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Detecting Financial Fraud Following The Covid 19 Pandemic: Role of The Board of Directors

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ABSTRACT: Today, the era of COVID-19 has exacerbated the problem of financial fraud. Indeed, many companies are migrating to remote virtual working environments, where fraudsters can find new ways to bypass existing controls, especially those that are important for the preparation of annual financial statements. Thus, this new economic environment can weaken internal controls and increase the risk of fraud. The aim of this paper to identify the effect of the COVID-19 pandemic on the aggravation of the problem of financial fraud and to emphasize the role of the board of directors in detecting financial fraud

KEY WORDS: Financial Fraud Detection, COVID-19, Board of Directors
JEL CLASSIFICATION: M41, G34

I. INTRODUCTION

Today, the COVID-19 pandemic has a very significant economic and operational impact on businesses and thus represents a major challenge for everyone. Many companies are now measuring the consequences of this crisis on, among other things, their supply chain, their income, their liquidity and their employees. This new context, which is becoming more and more unstable, has considerably increased the risk of fraud. Two elements of the fraud triangle are now exacerbated, pressure and rationalization. In times of crisis, companies, employees and third parties come under considerable pressure. The line between ethical behavior and fraudulent behavior becomes blurred, and some people justify inappropriate acts (through a rationalization mechanism), which increases the risk of fraud. On the other hand, the great losses caused by financial fraud have attracted the continued attention of academia, industry and regulators. Even more alarming, the ongoing coronavirus pandemic (COVID-19) has dramatically worsened the situation by accelerating the use of digital financial services. New challenges in the effective detection of financial fraud have therefore emerged. In fact, new features of fraud risk are caused by the pandemic which requires smarter fraud detection methods. The importance of governance mechanisms, especially the board of directors in oversight and risk management has been extensively studied in previous studies (Liebenberg, & Hoyt, 2006; Wan Daud et al, 2011; Wachtell et al 2020). However, studies examining the relationship between the board of directors and financial fraud remain timid. The motivations for this study are twofold. First, the failure of boards of directors and senior management is undoubtedly one of the major causes of the bankruptcy of several companies around the world. As such, Nam & Nam, (2004), stipulates that the board of directors is the main actor in the corporate governance process, since it is responsible for the effectiveness of governance mechanisms and specifically of internal control systems. The second motivation is the worsening of financial fraud following the COVID-19 pandemic.

The aim of this paper is therefore to identify the effect of the COVID-19 pandemic on the aggravation of the problem of financial fraud and to emphasize the role of the board of directors in detecting financial fraud

The article is organized into three sections. The second section is devoted to the review of the exploration of the aggravation of financial fraud following the COVID-19 pandemic. We then examine in the third section the role of the board of directors in detecting financial fraud. Finally, the last section concludes the paper

II. FINANCIAL FRAUD FOLLOWING THE COVID-19 PANDEMIC

Financial fraud is defined by the Association of Certified Fraud Examiners (ACFE) as follows: "The deliberate, intentional, misstatement or omission of material facts, or accounting data which is misleading and, when considered with all the information made available, would cause the reader to change his or her judgment or decision".

In fact, the COVID-19 pandemic has resulted in increasing economic pressure and stronger grounds for fraud for businesses and individuals following economic downturns. COVID-19 is already revolutionizing most businesses and their environment, and opening up new areas of risk that fraudsters take advantage of. These changes will persist for long after COVID-19. New procedures and new methodologies must be deployed now to modernize the compliance function and investigations in order to better prevent the risks, exacerbated by the pandemic.

Recently, the increase in cybercrime and financial fraud during the COVID-19 crisis has come to the attention of the general public, politicians, academics etc. in this context, several recent studies have analyzed the effects of the covid 19 pandemic and these repercussions on companies and on the economy in general (Zhu et al ,2021; Widiyati et al 2021, etc) . This is mainly due to threats to computer systems in financial services and data from mobile malware, phishing, botnet attacks, ransomware and insider threats.

Other vulnerabilities include the distraction of telecommuters, unprotected infrastructures such as virtual private networks and endpoints (Remote Desktop Protocol). At the same time, financial pressure has forced many companies to cut budgets for IT security, cybercrime, fraud and risk management departments. These incidents caused stress and tension for many consumers, but they also noticed malicious activity online. Almost a quarter of today's consumers are more interested in cybercrime than physical crime,

Numerous security breaches have left the field to the culprits between the rapid development of online services, the influx of consumers who have carried out many transactions in the real world, and what has been digitized by the situation. As a result, company employees had to adapt quickly to trigger business continuity plans and implement telecommuting measures. Since then, several issues have arisen including congestion in internet speeds, inaccessibility of databases, lack of access to physical tools and documents used in the workplace and lack of specific staff to adapt. to sudden changes. No reception screen), extension of access rights, suspension or suspension of control over time. Therefore, it is possible to stop monitoring during this period and favor the occurrence of errors in processes that were previously considered low-risk controlled processes. Financial institutions are generally shielded from these practices, but the reallocation of social distance and resources places great strain on financial institutions. Identity checks are becoming increasingly complex with physical branch closures, paperless offices, new business relationships and faster time savings. A welcome window for the general public, or an exponential growth of 100% digital offers.

Many pending checks have been postponed, in particular due to confinement and lack of personnel. Therefore, scams have many faces consisting of a clear desire to deceive a third party. Scammers Recycle Scenarios and Perform New Financial Scams ... When the first blockade began, the scams that rushed in were straightforward and easy to find. However, given the current crisis, fraudsters are increasing the number of attacks, making the well-known patterns of classic fraud more complex (eg fraud against presidents and bogus vendors) and more difficult to stop. The Observatory for the Security of Payment Instruments (OSMP) shows the trend towards digitization and digitization of companies. The strengthening of these practices has resulted in the loss of benchmarks for the company's employees and customers, the creation of a large pool of vulnerabilities, and the emergence of vulnerabilities. We have found that contactless and internet payments are on the rise, while the use of checks and withdrawals is declining (at least temporarily). Since 2020, wire transfer fraud and technician fraud have also become increasingly important. These allow thieves to remotely control a company's accounting or banking environment. The real thing is to collect personal information (bank cards, bank IDs, current assets and asset information). This allows criminals to purchase remotely or steal their identities later. This approach is mainly aimed at large companies that rely on a large number of suppliers. It's easy for a scammer to impersonate a particular vendor, have the company pay an invoice with a new IBAN, and direct the flow of money to a bank account operated by a scammer. Working from home minimizes telephone conversations, increasing the risk of this type of fraud.

III. THE ROLE OF THE BOARD OF DIRECTORS IN DETECTING FINANCIAL FRAUD

Businesses should be more transparent about current financial fraud campaigns. They also face the challenge of strengthening and improving their security. It continually educates employees on best practices for raising awareness of cybercrime, breaking compliance, fraud, silos between security teams, and adhering to internationally recognized governance frameworks and standards. Also, companies need to improve cybersecurity and fraud detection capabilities with a focus on defense in depth, automation and integration.

Recently, in view of the aggravation of the problem of financial fraud, studies on the importance of internal control in the detection of financial fraud have emerged (Engels et al, 2020; Jarrod et al, 2016). In this context, the recent financial scandals (the Enron affair in the United States: Enron, 2001; Worldcom, 2002; Anderson, 2002; global crossing, 2003; Elf et crédit de Lyonnais 2004) called into question the issue of confidence in the quality of the financial information disclosed. This has prompted regulatory authorities as well as businesses to emphasize the primary role of governance mechanisms, especially the board of directors, in detecting financial fraud. Indeed, the board of directors is considered to be one of the main players in the internal control process. Woidtke and Yeh. (2013) argue that policymakers around the world have focused on restructuring corporate governance. Professional reports and regulatory commissions have followed one another at the international level (Treadway in the United States, 1987, Cadbury in the United Kingdom, 1992, Viénot in France, Report of the Toronto Stock Exchange in Canada) to recommend the introduction of specialized committees emanating from from the administration board. The purpose of these recommendations was to ensure more adequate control of managers for the benefit of shareholders. A control which leads to improving the quality of financial information and reassuring the various users.

In fact, governance theories assign different roles to the board of directors. According to contractual theory, the firm is considered as a node of contract between the firm and the various providers of resources. As a result, agency conflicts arise because of information asymmetry. According to this current, the board of directors aims, on the one hand, to discipline managers in the service of shareholders, and on the other hand, to facilitate the creation of value for all stakeholders. In fact, two types of governance theories arise from this same current.

First, the financial contractual theory, two agency relationships can exist: on the one hand between the shareholder and the manager and on the other hand between the firm (represented by the managers and the shareholders) and the financial creditors (Jenson and Mekling, 1976). According to which the role of the governance system is to "secure" the profitability of the financial investor; this explains the use of mechanisms such as the board of directors, the general meeting of shareholders, executive compensation systems, public offers, etc. in order to align the interests of directors with those of the shareholders. In contrast, in partnership theory, the board of directors is seen as an instrument facilitating the creation of value for all stakeholders. From these broad approaches to governance, it can be said that the board's missions are not limited to overseeing managers for the benefit of shareholders but also helping to protect all value-creating relationships and to preserve and increase the productive character of the contract node. The board of directors is therefore the main actor in the governance process.

On the other hand, according to strategic theory, the survival of the firm is conditioned by its ability to control certain essential resources, so as to relax, for example, market constraints or stabilize the environment. The firm seeks to establish inter-organizational links with the external environment, in order to control these critical resources; when the environment becomes more uncertain or lacking, the firm strengthens or increases these links. To this end, the firm will incorporate representatives of the most critical resources, such as bankers, into its board of directors, in order to guarantee its survival. This integration of strategic considerations within governance theories will, however, limit the latitude of managers whose decisions will be influenced and constrained by the administrators representing the resources.

However, this integration is not done only from a defensive perspective, by controlling or protecting access to critical resources, but it must help the firm to build strategies for creating sustainable value. Indeed, this approach is said to be offensive, it borrows from the cognitive theories of the firm. The behavioral theory of the firm is inspired by the work of Simon (1997) and Cyert and March (1963), the evolutionary theory of Nelson and Winter (1982), and the theories of resources and skills resulting from the research of Penrose (1959). Indeed, the cognitive theories of the firm, as their name suggests, attach paramount importance to the internal creation of knowledge resulting from organizational learning, as well as to the phenomena of vision and attention. Certain theories are focused (Prahalad and Hamel (1990) and Teece et al., (1997)) on the construction of skills, on the capacity of firms to innovate, to create their investment opportunities and to modify their environment.

Thus, this strategic approach provides new justification for the board of directors, whose role would also be to facilitate the development of skills and help build new strategic options. According to this theory, the board of directors should be composed as a priority of directors who can best contribute to the creation of competence and help the leader to design a vision facilitating organizational learning. Therefore, the qualities required of directors are no longer conceived in terms of independence and expertise in terms of control, according to the internal-external distinction, but in terms of cognitive contributions.

Therefore, the role of the board of directors is very important in stopping fraudulent activities. Of course, different stakeholders must adhere to specific business ethics and corporate values and continuously monitor management to ensure that the focus is on preventing and detecting potential financial fraud. This supervision given to management can both allow this actor to prevent the actor from circumventing the rules, and therefore its importance for the prevention and fight against financial fraud in the company.

IV. CONCLUSION

At the end of this work, we presented the new challenges regarding the aggravation of the problem of financial fraud following the COVID-19 pandemic. We again emphasized the role of the board of directors in detecting financial fraud as a key player in internal control. At this stage, we have contributed to the literature on governance and its importance in the detection of financial fraud. Shareholders may find some clarification in this work. They are required to be increasingly vigilant against fraudulent behavior by managers, by adopting the necessary means of control. Businesses must learn the right lessons from the COVID-19 pandemic and take the appropriate steps to be successful in the post-pandemic future.

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