

## FORENSIC AUDIT<sup>1</sup>

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Forensic is derived from the Latin word forensic, meaning "of the court". As a term, it refers to the disciplines that help to clarify the incidents which involve criminal activity and contribute to the enabling of material facts to be uncovered. In this context, forensic accounting and forensic auditing are sub-disciplines that aim to discover and elucidate financial crimes.

Forensic audit and forensic accounting are closely related concepts. Forensic accounting is for the purpose of providing the courts with an analysis of financial transactions that are allegedly criminal. Forensic audit may be considered one of the functions of forensic accounting. From the public audit perspective, forensic audit is aimed at detecting financial crimes including corruption, embezzlement, extortion and bribery.

The mind-set, approach and methodology of forensic audit are fundamentally different from those of financial audit. While financial audit may be defined as rendering an opinion on the reliability and integrity of financial reports and statements; forensic audit is a type of activity carried out in order to reveal the evidence that will constitute the basis for criminal cases involving financial transactions

of individuals or institutions. The concepts of materiality and reasonable assurance which constitute integral parts of financial auditing, are set aside in forensic auditing as every financial transaction which is deemed to be connected to fraud is investigated regardless of materiality threshold if there is an element of criminal activity. Another crucial point to note is that forensic audit inevitably entails a relatively more adversarial stance compared with financial audit and therefore requires a different mind set. It may be psychologically challenging for an auditor to conduct these two types of audit simultaneously.

Although criminal elements may be encountered as a result of traditional financial audits, the central theme of forensic audit is to reveal financial crimes. The Turkish Penal Code imposes a duty on public officers to report any crime they are witness to or those reported to them. Similar regulations exist in many countries<sup>2</sup>. Confronted with such a situation, the auditor should notify the relevant authorities before continuing with the audit procedures. By definition, the audit service that starts at this stage and is carried out for the sole purpose of collecting evidence falls within the scope of forensic audit.

<sup>2</sup>Kenneth M Dye, *Corruption and Fraud Detection by Public Sector Auditors* (2007) 36 EDPACS 6, 309.

## Forensic Audit and the Legal Mandate of SAIs

Not all financial irregularities warrant a forensic audit, but all financial crimes eventually and invariably distort integrity and accuracy of financial statements. SAIs in general have broad mandates to ensuring compliance with regulations<sup>3</sup> and forensic audit is one of the ways to achieve this. Article 36(2) of the Law No. 6085 on Turkish Court of Accounts establishes, inter alia, “determining whether revenues, expenditures and assets of public administrations, as well as accounts and transactions pertaining to those are in compliance with laws and other legal arrangements” as an element of regularity audit.

According to Article 78 of said law, “In the event of encountering an action involving crime in the course of audits and examinations; the evidence shall immediately be identified, and the case shall be reported to the Presidency of Turkish Court of Accounts by the auditor.” Per the Article, the process of collecting, identifying and analysing evidence fit squarely into the very definition of forensic audit.

### INTOSAI Standards:

INTOSAI standards do not specifically and explicitly mention forensic audit. Most closely connected INTOSAI document is the GUID 5270 Guideline for the Audit of Corruption Prevention, yet this Guideline

does not cover fraud investigations.

## International Cooperation in the Field of Forensic Audit in the Public Sector

### a) The INTOSAI Working Group on Fight Against Corruption and Money Laundering

The INTOSAI Working Group on Fight against Corruption and Money Laundering (WGFACML), is the most prominent international cooperation platform in forensic audit in the public sector. The Working Group held its 14th and last meeting virtually on 24 November 2020. 32 SAIs are currently members of this Working Group.

### b) A UN-INTOSAI Joint Project: Collection of Important Literature on Strengthening Capacities of Supreme Audit Institutions on the Fight against Corruption

The cooperation of the INTOSAI with the United Nations produced a collection of literature on the role of SAIs in the fight against corruption. This publication comprises of practical examples of best practice guides, audit types and methods, displaying how SAIs respond to fraud and corruption. In this publication, a whole section is devoted to forensic auditing in which SAIs of Japan, Italy, Brazil and Russia share their experiences, highlight prerequisites and lay out challenges with respect to forensic audit.

<sup>3</sup>International Journal of Government Auditing January 2000, Vol 27, s.8



**c) “Enhancing Compliance with International Standard of Supreme Audit Institutions and Forensic Audit” Workshops**

The Asian Development Bank organized three regional workshops on forensic audit for SAIs. First Regional Workshop on “Enhancing the Roles of SAIs in Selected ASEAN Countries” was held in Vietnam in March 2016, second Regional Workshop on “ISSAI Compliance and Forensic Audit” was held in place in October 2017. During these workshops, the participating SAIs exchanged views and experiences on forensic audit, among other topics.

**d) Status and activities of some SAIs regarding forensic audit**

- SAI India has a dedicated training institute as Centre of Excellence in Audit of Fraud, Fraud Detection Techniques and Forensic Audit<sup>4</sup>.
- United States General Accountability Office has established in 2005 its Forensic Audit and Special Investigations Unit (FSI).<sup>5</sup> Compared with other units, it has not only more extensive data-analysis capabilities but also utilizes more creative techniques in order to uncover financial crime.
- Tanzania, Philippines and Zambia SAIs have forensic audit units.

<sup>4</sup><https://www.asosajournal.org/role-of-sais-in-detecting-fraud-and-corruption-sai-india/>

<sup>5</sup><https://www.hsgac.senate.gov/media/majority-media/chairman-and-ranking-member-applaud-creation-by-gao-of-forensic-audit-and-special-investigations-unit-fsi>