



Research on Controls and Strategies to Prevent Fraudulent Financial Reporting in Large-Sized Companies

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Abstract

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<p>This research-based bachelor's thesis analyses the concept of fraudulent financial reporting, the factors that influence fraud, and the role of internal controls, audit, technology, and other practices in mitigating its occurrence. The study aims to provide insights into the most efficient controls and strategies to detect and prevent fraudulent reporting within organizations. This was achieved by assessing the effectiveness of these practices while also pinpointing their limitations, which could potentially expose vulnerabilities to fraudulent activities. Additionally, this thesis provides practical guidance on implementing and continuously updating these controls, ensuring companies remain vigilant of the ever-evolving fraud risks.</p> <p>The thesis comprises two sections: theoretical and empirical research. The theoretical framework provides an overview of the concept of fraudulent financial reporting. This includes theories discussing the determinants and motives for committing fraud, the most common types of financial statement fraud schemes, and real-world case studies illustrating these concepts.</p> <p>The empirical section is based on qualitative methods and analyses the results of the data gathered from a series of surveys and interviews carried out over the course of the study. The surveys were divided into two parts: the first part was administered to external auditors, while the second part targeted professionals working in large-sized firms in Finland. Simultaneously, unstructured interviews were conducted with three participants, each possessing significant expertise in the field of finance and especially the concept of fraud. The data gathered were analyzed using statistical analysis for the surveys and thematic analysis for the interviews. The collected data were also compared to the theory framework to highlight the practical implications and real-world relevance of prior studies related to the subject.</p> <p>The results from the research provided a step-by-step approach to recognizing and preventing the risks associated with financial statement fraud. These are based on the combination of previous studies and the recommendations from the professionals and experts who participated in this research. The results reveal that the first step is that a company should identify the possible motives behind fraud to recognize the warning signs and avoid the likelihood of it occurring already in the early stages. The second step is to classify the common types of financial statement fraud that could potentially arise given the nature of the firm's business, as well as the gaps in the current prevention strategies employed by the firm. The last step is then evaluating which controls and measures would be the most effective. This approach allows a company to select and implement anti-fraud practices, as identified in the second step of the process, that align with its specific needs and address the gaps identified in its existing controls and measures.</p>
Keywords Financial statement fraud, internal control, audit, risk management, data analytics, sustainability

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1 Introduction

This is a research-based bachelor's thesis for the Degree Programme in International Business with a major specialization of Financial Management at the Haaga-Helia University of Applied Sciences.

The following chapter demonstrates the structure of the thesis. The initial section of this chapter provides the background context of the research topic. It aims to offer readers an understanding of the relevance of the chosen subject matter. The second subchapter introduces the research question and investigative questions. The research question defines the purpose of the study and guides the entire research process. It is broken down into investigative questions to help explore the research question systematically.

Finally, the benefits of the research demonstrate how the outcomes of the study can be utilized by the stakeholders that could benefit from it. Moreover, it assures that the considerable time and effort invested in this project yield meaningful results. The last section talks about the key concepts and theories related to the topic to help the readers familiarize themselves more with the fundamental ideas underpinning the study.

1.1 Background to the Topic

Financial statements reflect the performance and overall financial health of a company, hence, potential investors use them as one of the main sources to determine whether they should invest in a business or not. The accuracy and reliability of financial statements are paramount for investors in making well-informed investment decisions.

In recent years, sustainability, specifically, Environmental, Social, and Governance (ESG) factors, have also been gaining special importance among investors (ACFE 2022, 6). ESG represents a set of non-financial criteria that companies are incorporating into their strategies to promote and assess the sustainability of their operations while addressing the expectations of various stakeholders including investors, consumers, employees, regulators, and communities (PwC 2023).

Although not a new concept, the growing recognition of ESG aligns with the globalized and competitive nature of today's markets. Individuals increasingly make conscious choices as consumers, favoring companies that support their ESG values. These choices demonstrate how consumers perceive value beyond financial metrics. Because of this, investors are increasingly relying on businesses' ethical decisions and employment of ESG-related policies, in addition to companies' financial performance, as bases for their investment decisions. (ACFE 2022, 6)

Gaining a credible investor is one of the main goals of a firm alongside maximizing their profit, gaining a competitive advantage, and enhancing reputation. Consequently, some firms have tendencies to unintentionally create inaccuracies in their financial statements or in worst-case scenarios deliberately produce fraudulent financial reports in the hopes of achieving these goals. (Okike 2011, 1–2.) On top of that, with sustainability gaining widespread attention and being more present in annual reports, there is a growing potential for firms and individuals to engage in fraud to also attain sustainability goals and gain investors' recognition (KPMG 2020, 7).

The Association of Certified Fraud Examiners or ACFE reported from their global study (2022, 9) that financial statement fraud is detected in only 10% of fraud cases, which makes it the rarest form of occupational fraud. However, it is the costliest and has the most negative impact on a firm, with a median loss of 593 000 US Dollars. In addition to that, it is determined that financial statement fraud schemes typically last for 18 months. With a median loss exceeding half a million dollars and a duration of almost two years, financial statement fraud schemes have the highest velocity of 32 900 US Dollars per month. This means that financial statement fraud schemes tend to have the greatest negative impact on a company in terms of financial loss. (ACFE 2022, 14–15.)

Throughout the history of accounting, there have been some cases of accounting fraud scandals committed by huge corporations. One example is the American blue-chip security systems enterprise Tyco International, in which the CEO and the CFO had overstated the business's earnings by over 500 million US Dollars in their financial reports (U.S. Securities and Exchange Commission 2006). Another huge fraud scandal was with the American telecommunications enterprise WorldCom, in which the management reportedly inflated the company's cash flow by nearly 3,8 billion US Dollars (Berenson & Romero 2002). Both cases resulted in similar harmful consequences including incarceration of responsible individuals, substantial job losses, and multi-billion-dollar costs to investors.

Fraudulent financial reporting is generally less prevalent in the European Union member states, particularly in Finland, compared to some other countries. However, Europe encompasses a diverse array of nations each with its own set of laws and regulations. Additionally, the European Union itself has varying and somewhat fragmented fraud policies. (Quirke 2000) This complexity can pose challenges when it comes to effectively applying and implementing fraud prevention measures across different European institutions.

Moreover, even in large economies within the EU, there have been some accounting fraud scandals that have had negative consequences. A case in point is the German fintech company Wirecard, which artificially inflated its revenue and balance sheet through fictitious transactions involving third-party partners. This scandal resulted in the prosecution of several key individuals

within the company. It also drew attention to the German authorities who had supported the company and highlighted regulatory delays in initiating investigations. (Poltz 2022) These financial statement fraud scandals and the scarceness in the laws and fraud policies between the member states of the EU and the whole of Europe prove that the risks of accounting fraud in Europe have always been present and need to be continuously addressed.

The studies, statistics, and cases highlighted above justify the need for enterprises in Finland to be aware of the risks of financial statement fraud. It is imperative to actively find mechanisms and strategies that are currently in place or adopt newly introduced efficient methods to prevent instances of financial statement fraud. Making this a central focal point should be a priority for companies.

1.2 Research Question

This thesis aims to provide a summary of valuable controls and strategies that various companies around Finland utilize to produce reliable and accurate financial statements and avoid potential fraud. Achieving this goal involves a complex approach, encompassing an exploration of the theoretical aspects of the topic, as well as gathering insights from real-world companies operating in Finland that have adopted established practices for mitigating the risks of fraudulent reporting. The advantages and disadvantages of each method are also taken into consideration to assess which procedures could be the most effective.

The research question (RQ) of the thesis is:

RQ: What are the most effective approaches for detecting and mitigating the risks of financial statement fraud?

The research question is divided into investigative questions (IQs) as follows:

IQ 1: What is fraudulent financial reporting and the factors influencing it?

IQ 2: What measures and mechanisms are presently taken to detect financial statement fraud and how effective are they?

IQ 3: What are the perceived gaps or challenges in the current controls and strategies and how to address them?

The table below is an overlay matrix that contains all the relevant information about the investigative questions, the key components of the theoretical framework to achieve the research objectives, and the research methods that will be used to collect and analyze the necessary data

needed to complete the research. The research results for each investigative question are also determined.

Table 1: Overlay matrix

Investigative Questions (IQs)	Theoretical Framework	Methods	Results (chapter)
IQ 1. What is fraudulent financial reporting and factors influencing it	Financial reporting, accounting laws, regulations and standards, financial statement fraud, and the fraud triangle.	Desktop research, surveys, and face-to-face thematic interviews.	4.1.1
IQ 2. What measures and mechanisms are presently taken to detect financial statement fraud and how effective are they?	Internal controls, internal and external auditing, whistleblowing and other anti-fraud controls.	Desktop research, surveys, and thematic interviews.	4.1.2 4.2
IQ 3. What are the perceived gaps or challenges in the current prevention strategies and mechanisms and how to address them?	Advanced fraud schemes, the application of IFRS, robust risk assessment and internal controls, and the role of external audit.	Surveys and thematic interviews.	4.1.3 4.1.4 4.2

1.3 Delimitation

This research emphasizes the problem related to business management in the field of finance, specifically in accounting and financial reporting. The emphasis is on the stakeholders involved in the finance operations of an organization. This includes managers, accountants, auditors, government, investors, and employees.

The primary focus of this research is to investigate fraudulent financial reporting, particularly looking into financial statement fraud. This excludes other primary types of occupational fraud, which are asset misappropriation and corruption. The study on financial statement fraud is

underpinned by the significant implications it bears for stakeholders, especially investors, management employees, and the broader financial market.

The target companies for the thesis are large-sized companies operating in Finland. Fraud can occur in organizations regardless of size. Nevertheless, large-sized companies could be more prone to fraud due to a combination of factors such as the complexity of their operations, larger financial footprint, hierarchal structure, and less direct communication between employees and the top management.

For the analysis of the topic, this paper will primarily concentrate on auditing, internal controls, risk management, and technology aspects, since they are the common methods used by large-sized companies to combat financial statement fraud.

1.4 Benefits

The results and conclusion of this research provide a summary of the most effective controls and strategies for large-scale enterprises in Finland to mitigate the risks associated with fraudulent financial reporting. A step-by-step guide is specified, from identifying the motivations for committing fraud and the challenges in the current fraud prevention practices applied by companies to evaluating the most suitable anti-fraud procedures for an organization based on the previous steps.

This step-by-step approach is formulated based on the opinions, experiences, and recommendations of the professionals and experts, who participated in this research. The participants are employees in large-sized firms, with most of them working in the finance field. Therefore, the data collected from them are reliable, up-to-date, and offer a real-world perspective on the topic.

Lastly, uncovering the ethical and sustainability issues surrounding the subject and highlighting the consequences of inaccurate reporting contributes to fostering a culture of sustainability, ethics, and integrity within organizations. Recognizing the ethical and ESG-related issues of financial reporting is also important, for finance students and professionals in their career development. The author can benefit mostly from this research, especially as a finance student and professional. The study encompasses awareness and knowledge about the ethical and ESG-related issues in accounting specifically in financial reporting, which often surface during the author's professional journey as an auditor, and are anticipated to continue to provide enduring benefits throughout the author's career in the finance field.

1.5 Key Concepts

This chapter provides the definitions of the key concepts and terminologies used throughout the research paper. These concepts will be explained in more depth in Chapter 2, which is the theoretical framework.

Financial statement fraud:

Occurs when an individual intentionally manipulates the financial statements or engages in unlawful activities that directly and materially impact the financial statements, all with the intention of misleading investors and creditors (Gupta & Nasib 2012).

Internal controls:

Internal controls are processes and/or policies that are implemented by company management and the board of directors. They are planned and employed to give reasonable assurance for accurate financial reporting (Harrison et al. 2014, 275).

Audit:

An analysis of an organization's financial report. The main objective is to examine the financial statements and determine whether the information given in the financial report reflects the overall financial position of an organization and is according to the requirements of the auditing standards, which are established by a government body. (PwC Middle East 2023.)

Data Analytics:

It is the process of assessing, cleaning, transforming, and interpreting data to discover valuable insights, patterns, and trends. This involves using various tools to extract meaningful interpretations from big sets of structured and unstructured data. (Sedkaoui 2018, 46-47.)

Robotic Process Automation (RPA)

RPA is a technology that utilizes software robots that copy human interactions that are otherwise repetitive, time-consuming, involving multiple people or multiple and complex steps, at high risk, and so on. Automating these processes eliminates human error, increases the efficiency and precision of the results, and improves the overall quality of work. (Tripathi 2018, 10-11.)

2 Theoretical Framework

This chapter demonstrates the literature framework of fraudulent financial reporting. First, general classifications regarding the theme, including theories explaining the determinants and predictors of fraud tendency, as well as examples of real-life cases related to the subject, are explained. Later in the chapter, the existing mechanisms and strategies utilized by companies in Europe are explored by explaining their effectiveness and how they are implemented into businesses.

2.1 Financial Statements and Financial Reporting

Given that this thesis research is about the concept of financial statement fraud, it is important to establish clear definitions for financial reporting itself and the financial statements that typically constitute this process. This involves explaining their elements, preparation methods, and presentation to stakeholders.

The International Accounting Standards 1 (IAS 1 Presentation of Financial Statements) states that the purpose of preparing financial statements is to provide details about an entity's financial condition, performance, and cash flows. This information aims to be beneficial for stakeholders involved in the economic decision-making process of a firm. To meet this goal, financial statements should include accurate data on the entity's assets, liabilities, equity, income, expenses, contributions from equity holders, and cash flows.

According to the IAS 1 (IAS 1 Presentation of Financial Statements), a complete set of financial statements includes the following:

1. A balance sheet (statement of financial position)
2. An income statement (statement of profit or loss)
3. A statement of changes in equity
4. A cash flow statement
5. Notes, which provide essential information about accounting policies and other explanatory details.
6. Comparative information presenting the corresponding figures for the prior period.

A balance sheet reflects the financial position of a business at the end of the period by comparing its assets, which are valuable resources against its liabilities and stockholders' equity (ownership claims to those assets). An income statement, on the other hand, provides a summary of a company's revenues, expenses, gains, and losses over a certain period, depicting its financial performance.

A statement of stockholder's equity provides a breakdown and reconciliation of the beginning and ending balances in the elements of stockholder's equity presented in the balance sheet. This information helps the stakeholders understand the factors that contributed to the changes in the

equity and, hence, provides insights into the concern's financial health and distribution of earnings. Lastly, a statement of cash flow presents the fluctuations in cash over a specific period. The inflows and outflows of cash are related to the day-to-day operations, investments in assets or securities, and financing activities including debt or equity transactions. The information gives insights into the company's cash utilization and management, and therefore, reflects its liquidity position. (Doran 2012, 4–16.)

2.2 Financial Statement Fraud

The concept of fraudulent financial reporting has been present throughout the history of accounting and financial reporting. However, the collapse of the energy company Enron in 2001, following its scandal exposing the firm's deceitful reporting practices, contributed to increased awareness of the potential risks of the subject (Constable 2021). While the specific terms “fraudulent financial reporting” or “financial statement fraud” may not have been used extensively prior to the Enron scandal, fraudulent reporting practices and the need for actions regarding the problem have long been recognized in the accounting field.

In the 1999 research study (Beasley, Carcello & Hermanson 1999, 7) sponsored by the Committee of Sponsoring Organizations of the Treadway Commission, fraudulent financial reporting is described as the deliberate misrepresentation of financial statements or financial disclosures. It can also refer to the engagement in unlawful action that has a material direct effect on the financial statements. This separates financial statement fraud from other factors that can lead to materially misleading financial statements, such as unintended errors and corporate misconduct.

The Association of Certified Fraud Examiners (ACFE 2020, 86) provides a definition with examples: “A scheme in which an employee intentionally causes a misstatement or omission of material information in the organization's financial reports (e.g., recording fictitious revenues, understating reported expenses, or artificially inflating reported assets).”

Both definitions emphasize that fraudulent financial reporting and financial statement fraud result in material misstatements or omissions in financial reports. The second definition further highlights the involvement of the stakeholders within the company, which are individuals, such as employees or management.

2.2.1 Factors that Influence and Predict the Tendency of Fraud

To further understand the concept of financial statement fraud, it is crucial to recognize the underlying motives and other factors that drive individuals to commit fraud. This also helps in identifying individuals who are more likely to engage in fraudulent activities.

The nature and drivers of fraud can be described by the fraud triangle, which was originally laid out by Donald Cressey in 1953. The fraud triangle is composed of three characteristics that are described as criteria for someone to commit financial statement fraud. These three elements are incentive/pressure, opportunity, and rationalization. (Rezaee 2019, 3)

Panel A: Fraud Triangle

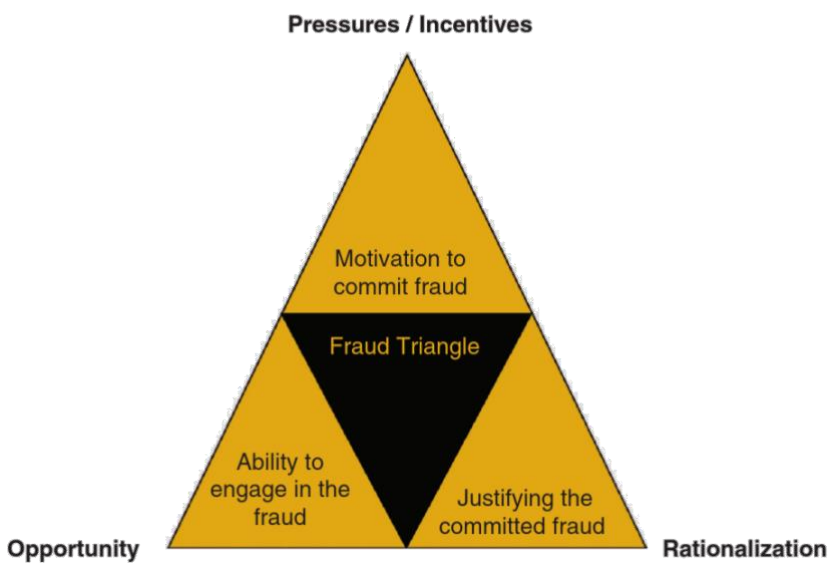


Figure 1. The Fraud Triangle (Rezaee 2019, 4)

The first element of the fraud triangle is pressure, which can arise from financial or personal circumstances. Financial pressure may include being burdened with debt or having unrealistic expectations to consistently exceed previous financial results. Personal motivations may come from greediness, the desire for psychological satisfaction, or the perceived need to prove oneself to be capable of doing the impossible for recognition. (Harrison Jr., Horngren, Thomas & Suwardy 2014, 274.) In other instances, like in a corporate environment, the concept of incentives is often analyzed as operational and financial characteristics that serve as motivating factors for the management to conduct more aggressive accounting policies and practices (Rezaee 2019, 5).

Perceived opportunity refers to an individual's belief that they can commit fraudulent actions without being detected or facing significant risk of exposure (Dorminey, Fleming, Kranacher, & Riley 2012, 558). This opportunity often arises when there are inadequate or ineffective internal controls in place. Ineffective controls can be the absence of password constraints, a lack of

safeguards against collusion, or the capability to bypass or override critical activities. Conversely, when there is a robust internal control system that includes a strong separation of duties and consistent checking of areas with higher inherent risks, the opportunity of committing fraud is diminished. (Rezaee 2019, 6.)

Once the perpetrator has a motive or pressure and has identified an opportunity, this individual creates a rationalization of his/her intentions. This means that the perpetrator creates internal justifications and convinces themselves that their actions are necessary under the circumstances to lessen or eliminate their guilt. (Harrison et al. 2014, 275.)

The fraud triangle is an effective model to help understand the topic and has been used by many experts and associations in the finance field. For example, one of the Big 4 auditing companies in the world PricewaterhouseCoopers has used the concept in explaining the nature of committing fraud and has further created surveys about these factors under the fraud triangle contributing to the tendency to commit fraud (PwC 2018).

2.2.2 Creative Accounting

Creative accounting refers to a collection of practices that managers use by taking advantage of the flexibility given to them by the accounting rules and regulations to present their organization's financial health in a more favorable light than its true state (Jones 2010, 5). According to Colasse (Balaciu, Bogdan & Vladu 2009, 174), these practices emerge due to limitations of standardizations and the unlimited nature of human creativity. It may seem like creative accounting should be illegal, however, it does not violate the law or any accounting standards. Instead, creative accounting is seen as a practice that works within the regulatory system. Utilizing the flexibility provided by accounting regulations, individuals manipulate the measurement and presentation of financial accounts to prioritize the interests of those preparing the accounts rather than serving the needs of the users. (Jones 2010, 5.)

On the contrary, managers may cross the line and deliberately violate the accounting standards and procedures to deceive users of financial statements. As mentioned in Chapter 2.2, financial statement fraud represents more severe misconduct, which involves deliberate and deceptive practices, such as inflating revenues, misclassification of liabilities, or engaging in other fraudulent activities to manipulate the financial statements for personal or organizational gain. In conclusion, creative accounting is the exploitation of flexibility in the accounting regulatory framework within acceptable boundaries, whereas financial statement fraud involves purposely breaching rules to manipulate financial information. The borderline between the two is vague, which indicates that a

perpetrator or a company can use both creative accounting and fraud when given enough pressure and opportunity. (Nişulescu & Popescu 2014, 63.)

2.2.3 Financial Statement Fraud Schemes

Financial statement fraud has a wide range of deceptive practices engaged by individuals or organizations to purposely manipulate financial information for the goal of misrepresenting the true financial health of an entity. The schemes involve falsifying financial statements, distorting key financial metrics, and concealing illicit activities.

One of the most common types of financial statement fraud schemes is **improper revenue recognition**. This means manipulating the recognition of revenue to inflate the reported income, however, it's not always the case. Gerard Zack mentions in his book (Zack 2012, 6–7) that revenue schemes can be classified into four categories:

1. Timing schemes
2. Fictitious or inflated schemes
3. Misclassification schemes
4. Gross-up schemes

Perpetrators conduct timing schemes by transferring income from one accounting period to another. After two or more periods, the fraud then self-eliminates. This action is against the accounting principles; therefore, it is considered a fraud. The most common way of doing timing schemes is when revenue is recognized earlier in the financial statements. In practice, this means that future revenues are borrowed in the hopes of improving the current results of the company's performance. Companies are motivated to resort to this type of scheme when they are falling short of revenue expectations. Perpetrators who commit this believe that this is a temporary hurdle and that the firm's results for the future would be better. (Zack 2012, 6–7.)

Fictitious revenue involves recognizing additional revenue without any basis whatsoever, encompassing fake customers, transactions, or both. Inflated revenue, on the other hand, comprises genuine customers and legitimate transactions, but the value of transactions is artificially inflated through various methods. (Zack 2012, 6–7.)

Misclassification schemes do not directly impact the overall financial results of the company. However, they can have a significant material impact on specific key financial metrics by categorizing transactions improperly, and as a result, those transactions end up being included in the wrong line items of the financial statements. (Zack 2012, 6–7.)

The last method of revenue schemes is the gross-up scheme, which is similar to the misclassification scheme where the bottom line is not directly impacted. Instead, gross-up

schemes involve overstating revenue and expenses associated with it by equal amounts. This type of scheme is exploited when the firm aims for growth or a specific revenue target but falls short of those expectations. The main goal is to make the business appear larger, handling a larger volume of transactions and activities (Zack 2012, 6–7.)

Asset misrepresentation is another type of financial statement fraud. In this practice, assets may be overstated or misclassified. The scheme includes manipulation of reserves, which involves manipulating the allocation of reserves, altering the useful lives of assets by modifying the expected duration of asset usefulness, and neglecting necessary write-downs, which means failure to reduce the value of assets to their appropriate levels when required, and manipulating fair market value estimates. This involves deliberately altering the valuations of the fair market value of assets or liabilities. The indicators for these schemes could be repeating negative cash flows despite reported earnings, large declines in customer demand and increased business failures within the industry or economy, and lastly, reliance on subjective assessments or uncertainties when estimating assets, liabilities, revenues, or expenses. (Ernst & Young 2009, 3.)

Other types of include **understating expenses**, which result in higher operating income and net income. This involves categorizing the cost of goods sold as non-operating expenses to avoid affecting the gross margin negatively, capitalizing operating expenses by reporting them as assets in the balance sheet rather than expenses, and omitting certain expenses and reporting in incorrect periods. Other financial statement schemes comprise **smoothing or earnings**, which means overestimating liabilities during prosperous periods, and excess funds are then stored to offset future potential declines in revenues, **improper disclosure of information** particularly in relation to transactions involving related parties and loans provided to management, and lastly, **execution of highly complex transactions** especially those involving structured finance, special-purpose entities and off-set balance sheet structures, and unconventional counterparties. (Ernst & Young 2009, 3-4.)

2.3 Company Cases in Europe

This subchapter sheds light on company cases of fraudulent financial reporting specifically within the Europe context. While the subject may be less common in Europe and especially in Finland, it is crucial to understand the seriousness and the potential depth of the damage it can cause to a firm and the economy overall. There have been several notable cases of financial statement fraud, with one of them being the infamous Tesco accounting scandal. Other examples are from smaller companies compared to Tesco, which demonstrate the occurrence of fraud and the scale of its damage regardless of the size of an entity.

2.3.1 Tesco

Tesco, which is one of the largest retail chains in the world has been exposed to an accounting scandal that unfolded in 2014. It involved the overstating of profits by £263m. Tesco inflated its revenue by manipulating its income and expenses. This was done by accelerating the recognition of income and postponing the recognition of expenses. This then resulted in artificially inflated profits in the business's financial statement. One of the practices involved recognizing revenue earlier than allowed under accounting standards. (Felsted & Oakley 2014)

The scandal resulted in significant financial and reputational damage for the entity. Tesco was investigated by regulatory bodies, including the Serious Fraud Office (SFO) and the Financial Conduct Authority (FCA). The firm was fined £129m by SFO and has separately settled a payment of about £85m to compensate for the damage it has caused to investors affected by the overstatement of its profits. Along with other legal costs, Tesco had been charged with a total of £235m. Multiple names had also been mentioned resulting in Tesco's chief executive at that time, stepping down from his role. With the new chairman, the company has implemented various measures to strengthen its financial reporting practices and its overall corporate governance. (Kollewe & Ruddick 2017)

2.3.2 Folli Follie

The Folli Follie scandal, although smaller than Tesco as a business, had also caused vast damage and affected a lot of individuals involved in the establishment. Folli Follie is a Greek luxury goods retail company founded in 1982. It has since gained prominence in the luxury retail market and managed to expand into an international retail brand operating in various countries. (McCrum 2018)

The investigation of the firm started in 2018 when a hedge fund called Quintessential Capital Management (QCM) raised concerns about the 2017 figures in Folli Follie's financial statements. As the investigation unfolded, it was revealed that the enterprise deliberately engaged in various practices to inflate its financial performance. These included overstating their revenue, manipulating inventory records, and fabricating financial statements. One example of the evidence found from the investigation was the inflation of the company's inventory and trade receivables. It was calculated that the inventory was inflated by half a billion dollars and the receivables by \$600bn. Overall, it was concluded that Folli Follie has recorded \$1bn of fake sales in 2017. (McCrum 2018)

Folli Follie's accounting scandal resulted in multiple trials for individuals involved in the deception. A total of 13 defendants were sent to trial, including the founder himself, as well as his wife and

son. The other defendants were the firm executives, including individuals from Folli Follie's Asian subsidiary. (Kokkinidis 2021)

2.4 Fraud Detection and Prevention Methods

This chapter focuses on exploring the measures and mechanisms presently employed by companies in Europe to eliminate and prevent financial statement fraud. The chapter begins by presenting the current regulations, policies, and accounting standards implemented in Europe to ensure the reliability of the information given by companies on their financial position, as well as to alleviate the risks of fraud. In addition to that, the key components of robust internal controls and how they are implemented by companies, including segregation of duties, authorization procedures, and regular audits, are examined. Finally, the growing role of technology and other strategies such as whistleblowing and fraud risk assessments, are analyzed.

By delving into these strategies, the chapter aims to provide an overview of the various methods currently utilized by European companies. Examining their effectiveness and limitations through reliable literature sources, readers can gain insight into the importance of implementing appropriate and efficient practices to enhance the transparency and trustworthiness of companies within the corporate world.

2.4.1 Financial Statement Fraud Regulation and Prevention

The effective uncovering and deterrence of financial statement fraud in Europe relies heavily on a robust framework of fraud policies, regulations, and accounting standards. These essential guidelines set the foundation for companies to ensure the accuracy, reliability, and transparency of their financial reporting.

The fraud policies in Europe, specifically in the European Union have been described as scattered. This means that there is no permanent or centralized framework, which results in coordination challenges when operating internationally, especially given the varied legal and accounting systems across the member states. Hence, effectively coordinating the fraud policies of various European institutions becomes a complex undertaking due to these disparities. (Quirke 2000)

Until 1999, UCLAF acted as the main EU organization in to fight against fraud. UCLAF had collaborations with national anti-fraud departments and played a pivotal role in coordinating and offering the necessary support to combat transnational organized frauds. In 1999, a new anti-fraud institution European Fraud Prevention OFFICE (OLAF) was established, whose main responsibility was to carry out investigations on the matter within the member states and local institutions. OLAF ensures the development of these policies in the EU, the safety of the financial interests of the EU

at the community level, and the essential task of reporting and recommending measures to the Commission department, EU institutions, and Agencies. (OLAF 2023)

As mentioned earlier, even with the establishment of OLAF, the lack of centralization on anti-fraud policies within the member states makes it challenging to strengthen the measures against fraud. However, the accounting standards applied within the EU seem to be more uniform, which enhances the quality of financial reporting, and therefore, ensures the transparency and reliability of financial statements. In 2002, the International Financial Reporting Standards (IFRS) was applied and accepted by the International Accounting Standard Board (IASB) and has since then increased the coordination of financial reporting. Publicly listed companies are required to prepare consolidated financial statements to give an overview of their financial performance and health. Limited liability companies, on the other hand, must produce annual financial statements and submit them to the appropriate national business register. All these financial statements must be in accordance with IFRS. (Regulation of the European Parliament and of the Council 1606/2002/EC)

Transitioning to IFRS has been particularly challenging for companies and auditors. The complex nature of IFRS standards and significant differences from previous accounting standards have made it more difficult for auditors to adopt IFRS. Furthermore, staying updated with evolving IFRS standards and complying with new requirements also demand significant effort and resources from auditors. Despite these challenges, IFRS plays a crucial role in upholding the integrity of financial reporting and promoting transparency and reliability in financial statements produced within the member states. (Achek & Khlif 2016, 338-340.)

2.4.2 Internal Controls

Effective internal controls are of utmost importance when preparing financial statements. These controls play a pivotal role in mitigating the risks of fraudulent financial reporting and add essential credibility to the financial statements. Weak internal controls are usually the main reasons why perpetrators get the opportunity to commit fraud. Sadly, many organizations realize the significance of implementing a robust internal control framework when it's too late, and deceitful activities have already occurred.

The Committee of Sponsoring Organization of the Treadway Commission (COSO 2013, 3) refers to internal controls as procedures and practices established within an organization to ensure accuracy and reliability in financial reporting, safeguard an entity's assets, and achieve compliance with relevant laws, regulations, and accounting standards. The three main objectives are, therefore, the consistency of financial reporting, adherence to laws and regulations, and efficiency of the entity's operations.

In 1992, COSO published its *Internal Control–Integrated Framework*, which can be utilized by companies as a structure of guidelines on how to design, implement, conduct, and assess the effectiveness of internal control. There are five components that make up an internal control. These are control environment, risk assessment, control activities, information and communication, and monitoring activities. (COSO 2013, 4-5.)

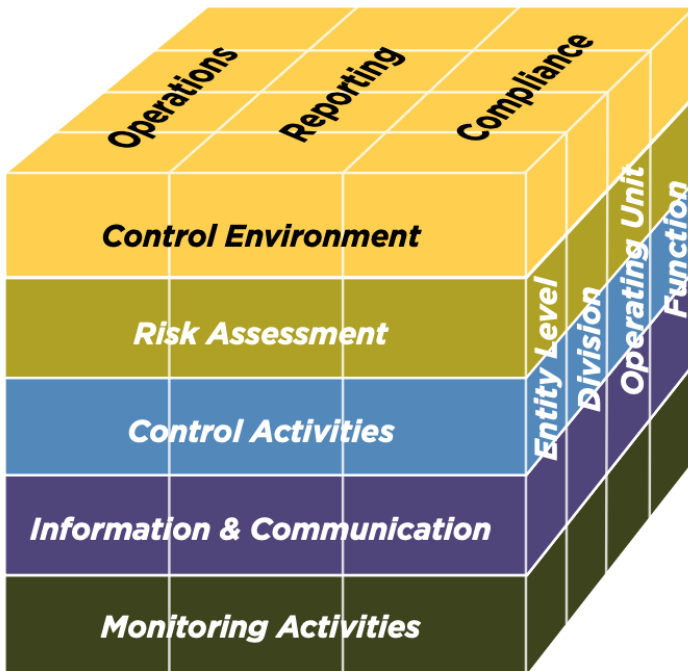


Figure 2. COSO Cube (COSO 2013, 5)

– The **control environment** sets the tone for the organization. It is a set of structures that provide the foundation and guidelines for implementing internal control within the organization. It encompasses integrity, ethical values, and the development and retention of competent management and employees. A positive control environment encourages ethical behavior and accountability, which contributes to a strong control foundation. (COSO 2013, 4.)

Some positive control environment characteristics that are significant for fraud control are companies having code of conduct and ethics policies that emphasize honesty and accountability, a reliable whistleblower system, where employees have no fear of reporting violations of the code of conduct, a board of directors, audit committee, and finance committee that are self-governing from the management and focuses only to their roles, clear segregation of duties and launch of organizational structure, and regular training of employees working in the accounting and financial departments to ensure their competence. (Wells & Zack 2012, 204.)

– **Control activities** are the specific policies and procedures established to perform the functions and achieve the organization's objectives. These procedures ensure that business processes are conducted in a manner that supports the organization's goals and alleviates the potential risks of fraud. Some factors involved in control activities are segregation of duties within financial reporting processes, controls used to make sure that certain individuals in the management cannot override established controls, procedures for adopting new accounting standards, and implementing measures to thoroughly review significant new transactions, such as business acquisitions and joint ventures, to ensure proper application of relevant accounting standards. (Wells & Zack 2012, 205.)

– **Risk assessment** comprises a sequence of procedures aimed at evaluating potential risks that could prevent the attainment of an organization's objectives. Processes involved in risk assessment are properly delegating duties for recognizing and evaluating the risks related to financial reporting, and the application of estimation techniques, including fair value measurement. Additionally, the assessment involves the scrutiny of external factors that may impact the reporting of financial statements, such as fluctuations in stock prices and the emergence of new competitors in the market, changes in directives, regulations, and accounting standards, as well as the introduction of new employees, including new subcontractors or IT systems that may have a relative effect on reporting systems under accounting and finance. (Wells & Zack 2012, 204.)

– **Information and communication** are essential in obtaining relevant information to support decision-making and enable the performance of internal controls. Internal communication allows the organization to convey the message from the management clearly to the personnel about their control responsibilities. Meanwhile, external communication delivers information to external stakeholders when addressing their demands and anticipations. (COSO 2013, 5.) Some components of information and communication are properly maintaining the supporting documentation for all transactions and journal entries, providing accurate and timely information to relevant parties involved in the decision-making regarding accounting estimates, and establishing effective channels of communication, such as hotlines, to encourage individuals (whistleblowers) who want to report suspicions or allegations of fraud, and providing clear instructions to personnel about their roles and responsibilities in maintaining internal controls. (Wells & Zack 2012, 206.)

– Finally, **monitoring activities** involve ongoing assessments of the quality of internal controls to ensure that they continue to operate effectively over time. Regular evaluations of present controls implemented help identify their weaknesses or deficiencies to be able to conduct appropriate corrective actions. These monitoring activities include **internal audits**, regular comparisons of financial results with the budget, benchmarking of the entity's performance against its competitors,

consistent and effective communication with external auditors, and many more procedures. (Moeller 2016, 54-56.)

Integrating these five components of an internal control system according to COSO, enables organizations to establish a strong system of internal controls that safeguard their assets, enhance the reliability and accuracy of their financial reporting and overall business operations, and promote integrity.

2.4.3 Artificial Intelligence and Data Analytics

The use of artificial intelligence and data analytics in various professional domains has significantly advanced in recent years following the continuous development of technology around the world. In this era of digitization, financial institutions, and departments are generating large volumes of data through digitalized financial transactions. Consequently, numerous financial operations are embracing AI in their workflows, spanning areas such as financial planning, budgeting, accounting, payroll management, cash flow oversight, and many more. As the finance operations become increasingly advanced, so do the fraudulent activities. These techniques have grown progressively sophisticated, creating intricate and hard-to-detect fraud schemes. Therefore, utilizing data analytics and AI to detect and prevent fraud is essential because of their ability to process large volumes of data in real time and adapt to evolving fraud schemes.

According to the study of ACFE in 2014, the utilization of data monitoring/analysis has been proven to be one of the most effective tools to control fraud. Organizations that incorporate data monitoring and analysis into their fraud risk assessment procedures have experienced substantial improvements, including a remarkable 59.7% reduction in median losses and a 50% reduction in the median duration of fraud schemes. (ACFE 2014, 38.)

Artificial intelligence refers to machines that are programmed to think and learn like humans to perform tasks that would normally require human intelligence. Machine learning is a subcategory of AI that develops algorithms and statistical models. This helps the AI learn from past data to make predictions or decisions. Another component of AI is Robotics Process Automation or RPA. It is a technology that uses software robots that mimic a human to perform tasks that are usually repetitive and rule-based. RPAs can copy a human as they interact with digital systems and system applications. Data analytics is also one of the techniques under AI, which focuses mainly on data. Data analysis is used to inspect, clean, transform, and interpret data to discover meaningful patterns and trends. When large and complex data have been collected, data mining is then used to help extract valuable insights from them through computational techniques and algorithms. (Sekar 2022.)

The three main applications of data analytics to control fraud are rules-based analytics, supervised learning, and unsupervised learning. With rules-based analytics certain indicators of fraud based on human knowledge are translated into rules that are applied to datasets. When these rules identify a potential fraud indicator within the data, it results in either flagging the transaction or initiating a predefined response. Examples of rules-based analysis are descriptive analysis, which uses basic statistical calculations like median and standard deviation to gain insights into datasets and their underlying distribution, and data matching, which compares two or more data to detect inconsistencies, for example, identifying a payment linked to an invoice not present in the master invoice table. (Commonwealth Fraud Prevention Centre 2022)

Supervised learning is used to forecast outcomes by examining the associations between initial inputs and final results. In the context of fraud detection, historical data is used to teach the algorithm to recognize patterns associated with fraud and non-fraudulent transactions. In contrast, unsupervised learning is a learning approach where the algorithm identifies patterns and anomalies in the data solely based on initial values. In detecting fraud, this means that the algorithm can identify anomalies in data without the need for labeled examples of fraud or non-fraudulent transactions. This makes it particularly useful for detecting unusual or previously unseen types of fraud. (Commonwealth Fraud Prevention Centre 2022)

In essence, data analytics and AI have revolutionized the field of financial statement fraud detection and prevention. These technologies offer a proactive, efficient, and accurate approach to identifying fraudulent activities. Nevertheless, harnessing the full potential of these tools demands a profound understanding of their functions. On top of that, new advanced and more complex schemes have been emerging with some of them even taking advantage of AI. Therefore, it is important to continuously monitor and update data analytics and AI tools to stay up to date with evolving fraudulent tactics, hence, optimizing the precision and effectiveness of fraud detection mechanisms.

2.4.4 Other Methods

Apart from the measures mentioned under internal controls, there are several other strategies to eliminate the risks of financial statement fraud. In subchapter 2.4.2, **auditing** has been mentioned multiple times, which indicates the importance of such practice in ensuring the reliability of a company's financial information. PricewaterhouseCoopers (PwC Middle East 2023) defines an audit as an independent examination of a firm's financial records, statements, operations, and transactions, to ensure their reliability, accuracy, and compliance with substantial laws, regulations, and accounting standards.

For **external auditing**, companies produce their financial statements and align them with a set of generally accepted accounting principles (GAAP), which is the IFRS in Finland and other EU member states. The assessment of the fairness of those financial statements is conducted by independent auditors following a framework of generally accepted auditing standards. These standards establish the necessary requirements and guidelines on how to perform an audit. (IFAC 2022)

Statutory audits are required to be undertaken by PIEs or “public interest entities”. These typically include publicly listed companies, credit institutions, and insurance undertakings. If an enterprise qualifies as a PIE, they are legally required to undergo statutory audits to review their financial records. (Directive 2014/56/EU 2014)

Auditing plays an important role in detecting fraud alongside other strategies. According to a survey led by the Association of Certified Fraud Examiners (ACFE 2022, 34) the most prevalent anti-fraud controls adopted by organizations around the world are external audits of financial statements and internal audit departments. The effectiveness of these controls was also analyzed, and it was concluded that surprise audits are linked to about a 50% reduction in both median loss and the median duration of fraud occurrences. This means that by having these controls in place, organizations experience lower fraud losses and quicker fraud detection. (ACFE 2022, 35-36.)

Other methods that are widely utilized by companies are related to the personnel involved in a company, which are whistleblowing hotlines segregation of duties, and training of employees about fraud awareness. In the survey published by ACFE (2022, 26), it is mentioned that 42% of frauds amongst organizations globally were detected by tips, and more than half of them were reported by employees. It is also revealed that the methods used by whistleblowers are evolving, from telephone hotline to email and other mechanisms. According to the Economic Crime Survey conducted by PricewaterhouseCoopers (PwC 2007, 16), roughly 71,4% of all types of fraud were committed by internal perpetrators, which highlights the importance of employment screening and employee training regarding fraud awareness.

Several effective methods have been mentioned in this chapter based on literature sources including, compliance with applicable laws, regulations, and accounting standards, having strong internal controls, regular audits, whistleblowing hotlines, employee training and awareness, and other methods like data analytics and other ratio analyses, organizations. Integrating these practices into a firm’s operations creates a more robust approach to eliminating fraud.

3 Research Methods

This chapter introduces the research approach, encompassing a detailed exploration of the research methodology and design. The selected research methods are initially explained, along with an overview of their application to address the investigative questions. The chapter further provides details of the data collection tools and the assessment of the data collected.

3.1 Research Design

The research type of the thesis project predominantly consists of desktop and empirical research. The process begins with researching the background theories and earlier studies related to the topic. Collecting and analyzing existing theories, data and concepts will help formulate the framework of empirical research, which will be the next stage of the process.

The research process used qualitative research techniques. Qualitative research means that the data collected are primarily qualitative in characteristic which involves collecting and analyzing nonnumerical data. This can be achieved through surveys, interviews, and visual materials including photographs, video recordings, and so on. (Beretvas, Leavy, & Saldana 2011, 3.) In this thesis project, the main focus will be mostly on the surveys and interview transcripts. The tools used for the data collection are an audio recorder, paper, and pen, the Webporol survey tool, and a laptop computer.

The research design follows a multi-phase approach, entailing the collection of two sets of data. The initial phase revolves around conducting surveys distributed to professionals employed in large-sized companies. This includes individuals from one of the Big 4 audit firms, as they possess pertinent knowledge regarding financial statement fraud. The process of reaching out to these professionals was facilitated through various social media platforms and networking channels.

The answers from the survey are then analyzed and used as a basis to formulate the interview structure, which is the next stage, giving more in-depth details to the research. The relevant data collected from the interviews are analyzed further and based on the results from both the surveys and the interviews, summary and conclusions are made.

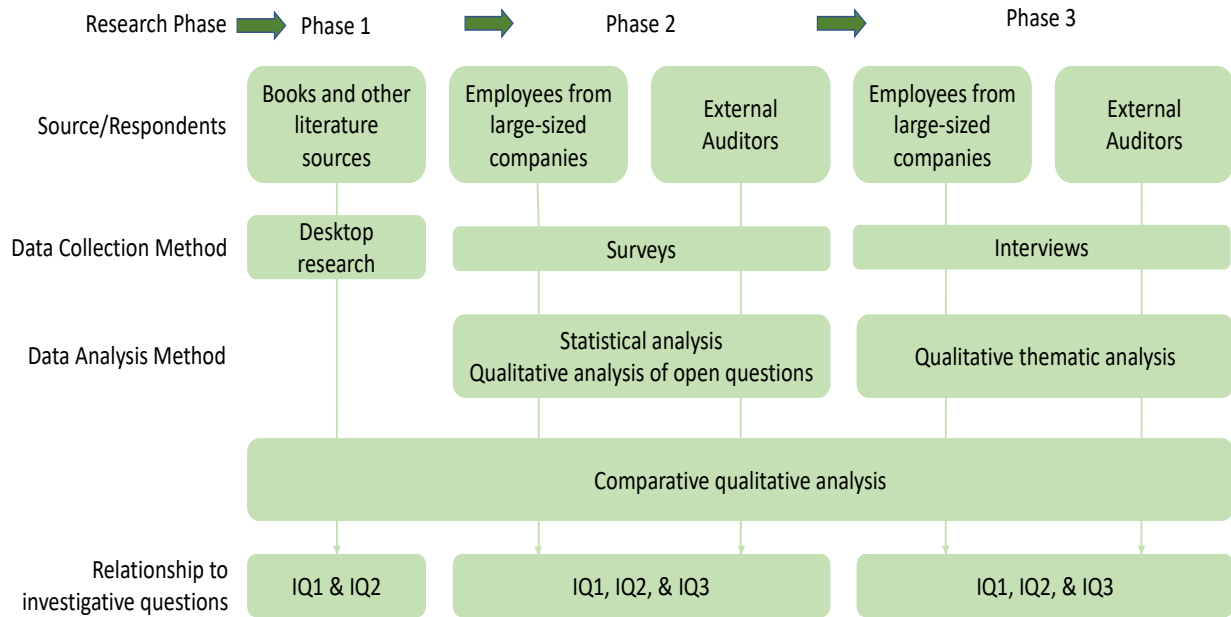


Figure 3. Research Design

3.2 Data Collection

The data were collected through desktop research, a series of surveys, and interviews. The sources concluded in the desktop research include books, academic papers, articles, and journals, which have been primarily gathered in the library of Haaga-Helia University of Applied Sciences. The information gathered from the desktop research served as the foundation for the structure of the surveys and interviews. In addition to that, the knowledge gained from the desktop research helped with understanding the main topic itself more thoroughly and, therefore can be used as a comparison to the data collected from the surveys and interviews (comparing theory to the practical aspect of the topic) and form a base for the arguments and conclusions.

3.2.1 Surveys

The surveys were bifurcated into two distinct groups: one aimed at external auditors employed by one of the Big 4 auditing firms, and the other targeting professionals working in large-sized companies based in Finland. This division was purposeful, as it yielded diverse perspectives on the concept of fraud. The results from the surveys taken by regular professionals also reveal the level of awareness of employees working in large-sized companies in Finland on the topic. This indicates how well these companies invest in training and educating their employees about fraud and its consequences.

The population of the professionals represents managers and employees, with the majority working in the finance industry. The external auditors are working from one of the Big 4 audit companies. The sample selection took place by contacting the external auditors directly via email or Teams. The author's profession as an auditor helped the process of reaching the right people much easier.

The other professionals were contacted mostly via LinkedIn, in which the selection was done based on their positions and fields of work (professionals working in large-sized companies). The surveys were published on the 8th of July and were sent via Webporol. During the two months, the surveys were able to collect 15 answers from external auditors and 16 answers from other professionals. The majority of the respondents were auditors, managers, and other employees, including accountants, controllers, salespersons, etc.

3.2.2 Interviews

The structure of the interviews was designed through an interview framework and with the help of the results from the conducted surveys. Each question is formulated from the research question and investigative questions by categorizing them according to each IQs. The interviews were officially conducted between the months of September and October.

The qualitative interviews were semi-structured. Semi-structured interviews are usually scheduled in advance, at a specified time and location. They are typically organized around a predetermined set of open-ended questions, with additional questions arising from the ongoing dialogue between the interviewer and the interviewee or interviewees. Normally, these interviews occur only once, and the interviewees are either individual or group. The interview may span a duration of 30 minutes to several hours for completion. (Crabtree & DiCicco-Bloom 2006, 315.)

The interviewees were selected based on their expertise and knowledge, which would give valuable insights into the topic. The first two participants were external auditors (Associate and Senior Associate) from PricewaterhouseCoopers Oy, and they were contacted directly via Teams. The last interviewee was a fraud specialist in a large company in Finland. Their position and the industry they work in highlight the expertise they have in this topic. They were contacted via direct message on LinkedIn, to which they responded immediately.

Two different interview frameworks were used, in which the questions were formulated and aligned based on their profession. The interviews with the auditors took place in their company's office in Helsinki. The last interview with the fraud specialist, on the other hand, was conducted online via Teams. The duration of the interviews varied from 15 to 30 minutes, in which they were recorded. To ensure the privacy and confidentiality of participants, the team sought their consent, and the

recordings were exclusively used for the transcription of participants' responses. This approach safeguarded the integrity of the valuable information contributed by the partakers to the research project.

3.3 Data Analysis

The data collected from the surveys were analyzed using statistical analysis and specifically descriptive statistics. This includes gathering, organizing, summarizing, and presenting the data. The main purpose is to summarize data in an organized manner by describing the relationship between variables in a sample or population. (Yellapu 2018, 60) In the context of a survey, descriptive statistics play a crucial role in creating concise summaries. These summaries are used to understand the distribution of responses and detect any data points that significantly deviate from the norm. The survey tool Webporol automatically created the graphs for the results of the surveys, in which the measure used is a mode. It is a value that appears with the highest frequency, meaning it occurs more often than any other value. The measure helped represent the response options that respondents selected most often for a particular question.

The interviews were analyzed through thematic analysis. According to Braun, Clarke, and Weate (2012, 191), thematic analysis serves as a systematic approach to recognize, structure, and provide an understanding of meaningful patterns within a dataset. In the context of the interviews, the dataset is the transcripts from the recordings. By analyzing the meaning across the dataset, the researcher can identify the mutual themes, patterns, and topics that come up repeatedly from the interviews, and interpret those commonalities.

Qualitative data analysis can also be done through categorizing. This involves collecting relevant parts of the data, analyzing them by conducting comparisons with the other data, and assigning names and classifications to the data elements. This process serves to establish a structured framework within the data, which is an essential step toward gaining a thorough understanding of the subject matter. (Flick 2018, chapter 10) For the interviews, the data results were compared between the answers of each interviewee. For example, the similarities and differences in the responses are linked to analyze any consistency or contradiction and to find which responses are the most common.

To do the comparison, the recorded audio of the interviews was transcribed into text. The text was reduced to remove unnecessary information including the greetings and introductions from the interviewer. The data was then examined by analyzing the keywords, phrases, and sentences that appeared in the data for each interview and comparing them. The data and results from the

surveys and interviews are categorized according to each IQs related to them. The results are then analyzed, compared, and used for the interpretation of findings and conclusions.

4 Data and Results

This chapter presents the results from the data collected through surveys and interviews. First, the results from the surveys are demonstrated. The results are divided into four sections: The first section determines the background of the respondents including their roles, responsibilities, and involvement in the decision-making in their respective companies. The last three sections represent the IQs of the research, to which the results from the surveys were categorized.

Furthermore, the results from the interviews are also divided according to which IQs they belong. The first section demonstrates the backgrounds of the interviewees as well as their awareness of the concept of fraudulent financial reporting. The other sections comprised the answers for each IQs from the perspective of experts, which are the auditors, and a regular employee in a large-sized company.

4.1 Surveys

The first part of the survey contained questions related to the background information of the respondents, including their involvement in the decision-making within their company. Most of the respondents were working in the finance industry. This included accountants, controllers, and auditors. Others were working in the sales and marketing departments, production, and other operations. 75% of them have 0-3 years of work experience. In terms of the level of awareness when it comes to their roles, and the frequency of them having the sole responsibility in the decision-making processes, 64% are quite aware of their responsibilities and 55% must make decisions by themselves occasionally. These answers give an idea of the level of knowledge and involvement of the respondents in contributing to the decision-making within the companies they work in.

The external auditors had varied responses to the questions regarding their background, roles, and responsibilities. 66% of them have 0-3 years of work experience in auditing and more than half of them are aware of their roles and responsibilities. When it came to their involvement in decision-making processes, the respondents provided a broad spectrum of answers. The frequency of "Rarely," "Sometimes," and "Often" responses were quite evenly distributed. This suggests that the decision-making procedures within auditing firms involve multiple individuals and are often arrived at through consensus. Such collaborative decision-making practices contribute to enhanced accuracy and reliability in decision outcomes.

4.1.1 Most Common Types of Financial Statement Fraud and Factors Attributed to Their Occurrence

When questioned about their familiarity with fraudulent reporting, respondents exhibited varying levels of awareness, which was expected given their diverse roles within companies and differences in their field of work. When asked about the types of financial statement fraud that most commonly occur in large-sized firms in Finland, two types appeared the most, which are manipulation of revenue recognition and misclassification of expenses. This corroborates with the theory mentioned earlier in chapter 2.2.3, in which these two types are under improper revenue recognition and asset misrepresentation schemes.

Financial pressure and opportunity emerge as the predominant factors frequently associated with the occurrence of fraud. One employee from a sales department revealed that most overestimations of expenses are linked to wasted items, which are usually stolen or broken items. This tells that fraud occurs even in the smallest areas of a business that is almost undetectable.

Additional contributing factors encompass weak internal controls, insufficient oversight from boards of directors, and hierarchical structures. These elements are closely interlinked with the concept of creative accounting discussed in Chapter 2.2.2. Here, the flexibility given to individuals in their financial reporting allows them to commit fraud (Nişulescu & Popescu 2014, 63).

4.1.2 Controls and Measures in Place to Detect and Mitigate Fraud

Some of the controls and measures presently employed by large-sized enterprises in Finland based on the respondents are regular internal audits and compliance with standards and regulations. These answers are expected since Finland has strict laws and regulations regarding financial statement reports. Moreover, large-sized companies typically implement internal audits in their business for the aim of uncovering inefficiencies in their operations, which would be difficult to detect in large businesses.

Are there any internal controls or procedures in place within your organization that aim to prevent fraudulent financial reporting? (Select all that apply)

Vastaajien määrä: 15 , valittujen vastausten lukumäärä: 44

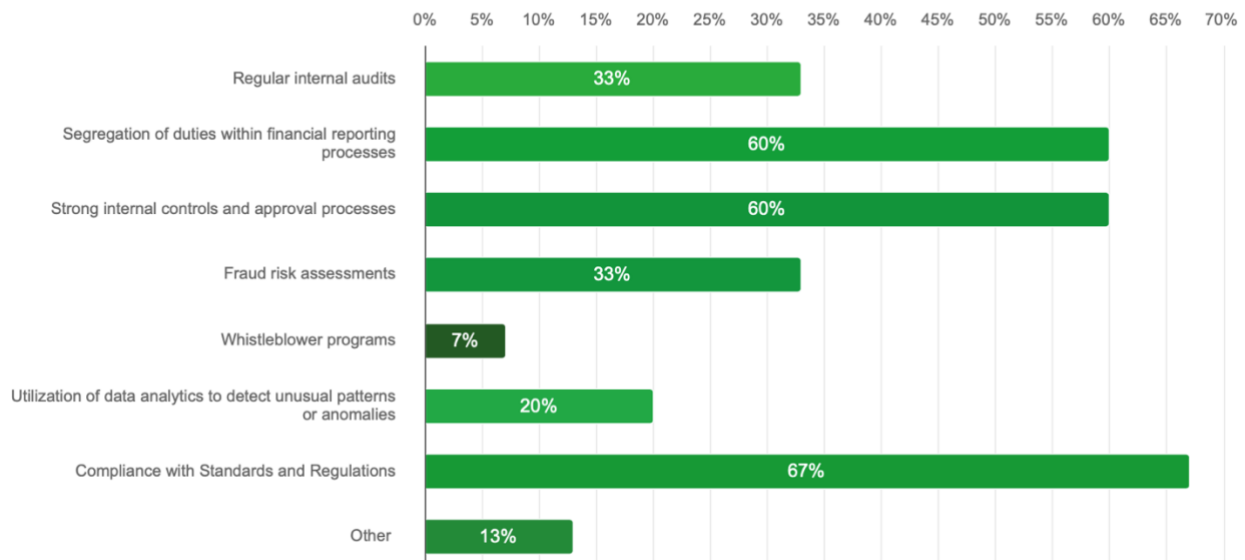


Figure 4. Common controls and other measures employed by companies to tackle fraudulent reporting

Other controls mentioned were the segregation of duties within financial reporting, strong internal controls and approval processes, and fraud risk assessments. On the contrary, it was surprising how whistle-blower programs and utilization of data analytics, were hardly mentioned. The external audit has been mentioned only a few times, which is quite understandable since it is mostly handled at the management level. Employees working in other operations of companies typically aren't aware of external audits.

When asked about their efficiency and which measures are the most effective in alleviating the risks of financial statement fraud, the responses were almost unanimous. 73% answered that these controls are somewhat efficient, with segregation of duties, strong internal controls, and external audits being the most effective ones. The majority also agreed that there is effective communication between different departments and teams regarding financial reporting and fraud within their companies.

For the external auditors, they have been asked what procedures they typically employ to detect financial statement fraud during audits. All of them answered performing substantive testing in high-risk areas of businesses. According to ISA 330 (International Standard on Auditing 330 paragraphs 6–24), the substantive procedure is a method used in auditing to identify significant

errors or inaccuracies within specific aspects of financial reporting. It includes tests of details and substantive analytical procedures, which are typically carried out in combination with tests of controls to assess the effectiveness of the company's internal controls. These analytical procedures and testing of controls mentioned in ISA 330 were also some of the most answered procedures that external auditors conduct in their audits. Other processes stated were external confirmation with third parties, evaluating management's fraud risk assessment process, risk assessment, and interviewing personnel.

As an external auditor, what procedures do you typically employ to detect financial statement fraud during audits? Please select the options that apply.

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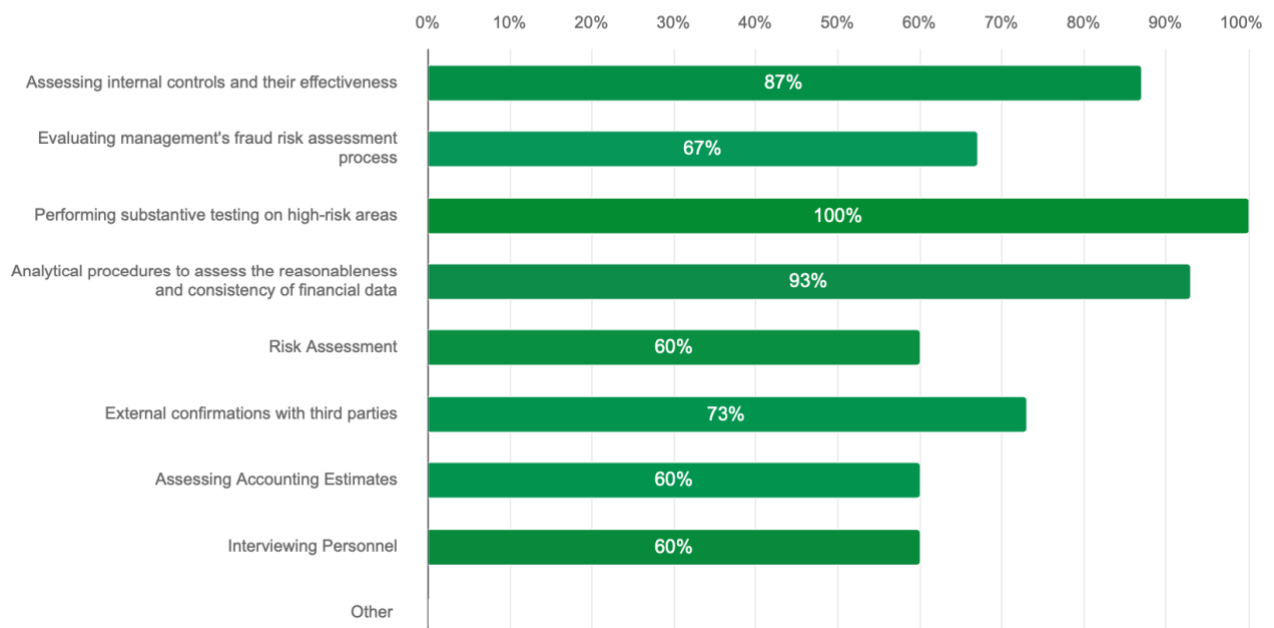


Figure 5. Overview of the typical procedures during audits according to external auditors

The auditors agree that these procedures are moderately effective in detecting fraud. They also shared opinions on which processes are the most efficient. Auditors emphasize that controls are crucial for detecting and preventing fraud, as deviations from normal business activities are often indicative of issues. However, they acknowledge that not all deviations necessarily indicate fraud. Auditors also stress the importance of understanding the client's business, including the board of directors, compensation systems, unusual journal postings, access rights, IT systems, and control reliance.

Evaluating management's fraud risk assessments or risk assessments in general are also mentioned. Based on the answers, we can see that the company as a whole and all its operations

are being audited, with the management and their internal controls as one of the main areas being evaluated during audit work. Other techniques regarded as very efficient were substantive procedures and reconciliations. Auditors recognize that a combination of these procedures is necessary to effectively detect and prevent financial statement fraud during audits.

4.1.3 Challenges in the Current Detection and Prevention Strategies Used by Organizations

Respondents reveal that there have been gaps and challenges in the existing controls that their firms employ, which rely heavily on the employees themselves. According to the respondents, the lack of awareness among employees about fraud presents a risk of incapability to detect potential fraud within the company. This indicates that although most of the respondents answered that they are somewhat familiar with the concept of fraud and that they are encouraged to report suspicious financial activities to some extent, it is not enough, and firms should invest more in educating and training their employees about the matter.

Another challenge that respondents mentioned is the lack or inefficiency of whistleblower programs, which is alarming. As mentioned in Chapter 2.4.2, whistleblowing hotlines help encourage individuals to report to management if they have any suspicions or allegations of fraud (Wells & Zack 2012, 204). Without them, it is extremely difficult for individuals from all positions and operations of a business to voice out their concerns and are likely to not report potential fraud detected. Other gaps in the current measures stated by the respondents are ineffective communication within the management and throughout the business, manual processes, and lack of automation in finance-related practices.

The external auditors on the other hand responded to the challenges and limitations of auditing in detecting financial statement fraud. Three of them mentioned the difficulty of obtaining the right evidence from clients and other sources to arrive at a conclusion. Some clients even take so much time to provide all the necessary information for the audit work, which delays the work and adds pressure on both sides. One auditor revealed that there have been cases where clients with highly automated controls were proven insufficient, which makes it difficult to rely on the information shared by the client. Hence, they had to perform extensive manual testing, which was very time-consuming.

4.1.4 Suggestions on Effective Approaches to Address the Gaps in Preventing Fraudulent Reporting

Recommendations on providing training among employees were mentioned heavily as one of the solutions to limitations in current fraud prevention procedures. Enforcing robust anti-fraud policies

and implementing mechanisms in monitoring transactions and other activities with high risk of fraud were also mentioned. These are targeted toward management, which tells how alleviating the risks of fraud in a company usually starts with the management. If the management invests properly in anti-fraud controls and measures, this will be reflected to the employees, which in return lessens the risk of a company encountering fraud.

How should your organization address the identified gaps or challenges? Please select the options that apply:

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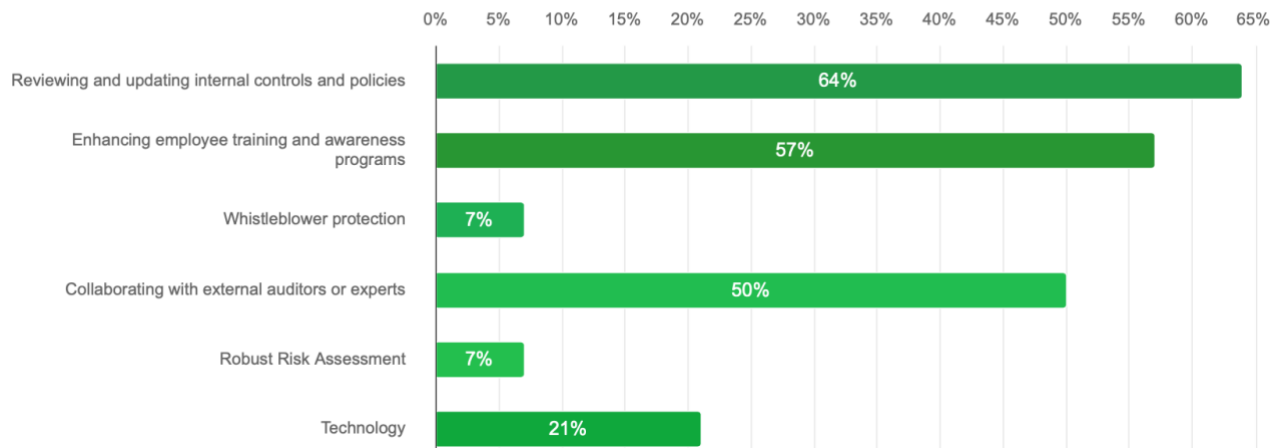


Figure 6. Suggestions on procedures and tools that can be utilized to address the gaps in the current fraud prevention strategies

The auditors have similar answers to professional workers but also revealed the significance of technology and automation in providing more accurate financial reporting. According to them, data analytics is also an effective way to scan client's data and detect if there are any suspicious activities. In addition to that, the auditors have mentioned that more frequent reviewing of journal entries, transactions, and other financial activities could reduce the risk of financial statement fraud.

4.2 Interviews

Table 2. Overview of the interviews

	Internal controls	External audit	Technology, AI and data analytics
Interviewee 1 (Associate - external auditor)	<ul style="list-style-type: none"> • Segregation of duties, approval processes, documentation, internal audit, and reconciliation 	<ul style="list-style-type: none"> • Following the International Auditing Standards regarding the methodology of the audit • Phases of audit: planning, execution, completion • The audit process goes through various people from associates to managers, and director signing the audit report 	<ul style="list-style-type: none"> • Application of data analytics in audit processes • Digital footprint
Interviewee 2 (Senior Associate – external auditor)	<ul style="list-style-type: none"> • Segregation of duties and proper control in terms of authorization and access to certain things. 	<ul style="list-style-type: none"> • Following the International Auditing Standards regarding the methodology of the audit • Phases of audit: planning, execution, completion 	<ul style="list-style-type: none"> • Application of data analytics in audit processes • Integrating technology and automation into companies' operations and controls.
Interviewee 3 (fraud analyst)	<ul style="list-style-type: none"> • Different softwares and measures to block potential fraud. • Complex approval process, internal auditing and proper documentation • Training employees (varies a lot in many companies, inconsistent) 	<ul style="list-style-type: none"> • Planning phase - Discussion with the client about their overall business operations, how their internal controls run and so on. • Assessing the controls • Following the audit requirements from ISA 230 and 240 	<ul style="list-style-type: none"> • Implementing technology can be costly • Utilizing third-party service providers to apply anti-fraud procedures in an organization

The thematic interviews engaged three participants in discussions. Initially, the participants shared insights into their backgrounds and their familiarity with the subject matter. Two of them have had long experience in the field of finance and the last one has been in the field for about three years. Their professional backgrounds, comprising two external auditors and one fraud specialist, indicate the knowledge and the level of expertise they have about the topic of fraud.

The themes extracted from these interviews have been thoroughly categorized into three distinct chapters. These categories encompass internal controls and risk management, external audits,

and technology. These themes appeared the most from the thematic analysis conducted. As indicated by the participants, these strategic measures could help large-sized companies avert potential fraud threats and enhance the accuracy of their financial reporting. The following chapters discuss these themes in more detail.

4.2.1 Internal Controls and Risk Management

The role of internal controls in mitigating the risks of fraud was heavily pointed out in the discussions. This correlates with the theory from Chapter 2.4.2 as well as the surveys. This proves the significance of having robust internal controls as a first step in fighting financial statement fraud. Internal controls are a series of policies, procedures, and practices employed by an organization to ensure the accuracy and reliability of its financial information, safeguard its assets, and promote compliance with applicable laws, regulations, and accounting standards. (Harrison et al. 2014, 275.)

The interviewees mentioned some of the procedures that are most used by large-sized companies in Finland and are the most effective. These methods are segregation of duties, approval processes, documentation, internal audit, and reconciliation. Assigning different individuals to certain financial-related tasks, for example, one person is handling the ordering of goods, while another is responsible for making the payments, can easily lessen the risk of potential fraud. Also, limiting and controlling the authorization and approval processes in certain transactions ensures their legitimacy before they are executed. Thorough documentation of financial transactions and activities as well as reconciliation of financial accounts and records help identify any suspicions of fraud.

While the theory tells us that implementing all these procedures is very significant, in practice, applying such a framework is not easy and needs proper planning and assessment. According to the interviewees, one challenge that could arise in the internal controls of companies is the incomplete implementation of the procedures. Interviewee 2 mentioned that there have been instances when some controls aren't conducted or are not being focused on.

Interview 3, which is the fraud analyst also mentions the lack of training and awareness, as well as the lack of overall interest of companies in investing in preventive procedures, are some of the main challenges that firms face in preventing fraud. Based on their experience within the finance field, the level of awareness and employment of training on fraud prevention practices vary within the large-sized enterprises in Finland. The main reason for this is the perception of companies that the likelihood of fraud occurring in Finland is very little since there have been only rare fraudulent

reporting cases that happened in the country throughout history. However, it doesn't mean that it can never happen.

Interviewee 3 even mentioned one case of fraud that happened in Finland at a psychiatric center that had a data leak and people were threatened. That is just the basic part of not having proper security measures for the technology that companies have. This is the reason why Interviewee 3's profession as a fraud analyst exists because they help convince firms to invest more in implementing procedures to prevent potential fraud, and to change their idea of it as a cost and more as a benefit to companies.

Another highly effective approach, as highlighted by Interviewee 3, involves the implementation of robust risk management practices, particularly those encompassing fraud risk assessment. This procedure aids in the identification, assessment, and thorough analysis of potential risks or vulnerabilities within an organization's systems, processes, and controls. Which could potentially be exploited by malicious individuals seeking to engage in fraudulent activities.

4.2.2 External Audit

The importance of statutory audits and external audits in detecting and preventing fraud has been emphasized by the participants. Interviewees 1 and 2, who are external auditors, have highlighted the presence of well-defined and effective procedures outlined by the International Auditing Standards (ISA) that auditors adhere to during their audit processes. The audit procedures start with the planning phase. In this initial phase, auditors discuss with the client about its business, internal controls, and risks. This helps auditors determine the scope of the audit and the procedures that should be established during the audit. In the second phase, auditors assess the risks associated with the company's financial statements and evaluate its internal controls in place. The rest of the phases are the core of the audit. For example, as Interviewee 1 mentioned, testing all the manual accounting entries that have been made in the year.

As per insights from Interviewees 1 and 2, the audit process involves several individuals, ranging from associates to managers and directors, all of whom contribute to the signing of the audit report. This multi-tiered approach to audit work enhances its precision and reliability. Furthermore, auditors undergo continuous training sessions aimed at honing their auditing skills and expanding their knowledge base on pertinent subjects related to their field, including specific accounting standards, financial statement structures, and more. These training sessions frequently delve into the concept of fraud and emphasize the consequences of failing to detect it for the audit company, the auditor, and the client involved in the activities.

The interviewees also discussed the actions that they do when there's a situation where there is suspicion or indication of potential financial statement fraud during an audit. According to them, discussing with a more experienced member about the matter is the first step. Informing the client about it is not recommended as it is against the policy of independence and objectivity. If deemed necessary, they may engage in discussions with the management to address the issue.

The procedures and rules of auditing mentioned above by the Interviewees conclude the effectiveness of external auditing. Auditors bring their expertise, independence, and methodical audit processes to analyze the accuracy of the companies' financial statements, hence helping uncover potential fraudulent activities.

4.2.3 Technology and Data Analytics

The focus of discussions has predominantly revolved around the role of technology and AI in various business operations, particularly in the context of anti-fraud practices. From emphasizing their efficiency and how to utilize it in different business operations including anti-fraud practices, to their potential limitations and continuous need for development.

During the interviews with auditors (Interviewees 1 and 2), a prominent topic of conversation was the application of data analytics in their audit processes. Data analytics includes procedures of evaluating, cleaning, transforming, and analyzing large sets of data (Sedkaoui 2018, pp. 46-47). When data are collected, they are cleaned and converted with the help of data mining. Converted data can then be used to uncover valuable insights, recurring patterns, and trends. (Sekar 2022) The auditors emphasized the ongoing adoption of data analysis tools within auditing firms due to their capacity to enhance accuracy and efficiency.

The auditors have also indicated the importance of integrating technology and automation into companies' operations and controls. Interviewee 1, for instance, pointed out that in operations like accounting, where manual operations such as journal entries and data reconciliation are still done by many companies, the vulnerability to fraud increases. Automating some areas of accounting and other operations can reduce inaccuracies and especially the risks of fraud. Interviewee 1 also specified that through digital footprint, any entries or modifications done on any IT systems are recorded and will stay there forever, thus diminishing the potential of committing fraud.

Interviewee 3 on the other hand, although agrees about the advantages of employing technology in business operations and fraud prevention, mentioned how costly it can be for companies. On top of that, implementing data analytics tools or IT controls, for example, requires training, which is also a cost for a company. That's why Interview 3 specifies the benefit of outsourcing these practices, which is the idea of their profession. Interviewee 3 works for a company that offers services to

firms in Finland services for all the procedures related to fraud detection and prevention. By outsourcing the processes to them, companies won't have to buy their tools as the service provides all of that for them including training of their employees as well as enhancing the overall awareness of fraud.

In summary, adapting to advanced technology and data analytics enhances fraud detection and prevention providing speed, accuracy, and efficiency to business operations. This is in line with the previous study of ACFE (2014, 38) mentioned earlier, proving the effectiveness of integrating data analytics tools into an organization's fraud risk assessment procedures. Moreover, as the interviewees mentioned about the increasingly sophisticated financial fraud schemes, leveraging these technological advancements is crucial and can help companies identify potential fraud indicators and suspicious activities that may go unnoticed through traditional methods.

5 Conclusions

This chapter presents the key findings pertaining to the concept of fraudulent financial reporting and a summary of the most effective controls and measures to alleviate the risk of it occurring in large-sized companies in Finland. Building upon these findings, recommendations from the professionals and experts from the surveys and interviews conducted are drafted for future research. Finally, the reliability and validity of the results are evaluated, followed by the author's personal learning and development during the whole thesis process.

5.1 Key Findings and Recommendations

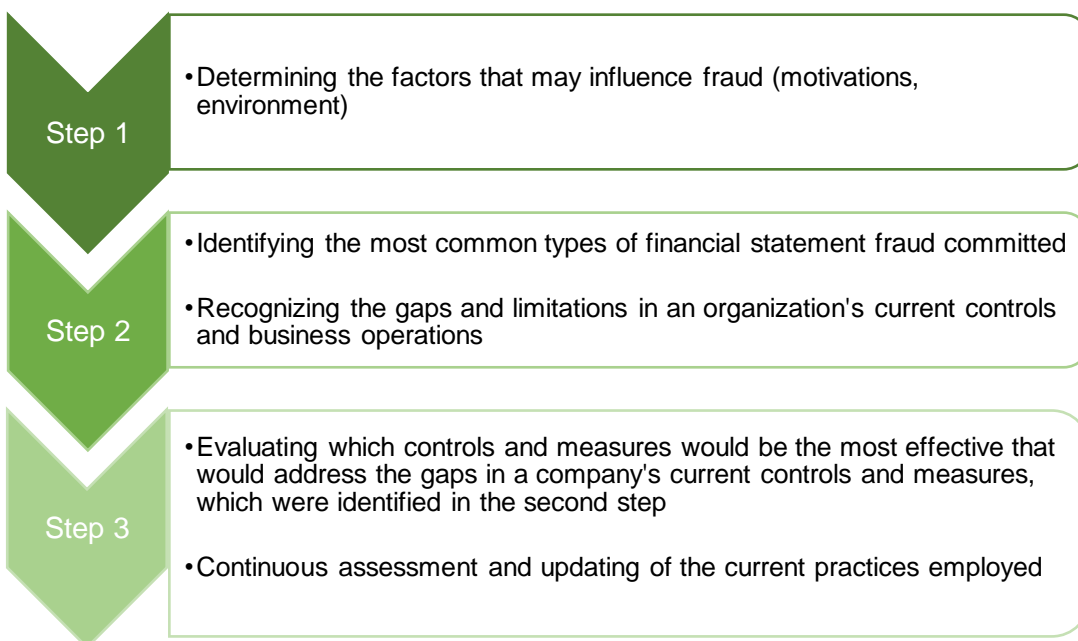


Figure 7. Steps on the approaches to carry out to detect and mitigate the risks of fraudulent financial reporting

The results of the research demonstrate the relevance of fraudulent reporting to organizations both in theory and in practice. Through previous studies and the surveys and interviews conducted in this research, it is revealed that understanding how financial statement fraud is perpetrated is the most important and the first step in mitigating its risk of occurring. This means gaining insight into the motivations driving financial statement fraud, enabling the early recognition of warning signs.

The second step is identifying the most common types of financial statement fraud that may occur according to a firm's business environment, as well as recognizing the gaps and limitations in the

current controls and business operations that may offer opportunities for fraudulent activities is crucial. Lastly, the third step is to implement various procedures that are most effective in detecting and preventing fraud, which were mentioned in this research. Moreover, continuous assessment and updating of the current controls and measures employed and implementing more advanced procedures, if possible, to stay ahead of evolving fraud risks are crucial.

The first step is a very essential element of fraud detection and prevention, and it is through a thorough understanding of the environment in which a perpetrator operates. This supports the theory of the fraud triangle and the factors that contribute to fraudulent behavior within organizations. These factors are pressure, opportunity, and rationalization (Abdullahi & Mansor 2015, 39–41). The respondents from the surveys and interviews agree that the fraud triangle theory exists in real-world situations. The concept is even utilized by external auditors according to Interviewee 2, to create certain audit procedures that follow the model to detect potential fraud in an organization.

The second phase is to recognize the most common types of financial statement fraud that could potentially arise in an organization depending on the nature of its business. According to the surveys, these could be revenue recognition manipulation, and expense misclassification for most companies. By identifying these schemes, a company could focus more on those areas when working on financial reports and creating fraud risk assessments.

Another part of the second phase is to recognize the possible gaps and limitations in the current controls and overall business operations that could give opportunities for fraud. The previous studies and the results from the surveys and interviews on this research provided the most common gaps and challenges in an organization's controls and management, which are the lack of awareness among employees regarding fraud risks, inefficient whistleblower programs, ineffective communication among employees and the managements, incomplete implementation of internal controls, and the costs of integrating technology.

After identifying and evaluating the risks of these challenges in the controls and management, companies can then implement the most appropriate and effective procedures to address them and prevent fraud. For example, as the respondents revealed in the surveys and interviews, one of the problems in an organization's management in Finland is the lack of awareness and training among the employees about the risks of fraud. Interviewee 3 suggests that this may be due to the overall lack of interest of firms in investing in this matter. The perception of fraud occurring in companies in Finland is very little because cases of fraud have been quite rare throughout the country's history.

To address this problem, companies should recognize that although the likelihood of fraud appearing is small, it is still necessary to invest in these practices, as the consequences of fraud occurring can be very costly for them. Companies could invest in ongoing training and education programs to ensure employees are equipped with the knowledge and skills to detect and prevent financial statement fraud. This includes ethical conduct, reporting mechanisms, and training about the overall concept of fraud and emerging fraud schemes.

Another major problem that can arise in a business is the improper employment of internal controls. This may be due to the lack of knowledge about the framework of internal controls. One of the most known models for designing and implementing internal controls is COSO's *Internal Control-Integrated Framework*. The framework encompasses five components that make up an internal control, which are control environment, risk assessment, control activities, information and communication, and monitoring activities. (Zack 2013, 153–156.) By following this framework, companies can design and employ effective internal controls for their businesses. These controls should include segregation of duties, approval processes, documentation, internal audit, and reconciliation, which are also mentioned by the participants in this research as some of the most effective practices under internal controls to eliminate fraud.

Risk management and regular fraud risk assessments are also essential procedures in mitigating the risks of fraud. By identifying potential vulnerabilities in an organization's financial reporting processes and assessing their likelihood and impact, a company can then develop controls and countermeasures for these identified risks. This creates a robust control environment that promotes ethical behavior and discourages fraudulent activities.

In addition to the measures mentioned above, companies can also benefit from utilizing external audits. The results from the surveys and the discussions with the external auditors reveal the procedures conducted in audit work, which are proven to be effective in detecting financial statement fraud. These procedures encompass a broad spectrum, spanning from the macro level, involving an evaluation of a client's entire business operations, down to the micro level, which entails careful testing of a company's transactions and records, supported by examinations of controls and substantive testing. The phases of an audit procedure and the expertise of the external auditors don't just help detect potential fraud but also provide a company with some recommendations to enhance the accuracy of its financial statements and improve its controls and systems in place.

The final step in the process is the continuous assessment, upgrading, and updating of the procedures mentioned earlier as well as finding more new practices to stay ahead of evolving fraud risks. For this, the professionals and experts who participated in this research heavily suggest the

use of technology and data analytics. Integrating data analytics on financial reporting, for example, enhances the accuracy of the financial statements, starting from the journal entries to period- and year-end reporting. Furthermore, embracing technology more extensively within an organization's controls and systems fosters an overall boost in operational efficiency.

Interviewee 3 also gave an insight into the possibility of outsourcing the processes related to tackling fraud risks. By leveraging the services of third-party providers, companies can access specialized tools, proper training programs, and well-established procedures tailored to the task. This approach represents an innovative and proactive strategy around fraud risk management.

In conclusion, following the steps mentioned above, which is the summary of opinions and suggestions from the professionals and experts in this study, could provide companies with some insights into effective methods of mitigating fraudulent reporting tendencies in their businesses. Seeking ways to prevent fraud reflects an organization's commitment to ethical and corporate sustainability goals. Such a commitment helps build and maintain stakeholder trust, comply with regulations, and protect the company's reputation and long-term viability, all of which are fundamental to achieving sustainability in today's business environment.

5.2 Reliability, Validity, and Relevance

Reliability and validity are measurements used to assess the quality and integrity of research methods and the data they produce. Reliability refers to consistency in the results produced when applied repeatedly. This indicates that there is no bias in the results and that the measurements and data are consistent and stable. Validity on the other hand is concerned with the accuracy of a measure. This means that validity evaluates whether a research instrument accurately measures what it's intended to measure. (Haradhan 2017, 10–14.)

The reliability and validity have been taken into account during the whole research process. The data, results, and analysis were based on previous studies, surveys, and introductions that were carried out. The previous studies were taken from legitimate sources, such as academic books, articles, research data, and statistical information.

The surveys were designed properly with the help of Webporol. The tool accurately measured the results of the data and precisely generated the analysis and report. The respondents of the surveys were professionals working in large-sized companies in Finland, as well as external auditors who are specialists in their field of work and specifically the concept of fraud.

The interviews were conducted online, in which each interview was recorded. Moreover, the author created an interview framework as a place to write down the answers given by the interviewees.

The framework also gave structure to the questions asked and categorized them according to each investigative question where they belong. The framework and the recordings helped the author interpret and analyze the answers of the participants accurately and transparently. The interviewees were all professionals and experts in the field of finance, especially in fraud.

The measurements used and the individuals who participated in the surveys and interviews indicate the reliability and validity of the data produced. The biggest concern, however, is the limited number of respondents from the surveys and the interviewees. The surveys had 31 respondents overall, whereas the interviews had three participants. Regardless of, the background of each participant and the diversity in the population in terms of their age, gender, positions, and field of work, the author was able to obtain relevant data to some extent. Although the results from the data collected can only reflect a limited view on fraudulent reporting from the whole population of large-sized companies in Finland to some extent, the answers from the participants were all clear and similar to each other, which makes the data reliable and valid.

The research provides a concise summary of the most effective controls and procedures and the steps to take to properly assess, detect, and prevent the tendencies of financial statement fraud occurring in large-sized companies. The summary came from previous studies, professionals, and experts in Finland. This makes the results relevant to the purpose of this thesis, which is intended for organizations operating in Finland.

Further studies on the topic could involve additional assessments of the methods mentioned in this research including internal controls, external audits, the use of third-party service providers, and integration of technology. For external auditing, the cooperation between companies and the external auditors that they appoint could be investigated. As mentioned in the previous chapters of this research, there have been cases of fraud in companies, where the external auditors failed to detect the act, or if they did, failed to report on it. For the use of third-party service providers and integration of technology into a firm's controls, their usefulness can be analyzed, as well as their possible limitations and disadvantages. Lastly, the topic of fraud could be emphasized more on the management and the board of directors, by researching the procedures that can be carried out for the top level of a firm to mitigate the risks of fraud.

The study also gives meaningful knowledge to fellow finance students and professionals working in the finance field. Learning about the ethical and sustainability aspects of financial reporting and the significance of accurate reporting is valuable for students and professionals in their careers. The concept of fraud isn't tackled as much in Finland, however creating awareness of its consequences and impacts on an organization, may prevent companies and individuals from committing fraud.

Over time, this increased awareness could contribute to enhancing the overall trustworthiness of the country's business landscape.

5.3 Reflections on Learning

This whole research process has been a valuable experience for me as a student, professional, and personally. This journey has not only deepened my understanding of the subject matter but has also equipped me with a range of essential research and analytical skills.

One of the key takeaways from this study is the recognition of the complex nature of fraudulent reporting. Initially, I approached this topic by sticking strictly to the research question and investigative questions that I've set for the structure of this study. Eventually, I realized having adequate and effective controls and measures isn't enough to tackle the risks of fraud. Finding out the most effective procedures won't be possible without going through other steps. This includes pinpointing the factors that contribute to fraudulent behavior within an organization, identifying the gaps and limitations in the current controls and measures applied in a company, and finding out the most typical types of financial statement fraud that could occur given the nature of the firm's business. After carrying out those steps, it would be easier to evaluate the proper anti-fraud practices best suited for the company.

Another significant realization during this research is the intricate interplay between theory and practice. While the theoretical framework provided a robust foundation for my study, surveys and real-world interviews with finance professionals exposed distinctions and practical considerations that theoretical frameworks alone cannot capture. The same goes the other way. The results from the surveys and interviews confirm the relevance of the previous studies because of the similarities in the answers from the respondents and theories.

Undoubtedly, the research journey was not without its challenges. I encountered obstacles in gathering enough data for the analysis since there wasn't enough population (participants) to obtain data from. I have sent out dozens of emails and messages asking people to answer my surveys, however, in the end, only 16 people were able to answer. The interviews on the contrary, although there were only three interviewees, each of them, however, are competent and highly knowledgeable in the area of the topic, providing relevant data to this study. Another major problem that I had was failing to find a commissioning company for this research. I had a few contact companies that showed interest in collaborating throughout the process, nevertheless, all of them backed down for the reason of not finding the time to assist me with this project. Despite that, I still think that my thesis would provide any large-sized companies valuable insights on the topic, that they can benefit from.

Overall, despite the challenges I had during the process, the results of this thesis were gratifying. The research has not only expanded my knowledge of fraudulent financial reporting, but has also equipped me with essential research skills, problem-solving abilities, and an improved sense of ethical responsibility. It has reaffirmed my belief in the importance of continuous pursuit of knowledge and spreading awareness about fraud in contributing to a more transparent and trustworthy financial environment.

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Appendices

Appendix 1. Interview questions for Interviewee 3 (fraud analyst)

IQ 1: What is fraudulent financial reporting and the factors influencing it?

1. From your profession as a fraud analyst, how familiar are you with the importance of accurate financial reporting and the concept of fraudulent financial reporting?

IQ 2: What measures and mechanisms are presently taken to detect financial statement fraud and how efficient are they?

1. From your professional experience, do you know what controls or procedures are currently employed by large-sized companies in Finland to detect and prevent financial statement fraud? Do you believe the current measures in place are sufficient?
2. Which one of these methods do you think is the most efficient and are there any areas where you think improvements could be made?
3. Have you ever come across any fraud cases in Finland?

IQ 3: What are the perceived gaps or challenges in the current prevention strategies and mechanisms and how to address them?

1. Are there any specific areas or processes within companies where you believe there might be vulnerabilities to potential financial statement fraud? (Are there any limitations and challenges in the current methods used by your organization in detecting financial statement fraud?)
2. Are there any suggestions or improvements you would like to propose to strengthen the overall approach to detecting and mitigating financial statement fraud in companies in Finland?
3. How do you believe technology and data analytics can contribute to enhancing fraud detection efforts within the company?
4. Have you observed any emerging trends or advancements in fraud detection methodologies in recent years? If so, how do these new approaches differ from traditional methods?

Appendix 2. Questionnaire for Interviewees 1 and 2 (external auditors)

IQ 1: What is fraudulent financial reporting and the factors influencing it?

1. Can you provide a brief explanation of fraudulent financial reporting and its potential impact on a business?

IQ 2: What measures and mechanisms are presently taken to detect financial statement fraud and how efficient are they?

1. As an external auditor, what procedures do you typically follow to detect financial statement fraud? (The five phases of audit)
2. How effective do you think these procedures of financial statement audit are?
3. What actions do you and your team take when there's a situation where there is suspicion or indication of potential fraud during an audit?
4. Could you share any notable examples or cases where your audit team successfully uncovered financial statement fraud using these methods if there have been any at all? What were the key factors that contributed to the detection?
5. Apart from the standard audit procedures, what additional measures or specialized techniques do you utilize specifically to address the risk of fraud? For example the use of data analytics tools and AI
6. From your experience as an external auditor, do you know the most common controls and strategies currently employed by companies that you audit to prevent financial statement fraud?

IQ 3: What are the perceived gaps or challenges in the current prevention strategies and mechanisms and how to address them?

1. In your opinion, what are the perceived gaps or shortcomings in the current prevention methods against fraud? How do companies typically respond to these gaps?
2. Have you observed any emerging trends or advancements in fraud detection methodologies in recent years? If so, how do these new approaches differ from traditional methods?

3. Are there any best practices or recommendations you would suggest for organizations to strengthen their fraud detection and prevention measures based on your experiences as an external auditor?

Attachments

Attachment 1: Questionnaire for professionals

Questionnaire

1. Please indicate your role within the company:

- Executive/Management
- Finance/Accounting
- Human resources
- Sales and marketing
- Production
- Operations
- Other (please specify)

2. How many years of work experience do you have on this field?

- 0 to 1 year
- 1-3 years
- 3-5 years
- 5-10 years
- 10+ years

3. From 1 to 5, how aware are you of your own role and responsibilities in the company? (1=not at all, 5=very well aware)

1	2	3	4	5
<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

4. How frequently are you solely responsible for making decisions within your role? (1=rarely, 3=sometimes, 5=regularly)

1	2	3	4	5
<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

5. How familiar are you with the concept of "fraudulent financial reporting" or "financial statement fraud"?

- Very familiar
 Somewhat familiar
 Not familiar at all

6. In your opinion, which types of fraudulent financial reporting are most common to occur in medium-sized companies? (Select all that apply)

- Manipulation of revenue recognition
 Misclassification of expenses
 Overstatement of assets
 Understatement of liabilities
 Other
-

7. Have there been any cases of financial statement fraud or any other types of fraud in your organization's history?

- Yes
 No
 Maybe

8. What impact or outcomes have resulted from the situation, and how has it been addressed or managed?

9. What were the primary factors or causes attributed to the occurrence of the fraud?

10. Are there any internal controls or procedures in place within your organization that aim to prevent fraudulent financial reporting? (Select all that apply)

- Regular internal audits
 - Segregation of duties within financial reporting processes
 - Strong internal controls and approval processes
 - Fraud risk assessments
 - Whistleblower programs
 - Utilization of data analytics to detect unusual patterns or anomalies
 - Compliance with Standards and Regulations
 - Other
-

11. From your perspective, how efficient and significant are the existing measures and mechanisms in detecting and preventing financial statement fraud within your organization?

- Very efficient and significant
- Somewhat efficient and significant
- Not efficient and significant

12. Which measure or mechanism in particular is the most effective for alleviating the risks of financial statement fraud in your opinion?

13. How often does your company conduct internal audits?

- Regularly
- Every other year
- Rarely
- Other
-
- I'm not aware

14. How often are the risk management and internal control system reviewed by the board?

- Quarterly
- Annually
- Irregularly
- Other
-
- I'm not aware

15. Do you believe that there is effective communication and collaboration between different departments and teams regarding financial reporting and fraud prevention within the company?

- Yes, definitely
- To some extent
- No, not at all

16. Are employees encouraged to report suspicious financial activities or concerns within the company?

- Yes, actively encouraged
- Yes, to some extent
- No, not encouraged

17. In your opinion, what are the gaps or challenges in the current prevention strategies and mechanisms used by your organization to address financial statement fraud? Please provide details.

**18. How should your organization address the identified gaps or challenges?
Please select the options that apply:**

- Reviewing and updating internal controls and policies
- Enhancing employee training and awareness programs
- Whistleblower protection
- Collaborating with external auditors or experts
- Robust Risk Assessment
- Technology

19. Have you received any training or education on recognizing and preventing financial statement fraud? If yes, how effective do you believe these initiatives have been?

20. What additional resources or support do you think would be beneficial for your company in identifying and reporting potential instances of financial statement fraud? Please provide details.

21. Any final comments?

Attachment 2. Questionnaire for external auditors

Questionnaire

1. Please indicate your role within the company

- Executive/Management
- Auditing/Finance/Accounting
- Other (please specify) _____

2. How many years of work experience do you have on this field?

- 0 to 1 year
- 1-3 years
- 3-5 years
- 5-10 years
- 10+ years

3. From 1 to 5, how aware are you of your own role and responsibilities in the company? (1=not at all, 5=very well aware)

- | | | | | | |
|-------|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| | 1 | 2 | 3 | 4 | 5 |
| _____ | <input type="radio"/> | <input type="radio"/> | <input type="radio"/> | <input type="radio"/> | <input type="radio"/> |

4. How frequently are you solely responsible for making decisions within your role? (1=rarely, 3=sometimes, 5=regularly)

- | | | | | | |
|-------|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| | 1 | 2 | 3 | 4 | 5 |
| _____ | <input type="radio"/> | <input type="radio"/> | <input type="radio"/> | <input type="radio"/> | <input type="radio"/> |

5. As an external auditor, what procedures do you typically employ to detect financial statement fraud during audits? Please select the options that apply.

- Assessing internal controls and their effectiveness

-
- Evaluating management's fraud risk assessment process
 - Performing substantive testing on high-risk areas
 - Analytical procedures to assess the reasonableness and consistency of financial data
 - Risk Assessment
 - External confirmations with third parties
 - Assessing Accounting Estimates
 - Interviewing Personnel
 - Other
-

6. In your experience as an external auditor, how effective do you believe your measures and mechanisms are in detecting financial statement fraud during audits?

- Very effective
- Moderately effective
- Not very effective

7. Which procedures of auditing in your opinion are the most efficient in detecting financial statement fraud and why?

8. Have there been instances where you encountered challenges or limitations in detecting financial statement fraud during audits? If yes, please provide brief details of such cases.

9. How do you handle situations where there is suspicion or indication of potential financial statement fraud during an audit? Please select the options that apply

- Performing additional testing and procedures
- Communicating with management and those charged with governance
- Seeking assistance from forensic experts or specialists
- Referring the matter to regulatory authorities
- Other
-

10. Have you encountered situations where financial statement fraud was later discovered after the completion of an audit? If yes, how do you believe external auditors can enhance their procedures to minimize the risk of undetected fraud?

11. In your experience, how efficient and significant are the existing measures and mechanisms in detecting and preventing financial statement fraud within the organizations you audit?

- Very efficient and significant
- Somewhat efficient and significant
- Not efficient and significant

12. Based on your observations, what are the common gaps or challenges in the prevention strategies employed by the organizations you audit in addressing fraud? Please provide details.

13. Have there been any cases of fraud, specifically financial statement fraud detected in one of your audits or in your organization's history and how often or rare have they been?

- Yes, very often
- Yes, seldom
- Yes, rarely
- No

14. How do you assess the overall level of awareness and understanding of financial statement fraud among employees within the organizations you audit?

- High level of awareness and understanding
- Moderate level of awareness and understanding
- Low level of awareness and understanding

15. Are there any innovative or effective approaches you have encountered or recommended to organizations you audit to address the gaps or challenges in preventing financial statement fraud? If yes, please provide examples.

Attachment 3. Thesis template time chart (GANTT)

