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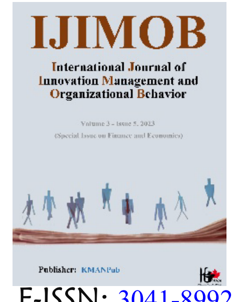
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Identification of Fraud Components and Political Factors Influencing Fraud in Financial Statements

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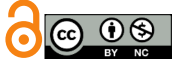
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ABSTRACT

Objective: The purpose of this research was to identify the components of fraud and the political factors affecting fraud in financial statements.
Methodology: The research method was fundamental in objective, qualitative in data type, and Delphi in data collection method. The population consisted of 20 experts from academia and finance, economic experts related to auditing and fraud, senior managers of leading companies listed on the Tehran Stock Exchange, and economic managers and professors. The research tool included targeted non-random interviews. For data analysis, the Delphi method was utilized.
Findings: The findings revealed that the components of fraud and political factors influencing fraud in financial statements include the fraud triangle and diamond (pressure, opportunity, rationalization, and capability) and political factors (individual and organizational).
Conclusion: In conclusion, this study highlights the intricate interplay between individual and organizational political factors and the traditional elements of fraud, providing insights into the mechanisms through which political dynamics influence fraudulent practices in financial reporting. This understanding could guide the development of more effective detection and prevention strategies.
Keywords: *Fraud components, Political factors, Financial statements.*

1 Introduction

Examining recent events in the realm of banking embezzlements and corporate accounting scandals, fraud and deception are no longer considered unexpected news. High-profile cases such as Enron, WorldCom, and Tyco have been notably affected by the destructive impact of fraud. These costly scandals have heightened global concerns about fraud, eroded billions of dollars in shareholder value, and resulted in the loss of investor capital and public trust in financial markets (Esmaeel et al., 2022; Ghadimi et al., 2022). In everyday life, fraud occurs in various business sizes, from small to large. This fraud involves asset misappropriation and deceptive financial statements. Asset misappropriation is a type of fraud involving the use or taking of company assets for personal

gain. Regarding the use of company money, inventory, or official vehicles for personal purposes, deceptive financial statements are acts of fraud conducted by concealing financial information so that the preparers alter the content of the financial statements to deceive financial statement readers for corporate or personal benefits. The increasing era of development has escalated the level of fraud, one of which is deceptive financial statements. Financial statement fraud is perpetrated by companies that manipulate their financial statements to attract investor interest in investing their funds in the company. Examples of such frauds include South Health Company, Enron, WorldCom, Tyco, International Trade, credit banks, and many other cases (Serly & Eddy, 2020). Fraud is generally an illegal act and a violation of the law aimed at personal gain. Financial fraud undermines trust between companies and market participants, threatening the existence and efficiency of the capital market (Liao et al., 2019). According to the 2016 report of the Association of Certified Fraud Examiners, the most significant losses to companies have been due to deceptive financial reporting. In Iran, the government's share in the economy is greater than that of the private sector; to such an extent that Iran's economy can be termed a state economy. The predominance of state-owned companies and major industries impacting the economy increases the government's power in decision-making and guiding macroeconomic policies in the capital market. For this reason, companies are inclined to establish close relationships with the government. Therefore, political factors not only influence the financial status of commercial units but can also affect the motivation and ability of managers in relation to financial reporting and the preparation of financial statements. This issue may lead to differences in the quality of financial reporting of business units that have political relationships with the government compared to those that do not (Wang et al., 2017).

This research focuses on the non-recognition of fraud components and political factors affecting them in financial statements and examines the economic and social consequences of non-recognition of fraud and political factors affecting them, showing how these issues can lead to serious damages for investors, public trust, the financial system, and even adverse political impacts. The current study investigates the economic and social risks associated with the non-recognition of fraud and political factors affecting it, demonstrating how these issues can weaken the economy and society, with a focus on the broader analysis and consequences of the non-recognition of fraud and political factors affecting it.

2 Methods and Materials

Given that the present study focuses on identifying the components of fraud and political factors influencing fraud in financial statements, the research method was foundational in purpose. The data collection was descriptive-survey in nature; the reasoning used was both inductive and deductive, and the nature of the data was qualitative. To delve deeper into the topic of fraud, particularly forecasting fraud based on political factors, the Delphi technique was utilized.

The population included academic and financial experts, economic experts related to the field of auditing and fraud, senior managers of leading companies listed on the Tehran Stock Exchange, economic managers, and university professors in economics who have executive backgrounds in auditing and are known as informed experts. This group was selected for the research and participated in the research process using the fuzzy Delphi method.

For determining the sample size in the qualitative section and selecting this group of experts, a purposive non-random sampling method was used. Given the time and resources available, 10 to 30 samples could be used for conducting interviews. Therefore, 20 experts divided into two groups—academic and operational—consisting of individuals who are prominent in their knowledge and information in the field of auditing were included.

2.1 Data Collection

In the fuzzy Delphi process, initially, variables and primary indices extracted from existing theoretical foundations are presented in a semi-open questionnaire format to the experts, who express their agreement with the initial and proposed indices and variables on a fuzzy trapezoidal scale from zero to ten and provide suggestions on other relevant variables if any. The researcher then analyzes the data from participants to address any incomplete responses with new information obtained from new participants.

2.2 Data Analysis

Fuzzy Delphi method was used to analyze the research data. The fuzzy Delphi method is used to examine the judgments of experts and to screen the most important factors in order to reach the most reliable group consensus on a specific topic. This is achieved through repeated questionnaires and consultations with experts, considering

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the feedback received. In this research, after extracting the indices and influential variables from the existing theoretical foundations, the initial influential variables were identified and presented in a semi-open questionnaire format for the experts' final remarks. Following the selection of experts and the preparation and dispatch of the worksheets to them, the responses were received and analyzed, disagreements were noted, and this process was repeated until a consensus was eventually reached. The results of this phase provided the infrastructure for the next stage. Finally, the quantification and measurement of the research variables were prepared and distributed in the statistical sample of the study. The data was collected and analyzed, necessary adjustments and modifications were made to the model, and the final research report was presented. The software used in this section was Excel. The Delphi method encompasses a series of rounds, with the classical Delphi typically involving four stages, usually adjusted to three rounds.

3 Findings and Results

In this research, the Delphi technique was employed for screening indicators. After the screening of indicators, the final model of the research was presented. Initially, each member of the group was given a questionnaire including the desired sub-criteria. These sub-criteria were then examined by experts in the field, consisting of 10 people in the selected sample who were familiar with all related matters, using the Delphi method. The scores assigned in the Delphi were between 1 and 5, consequently, sub-criteria with a score below 4 were eliminated. In this regard, experts assigned scores from 1 to 5 based on the importance of each indicator. The findings from the first round of Delphi showed that 10 indicators scored less than 4. Therefore, these indicators were not presented in the second round of Delphi. Also, 8 indicators were introduced by experts, which were included in the second round of Delphi.

In the second round of Delphi, all indicators scored above 4. As a result, no indicator was eliminated. To ensure the finalization of the process, Delphi was repeated in the third round as follows:

Table 1

Third Round of Delphi

Index	1	2	3	4	5	6	7	8	9	10	Mean
Threat to stability or financial profitability	5	4	5	3	5	4	5	5	5	5	4.6
Lack of adequate rights and benefits	4	5	5	5	5	5	3	5	5	5	4.7
Threat to personal financial interests of executive managers due to company performance	5	5	5	5	5	5	5	5	5	5	5.0
Company's inability to repay debt	5	5	5	5	5	4	5	5	5	5	4.9
Autocratic management style	5	5	3	5	5	5	5	5	5	5	4.8
History of claims against the unit under review, managers, board members due to fraud and law violation	5	4	5	3	5	5	4	5	5	5	4.6
Industry competition	5	4	5	5	5	3	5	5	4	4	4.5
Presence of repeated negative cash flows	4	5	3	5	3	5	5	5	5	5	4.5
Managers' tendency to use inappropriate methods to minimize profits for tax motives	5	4	5	4	5	3	5	5	4	5	4.5
Desire to conceal poor financial status	5	4	5	4	5	4	5	5	5	5	4.7
Violation of laws and regulations history	3	5	5	5	5	5	5	3	5	5	4.6
Tendency to attract financing from outside at minimal cost	5	4	5	5	5	5	4	5	5	5	4.8
Tendency to present expected profits	5	5	5	5	3	5	4	5	5	5	4.7
Tendency to demonstrate competence and enhance reputation in the profession	5	5	5	5	5	5	5	5	5	5	5.0
Interest in keeping stock prices high	5	4	3	3	5	5	5	5	5	5	4.5
Insufficient and inadequate time budget for auditing	5	5	5	5	5	5	5	5	5	5	5.0
Complex laws and regulations	5	5	5	5	5	5	5	5	5	5	5.0
Presence of corruption conditions in the country	5	3	5	5	5	5	5	5	5	5	4.8
Creation of limitations in the work of auditors	5	5	5	5	5	5	4	5	5	5	4.9
Unfair treatment of employees	5	4	5	5	5	5	5	5	5	5	4.9
Lack of appropriate incentive plans	5	5	3	5	5	5	4	5	5	5	4.7
Decrease in demand or increase in bankruptcies	5	4	5	4	5	5	5	5	5	5	4.8
Greed	5	5	5	3	5	5	5	3	4	5	4.5
Personal financial problems	5	5	3	5	5	4	5	3	5	5	4.5
Lack of sensitivity by society and the profession to the actions of auditors, accountants, and companies	5	5	4	5	5	5	3	5	5	5	4.7
Complex and illogical business transactions	5	5	5	5	5	3	5	5	5	5	4.8
Irresponsibility (failure to meet commitments)	2	5	5	5	5	5	5	5	5	5	4.7

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Access to timely position	5	4	3	5	5	5	5	5	5	5	4.7
Relationships among employees	5	4	3	5	5	5	4	5	5	5	4.6
Presence of weak internal control systems	5	4	5	3	5	5	5	3	4	5	4.4
Ineffective review and monitoring	5	4	5	5	5	5	5	3	5	5	4.7
Lack of awareness of laws and regulations	5	5	5	5	3	5	5	5	5	5	4.8
Lack of access to information	5	5	5	5	5	5	5	5	5	5	5.0
Inability to make quality decisions	5	4	3	5	5	5	5	5	5	5	4.7
Non-execution of duty by white-collar crime offenders	5	4	3	3	2	5	5	5	5	5	4.2
Insufficient investment in auditing	5	5	5	4	5	5	5	5	5	5	4.9
Lack of a proper process for recruiting employees	5	4	5	5	5	5	5	5	5	5	4.9
Lack of mastery of accounting standards	5	5	5	5	5	4	5	5	5	5	4.9
Lack of regular audit processes	5	2	5	5	4	5	5	5	5	2	4.3
Inability to recognize intentional distortions	4	4	4	5	5	5	5	5	5	5	4.7
Lack of separation between ownership and management	5	5	4	3	5	5	4	4	4	4	4.3
Organizational complexity	4	3	5	4	5	3	5	5	4	4	4.2
Change in management and senior managers	4	3	5	5	5	4	5	5	5	5	4.6
Lack of a culture of accountability and inquiry	5	5	5	5	4	5	4	5	4	5	4.7
Lack of appropriate financial and accounting reporting systems	5	5	5	5	5	5	5	5	4	5	4.9
Employer's ignorance	5	5	5	5	5	5	5	5	5	5	5.0
Transactions with related parties	5	4	5	3	2	5	4	5	5	5	4.3
Poor job segmentation	5	5	5	4	5	5	5	5	5	5	4.9
Job insecurity	5	5	3	5	5	4	5	3	5	5	4.5
Service history	5	4	5	5	2	5	4	5	5	5	4.5
Managers' disbelief in transparency	5	5	5	4	5	5	5	5	5	5	4.9
Lack of honesty and integrity in executive managers	5	5	5	3	5	5	5	3	5	5	4.6
Management response to actual fraud incidents	5	4	5	5	5	5	4	5	5	5	4.8
Moral weakness in the organization	5	5	5	5	5	4	5	5	5	5	4.9
Management's ability to circumvent controls	5	4	5	4	5	5	5	5	5	5	4.8
Confidence	5	5	5	3	5	5	5	3	4	5	4.5
Innate intelligence	5	5	3	5	5	5	5	5	5	5	4.8
General experience	5	5	3	5	5	5	4	5	5	5	4.7
Specialized experience	5	4	3	3	2	5	4	5	5	5	4.1
Individual's position in the organization	5	5	5	4	5	5	5	5	5	5	4.9
Access to documents and resources	5	5	5	5	5	5	5	5	5	5	5.0
Political connections	5	5	3	5	5	5	5	5	5	5	4.8
Political orientation	5	5	5	5	5	5	4	5	4	5	4.8
Major shareholder (as explained by Faccio (2006), if at least one shareholder owns at least 10% of the total voting shares)	5	4	5	5	5	5	5	5	5	5	4.9
Retirement of provincial authorities	5	5	4	5	3	5	5	5	5	5	4.7
Political stability	5	5	5	4	5	4	5	5	5	3	4.6
Economic policy	5	4	5	5	5	5	5	5	5	5	4.9
Political changes	4	5	5	3	5	5	5	5	5	5	4.7
Government oversight	5	4	5	5	5	5	4	5	5	5	4.8
Corporate governance	5	4	5	3	5	4	5	5	5	-	4.6
Anticipated financial goals	4	5	5	5	5	5	3	5	5	5	4.7
Industry margin decline due to external pressures and political conditions	5	5	5	5	5	5	5	5	5	5	5.0
Active personality traits	5	5	5	5	5	4	5	5	5	5	4.9
Rapid technological changes	5	5	5	4	5	5	5	5	5	5	4.9
Presence of monopolies in suppliers and wholesalers of the industry	5	4	5	5	5	5	5	4	4	5	4.5
Need to increase capital by management	5	4	5	4	3	5	5	5	5	5	4.4
Increased use of estimation bases that are allowed under standards for a specific industry	5	4	3	5	5	4	5	4	5	5	4.5
Non-application of a reasonable basis in calculating management accounting estimates	5	4	5	4	5	5	5	5	5	5	4.8
Necessity for investors to compare the company with similar companies	5	4	5	5	5	5	5	5	4	5	4.8
Lack of proper and timely documentation for transactions	5	4	5	4	4	5	5	5	5	5	4.5
Operational characteristics, liquidity, and financial stability	5	4	4	5	5	4	5	4	5	5	4.6
Pressure from external expectations	5	4	5	4	5	5	5	5	5	5	4.8
Decline of industry customers and industry downturn	5	5	5	5	5	5	5	5	5	5	5.0

In the third round of Delphi, all indicators again scored above 4. As a result, the Delphi process was concluded in the third round.

Finally, the identified factors were categorized in Table 2:

Table 2

Results of Identified Factors from Delphi Technique

Factor	Dimension	Component	Index
Triangle and Diamond	Pressure	Financial Pressures	Threat to stability or financial profitability
			Company's inability to repay debt
			Presence of repeated negative cash flows
			Decrease in demand or increase in bankruptcies
			Personal financial problems
			Threat to personal financial interests of executive managers due to performance ties
		Managerial-Organizational Pressures	Autocratic management style
			Managers' tendency to use inappropriate methods to minimize profits for tax motives
			Desire to conceal poor financial status
			Interest in keeping stock prices high
			Tendency to attract financing from outside at minimal cost
			Tendency to present expected profits
			Tendency to demonstrate competence and enhance professional reputation
			Industry competition
		Legal Pressures	Complex and illogical business transactions
			History of violating laws and regulations
			History of claims against the unit, managers, board members due to fraud and law violations
			Complex laws and regulations
			Presence of corruption opportunities in the country
			Creation of limitations in the work of auditors
			Lack of societal and professional sensitivity to actions of auditors, accountants, and companies
			Insufficient and inadequate time budget for auditing
		Ethical-Behavioral Pressures	Lack of adequate rights and benefits
			Lack of appropriate incentive plans
			Unfair treatment of employees
			Irresponsibility (failure to meet commitments)
			Access to positions
			Relationships among employees
		Greed	
	Opportunity	Auditing and Internal Control	Presence of weak internal control systems
			Ineffective review and monitoring

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			Insufficient investment in auditing
			Lack of regular audit processes
			Lack of appropriate financial and accounting reporting systems
		Knowledge and Awareness	Lack of awareness of laws and regulations
			Lack of access to information
			Lack of mastery of accounting standards
			Employer's ignorance
		Structural	Lack of a proper process for recruiting employees
			Organizational complexity
			Change in management and senior managers
			Poor job segmentation
			Lack of separation between ownership and management
		Execution of Duties	Inability to recognize intentional distortions
			Lack of a culture of accountability and inquiry
			Inability to make quality decisions
			Non-execution of duty by white-collar crime offenders
			Transactions with related parties
	Rationalization	Individual Factors	Job insecurity
			Service history
			Moral weakness in the organization
		Organizational Factors	Managers' disbelief in transparency
			Lack of honesty and integrity in executive managers
			Management's response to actual fraud incidents
			Management's attitude towards fraud risk
	Ability	Individual Characteristics	Confidence
			Innate intelligence
			General experience
		Job Characteristics	Specialized experience
			Access to documents and resources
			Management's ability to circumvent controls
			Individual's position in the organization
Political Factors	Individual		Political orientation
			Major shareholder explains that if at least one shareholder owns at least 10% of the total voting shares)
	Organizational		Political connections
			Retirement of provincial authorities
			Political stability
			Economic policy
			Political changes
			Government oversight

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Figure 1

Final Paradigm Model of Study

4 Discussion and Conclusion

The findings of this research demonstrated that the fraud triangle and diamond significantly impact fraud in financial statements. The fraud triangle and diamond (Fraud Triangle) is an analytical model used to describe the factors that may lead to fraud in financial statements (Serly & Eddy, 2020). This model includes three main factors: pressure, opportunity, and rationalization. It can be explained that:

Individuals in difficult financial situations, such as significant debt, personal financial problems, immediate economic needs, etc., are more likely to commit fraud in financial statements. Pressures may lead an individual to seek illegal or fraudulent solutions to solve their financial problems.

The opportunity to commit fraud in financial statements depends on the access and power an individual has. The presence of weaknesses in systems and internal controls, insufficient supervision, lack of segregation of duties and responsibilities, inadequate performance evaluation, etc., provide ideal opportunities for committing fraud. In other words, if a person can easily commit fraud and exploit it without detection, the opportunity for fraud exists (Moradi et al., 2014). Rationalization is the psychological and psychological meaning that an individual creates for themselves to justify their fraudulent actions. Some rationalizations include feeling unfairness, dissatisfaction with salaries and wages, belief in social needs, or personal motives for obtaining illegal profits, etc. Rationalizations can give a person a greater sense of control and power, making them ready to commit fraud (Arum & Wahyudi, 2021). In line with preventing and reducing the risk of fraud in financial statements, the following suggestions are offered:

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Creating an organizational culture that emphasizes ethics and lawful and ethical behaviors is of great importance. Employees and managers of the organization should be encouraged to avoid behaviors inconsistent with ethical principles and act as proper examples for others.

Reviewing and improving internal controls of the organization can help identify and prevent fraud. Examining systems, processes, and existing methods and making necessary changes to reduce the chances of fraud can be effective.

Providing regular training to employees and managers of the organization on recognizing signs of fraud, its negative effects on the organization, and the importance of adhering to ethical principles can help prevent fraud. Raising awareness about the dangers and legal effects of fraud can also deter employees from engaging in fraudulent actions.

Establishing mechanisms such as hotlines, direct reporting systems, and not transferring important information through hierarchy can empower and encourage employees to report fraud without fear of retaliation or discrimination.

Continuous review and accurate monitoring of the organization's financial and accounting processes and systems, improving internal controls, and identifying any deficiencies or vulnerabilities can prevent fraud.

Another significant finding of this research was the impact of political factors, including individual and organizational, on fraud in financial statements. It can be said that individuals who are in environments with limited access to education and information may have weaker financial and ethical principles and are more prone to commit fraud. Social injustice and inequality in the distribution of wealth and resources can lead individuals to commit fraud in financial statements. Poverty and financial needs may encourage an individual to engage in illegal actions to meet their needs. The presence of corruption in the political system and governmental institutions can be a factor in increasing fraud in financial statements. An individual living in a corrupt environment may seek to exploit conditions and deviate from the laws (Maaloul et al., 2018).

Financial and political regulations in the financial and accounting field can act as a constraint or a driver for fraud. If laws and regulations related to financial stability and transparency in organizations are not properly implemented or fail, this can enhance the spirit of fraud in organizations. Political policies and decisions can have a significant impact on the business environment. If political policies and decisions are improperly designed and cause imbalances in the financial and tax system, the likelihood of financial misconduct in organizations increases. Strong oversight and disclosure activities at the political level can prevent fraud in financial statements. If organizations are continuously monitored and financial misconduct is disclosed, the likelihood of committing fraud decreases (Lim, 2002). Finally, it can be stated that the findings of this research are consistent with the results of prior studies (Liao et al., 2019; Lim, 2002; Serly & Eddy, 2020). In line with the impact of political factors including individual and organizational on fraud in financial statements, the following suggestions are presented:

Educational programs and awareness about financial and ethical principles for individuals at the individual and organizational level should be organized. These programs can include providing financial education, internal control, fraud identification, and its consequences.

Enhancing transparency: Providing transparent and accurate financial and accounting information in organizations and government institutions can prevent fraud. This includes disclosing financial information, conducting independent audits, and ensuring the independence of the audit section.

Intensifying financial laws and penalties: Implementing strict financial laws and enforcing heavy penalties for individuals and organizations that commit fraud can serve as an incentive to comply with financial laws and ethics.

Finally, limitations such as restricted access to some data, difficulties in data collection, improper reporting, and a lack of referable studies can be considered as research limitations in this field.

Authors' Contributions

All authors have contributed significantly to the research process and the development of the manuscript.

Declaration

In order to correct and improve the academic writing of our paper, we have used the language model ChatGPT.

Transparency Statement

Data are available for research purposes upon reasonable request to the corresponding author.

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Declaration of Interest

The authors report no conflict of interest.

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Ethical Considerations

In this research, ethical standards including obtaining informed consent, ensuring privacy and confidentiality were observed.

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