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THE ROLE OF INTERNAL AUDITORS IN FRAUD PREVENTION

(CASE STUDY OF NIGERIA BANK)

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Petos on tunnistettu yhdeksi suurimmista haasteista bisnes maailmassa. Sen tuhoisa vaikutus manifestoi itsensä pankin heikkenevänä esityksenä, kuin myös ekonomisena takaperisyytenä. Seurauksena, toimenpiteet petoksen torjumiseksi pankki sektorilla tuli johdon ja sisäisentarkastajien pääpainoksi.

Tämä tutkielma oli näiden taustojen takia suunnattu antamaan empiiristä todistusaineistoa sisäistentarkastajien roolista estämään petosta pankkialalla.

Teoreettinen osuus sisältää asiaan liittyvää kirjallisuutta jota käytettiin tämän tutkielman kirjoittamiseen. Se kuvaa pääsääntöisesti teoreettista materiaalia, mikä auttoi tutkielma prosessissa.

Lopputulos kyselystä osoitti, että suurin osa petoksista tapahtui heikon sisäisen valvonnan, huonon hallintajärjestelmän ja huonon kirjanpidon takia. Se tuli todistettua, että sisäistentarkastajien rooli petoksen estämiseksi voidaan toteuttaa hankkimalla riittävästi tietoa pankkien ympäristöstä ja sisäisistä valvontajärjestelmistä.

Avainsanat Sisäinen Tarkastaja, Petos, Sisäinen Kontrolli

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ABSTRACT

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Fraud has been identified as one of the major challenges to the entire business world. It`s devastating effect manifests itself in the deteriorating performance of the bank as well as in economic backwardness. As a result, measures to curb fraud in the banking sector become a major focus of the management and internal auditors.

It was against this backdrop that this thesis was aimed at providing empirical evidence on the role of auditors in prevention of fraud in the banking industry. In order to achieve the objective of the thesis, materials like related reports, articles, and textbooks about fraud and the auditor`s role were examined.

In evaluating the role of the auditor in fraud prevention in the case study bank, data were obtained from the bank website, internal control department and through personal interviews. The data obtained were analyzed qualitatively.

The study confirmed that internal controls were observed to be generally effective in the case study bank, but there are still some loopholes which are clear indications of failures in some of the control process.

Based on the findings of this study, it was recommended that antifraud seminars should be conducted on regular basis; job rotations within the bank should be planned by auditors and other senior officers to ensure effectiveness, division of responsibility as regards employees who handle financial transactions, and a viable internal audit to evaluate and oversee everyday transactions.

It was concluded that the bank`s internal controls if reviewed regularly and followed accordingly will help in reducing the occurrence of fraud.

Keywords Internal auditor, fraud, internal control

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1 INTRODUCTION

Fraud can be damaging to a business, especially in today`s unsettled economy. Its occurrence is ever-increasing on daily basis despite the fact that the banking industry is one of the most supervised and well-coordinated sectors in Nigeria. This leaves a doubting question in the heart of many people as to why it is so. Hence, the need for this research work, which helps explore how fraud occurs in the industry and the role of auditors in preventing it.

The banking sector is the bedrock of an economy. For any economy to be thriving, the financial sector must be solid, efficient, and effective because it is the sector that ensures the circulation of money into every other sector of an economy. The existence of a viable banking industry cannot be underestimated in a growing economy. Although the banking sector has been given out its vital function of being a change off in economic development in Nigeria in all branches, yet its operation over the years has not been healthy. This is because of fraud and other related activities that undermined the banks' full potentials (Ningi S.I. and Dutse A.Y. 2008).

Fraud has been identified as one of the major threats to the growth and development of the banking sector; even while control systems, policies and procedures are designed to bring errors to light, they cannot expose all fraud (Coenen, T.L., 2008, 2). The issue of fraud is not attributed to Nigeria only, but a global issue. Internationally, it has been a major problem given a precise definition of what is all about, but the definition of fraud according to business dictionary involves an act of deception, an intentional concealment, misrepresentation of data, or omission of truth in order to gain unlawful advantage. This definition requires auditors to understand the legal implication of the terms in the definition. The term misrepresentation in the context indicates false representation of accounting figure or material fact rather than a simple opinion (Vona, 2008, 5). To make the explanation of fraud clear, it is also important to explain what bank fraud is all about which is the main reason for this research work.

Bank fraud according to the legal dictionary is the use of deceptive measures to obtain money, assets, or other property owned or held by a financial institution, or to obtain money from depositors by fraudulently misrepresenting to be a bank or financial institution. For an action to be termed fraud there must be an untruthful intention and the action must be intended to benefit perpetrators to the detriment of another person. Bank fraud ranges from cheque kiting, money transfer fund, account opening, computer fraud, telex fraud, loans fraud etc. (Legal dictionary).

According to Oseni (2006), the perpetual frauds in the banking sector are getting to a level at which many stakeholders in the industry are losing their trust and confidence in the industry. Stakeholders are all those who have interests in the integrity of the bank: for example, shareholders, employees, suppliers, customers, or members of the general community (who could be affected by the social or environmental consequences of an organization`s activities). When this set of people lose their interest in the industry as a result of fraud, the bank tends to lose customers and money, because these shareholders are the major contributors of capital.

Efforts have also been made by the Apex bank to curb the incidence of fraud in the banking industry. For instance in July 2004, Central Bank of Nigeria (CBN) unveiled new banking guidelines such as the guideline on Automated Teller Machine (ATM) Operations, payment guidelines, credit guidelines etc. designed to consolidate and re-structure the industry through mergers and acquisition process. Banks and other Financial Institution Act (BOFIA) 1991, section 15, were also designed to prevent fraud and to make Nigerian banks more competitive and active in the global market.

The Nigeria Deposit Insurance Corporation (NDIC) raises concern over high incidence of fraud and forgeries in the banking sector. In a statement released by the Corporation public affairs unit, He noted that fraud cases within the banking industry contracts stood at 12,279 in 2015. This figure represented an increase of 15.71 per cent over the 10,612 cases reported in 2014. Thou, the amount involved decreased by 7.59 billion naira (17,555,221.46 Euro) or 29.63% from 25.608 billion naira (59,229,790.67 Euro) in 2014 to 18.021 billion naira (41,681,508.03 Euro) in 2015. The types and nature of frauds and forgeries were largely web-based, ATM card related, fraudulent transfer, among others.

The regulator noted that out of the 12,279 fraud cases reported by the commercial banks, 425 were attributed to staff while the highest percentage of frauds and forgery cases of 38.59 per cent by temporary staff (Www.Naija247news.com, Tuesday, June 28, 2016). The above statistical data reveals the level to which fraud had affected the financial strength of the banking industry in Nigeria. The frequent occurrence of fraud in the banking sector brings a doubtful question to mind as regards the competence, skills, due care, honesty, and integrity of auditors' role in banks. They are believed to hold a strategic position of trust which the general public rely on. It is this very strategic position and duty of trust bestowed on auditors that Ioasase (2004) notes that when fraud occurs in the work place, the question that readily comes to mind and always asked is "where were the auditors?"

According to Agbaje (1996), while commenting on the distressed condition of commercial banks in Nigeria in 90's stated that "it is a matter of regret that the confidence reposed on the auditors responsible for the affected banks has been dashed". This statement clearly shows the level of responsibility and trust the general public have in auditors as regard fraud detection and prevention in the banking sector. The detection and prevention of fraud in the bank should be considered as one of the main responsibilities of the bank auditors whether explicitly or implicitly stated in the bank statutory requirement in order to ensure the effective management and performance of the bank.

1.1 Research Problem

All organizations in one way or the other felt the consequences of fraud and its occurrence has resulted in financial loss. The existence of fraud in the banking industry has been a long time threatening factor which has affected their performance and profitability and in the long run may lead to distress. The evidence of this distress was a huge collapse of the commercial banks due to massive accounting and misappropriation related frauds. This problem resulted in the establishment of Asset Management Company of Nigeria (AMCON) to prevent distress especially in the Nigeria banking sector by acquiring and financing distress companies.

Fraud is a major threatening issue to the successful operation of the banking industry; all banks are vulnerable to it and in all facets of life (Olorunsegun, 2010). The bank`s customers expect banking operation to be accountability, fairness, transparency in their daily operation for effective intermediation. Though, there has been some reported cases of fraud in the banking sector, one major problem remained unsolved as to the nature and different means at which fraud is been perpetrated by the banks. According to Adeyemo (2012), he stated that fraud is only possible in the bank with support from an insider (employees of the bank). The banks are expected to carry out their duties with sincerity of purpose that will not undermine the public trust in them. This is of great importance if the banking sector wants to gain public trust and goodwill.

Another constraint is that the management has not put in place effective measures in the prevention of bank fraud. The management has failed to design accurate control measures which will help auditors to tackle some cases of fraud which are routine in nature and obtain sufficient understanding of the bank operating environment in order to assess and evaluate risk of material misstatement of the financial statement whether due to error or fraud and to design the nature and timing of audit procedures. The management might also override controls since they were the ones who established them and this might also pose a problem to auditors because over reliance on the punctured internal controls by management will cause a great havoc.

In Nigeria, despite the banking regulation and examination by the Central Bank of Nigeria (CBN), the supervisory role of Nigerian Deposit Insurance Corporation (NDIC), and the Chartered Institute of Bankers of Nigeria (CIBN), there is still a concern about fraud and other illegal practices in the banking industry. Evidence from the NDIC report (2008) shows that the report of examinations and special investigations showed that some banks were still bedeviled with the problem of fraud, weak board and management oversight; inaccurate financial reporting; poor record keeping practices; non-performing insider-related credit; declining asset quality and attendant large provisioning requirements; inadequate debt recovery; non-compliance with banking law, rules and regulations; and significant exposure to the capital market through share and margin loans (Uchenna, C.& Agbo, J. 2013, 14).

1.2 Summary of Research Problems

Despite the tremendous impact of bank fraud on the Nigerian economy, it is widely believed that there is little information available on the costs and impact of frauds in the Nigerian banking sector, how it occurs, and why. Fraud is a hidden problem that no bank likes to acknowledge or disclose. Only few banks are ready to publish the incidence of fraud in order not to tarnish their goodwill and undermine public interest in them, this is in line with the above problem noted by Adeyemo, (2012).

Similarly, there is no repository for gathering, analyzing, and disseminating fraud-related research findings and statistics. Nigerian banks has yet to reach a stage where all banks will come together to share their experiences and provide data for further research of the problem. Apart from the periodically updated NDIC (Nigeria Deposit Insurance Corporation) report which gives details of fraud related issues that has been reported by the banks, the psychological and criminological aspects require study and also, getting data for this type of research is a challenge.

In Nigeria, the multiple systems of fraud prevention tools developed by banks made it difficult to cover all of their line of defense and expose them to more fraud risk. Different tools of fraud detection are used across various channels instead of implementing a consistent and integrated approach that will truly fight fraudsters. For instance, a fraudster that does not succeed online could call in, and if the call center's screening process is not connected to the bank web fraud detection system, the fraud attempt might still scale through.

1.3 Objectives of the Study

The general objective of the study are highlighted below:

I. Examine the roles of internal auditors in the prevention of fraud
II. Examine various means employed in defrauding banks.
III. Suggest measures of reducing the incidence of bank fraud.

1.4 Significance of the Study and Limitations

This research work will be of great importance to the following groups:

- ✓ Banks and Financial institutions

  It will be beneficial to the authorities involved with banking operations, the management, staff, customers and prospective investors in the industry so as to identify the causes of fraud and the various means (theft, forgeries, embezzlement) employed to defraud banks in Nigeria.
- ✓ Government

The government will find this research work useful because it will enable them to set up policies that will enhance future decision making such as restructuring its agencies for better performance.

- ✓ General public

  This research work will be useful to the general public because the banking sector touches the life of everyone in the country. As such, problems such as fraud should be viewed with all seriousness in order not to affect.
- ✓ The time involved in this thesis was limited hence only few respondents were interviewed.
- ✓ The respondents also asked for non-disclosure of their identities.

1.5 Structure of the Study

This thesis is structured into five chapters. The first chapter contains information about the background of the study, research objectives, significance of the study and summary of research problems.

In chapter two of the thesis related literatures about internal audit in bank and fraud was discussed; ranging from nature and concept of auditing, fraud implementation and the role of auditor in fraud prevention. This chapter was later applied into empirical part of the thesis.

Research methods was explained in chapter three, which explains the methodology and source of data used in the thesis writing; the qualitative research method was adopted in carrying out the research and also data collection method through primary (interview) and secondary (journals and online webs) data.

Empirical framework was dealt with in chapter four, the bank internal controls was discussed and interview was carried out with the internal auditors of the case study bank.

Finally in chapter five, I present the summary and conclusion of the findings and suggest recommendations and the ways to improve internal controls in the bank.

2 REVIEW OF RELATED LITERATURE

In this chapter, an attempt is made to review related literature about the nature of bank fraud, internal auditing and its legal framework, the steps and skepticism involved in internal auditing in bank, as well as the role of auditor in fraud prevention.

2.1 Concepts of Bank Fraud and Internal Auditing

Bank fraud is an aspect of corruption and it occurs in organizations where governance structures and supervision are weak. Fraud covers a wide range of fraudulent acts involving intentional deception or misrepresentation (Georgio, L.V. 2015).

The institute of Internal Auditors International Professional Practices Framework (IPPF) Defines fraud as: “Any illegal act characterized by deceit, concealment, or violation of trust. These acts are not dependent upon the threat of violence or physical force. Frauds are perpetrated by fraudsters to obtain money, property, or to gain personal advantage.” Fraud impacts banks in many ways for example in financial, operational, and psychological ways. While the monetary loss owing to fraud is significant, the full impact of fraud can be unbearable. The significant losses to reputation, goodwill and customer relations for the bank can be devastating, even threatening its own survival.

The Association of Certified Examiners in the USA defines fraud as the “use of ones occupation for personal enrichment through deliberate misuse or misappropriation of employing organizations resources and assets.”

However, in the perspective of the financial industry and specifically the banking sector, fraud remains a big problem, especially in this recent financial crisis. Banking fraud therefore is defined as the use of intentional misrepresentation in order to deceitfully obtain money, assets or other property owned by a financial institution (Georgio, V.L. 2015, 4). Moreover, in criminal law, bank fraud is explained as intentional deception made to gain an undue advantage in order to damage the financial institution. It is different from normal bank robbery or theft, because the perpetrator usually perpetrates the fraud in secret hoping it will not be noticed until he has enough time to move on. It usually requires some sort of technical experience as well. Because of this reason, bank fraud is one of the offences referred to as white-collar theft. As fraud can be perpetrated by an employee within the organization or by people from outside, it is necessary to have an effective fraud management system in place to protect the organization's assets and reputation. While the senior management and the board of directors are ultimately responsible for a fraud management system, an internal audit can be a major help in tackling bank fraud by providing an evaluation of the potential for the occurrence of fraud. An internal audit can show an organization how it is prepared for and is managing these fraud risks. In today`s automated world, many business processes have embraced the use of modern technology. This allows for people committing fraud to take advantage of weaknesses in security, controls or oversight in business applications to commit their frauds. However, technology can also be a major factor of tackling fraud. Internal audit needs to embrace technology in their work as an important tool that can help prevent and detect fraud. Leveraging technology to implement fraud prevention helps protect organizations from the risk of fraud and reduce the time it takes to discover fraudulent activity (Georgio, V.L. 2015, 3).

2.1.1 Fraud in the Nigeria Banking Industry

Fraud in the Nigerian banking industry has always been at an alarming rate. Despite the major important role the sector plays in the economic development, its failures are becoming well noticeable. According to The Dictionary of Economics and Commerce, 200 banks were reported to be distressed in England between 1815 and 1850; fraud has been recognized as one of the reasons attributed to this failure.

The problem of fraud in the banking industry is a general issue that is not attributed to any economy, nation, or environment. The origin of bank distress in Nigeria can be traced back to the 1930s bank distress and crises. Nwankwo (1994) wrote that "the crises of confidence in Nigerian banking sector is not a new one, it has been with us for a long time. It occurred again during the banking doom and crash of the 1940s when all but four indigenous banks failed. In the late 1990s, 26 failed banks were liquidated at once while others went through various operations ranging from restructuring, renaming, acquiring and complete sales to new investors. One thing that in constant in all the banking reforms was that, fraud was a prominent factor in major failures. Several laws were put in place to reduce, alleviate and if possible eliminate the occurrence and incidences of fraud in the sector most popular among them are:

The Criminal Code Act, 1990 laws of the Federation: The criminal code of the federation exits above all other laws related to fraud issue in Nigeria. Though the law did not define fraud in an actual sense it makes provisions against frauds committed against banks. Section 435 of the criminal code act makes it a punishable offence with maximum imprisonment of seven years for any director or officer of the bank who destroys, alters, mutilates, or falsifies any book, document, valuable security, or account which belongs to the bank.

Section 436 also imposed punishment of a maximum of seven years on any staff or auditor of the bank who commits offences related to section 435.

Finally, section 472 also makes punishable provision for any person with the intent to defraud of a bank either through crossings on a cheque, or to alter cheques which crossings has been obliterated (CCA 1990).

The Banks and Other Financial Institutions Decree no. 25, 1991 (BOFID) : The Central Bank of Nigeria is empowered under the general provision of BOFID decree to license and regulate the activities of banks and other financial institution operating in Nigeria. The decree made provisions for punishable offences against any act committed by the directors or any other bank officers which are as threat to the normal running of a bank. Some of the provisions of BOFID that creates sanctions against malpractices in banks are explained below:

- **Insider Abuse Act – Section 18:** This section prohibits insider abuse and imposes sanctions against any act of fraudulence associated with the granting of loans and or credit facility by banks. Going by this provision, managers or officers of the banks are required not to have any interest or derive benefit in any credit facility granted to the customers, but in a situation where any interest exists, such interest must be disclosed from the onset.

  More so, bank officers are not allowed by the provision of this act to grant any loan or credit facility contrary to their internal rules and regulations and where such provision speculated them to obtain collateral, such collateral must first obtained before granting of loan. Any deviation from this provision carries maximum imprisonment of 3 years or a fine of 100,000 naira apprx.250 Euro (BOFID 1991).

- **Restriction on certain operations of the bank – Section 20:** This section restricts certain operations of the banks without prior approval from the Central Bank of Nigeria. Such operations include the maximum amount of loan or credit facility that can be granted to any customer. For merchant banks, it is 50% of the shareholders' funds while 20% for commercial banks (BOFID 1991).
- **Maintaining proper books of accounts – section 24**: This section made it compulsory for all banks to keep and maintain proper books of account in a safe place in respects of all transactions relating to the operation of the bank. Section 24(5) made it compulsory for bank directors and management to comply with the provision of this section in order to ensure that all financial statements submitted in relation to the bank are accurate and free from any form of falsification. Any director or bank officer who fails to comply with the provision of this act is liable to imprisonment of maximum five years or a fine of 10,000 Naira, approx. 30 Euro (BOFID 1991).

The Companies and Allied Matters Decree (CAMD) 1990: Section 281 of CAMD made it clear that the directors are trustees of the bank's money, properties and their power as such must give account for all the money over which they exercise control and are liable to refund any money improperly given out. The subsequent section of the same act impose a strict standard of behavior and duty of care on bank directors with a view to prevent fraudulent transactions by requiring them to exercise their duties in the best interest of the bank.

The provisions under section 503 – 508 imposed liabilities on directors or any other officers of the bank in the event of being wound-up. For example, these sections made it clear that any officer of the bank who falsifies any book of account in the event of being wound up is liable to imprisonment for two years (CAMD 1990)

Nigeria Deposit Insurance Corporation (NDIC) Decree 1988: The body is empowered under section 16(1) of this act to appoint an examiner with the power to examine periodically, and under condition of secrecy, the books and affairs of every banks in the country. Section 17(2) of this decree enjoins all banks to produce upon request by the examiner appointed by the body the necessary books accounts. It is a punishable offence for any bank under this section of the act to willfully refuse to produce any book, account, document or information; or negligently with intent to defraud. Section 19 of this act made a punishment of two years imprisonment for any director or officer of a bank who fails to take all reasonable care to secure the authenticity of any statement submitted in pursuant of this act (NDIC 1988).

Banks Employees (Declaration of Assets): Under the provision of this act, no bank director or any employee of a bank is expected to own assets in excess of his or her provable income. Contravening this offence carries 10 years imprisonment and forfeiture of the assets to the Federal Government of Nigeria.

In an attempt to solidify the banking industry, a recapitalization programme was instituted by the Central Bank of Nigeria (CBN), which was concluded on December 31, 2005. The twenty-five banks that survived, out of eighty-nine, witnessed remarkably structural changes in the area of shareholders fund, deposit base, branch network, size and ownership. Arising from the recapitalization requirement, a total of #360 billion was raised by banks in addition to foreign direct investment of 652 million U.S dollars. In addition, 20 out of 25 banks are now on the top ten in Africa while 17 out of 25 banks are in the top 1000 in the world (CBN 2006). In association with banking reforms of 2005, the least capitalized bank in Nigeria achieved a capital base of about #25 billion as against #1.3 billion before consolidation. In the same vein, the aggregate capital base rose geometrically from #311 billion to #932 billion. All these parameters are symbols of adequate preparation of the financial sector to jump-start the Nigerian economic development; the major noticeable implement to the attainment of this laudable objective is fraud (Owolabi, S.A, 242).

Currently the changes in the Nigerian banking sector have been outstanding. Of the top 100 companies in Nigeria, out of the first 20 are from banking industry. This clearly indicates that we can no longer afford to leave the banking sector in the hands of bankers because the only active players left in the economic playing field are the other banks; the other players are wounded – either limping (oil and gas) or in the case of manufacturing, confined to wheel chair (see Owolabi, S.A. 2010, 242).

2.1.2 Categories of Bank Fraud

Bank fraud can be categorized into two groups as follow:

1. **Internal Fraud**

Internal frauds are generally committed by the bank's employees and managers either individually or collectively through collision with outside parties. The detection of this kind of fraud poses a great threat to the organization because managers have access to most information and systems and have power to manipulate their actions because they know that their decisions may not questioned by others. Sometimes, they can collaborate or instruct junior employees to commit fraud on their behalf.

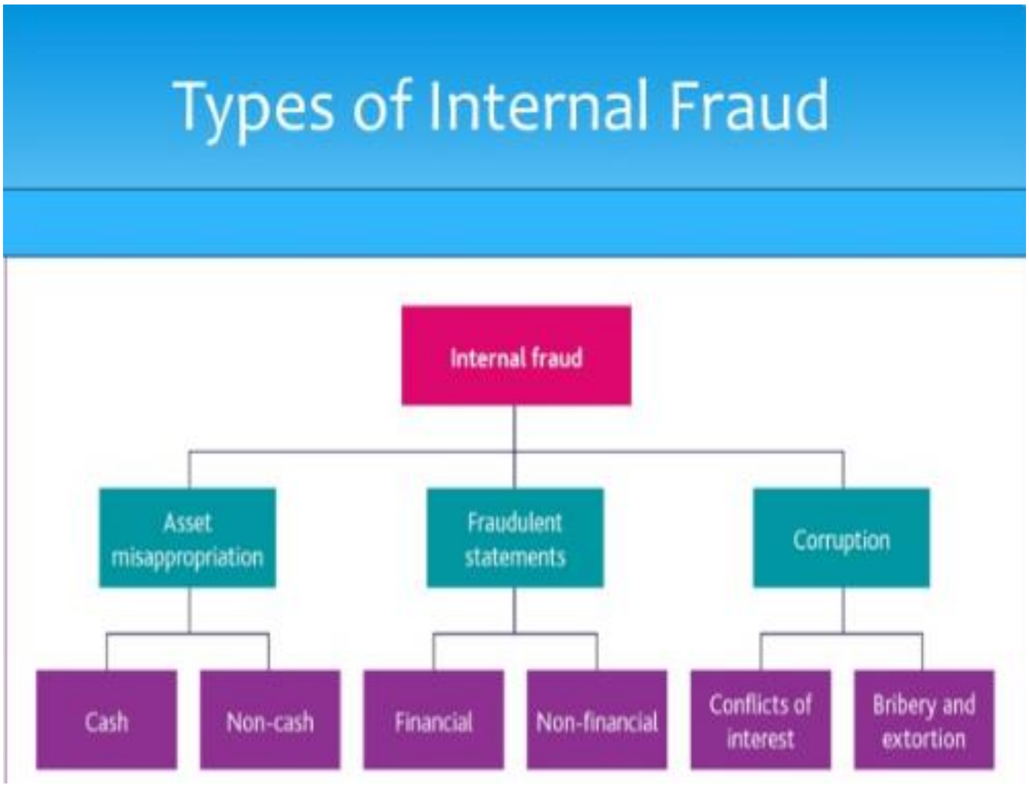

Figure 1. Types of Internal Fraud (source: Fraud Risk Management, CIMA 2008, 8)

i) **Asset Misappropriation** – Asset misappropriation fraud involves third parties or employees in the bank who abuse their position of trust to defraud the bank. This is also referred to as insider abuse. Typically, the assets stolen are cash and non-cash equivalent. The cash related aspect of asset misappropriation include the theft of fund after they have been recorded, false payment requests, cheque fraud, billing schemes, misuse of accounts. Non-cash misappropriations involve those schemes where employees misuse the non-cash assets of the bank such as theft of inventory, unauthorized use of bank property, forging signatures on payment authorization, adding private expenses to legitimate expense claims (CIMA 2008, 57).

ii) **Fraudulent Statements** – The most common method of perpetrating this type fraud is by intentional misrepresentation or misappropriation of financial transaction data involving manipulation of revenue figures e.g. manipulating expenses, improper disclosure, overstating assets etc. (CIMA 2008, 58).

iii) **Corruption** – Corruption is dishonest activity in which an officer of the bank abuses his/her position of trust to favor themselves of favor another person. Insider corruption practices in the bank take many forms including conflicts of interest, preferential treatment of customers in return for a monetary benefit, giving and accepting payments to favor or not favor other commercial transactions etc. (CIMA 2008, 59).

2. **External Fraud**

According to (ACFE), external fraud covers a broad range and is committed by third parties to the bank such as suppliers, partners, and customers. Other external fraud parties may include potential customers, government and criminal organizations. The perpetrators sometimes work independently or can liaise with the bank staff to defraud the bank. The various types of external fraud witnessed by the bank are money laundering related issues, identity theft and use of lost or stolen documents, use of counterfeit cards, theft and confidential information etc. these types of fraud can be relatively costly if it is not discovered on time. The probability that the bank could unknowingly be transacting with criminal gang is very challenging. If such transaction comes into limelight, the bank could face a great damage on its reputation and customer's confidence.

2.1.3 Who Commits Fraud

There are no special absolutes regarding the characteristics of those who perpetrate fraud in the bank. Rather, there are some common characteristics that have been identified by auditors. The identification of these characteristics has been a major tool in their fight against fraud in the banking industry (Coenen 2008, 26).

For instance, the Association of Certified Fraud Examiners (ACFE) has been conducting regular surveys of fraud investigators during the last decade to examine who perpetrate fraud, how it is done, what common features occur, and how has bank been able to combat the incidence of fraud.

Based on the revealed statistics from a fraud survey conducted by ACFE, 92% of the fraudsters have no prior criminal charges or any convictions related to fraud. Even though it is important for the bank to obtain a criminal record to weed out undesirable employees in their recruitment process, this has not proven to be effective as employees who commit fraud while on the job often do not even have a criminal record.

It was also revealed that the amount of money lost to fraud is most significantly influenced by the perpetrator's position in the bank. While examining the characteristics of the perpetrators in this particular type of people, it was concluded that their access to vital information in the bank creates the opportunity that makes it easy for the fraud to be perpetrated. For example, the higher a position moves in the bank, the greater access she or he is granted information to assets, data, and people that creates avenue to commit fraud (Coenen 2008, 28).

There is also a great similarity between genders that commit fraud in the bank. According to most recent ACFE survey which shows that 61% of frauds were perpetrated by men, while 39% were perpetrated by women. Given this percentage, the general consensus is that men and women participate in a fairly equal number of frauds in the bank but the severity of the frauds committed is different. For instance, men participate in much more costly frauds compare to their women counterparts in the bank. This clearly shows that frauds committed by men are more than twice as expensive because of the higher positions men tend to occupy in the bank (Coenen 2008, 29).

2.1.4 Fraud Theory

Since there are no absolutes as regard the characteristics of those people who commit fraud in the bank but there are theories put forward to explain rationale behind the fraud been committed. The understanding of the motive behind fraud is most important in preventing it. The proponent of the theory of fraud triangle came to the conclusion that the propensity for fraud occurred when three elements came together: pressure, opportunity, and rationalization. These elements are interdependent on each other for a person to actually commit a fraud.

Figure 2. Fraud triangle. (Source: Executive roadmap to fraud by Martin T. Biegelman, and Joel T. Bartow)

Financial Pressure – The first phase in the fraud triangle is pressure which is believed to be the motivating factor in committing fraud. It is the element that makes perpetrator act and often implies an emotion or desire. The fraud perpetrator in this situation has financial problems that he is unable to solve through legitimate means, so he begins to figure out illegal means such as stealing money or falsifying a transaction document as a way to meet its end means. The financial problem can be in form of inability to ones bills, drug addiction, desire for impressive status such as having a nicer car or bigger apartment etc. Financial pressure could also be as a result of lack of job security (an occasion which sometimes makes employees feel insecure on their job and look for any possible means to perpetrate before they are been sacked), or reduced bonuses (Biegelman, M.T, and Joel T.B, 2012, 33).

Opportunity – The second phase in fraud triangle is opportunity which explains the method by which the perpetrator carries out his/her fraudulent act. The opportunity to commit fraud has to do with which position the perpetrator is holding in the bank. The higher the position of trust a person holds the higher the likelihood that such person will have access to vital information, assets and records which he abuse to solve his financial problem with a low perceived risk of getting detected. In the case of fraud, opportunity to commit fraud could be as a result of weakened internal controls which employees or managers sometimes override or lack of segregation of duties. Among these three proposed elements, opportunity is the only area in which fraud prevention can prevail (Biegelman, M.T, and Joel T.B, 2012, 34).

Rationalization - The third phase of the fraud triangle is rationalization which explains how fraudster justifies their illegal act. The perpetrator in this situation try to justify their action has been honest who are caught in a bad set of situations. When the first two elements in fraud triangle (Pressure and Opportunity) come together, the fraudster in this situation is convinced that what occurred is never bad. For instance, a nation of borrowing from the bank money is consider to them as not been stealing since they are going to pay the money back; or by trying to justify their action due to inadequate compensation, lack of promotions or sense of mistreatment (Biegelman, M.T, and Joel T.B, 2012, 35).

2.1.5 Process that leads to Fraud

The major processes that lead to fraud in the bank are discussed from the institutional and environmental factors' point of view below:

Institutional factors

Asukwo (1999) and Idowu (2009), identified some of the causes and they are factors which are in the control of the management of the bank.

- **Poor Internal control**
  Inadequate internal control systems usually give way for fraudulent staff, customers and non-customers to perpetrate frauds. In finding solutions to this, there is a need to always have an effective and functioning audit department, security systems and observant staff at all times during and after bank official operating hours.
- **Poor book keeping**
  Inability to keep up-to-date books of accounts together with failure to balance the various accounts of the bank on a regular basis will result in frauds.
- **Poor remuneration**

Poor remuneration in terms of salaries and other benefits can also cause and encourage fraud. Employees that are less satisfied with their salary are often tempted to fraudulently convert the bank's money to their own use in order to meet their personal needs. This is common especially among the front line staff who on a daily basis have to deal with cash and other near cash instruments.

- **Frustration**

  Frustration in the work place as a result discrimination between the staff. This happens where one set of staff feels short-changed in terms of qualification, promotion and other financial rewards. This kind of frustration could lead to fraud as such employee would attempt to compensate himself in a fraudulent means.

- **Poor management**

  This is as a result of inadequate supervision by the bank. A greedy staff with fraudulent tendencies that is not being monitored closely would be tempted that the environment is secure for the perpetration of fraud. Poor management can also be as a result of imbalance in the management policies and procedures which a fraudulent minded operator in the system will capitalize on.

- **Inadequate infrastructure**

  For instance a poor communication system within the bank and the state of incessant power failure in the country has resulted in a build to unbalance of daily transactions.

- **Job rotation**

  The inexistence of this kind of situation in a bank is clear evidence of lapses in the management policies which encourage staff to overstay in one particular position for over a long period of time. The longer a staff stays in one particular position, the more proficient such staff is likely to be. For instance, a staff who has spent so long on a particular position may have accumulated of fraud been carry forward on a daily basis that no one else can uncover until such staff is been relocated to another unit.

- **Recruitment System** – Poor recruitment system where cognate experience is not being properly evaluated, relevant technical knowledge, area of competence, integrity and other sterling qualities are traded at the altar of non-performance-related factors such as societal connections and tribalism constitute important rationale in selection process.

Environmental Factors

Environmental factors are factors that can be traced to the immediate and remote environment of the bank. Several social issues encourage people to fall victim of fraud and thus join the group of fraudulent individual in the society. The Nigeria society can be seen as a materialistic environment where wealth is honored without questions. The desire to acquire wealth by all possible means is noticeable in almost every individual in order to be with the high and mighty caliber of the society whose source of wealth cannot be ascertained.

Major environmental factors can be categorized as follows:

- Honesty in offices is no longer encouraged. Honest staff is tagged and often despised and regarded as being too strict and not knowing how to utilize the opportunities at their disposal to make quick wealth.
- Much weight is placed on the accumulation of raw wealth in our society without the curiosity to know if the wealth is legitimate.
- In meetings, launchings or similar social events, the cynosure of all eyes are usually those who are in position to dole out cash or make mouthwatering pledges or promises of what to do. These are the ones that are instantly recognized and respected why nobody cares to know how they acquired the wealth.
- The dispensing of a chieftaincy title and similar honors has become highly monetized in favor of the rich and those who are in the highest position in the public

2.1.6 Fraud Concealment Strategy

Fraud can be perpetrated in banks through various means. Though the methods seem to be changing as new means are being devised with time. The most common means of perpetrating fraud highlighted by Akindele, R.I. (2011) were discussed below:

- **Account opening fraud**

  This involves the deposit and cashing of fraudulent cheques. This normally occurs when an individual open a transaction account with a bank with false identification papers with intention to defraud the bank. This type of fraud is detected by the bank through referee forms or status enquiry when closely scrutinized. Also in recent times, it has been mandatory for banks to do address verification before any transaction account is been opened. This is done by the marketing staff of the bank that pays visit to the customer at an agreed time to confirm the genuity of the address being submitted to the bank. (Akindele, 2010)

- **Cheque Fraud**

  The most common cases of this kind of fraud are through stolen Cheque and forged signatures of the account holder. This is very popular because cheques are used daily and not too hard to come by. Most times, this type of fraud does not collusion unless the perpetrator is greedy. In case of the forged cheque, the genuity of the cheque can be confirmed by the bank whenever such is presented for cash withdrawal by simply cross check through the use of mercury light which reveal the hidden security information on the original cheque, and also the forged signature can also be reconfirmed with the original signature of the account holder in the mandate.

- **Computer Fraud**

  This could be perpetrated by the corruption of a programmed, hacking, tampering with diskette to sign access to unauthorized areas and give credit to an account for which the fraud were not originally intended.

- **Clearing Fraud**

  This fraud is perpetrated by clearing of cheques. It is done by suppression of an instrument so that expiration of the clearing period applicable to the instrument, the collecting bank will give as though the paying bank had confined the instrument good for payment. Clearing cheques can also be substituted to enable the fraudster divert the fraud to a wrong recipient.

  Asukwo, (1991) states that, a local clearing item can be routed to an up country branch; the delay entailed will give the collecting bank the impression that the paying bank had paid the instrument.

- **Letter of Credit**

  This is the most common in international trading. These are instruments used across borders and can be forged, altered, adjusted and take no longer time to identify. So, in most cases, perpetrators escape.

- **Loan Fraud**

  This is perpetrated when funds are lent to non-borrowing customer or a borrowing customer that has exceeded his credit limit. In most cases, the staff is the perpetrators, like the cashiers, and they hide this from the management. In addition, manager sometimes override the issue of collateral and take out loan to finance their personal business.

- **Counterfeit Securities**

  It is regarded as one of the oldest form of crimes. Documents, securities, bonds and certificate could be forged, duplicated, altered or adjusted and presented for loan collection. Also cashier cheques, treasury notes, banker`s acceptance, certificate of deposit in an altered form could be presented to a banker´s redemption.

- **Money Transfer Fraud**

  A fraudulent money transfer fund may result from request solely for the purpose of committing fraud or the alteration of a genuine funds transfer request. This can be changing names, adjusting amount figures or account number. This form of fraud is made easy for fraudsters because of the ease at which they can be done for example through the mail, telephone, electronic process, telex and through the mobile banking application.

- **Telex Fraud**

  Coded messages for the transaction are sometimes hacked by fraudsters and possibly divert the funds to another recipient.

- **Unofficial Borrowing**

  This occurs when a cashier borrows from vaults and teller tills off the record. These borrowings are more rampant especially on weekends and during the month end when salary is yet to be paid. Also, this kind of unofficial borrowing is common among cashiers who have fast business that require cash to be run on daily basis. In this situation, a cashier collects deposit from customers in the morning without crediting the customer's account immediately and uses this money for his personal business while crediting the customers later in the day.

Expenses and Payroll

As a measure to regulate the expenses incurred at branch level, the bank has adopted the method of treating every expense incurred at each branch level before profit is being remitted to the head office at regular intervals. In the past, the process of transferring expenses incurred at each branch of the bank on monthly basis create the avenue for perpetrating fraud at the branch level by the administrative officer. This is an area in the bank where the losses cannot be ascertained and where the original prices of expenses incurred is poorly captured.

Committing any of the above discussed fraud presents the need to conceal the act. If the perpetrator is not certain the act can be concealed, they are not likely to commit the fraud unless the pressures or rationalization factors are present that the person's logic is overcome (Vona, 2008, 14). When employees commit any of the fraud discussed above for instance, part of their plan is how to disguise the true nature of the transaction. Generally, each fraud comes with a means of concealment but how employees disguise the true nature of the genuine transaction depends on the bank`s working system, the position of employee within the bank, internal controls system of the bank, and the use of computerized systems as against manual systems (Vona, 2008, 14).

In some instances, fraudsters may use more than one means of concealment techniques to disguise the true nature of transaction. How the fraud is been conceal depend on any the following:

- Management override – perpetrator in this situation uses their position of authority to approve a transaction or collide with other employees to approve the transaction
- Collusion – this allows perpetrator to evade the internal controls procedures which make it possible to provide a false representation of the transaction.

- False documentation – perpetrator in this situation uses an altered, missing, or created document to conceal the fraud (Vona, 2008, 15).

2.1.7 Effects of Fraud

The direct effect of fraud in the Nigerian banking sector is felt by the customers, in the long run it has a chain reaction on the community as a whole because the banking sector constitutes an important position in the community. Every single aspect of the economy especially the banking sector is prone to fraud, thus, its success or failure has a multiplier effect in determining the success of the community. Fraud has been identified as a major cause of bank distress. The number of fraud incidents that occur in Nigeria banks is on the increase with the overall effect on poor bank performance. The amount of money lost to fraudulent people is enormous; such amounts taken out of the banks do not generate any income for banks, but rather result to bank distress and liquidity problem. Frauds lead to loss of money which belongs to either the bank or customers. This loss results in a general decline of productive resources available to the bank. The following are some under listed effects of bank fraud

- It destroys the bank`s reputation
- It reduces bank`s profitability
- It places emotional and psychological burdens on the victims
- the bank ceases to meet up with staff welfare
- It discourages banking habit among the banking public.

2.2 Internal Auditing

Auditing in some form has existed was seen in for as long as men have been required to account for their transactions. Evolution of auditing dates back to the medieval ages. It was recorded that in the ancient Egypt or Rome, people were employed to examine the work done by tax collectors and estate managers. It is also on record that in ancient Britain, an independent person was employed by the Federal Barons to ensure that returns from tenant farmers accurately reflected revenues received from the estates. In other eras, emphases were laid on the detection of fraud and irregularities.

In Nigeria, Companies and Allied Matters Act **CAPC20LFN2004** has made it compulsory that every public liability company must have its annual financial statements audited before circulating them to members, specifically, Section 357(1) states as follows: "Every company shall at each general meeting appoint an auditor to audit the financial statements of the company".

An audit can be divided into two types namely: External audit and internal audit. The Auditing Practice Board (APB) defines External Audit as an exercise whose objective is to enable auditors express an opinion on whether the financial statements shows a true and fair view of equivalent of entities affair at the end and profit and loss for the period ended and have been properly prepared in accordance with the applicable reporting framework (for example, relevant legislation, and applicable reporting accounting standards) or where statutory or other specific requirements prescribe the term present fairly.

It should be noted from the above definition that audit is an independent of financial statements i.e. an auditor must be independent of those responsible for the financial statements i.e. the management. And that the matters to be addressed in the audit report are dictated by the terms of the auditor's appointment. It is important to note that the responsibility for the preparation of the financial statements rest with the management. The auditor's responsibility is to report on the financial statement as presented by the management.

2.2.1 Legal Background of Auditing

Since there was a great separation between the provider of fund for a business entity and its management, this gave rise to the need for an independent examination of account to protect investor's interest. The joint stock company Act of 1844 was the first Legislature in Britain to require all incorporated companies to have their annual financial statement examined by an independent person. First, the company's auditors were appointed from the shareholders. The Act of 1856 introduced the idea that the auditor should be independent of the company, and then encouraged the development of professional auditors. The company Act of 1876 made appointment of auditors compulsory for banking companies.

Early auditors were in many cases non-accountants who were required to state whether the account showed a true and fair view of the state of affairs of the company. It was the company Act of 1990 that required the auditor to be independent and the audit at that time concerned only the balance sheet alone. The Company Act of 1929 extended audit to include the profit and loss account. Finally, in the 1948 Act, Auditors were required to be professionally qualified and disclosure requirements were introduced.

2.3 Internal Auditing in Bank

The definition of internal audit is provided by the Institute of Internal Auditors (IIA) as: an independent, objective assurance and consulting activity designed to add value and improve an organizations operation. The internal audit activity assists an organization to achieve its objective by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and good governance processes

The internal audit functions as an independent department in the bank with primary responsibility of reviewing the effectiveness of management controls aim at mitigating the occurrence of frauds and protect the assets of the bank. Internal controls procedures are related to the day-to-day bank activities that need approval and authorization processes, account reconciliation, access restrictions and daily transaction controls, and physical security. These set of rules often include the separation of responsibilities in order to give room for checks and balances to reduce the occurrence of fraud.

The internal audit in banks particularly, is a department that is independent of the management. Their primary duty is to review the quality and effectiveness of controls within the banks, to manage and protect the assets. According to Basel Committee on Banking Supervisor (BCBS), an effective internal audit function independently and objectively examines the quality and effectiveness of a banks internal control system, evaluation of risk and good governance processes, which assists senior management and the board of directors in protecting their organization and its reputation (BCBS, 1997).

The Basel Committee on Banking Supervision (BCBS) principles for enhancing corporate governance require modern banks to have an internal audit department with absolute authority, independence, resources and access to the board of directors. As a result, independent, efficient and qualified internal auditors are of great importance in contemporary banking corporate governance. Moreover, banking supervisory authorities must be satisfied by the effectiveness of a bank`s internal audit function by requiring effective policies and procedures to be followed and that management takes appropriate corrective action in response to internal control weaknesses identified by internal auditors

(BCBS, 1997). An effective internal audit provides vital assurance to a bank`s board of directors as to the quality of the bank’s internal control system. In doing so, the function helps to reduce the risk of loss, fraud and reputational damage; and improve the efficiency and effectiveness of the bank`s risk management system, control systems and corporate governance. The internal audit function monitors the bank`s internal control systems by:

- Ensuring that audit activities are carried out by qualified personnel
- Determine whether the management has put in place appropriate measures to address control deficiencies and audit report recommendations.
- Determine whether the bank is operating in line with laws and regulations and adheres to established bank policies, procedures, and processes.
- Accessing the reliability, adequacy, and effectiveness of control systems that promote the safety and soundness of the bank.

2.4 Internal Auditing Process

International Standard Organization (ISO) guidelines on internal audit explain what is required for internal audit procedure. The standard spells out that the general procedure must define the area of internal auditor responsibilities and requirements for:

- ✓ Planning the audits;
- ✓ Conducting the audits;
- ✓ Communication with the board;
- ✓ Completion of audits work and recommendations.

Planning the Audits

In planning the audit, it is worth noting that emphasis must be laid on considering the status and importance of the area to be audited as well as meeting the conformity requirements of ISO 9001. Part of the statutory requirements explains that the internal auditor must be objective in their assessment. Therefore, it is required that the auditor is completely independent and gives no special treatment to any unit of the bank being audited audit.

Before conducting the audit work, the standard also requires the auditor to assess the size and nature of the audit. This includes a projection of how many members of the internal audit unit to be involved and how long the audit work will take. It also includes an assessment of any special or transaction-intensive investigations that auditor normally made during the audit. Before the audit work is being carried out, the auditor is expected to use their past experiences and the banking knowledge to attempt and predict areas where the unit to be audited have misstated financial information in the past.

Once this preliminary assessments have been made, the auditor creates a plan to carry out the audit.

Conducting the Audits

In carrying out the audit, the law requires the internal auditor to:

- ✓ Consider fraud risks in the assessment of internal control design and determination of audit steps to perform. Internal auditors are not expected to detect fraud, but internal auditors are expected to obtain reasonable assurance that business objectives for the process under review are being achieved and material control deficiencies – whether through simple error or international effort – are detected. The consideration of fraud risks is documented in the work papers, as well as linkage of fraud risks to specific audit work.
- ✓ Have adequate knowledge of fraud to identify red flags suggesting fraud may have been committed. This knowledge includes the characteristics of fraud, the techniques used to commit fraud, and the various fraud schemes and scenarios associated with the activities reviewed.
- ✓ Be alert to opportunities that could allow fraud such as control deficiencies. If significant controls are detected, additional tests conducted by internal auditors could be used to identify whether fraud has occurred.
- ✓ Examine whether management is actively retaining responsibility for oversight of the fraud risk management program, that timely and sufficient corrective measures have been taken with respect to any noted control deficiencies, and that the plan for monitoring the program continues to be sufficient for the program`s ongoing success.

- ✓ Evaluate the indicators of fraud and decide whether any further action is compulsory or whether an investigation should be recommended.
- ✓ Investigation should be recommended at the appropriate time.

Communication with the Board

The relationship between auditor and the board of directors includes reporting and oversight functions. Internal auditors, through the special role they perform, are well positioned to elevate the importance of fraud detection programs with management and the board staying aware of what is happening in their specific units which will enhance the internal auditors' ability to address fraud risks with the board.

In discussion with the board, the auditor may include:

- ✓ All fraud audits performed
- ✓ The fraud risk assessment process
- ✓ Fraud or conflicts of interests and results of monitoring programs concerning compliance with law, code of conduct or auditing ethics.
- ✓ The internal audit activity's organizational structure as it pertains to addressing fraud
- ✓ Coordination of fraud audit activity with external auditors
- ✓ Overall assessment of the organizations control environment
- ✓ Productivity and budgetary measures of internal audits fraud activities
- ✓ Benchmarking comparisons of internal audits fraud activities with other organizations.
- ✓ Role of internal audit in fraud investigations.

The auditor may have a genuine opinion from the senior management and the board as regards the right time to inform them of threatening issues including fraud. The way out for addressing this timing issue is for the auditor to have discussions with the senior management and the board before issues arise pertaining what they need to know, when they need to know it, and how the communication will be made. Conducting this discussion is evidence that the auditor is complying with IIA Standard 2060: Reporting to Senior Management and the Board.

Completion of Audit Work and Recommendations

At the conclusion of the audit work, the auditor drafts an audit opinion according to standard requirements. These documents literally state whether or not the information provided by the unit being audited is free of material misstatements or any error that aims at defrauding the bank. If these statements are reported correctly and free of error, the auditor issues a clean opinion, and if otherwise, the auditor issues modified opinion stating the error detected during the course of audit work such as missing cheques, receipts, wrong postings etc. stating these errors detected in the report assists the management in fixing those issues or preventing their recurrence in the future.

2.4.1 Skepticism Involved in Audit Process

Professional skepticism is an attitude that involves a questioning mind and a critical evaluation of audit evidence. An objective, skeptical internal auditor neither assumes that management or employees are not trustworthy.

In all aspects of the audit work, the exercise of due professional skepticism is important. Inadequate professional skepticism is always cited as a significant reason why internal fraud has not been detected. Internal auditors play a crucial role in the success or failure of fraud risk management. With their intimate knowledge of the workings of an entity, internal auditors are in a special position to identify many indicators of fraud. When internal auditors act within skepticism and they focus on the effectiveness of internal controls, the tendency that will discover the common features of fraud increases, and they might discover possible fraudulent activity if and where it exits.

In order for the internal auditor to exercise skepticism, IIA Standard 1111: Direct Interaction with The Board states that the auditor must communicate and interact directly with the board. In addition, Standard 1120: Individual Objectivity states that internal auditors must have an impartial and unbiased attitude, which is consistent with the exercising skepticism. The audit committee’s oversight and support of the internal audit activity helps the internal auditor maintain independence and objectivity as well as keep an attitude of skepticism.

2.5 Internal Auditor of a Bank

There are two different types of auditors; the internal and external auditor. An external auditor is an independent person or expert with the duty of examining the prepared account of business entities, forming an opinion as to the accuracy, truth and fair view, and reporting to the interested parties. While an "internal auditor" is an employee of a company charged with providing independent and objective examinations of the company's financial and operational business activities, including its corporate governance. Internal auditors also provide evaluations of operational efficiencies and will usually report to the superior officer in the company on how to improve the overall structure and practices of the company. (www.investopedia.com).

The Basel Committee on Banking Supervision (BCBS) stipulates that large banks and internationally active banks must have a viable audit committee or its equivalent. The audit committee in according to the provision of this body typically responsible for providing an oversight of the bank's internal auditor (BCBS, 1997).

According to BCBS in principles, the bank`s internal auditor is viewed as a separate entity i.e. The internal auditor must be independent of the audited activities, which requires the internal auditor to have professional competence including adequate knowledge and absolute authority within the bank, thereby enabling them to execute their tasks with independence and objectivity (BCBS, 1997).

2.5.1 Responsibilities of an Auditor

To the degree that fraud may be present in activities covered in the normal course of audit work, the auditing Standards state that internal auditor have the following responsibilities with respect to fraud prevention and detection:

Due Professional Care – It is expected of internal auditor to exercise due professional care by considering the:

- Extent of work needed to achieve the audit engagement`s objectives;
- Relative complexity, materiality, or relevance of matters to which assurance procedures are applied;
- Adequacy and governance effectiveness, management of risk, and internal control processes;
- Probability of significant errors, fraud, or noncompliance with rules;
- Assurance cost in relation to potential benefits (Standard 1220).

Risk Management – The internal auditor is expected to evaluate the risk exposures relating to the bank`s governance, operations, and information systems in relation to the:

- Achievement of the bank's strategic objectives;
- Reliability and integrity of financial system information
- Safeguarding of assets;
- Acting in accordance with the rule of laws, regulations, policies and procedures (Standard 2120)

Engagement Objectives – Internal auditor is expected to conduct a preliminary review of the risks relevant to the audit work under review. Engagement objectives must reflect the results of the risk management and controls.

However, most internal auditors are not expected to have the knowledge equivalent to that of a person whose primary responsibility is detecting and investigating fraud. Also, audit procedures alone, even when carried out with due professional care, do not guarantee that fraud will be detected. A well-designed internal control system should help prevent or detect material fraud. Tests carried out by internal auditors improve the likelihood that important fraud indicators will be detected and considered for further testing (Standard 2210).

2.6 The Role of Auditors in Fraud Prevention and Management

Fraud prevention is a collective effort form both the management and auditors, only auditors should not be saddled with the responsibility of preventing fraud in the bank. Nevertheless, the auditors can be of great assistance in helping to gather resources of different departments in the bank and work with top management including the employees and other people to prevent fraud.

Firstly, the management of the bank bears the larger responsibilities of establishing, maintaining, and enforcing an effective internal controls (Coenen, 2008, 148). Internal auditors play a major role by testing and evaluating the effectiveness of the bank`s internal control system if commensurate with the level of potential exposure or risk in the different segments of the bank`s activities. Though, the cost of creating, implementing, and maintaining effective internal controls can be high, there are some other checks and balances that are not expensive to implement like segregation of duties and regular reconciliation of statement (Coenen, 2008, 149).

On the part of internal auditors in combating the fraud, internal auditors may conduct proactive auditing to search for misappropriation of assets and information misrepresentation. This means that internal auditor is securing the physical assets by ensuring that all the bank`s doors are securely locked, locking of all the storage areas, secured desks and filling cabinets are locked, and maintaining good records of the assets (Coenen, 2008, 153).

In addition to this, internal auditors ensure that all blank cheques are secured especially access to room where cheques are being printed are restricted only to authorized personnel, access to computers are also secured with passwords, and data is protected with security software (Coenen, 2008, 153).

Segregation of duties is one of the most widely disregarded internal controls that often lead to fraud. The work of segregation of duties is performed by internal auditors without any prior notification aiming at separating the custodial, recording, and authorization functions in the bank (Coenen, 2008, 154). By separating the duties, it makes it difficult for one individual to assume the responsibility of initiating a transaction and complete it.

On the authorization of transaction level, internal auditors ensure that transactions are duly signed and verified by the appropriate officers of the bank (Coenen, 2008, 155). For instance in the case study bank, each cashiers has a paying limit which must be duly adhere with. If a customer is presenting a cheque for withdrawal that is above their paying limit, approval from supervisor must be seek for before finalizing the payment.

In formulating the general preventive measures, the bank needs to appreciate the main feature of fraud, one of which is that fraud is ever increasing with the advent of modern technology and it is highly profitable and source of cool money for the fraudsters. Based on this notion, comprehensive fraud prevention measures are not a one way plan that focuses on accounting department activities; it must be implemented across the whole departments for the best possible results (Coenen, 2008, 159).

The preventive measures according Coenen, (2008) includes fraud education, fraud investigations and proactive fraud preventive techniques which are dependent on each other, attempt to override one will cause the whole components to be ineffective (Coenen, 2008, 159).

Coenen, 2008 suggested that fraud education should be conducted on a regular basis. In line with this, internal auditors ensure that employees are given fraud awareness training in line with the management principles. For instance in the case study bank, training are always targeted at departments and job functions that have higher occurrence of fraud.

In developing a good fraud investigations, Coenen, (2008) suggested that a series of red flags that will cause management to consider investigation should be created. Internal auditors watch carefully those red flags and determine if there is any need for investigation in case of any suspicious transactions.

Also Coenen, (2008) suggested that the proactive preventive techniques should start with a risk assessment. Once these risks has been identified, management must develop a means to deal with them. This sometimes involves focusing on risks which can create larger financial loss in case of fraud.

The Central Bank of Nigeria also plays its role in helping banks manage fraud through monetary policy directives. As part of its monetary policy, Central Bank of Nigeria demands that banks should make provision against occurrence of loss through frauds from its gross profit earnings. This directive was formulated to protect the general interest of depositors.

2.7 Summary of Research Related Literature

A study of this nature will be incomplete without the review of related literature and other articles written on the topics by professionals in the field. This chapter discussed a historical overview of auditing and contemporary expectations as regard the functions and responsibilities of internal auditor in fraud prevention in the bank. Variety of questions for further exploration about internal controls process to combat fraud in the bank shall be discuss further in the subsequent chapter in this thesis.

The literature revealed different challenges postulated by the theory of fraud such as the pressure which explain the motivating factor in committing fraud, opportunity which explains the method through which perpetrator carries out its fraudulent act; while rationalization explains how a fraudster justifies their illegal act. Out of this reviewed related theory of fraud, it was discovered that fundamental theory recognizes that opportunity is an essential part of the fraud triangle and is the one area in which fraud prevention can excel (Vona, 2008, 60).

Another major issue that emerged out of the review is that fraud prevention in bank should be seen as a collective effort from both the management and internal auditors. Only auditors should not be left with the absolute responsibility of fraud prevention in the bank. It is evident from the review that there is a strong synergy between the management which formulate the control processes and the internal auditors. Coenen, (2008) opined that, in order to attain this synergy of managing fraud in the bank, there is need to develop a preventive measures such as fraud education, fraud investigations, and proactive fraud preventive techniques.

Chapter three will systematically examine the research methodology and data collection method used in gathering information for this thesis work.

3 RESEARCH METHODS

In this part an attempt is to present the method used in this thesis. More so, to give the explanation of the thesis design, instruments and method of data analysis used.

This thesis is designed to look into the role of internal auditors of a bank in fraud prevention. The various methods used in the data collection are as follows: personal interview guided by semi-structured questionnaire, observation and secondary data.

Research is a systematic process of gathering and analyzing data in order to increase understanding of the fact about which are interested (Sachdeva, J. 2008, 13). A good research according to Sachdeva, (2008) must have scope and limitations of the research work to be defined clearly without any ambiguity, findings are presented in such a way that they are free from unambiguously and all conclusions be justified by adequate evidence, and all data are analyzed and explained adequately. The objectives of any research work can be achieved with different techniques like qualitative and quantitative.

Qualitative research is concerned with qualitative fact relating to or involving quality (Kothari, C. 2004, 4). Qualitative methods are normally used at various stages of research including data collection and data analysis (Sachdeva, J. 2008, 173). The techniques at data collection stage includes focus group, individual in-depth interviews, case studies, and action research observation (Sachdeva, J. 2008, 173). The techniques at analysis level focus on content analysis of written or recorded materials drawn from participants' expressions, and evidence from the physical environment. Qualitative research focuses on achieving an in-depth knowledge of a situation and make little attempt to generate representative sample (Sachdeva, J. 2008, 174).

Quantitative research is concerned with the measurement of quantity or amount. It is applicable to fact that can be expressed in terms of quantity (Kothari, C. 2004, 3). The number of respondents during quantitative research often run into thousands which can results in large set of data to analyze except interpreting through the use of statistical data which make the data interpretable into fewer numbers (Sachdeva, J. 2008, 202).

The research methodology that will be used in this thesis will be qualitative research method where emphasis will be on the understanding of the respondents view on the subject matter. The goals of qualitative research are many, depending on the purpose of the particular project. One clear goal is that qualitative research method is that research structured with the idea of evaluation of the effectiveness of programs or policies as in the case of this research work (Saldana, 2014, 4).

3.1 SAMPLE TECHNIQUES

Sample techniques refers to the technique or the approach the researcher adopt in selecting items for the sample (Kothari, 2014, 56). The sampling for this study was restricted to specific type of people in the case study bank and therefore were able to provide the information needed to conclude on this thesis. Specifically, non-probability sampling methods was employed to select participants for this study. A non-probability sampling is that sampling method which does not afford any basis for estimating the probability that each item in the population has a chance of being selected in the sample (Kothari, 2004, 59).

3.2 DATA COLLECTION

The two sources of data to gather relevant information for this thesis are discussed below:

Primary sources

Primary source is used to gather initial material during the thesis process. This data collection uses techniques such as surveys, direct observations, and interviews (Sachdeva, J. 2008, 116). Primary sources of data allow researcher to access original and undiluted information from the source.

For this study, primary data was collected from the interviews conducted with informants from the case company internal auditing department which comprises of Three (3) respondents (The Regional Auditor Manager, Branch Internal Auditor, and Area Control Officer). An in-depth interview was conducted with the case study bank (United Bank for Africa Plc) through telephone and teleconferencing due to geographical distance. This method was adopted to enable the researcher get access to first-hand information that will help solve the research problem regarding the research questions. The researcher was able to ask directly from internal auditors concerning their role in fraud prevention in the bank. This allows for a question-answer response. Therefore, these method are used to arrive at reasonable information needed to locate serious details for this thesis.

Secondary Sources

Secondary data are those which have been collected by another researcher and has passed through the statistical process (Kothari, C. 2004, 95). They are considered to be one of the cheapest means of access to information and takes the role of analyzing, explaining, and combining the information from the primary source with relevant information (Sachdeva, J. 2008, 116). Secondary data gives support to primary data in order to gain deeper knowledge about the role of auditors in fraud prevention.

The secondary data used in this work includes academics journals (electronic and prints), documents and materials of the case company.

3.3 Validity and Reliability

The validity of any measure is the degree to which researchers have discovered what they think their results show and how relevant the results are to other populations. Validity of this research work was achieved since the respondents who had the opportunity to answer the interview questions had adequate knowledge in internal auditing and controls in the case study bank.

4 INTERNAL CONTROL IN NIGERIA BANKING SECTOR

The methods used in data collection for the thesis were clearly explained in the previous chapter. This helped in gathering the useful information needed for the thesis. This chapter focuses on the review of the case study bank (internal controls process). The findings from the case study bank are analyzed qualitatively in order to reach a conclusion and suggest recommendations regarding fraud issues in the bank.

Internal controls include the policies and procedures that financial institutions formulate to reduce risks and ensure they meet their daily operating, reporting, and compliance with set objectives. The oversight duties of internal control cannot be delegated to others within the system or to third parties, the operational activities of the bank might be delegated to others.

Poor internal controls have been identified as one of the major causes of fraud in bank. For instance, the highest fraud incidence ever reported in any particular year by a Nigerian bank occurred in 1998 when United Bank for Africa Plc wrote off 786 Million Naira (2.4 Million Euros) on account of fraud and other malpractices. Because of this, the bank has consistently improved its internal control systems to ensure effective management of frauds.

According to the COSO published of 1992 which established a framework for internal control and provided evaluation tools that businesses and other entities could use to evaluate their control systems. These basic components are related to the operational effectiveness and efficiency, reliable and financial reporting and ensuring regularity. The five basics components are: fostering a free risk environment, control environment, managing risk assessment, formulating control activities, providing effective information and communication, and conducting monitoring of the effectiveness of control policies.

Going by these five components, the success of any system of internal control is relying on how effective each of these elements are well articulated with each other.

4.1 Introduction of Case Company

United Bank for Africa Plc is one of Africa's largest financial institutions with operations in 19 African countries and 3 global financial centers; New York, London, and Paris. UBA has been operating in Africa since 1949, referred to then as the British and French Bank Limited (BFB). It took over the assets and liabilities of BFB and was incorporated as a limited liability company on 23rd February 1961 under the compliance ordinance (cap 37) 1922. In 2005, it completed one of the biggest mergers in the history of Nigeria's capital markets with the business combination with Standard Trust Bank (STB) plc. From then, it continued to expand to other Africa countries (www.ubagroup.com).

4.1.1 Business Summary

UBA is a financial services institution, which provides commercial banking and pension custody services to its corporate, commercial and retail customers. The company operates through three segments: Corporate banking, Retail/commercial banking and Treasury and Financial markets.

The corporate banking segment provides a broad range of financial solutions to multinationals, regional companies, state-owned companies, non-governmental organizations, international and multinational organizations and financial institutions.

The retail/commercial banking segment provides commercial banking products and services to the middle and retail segments of the market. The treasury and financial markets provides innovative financing and risk management solutions and advisory services to the company's corporate and institutional customers.

4.1.2 Case Study Bank Internal Control Systems

The nature and operation of United Bank for Africa Plc. requires an effective system of internal control which is normally review by the board of management for effective management. These controls are designed to prevent the occurrence of fraudulent activities in the system. Some of the controls discuss below are gotten from internal guide of the bank are highlighted below:

- ✓ **Custody Control** – Access to strong room, vaults, and other sensitive places in the bank are restricted to authorized personnel only. In most cases, entering into these places require the presence of another two designated bank officials like manager and branch operation manager. A sign in and out form is maintained to monitor the entrance of people into these places.
- ✓ **Segregation of Duties** – No staff of the bank is allowed to have absolute control over a transaction. Line of duties are segregated in such a way that a transaction has to pass through more than one person before it is been authorized. The segregation of duties allows one person's work to authenticate that transactions initiated by another employee are duly authorized and recorded according to the bank's regulation. For instance, the policies stipulate that an officer of the bank processing the loan should not perform more than one of the following tasks: accept a loan request, disbursement of loan proceeds, or accept loan payments, and also information technology personnel is not allowed to initiate and process transactions, or correct any data errors unless corrections are required to complete timely processing. Additionally, every paying cashier has a minimum withdrawal request she or he can process. If the withdrawal request is above their paying limit, approval is needed from line supervisor like cash officer or branch operation manager. This gives the possibility of fraud being reduce when two or more people are involved in transaction processing.
- ✓ **Authorization** – In granting loans and overdrafts, every branch of the bank has a limit they can grant customers on request. Limit is placed on every branch manager's authority. Approval is always needed from higher authority from facilities request that is above their limit.
- ✓ **Reviews of customer's account** - Customer accounts are always review at regular interval to detect any unusual lodgment of funds, possibly to detect any fraudulent transaction.
- ✓ **Active Internal control department** – The control department within the bank inspects the banks operation on a daily basis. The cashier work is review by the control department on preceding day basis. This involves regular verification of journal, mandate and signature verification, review of general ledger account with the source of entry, particularly as to who originated and approved such transaction, and to check cashier cash till.

- ✓ **Sound personnel policies** - Sound personnel policies are essential components of effective control systems. This policy requires that the boards and officers of the bank to check employment references, hire most qualified officers and competent employees, and perform periodic performance reviews.
- ✓ **Vacation Policies** – The bank have a policy that requires all employees and officers to be absent from their work for a definite period of 21 working days. This policy is highly effective in revealing any fraudulent activities which usually require a perpetrators ongoing presence to manipulate accounting records, respond to inquiries, and conceal early detection.
- ✓ **Rotation of Personnel** – This system ensures that no employee stays longer than expected in a position for a long period of time. The bank rotation system is planned by the auditor with the approval from the top management to ensure effectiveness.
- ✓ **Cash Controls** – This system ensures that each teller have a separate cash drawer to which they have sole access. The bank disregards the use of common cash funds.

4.2 Interview Question and Answer

This research work aims at identifying the role of internal auditor of a bank in prevention of fraud. In order to achieve the aims of this research work; some background questions were asked to know what roles internal auditors play in fraud prevention in the bank; questions were also asked related to different frauds confronting the bank, and questions also came up through my theoretical studies. The interview was conducted with three key personnel from internal auditing department of the case study bank (Regional Auditor Manager, Branch Internal Auditor, and Area Control Officer). The questions were answered to the best of their knowledge and their opinion are quite almost all the same. Answers were collected and presented in the appropriate manner in which the questions were asked. The findings are presented in four themes namely: benefits of Auditors, Fraud concealment, Fraud motivation and Fraud Prevention.

BENEFITS OF INTERNAL AUDITORS

With this question, the intention was to find out the benefits and role which internal auditors play in the prevention of fraud in the case study bank. The first two questions in the questionnaire were asked to discuss this issue in details.

According to the respondents' views, there are enormous benefits which bank derives from having a viable internal auditing department. Opinion on their benefits are quite similar as they must have been conversant with several internal control checks based on their long time working experience with the bank thereby justifying their answers. The respondents are of the views that the existence of a viable internal auditors has help the bank at determining the fairness of the bank`s operational activities, determines if the operational activities are performed efficiently and cost effectively. These benefits are in line with the responsibilities of internal auditors discussed under the theoretical framework as stipulated by Auditing Standard. In ensuring this cost efficient operation, they cited instances from their internal routine check report in which they have suggested means of reducing wastages at each branch level of the bank which has improved the efficient way of using the bank`s resources. Most of these internal checks are in line with internal controls of the bank discussed in the previous chapter. To affirm this further, the respondents highlighted that fraud preventive measures is what they do on daily basis especially checking of transactions journal to review the compliance level. In this regard, exceptions are normally pick against transactions which are not done according to the bank`s regulation and communicate to the officer involved for quick reconciliation.

FRAUD CONCEALMENT STRATEGY

This question was asked to know the different ways in which fraud is been concealed in the bank. Eleven types of fraud I discussed in my theoretical were mentioned during the interview. Among the process listed and according to the respondents view on this question, the advent of modern technology in recent time has increased the occurrence of computer fraud making it the highest perceived type of fraud currently affecting the bank. The respondents pointed out that the recent complexity and over reliance on technology by all and sundry have created more fraud opportunities and other forms of exploitation especially on the internet and other electronic platforms for fraudsters, and also with the increase in the use of mobile payment transactions and other electronic payment platforms. Fraudsters has also deployed various means of defrauding the bank customers like creating of fake mobile applications on the websites of the bank. The fake applications are used to extract customers` details and financial details with intention of defrauding the customers. To affirm this concealment strategy further, the loan fraud according to the respondents view were perpetrated mostly by issuing authority like managers who give final approval for loan. The concealment method of this kind of fraud happens when manager takes out loan without taking appropriate collateral either from customers due to bribery or use the loan to finance their own business. All other types of fraud discussed also occurred but some are routine in nature except for unofficial borrowing which the respondents said is widely practice by mostly all employees of the bank. The practice of unofficial borrowing according to the respondents is very rampant especially when the month is running out. This happens when a cashier collects a cash deposit from customers and deliberately fails to credit the customer`s account to meet his/her financial needs. Employees who commit this kind of fraud were able to succeed because of the fact that not all account holders subscribe to transaction alerts because of the transaction fee involved.

MOTIVATION FACTOR

This question was designed to know what motivates fraudsters to commit fraud. The motivating factors according to the respondents vary because of the fact that the ability to identify and rank motivating factors is difficult on a person-by-person basis within the bank. Eight processes that lead to fraud derived from the literature review were made mentioned as basic motivators towards engaging in fraud. One of the respondents was of the opinion that internal controls do not always function as intended by the board of management and while the transactions may show that control is functioning, the employee on the other hand might not be processing the transactions in accordance with the control guidelines. Another respondent cited poor management as a motivating factor for committing fraud. He pointed out that the management has turned recruitment of employees to a bi-annual task in which they recruit any time they deem fit and layoffs whenever they want and do not consider the psychological effects of it on the employees. This also made employees look for any possible means to perpetrate fraud because of the fear of losing their job. The third respondent cited poor remuneration as a result of employees' entry level certificate in same profession as a motivating factor.

FRAUD PREVENTION

This part of the interview focuses on analyzing the respondents views with the three research`s theory, which are pressure, opportunity and rationalization. As discussed in chapter two of this thesis, propensity for fraud occurred when three elements came together: pressure, opportunity, and rationalization. To justify the findings with the theoretical framework, it was discussed in the theoretical framework that pressure as a motivating factor to commit fraud could be as a result of inability of perpetrator to pay bills, lack of job security, or poor remuneration, while the opportunity to commit fraud could be as a result of poor internal control system which perpetrators override; or rationalization which the perpetrators use to justify their action when the first two elements came together. Respondents cited the case of unofficial borrowing to justify this point. All these points are strongly connected with the theoretical findings and findings discussed above.

As regard what the management has put in place to curb the occurrence of fraud in the bank, some of the internal controls mentioned in the findings were presented and in addition to this controls, the respondents added that the bank has put in place formidable and efficient fraud control measures such as periodic integrity test, asset declaration and oversight function of monitoring staff members life styles in order to reduce the occurrence of fraud. This study make use of the same theory to analysis the respondents view on this preventive measures further which are discussed below:

PRESSURE

The respondents cited that they work to identify any possible pressures the bank policies could have on employees. Working to relieve pressures discussed in the interview can help prevent occurrence of fraud.

OPPORTUNITY

In eliminating the opportunity to commit fraud in the bank, the respondents pointed out that they work to ensure the effectiveness of the internal control policies of the bank; communicate these policies to employees; and by conducting proactive auditing, frequent reviews of record books, and careful verification of all transaction documents.

RATIONALIZATION

Another way to prevent fraud in which the respondents pointed to is by keeping employees of the bank from being able to rationalize their bad behavior. They cited that the bank has a zero tolerance policy towards fraudulent act and always employees of this policy on a regular interval. The notion of unofficial borrowing from customers was sighted which the bank has a zero tolerance for.

4.3 Summary on research`s findings

The findings had shown that fraud are motivated by pressure, opportunity, and rationalization. The severity of the fraud committed varies with perpetrator and the methods to conceal the true nature of transaction always vary with the perpetrator position in the bank, the use of computerized systems, and lapses in the controls system.

5 CONCLUSIONS & RECOMMENDATIONS

This chapter summarizes the results from thesis findings, conclusion and additionally the necessary recommendations were made based on the results from interview.

This thesis examined the role of internal auditors in fraud prevention in the bank and it also looked into the internal routine and controls on fraud prevention by auditors in the bank.

5.1 Summary of Findings

The findings of the thesis were as follows:

- ✓ The internal auditor`s role is to help in fraud prevention in the bank and this is achieved by assessing the potential for fraud within the bank through identification of fraud motivating factors.
- ✓ The internal auditor also helps in fraud prevention by studying and obtaining sufficient understanding of the bank`s environment and conduct the audit with due professional care.
- ✓ The internal routine and control systems of the bank, if meticulously put in place, assists the auditor in preventing fraud. In regard to this, the information gathered from the study indicated that the case study bank undertakes various internal controls to prevent occurrence of fraud. The following internal controls were identified:
  - Proper control of the bank`s vault
  - Job rotation
  - Cash controls
  - Regular review of customer`s account
  - Vacation policy.
- ✓ The degree of professional experience of the auditor also assists in preventing fraud.

5.2 Recommendations

Based on the above summary from the findings of this research, the following recommendations were made:

- ✓ A successful fraud risk assessment by the auditor will identify the employees that is vulnerable to fraud within the bank and once the auditor has identified this, the board of management can implement a fraud prevention program that will decrease the fraud risk.
- ✓ A viable audit committee to evaluate and oversee everyday transactions of the bank and assist the management with oversight of reporting any lapses in the internal controls process of the bank.
- ✓ There should be division of responsibility as regards employees who handle financial transactions. The likely occurrence of fraud reduces when two or more employees are involved in processing a transaction.
- ✓ The management should also put in place a mechanism through which employees can anonymously report possible frauds and suspicious activity within the bank.
- ✓ Antifraud seminars should be conducted on regular basis to employees.
- ✓ Job rotations within the bank should be planned by auditors and other senior officers to ensure effectiveness and the rotations should not be communicated ahead of time to the involved employee

5.3 Conclusions

Conclusions drawn from the research indicated that most frauds happened because of the poor internal controls, poor book-keeping, poor remuneration, and employee’s frustration on the job, poor management system, and lapses in the recruitment systems etc. accompanied with the fear from the bank in exposing the frauds to the public in order not to tarnish their goodwill. The research further revealed the controls processes if follow accordingly will help in reducing the occurrence of frauds in the bank.

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Respondent 1. Regional Auditor Manager, UBA Ilorin, Kwara-State, Nigeria.

Ilorin, Nigeria. 13.04.2017. 16.00 – 17.00, 06.10.2017. 16.00-16.30.

Respondent 2. Branch Internal Auditor, UBA, Ilorin, Kwara-State, Nigeria

Ilorin, Nigeria, 17.04.2017. 16.30-17.00, 06.10.2017. 16.00-16.30

Respondent 3. Area Control Officer, UBA, Ilorin, Kwara-State, Nigeria

Ilorin, Nigeria, 18.04.2017. 16.00-16.30, 06.10.2017. 16.00-16.30

APPENDICES

Questionnaire guide to internal auditor of the case company

THE ROLE OF INTERNAL AUDITORS IN FRAUD PREVENTION (A CASE STUDY OF NIGERIA BANK)

This study seeks to understand the role of auditors in fraud prevention in Nigeria banking sector, the method of perpetrating the fraud by both employees and external customers, and evaluate the internal control measures in place. Your views will be expressed as confidential as possible.

1. What exactly does internal auditor do?
2. In your opinion, what are the benefits of internal auditors?
3. What are the types of fraud confronting the bank?
4. What are the common indicators of fraud among employees?
5. What are the common indicators of fraud among bank customers?
6. What do you think motivates staff involvement in fraud
7. What has bank put in place to curb the occurrence of fraud?

APPENDIX 2