

IMPACT OF FORENSIC AUDITORS ON CORPORATE GOVERNANCE FOR SUSTAINABLE DEVELOPMENT IN NIGERIA

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ABSTRACT

The incessant financial Fraud resulting in corporate collapse and the failure of the statutory audit to detect and prevent fraudulent activities which have led to the impoverishment of investors has given rise to the need for forensic auditors. In view of the above, this paper considers the role of forensic auditor on corporate governance. The study is theoretical research which is considered the roles of forensic auditors in combating fraudulent activities, distinction of forensic auditor and statutory auditor, characteristics of a forensic auditor and impact of forensic auditors on corporate governance. From studies carried out, this paper concludes that forensic auditors having improved management accountability, strengthened external auditor independence and assisting audit committee members in carrying out their oversight functions by providing them assurance on internal audit report have impacted positively on corporate governance thereby reducing corporate failure and impoverishment of investors.

Introduction

Overview Of The Study

The incessant financial fund and its impact on corporate performance has led to the need for multi-dimensional relationship (that is inter-relationship between the audit committee, the external auditor and the management) in corporate governance as to protecting the interest of shareholders and other market participants with common goal of improving oversight function and ensuring good corporate governance (Deloitte and Touch 2006).

However, despite the multidimensional relationship between the three major groups in corporate governance, the financial fraud, which has to poor performance and most times to corporate collapse, resulting in huge loss of investment and impoverishment of many investors has contributed has continued to be on increase (Rezae, 2005). Ramaswamy (2009) in line with the above, states that the failure of the corporate structure has made the financial community realize that there is a great need

for skilled professionals who can identify, expose, and prevent weaknesses in three key areas, namely poor corporate governance, flawed internal controls, and fraudulent financial statements. Owojori and Asaolu (2009) state that the failure of Statutory Audit to prevent and reduce misappropriation of corporate fraud, leading to an increase in corporate crime, has put pressure on the professional accountant and legal practitioner to find a better way of exposing fraud in the business world. The above problems have posed a serious concern to the accounting profession and users of accounting information, thus giving rise to the call for forensic auditors. In view of the above, this study aims to ascertain the role of the forensic auditor and his impact on corporate governance.

Statement Of The Problem

The failure of the major corporate governance mechanism to reduce financial fraud and the increasingly sophisticated financial fraud has posed a serious threat to investors, the government, and the general

public (Eyisi, 2009). More so, the stakeholders of most companies are worried over the unqualified audit report being certified by external auditors and few weeks after such reports have been certified, such companies are found to be in serious financial crisis leading to bankruptcy and most times liquidation, thereby impoverishing the corporate investors and affecting the economy (Aneto 1993). An instance of case of corporate financial statement audit fraud could be drawn from Enron and Worldcom which has capitalized expenses resulting to increased profit which is not in existence and yet such companies audit was qualified by their auditors (Anderson) resulting to corporate failure of two big companies in USA (Zimbeirnan 2012 et al). Another instance could be drawn from a 2007 report for the Federal Bureau of Investigation (FBI) which estimates that fraud in non-health insurance costs more than \$40 billion per year.

Another instance of corporate financial fraud could be drawn from recent banks failure in Nigeria where management has fraudulently given loans without board approval and yet such banks annual reports have been qualified. From the above it could be said that the external auditors have continued to qualify fraudulent financial statement thus resulting to impoverishment of investors and most times corporate collapse and economic crisis. Since the external auditors have refused to accept the responsibility of laying credence to financial statement, this has created a gap between the users of accounting information and accounting profession. This gap is known as Audit Expectation gap (Adenji 2001 and Ekwueme, 2006). Hence, the failure of statutory audit to prevent and reduce fraudulent activities in corporate governance had necessitated the need for Forensic

Accounting (Owojori and Asaolu, 2009). In view of the above problems, this study examines the role of forensic auditors in combating fraudulent activities and its impact in corporate governance.

Objectives Of The Study

In view of the above problem, this study considered the following:

1. Examining the roles of forensic Auditors in combating fraudulent activities in organization.
2. Determining the characteristics required of forensic auditors for effective combating of fraudulent activities
3. Differentiating between a Forensic Auditor and a Financial Auditor
4. Ascertaining the impact of forensic auditors in corporate governance

Literature Review

Concept of a Forensic Auditor

The term forensic means "relating to the application of scientific knowledge to legal problems or usable in a court of law". (Bolgana and Robert 1985), Webster dictionary defines forensic as belonging to; used in, or suitable to courts of judicature or to public discussions and debate. Thus, from the above definition, it could be said that Forensic Auditors are experts in financial matters who are trained in detecting, investigating and deterring fraud and white-collar crimes which are to be presented in court for legal action or to public discussion and debate. This is in line with (Messier, 2000) definition which states that forensic auditors are fraud examiners employed by corporations, government agencies, public accounting firms and are trained by Association of Certified Fraud Examiners (ACFE) on areas which cover fraudulent financial transactions, legal elements of fraud investigation, criminology and ethics.

Singleton and Singleton (2004) accordingly state that Forensic in the accounting profession (see.pg2). From the above definition, it can be said that forensic auditors are financial experts who use and apply scientific knowledge to detect fraud and crime in legal matters, which may be criminal or civil disputes.

According to AICPA (2008) forensic Accounting Services generally involve application of special skills in auditing, accounting, quantitative methods, finance, specific areas of the law, information and computer technologies, research and investigative skills to collect, analyze, and evaluate evidential matter which in the forensic area is called the evidence. Form the above it could be said that the forensic auditor possesses expertise skill and can be called upon to carry out investigation on financial matter which may be used in law court and also, he can be called in the law court to give evidence on issues relating to financial fraud.

Activities Carried out by Forensic Auditors

Institute of Forensic Auditors (IFA) defines forensic activity as the activity that consists of gathering, verifying, processing, analyzing and reporting on data in order to obtain facts and evidence in predefined context in the area of legal financial disputes (including fraud) and giving preventive advice. From the above, one can say that a forensic auditor is an expert in accounting with experience and special skill in auditing, fraud detection, and criminology who carriers out investigation that are usable in the Law Court. In order to understand activities being carried out by the forensic auditor, there is need to know the objective of forensic audit.

Objectives of Forensic Audit

The objectives of forensic audit will help us to understand the role of the forensic auditor and his impact on corporate governance. These objectives are:

- To improve management accountability
- To improve corporate governance and the statutory audit function
- To improve financial reporting system
- To help in detecting financial fraud
- To help in strengthening auditors independence
- To provide additional assurance for audit committees
- To make financial statement auditors to take greater responsibility for the detection of fraud and illegal acts when auditing financial statements due to the fact that another set of auditors (forensic auditors) would be critically evaluating their role.
- Forensic Audits conceivably could give the audit committees tool better evaluate the quality of the financial statement audited by the external auditor.

The above objectives could be said to have stronger impact on corporate governance, since the forensic auditor is expected to go beyond normal audit as to search for fraud and investigate deeper, using more sophisticated scientific analytical tools and software packages to detect fraudulent activities perpetrated by the management and their employees or fraud which the external auditor has connived with the management cover.

Differences Between Forensic Auditor and Financial Auditor

Forensic Auditor or Non-statutory Auditor is employed or appointed by on	Financial Auditor or Statutory Auditor is usually appointed to carry out statutory
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<p>organization to resolve allegations and detect or prevent fraudulent activities suspected or envisaged in the organization. Thus, Forensic Auditors carries out investigation as to resolve allegations on fraudulent financial matters through court. Thus, it is not a normal audit but audit which may or may not follow auditing procedures and GAAP in carrying out its function. Zimbeldametal (2012) states that, such audit is a proactive audit which goes beyond normal audit procedures.</p>	<p>audit. The financial audit is usually carried out to satisfy statutory requirements, and ensure that accounts prepared/maintained are in line with GAAP. Mill champ (1990) states that the statutory audit is a compulsory audit which ensures that financial statement are in line with GAAP.</p>
<p>A Forensic audit is directed at specific allegations. Forensic Auditor carries out investigation on specific allegations. Hence he has much time to investigate and analyze thoroughly specific fraudulent financial issue with emphasis on using such as evidence in law court in case of dispute (Albrecht and Albrecht, 2009)</p>	<p>Financial audit carried out by the financial auditor is general in nature. According to Millucky and Mac (2013), Financial audit is carried out on general financial matters. (That means, his accounts consider all issues which concern all relating to accounting.)</p>
<p>A Forensic Auditor is not apt to accept explanations and documents at face value (Cole, 2009). From the above, the forensic auditor is expected to always go beyond the normal audit and a search for fraud which is to be reported to whosoever has appointed the forensic auditor or to be used as expert evidence in the law courts.</p>	<p>Financial auditors usually do not burrow deeper into documents and explanations. This means that the financial auditor usually does not carry out detailed analytical study of financial tries to lay credence that accounts prepared by management and their employees are in line with GAAP and statutory regulation (Cole,2009)</p>

Responsibilities of Forensic Auditors in Combating Fraudulent Activities

The forensic auditors have the responsibilities that are listed below:

- 1. Conducting Investigation:** the forensic auditor does not carry out procedural audit or crime using computer programs or scientific knowledge. This means the forensic auditor should have the capability to use computer forensic tools that could be both software and hardware in carrying out its function so as to detect or prevent

fraudulent activities. Thus, by using the computer forensic tools in carrying out his responsibilities, sophisticated fraudulent activities can be combated. Owojori and Asaolu (2009) state that the failure of the statutory audit and the sophisticated financial fraud has led to the need for forensic audit. Thus, the forensic

auditor could be said to have special tools for conducting investigation with a view to detecting and preventing fraudulent activities thereby combating financial fraud. An example of software packages used to combat fraud is case ware software. A Zimbelman (1997) state that being a fraud investigator is very much like being a physician, it requires significant amount of diagnostic and explanatory work to discover what is really happening. In view of the above, it can be said that the forensic auditor goes beyond the normal audit as to unveil fraudulent activities using forensic software tools in conducting and investigating transactions and events.

2. Analyzing Financial Transaction: Forensic auditor in carrying out his function analyzes financial transaction involving unauthorized transfers of cash between companies. (Owojori and Asaolu 2009), Cole (2009) states that the forensic auditors are required to have special skills in inspecting documents for authenticity, alteration, forgery or counterfeiting. Hence, by possessing such skills, the forensic auditor in carrying out his duties can easily detect errors, fraudulent activities and omissions thereby preventing and reducing fraudulent activities. Zimblemanetal (2012) states that the forensic audit is responsible for analyzing, identifying the kinds of fraud that could occur and their symptoms. Thus, since forensic auditor is a fraud detector that not capabilities to analyze financial transaction which will help him to easily detect errors, fraudulent

activities and omissions that may be presented for litigation or sent to the audit committee as to enable the audit committee to evaluate the quality of financial statement audit.

3. Reconstruction of incomplete accounting records:

The forensic auditor in carrying out his function reconstructs incomplete accounting records so as to settle insurance claims, over inventory valuation, proving money laundering activities by reconstruction of cash transactions (Owojori and Asaolu,2009).

To combat fraudulent activities, the forensic auditor with his skills (Technological communication and expertise skills) in accounting knowledge can reconstruct incomplete accounting records, hence helping to detect and prevent fraud and ensuring a good internal control system and good corporate governance.

4. Embezzlement investigation:

In carrying out an embezzlement investigation and providing documentation, and negotiation of insurance settlements, the forensic auditor uses their special skill and experience, thus helping to detect the culprit and the amount embezzled. Cabole (2009) states that what forensic auditors do includes:

- i. Fraud detection, documentation, and presentation in criminal trials and terms
- ii. Calculate economic damages; trace income and assets, often in an attempt to find hidden assets or income,

- iii. Reconstruction of a financial statement that may have been destroyed or manipulated.

- iv. Expert witness

The above responsibilities listed by Caboles (2009) and Wallace (2009) show that forensic auditors must be specialists (experts) in financial matters and must have legal knowledge that enables them to detect fraudulent activities which are to be presented in the law court. This is in line with Owojori and Asaolu (2009), who state that the major contribution of the forensic accountant is to translate complex financial transactions and numerical data into terms that ordinary lay persons can understand. The above responsibilities carried out by the forensic auditor require that the forensic auditor, being a fraud-fighting professional, possesses certain characteristics which enable him to carry out his responsibilities effectively.

Characteristics of Forensic Auditors

The forensic auditor should possess the following characteristics to enable them to detect fraudulent activities that have been perpetrated.

High level of Competence: The forensic auditor, since his task is to detect financial crimes and criminal issues using specialized computer programs which must be well competent. Thus, the forensic auditor is expected to have undergone specialist training in accounting, auditing, criminology, sociology and fraud investigation (civil and criminal) (Association of Certified Fraud Examiners, 2008), From the above it

can be said that the forensic auditor is not only professional in accounting but also have knowledge in other fields of study which enables him to carry his function effectively. Wallace (2009) listed the minimum requirements a forensic Accountant must possess to include:

- ❖ An ability to review a large volume of documentation ranging from the more usual accounting records and management information system to memos, correspondence, and other less obviously financial data, and to extract the key issues quickly
- ❖ A sound understanding of the peculiarity of various business methods
- ❖ A sense of urgency and commitment which will ensure prompt response when required, however slow civil litigation may appear to the onlooker or even to the participants in a dispute
- ❖ Adherence to a strict timetable even when a need arises to work for more hours to meet the targeted time
- ❖ Most essentially, ability appears as objectives and professionalism even when taking part in the inherently partisan process of a court case.

From the above, it could be said that forensic auditors are expected to possess analytical skills, communication skills, and technological skills. These skills are special skills that enable

the forensic auditor to combat fraudulent activities.

Special Skills Possessed by the Forensic Auditors

The forensic auditor requires special skills in auditing, accounting, quantitative methods, finance, specific areas of the law, information and computer technologies, research and investigate skills as to be able to collect, analyze and evaluate evidential matter which in the forensic area is called evidence (Forensic and Compliance institute, 2009)

Communications skills: forensic auditor should have a good interactive skill.

According to Nathan (2009), for the forensic auditor to detect fraudulent activities he requires special skills which include:

- Being a good interviewer
- Having ability to observe behavior especially during interviews
- Ability to reconstruct financial transaction through information obtained from the parties
- Knowing legal implications of evidence obtained

Technical/Financial Skill: The most important skill required by the forensic auditor so as to detect fraudulent activities should have solid technical accounting and financial skills (Nathan 2009 and Zime).

The basis of your expertise, ability to quickly prioritize issues and map out a game plan, "good judgment: ability to communicate well both verbally and in writing – is necessary to obtain information, directing your staff. Presenting your findings and achieving your desired results. Even the best concisely presents your findings.

Analytical Skill: A forensic auditor needs to be precise, pay attention to detail, and be a broad thinker; that is, not suffer from tunnel vision (Singleton and Singleton, 2004)

Investigating skill: When looking at a given forensic accounting engagement, two major areas come to mind in the completion of a given case. First, there is the investigative aspect, and second, the communication aspect. Investigative skills would include areas such as the ability to assimilate large volumes of information, general organization and administration skills, use the microcomputer or understand the abilities of the microcomputer and interpersonal skills. Communication skills would include the ability to write a comprehensive report understandable.

Honesty and High Integrity: - Since the forensic auditor is expected to detect fraud, he is expected to be of high integrity and honesty in carrying out his functions. According to CPA (2009) the forensic accountants are vital allies in the fight against fraud and provide assistance to the Audit Committee; hence, he is expected to show high integrity and honesty in carrying out their function.

Role of Forensic Auditor Incorporate Governance

Improved Management Accountability: Management is accountable to shareholder, and other stakeholder Management of companies are said to be solely responsible for preparing Accounts and maintaining adequate proper financial records (Millichamp, 2002). More so, they are responsible for detecting and preventing fraud in their organization, while the external auditors' responsibility is to ensure that accounts prepared by companies' management are in line with Generally Accepted Accounting Principles (GAAP) and statutes. However, the auditors in carrying out their duties may unveil fraud if such is discovered. The external auditor to report a

material misstatement and errors arising due to fraud.

Nevertheless, the above responsibility functions have not been achieved; thus, resulting in corporate fraud and, most time, corporate failure and poor corporate governance. To ensure proper accountability and prevent fraud, matters with special skills in scientific knowledge and legal matters are handled, which enables management to easily detect and prevent fraudulent activities. Also, since management are aware that the forensic auditor may be called upon by shareholders/External auditors and audit committee at any time to investigate and detect financial fraud, the management will be more diligent in carrying out his function knowing full well that the forensic auditors may be invited to detect and prevent fraudulent activities they will most time ensure that their organization has a good internal control system, checks and balances which are transparent.

Ramaswamy (2009) states that the failure of the corporate communication structure has made the financial community realize that there is a great need for skilled professionals that can identify, expose, and prevent weaknesses in three key areas; poor corporate governance, flawed internal controls, and fraudulent financial statement. Forensic accounting skills are becoming increasingly relied upon within a corporate reporting system that emphasizes its accountability and responsibility to stakeholders. From the statement the Forensic Auditor with his expert knowledge in crime will help to improve corporate reporting system designed by management which will expose and prevent poor governance, flawed internal control and fraudulent financial statement.

Improved Corporate governance and statutory Audit-Function: Statutory Audit is an audit required by law as to lay credence to financial statement and ensure that adequate and proper financial records have been maintained as required by statutes and GAAP and regulations.

However, the external auditor in carrying out the audit function has not been able to carry his function effectively due to his mode of appointment. The external auditor by law is required to be appointed by shareholders; most time the management on behalf of the shareholders appoint the external auditor whose book of account is being examined (audited).

Thus, auditors most times, may not report cases of fraud perpetrated by the management to the shareholders (owners). Given the above, it can be said that the mode of appointment of the external auditor has negatively affected external auditors' performances in carrying out their corporate governance function effectively, thereby causing investors to lose confidence in annual corporate reports of companies (Lee,2001).

An instance of this could be drawn from Arthur Anderson of Enron and WorldCom. Auditors who were indicted for obviously fraudulent financial statements that affected investors and the economy of U.S governance can (Zimblemanetal, 2012). Nevertheless, the issue of fraud in corporate governance can be reduced due to use of a forensic auditor. The forensic auditor with special skills (that is, Analytical, Communication, and Technological skills) can reduce and improve corporate governance by instilling fear both to the management and their employees when carrying out his audit function. More so, the external auditor being appointed by management will no more have fear in reporting fraudulent activities performed by management due to fraud to

the forensic specialist. According to SAS 99 external auditors are provided guidance that has the potential to improve audit quality misstatements, whether caused by fraud or error. SAS No. 99 includes the suggestion that an "auditor may respond to an identified risk of material misstatement due to fraud by assigning forensic specialists (AICPA, 2002). From the above, the forensic auditor may improve corporate governance and statutory audit function by using specialist skills to help statutory to detect fraudulent activities which the external auditor may not discover he has no expertise skill and knowledge in detecting modern sophisticated fraudulent activities in organizations.

Methodology

This study is theoretical study of the role of forensic auditors in corporate governance which employed the secondary source of data collection by making use of available literature and forensic auditors and their roles on corporate governance.

Conclusion

Since the forensic possesses special skills and knowledge that can easily detect and prevent fraudulent activities, this will enable the corporate governance mechanism (the External auditor, audit committee, and management) in carrying out their responsibilities of achieving corporate goals and reducing financial fraud. Thus, the forensic auditor could be said to have impacted effectively on the corporate governance of the organization by improving the management accountability, financial reporting system, strengthening independence of the external auditor, assisting audit committee members in their oversight functions by providing additional assurance and giving greater responsibility in the external auditor in carrying out their statutory audit function.

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