.

Suppose the audit committee interprets whistle-blower allegations as implicating the revenue recognition practices of the company but not policies involving the deferral and amortization of related marketing costs, and the forensic accounting investigator disagrees? What is the forensic accounting investigator to do? The evidence should be the driving force in determining the scope and course of the investigation. On one hand, in situations of this kind, be insistent. Historically, materiality has been evaluated primarily by using quantitative measurement standards such as X percent of total assets or net income. In 1999, however, the SEC released Staff

Accounting Bulletin 99 (SAB 99), which reemphasized the view that materiality, should be evaluated from a qualitative as well as a quantitative standpoint. View at while following the standards, methodologies, and practices that experience suggests are most appropriate in the circumstances. On the other hand, unlike decisions about the scope of the audit procedures—which rest solely with the auditors—decisions about the adequacy of an investigation's scope rest with the audit committee. Typically, the best and most practical use of a forensic

accounting investigator is to conduct sufficient procedures to unambiguously resolve the allegations. This is the clearest outcome of an investigation. There is, of course, another outcome: “We conducted our investigative procedures and noted no evidence of fraud.” This may or may not be acceptable, depending upon whether the investigation was robust and thorough. A no-fraud-found result could amount to a comfort level consistent with the objective of the investigation at its outset: that of resolving the allegations. Or, if those who evaluate the outcome of the investigation—such as the auditors or the SEC—conclude that procedures were not robust and thorough, it will be difficult for them to arrive at a satisfactory comfort level with a finding of no fraud. In situations in which a no-fraud finding is the investigative result, the adequacy of the scope is often a key element in justifying the conclusion.

Ideally, the forensic accounting investigator should have significant influence over procedures pertaining to the financial aspects of the investigation.

Counsel should obviously take responsibility for the legal aspects of the matter and support the efforts of the forensic accounting investigator by providing appropriate guidance. The audit committee should rely on these and other professionals, but in the end it is the audit committee’s investigation. The committee must take ownership, albeit with the advice of other parties in the core team that influences the direction of investigation. These may include forensic accounting investigators, legal counsel, internal and external auditors, and possibly others such as a public relations firm. Conferring early and often is routine in these matters and should be strongly encouraged by the forensic accounting investigator.

Question No 3:-

What is the BASIC ELEMENTS TO CONSIDER FOR INCLUSION IN A REPORT OF INVESTIGATION?

Answer:-

- Identify your client:

[Firm] was engaged by Cutting Edge Technology Corporation (the “Company”).

- In the case of a lawsuit, identify the parties: I, [forensic accounting investigator’s name], have been retained by [name of law firm] (“Counsel”) to investigate certain of the claims and allegations made by Philip Hart (“Hart”), John Harrington (“Harrington”), and Robert Geller (“Geller”) against Peter Langley (“Langley”).

- State in broad terms what you were asked to do—for example, “to provide expert testimony or investigate certain allegations”:

. . . to provide forensic accounting investigation services in order to assist in pursuing your concerns related to certain allegations made against Jane

- Describe your scope, including the time period examined:

I was engaged to perform investigative procedures related to review of the

Company's purchasing and receiving policies and practices in effect over fiscal years 2001–03. We have performed background checks of certain employees at the direction of [name of outside counsel], reviewed and analyzed certain of the Company's accounting records and other documents, performed various data mining and data interrogation of the Company's electronic files, and conducted interviews of current and former Company employees.

- Include mention of any restriction as to distribution and use of the report:

This report was prepared in connection with the aforementioned matter and is intended solely for your information. It may be used only for the purposes of this engagement and may not be used for any other purpose without our written consent.

- Identify the professional standards under which the work was conducted:

We performed our work in accordance with the American Institute of Certified Public Accountants' ("AICPA") Statement on Standards for Consulting

- Identify exclusions in the reliance on your report:

Our work does not constitute either an audit performed in accordance with the AICPA's generally accepted auditing standards or an attestation service.

We make no representation as to the adequacy of our procedures for your purposes.

- State that your work should not be relied on to detect fraud:

Fraud and irregularities by their very nature are most often hidden, and no absolute assurance can be given that all such matters will be detected. Our engagement cannot be relied on to disclose all irregularities or illegal acts, including fraud that may exist. During the course of this engagement, we will inform you of any such matters that come to our attention unless they are clearly inconsequential.

- Include the procedures you performed, technical pronouncements relied upon, and findings:13

12. You might consider indicating that if you are presented with a subpoena, you will inform the client that you intend to comply unless the client makes court filings in an attempt to quash the subpoena.

13. If appropriate, also perhaps include the implications of your observations and findings.

SUMMARIZING YOUR FINDINGS

A summary can be helpful to the reader but may be perilous for the report writer in terms of keeping critical information and perspectives intact. Caution is advised when preparing two types of summary sections: executive summary and conclusion. We do not recommend writing a summary conclusion. If for any reason you nonetheless do so, be careful not to offer an opinion on the factual findings unless specifically requested to do so. The facts should speak for themselves. It may be appropriate to position in a concluding section of the Report of

Investigation certain recommendations for additional investigative procedures or a description of control breakdowns you have observed.

Again, while we do not recommend summary conclusions, a carefully written executive summary at the beginning of the report can be extremely helpful to the reader, especially when it precedes a long and complex report. The executive summary should offer in simple, straightforward language an accurate statement of significant findings. Each summarized finding should include a reference to the full description of findings included in the complete Report of Investigation.

Question No 4:-

What MISTAKES should you AVOID IN REPORTING?

Answer:-

A MISTAKES TO AVOID IN REPORTING

The following brief discussions highlight and review issues raised earlier in this chapter.

Mistakes to Avoid in Reporting

AVOID OVERSTATEMENT

In the memorable TV series *Dragnet*, Sgt. Joe Friday used to say, “Just the facts, ma’am.” The same holds true when it comes to reports of investigation. The closer one sticks to the facts, all the facts, and just the facts, without embellishment, the better the report. The facts should speak for themselves. This is not to say that all facts are created equal: some facts are smoking-gun discoveries—for example, memos demonstrating both knowledge and intent. However, even in respect of obviously important facts, be careful not to overstate them.

AVOID OPINION

Other than the engagement to serve as an expert witness in a civil matter, the forensic accounting investigator should not offer opinions about the matter at hand. Also, opinions as to the intent or culpability (in criminal matters) of certain persons or as to whether an act was in fact a fraud should be avoided. These are matters to be decided by the trier of fact based on the factual material gathered and presented by the forensic accounting investigator. The forensic accounting investigator should not endeavor to influence the outcome beyond presenting the findings of the investigation in a clear and logical order.

Question No 5:-

How would you distinguish forensic accounting, fraud auditing, and investigative auditing from financial auditing?

Answer:-

A. The distinction is related to one’s goals. Financial auditing attempts to enable the auditor to render an opinion as to whether a set of statements upon which the opinion is rendered are always the representations of management. The auditor is primarily concerned with qualitative

values (hence the concept of materiality comes into play) and generally is not concerned about whether the financial statements communicate the policies, intentions, or goals of management.

B. Forensic accounting is a general term used to describe any financial investigation that can result in a legal consequence. Fraud auditing is a specialized discipline within forensic accounting, which investigates a particular criminal activity, namely fraud. Investigative auditing involves reviewing financial documentation for a specific purpose, which could relate to litigation support and insurance claims as well as criminal matters.

C. The objective of financial auditing is to provide the auditor with a degree of assurance in giving an opinion with respect to a company's financial statements. The materiality level of an investigative auditing engagement is much lower and more focused than that of the normal financial auditing engagement.
