

# Impact of Forensic Accounting in Jazan Industrial Zone

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**Abstract:** This paper presents an overview of impact of forensic accounting in Jazan industrial zone.

**Keywords:** Forensic Accounting, Sarbanes-Oxley, Earning Before Depreciation and Tax.

## 1. Introduction

Due to rapid increase of Financial frauds and White Collar Crimes, over the past few decades has boosted the implementation of Forensic Accounting. Although, there are many objectives, out of which survival is the most important factor. Since, the consequences of failure are always experienced by the Shareholders, Employees, Financial Institutions, Suppliers, Customers and the Society as a whole. In all economies, business failure is a reality of commercial life. However, there are evidences that Forensic Accounting, is becoming increasingly "a common" in many organizations (Aderibigbe, P., 2000; Satyanarayan, T., 2005; Oduala, J., 2005;). The purpose of this paper is to review the literature and the Impact of Forensic Accounting in Jazan Industrial zone which is expected to attract more than SAR100 billion and Creating 100,000 new jobs and out of which 12000 new jobs for Industrial zone. And in today's competitive environment, doing well is not guarantee for succeeding all the time and complacency is the greatest enemy of corporate progress. Furthermore, dramatic increase of Fraud/challenges over the last decade has directed the attention of management to see the basic causes of business failures. This research is based on the theoretical analysis as well as reference based, basic causes of business failures and parameters for detection of industrial sickness is discussed, which will help in solving the problem of corporate world.

## 2. Framework

At the current stage of research, the framework was divided into two part, first was empirical research and secondly the need to understand the meaning and concepts of forensic accounting, causes of business failures and parameters for the detection for industrial sickness is discussed. To keep the task meaningful and to provide the quality of the research work, studies published in refereed national/international journals, books, conference, working papers, annual reports, etc. were

considered.

## 3. Review of Literature

It's a misdeeds of Corporate which leads to implementation of Accounting Scandals, this misdeed generally involves misusing of funds in a direct or indirect form. In order to increase the revenue, WorldCom reduces the amount of money which was in its reserve (to cover its liabilities) by \$2.8 billion and shifted this money into the revenue, in its financial statements. WorldCom's losses its profit to the tune of \$ 1.38billions in 2001. In 2001, Enron Scandals exposed causing its stock to drop from nearly \$100 a share to less than \$1 a share (2001-2006 Wikipedia contributors). Michelle in 2008 pays \$200,858 to the Internal Revenue Service and \$825,400 as fine to the Brook and Leroy Inc. for federal wire frauds and also the tax evasion (Consuelo Herrera 2010). ACFE 2008 report to the nation that there was a losses of Asset Theft of \$150,000; Corruptions \$375,000; Fraudulent statements \$ 2,000,000; Annual loss of \$ 994 billion. In response to financial statement frauds and bankruptcy the federal government enact accounting and business laws including the Sarbanes-Oxley Act 2002, in which Chief Financial and Executives Officers are responsible for accuracy of financial statements, with significant fine and extensive prison terms for the violators. Saudi organization for certified Public Accountant in 2006 have expressed concern on the accounting related scandals in the Bishah Agriculture Development Company and Anaam International Holding company. Almoghawli (2001) shows a single accounting policy, namely the Zakat policy, in which relationship between the accounting treatment of Zakat by more than forty Saudi companies and incentives for the earnings management is taken. Aleshali (2006) shows a relationship between incentives for earnings management and aggregate accruals in which it was observed that in order to achieve the benchmarks, the managers of forty Saudi companies manipulate the accruals (Al-Moghawli, Mohammed 2010). Over 34 percent of 3877 business in 78 countries had been victimize of fraud over the last 12 months in 2011, reported by Prince water house coopers (PwC) said up to 30 percent of business in 2009 leading to loss over \$5million (3.7 million euros) to fraud in the said period. Saudi Arabia's Petro Rabigh, which is a joint venture of Saudi Aramco and Sumitomo Chemical, has reported a net loss of SR

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280.5m for the third quarter of 2011.

#### 4. Need for the Implementation of Forensic Accounting

In view of above literature, there is need for the implementation of forensic accounting in order to avoid frauds and white Collar crimes but before implementing this, there is urgent need to understand the meaning and concepts of forensic accounting. Several definitions are discussed; Webster's Dictionary defines forensic as "belonging to, used in, or suitable to courts of judicature or public discussion and debate." While, e-how contributor William Pirragila says that the forensic accounting is a strong combination of auditing procedures with an sophisticated investigation techniques, verifying the legitimacy and accuracy of financial reporting. Same Association of Certified Fraud Examiners quoted Forensic accounting as a use of professional accounting skills involving civil or criminal litigation, including but not limited to, generally acceptable accounting as well as audit principles, the determination of lost profits, income or damages, evaluation of internal controls, fraud, and any other matter involving accounting expertise in the legal system. While Black's Law Dictionary defines forensic accounting as "used in or suitable to courts of law or public debate." Therefore, we can say that "forensic accounting" is a litigation support involving accounting principles and techniques to detect errors or frauds. Similarly, West's Encyclopedia of American Law 2008 defines forensic accounting, sometimes called investigative accounting, involve the application of accounting concepts and techniques to legal problems. Horty defines Forensic Accounting as "The science that deals with the relation and application of finance, accounting, tax and auditing knowledge to analyze, investigate, inquire, test and examine matters in civil law, criminal law and jurisprudence in an attempt to obtain the truth from which to render an expert opinion." From this it is clear that forensic accounting is divided into two parts i.e litigation support; and investigation and dispute. Litigation only estimates the damages for the parties involve in legal disputes and also helps in solving it. While on the other hand investigation and dispute only shows the criminal matters, which is related to employee thefts, frauds including manipulation of financial statements, misappropriation of funds, Embezzlement of Cash, insurance frauds, etc in this matter there is a need how to minimize further damages and losses. There is an urgent need for the implementation of forensic accounting since the audit committee and internal audit could not trace out the different facts and other hidden aspects of corporate frauds and also because of poor or non-existent of Internal Control System.

#### 5. Parameters used for the Prediction of Sickness

In spite of loans given by the banks the industries faces the problems of sickness due to frauds; either just because off accrual based accounting i.e. treating Deferred revenue as earned revenue or in case of Accounts Receivables apart from it the analysts should also see whether the three parameters i.e Cash position, Net Working Capital and Net Worth of the

company shows a favorable sign or not, if it deviates from it then they should monitor the following Cash flow here cash flow represents the Earnings Before Depreciation and Tax (EBDT) (Ravi Kishore 2001)

#### 6. Reasons for Business Failure

A company ceases its trade because either the bank or creditors stops it. In such a cases, action is to be taken since the firm is unable to pay its debts or likely to be unable to pay in its near future. Why a firms gets this kind of situations? (Ravi Kishore 2001) from this it reveals that there are two levels of causes: The Accounting manifestations and the Root problems. The accounting manifestations of failures which covers: - too much working capital, Insufficient/ In proper working capital, too high interest charges, huge debt, giving high dividends, making a trading loss, selling parts of the firms at a loss and marginal profitability. If these sign appears several times it means that there is a danger sign. And root causes of failure mean: - not selling at a right price, buying useless/baseless assets, failure to control cost in direct or indirect form, failure to control working capital, reckless borrowing, etc. Again, if these things frequently appear then there is a need to take corrective actions.

Finally, it was observed from the above literature that Scandal/Frauds/Failure are becoming a common practices either in small scales or the large scale industries and since Jazan two thirds of the city has been allocated for industrial set up which is expected to be start functioning in the 2013, so the analyst should foresee all the factors which is discussed above and also try for the implementation of the Forensic Accounting, which is used as a common practice used in US in early 1995 and also the implementation of Sarbanes-Oxley Act of 2002, but now the stem of this specialization has yet to adopted in the Asian countries in order to protect from fraudulent practices and White Collar Crimes.

#### 7. Conclusion

This paper presented an overview of impact of forensic accounting in Jazan industrial zone.

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