

CORPORATE GOVERNANCE, TRANSPARENCY AND SHAREHOLDERS' RIGHTS: THE ROLE OF THE FORENSIC ACCOUNTANTS IN PROPELLING ECONOMIC GROWTH

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Abstract

The goal of realigning organizational activities with the interest of shareholders and regulatory authorities has made the prevention of weaknesses in the key areas of corporate governance, internal control and financial statement very crucial. Scandals in the corporate accounting world and the resultant need for transparency and honesty in reporting have made needful the engagement of forensic accounting skills in untangling complicated accounting maneuvers and entrenching good corporate leadership. This paper shows the role played by forensic accountants in responsibly addressing the concerns of investors about the financial report system, so as to protect shareholders' rights. It discusses the current corporate governance framework in Nigeria, the country's forensic accounting related effort and submit that in today's rapidly changing business landscape, it is important for accountants and companies to step away from the traditional approach that emphasized mere compliance with rules, and focus on the study and investigation of the traits underlying corporate behaviour and management. It recommends a very extensive engagement of the forensic accountant as a key component in the corporate governance system in order to engender economic growth.

Introduction

A number of fraud discoveries shook public confidence and the system of checks and balances designed to protect the interest of shareholders, creditors and other beneficiaries of public companies. The public and policymakers were jolted in October of 2001 when Enron, then the United States' seventh largest company, revealed more than \$1 billion of accounting errors that stunned investors and launched investigations. Since then, dozens of companies have been prosecuted or investigated for financial fraud, including WorldCom, which was responsible for the largest instance of accounting fraud as well as the largest bankruptcy in history. The conviction was on nine counts of fraud including securities fraud, filing false reports, and conspiracy. Up until that time, convictions for corporate fraud have been much more widespread than many realized. On March 22, 2005, the Wall Street Journal reported that from 1978 – 2002, Federal regulators initiated 585 enforcement actions for financial misrepresentation by publicly traded companies. (Crumbley, Apostolou, and Nicholas, 2005).

These recent corporate accounting scandals and the resultant outcry for transparency and honesty in reporting have made crucial the need the engagement of forensic accounting skills in untangling complicated accounting maneuvers that have obfuscated financial statements. The public demand for change and subsequent regulatory action has transformed the field of corporate governance. Increasingly, company officer and directors are under ethical and legal scrutiny. The goal is to responsibly address investors' concerns about the financial report, thereby protecting their shareholder rights (Ramaswamy, 2005). The fact of failure of the corporate communication structure have made the organizational stakeholders realize that there is a great need for skilled professionals that can identify, expose and prevent weaknesses in the key areas of poor corporate governance, flawed internal controls, and fraudulent financial statements.

Entrenching good corporate governance in Nigerian quoted companies is a must. There have been incidents of corporate failures, corporate frauds, and overstatement of accounts both locally and internationally. Any failure to properly deal with this problem may result into total loss of confidence in the capital market with all the attendant negative consequences. In particular, the match towards attaining international competitiveness of the Nigerian capital market would suffer a major set back. Not long ago, there was another unpleasant discovery of overstatements of accounts Cadbury. (Nig) Plc. This no doubt is another challenge to the regulators as it apply showed that no company is above board on this problem. Corporations scramble to realign their interests with those of their stakeholders by ensuring a well-developed and implemented policy of corporate governance, and honest and transparent reporting system, and effective/efficient internal control system.

It is believed that repositioning the Shareholder Associations will enable them become more effective in entrenching good corporate governance and that an efficient and focused Shareholder Associations' oversight on activities of company management will go a long way stemming cases such as the discovered Cadbury saga. This way, infractions and misconduct by those entrusted with managing corporate investments would be detected and dealt with (Al-Faki, 2007a).

It is against the background of recent accounting standards which are focused peoples' attention on the role of financial reporting and forensic accounting that this paper set out to: enunciate how forensic accounting serves as a catalyst in entrenching good corporate governance practice, transparency, and the protection of shareholders' rights; and bring limelight the Nigerian contexts as regards corporate governance, transparency and shareholders' rights. Since accounting is one of the links in the chain needed to promote good governance, transparency and protection of shareholder rights, it therefore becomes necessary for forensic accounting skills to become increasingly relied upon within a corporate reporting system that emphasizes accountability and responsibility to shareholders.

Shareholder Rights and Challenges in Nigeria

Although, the law provides that directors are to have regard to the interests of the shareholder and the company's employees in the performance of their duties, many times there is a divergence of opinion between the directors and shareholders as to how this works in practice. For example, the directors may prefer deferring a dividend or paying a lower dividend in for the reason of building reserves whilst shareholders maybe rooting for an immediate payout. More often today, the issue may be curbing a ballooning management compensation structure or the more complex manipulation of any forecasts in order to benefit from share option schemes agreed for management. The shareholder's challenge is how to ensure that a reality, the director's duties of care and skill are exercised with his best interest at heart. Regardless of the legal provision of the general meeting at the shareholder forum of overseeing the board, certain hurdles remain in the way of a proactive shareholder. These include problems such as holding meetings at locations inconvenient to many shareholders, affording shareholders an opportunity to heard in the actual conduct of meetings, failings in providing timely notification of meetings. However, the changing face of capital market calls for a radical departure from current shareholder attitudes of passivity. Evidence indicates that most individual shareholders buy and keep shares looking to long-term capital appreciation without an active monitoring of the corporate decision making process. An encouraging trend is the fact that the privatization process in Nigeria has enabled the average Nigeria to own shares in the newly privatized entities, heightened chances for increased participation, increased awareness of the mechanics of the corporate sector and increased demand on the process of wealth creating that is embodied in the

capital market. This hopefully should lead the shift from passivity to active involvement in the process of managing public corporation in the country.

In Nigeria, shareholder right issues such as the handling of general meetings, compliance and enforcement of the prohibition against Insider trading, the publication of director's dealings and transactions, adequate notification to shareholders of changes in capital affording them adequate time to participate, as well as the transparency of any extra ordinary transactions regarding price must always be adequately addressed. According Ali-Faki, 2007a, the following areas have been identified as key problem areas towards the effectiveness of Shareholders Associations in Nigeria: Proliferation of Shareholder Associations; Lack of regulatory oversight; Concerns over behaviour of some members at Annual General Meetings (AGM); Intense competition towards getting on companies' Audit Committee; Funding constraints; Governance problems and unclear succession arrangements; and Inadequate public enlightenment on shareholders rights, privileges and responsibilities. In a survey conducted amongst regulatory agencies, and other relevant stakeholders like chambers of commerce, issuing houses, lawyers, stockbrokers and shareholder organizations using the organization for Economic Co-Operation and Development (OECD) corporate governance assessment instrument, Nigeria was ranked low in the enforcement of shareholder rights in court and shareholder access to information.

The Code best practices on corporate governance in Nigeria stipulates the following on Shareholders' rights and privileges: directors should ensure that shareholders' statutory/general rights are protected on the time; shareholders are to elect directors and approve the terms and conditions of their directorships; venue of annual general meetings should be carefully decided such that majority of shareholders can attend and vote at the meeting and not be disenfranchised in terms of distance and cost; notices of annual general meetings should be sent a least 21 working days before such meetings with details such as annual report, audited financial statements and other information that will enable shareholders vote properly or any issue; the board should propose a separate resolution at general meeting on every substantial issue in such a way that the issues can be voted for in an organized manner; the board should ensure the implementation of decisions reached; at least one director should be on the board representing minority shareholders; shareholders holding more than 20% of the total issued share capital of a company should have a representative on the board unless they are in a competing business or are having conflicts of interest that warrant their exclusion; all shareholders should receive equal treatment from the board such that none is given preferential treatment or superior access to information or other materials; and the board should use the annual general meeting to communicate with shareholders as well as encourage their participation.

Further, the code states that with respect to institutional investigators, shareholders' activism through either institutional organized shareholders' group should not be discouraged by the board, institutional and non-institutional shareholders with larger holdings should act and influence the standard of corporate governance positively and thus ensure the optimization of stakeholders' value, and that information made available to institutional shareholders should as well be made available to other shareholders at the same time in such a way that neither group enjoys preferential treatment (Institute of Chartered Accountants of Nigeria, 2006).

Corporate Governance

Corporate governance mechanisms aim to protect shareholders' interests by limiting, without stifling, the decision rights of managers and controlling shareholders. According to the Institute of Chartered Accountants of Nigeria (ICAN) (2006), corporate governance is the system by which a company's affairs are directed and controlled by those charged with the responsibility.

Focus on Corporate Governance to Prevent Fraud: It is important to situate Shareholder rights in an anti-fraud context. Governance structures must serve to protect all investors and not individual investors (e.g. a company with single controlling shareholders) so that fraud will be allowed to proceed (Example: the “Parmalat” report). Some types of governance protection are:

1. **Independence of Board Members:** The purpose of independent directors is to help protect the interests of shareholders from that of management. Directors who are truly independent/honest can, for example, prevent the outright corporate looting and shady related-party transactions by preventing controlling shareholders from extracting private benefits from the company to the detriment of minority shareholders.
2. **Controls on Related-Party Transaction:** The existence of stricter controls on related-party transactions should be an important way of reducing the ability of both management and controlling shareholders to undertake transactions to benefits themselves over shareholders generally or individual shareholders in particular. Jurisdictions could require: (1) disclosure; (2) specific board approval of related-party transactions or (3) approval of a majority disinterested directors of such transactions, in order to be able to achieve this.
3. **Legal Protection for Shareholders and Minority Shareholders:** Specific legal protection designed to give concrete right to minority shareholders are important to individual shareholders. Examples are: (1) preemptive rights with respects to additional stock issues; (2) independent appraisals for buyout or going private transactions; (3) heightened voting requirements for certain transactions; and (4) direct and quick access to the court to address any potential violation of these rules. In addition, directors should be bonded by fiduciary duties to all shareholders, including minority shareholders. However, fiduciary duties are only as good as the ability of a shareholder to bring an action for redress in the court as a different access to the court or too lenient standard for directors will result in the existence of amorphous fiduciary duties which amount to very little.
4. **Sarbanes-Oxley, Internal Control and The Audit Committee Relationship:** A large part of a Sarbanes-Oxley Act is designed to help private fraud by, among other things, improving internal controls, requiring Chief Executive to satisfy the accuracy of their financial report, and strengthening the independent auditor relationship with the independent audit committee. It is important that internal controls, an independent auditor, an audit committee and Chief Executive Certification does not exist as mere requirements but that they operate effectively and should not be overridden-able by circumstances. It should be made possible CEOs and CFOs to override or sidestep internal control above fictitious revenue. A concentration of better controls, better follow-up of suspicious conduct, and Forensic Audit, cannot be overemphasized in this respect. (Campus, 2007).

Corporate Governance in Nigeria

These days, the need to ensure good corporate governance by management becomes difficult to realize as shareholders only have opportunity to find out about a company’s management at annual general meetings, and these meetings are poorly attended. The security and exchange commission (SEC) in junction with corporate affairs commission (CAC) inaugurated a 17 member committee head by Peterside Atedo in June 2000 in Nigeria to identify weaknesses in corporate governance practices, examine international best practices, and make recommendations. The final outcome of the committee’s work was an approved Code of Best Practice on Corporate Governance in Nigeria. The code is applicable to quoted companies and public companies with multiple ownership (Al-Faki,

2007b) and its main goal is the board of directors as leaders of corporate organizations and the responsibility of other stakeholders, shareholders and professional bodies inclusive. The code was divided into three parts namely: Board of Directors, Shareholders and the Audit Committee. Al-Faki (2006) affirms that all the public companies have been directed by the Nigeria federal government to report their level of compliance with the code in their annual report, accounts and prospectus (when ever issued). One of the SEC's operations departments (Office of the Chief Accountant) has been changed among others with the responsibility of monitoring public companies compliance with the code.

On reporting and control, the code emphasize that: the duty of presenting a balance, reasonable and transparent assessment of the company's position is that of the board; there is an overriding need to promote transparency in financial and non-financial reporting ensuring good internal control in the primary responsibility of the board; the board has a duty to ensure that the objective and professional relationship is maintained with external auditors who should not be involved in business relationships with the company; there should exist an audit committee of at least 3 non-executive directors with written term of reference which clearly spells its authorities; the director's presentation of a report on the effectiveness of the organization's internal control system in the annual report; and the directors ought to report that the business is a going concern with supporting assumptions/qualification as imperative, with written reference terms.

The enforcement and compliance of corporate governance in Nigeria is more of self regulatory effort than statutory backing has obtained in the United Kingdom, United States of America, and internationally, because large institutional investors exerts pressure on organisation to improve on corporate governance. Thus, the position of SEC and CAC is enforcing the code in Nigeria is the voluntary compliance should be encouraged, but appropriate sanctions applied where this become necessary and applicable.

Role of Forensic Accounting

The growth in field of Forensic Accounting has been as a result of the large-scale corporate scandals in the United States and Europe. It is a specialist area which has existed for a very long time, although forensic accountants are just now being increasingly quoted in the press, used by regulators and law enforcement agencies as well corporate organizations. Forensic accounting is the application of the skills and training of a chartered accountant to investigations, disputes and other reviews, the result of which might end up in a law court. Michael Brocks and Associates (2007) asserts that Forensic Accounting uses investigative and audit skills to reveal an accurate accounting of transaction or series of transactions, and that forensic accounting services are called upon before legal action commences as well as after the filing of a suit. Forensic accounting is further defined as "pertaining to or employed in legal proceedings". At the conclusion of the investigative process, the forensic accountant typically, issues an expert's report and is expected to defend the report and findings in court. The forensic accountant cannot rely on the works of internal and external auditors.

The forensic accountant is usually required to unravel the transaction issue and review what as actually occurred in cases of fraud, which by nature, are hidden in the accounting systems of the organizations. The forensic accountant is often the one called upon to qualify the value of the loss experienced by an organisation or individual (e.g. a shareholder). Loss funds are traced from back accounts to back accounts in order to identify where funds (or other assets) have ended up before working with a legal team to secure the necessary freezing and recovery of such funds or assets. The forensic accountant role is to understand the accounting records and show the true nature of the transaction been recorded.

For instance, in financial statement fraud cases (e.g. Enron), it might not be so much the case cash been stolen, but company loses or liabilities been hidden (or assets been overstated) by false accounting in the financial statements and records.

Forensic accountants are a key part in the investigation of shareholder or director disputes and insurance claims. Above all, the key skill of the forensic accountant is in communicating complex financial transactions or information in a succinct manner using pictures, graphs, and language which are readily understandable by non-accountants, particularly the legal profession, the judiciary, and juries. (PricewaterhouseCoopers New Zealand, 2007).

Although the forensic accountants is retained in a variety of areas, the following are his most common assignment: shareholders and partnership disputes; business interruption claims; employee fraud investigations; Matrimonial disputes and criminal investigations. Forensic accountant is retained by lawyers, insurance companies, courts, business and individuals. More often than not, the forensic accountant get advice by a client's counsel or legal protocol and privileges issues before the commencement of an engagement (Michael Brocks and Associates, 2007). Other services that might be rendered by forensic accountants include: the acquisition and disposal of businesses, resolution of disputes between shareholders and joint venture partners, resolving ambiguity in the accounting aspects of purchased price adjustment and helping to minimize the risk of disputes arising post deal, professional negligence claims, undertaking forensic due diligence on target companies and individuals prior to the completion of deals, reviewing compliance with anti-money laundering regulations for transactions involving regulated entities, tackling transaction related misrepresentation and helping to resolve shareholder disputes which might arise, for instance, as a result of difference of opinion concerning contractual liabilities, suspected fraud or negligence and minority prejudice actions. (PricewaterhouseCoopers U.K, 2007).

In spite of the introduction of the Sarbanes-Oxley Act (SOX), the Statement on Auditing Standards-99 (SAS 99), and the Public Company Accounting Oversight Board (PCAOB) the pressures on chief financial officers to manipulate accounting statement have not been removed. The PCAOB recommends that an auditor should perform at least one walk through for each major class of transactions. SAS 99 recommends brainstorming, increased professional skepticism and unpredictable audit tests. These are ensured through a proactive fraud approach which involves a review of internal control and the identification of the areas most subject to fraud. Certified Forensic Accountants (CFA) are on hand to always supplement the efforts of internal and external auditors in these regards. In the wake of recent landmark corporate governance reforms, the demands on expectations of the audit committee have changed dramatically in the sense that the audit committee's role, on behalf of the board of directors (and ultimately the shareholders), is more demanding and requires a deeper level of commitment. A failure to tackle these stepped-up responsibilities would be a detriment to the audit committee, the board and, most important, the shareholders (Reed, 2003). What ought to be the driver for the agenda of audit committees are financial reporting risks, the task for which forensic accountants are well qualified.

According to Ramaswamy (2005), the alignment between corporate governance, internal control, and external reporting activities are driven by governance committees. The forensic accountant can make significant contributions as part of the governance committee. For instance, in the area of corporate governance, the forensic accountant helps formulate and establish a comprehensive governance policy which ensures an appropriate mix of management, independent directors on the board, sets out the appropriate responsibilities of the board and the audit committees; and reinforce ethical behaviour through code of ethics for employees and management.

Others are: (i) helping to establish an efficient control system that encompasses a good control environment underlined by ethical behaviour and strong corporate governance policies, a superior accounting system which reports all relevant transactions; and strong procedural controls that guarantees the safeguarding of assets, proper authorizations, audit mechanisms, and proper documentation, in order to prevent fraud (ii) create, through policies, a positive work environment where employees are highly motivated and very responsible (iii) support the dissemination of the required information about governance and ethics policies to interested parties within and outside the organization since adequate reporting is also necessary to meet the compliance requirements of the stakeholders and the stock markets. This translates to the establishment of communication for stakeholders to be aware of their rights and responsibilities. (iv) Ensure vigilant oversight through monitoring compliance at the top levels of corporate power, management procedures and employee activity. (v) Initiate fraud deterrence by establishing consequences through an expectation of punishment. (vi) Tidying up forensic investigation issues by ensuring the integrity of financial statements against fraud, areas of risk and associated fraud symptoms, pursuing each anomaly aggressively, and rooting for the minutest details of accounting and financial anomalies.

Forensic Accounting Efforts in Nigeria

Forensic accounting is very new in Nigeria. There are private and public consultants who have shown strong interests in the forensic accounting discipline. Adeyemo (2007), a Nigerian forensic accounting report, attests to the need for forensic accountants by asserting that Nigerian banks are ripping off their customers and shareholders through means such as spurious or fraudulent bank charges, transaction debits, and excessive interest deductions on loans, advances, or credit facilities. Forensic accounting efforts in Nigeria include: the Due Process Review, Budget Monitoring and Price Intelligence Unit (BMPIU) (regulatory functions certification functions, monitoring functions, and training/advisory functions), Independent Corrupt Practices and other Related Offences Commission (ICPC), the Economic and financial Crime Commission (EFCC) and the Extractive Industries Transparency Initiative (EITI).

Conclusion

This work has been able to showcase forensic accountants as those who uncover the investigate fraud, financial detectives, as well as independent experts employed by management to uncover fraudulent financial reporting and misappropriated assets. Currently, forensic accountants are in great demand for their accounting, auditing, legal, and investigative skills in addition to their ability to coordinate company efforts to achieve a cohesive policy of ethical behaviour for the enthronement of a good corporate governance culture. The forensic accountant's skills in financial accounting, internal control systems, the law, other institutional requirements, investigative proficiency, and interpersonal skills have made it possible for corporations to rely on them for the development of a consistent system of corporate governance, disseminating such governance information within and outside the company, ensuring that governance policies and objectives are interwoven into the internal control system, setting up fraud prevention systems, and investigating any existing fraud.

An increasing number of researchers are finding that poor corporate governance is a leading factor in poor performance, manipulated financial reports, and unhappy stakeholders. Corporations and regulatory bodies are now trying to analyze and correct any existing defects in their reporting system. The interests of investors and other stakeholders are usually protected by a three-tier security system vis-à-vis reporting system regulated by public and private institutions which subject public companies to accounting and disclosure standards, and their auditors to audit, independence, ethical,

and quality control standards while the third is the system of internal control, which provides reasonable assurance on the effectiveness and efficiency of operations, the reliability of financial reporting, and compliance with applicable laws and regulations. Organizations/accountant should step away from the traditional approach to mere compliance with rules to begin the study of traits/behaviour of corporate management, which forensic accounting affords.

The legal framework for effective corporate governance in Nigeria appears to be in existence but compliance and/or enforcement appears to be weak or non-existent. The role of the courts in strengthening the corporate governance enforcement mechanism by the regulatory institutions is not in place.

Recommendations

The following measures are therefore recommended for Nigeria in respect of corporate governance, transparency, shareholder rights protection and the forensic accountant:

- (i) The role of courts as an enforcement mechanism of regulatory bodies should be strengthened in order to restore the confidence of the average shareholders in the capacity of the judicial system to help him enforce his rights through the rule of law.
- (ii) The capacity of the regulatory bodies e.g. SEC, CAC, etc be strengthened to enable them put in place more robust enforcement mechanisms to carry out oversight function on corporate governance compliance and monitor the activities/performance of quoted companies.
- (iii) The Institute of Directors (IOD) in Nigeria partner with the Securities and Exchange Commission in monitoring compliance with the code of corporate governance by companies for the purpose of promoting investors' protection.
- (iv) Companies, shareholders, and the government, must, more than ever before engage the services of forensic accountants in adopting and disclosing a code of business conduct and ethics for directors, officers and employees. The code must address conflicts of interest, confidentiality, fair dealing, protection, proper use of company's assets, reporting of illegal and unethical behaviour and compliance with laws, rules and regulations.
- (v) To prevent or deter fraud, prevent future meltdowns, and guarantee transparency and honesty which are the two important qualities of corporate reporting, the forensic accountant's role must be accorded a prominent attention.
- (vi) There should be effective and honest communication with shareholders to enable them understand the business, risk profile, financial condition and operating performance and trends of the company. Other avenues such as company websites and establishment of investors' desks at designated locations should be explored apart from annual report and accounts, proxy statements and formal shareholders' meetings. Shareholders should participate in not only in removal of directors but also in nominating them for appointment. They should also be given opportunity to place items on the agenda, ask questions of the board at the general meeting on the company's remuneration policy for key executives and board members which should be linked to performance.
- (vii) Finally, the active involvement of Institutional investors ought to ensure that: Board members possess adequate experience and are truly independent; Executive remuneration is not excessive; Early warning signals are detected from the wealth of information made available to shareholders; Company funds are not diverted to non-core activities or for the benefit of related parties; and Shareholders are led in demanding corrective action where such action is warranted.

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