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Adoption of Forensic Accounting Practices in Fraud Detection

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1. Introduction / Background

The study addresses the increasing threat of financial fraud and the corresponding need for forensic accounting as a response. In Sri Lanka, the use of forensic accounting is still emerging. The authors highlight a gap in knowledge and skills among accounting professionals in using forensic accounting for fraud detection (Abdulrahman, 2019). The study sets out to determine whether forensic accounting knowledge significantly impacts the ability to detect fraud within the Sri Lankan business context.

2. Literature Review

The review of literature in this study is segmented into three thematic areas: forensic accounting, fraud detection, and the relationship between forensic accounting and fraud detection. This division allows for a systematic exploration of theoretical foundations and empirical findings that support the study's focus on how forensic accounting knowledge impacts fraud detection in Sri Lanka (Alrawashdeh, 2021).

2.1 Forensic Accounting

Forensic accounting is a specialized field of accounting that merges accounting, auditing, and investigative skills to examine financial information suitable for legal proceedings. According to Crumbley, Heitger, and Smith (2005), forensic accounting is defined as accounting work that is suitable for use in a court of law. This characteristic distinguishes forensic accounting from other branches of accounting, as its primary goal is to uncover irregularities, misrepresentations, or financial crimes that can stand up to legal scrutiny.

Howard and Sheetz (2006) expand on this definition by describing forensic accounting as a process of interpreting and presenting complex financial data clearly and factually in legal forums. The application of forensic accounting is therefore not limited to identifying fraud but includes preparing litigation strategies, estimating economic damages, and detecting financial misrepresentation.

In practical terms, forensic accountants are employed by accounting firms, consulting agencies, legal bodies, insurance companies, and financial institutions. Their work typically involves investigative auditing, damage calculations, asset tracing, and fraud risk assessments. Bologna

(1984) highlighted the critical skills a forensic accountant must possess, including integrity, analytical ability, independence, objectivity, and strong communication skills.

Forensic accounting has grown rapidly due to increasing corporate scandals, public sector frauds, and global awareness of financial accountability. In response, educational institutions and accounting bodies are now incorporating forensic accounting into professional development programs. In Sri Lanka, this field is still in its infancy, with limited availability of training and certification programs. As the demand for transparent financial reporting increases, the integration of forensic accounting into mainstream accounting education is crucial.

Digabriele (2008) surveyed accounting professionals in the United States and identified a range of necessary skills for forensic accountants, such as analytical thinking, investigative aptitude, and legal knowledge. Similarly, Amiri and Babaei (2020) conducted a study in Iranian universities and emphasized the need to embed forensic accounting in the academic curriculum to meet growing demand. Their findings indicated a consensus among academicians and practitioners that forensic accounting plays a critical role in fraud detection and legal support.

The literature collectively points to the growing global recognition of forensic accounting as an essential domain in combating financial crimes. However, there remains a shortage of certified forensic accountants in developing countries like Sri Lanka, underscoring the importance of further studies in this area.

2.2 Fraud Detection

Fraud detection is a major area of concern in both public and private sector organizations, primarily due to the complexity and evolving nature of fraudulent activities. Fraud is broadly defined as an intentional act of deception for personal or financial gain. David (2005) emphasized that fraud is not merely a possibility but a probability in any organization, requiring constant vigilance and preventive measures.

According to Bello (2001), fraud is a generic term encompassing a wide array of criminal acts, including embezzlement, bribery, falsification of documents, and asset misappropriation. These acts often exploit weaknesses in organizational internal controls, accounting systems, or governance frameworks. Courts and regulators have struggled to provide a definitive classification due to the wide variability in types and methods of fraud, which are often creative and dynamic.

Traditional auditing methods, while useful, have often been criticized for their inability to detect sophisticated fraud schemes. The primary goal of conventional audits is to ensure financial statement accuracy and compliance with accounting standards. However, as Enyi (2009) argued, this often overlooks deeper investigative elements necessary to unearth intentional misstatements or hidden financial activities. Consequently, there is a growing need for forensic auditing approaches that incorporate skepticism, analytical techniques, and investigative tools.

Several scholars have attempted to identify the root causes of fraud within organizations. Ramaswamy (2005) linked fraud to poor corporate governance, flawed internal controls, and ineffective risk management systems. Dewi et al. (2020) conducted a study on fraud in local governments in Indonesia and concluded that the elements of "pressure," "opportunity," and "rationalization"—often referred to as the fraud triangle—are consistently present in fraud cases. Among these, pressure was found to have the greatest influence.

Fraud detection is therefore a multidimensional process requiring more than just routine checks. It involves profiling potential fraudsters, understanding organizational behavior, monitoring anomalies in financial reports, and leveraging advanced tools such as data mining and predictive analytics.

In the Sri Lankan context, however, the literature on fraud detection is sparse. Bandara et al. (2015) examined the role of internal control systems in Sri Lanka and found that strong internal controls and management integrity significantly reduce the risk of financial statement fraud. The study suggested that while detection mechanisms are slowly evolving, they are not yet adequate to handle sophisticated fraud cases.

Overall, the body of research indicates a growing realization that enhanced fraud detection mechanisms—particularly those informed by forensic accounting—are essential in the modern financial landscape.

2.3 Relationship Between Forensic Accounting and Fraud Detection

The link between forensic accounting and fraud detection has been extensively examined in international contexts, with numerous studies concluding that forensic accounting is more effective than traditional audit techniques in identifying fraud. This is particularly relevant in environments where fraud risk is high, and traditional audits may not uncover deeper, concealed irregularities.

Okoye and Gbegi (2013) conducted a study in Nigeria and found that forensic accounting is significantly more effective in detecting managerial fraud than conventional auditing methods. Their research indicated that forensic accountants' investigative approaches help identify and prevent high-level fraudulent activities that may not be visible through standard audits.

Similarly, Oyebisi et al. (2018) studied the Nigerian banking industry and observed that awareness of forensic accounting was low, but where applied, it led to a significant reduction in fraudulent practices. Their findings reinforced the need for increased awareness and training in forensic techniques across the industry.

Johnson et al. (2014) also explored the influence of forensic accounting knowledge and mindset on fraud risk assessment. They concluded that professionals equipped with forensic skills demonstrated higher performance in fraud-related tasks compared to those with only traditional accounting backgrounds.

In Sri Lanka, the relationship between forensic accounting and fraud detection is still under-researched. Priyangika and Bandara (2017) attempted to bridge this gap by examining education, practice, and perception of forensic accounting. Their study revealed an increasing demand for forensic accountants due to the rising complexity of financial crimes, but also highlighted the limited integration of forensic content in existing accounting curricula.

The current study by Walakumbura and Dharmarathna (2022) contributes to this growing body of knowledge by empirically testing the effect of four key variables—accounting skills, legal background, knowledge of procedures, and forensic accounting knowledge—on fraud detection. Using regression analysis, the authors found that forensic accounting knowledge, accounting skills, and procedural knowledge had significant positive effects on fraud detection. Interestingly, legal background did not show a significant influence, suggesting that practical, technical skills may be more important than legal theory in fraud identification.

These findings align with global literature and provide critical insights into the Sri Lankan context. They support the argument that forensic accounting plays an essential role in fraud detection and should be more widely adopted across industries. Additionally, the results highlight the need for skill development, policy change, and educational reform to promote forensic accounting as a proactive fraud deterrence mechanism.

The literature reviewed illustrates the growing importance of forensic accounting in detecting fraud, especially in environments where traditional audits are insufficient. Forensic accounting is a robust, investigative tool that combines accounting expertise with legal and procedural knowledge to uncover fraudulent activities. The review also underscores the inadequacy of traditional methods in identifying complex fraud and the urgent need for forensic approaches in countries like Sri Lanka.

Although international research provides a strong foundation, the Sri Lankan literature remains limited, emphasizing the relevance of the present study. By focusing on how forensic accounting knowledge impacts fraud detection, this research contributes meaningfully to the local academic and professional discourse. It calls for a more structured and strategic integration of forensic accounting in both education and professional practice to strengthen Sri Lanka's financial reporting and fraud mitigation frameworks.

3. Main Themes / Topics / Concepts

The study is structured around four independent variables and their impact on fraud detection:

- Accounting Skills
- Knowledge of Procedures
- Legal Background
- Forensic Accounting Knowledge

The research hypothesizes that each of these variables has a significant impact on the dependent variable—fraud detection.

Methodology

- **Data Collection** - Structured questionnaires from 165 Sri Lankan accounting professionals.
- **Statistical Tools** - Descriptive statistics, factor analysis, and multiple regression analysis using SPSS.
- **Conceptual Framework** - A model was developed to test the four variables.

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4. Findings and Discussion

This section presents the key empirical findings of the study and interprets them in light of both statistical evidence and existing literature. The research sought to evaluate the impact of forensic accounting knowledge and associated competencies on the detection of fraud in the Sri Lankan context. The analysis was conducted using multiple regression techniques based on responses from 165 professional accountants. Four key independent variables were tested: accounting skills, knowledge of procedures, legal background, and forensic accounting knowledge.

Key Findings

The results of the regression analysis revealed the following

- Knowledge of procedures demonstrated the strongest influence on fraud detection ($\beta = 0.556$, $p = 0.000$). This implies that procedural knowledge—such as data analysis, investigative methods, and reporting mechanisms—is central to identifying and addressing fraudulent activities.
- Accounting skills were also found to have a significant positive impact ($\beta = 0.286$, $p = 0.000$), suggesting that a sound foundation in core accounting practices, including interpretation of financial statements and transaction reviews, is critical for uncovering financial irregularities.
- Forensic accounting knowledge had a positive and statistically significant impact as well ($\beta = 0.117$, $p = 0.012$), highlighting the value of specialized training in forensic accounting methods for enhancing fraud detection capacity.
- In contrast, legal background did not have a statistically significant effect on fraud detection ($p = 0.240$), indicating that while knowledge of the legal system may complement forensic efforts, it does not independently contribute significantly to detecting fraud in the Sri Lankan setting.

Interpretation of Findings

The findings offer several key insights into the competencies that are most effective in fraud detection in Sri Lanka. Notably, knowledge of procedures emerged as the most influential variable. This suggests that fraud detection is primarily operational in nature, relying heavily on professionals' familiarity with detection techniques, control systems, and investigative methodologies. Professionals who understand how to trace transactions, interpret suspicious patterns, and apply forensic tools are better equipped to uncover fraud.

Accounting skills, though more general in nature, also showed a meaningful effect. This is consistent with the idea that fraud often originates from manipulation or concealment within financial statements. Thus, those with strong accounting acumen can identify inconsistencies or red flags that may indicate fraudulent activity.

Forensic accounting knowledge, while not as dominant as the other two, still made a statistically significant contribution. This demonstrates the importance of having specialized knowledge in areas such as litigation support, evidence gathering, and the use of digital tools. It reinforces the argument that forensic accounting is not simply an extension of traditional accounting but a unique discipline with its own methodologies and investigative scope.

On the other hand, legal background was not found to be a significant predictor. While legal awareness may support the process of preparing fraud-related cases for court proceedings, it appears that legal knowledge alone does not directly facilitate the detection of fraud. This finding suggests that the application of legal principles, although important for the prosecution of financial crimes, is less relevant at the initial stages of identifying those crimes. In Sri Lanka, this may reflect the structure of the professional environment, where legal proceedings are often handled separately from accounting and investigative work.

Supporting Literature

The results of this study are consistent with several international research findings that emphasize the importance of specialized forensic accounting skills over legal knowledge in fraud detection.

For example, Hamdan (2018) highlighted the growing global need for forensic accounting to combat rising fraud incidents. His study demonstrated that accounting professionals equipped with forensic knowledge were more effective in detecting fraud than those without such expertise. This aligns with the current study's finding that forensic accounting knowledge significantly contributes to fraud detection outcomes.

Similarly, Oyebisi et al. (2018) conducted research in the Nigerian banking industry and observed that a low level of awareness about forensic accounting correlated with higher instances of fraud. Where forensic practices were implemented, fraud detection and prevention rates improved significantly. This supports the finding that procedural knowledge and specialized forensic training enhance fraud identification.

Moreover, Okoye and Gbegi (2013) emphasized that forensic accountants were more successful in detecting management-level fraud compared to traditional auditors. Their study noted that traditional audits, which primarily focus on compliance, are often inadequate in uncovering complex fraud schemes. This observation parallels the current study's conclusion that accounting skills and investigative procedures play a much greater role in fraud detection than general legal knowledge.

Implications

These findings have practical implications for accounting professionals, educators, and policymakers in Sri Lanka. To enhance the country's capacity to detect and mitigate fraud, training programs should place greater emphasis on the development of procedural and forensic accounting skills. Professional accounting bodies such as CA Sri Lanka, as well as universities and training institutes, should consider integrating forensic accounting modules into their curricula.

Additionally, organizations should prioritize hiring or upskilling staff with these competencies, particularly those involved in auditing, compliance, and financial reporting. Finally, while legal knowledge remains an important supplementary skill, it should not be viewed as a substitute for practical forensic training.

5. Conclusion

The study concludes that forensic accounting is an essential tool for fraud detection in Sri Lanka. Accounting skills, procedural knowledge, and forensic expertise significantly contribute to identifying and mitigating fraud, while legal background does not show a direct effect. The findings suggest a need to incorporate forensic accounting into academic curricula and professional training in Sri Lanka to build a workforce capable of addressing financial crime effectively.

Policy Implications

- Academic institutions and professional bodies in Sri Lanka should develop curricula and certifications focusing on forensic accounting.
- Organizations should prioritize hiring accountants with forensic skills.
- Future research should explore the integration of technology and forensic tools in fraud detection.

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