RAMIFICATIONS OF MANAGEMENT FRAUD

Written By ***Sharad Kumar***

Faculty, Associate Professor Unicaf Federal University, Cyprus

Orcid Link: https://orcid.org/0000-0003-0664-9313

ABSTRACT

Management Fraud is a form of fraud, which normally does not come on surface, but its impact is staggering both in economic terms as well its effect on victims.

Fraud whether it is committed by an employee or a manager is a concern of total society. Controlling fraud is everyone's business. However as citizens of a democratic society we accept the top executives of various organizations to foster conditions and create environment, which would inhibit temptations of the managerial staff to commit frauds.

Primarily, responsibility for controls therefore lies with top executives, financial controllers, Auditors and Fraud Examiners. They can have a better understanding of the scope of management fraud and how to deal with it. The menace needs to be controlled.

In order to understand what management Frauds is. It would be appropriate first to have some idea and appreciation for the term fraud "For that purpose one must know its legal definition, implications and the basic reasons for its occurrence. It is more so necessary because management fraud is nothing but ramification of fraud.

The term fraud goes by many names such as theft, embezzlement, defalcation, manipulation and now days referred to as white-collar crime.

A dictionary definition of Fraud is "Intentional deception to cause a person to give up property or some lawful right. The intention to deceive is the key and in some situations it is not necessary that fraud be successful."

WHY PEOPLE COMMIT FRAUD

It is difficult to understand the rationality or the motivation that induces a person to commit fraud. Some perpetrators commit this crime to have a lavish life style and some do it to maintain a façade of some or to nourish their ego. Some steal to give generously to the less fortunate and justify it as fair means for redistribution of wealth.

In the modern world frauds are rampant and flourishing in unassuming proportions. Their impact in terms of money is enormous. They are a menace to any civilized society. However many persons claim that this menace is a gift of modern civilization and by-product of advance science and technology. Some of the reasons, which have fostered the growth of frauds, include

- The ever expanding human relationship nationality and internationally provide greater opportunities of interactions. This in turns results in behavioral complexities and consequently giving rise to a variety of fraudulent practices.
- The ever-increasing population and ambition to have decent living standards has given rise to increased commercial activities and consequently to greater fraud opportunities.
- Increasing world resources tempt many ambitions persons to engineer new methods of committing frauds they claim that they have their share in the resources.

Technological advancements and improved scientific knowledge though provide with better means of dealing with frauds but ingenuity and craftiness of perpetrators does not lag behind. At times they outpace the scientific knowledge of the victims.

- Excessive influence of a few lucky citizens to become eyesore to some persons. They develop jealousy and frustration. Such condition pose threat to high moral standards and quite often encourage some persons to improve their lifestyles though deception

In short various forces are collectively responsible for fraud.

CATEGORY OF CORPORATE FRAUDS

Frauds in economic sense can be broadly categorized into two category Employees Fraud and Management Fraud.

Employees Fraud

Employees Fraud for the sake of convenience can be referred to as common Fraud. It relates to Frauds committed by employees in an organization.

Management Fraud

Management Fraud requires special considerations. It is a form of Fraud, which strictly does not fall within the narrow and legal definition of theft, embezzlement or Fraud though they closely resembles to that. It comprises deceitful practices adopted by Management to benefit them economically, socially or to sustain jobs to detriment to organization they work for. The Securities Fraud, insider trading, vanishing companies which collect unsuspecting investors' money from stock markets and tax evasion are few examples of such frauds. It is an organized crime carried out by either Board of directors on one hand or a group of employees on other hand to damage the Economy and organization respectively. Managers in this context imply line Managers i.e. Heads of divisions autonomous units or profit centers.

Managers referred to above are persons of high reputation, occupy positions of responsibility and are vested with powers. The appointing authorities have complete faith and in trust in them so much so that their offences many a time are covered up by authorities to avoid adverse effects of publicity. The paper deals with Frauds committed by such managers.

ASYLUM FOR MANAGEMENT FRAUD

Where it occurs?

There can be several factors for the occurrence of management frauds but mostly they hinge on two things the need and opportunity.

The Need

The need for committing fraud by a manager may arise to improve his status (life style) to satisfy an ego or to retain the job. Ambition to improve status i.e. living standards through deception and fraudulent practices has lured many managers to commit fraud.

Sometime managers may be forced to commit this offence due to economic reasons such as financial problems, sickness or to meet some other social obligations. But many a time managers have committed Fraud to have successful career or to retain job.

The Opportunity

The opportunities for managers to commit this offence are greater than compared to other employees because they enjoy fiduciary positions in an organization occupy position of trust and they command belief and trust of higher authorities.

Moreover, their motives are rarely disputed and their positions placed them above suspicion.

In addition, the managers are not generally subjected to ordinary check and balances techniques as is generally done for the subordinate staff.

In some organizations the managers are vested with wide and absolute powers and complete authority. Their performance is judged by results i.e. Attainment of corporate objectives and accomplishment of set goals. Their performance is generally communicated through periodical reports, financial statements statistical analysis and similar other methods of communication.

An alert and imaginative manager can easily conceive a Fraud and conceal it by using camouflaging techniques in such reports. The deception may remain obscure for a number of years or never come to surface if there is no surveillance.

REASONS FOR MANAGEMENT FRAUD

Generally job pressure compels managers to adopt deceptive tactics. These pressures may either be external or internal

The internal pressures comprise self- imposed disciplines, inner desires or obsessions for variety of purpose such as

- To excel in performance in comparison with prior periods.
- To show superior performance in comparison with contemporaries or colleagues
- To earn promotions, larger bonus or incentives
- To win favor of bosses for various reasons
- To retain the coveted positions by any means

These are undoubtedly healthy practices but some time goals set for one may be unrealistic i.e. beyond ones reach either due to capacity limitations or due to resource constraints. Under such circumstances a manager is very tempted to employ deceitful tactics.

Sometimes the pressure may be external that is these may come from bosses. The goals set by bosses may be unrealistic and highly demanding. Since Managers may not refute them, they employ deceitful tactics to accomplish them or to make them appear as accomplished.

Whether forced internally or externally, reasons behind Management Fraud are summarized as follows:

Public Image

The Chief executives (policy makers) sometimes makes boastful statements in public from which they cannot retreat. Such utterances or pronouncement become corporate goals, plans or projects, which Managers are given to achieve. In the event of their failures they try to cover up the shortfalls various manipulative tactics and camouflage them by false and deceitful reports.

Self-Preservation

The first law of nature is self-preservation and in order to survive people quite often employ unethical methods. For example fear of layoffs due to closing down of a loss making division or unit process or an entity may compel managers to adopt fraudulent practices and conceal such actions by preparation of false reports.

Concealment of incompetency

Incompetent managers may adopt fraudulent practice in order to conceal their weakness. Competent managers generally have no fears. They advance in jobs on their merits but the incompetent ones try to use manipulative methods. In order to show good performance they may puff up their reports by distorting facts and figures.

Output Linked Incentive Plans

In most cases incentive plans are result oriented such as better the performance, fatter the bonus pay packet. In many organizations performance is shown in various forms of reports and statements. Human beings generally have one great weakness. They would like to glorify their attainments. However it becomes more prominent when the size of the reward is based on the size of reported figures. Wherever managers feel they can tamper with reported figures. To their advantage without the possibility of detection, some of them do succumb to such a temptation.

Ambition for Self Advancement

To be reckoned as a successful manager is the ambition of almost every manager. At times the ambition becomes an obsession. So when ambition becomes an obsession without solid accomplishments some managers resort to manipulative tactics. For example a production manager may have been given some time bound short term and Long-term goal.

In order to gain recognition and win confidence, he may attempt to show superior performance in short-term goals to detriment of long-term goals.

Vested Interest

Some unscrupulous managers may have some personal interest in some activities, which may jeopardize the interest of the organization. For example a production managers may have personal interest in a particular supplier because of some direct or indirect benefit. Under such circumstances he will manipulate to procure raw materials only form this favoured supplier? For this purpose he may even collude with the purchase officer and stores officer who would certify a low quality supplier for some price such type of arrangement will flourish by concealment and /or falsification of records.

Manipulation in Accounts

Some managers may prefer to show inflated profits or assets to improve their image in the market. The managers who wish their company shares be highly marketable may attempt to inflate profits or assets unfairly. The motive may be either to obtain short-term loans or to improve credit worthiness.

Such malpractices are adopted by managers mainly when they are assured of some material gain have the opportunity and are bold enough to face consequences in the event of detection.

When managers occupy strategic positions both in regard to accounting as well physical control of assets they may manipulate the records to their advantage. This may be detrimental to the interest of the organization they serve.

MANAGEMENT FRAUD INDICATORS

Although it is difficult to discern that a certain symptom is indicative of a management fraud usually an improper condition is a reliable indicator of this malady. The symptom only indicates that something is fishy looking barely on surface but real scandal may lie beneath. Some of the indicators of management fraud include

- Abnormal Delays in Submission of Reports: The report here implies statistical data, financial statements or similar other communications which is generally submitted by managers to higher authorities for decision making, planning, controlling or even evaluation of progress. Or that matter any report in order to serve the intended purpose should be timely and factual.
- However when the motive is to deceive the culprit deliberately delays in its preparation and submission with a view to manipulate the facts and figures. He makes delays to ensure that manipulations are not apparent and prone to questioning. He would analyze the data and test it from different angles to obtain reassurance that report would not trigger off any query.

Except in rare cases and exceptional circumstances, consistently late submission of reports should pose a question mark in the mind of receiving officer. He should investigate the reasons for undue delays. May be it is deliberate and with some ulterior motive.

- Bosses Performing subordinate duties: Generally a business transaction is completed in three phases namely Authorization, recording and custodial function. A manager often is entrusted with authorization function. No Fraud can easily be committed unless person responsible for receiving recording and custodial function are also taken in confidence or conspire to do the crime. The subordinates generally carry out the recording and custodial functions. A manager with ulterior motive would prefer to do the subordinate functions himself rather than to per4suade them to collude in the crime. So when managers prefer to assume subordinates duties regularly, the symptom should raise an alarm.
- Flouting Corporate Directives: Some managers quite often attempt to ignore or evade corporate directives or work in defiance of prescribed policies and procedures. Non-compliance with directives and use of evasive tactics are indicators of some inherent problems, which the officer wants to hide.

For example in one case the chief of finance of an organization was directed by corporate executive to introduce standard costing system but finance officer on one pretext or other delayed the matter for about three years. Eventually it was discovered that finance officer was trying to hide some costing problems, which the standard costing system would have exposed.

- **Private Business or Profession:** Some managers engaged themselves either Actively or thorough some dummy persons in private business, profession or vocation simultaneously with the job. They make the job as a springboard for diving deep into their own business. Apart from lack of concentration on the job they attempt to use company's funds and facilities for personal business.
- **Mixing of Support Documents to Effect Dubious Payments:** Sometimes frauds can be committed by a manager by preparing tow set of payment documents for one transaction. The duplicate payment is either fully misappropriated or shred with the payee. This is done by mixing the documents (originals and the duplicates) in such a way that both set of document give the impression of two different transactions Generally some time gap is provided to present the second set for payment. The dubious payment become more convenient when managers also perform subordinate functions.
- **Uneven relationship between Correlated Transactions:** There are various type of transactions in business for example sales man Commission to sales, insurance

premium to assets, interest to loan and raw material to production. These items have some sort of relationship. Variation may not always be in the same proportion but one item cannot be absolutely static and other may vary significantly.

For Example sales figure may be manipulated by manager by booking fictitious orders or contracts but if commission to salesman does not vary commensurate to sales the situation calls for an investigation. If commission is paid on inflated (bogus) sales. The salesman would undoubtedly accept the commission but would smell something fishy and may blow the whistle.

CONTROLLING MANAGEMENT FRAUDS TOP MANAGEMENT ATTITUDE

Generally management frauds breed and flourish because of the attitude and environment created by the policy makers. When the managers (middle level management) see the top executives' lifestyle are they living luxurious lifestyle enjoying lavish entertainments expensive holiday tours unethical dealings with government officials for various favors the seed for management frauds are sown.

Top management should stress publicly that honest dealings are the corporation's way of life. It should practically demonstrate it by showing its own commitment to the principle.

Reward the honest employees and managers by instituting incentive awards and accord promotions to employees with proven integrity.

The policy makers should create an environment, which puts honesty and integrity at a premium and improbity at a discount. The top executives must understand that the line managers have generally a good deal of autonomy in their functions. They generally have unbridled freedom. Consequently they have the scope and the opportunity for adopting malpractices.

Therefore there is a need to have such systems, which would provide necessary checks and balances on their actions without impairing their ego or innovative talents.

CONTROL MEASURES

- Establish realistic targets, standards and norms for various corporate plans and projects. Investigate all material deviations and try to establish the reasons, which are responsible for such deviations.
- Develop quantitative and analytical techniques to discover adverse trends and abnormal behavior for various business operations.
- Design management information systems (MIS), which may provide necessary data and feedback on quantitative and analytical techniques.
- Compare performance and efficiency of various production process and operations with established norms in industry.
- In case of manufacturing units establish norms for process wastes and production loses in critical areas. Similarly establish essential accounting ratios to study profit trends and Asses growth etc. in trading commercial concern.
- Clearly distinguish between acceptable performance and substandard performance. Investigate into the reasons for poor performance.
- Use surveillance techniques to discover cases where managers are engaged in side business.
- Introduce necessary surveillance or review procedures either by establishing a strong Internal audit or having a Fraud Examination section to deal with it. It should be given necessary independence to carry out periodic review of all my operations with a view to highlight departures from approved/established plans, policies targets and goals set for attainment by the concerned line managers.
- Identify instances of adverse trends in business operations; disintegrate self-interest, reckless decision and flouting directives.

CONCLUSION

Management Fraud is a form of fraud, which normally does not come on surface, but its impact is staggering both in economic terms as well its effect on victims.

Fraud whether it is committed by an employee or a manager is a concern of total society. Controlling fraud is everyone's business. However as citizens of a democratic society we accept the top executives of various organizations to foster conditions and create environment, which would inhibit temptations of the managerial staff to commit frauds.

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