FINANCIAL INVESTIGATION AND DISCLOSURE AS DEFENCE MECHANISMS AGAINST CORPORATE FRAUD IN NIGERIA: ARE WE THERE YET?

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ABSTRACT

This paper examines the concept of financial investigation and disclosure as defense mechanisms against corporate fraud in Nigeria within the ambience of reforms that followed corporate frauds and failures that swept across the world in the last one decade. In writing this paper, the doctrinal research method (i.e. the library-oriented research) was adopted. Accordingly, primary research materials were reviewed from the Bank and Other Financial Institutions Act, LFN 2004 (as amended), the Companies and Allied Matters Act, Cap C20 LFN 2004, the Assets Management Corporation of Nigeria Act 2010 (the AMCON Act) and the libraries in writing this paper. Secondary research materials such as textbooks and law journals containing articles by academic writers were also considered. The paper finds that though investigations are usually mounted after the incidence of corporate fraud had happened, it could be a useful tool in curtailing the occurrence of corporate fraud and can reduce or even prevent the menace resulting therefrom. Company administrators and managers are enjoined to do more by benchmarking the position of disclosure in corporate governance in checking company failures and insider abuse.

Keywords: Financial Enquiry, Disclosure, Corporate Fraud, Corporate Governance.

1. INTRODUCTION

The alarming rate, which corporate entities commit financial and accounting fraud today is unbelievable signaling a red alert to all and sundry. The number of companies and multinationals that were found window dressing their operating revenues and profits or applying income smoothening in reporting their operating performance is quite disappointing. These financial corporate frauds involved huge amounts of money and were geared towards maintaining or increasing the share price of the perpetrating companies in the stock exchange market. The subject matter of corporate fraud and corporate governance leapt into the global business limelight from relative obscurity after a string of collapses of high profile companies. Enron, the Houston, Texas based energy giant and WorldCom the telecom behemoth, shocked the business world with both the scale and age of their unethical and illegal operations. These organizations seemed to indicate only the tip of a dangerous iceberg. While corporate practices
in the US companies came under attack, it appeared that the problem was far more widespread. Large and trusted companies from Parmalat in Italy to the multinational newspaper group Hollinger Inc., Adephs Communications Company, Global Crossing Limited and Tyco International Limited, revealed significant and deep-rooted problems in their corporate governance. Even the prestigious New York Stock Exchange had to remove its director (Dick Grasso) amidst public outcry over excessive compensation.¹

In developing economies, the banking sector among other sectors has also witnessed several cases of collapses, some of which include the Alpha Merchant Bank Ltd, Savannah Bank PLC, Societe Generale Bank Ltd, All States Trust Bank PLC, African International Bank PLC (all in Nigeria), The Continental Bank of Kenya Ltd, Capital Finance Ltd, Consolidated Bank of Kenya Ltd and Trust Bank of Kenya among others.²

According to Waymark,³ studies in South Africa show that South African companies reported, as at October 2007, an average of 23 cases of corporate fraud during the preceding two years, with each organization losing an average of over R7.4 million in that period. However, despite the introduction of new and more stringent corporate governance regulations in that country, corporate fraud remains a significant concern for South African business.

In Nigeria, however, the most notable corporate fraud is the case of Cadbury Nigeria PLC. The company was found to be falsifying its financial and accounting reports by inflating its profit figure by millions of Naira. It is suspected that other big companies in Nigeria and other African countries may be doing the same thing in order to influence their share prices and attract investments⁴. Another similar case to Cadbury's is that of Afribank Nigeria PLC. Afribank's financial statement showed high profits amid accusation by its former Managing Director that the Board of Directors colluded with its auditors to cook the books. This came more than a month before Cadbury's.⁵

Corporate financial reporting is the medium through which companies communicate to the external society and the general public about their operational performance in terms of profitability, efficiency, and responsibility.⁶ Corporate financial reports are a company’s bill of health. Various stakeholders do take their respective decisions relative to a company based on the information supplied by it in its annual financial reports and accounts.

The objective of corporate financial report is to provide information about the financial strength, performance and changes in financial position of an enterprise that is useful to a wide range of users in making economic decisions.⁷ The report should be understandable, relevant, reliable, and comparable. When the financial reports are distorted they will no longer portray the true and fair view of the financial performance and position of the reporting entity, which will go a long way in making the various stakeholders to take wrong decisions and even suffer damages. Where this happens, an accounting scandal or corporate fraud is deemed to have been committed.

Financial investigation, on the other hand, is the medium through which the financial activities of an entity are checked and examined in order to ascertain their true and fair status. It is a process that involves a series of verifications and examinations aimed at unveiling both

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³ Waymark, Stuart’ ‘Preventing corporate fraud: Know and avoid the myths’, Fraud Investigations & Dispute Services partner, Ernst & Young, 2007.
intentional and accidental financial misstatements; and other deliberate deceptions for the purpose of deriving benefits therefrom.

Disclosure, on its part connotes openness in company affairs at all levels. It refers to the volume of information to be made available to concerned and interested members of the public either through the regulatory authorities or by all persons involved before, during, or after the formation of the company on the one hand; and during the lifetime of the company, its drying times and after the death of the company on the other hand. Thus Disclosures of information by companies have over the years become a very important tool of corporate governance. Its importance is anchored on the fact that issues of transparency and good governance have attained prominence in the effort by nations to increase their competitiveness in the global economic market. Disclosure has become more relevant in recent times in view of several high profile corporate scandals, the unimaginable collapse of several industrial giants, business failure and particularly in Nigeria’s banking sector; monumental level of corruption and insider abuse.8

A securities market will be efficient if information affecting the value of securities is readily available to investors. The ultimate aim of regulation, therefore, is to prevent or minimize abuse, which might distort information and the value of securities, thereby having investors’ confidence and the market’s integrity marred. As succinctly put by Farrar9, disclosure of information is the best guarantee of fair dealing and the best antidote to mistrust. Its overriding aim is to afford an umbrella protection primarily to investors and to some degree, to creditors and those to whom the corporate form owes corporate responsibility10.

This paper therefore attempts to carry out an analytical study, of the concept of financial investigation and disclosure and how they can be used to curtail or hinder the occurrence of corporate and accounting frauds in Nigeria. The paper provides discussions on the concepts of corporate fraud, financial investigation and for disclosure, thereby bringing to bare some of the notable corporate frauds that happened in this new millennium. Part 2 examines the concept of Financial Investigation as a necessary panacea to checking corporate fraud and ultimately, corporate failures. In Part 3, the concept of corporate governance and corporate fraud are examined. In doing this, the paper analyses some Disclosure mechanisms at checking incidences of corporate fraud. In Part 4, the paper is concluded and recommendations for reform made.

1.1 THE CONCEPT OF FINANCIAL INVESTIGATION

The existences of fraud in the administration of corporate entities make it imperative for it to be investigated so that its causes and effects could be established and guarded against

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10The general principles of regulatory control centre around the following issues; Reporting: the Companies and Allied Matters Act Cap C20 Laws of the Federation of Nigeria, 2004 (hereinafter referred to as ‘CAMA’), Investment and Securities Act 2007 (hereinafter referred to as ‘ISA’), Bank and Other Financial Institutions Act (hereinafter referred to as ‘BOFIA’) et al; impose various reporting requirements. These may be general such as Directors’ Reports under s 342 of CAMA or Financial Statements under s 345 of CAMA and Auditors Report and filing with the Commission under s 345 (3) of CAMA. Reporting could be to shareholders in a general meeting or to the regulators or both. See also Solomon, Lewis D Bauman, Jeffrey D et al, Corporation Law and Policy Materials and Problems (4th edn, St Paul, MINN, 1990) 281. They submitted that the only standard which must be met when registering securities is adequate and accurate disclosure of required material facts concerning the company and the securities it proposes to sell.
future occurrences. Investigation simply means an examination or inquiry into something, especially a detailed one that is undertaken officially. The aim of any investigation is to discover the fact or truth.

Financial investigation, however, implies the process of discovering the fact about financial misconduct through a detailed verification and examination exercises so that the causes, effects and perpetrators could be ascertained. Financial investigations are undertaken by designated professionals, including the accountants, auditors, police, or other government agents.

Corporate financial activities are usually undertaken by the professional accountants who have the requisite knowledge and legal qualification to act as such. The investigation of fraud within a corporate entity requires a specialized skill and manner of approach, hence the introduction of forensic accounting. Forensic accounting is the specialty practice area of accountancy that describes engagements that result from actual or anticipated disputes or litigation. Forensic means suitable for use in a court of law, and it is to that standard and potential outcome that forensic accountants generally have to work.

Forensic accountants, also referred to as forensic auditors or investigative auditors, often have to give expert evidence at the eventual trial. All of the larger accounting firms, as well as many medium-sized and boutique firms have specialist forensic accounting departments. In the words of Crumbly, the value of forensic accounting is not limited to determining the extent of business fraud; but can help business owners avoid bad decisions in mergers and acquisitions and help attorneys distinguish between business valuation and financial investigation. Investors buy stocks and bonds to make money; therefore they generally invest in companies that appear to be successful. Corporate fraud occurs when companies mislead the public and analysts by manipulating information to appear strong and profitable when in reality they are not.

2. APPROACHES TO FINANCIAL INVESTIGATION

Van Duyne and Levy identified a three-step approach to financial investigation as follows:

- Secure and collect all tangible and oral evidence in a manner consistent with the rules of evidence to ensure admissibility;
- Gather additional evidence through interviews;
- Analyze the evidence; and,
- Present the evidence in an understandable manner.

The above listed stages normally involve using the technology of computer forensic analysis, data analytics and conducting interviews.

2.1 Securing and Collecting the Evidence: Computer Forensics:

The most successful method of detecting improper activities at corporations where fraud is suspected is through the use of technology. Nearly all of a company's information is created and managed electronically, yet typically only a third of that information is committed
to paper. The majority of investigations, therefore, requires careful searches of electronic information rather than following a paper trail. Computer forensics allows fraud investigators to uncover more of the facts, support otherwise unsubstantiated information, confirms or refutes allegations, and analyzes competing theories in relation to those facts. It involves identifying, collecting, analyzing large numbers of data. But without the correct presentation or codification of data, it may not be admissible in a legal proceeding. Typically, the forensic group would search and analyze:

- Emails
- Documents and files that may be hidden, password protected, or encrypted
- Files that have been generated from the operating system (i.e., enhanced metafiles)
- Databases of all user input and activity
- Recently opened, accessed, created or deleted files, and
- Online activities, including Internet banking transactions
- However, electronic evidence is not limited just to laptop and network computers at the workplace. Offsite computer files, servers, and even the head accountant's BlackBerry can prove valuable in an investigation.

2.2 Gathering Additional Evidence Through Interviews

Successful fraud investigations require interviewing potential witnesses, people with information about a particular infraction, and in some cases, speaking with the suspected perpetrators of fraud themselves. The professional interviewer, therefore, has a detailed and organized plan in place. Knowing this will help you understand how investigators acquire oral evidence. The objective of an interview in a fraud situation is to gather facts related to potential motives on the part of the perpetrator, and to verify opportunities presented to the perpetrator for committing a fraud.

The interviewer carefully organizes the structure of the interview, including its location, attendees, and the series of questions that will be asked. Questions are designed so that they draw out the best possible information from the interviewee. For instance: What will be gained from the interview? What should be known about this individual's activities? Is the interviewee a suspect or just a lead? As well, the interviewer often takes into account body language and certain words and phrases which could indicate deception.

- **Analyze the Evidence:**
  The evidence so collected in (a) and (b) above are adequately collated and analyzed so that appropriate conclusion can be obtained.

- **Present the Evidence in an Understandable Manner:**
  The evidences discovered from the investigation are presented in the most appropriate manner and using such presentation format that is most suitable.

According to Crumbley et al,16 forensic accountants utilize an understanding of business information and financial reporting systems, accounting and auditing standards and procedures, evidence gathering and investigative techniques, and litigation processes and procedures to perform their work. Forensic accountants are also increasingly playing more proactive risk reduction roles by designing and performing extended procedures as part of the statutory audit, acting as advisers to audit committees, fraud deterrence engagements, and assisting in investment analyst research.

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3. THE CONCEPT OF CORPORATE FRAUD

According to the Encyclopedia, fraud in the broadest sense is a deception made for personal gain or to damage another individual. The specific legal definition varies by legal jurisdiction. Fraud is a crime, and is also a civil law violation. Many hoaxes are fraudulent, although those not made for personal gain are not technically frauds. Defrauding people of money is presumably the most common type of fraud. Podgor\textsuperscript{17} said in criminal law, fraud is the crime or offense of deliberately deceiving another in order to damage him/her usually to obtain property or services unjustly. Fraud can be accomplished through the aid of forged objects.

The Canadian Institute of Chartered Accountants defines fraud as ‘an intentional act, by one or more individuals among management, other employees, those charged with governance or third parties, involving the use of deception to obtain an unjust or illegal advantage.’ These activities can include misappropriation of cash or inventory, fraudulent financial reporting and money laundering.

Fraud, in addition to being a criminal act, is also a type of civil law violation known as a Tort. A Tort is a civil wrong for which the law provides a remedy. A civil fraud typically involves the act of intentionally making a false representation of a material fact, with the intent to deceive, which is reasonably relied upon by another person to that person's detriment. A ‘false representation’ can take many forms, such as:

- A false statement of fact, known to be false at the time it was made;
- A statement of fact with no reasonable basis to make that statement;
- A promise of future performance made with an intent, at the time the promise was made, not to perform as promised;
- A statement of opinion based on a false statement of fact;
- A statement of opinion that the maker knows to be false; or
- An expression of opinion that is false, made by one claiming or implying to have special knowledge of the subject matter of the opinion. ‘Special knowledge’ in this case means knowledge or information superior to that possessed by the other party, and to which the other party did not have equal access.

Fraud for profit involves industry professionals. There are generally multiple loan transactions with several financial institutions involved. These frauds include numerous gross misrepresentations, including overstating income, assets, loan collateral, the length of employment or reporting fictitious employment, etc. It could also be in the form of understating operating expenses by corporate entities.

Corporate fraud (also known as Accounting scandals, or corporate accounting scandals) are political and business scandals which arise with the disclosure of misdeeds by trusted executives of large public companies.\textsuperscript{18} Such misdeeds typically involve complex methods for misusing or misdirecting funds, overstating revenues, understating expenses, overstating the value of corporate assets or underreporting the existence of liabilities, sometimes with the cooperation of officials in other corporations or affiliates. In public companies, this type of ‘creative accounting’, do amount to fraud and investigations are typically launched by government regulatory agencies, such as (in Nigeria for example) the Securities and Exchange Commission (SEC), the Institute of Chartered Accountants of Nigeria (ICAN), etc. Moreover, the accounting scandals that rocked the corporate world have been blamed for a range of

factors, including unethical behavior among executives, incentives to manipulate financial information for personal gain and lack of independence among monitors.  

4. SOME EXAMPLES OF GLOBAL CORPORATE FRAUD

As contained in Microsoft Encarta Premium, the summary of some notable corporate frauds and accounting scandals that occurred in this new millennium is provided below:

(a) Worldcom Inc.

The accounting fraud uncovered at Worldcom in 2001/2002 proved to be the largest in U.S. history. The company overstated its earnings by $11 billion, and its subsequent bankruptcy cost investors an estimated $200 billion. The U.S. Department of Justice brought criminal charges against Worldcom’s former chief financial officer, and the SEC of the United States filed civil lawsuits against four former Worldcom executives.

(b) Enron

In April, 2001 Enron revealed that it was owed more than $500 million by bankrupt California energy companies. In August its chief executive officer (CEO), Jeffrey Skilling, resigned, a sign that all was not well in the company. On October 16 Enron reported a third-quarter loss of $618 million. The next day Enron revealed that due to an accounting error it had overstated the company’s net worth by more than $1 billion. The two reports caused investors to lose confidence in Enron and its stock price fell.

(c) American International Group (AIG)

In 2005, was under investigation for accounting fraud. The company already lost over 45 billion US dollars worth of market capitalization because of the scandal. This has been the fastest decrease since the Worldcom and Enron scandals. Investigations also discovered over a billion US dollars worth of errors in accounting transactions. Future outcome for the company is still pending.

(d) Cadbury Nigeria Plc

The most notable corporate fraud or accounting scandal in Nigeria involved Cadbury Nigeria PLC, one of the biggest food and beverage manufacturer in Nigeria. It was discovered that the profit reported by the company for some years were overstated by N1 billion to N2 billion via creative accounting. Cadbury, which is one of Nigeria’s leading companies, was fined for publishing misleading accounts for a number of years in order to boost its profits. The suspicion, however, is that it is not the only company engaged in this practice. The case is believed to be the first of its kind in Nigeria, the country that is trying to shed its image of corruption to attract foreign investment. The Nigerian chief executive, Bunmi Oni, who was named by PricewaterhouseCoopers, the company’s auditors, as Nigeria’s ‘most respected CEO’ at that time, and the finance director, Ayo Akadiri, were ‘relieved of their positions’.

In 2002, a wave of separate but often related accounting scandals became known to the public in the U.S. All of the leading public accounting firms, for example, Arthur Andersen,


Deloitte & Touche, Ernst & Young, KPMG, PricewaterhouseCoopers, and others have admitted to or have been charged with negligence in the execution of their duty as auditors to identify and prevent the publication of falsified financial reports by their corporate clients which had the effect of giving a misleading impression of their client companies’ financial status.\textsuperscript{21} In several cases, the monetary amounts of the fraud involved are in the billions of US Dollars. The audit firms and the companies ensnared by accounting scandals, which mostly occurred in the third millennium, are listed below:

- Ernst & Young: AOL Time Warner, Dollar General, PNC Bank, Cendant, HealthSouth.

5. CORPORATE GOVERNANCE, CORPORATE FRAUD AND DISCLOSURE

Corporate governance refers to the processes and structures by which the business and affairs of an institution are directed and managed in order to improve long-term shareholder value by enhancing corporate performance and accountability, while taking into account the interest of other stakeholders. Corporate governance is about building credibility, ensuring transparency and accountability as well as maintaining an effective channel of information disclosure that would foster good corporate performance. Corporate Governance therefore is the processes and systems by which a company is governed which ensure appropriate checks and balances as well as the manner companies and enterprises are managed efficiently.

According to Crawford,\textsuperscript{22} Corporate governance is the set of process, customs, policies, laws and institutions affecting the way a corporation is directed, administered or controlled. Corporate governance also includes the relationships among the many stakeholders involved and the goals for which the corporation is governed. The principal stakeholders are the shareholders, management and the Board of Directors (BOD). Other stakeholders include employees, suppliers, customers, banks and other lenders, regulators, the environment and the community at large. An important theme of corporate governance is to ensure the accountability of certain individuals in an organization through mechanisms that try to reduce or eliminate the principal-agent problem.

Corporate Governance for quite some time was misconstrued as confining to only corporate management. However, it is something much broader for it must include a fair, efficient and transparent administration to meet certain well defined objectives.\textsuperscript{23} Corporate governance also must go beyond the law. The quantity, quality and frequency of financial and managerial disclosure, the degree and extent to which the Board of Director exercises their trustee responsibilities and the commitment to run transparent organization. These should evolve due to interplay of many factors and the role played by more progressive elements within the corporate sector.

Key elements of good corporate governance principles include honesty, trust and integrity, openness, performance orientation, responsibility and accountability, mutual respect, and commitment to the organization.\textsuperscript{24} Of importance is how directors and management to develop a model of governance that aligns the values of the corporate participants and then

\textsuperscript{22} Crawford, C. J., \textit{Compliance & Conviction: The Evolution of Enlightened Corporate Governance}, (2007), Santa Clara, California: XCEO. 
evaluate this model periodically for its effectiveness. In particular, senior executives should conduct themselves honestly and ethically, especially concerning actual or apparent conflicts of interest, and disclosure in financial reports. The positive effect of good corporate governance on different stakeholders ultimately is a strengthened economy, and hence good corporate governance is a tool for socio-economic development. For example, following the dawn of privatization in Nigeria there was an upsurge in the number of shareholders and a change in the nature of shareholding from concentrated to dispersed ownership. The implication of this is that shareholders of the privatized companies are not only scattered all over Nigeria but held insignificant shares each to be able to monitor the performance of their directors. Consequently, the gap between ownership and control is widened beyond expectation. Corporate law is therefore not adequate to meet the challenges by dispersing ownership leading to renewed interest of stakeholders, investors, creditors and governments all over the world to search for effective corporate governance and management. Share ownership is now dispersed in Nigeria and the gap between shareholders and directors is getting wider. Shareholders are passive and have been reduced to mere supplier of capital.

The governance of corporations is now as important in the world economy as the governance of countries. Developments at the global level have necessitated the need for corporations and their stakeholders to imbibe the full complements of corporate accountability and efficiency. Similarly, globalization of economics on the world scale has brought with it the need to develop international standards of best practices for the benefit of investors, and all the stakeholders, a development necessitated by corporate failures which affected America, Asia, Europe and Africa and creating in the process economic instability. In the case of Nigeria, the commercial and banking terrain has been groping and grasping for breath and survival since the 80s and 90s. Even in this millennium, the ghost of financial distress is still seen haunting the financial service sector leading to the great Soludo and Sanusi era of banking reforms.

There is an inseparable link between corporate governance, management and investor confidence. No investor will consider investing in an enterprise devoid of transparency and accountability. While it is true that in the past few years, the Nigerian commercial terrain has witnessed vigorous legislative activities, particularly in the area of Company Law to facilitate business activities in the country and ensure that the tripartite interests of the investing public, the general public itself as well as that of the nation were protected, recent experiences have shown that deep rooted lack of corporate governance and management efficiency have continue to bug down the growth of corporations in Nigeria.

30 J. Ekeng, ‘The Paradox of Bank Ratings’. Available at www.m2weekly.com/feature/the-paradoxofbankratings/> accessed 30 March 2014. Shortly after the 2004 consolidation exercise, there was an unusual rush by Nigerian banks for awards and other forms of international recognition. No bank wanted to be outdone in the mad rush. Then the rating agencies got involved. Every bank was adjudged to be in great condition. But the ongoing shake-up in the industry has proved that the whole exercise was not a
In most organizations, corporate governance and responsibility have been sacrificed at the altar of nepotism and corruption. In Nigeria, according to Ajayi,\(^\text{31}\) it is no news to declare that more than 60% of the current banks in Nigeria today are padded up and their financial statements heavily suspect. Many of them are not worth placing funds with and their leaderships continue to carry on business as usual. The era of forex magic and round tripping may not be over yet at these banks.

At this juncture, it must be emphasized that financial reporting is a crucial element necessary for the corporate governance system to function effectively. Accountants and auditors are the primary providers of information to capital market participants. The directors of the company should be entitled to expect that management prepare the financial information in compliance with statutory and ethical obligations, and rely on auditor competence.\(^\text{32}\)

Current accounting practice allows a degree of choice of method in determining the method of measurement, criteria for recognition, and even the definition of the accounting entity. The exercise of this choice to improve apparent performance (popularly known as creative accounting) imposes extra information costs on users. In the extreme, it can involve non-disclosure of information. One area of concern is whether the accounting firm acts as both the independent auditor and management consultant to the firm they are auditing. This may result in a conflict of interest which places the integrity of financial reports in doubt due to client pressure to appease management.

The fraud committed in many corporate entities suggested that corporate governance in those entities is not living up to the expectation. The Directors have failed and that is why in each of the corporate accounting scandals they are greatly held responsible. Therefore, good corporate governance should be the one that is fair to all the various stakeholders in terms of corporate general administration and reporting the actual operating performance and position of the entity as at a particular date.

Comer\(^\text{33}\) concludes that board composition and the structure of a board’s oversight committees significantly correlate with the incidence of corporate fraud. He added that as the number of independent outside directors increased on a board and in the board’s audit and compensation committees, the likelihood of corporate wrongdoing decreased. However, Grant and Visconti\(^\text{34}\) argued that as more rigorous requirements for company reporting result in Board members and executives redirecting their efforts from strategy to compliance, recent regulatory measures may do little to enhance effective corporate governance.

As earlier discussed, Disclosure connotes openness in company affairs at all levels. It refers to the volume of information to be made available to concerned and interested members of the public either through the regulatory authorities or by all persons involved before, during, or after the formation of the company on the one hand; and during the lifetime of the company, its dying times and after the death of the company on the other hand. Disclosure of information by companies has, over the years, become a very important tool of corporate governance. Its importance is anchored on the fact that issues of transparency and good governance have attained prominence in the effort by nations to increase their competitiveness in the global economic market. Disclosure has become more relevant in recent times in view of several high profile corporate scandals, the unimaginable collapse of several industrial giants, business

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34 Grant, R. M. and Visconti, M, ibid note 19.
failure and particularly in Nigeria; monumental level of corruption and insider abuse as recently discovered by the Central Bank of Nigeria in the Nigerian banking sector.\textsuperscript{35} A securities market will be efficient if information affecting the value of securities is readily available to investors. The ultimate aim of regulation therefore, is to prevent or minimise abuses, which might distort information and the value of securities thereby having investor’s confidence and the market’s integrity marred. As succinctly put by Farrar\textsuperscript{36}, the disclosure of information is the best guarantee of fair dealing and the best antidote to mistrust. Its overriding aim is to afford an umbrella protection primarily to investors and to some degree the creditors and those to whom the corporate form owes corporate responsibility\textsuperscript{37}. Arguing further, Gower\textsuperscript{38} said:

England has pinned its faith on a philosophy of disclosure rather than of supervision. Our rules are based upon the assumption, which indeed underlies the whole of our company law that the best protection of the public lies in publicity. It is assumed that if one gives the investor full information about the company’s affairs he will avail himself of it and make an intelligent appraisal of the worth of the security offered.

For example, to ensure transparency in the operations of banks in Nigeria,\textsuperscript{39} the Central Bank of Nigeria has recently adopted the practice of publishing on its website the total interest

\textsuperscript{35}Igwe Kingsley, 'Investment, Nigeria Capital Market & Corporate Governance Laws, Practice & Ethics’ (2005) Corporate Governance, Disclosure and Transparency Law Development, Research, Publications & Consulting Ltd Vol 3 p.1 in Funmi Ogundare’s, ‘Sanusi: Corporate Governance, Key to Financial Stability’ ThisDay (Lagos, 11 February 2010). The Governor of Central Bank of Nigeria, Mallam, Sanusi Lamido Sanusi called on captains of industries to find lasting solutions to the lingering problem of weak corporate governance confronting the country’s financial system. He noted that the Central Bank of Nigeria in collaboration with other regulatory agencies is aggressively pursuing measures to stem unethical practices in financial institutions in Nigeria.


\textsuperscript{37}The general principles of regulatory control centre around the following issues; Reporting: Company and Allied Matters Act 1990 (hereinafter referred to as ‘CAM”), Investment and Securities Act 2007 (hereinafter referred to as 'ISA”), Bank and Other Financial Institutions Act (hereinafter referred to as ‘BOFIA”) etc; impose various reporting requirements. These may be general such as Directors’ Reports under s 342 of CAM or Financial Statements under s 345 of CAM and Auditors Report and filing with the Commission under s 345 (3) of CAM. Reporting could be to shareholders in a general meeting or to the regulators or both. S 24 of BOFIA contains duty of director to ensure that proper books of accounts are kept on all transactions necessary to explain such transactions and give a true and fair view of the state of affairs of the bank. Disclosure: Various laws require disclosure by directors of certain information; conflict of interest situations, interests in transactions, loans to directors, related party transactions etc. S 18 of BOFIA provides that no manager or any other officer of a bank shall (a) in any manner whatsoever, whether directly or indirectly have personal interest in any advance, loan or credit facility; and if he has any such personal interest, he shall declare the nature of his interest to the bank. Regulatory Responsibilities: Prohibition/exemption- Certain conduct may be prohibited (eg insider dealings in securities, ISA s 111. See also Solomon, Lewis D Bauman, Jeffrey D et al, Corporation Law and Policy Materials and Problems (4th edn, St. Paul, MINN, 1990) 281. They submitted that the only standard which must be met when registering securities is adequate and accurate disclosure of required material facts concerning the company and the securities it proposes to sell.


\textsuperscript{39}According to Bolodeoku Ige, ‘Corporate Governance: The Law’s Response to Agency Cost In Nigeria’ (2007) Brooklyn Journal of International Law volume 32 Number 2; the Code of Corporate Governance Practices issued by the Central Bank of Nigeria known as Code of Corporate Governance for Banks in Nigeria Post Consolidation (2006) 1.7, unlike most corporate governance code is mandatory. The facts that banks must comply with it and include the Code’s compliance status report in the audited financial statements underscores the banks’ responsibility to actively take steps that policymakers believe could prove useful in dealing with agency costs. The Code among other provisions requires banks to establish ‘whistle-blowing’ procedure that encourages (including assurance of confidentiality) all stakeholders to report any unethical activity or breach of the corporate governance code using, among others, a special email or hotline to both the bank and the CBN.
rates and charges obtainable in each of the financial institutions in Nigeria. The publication of
the rates and charges for January 2009 was sequel to allegations by the banking public of hidden
charges by Nigerian banks. These publications, as against the past ones contain the lending rate
of every bank, including all charges, fees and commissions. There are four main themes
underlying disclosure of information on company law. The first theme is that the assumption
behind many disclosure requirements is that behaviour can be influenced merely by requiring it
to be disclosed without the need of negative prohibition or positive regulation. According to
Gower:

If those who invest in, and manage companies know that their
activities will be subject to public security, their behaviour will be
modified to avoid public disapproval.  

The second theme is that apart from making full and frank disclosure to the creditors
and shareholders; pieces of information that are more obviously in the public interest must also
be disclosed by the companies because of the externality companies generate. Hence disclosure
can be viewed from this background as the recognition of new interest, besides those of
investors, in the way the company operates. The third underlying theme is that company must
make disclosure to the shareholders by the registration of its audited balance sheet and financial
information and at registration at the Companies House. The purpose of disclosure to the
shareholders is to promote efficient management by requiring the management to account for
their stewardship of the company. In this respect disclosure is just one of a number of
techniques used by company law to ensure the accountability of the management to the
shareholders.

We argue that the requirement of registration of companies at the Corporate Affairs
Commission, (as it is known in Nigeria) is in itself a justification for disclosure in the public
interest. Therefore, disclosure is all about openness and transparency in the affairs of the
company form. Many authors have referred to the word ‘disclosure’ in a number of ways which
captures its very essence. The critical issue about disclosure is that it is the price to be paid by
shareholders in return for the conferring of limited liability which insulates their personal
fortunes from the reach of the company’s creditors unless the shareholders have been persuaded
to give personal guarantees.

We opine that the disclosure regime in Nigeria is inadequate and had failed to provide
adequate information needed to safeguard the corporation, corporate investors and the public.
The disclosure mechanisms contained in the Company and Allied Matters Act 1990 and the
Securities and Exchange Commission Act do not carry with them efficacious sanctions and
punitive measures strong enough to deter those who man corporations in Nigeria from hoarding
and trading such information against the corporate interest and the investing public. The paper
suggests reform of the Nigerian corporate laws to match the rising cases and challenges of
corporate fraud, failures and insiders’ abuses with a view to boosting investors’ confidence in
corporate.

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40Gower LCB, fn 4 at page 463. The Learned Authors cited the example of the philosophy behind the
 provision introduced in the United Kingdom in 1967 that companies must keep a copy of any written
 service contract or if not in writing a written memorandum of its terms available for inspection by
 members of the company – the philosophy is that if the members could see how the Directors provided
 for themselves they might be more restrained in their generosity.

41Farrar JH & Hannigan BH, fn 2 page 464. In Nigeria, the Companies House is the Corporate Affairs
 Commission established under the Companies and Allied Matters Act, 1990.

Disclosure as ‘Transparency Obligation’.
6. THE USE OF FINANCIAL INVESTIGATION AND DISCLOSURE MECHANISM TO CURTAIL CORPORATE FRAUD

An investigation is usually mounted after an incidence has occurred. However, it can serve as a deterrent measure to the perpetrators, especially where severe punishments are integrated. In the corporate environment, companies try as much as possible to show to the public that they are successful and profitable in order to attract the right type and quantity of investment; and to ensure a steady movement in their share prices. That is why many of them resulted in creative accounting and income smoothing so that their financial performance and position are beautified.

In Nigeria, auditors are usually involved in corporate financial investigations, including those relating to fraud. In most of the African countries, forensic accounting is not viewed as a separate technique required for a thorough financial investigation. Once one qualifies as a chartered accountant and possesses the license to practice, he/she is adequately qualified to carry out financial investigations for the clients. The developments in the area of fraud investigation are yet to reach our environment in full and therefore heavy reliance is placed on the auditors as far as financial investigations are concerned. South Africa, Italy and Japan have recently beefed up their corporate governance codes to strengthen shareholders' oversight of corporate boards, pay practices. Financial investigation was used in these countries to discover the genesis and procedures of corporate fraud and other accounting scandals so that best strategies would be employed in curtailing and preventing the menace.

In the words of Hatice, et al., there are a number of systems available to help businesses protect themselves from corporate fraud, but being aware of the problem is the first step to closing the net on the criminals. His study reveals three commonly used types of corporate fraud mostly having direct bearing to the composition of the Board of Directors; and proffered strategies through which businesses can take some simple precautions to keep the fraudsters at bay. He, however, concluded that financial investigation could serve as a tool for unveiling the nature and attributes of such corporate frauds.

However, for financial investigation to be effective in checkmating and guarding against corporate fraud, there is the necessity to apply it both as a proactive and reactive mechanism. The United States government and its investigative agencies failed in their role to provide adequate protection to investors and their investments. The paper suggests that Wall Street Companies should be subjected to regular financial checks/investigations rather than waiting for an incidence to happen before mounting the investigation. This clearly reflects that even the largest economies in the world fail to take advantage of financial investigation as a proactive mechanism against corporate frauds.

In North Africa, the fight against corporate fraud was approached mostly under the introduction of new reforms on the area of corporate governance. Sourial recommends that, in North Africa, traditions and cultures should be allowed implicitly to choose their acquaintance with the number of reform measures that yield to better corporate governance practices. He further stated that shocking the system with a new wave of ideas might create resistance to reforms and deterioration.

7. CONCLUSION AND RECOMMENDATIONS

The issue of corporate fraud is a global issue. Many companies all over the world have been found in one way or the other adopting illegal measures towards making their financial

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statements attractive and beautiful. This paper has collected and collated background information on some of these incidences and the reasons behind them. The concept of financial investigation and disclosure were looked into as defence mechanisms for guarding against corporate fraud. Also, detail discussions were provided on the concepts of corporate fraud, financial investigation and corporate governance. The paper concludes that though investigations are usually mounted after fraud incidence happens, it could be a useful tool in curtailing the occurrence of corporate fraud and can reduce or even prevent the menace resulting therefrom. It was also discovered that financial investigation is mostly used as a reactive mechanism in Africa and Nigeria in particular and in most part of the world for unveiling corporate and accounting scandals of corporate entities. It is recommended that for financial investigation to be effective in curtailting and preventing corporate fraud in Nigeria, it should be complemented by the following:

- The introduction of more accounting and reporting reforms in the area of corporate financial reporting and the mounting of more severe punishments on any corporate entity discovered applying creative accounting and income smoothening.
- The composition of the Board of Directors and Audit Committees should be altered to incorporate more independent outside directors.
- The regulatory authorities to corporate entities in Africa should find a way of using financial investigation as a proactive mechanism rather than relying more on it as a reactive mechanism.

The paper also proposes that there should be a revisit to the state of the law guiding the regulations of private companies with a view to widening their scope. The realities of the present times have established beyond doubt that the view taken by the law that private companies are commercial ventures of private concerns are no longer valid and realistic. The law should accept the view that they are companies limited by shares and therefore there is the need for as much control over their activities in the same manner as SEC regulates dealings in shares by public companies. The reasons are not far-fetched. First, private companies constitute the majority of incorporated companies and have ceased to be mere family based businesses. Secondly, private companies are increasingly being funded by public funds and loans provided by financial institutions from the vast accumulation of public savings. This is beside the fact that there has been informal trading in the shares of private companies. In light of the above, the paper proposes that the present state of the law as it affects the securities of private companies be reviewed as follows:

- The disclosure philosophy should be extended to cover the formation and operations of private companies.
- There is a need for the SEC to regulate the private offering of private companies with the same tenacity as public offers of public companies.
- The same law applicable to public companies in respect of prospectus, disclosure, allotments liability for misstatements and free transferability of shares should also extend to private companies.
- Considering the relevance of private companies in term of the externalities they generate with the investing public, there is the compelling need to subject private companies to a compulsory registration and disclosure regime with a security ombudsman, SEC.
- Private placement documents generated by private companies should be subjected to the same disclosure rules stipulated by SEC for public companies.
- The private placement memorandum should be made to contain as much detail as the prospectus. The front page of the memorandum should summarize the terms of the offering. A brief description of the issuer's business should be given. Ideally, the front page should contain legal legends or red herring with respect to legal requirements of
the offering; persons capable of accepting the offer, the absence of representation other than those contained in the memorandum and the need for investors to obtain independent advice with respect to the offering and other matters.

- The proposed reform should also provide for the requirement of thorough scrutiny of memorandum of private placement with the same vigour as that imposed on the prospectus.
- The statutory civil and criminal liabilities attached to a misstatement in the prospectus should also apply to misstatement in memorandum of private placement.

Furthermore, this paper recommends a review of the registration of public companies. The present position is that public issues in Nigeria are patterned after a securities-based registration model. That is, the regulations come into play only when a company decides to go public with its securities. The Investments and Securities Act 2007, does not regulate the private offering or securities sold other than by way of public offer. It makes detailed provisions about the disclosure obligations of companies going public and for updating information on companies whenever they intend to issue further or other securities. It is aimed at disclosure that would inform an investor about an investment in a public offering, but does not aim at providing future or ongoing information about an issuer. The present procedure is a complete antithesis of disclosure philosophy which in simple terms preaches continuous inflow of information. Under the ISA, public companies seeking to raise capital from the securities market are obligated to make very extensive disclosure of the companies’ activities and prospects.45

Consequently, this paper proposes a company-based registration system where the focus will be on the registration of companies and not merely on the securities they intend to issue. The focus of a company-based registration system would be one which would require certain companies identified either by size of capital assets or employment enrollment to mandatory register with the SEC. The merits of this system are numerous, but paramount among them is the ease of information flow. Company-based registration models mandate the company (issuer) to make available by periodically filing its performance in the market and updated records of its activities.

Finally, this paper proposes that there is the urgent need for reform to require private companies of a certain size to be subject to registration and disclosure rules of the SEC. Eligibility for compliance by private companies could be dependent on the size of the company measured by its capital and number of employees. A company with assets about N10 million (Ten Million Naira) equity and loan capital inclusive for instance, has responsibilities to the public notwithstanding that its membership is below 50. Its loan portfolio is invariably owed to public finance institutions with obligations to savers/members of the public. This paper submits that they be co-opted under the regulatory ambit of the SEC.

One of the ways of organizing the dispersed shareholders for corporate monitoring is through the instrument of proxy. In view of the problems associated with the proxy system, the Japanese and the German bank-proxy model is being recommended as a means of reforming the proxy system in Nigeria. Under the bank-proxy system, the shares are bought by the banks on behalf of their customers who executes proxy authorization on their behalf so that the bank can sit on the board of those companies and also vote at the general meeting. Most of the time those banks also have shares in those companies. The proxy rules process should be changed to accommodate relatively new and important category of shareholder activity, namely the desire to influence management and the board of directors without directly seeking control of the entire board through proxy contest. In some cases, a shareholder Advisory Committee is put in place to serve as a shadow board. This is a product of the voting rights exemplified in the proxy process.

45 See Investment and Securities Decree No 45 (1999).
process. It is further recommended that the management of the affairs of the company should be left in the hands of the directors. Directors are technocrats in the art of corporate governance and they are in a better position to manage the affairs of the company and control management. However, we have witnessed several cases where the directors have failed in their responsibility resulting in cases of corporate scandals ever recorded in history. This led to various suggestions as to the composition of the board of directors. Some people have advocated for a single board consisting of independent directors. Others prefer a dual board structure as in Germany. Because of the peculiar situation of Nigeria, the unitary board with independent directors is hereby recommended. However, for public companies, half of the board should consist of independent professional outside directors. The directors will serve as a full time basis and they will be on the board of several companies. This will consist of academics, chartered accountant, management and financial experts, etc.

It is also recommended that good corporate governance can only be achieved by a combination of both formal and functional convergence. Formal convergence alone may not be effective, but functional rules without any elements of coercion will even be less effective. Most of the principles expressed in the rules of best practices are already part of an existing legislation which is enforceable. The conventional means of minority protection are no longer suitable for the type of dispersed ownership, we are now witnessing in Nigeria. In order to avoid the crash of our stock exchange, just as it happened in Czechoslovakia and Poland, urgent steps must be taken to evolve a suitable corporate governance rules. As we have pointed out that the British conventional means of minority protection afforded protection against controlling shareholders and not against management. While the government has taken steps to reform the capital market, however, the level of ignorance on the part of Nigerian investors is still a cause of serious concern. Therefore, the SEC and Stock Exchange still have a lot to do in sensitizing the investors on the operation of the securities market.

The leveraged buyout option is being recommended for Nigeria. As we have seen in LBO brings together three groups of people (expert in their own right), the management, the financier (banks) and institutional Investors. It is also a cross between equity capital and loan capital. Because of the involvement of funds from the bank, there is an effective check in the management to run the enterprises to repay back the loan. This process could have complemented the public offer for sale employed by the banks in making the mandatory equity ceiling of the Central Bank of Nigeria.

Although, there has been significant inroad to derivative action under CAMA, much still has to be done in this area. As has been shown in this work, the derivative action has been more effective in the United States, which gave shareholders unhindered access to the court to challenge any corporate wrong. Nigeria has a lot to learn from the U.S system. Moreover, there will be the need to clearly spell out, as is done in England presently, the procedures for bringing a derivative action under the Rules of the Federal High Courts in Nigeria as far as it affects corporate rights.

It is recommended in this work that institutional investors should get more involved in the sale of shares on the stock exchange. There is a need for a systematic growth of this investment group in Nigeria, especially with the dispersed ownership being witnessed today. It is against this background that we further endorsed the three approaches suggested by John Coffee for a privatization economy like Nigeria.

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46 For example, the fall of hitherto acclaimed first class companies like Enron, WorldCom, Tyco International, Adelphia Communications, Imclone, Nicor, Global Crossing, Sprint and Merck in the case of the United States woke the corporate world from its inebriate slumber.


Apart from suggesting optimal monitor through the institutional investors who has the necessary skill to monitor management, he suggested three approaches to reforms in the privatized economy of the civil law jurisdiction. They are Judicial, Structural and Legislative reforms. In his judicial reforms, he posited that the courts should be prepared to fill any vacuum created by statutory provisions. A corporate charter is highly incomplete contract and those gaps contained in the contract must be filled up. That the courts in common law jurisdiction has much more discretion to fill in the gap than those of civil law jurisdiction and this accounted for the protection offered by the corporate governance of common law countries.

Another aspect of judicial reforms he recommended has to do with the establishment of specialized courts to hear and determine security law disputes. For instance, in the US some aspects of the Federal Securities Act can be enforced before administrative law judges and the SEC has powers under section 21C of the Act to impose administrative cease and desist order, in effect, a type of civil injunction. It is a form of in-house securities remedy. Section 224 of the Investments and Securities Act 1999 in Nigeria established an Investments and Securities Tribunal which powers seem to cover this. However, there is the need to train judges of the tribunal on corporate governance and especially on securities law. The time for our public companies to devote more funds to serious professional research on corporate governance has come. This should not be left for government or agencies like the SEC, CAC alone. The study carried out by John Pound\textsuperscript{49} showed that the institutional investors in the US devote enormous resources to research.

Institutional investors would not mind committing a sum of $18 million on research in order to get an appreciation in the value of the shares that may fetch additional $80 in a year. The SEC could come in here and insist on companies committing a percentage of their fund on research and also the Bureau of Public Enterprises could do same for their privatized enterprises. The special share introduced in Britain for privatized company can also be explored in Nigeria to prevent a situation where the privatized companies are left exclusively at the mercy of core investors. One of the reasons for bringing in core investors and giving them majority shares is because they are considered to have the required technical and managerial abilities to manage those enterprises better. So Government could retain some shares in enterprises rendering essential services to avoid a situation where the country could be held to ransom. However, the government will undertake not to be involved in the directional policies of the company.

It is also recommended that the Nigerian Bar Association should be more involved in the evolution of suitable corporate governance in Nigeria. They should take a clue from the American Bar Association, which has intervened severally to ensure that effective corporate governance rules are put in place in the United States. For instance, in March of 2002, following the bankruptcy of Enron, the President of the American Bar Association appointed a task force to investigate corporate responsibility concerns. The task force produced a report which has been helped in shaping corporate governance debate in the United States. The Nigerian Bar Association should follow this honourable path. It is recommended that the Nigerian codes of best practices should be reviewed with the aim of incorporating some of the corporate and securities legislation that were enacted since 1995. These laws include the Nigerian Investment Promotion Commission Act, the Investments and Securities Act. This will give investors, especially international investors, a good idea of the investors’ protection in Nigeria and also help in checking corporate fraud.