

1.(Research Title)

The impact of the Fraud Examiners in the Fraud Risk Management in the Corporates in the United States.

تأثير فاحصي الاحتيال في إدارة مخاطر الاحتيال في الشركات الكبرى لدى الولايات المتحدة الأمريكية

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3rd Semester 2023 / 1445

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2.Introduction:

Fraud refers to obtaining benefits (goods/service / money) through illegal act, the cases committed by the company are corporate fraud, which usually arises from the fraud examiners findings, anonymous tip off, Suspicion, Compliant, whistleblower or allegation. (1), this kind of fraud is designed to give an advantage to the perpetrating individual or company. Fraud deals with events which involve criminal motives that mostly are difficult to identify, therefor risk management provides signs for the critical area in the corporate, so the corporate is more responsive in preventing fraud risk. Corruption, Bribery, Conflict of interest, are forms of fraud risk that causes the most losses to the corporate. In the late 2000s, many giant U.S. corporations were on the verge of collapse as a result of years of risky investing, these corporations employed thousands of workers and contributed billions of dollars to the global economy as a whole (2). Poor risk management leads to uncertain business performance or in the worst-case scenario, the collapse of the business. It is also important to know to which extent the risk can be mitigated if it occurs. (3) The role of fraud examiners in managing the risk in U.S. corporate is to identify improper conduct and the person in charge for preventing the fraud by sending a message throughout the organization that fraud will not be tolerate, determining the extent of potential liabilities or losses that might exist, helping the recovery of the losses, mitigating other potential consequences and strengthening internal control weaknesses, investigating/interrogation the fraudsters, examining fraudulent documents (forged, altered, fabricated and suspicious). (4) An entity's risk management program must be tailored to the specifics of the organization for it to be effective. While everyone within the corporate has the duty to help fight fraud the practical implementation of fraud risk management must start somewhere. The corporate must have a team of specific individuals or dedicated department to ensure the success of the fraud management and performs comprehensive fraud risk assessment to identify specific fraud schemes and risks, assess their likelihood and significance, evaluate existing fraud control activities, and implement actions to mitigate residual fraud risk. (5)

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1. Mansor, Noorhayati, and Rabiul Abdullahi. "Fraud triangle theory and fraud diamond theory. Understanding the convergent and divergent for future research." *International Journal of Academic Research in Accounting, Finance and Management Science* 1.4 (2015): 38-45.
 2. DEPERIO, G. (2021, Jul 21). Investopedia. Retrieved from <https://www.investopedia.com/ask/answers/040815/what-are-some-examples-moral-hazard-business-world.asp#toc-moral-hazard-in-salesperson-compensation>
 3. Forensic, K. P. M. G. "Fraud risk management." *New York, NY: KPMG* (2006).
 4. Dyck, Alexander, Adair Morse, and Luigi Zingales. "Who blows the whistle on corporate fraud?." *The journal of finance* 65.6 (2010): 2213-2253.
 5. Cordis, Adriana S., and Elizabeth M. Lambert. "Whistleblower laws and corporate fraud: Evidence from the United States." *Accounting Forum*. Vol. 41. No. 4. No longer published by Elsevier, 2017.

3. Research problem:

Q1. What is the definition of Fraud?

Fraud” is any activity that relies on deception to achieve a gain, It becomes a crime when it is a “knowing misrepresentation or concealment of the truth of a material fact to induce another to act to his or her detriment”

Q2. What is the Corporate Fraud?

Corporate fraud refers to illegal act by an individual or company that are done in unethical manner (1)

Q3. What are the categories of Fraud?

Fraud can be categorized in countless ways, but fundamentally, every type of fraud is either organizational or individual.

1. Fraud against individuals:

The fraudster’s target is the single person, it’s included identity theft, phishing scams, Ponzi scheme,

2. Fraud against organizations:

- a. Internal organizational fraud.
- b. External organizational fraud.

Internal organizational fraud:

When the employees, managers, even executives inside organization deceives the organization itself, by embezzlement, cheating on taxes, mislead the investors and shareholders, it sometimes called “occupational fraud”

External organizational fraud:

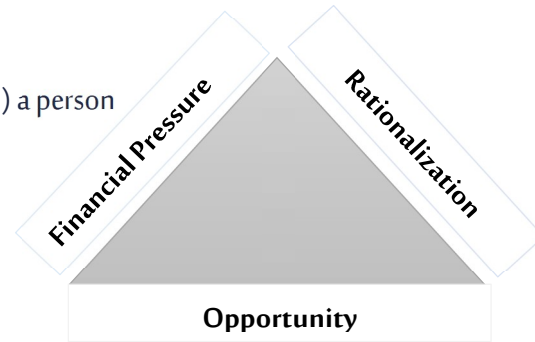
In this type of fraud, the fraudsters from outside, such as the cyber attack from the hackers to access the network, or when the customers submit a bad check. (2)

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1. Li, L., & McMurray, A. (2022). What Is Corporate Fraud?. In Corporate Fraud Across the Globe (pp. 3-22). Singapore: Springer Nature Singapore.
 2. Examiners, A. o. (2023). <https://www.acfe.com/>. Retrieved from <https://www.acfe.com/FRAUD-RESOURCES/FRAUD-101-WHAT-IS-FRAUD>

Q4.What's the reasons to commit Fraud?

The most accepted explanation for why some people commit fraud is known as the Fraud Triangle. The Fraud Triangle was developed by **Dr. Donald Cressey**, a criminologist whose research on embezzlers produced the term “trust violators.” (1)

If the three components are present (**Financial Pressure, Opportunity, Rationalization**) a person to a person, is highly likely to commit a fraudulent activity.



Assumption:

Person A is a salesman, he is under a **Pressure** because of his personal debt, a gambling problem, and his desire to live in the high lifestyle. He is also aim to achieve a sales target to be eligible for a good commission, he sees an **Opportunity** to commit fraud by making a fake sale at the end of the month only to achieve the target and then make return after the beginning of the next month. He knows that no one will notice the return in the next month, but he needs to **Rationalize** it to himself. By saying I deserve this, I'm only borrowing a little, I'll consider this in the next month... etc. These three factors lead Person A to commit fraud.

Q5.What is the Fraud Tree?

It classifies every type of internal organization fraud or occupational fraud as following: (2)

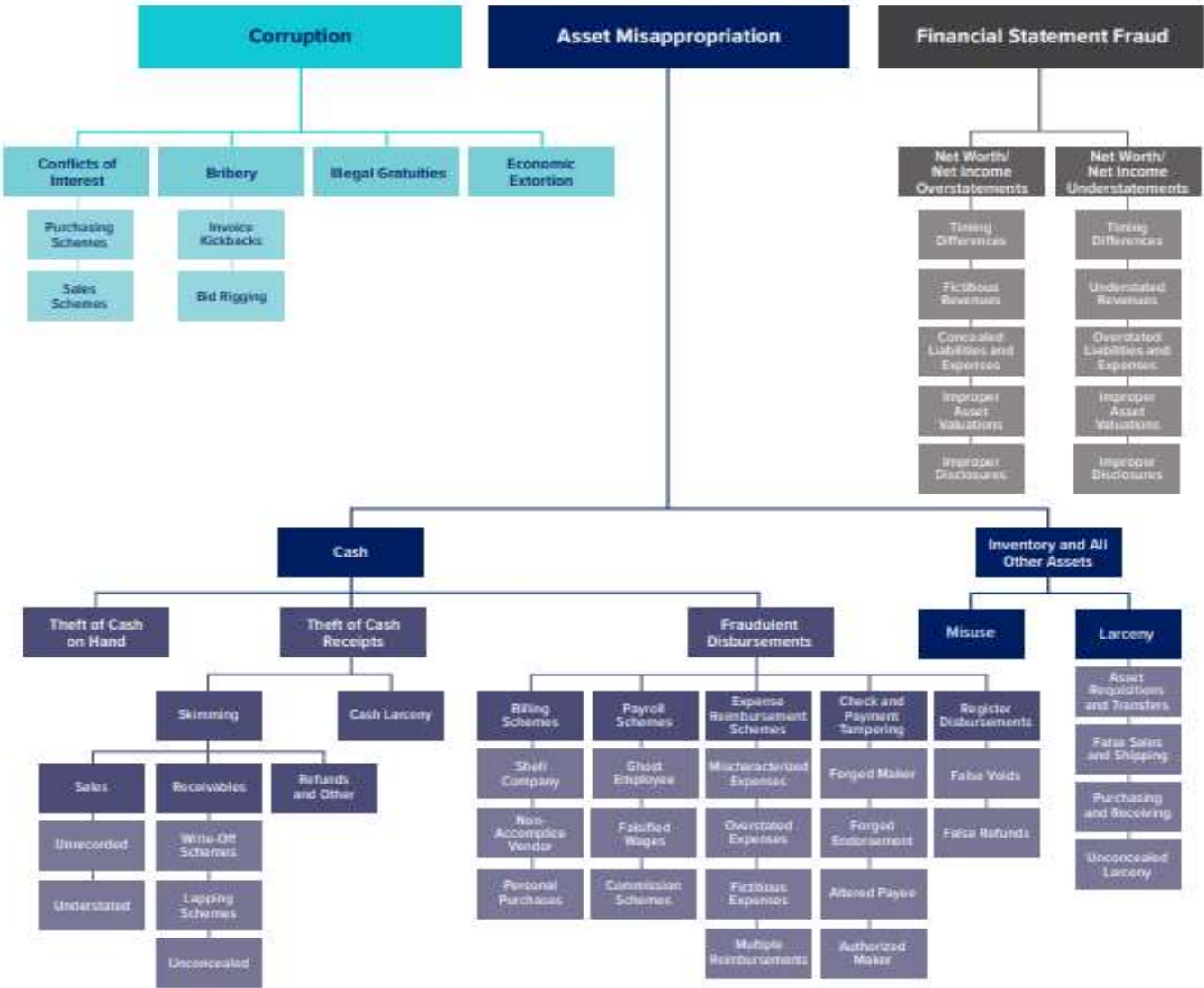
1. Corruption (Conflict of interest, Bribery , illegal Gratuities, Economic Extortion)
2. Asset's Misrepresentation (Theft Cash on hand, Fraudulent disbursement, Inventory, and other Assets)
3. Financial Statement Fraud (Overstatements Net Worth / Net Income – Understatements Net Worth/Net Income)

1. Examiners, A. o. (2023). <https://www.acfe.com/>. Retrieved from <https://www.acfe.com/FRAUD-RESOURCES/FRAUD-101-WHAT-IS-FRAUD>

2. ACFE. (2022). Retrieved from [www.acfe.com: https://www.acfe.com/-/media/files/acfe/pdfs/2022-rttn-fraud-tree.ashx](https://www.acfe.com/-/media/files/acfe/pdfs/2022-rttn-fraud-tree.ashx)

THE FRAUD TREE⁽¹⁾

FIG. 3 OCCUPATIONAL FRAUD AND ABUSE CLASSIFICATION SYSTEM (THE FRAUD TREE)¹



1. ACFE. (2022). Retrieved from [www.acfe.com: https://www.acfe.com/-/media/files/acfe/pdfs/2022-rttn-fraud-tree.ashx](https://www.acfe.com/-/media/files/acfe/pdfs/2022-rttn-fraud-tree.ashx)

Q6.What is the effect of the corporate fraud in US to global economic?

In past decades the corporate fraud had adversely affected economics worldwide. We have witnessed crises and collapse of large public companies in US with disastrous implications (for example, Enron, Waste Management Inc, WorldCom, AIG.. etc.) the direct impact of the corporate fraud is the financial loss due to theft or embezzlement, moreover it will affect the whole economy and the trust in corporate enterprise and market. (1)

4.The importance and objectives of the research:

Q1.Why the study of the corporate fraud is important?

The current study may provide a review of the literatures have conducted on the corporate fraud in addition to the financial crimes, moreover the prevention and detection methods to identify the causes and effects of this type of fraud in the economic in U.S. and it's effect to the global economic, corporate governance system's deficiencies may create an opportunities for financial statement fraud which mainly occurs with the knowledge of the top management which mean that the fraud comes from the top. (2) To better understanding the fraud framework, we briefly present the possible types of fraud which may faced, as per ACFE fraud schemes are classified into 3 categories which presented above in the fraud tree. The corporate scandals at the last century drew the attention of professionals and regulators of fraud prevention and detection, which shows the severity of corporate fraud and continuously evolving issue (3)

Q2.What is the impact of Fraud Examiners in the fraud risk management

Fraud examiners are necessary elements of an anti-fraud program, they are using the available tools like whistleblower hotline, Surprise visits , Fraud awareness, /ethics training reduce median losses in half, however the strong anti-fraud program does not guarantee that the corporate will not be victim of fraud but it decreases the losses from the crime. (4)

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1. Segal, S. (2016). Accounting frauds—review of advanced technologies to detect and prevent frauds. *Economics and Business Review*, 2(4), 45-64.
 2. Rashid, M. A., Al-Mamun, A., Roudaki, H., & Yasser, Q. R. (2022). An overview of corporate fraud and its prevention approach. *Australasian Accounting, Business and Finance Journal*, 16(1), 101-118.
 3. Bekiaris, M., & Papachristou, G. (2017). Corporate and accounting fraud: Types, causes and fraudster's business profile. *Corporate Ownership & Control*, 15(1), 467-475.
 4. Lister, L. M. (2007, Dec 6). <https://go.gale.com/>. (I. Institute of Internal Auditors, Editor) Retrieved from <https://go.gale.com/>: <https://go.gale.com/ps/i.do?id=GALE%7CA172637276&sid=googleScholar&v=2.1&it=r&linkaccess=abs&issn=00205745&p=AONE&sw=w&userGroupName=anon%7E710aef17&aty=open+web+entry>

5. Research hypotheses:

Existence of Fraud Examiners and their effectiveness in avoiding Fraud?

Creating a team to perform a fraud risk assessment “FRA” is important, since their plan should be document the origination’s significant activities and their associated risks, identify the organization’s universe of potential risk. In addition to analyzing the likelihood of each scheme or scenario occurring and assess the materiality of the risk.

The fraud examiners should evaluate the effectiveness of existing controls in preventing the specific fraud scenarios. ⁽¹⁾

Key elements of a fraud compliance program and their effect to avoid fraud:

1. Anti-Fraud environment.
 - a. Proper tone set by senior management.
 - b. Strong ethical corporate culture.
 - c. Code of conduct.
2. Education and Training
 - a. Anti-Fraud Training Program
 - b. Data and information security training program
 - c. Open communication with the other stakeholder.
3. Proactive detection
 - a. Effective fraud tip hotlines.
 - b. Whistleblower
 - c. Punishment protocol.
4. Investigation and follow up
Empowered audit committee with the oversight of fraud prevention program.

1. Brian Svoboda Kindle, K. B. (2019). In *CFCS CERTIFICATION EXAMINATION* (pp. 80-81). Florida: Donald Semesky, Financial Operations Consultants.

Governance:

The combination of processes and structures implemented by the board of directors to inform, direct, manage, and monitor the activities of the organization toward the achievement of its objectives.

Fraud Risk management:

A process to identify, assess, manage, and control potential events or situations to provide reasonable assurance regarding the achievement of the organization's objectives."

Control:

Any action taken by management, the board, and other parties to manage risk and increase the likelihood that established objectives and goals will be achieved. Management plans, organizes, and directs the performance of sufficient actions to provide reasonable assurance that objectives and goals will be achieved."

Ordinarily, the board is responsible for guiding governance processes, and senior management is responsible for leading risk management and control processes. (1)

The Fraud examiners in the corporates have responsibilities for the fraud risk management as following:

- a. Establish/Monitor the key risk indicators and implement corrective action plan in order to mitigate the fraud risks.
- b. Analyzing financial transactions and internal reports for the potential fraud risks.
- c. Issuing reports for the critical risks with the recommendations.
- d. Maintain the policies and procedures in addition to the control assessment in response to the identified risks.
- e. Evaluate the effectiveness of the internal control framework in addressing the fraud risks.
- f. Provide training and technical support to management and employees for the risk management strategies.

1. Joseph T. Wells, N. S. (2020). *FraudExaminersManual*. In N. S. Joseph T. Wells, *FraudExaminersManual* (pp. 1692-1694). Austin Texas .

6.Literature review

The report issued by Association of Certified Fraud Examiners “ACFE” to Nations about Occupational fraud 2022, based on the research shows how successfully the fraud examiners were able to adapt and detect the frauds and limit the relevant losses. The study shows that owners/executives committed 23% of occupational fraud, however they caused the largest losses \$337K. the presence of Anti-fraud controls is associated with lower fraud losses and Quicker fraud detection. Nearly 50% of cases occurred because of lack of internal control 29% or override of existing control 20%. Out of 2110 cases reported in this research there were 675 cases in U.S. and Canada. Since the first report release to the nation in 1996 ACFE have analyzed more than 20,000 cases of occupational fraud which reported by certified fraud examiners. The mechanisms explored in each study which used by the perpetrators to defraud their employers even after shifting to digital payments or remote work environment the methods used by fraudsters to commit occupational fraud remain consistent over time. Many organizations over the world have dealt with the consequences of the corporate’s collapse in U.S, either through closing or limit their operations. Therefor the study of the corporate fraud in U.S is still crucial since its consequences not only impact the U.S economy but impact the global economy as well.

How Corporate fraud is committed?

The association of Certified Fraud examiners’ 2020 Global study on occupational fraud and abuse identifies the three most common forms of accounting fraud:

	ASSET MISAPPROPRIATION (Theft)	86% of all corporate fraud cases	Median loss: \$100,000
	CORRUPTION (Misuse of Authority)	43% of all corporate fraud cases	Median loss: \$200,000
	FINANCIAL STATEMENT FRAUD (Incorrect or Omitted Material Information)	10% of all corporate fraud cases	Median loss: \$954,000

1. Burce Dorris J.D. President and CEO, A. o. (2022). *Occupational Fraud 2022 - A REPORT TO THE NATIONS*.

Three Lines of Defense model:

Provides a simple and effective way to enhance communications on risk management and control by clarifying how specific duties should be assigned and coordinated within the organization. The board of directors and senior management are the primary stakeholders served by the lines, and they are the parties best positioned to help ensure that the Three Lines of Defense model is reflected in the organization's risk management and control processes. (1)

1) Operational management

- a) Provides the first line of defense (functions that own and manage risk)
- b) Develops and implements control and risk management processes
- c) Implements corrective actions to address process and control deficiencies

2) Business-enabling functions

- a) Provide the second line of defense (functions that oversee risks)
- b) Support the entity through specialized skills and typically may include various risk management, compliance, inspection, and financial control functions
- c) Are typically responsible for the ongoing monitoring of control and risk (2)

3) Internal auditors

- a) Provide the third line of defense (functions that provide independent assurance)
- b) Provide assurance on the effectiveness of governance, risk management, and internal controls, including the manner in which the first and second lines of defense achieve risk management and control objectives (3)

1. Davies, H., & Zhivitskaya, M. (2018). Three lines of defence: a robust organising framework, or just lines in the sand?. *Global Policy*, 9, 34-42.

2. Luburic, R., Perovic, M., & Sekulovic, R. (2015). Quality management in terms of strengthening the "three lines of defence" in risk management-process approach. *International Journal for Quality Research*, 9(2), 243.

3. Luburić, R. (2017). Strengthening the three lines of defence in terms of more efficient operational risk management in central banks. *Journal of Central Banking Theory and Practice*, 6(1), 29-53.

7. Research methodology:

Historical Method

By analyzing the common financial scandals that have occurred in the U.S. market, we came out with the fact that the losses affect the global economy. The data obtained from the official website for U.S. Securities and Exchange Commission

Example of corporate fraud in U.S. which impact negatively the global economic.

The world saw the worst accounting scandals in history, Billions of dollars were lost as a result of these financial disasters which destroyed the companies and peoples' lives. The following are the top 10 of biggest accounting scandals which revealed the 9 out of 10 scandals (90%) were in U.S. (1)

1. Waste Management Scandal (1998)

Publicly-traded U.S. waste management, the company overstated its profit by \$1.7 billion dollars

2. Enron Scandal (2001) :

Enron corporation was a U.S. energy, in 2001 the company hid billions of dollars of bad debts while inflating the earnings, in addition the management pressured the company's audit firm **Arthur Anderson** to ignore the issue, the scandal resulted in losing over \$74 billion dollars and the share's price collapse from around \$90 to under \$1 within a year.

3. WorldCom Scandal (2002) :

WorldCom was an American telecommunication company in 2002 just a year after the Enron scandal, it was discovered that the company had inflated its assets by almost \$11 billion, moreover the company underreported line cost by capitalizing instead of expensing them and inflated its revenues by making false entries, the scandal first came to the light when company's Internal Auditors found almost \$3.8 billion in fraudulent accounts. The scandal resulted in over 30,000 job losses and over \$180 billion in losses by investors.

4. Tyco Scandal (2002) :

Tyco International was an American blue-chip security systems company and it was discovered that both CFO & CEO had stolen over \$150 million from the company and had inflated the earnings by over \$500 million in their reports. The scandal was discovered when an investigation conducted related to questionable accounting practices by the company.

5. HealthSouth Scandal (2003)

HealthSouth Corporation is a top US publicly traded healthcare company, it was discovered that the company had inflated earnings by over \$180 billion. CEO of HealthSouth had sold \$75 million in stock a day before posting a huge loss.

6. Freddie Mac Scandal (2003)

Freddie Mac is a US federally backed mortgage financing; it was discovered that earnings misstated by over \$5 billion.

7. American International Group (AIG) Scandal (2005)

American International Group (AIG) is a U.S. multinational insurance firm with over 88 million customers across 130 countries, in 2005 it was discovered that CEO has manipulated in the stock price and after investigation it was revealed a massive accounting fraud of almost **\$4 billion**, The loans were booked as a revenue, and the stock traders had inflate the company's share price.

8. Lehman Brothers Scandal (2008)

It was one of the largest investment banks in united states, in 2008 financial crisis it was discovered that over \$50 billion in loans had been disguised as sales using the accounting loopholes. Lehman brothers had sold a toxic asset to the banks in Cayman Islands on the short-term basis, to buyback these assets which gave the impression that the company had \$50 billion in cash and \$50 billion less in toxic assets.

Then Lehman Brothers went bankrupt.

9. Bernie Madoff Scandal (2008)

Bernie Madoff is a former American stockbroker who orchestrated the biggest Ponzi, it was discovered that Madoff had tricked investors out of over **\$64.8 billion**.

10. Satyam Scandal (2009)

Satyam computer service was an Indian IT service and back-office accounting firm based out of Hyderabad; the management had inflated revenue by \$1.5 billion.

The financial crimes also contain a money laundering and tax evasion which negatively affect the U.S economy and reflected to the global economy (2)

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1. Team, C. (2023, Jun 28). corporatefinanceinstitute.com. Retrieved from <https://corporatefinanceinstitute.com/resources/accounting/top-accounting-scandals/>
 2. Kindle, B. S. (2019). CFCS CERTIFICATION EXAMINATION STUDY MANUAL. In E. B. Kenneth Barden. Association of Certified Financial Crime Specialists.

Research limitation:

No study can explore everything related to the topic, the current research is depend on the historical data for the fraud cases which occurred since more than 20 years, and it may recommend to perform a survey for the certified fraud examiners over the world to receive the real cases recently investigated by them to know what is the new methods which my followed by the fraudsters. Therefore, due to the time constrains the current study analyzed the cases which already happened in order to remind the readers with the impact of the worst accounting scandals in U.S. history

The current study will be enhanced by embed the new technology such as Artificial Intelligence and its impact to improve the fraud detection tools in order to minimize the fraud risk.

Abstract:

Currently the organizations are facing a big challenge when managing the fraud risks, the financial pressures and rapid growth in addition to the lack of resources and awareness, expertise (Fraud Examiners...) create opportunities for motivated fraudsters to take advantage of the organization, in this research we try to provide a practical recommendation to help the business leaders prevent and detect the fraud in various business environment, these strategies may help the companies to make a difference when it comes to fraud risk management through highlighting the importance of fraud examiners in the fraud risk management.

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