FORENSIC ACCOUNTING: A STRATEGIC TOOL TO STRENGTHEN CORPORATE GOVERNANCE AGAINST FRAUD

Aggelia Xanthopoulou [*], Petros Kalantonis [*], Panagiotis Arsenos [*], Christos Kallandranis [*]

[*] University of West Attica, Athens, Greece

OPEN ACCESS

How to cite: Xanthopoulou, A., Kalantonis, P., Arsenos, P., & Kallandranis, C. (2023). Forensic accounting: A strategic tool to strengthen corporate governance against fraud. In E. Karger & A. Kostyuk (Eds.), *Corporate governance: An interdisciplinary outlook* (pp. 33–38). Virtus Interpress. https://doi.org/10.22495/cgaiop7

Received: 15.10.2022
Accepted: 24.10.2022
Keywords: Forensic Accounting, Corporate Governance and Fraud
JEL Classification: G30, G34, M41, M42
DOI: 10.22495/cgaiop7

Abstract

Various economic scandals involving fraud of all kinds hurt both developed and developing economies due to their negative economic impact (Bhasin, 2013). Companies in public and private sectors operate in an environment that is not free of fraud. Until 2010, the most pressing issues in the corporate world were the theft of physical assets, misuse of data due to untrue accounting reports and financial misreporting (Organisation for Economic Co-operation and Development [OECD], 2014). Today corporate fraud became more sophisticated and the biggest threat is fraudulent activities connected to technology and the internet. The technological evolution changes rapidly the nature of the modern economy and its digital transformation created great vulnerability to the economic environment (Ernst & Young [E&Y], 2018). All companies face a certain level of digital fraud which has become an essential cost of doing business (Deloitte, 2021c). According to PwC's Global Fraud Survey (PwC, 2022), cybercrime, customer fraud and asset misappropriation are the most prevalent types of fraud. As result companies began paying more attention to the effectiveness of their internal control system and corporate risk management. The need to

avoid creating opportunities for fraudsters compels them to implement risk elimination and fraud detection measures.

Corporate leaders prioritize the establishment of preventive measures and contingency plans in order to protect the company from fraudulent activities, preserve its integrity, safeguard the company's assets and ensure the efficient operation of the business. They start taking compliance with anti-corruption legislation more seriously and alter their antifraud policies in response to it. The increased concerns about the control environment effectiveness and anti-fraud policies in order to eliminate and mitigate fraud affect the quality of corporate governance. Good corporate governance yields increased investment, improved capital market access, increased asset value, job creation, economic growth and sustainable development (Inairat, 2015).

The lack of honesty, accountability and transparency in governance is one of the primary reasons for the emergence of criminal activities (Farber, 2005). Fraudulent behavior damages business financially influences negatively the decision-making process of investors and governance bodies and undermines public trust in them. The major component of dependable corporate governance to combat fraud is the implementation of an effective internal control system that includes external audit activities, internal audit function, fraud risk assessment and forensic accounting (FA) services (Rehman & Hashim, 2018). Efficient audit activities ensure the consistency of the financial reporting process, guarantee its credibility and enable companies to achieve their profitability objectives (Bhasin, 2017).

Governance bodies' commitment to control mechanisms determines the level of corporate fraud and their willingness to fight it (Eko et al., 2020). In order for a business organization to remain competitive and survive, its structure must be based on all its members' ethical and moral conduct and ensure ethical standards through its oversight activities (He et al., 2009). The structure of governance bodies affects the company's effectiveness and financial integrity concerning fraud. According to numerous studies, the occurrence of fraudulent activities is significantly related to ownership structure, board of director's and audit committee's composition and characteristics and the role of chairman and chief executive officer (CEO) (Beasley, 1996; Farber, 2005; Smaili & Labell, 2007; Sharma, 2004; Chen et al., 2006; Klein, 2002; Vafeas, 2000; Persons, 2009; Owens-Jackson et al., 2009; Mustafa & Meir, 2006; Alwi et al., 2013).

FA is the best audit option for controlling, eliminating and mitigating fraud (Rehman & Hashim, 2020). It has a proactive role in identifying deficiencies and internal control weaknesses and can successfully adopt and implement a corruption prevention plan (Siregar & Tenoyo, 2015). The use of FA techniques to analyze accounting and financial data improves the quality of the financial reporting system and strengthens audit independence (Eyisi et al., 2014). It guarantees the reliability of economic data by identifying patterns and suspicious transactions, detecting and minimizing accounting frauds and eliminating their existence. It is responsible to oversee and conduct investigations in the business environment in order to improve governance procedures' qualities concerning fraud. Corporate leaders rely on FA to develop a consistent corporate governance system because it ensures that their policies and objectives are intertwined with the internal control system. FA is a strategic tool to strengthen corporate governance against fraud.

The aim of the present study is to highlight the framework of FA implementation to combat fraud risks and crimes and improve corporate governance's effectiveness in fraud defense. It examines the techniques, knowledge and skills and the interaction of FA and corporate governance in eliminating fraudulent activities. FA guarantees the reliability of financial reports, enhances their accountability and thus has a significant positive impact on corporate governance accountability.

REFERENCES

1. Akinbowale, O. E, Klingelhofer, H. E., & Zerihun, M. F. (2020). An innovative approach in combating economic crime using forensic accounting techniques. *Journal of Financial Crime, 27*(4), 1253–1271. https://doi.org/10.1108/JFC-04-2020-0053
2. Al Abbadi, M. H., Alrawashdeh, B., Dadaghia, N. M., & Darwazeh, N. R. (2021). The challenges of application of forensic accounting in Jordan. *Academy of Strategic Management Journal, 20*(2, Special Issue), 1–10. https://www.abacademies.org/articles/the-challenges-of-application-of-forensic-accounting-in-jordan-11137.html
3. Alwi, M., Risda, K., Gajah, A., Ismail, W. A. W., & Kamarudin, K. A. (2013). The effectiveness of audit committee in relation to financial reporting fraud. In *Proceeding of the 5th International Conference on Financial Criminology (ICFC)* (pp. 332–344).
4. Balios, D., Tantos, S., Eriotis, N., & Vasiliou, D. (2020). The conjunction of tax auditing mechanism with behavioral and institutional parameters of tax evasion: The role of accounting rules and forensic accounting. *European Journal of Accounting, Auditing and Finance Research, 8*(2), 59–80. https://doi.org/10.37745/ejaafr/vol8.no2.pp59-80.2020
5. Beasley, M. S. (1996). An empirical analysis of the relation between the board of director composition and financial statement fraud. *The Accounting Review, 71*(4), 443–465. https://www.jstor.org/stable/248566
6. Bhasin, L. M (2013). Corporate governance and forensic accountants' role: Global regulatory action scenario. *International Journal of Accounting Research, 1*(1). https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2676468
7. Bhasin, L. M. (2017). Integrating corporate governance and forensic accounting: A study of an Asian country. *International Journal of Management Sciences and Business Research, 6*(1), 31–52. https://ssrn.com/abstract=2912728

8. Chen, G., Firth, M., Guo, D. N., & Rui, O. M. (2006). Ownership structure, corporate governance, and fraud: Evidence from China. *Journal of Corporate Finance, 12*(3), 424–448. https://doi.org/10.1016/j.jcorpfin.2005.09.002
9. Das, P. K. (2020). Forensic accounting in India. *Journal of Business and Social Science Review, 1*(5), 59–66. https://jbssrnet.com/wp-content/uploads/2020/06/7-1.pdf
10. Deloitte. (2021c). *The nature of fraud is changing: Act now to bear it* (Report). https://www2.deloitte.com/uk/en/pages/financial-advisory/articles/the-nature-of-fraud-is-changing.html
11. Deloitte. (2021a). *Global risk management survey: A moving target: Refocusing risk and resiliency amidst continued uncertainty* (12th ed.). https://www2.deloitte.com/content/dam/Deloitte/rs/Documents/risk/rs_Global-risk-management-survey-12th-edition.pdf
12. Deloitte. (2021b). *Middle East fraud survey*. https://www2.deloitte.com/content/dam/Deloitte/xe/Documents/finance/me_fraud-survey-2021.pdf
13. Eko, U. E., Adebisi, A. W., & Moses, J. E. (2020). Evaluation of forensic accounting techniques in fraud prevention/detection in banking sector in Nigeria. *International Journal of Finance and Accounting, 9*(3), 56–66. http://article.sapub.org/10.5923.j.ijfa.20200903.02.html
14. Ernst & Young (EY). (2018). *15th global fraud survey 2018*. https://assets.ey.com/content/dam/ey-sites/ey-com/en_gl/topics/banking-and-capital-markets/bcm-pdf/ey-global-fids-fraud-survey-2018.pdf
15. Eyisi, A. S., & Ezuwore, C. N. (2014). The impact of forensic auditors in corporate governance. *Research Journal of Finance and Accounting, 5*(8), 31–39. https://iiste.org/Journals/index.php/RJFA/article/view/12353/12728
16. Eze, E., & Okoye, E. I. (2019). Forensic accounting and fraud detection and prevention in Imo State Public sector. *Accounting and Taxation Review, 3*(1), 12–26. https://www.atreview.org/admin/12389900798187/ATR%203_1_%2012-26_pdf.pdf
17. Farber, D. B. (2005). Restoring trust after fraud: Does corporate governance matter? *The Accounting Review, 80*(2), 539–561. https://doi.org/10.2308/accr.2005.80.2.539
18. Hashem, F. (2021). The role of forensic accounting techniques in reducing cloud-based accounting risks in the Jordanian five stars hotels. *WSEAS transactions on business and economics*, 18, 434–443. https://doi.org/10.37394/23207.2021.18.44
19. He, L., Labelle, R., Piot, C., & Thornton, D. B. (2009). Board monitoring, audit committee effectiveness, and financial reporting quality: Review and synthesis of empirical evidence. *Journal of Forensic & Investigative Accounting, 1*(2), 1–41. https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1159453
20. In'airat, M. (2015). The role of corporate governance in fraud reduction — A perception study in the Saudi Arabia business environment. *Journal of Accounting and Finance, 15*(2), 119–128. http://www.m.www.na-businesspress.com/JAF/In_airatM_Web15_2_.pdf
21. Khersiat, O. M. (2018). The role of forensic accounting in maintaining public money and combating corruption in the Jordanian public sector. *International Business Research, 11*(3), 66–75. https://doi.org/10.5539/ibr.v11n3p66

22. Klein, A. (2002). Audit committee, board of director characteristics, and earnings management. *Journal of Accounting and Economics, 33*(3), 375–400. https://doi.org/10.1016/S0165-4101(02)00059-9
23. KPMG. (2019). *Global banking fraud survey 2019: The multi-faceted threat of fraud: Are banks up to the challenge?* https://home.kpmg/ua/en/home/insights/2019/12/fraud-banking.html
24. KPMG. (2022a, January). *A triple threat across the Americans: Fraud outlook*. https://assets.kpmg/content/dam/kpmg/xx/pdf/2022/01/fraud-survey.pdf
25. KPMG. (2022b, February). *Fraud barometer 2021: A snapshot of fraud in the UK*. https://assets.kpmg/content/dam/kpmg/uk/pdf/2022/02/fraud-barometer-2022.pdf
26. Lamba, J., & Jain, E, (2020). Forensic accounting: A way to fight, deter and detect fraud. *International Research Journal, 10*(1), Article 8280. https://doi.org/10.51611/iars.irj.v10i1.2020.106
27. Mustafa, S. T., & Meier, H. H. (2006). Audit committees and misappropriation of assets: Publicly held companies in the United States. *Canadian Accounting Perspectives, 5*(2), 307–333 https://doi.org/10.1506/CCWW-JRWB-ECUE-YMMN
28. Organisation for Economic Co-operation and Development (OECD). (2014). *Risk management and corporate governance*. https://doi.org/10.1787/9789264208636-en
29. Owens-Jackson, L. A., Robinson, D., & Shelton, S. W. (2009). The association between audit committee characteristics, the contracting process and fraudulent financial reporting. *American Journal of* Business, 24(1), 57–66. https://doi.org/10.1108/19355181200900005
30. Ozili, K. P. (2020). *Forensic accounting theory* (MPRA Paper No. 102566). Munich Personal RePEc Archive. https://mpra.ub.uni-muenchen./102566/1/MPRA_paper_102566.pdf
31. Perduv, V. V., Ceklic, J., & Ceklic, B. (2018). The role of forensic accounting in corporate governance for economic societies. *Business Studies, 10*(19–20), 119–131. https://poslovnestudije.com/arhiva/radovi2018eng/vedrana.vukovic.perduv2018eng.pdf
32. Persons, O. S. (2009). Audit committee characteristics and earlier voluntary ethics disclosure among fraud and no-fraud firms. *International Journal of Disclosure and Governance,6*, 284–297. https://doi.org/10.1057/jdg.2008.29
33. Polycarp, S. U. (2019). The role of forensic accounting in detecting economic crimes. *Research Journal of Finance and Accounting, 10*(16), 98–107. https://doi.org/10.7176/RJFA/10-16-11
34. PwC. (2020, September 24). *Gaps in the facade: Three actions business should take to fight fraud*. https://www.pwc.com.au/digitalpulse/global-economic-crime-fraud-survey-2020.html
35. PwC. (2022). *PwC's global economic crime and fraud survey*. https://www.pwc.com/gx/en/services/forensics/economic-crime-survey.html
36. Rehman, A., & Hashim, F. (2018). Literature review: Preventive role of forensic accounting and corporate governance maturity. *Journal of Governance and Integrity, 1*(2), 61–82.
37. Rehman, A., & Hashim, F. (2019). Impact of mature corporate governance on detective role of forensic accounting: Case of public listed companies in Oman. In *KnE Social Sciences, FGIC 2nd Conference on Governance and Integrity* (pp. 637–665). https://doi.org/10.18502/kss.v3i22.5080

38. Rehman, A., & Hashim, F. (2020). Can forensic accounting impact sustainable corporate governance? *Corporate Governance, 21*(1), 212–227. https://doi.org/10.1108/CG-06-2020-0269
39. Sahdan, M. H., Crowton, C. J., & Drake, J. E. (2020). Forensic accounting services in English local government and the counter-fraud agenda. *Public Money & Management, 40*(9), 1–10. https://doi.org/10.1080/09540962.2020.1714208
40. Sharma, V. D. (2004). Board of director characteristics, institutional ownership, and fraud: Evidence from Australia. *Auditing: A Journal of Practice and Theory, 23(*2), 105–117. https://doi.org/10.2308/aud.2004.23.2.105
41. Siregar, S. V., & Tenoyo, B. (2015). Fraud awareness survey of private sector in Indonesia. *Journal of Financial Crime, 22*(3), 329–349. https://doi.org/10.1108/JFC-03-2014-0016
42. Smaili, N., & Labelle, R. (2007). *Preventing and detecting accounting irregularities: The role of corporate governance* (Working paper, HEC). http://ssrn.com/abstract=1324143
43. Vafeas, N. (2000). Board structure and the informativeness of earnings. *Journal of Accounting and Public Policy, 19(*2), 139–160. https://doi.org/10.1016/S0278-4254(00)00006-5