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FORENSIC ACCOUNTING AND THE PROFITABILITY OF COMMERCIAL BANKS IN  
NIGERIA: AN EMPIRICAL INVESTIGATION

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**Abstract**

*This research study investigated the effect of forensic accounting measures of investigative accounting and litigation support services on the profitability of commercial banks in Nigeria. The research which made use of the survey research method and collected data from primary sources with the use of structured questionnaire issued to accounting staff of ten (10) banks. The collected data was analyzed using Pearson correlation and multiple regression analyses. The findings of the study showed that there is positive relationship between the implementation of investigative accounting and litigation support services and the profitability of commercial banks. However, the findings were not statistically significant. Based on the findings of the study, it is concluded that investigative accounting and litigation support services have very little effect on the financial performance of commercial banks in Nigeria in terms of their profitability. It is thus recommended that commercial banks must continually improve on and implement investigative accounting practices that have the potential to enhance financial performance. It is also recommended that they study and garner in-depth knowledge of their forensic accounting methods in order to isolate and improve on the methods that enhance financial value the most. It is further recommended that commercial banks review their investigative accounting methods in order to establish why it is performing below expectation.*

**Introduction**

Globally, there has been an upsurge in fraudulent accounting practices in business organizations and Nigeria is not left out in the scourge. Reports of perpetration fraud more especially in the banking other non-bank financial institutions has become common and constitutes a problem that continually erodes the confidence of both investors and depositors alike in addition to having a severe negative effect on the finances of the concerned organizations.

Odelabu (2014) agree with this position stating that banking fraud is a major problem to various stakeholders of banks in Nigeria. According to him, fraud it diminishes the profitability

Of a bank which has the potential to lead to a reduction in firm value as a result of reduced bottom-line for to shareholders to partake in. In some extreme case, fraud it may threaten the going concern status of the concerned bank which of course impact negatively on shareholder wealth. Depositors are not left out as the fallout of fraudulent activities as this has been shown to lead to bank runs as a result of loss of confidence in the institution. Ultimately fraud especially in banks also has a negative effect on the wider economy as investors may become too wary to the detriment of the financial system.

These negative effects of bank fraud have led to a demand for action especially by investors and depositors who are always the first to be affected by such issues. Thus, regulators has over time introduced corporate governance practices for banks aimed at stemming the tide of financial malfeasance and widening the role and visibility of forensic accountants has been one of the outcomes. Forensic accountants according to Huber (2012), forensic accounting and fraud research has grown over the past two decades and one of the several factors that led to the growth in forensic accounting was the collapse of large US based companies such as Enron and WorldCom that engaged in fraudulent accounting-based corporate governance practices.

Forensic accounting according to Moduga and Anyaduba (2013) encapsulates all investigation related areas in uncovering financial fraud as performed by specially trained accountants with the necessary skill set. New developments in financial fraud (especially in upsurge and sophistication) requires that forensic accounting be added to the tools necessary for the investigation and uncovering of those individuals involved in criminal activities. Forensic accounting utilizes accounting, auditing, and investigative skill sets in order to conduct examination into a business organization's financial reports. They provide an accounting analysis and insight suitable for litigation.

An effective forensic accounting team should not only uncover fraud that has already been perpetrated but also help to reduce the future occurrence of fraud by putting in place preventive measures that will help in recognizing characteristics of fraud-in-progress that can be flagged. This research paper is intended to investigate the effect of forensic accounting practices in the prevention of fraud on the financial performance of commercial banks in Nigeria.

### **Statement of the Problem**

The increasing rate of fraud in the banking system has become a source of worry for all stakeholders in the industry and if not stemmed will have serious consequences for the stability and survival of individual banks and the performance of the industry as a whole (Nwankwo, 2013). Fraud has left untold hardship on the lives of bank investors, depositors and all other category of stakeholders as most bank failures are always associated with large scale of internal fraud. Fraud in bank shakes the foundation and credibility of the affected banks in Nigeria resulting in some of the banks being distressed thus impacting negatively on the nation economy (Ojo, 2008). Considering that banks play a vital role in determining and influencing the course of economic development of the country, it becomes pertinent that financial malfeasance be checked.

Over time, several mechanisms have been utilized by business organizations as methods of checking fraud. One of such mechanisms which in the recent past has gained prominence is forensic accounting. Cole (2009) stated that a forensic accountant is required to have special skills for inspecting documents for authentication, uncover alteration, forgery and counterfeiting. By possessing these skills, the forensic accountant can in the process of carrying out his duties can easily detect errors, fraudulent activities and omissions and thus prevent or reduce fraudulent practices.

However, many authors have expressed the view that in the face of the increased prominence of forensic accounting, fraudulent practices especially by individuals within the organization seem to be on the increase. For example, the last decade has witnessed an upsurge in large scale fraud that has led to the failure of some banking organizations that were previously thought to be financial healthy like Oceanic Bank, Intercontinental Bank, Northern Rock etc. Thus, this paper is aimed at investigating the effect of forensic accounting on the financial performance of banks in Nigeria. Previous research on the subject area has been mostly focused on the relationship between forensic accounting and the quality of financial reporting. This obvious gap in research motivated this research endeavor.

### **Research Objectives**

The major aim of this research paper is to investigate the effect of forensic accounting on the financial performance of commercial banks in Nigeria. Specifically, it will undertake to:

- Determine the nature of the relationship between investigative accounting and the profitability of commercial banks in Nigeria.
- Determine the nature of the relationship between litigation support services and the profitability of commercial banks in Nigeria.

### **Research Questions**

- What is the nature of the relationship between investigative accounting and the profitability of commercial banks in Nigeria?
- What is the nature of the relationship between litigation support services and the profitability of commercial banks in Nigeria?

### **Research Hypotheses**

Ho<sub>1</sub>: There is no significant relationship between investigative accounting and the profitability of commercial banks in Nigeria.

Ho<sub>2</sub>: There is no significant relationship between litigation support services and the profitability of commercial banks in Nigeria.

### **Legitimacy Theory**

The Legitimacy Theory is based on a generalized assumption that the activities of an entity are desirable, proper or appropriate with a socially constituted system of norms and values (Such man, 1995). The legitimacy theory offers an important mechanism for gaining an understanding of voluntary social and environmental issues made by business organizations. This understanding would provide an avenue for engaging in important public debate on relevant auditing related issues (Tilling, 2008). The problem for legitimacy theory in contributing to the understanding of issues relating to accounting disclosures and best practices specifically those that may threaten the ability of the firm to continue to be perceived as operating legitimately.

Consequently, legitimacy theory proposes that a business organization may be in one of four phases in regard of its legitimacy. The first phase is the phase of establishing legitimacy which is the early stages of a firm's development which tends to revolve around issues of competence, especially financial competence. But also, the organization must be aware of socially constructed standards of quality and desirability in addition to performing in accordance with accepted standards of professionalism (Hearit, 1995).

The second phase involves attaining and maintaining legitimacy which is the phase that most firms would generally expect to be operating in and where their activities include: ongoing role performance and assurance, that everything is happening as expected and that attempts to anticipate and prevent or forestall all potential changes to legitimacy are in place (Tilling, 2008).

However, maintaining legitimacy is not as easy as it may seem at first. Legitimacy is a dynamic construct because stakeholders' expectations are not considered static but change over time thereby requiring organizations to be responsive and proactive to the firm's environment in which they operate. An organization could accept this view; lose its legitimacy even if it is deemed to be legitimate due to the dynamics of an ever changing social setting (Deegan, Rankin and Tobin, 2002).

The third phase which involves extending legitimacy is the point where an organization enters new markets or changes the way it relates to its current market and environment. This can give rise to a need to extend legitimacy which tends to be intense and proactive as management of the organization attempts to win the confidence and support of wary potential constituents (Ashford and Gibbs, 1990). The final stage involves the organization defending its legitimacy and occurs when legitimacy is under threat as a result of an incident or competitor (internal or external) and therefore requires defense. Legitimizing activities tend to be intense and reactive as management attempts to counter the threat ((Deegan, Rankin and Tobin, 2002). Even barring a major incident, it is likely in an openly competitive (capitalist) system that most business organizations will regularly need to defend its legitimacy. But the fact that business firms must fulfill both a competence and stakeholder concerns while responsibility to the larger community often occurs at the expense of the stockholders (Hearit, 1995).

It is this last phase that tends to be the main focus of accounting researchers. It also provides us with a clear opportunity to examine the crucial links between legitimacy and resources Lindblom (1994). Fraud and other maleficent behaviors could mar the firm's legitimacy especially if the sources of such fraud are internal to the firm. Thus, Forensic accounting will be very critical for the firm to maintain its legitimacy as well as defend it when it comes under threat from fraud.

### **Concept of Forensic Accounting**

Forensic accounting is the integration of financial accounting and auditing knowledge with investigative skills that are gained from years of practical experience. It is an avenue for forensic accountants conduct critical review of instructions of clients usually through a solicitor and thoroughly investigate these instructions and the underlying circumstances giving rise to them as well as investigate the financial information and any relevant agreements and other agreements, obtain necessary evidence and furnish such information to the client for possible litigation.

Harris and Brown (2000) restated the specific desirable qualities of forensic accountants that they should possess as experts of their nature. They pointed out that a forensic accountant should be conversant with both criminal and civil law. They further stressed the need for understanding of court room procedures, litigation skills, investigative skills as well as creative thinking and communication skills. The skills of forensic accountants arise from experience in financial accounting, internal controls systems, auditing and taxation.

According to Golden, Skalak and Clayton (2011) in Bhasin (2016), forensic accounting consists of two main components viz: investigative accounting services which use a forensic accountant's skill set and may require possible litigation testimony and litigation support services which recognize the role of an accountant as an expert consultant in the investigation of fraud. Thus, the forensic accountant should be well versed financial accounting as well as internal control systems, the legal system while other requirements include investigative proficiency and communication skills. Business organizations can rely on these skills in order to develop consistent system of corporate governance, disseminate such information within and outside the organization in order to ensure that the finances of the organization are safe from fraud (Bhasin, 2016).

Forensic accountants can play a vital role in coordinating the organization's efforts to achieve acceptable ethical behavior within an organization. They are expected to be experts in accounting and the general workings of the financial systems. As companies continue to grow in size and complexity, detecting and preventing fraud requires Forensic accountants to become more proficient in new areas and competencies that may come into play in financial accounting practice (Bhasin, 2011).

Ramaswamy (2005) listed some of the major areas of useful expertise<sup>19</sup> for forensic accountants to include: In-depth knowledge of financial statements and ability to critically analyze them; ability to understand the internal control systems of organizations and be able to initiate a control system that comprehensively assesses risks, achieves management objectives, inform employees of their control systems responsibilities, and monitor the quality of the program so that corrective procedures and changes can be made without throwing the system into chaos; Proficiency in computer and knowledge of network systems. Knowledge of psychology in order to understand the impulses behind criminal behavior and to set up fraud prevention programs that motivate and encourage employees; Interpersonal and communication skills, which will assist in the dissemination of information about the organization's ethical policies; Thorough knowledge of the organization's corporate governance policies and the laws that regulate these policies; Finally, the forensic accountant should knowledgeable in crime law and the litigation procedure of the country.

### **Firm Performance**

Measuring financial performance as aligned with corporate governance has gained critical importance in corporate finance literature. This is because companies are not only providing the mechanism of investment but also helps to channel the funds in an appropriate way to support the business activities in the business environment (Franklin, 2001). Financial performance has the potential to provide organizations with many important benefits, including greater efficiencies and economies of scale, increased power, greater ability to withstand economic and market fluctuations, an increased ability to survive, greater profitability and prestige for organizational members.

There are many parameters that organizations may use to measure or analyze its performance. Since the ultimate goal of most companies is profitability, most firms will measure their performance in terms of net-profit, revenue, and other financial data. Other businesses may use one of the following criteria for assessing their growth: sales, number of employees, physical expansion, success of a product line, or increased market share (Business-School, 2012). In addition to the qualitative notions of organizational performance, there are many more tangible measurement parameters an organization may select to measure its performance. The most meaningful measure is one that shows progress in respect of its stated objectives.

For many companies, especially banks, the real measure of firm growth is the creation of wealth for owners/investors. While the bottom line is an indicator of wealth creation, corporate organizations may analyze their finances further to determine if they are in reality generating an economic profit or a profit that exceeds the implicit cost of the capital invested in the firm. The company may be said to create new wealth after the cost of capital has been met.

### **Empirical Review**

Odelabu (2014) investigated the effects of forensic accounting on the performance of commercial bank in Nigeria. The study which was conducted through explanatory research design requiring the analyses of how a set of independent variables affects the dependent variables. The findings of the study indicated that forensic investigation and forensic litigation was statistically significant in explaining changes in financial performance of commercial banks.

The findings of this study were crucial in the formulating study conclusions. However, the study also took into account the expectations of the study. The study findings further showed that forensic investigation and forensic litigation were statistically significant in explaining changes in financial performance of commercial banks in Nigeria.

Ezeagba (2014) examined the effectiveness of Forensic Accounting in enhancing qualitative financial reporting in Nigeria using the commercial banking sector as a reference point. The study which adopted survey and descriptive approaches as its research design also utilized secondary data for the study which were sourced from the annual reports of the chosen commercial banks. The findings of the study reveal among others that the fundamental qualitative characteristics (relevance and faithful representation) of financial reporting, accounting and the enhancing qualitative characteristics (understandability) can be significantly enhanced through forensic accounting.

In another study, Kasum (2008) researched on "The relevance of Forensic Accounting to Financial Crime in Private and Public sector of Third world economies. The researcher adopted the empirical survey cum exploratory approach. Questionnaires were distributed to diverse class of professionals comprising accountants, lawyers, economists and bankers. Analysis were done using Z-Score test of mean computed for the first three hypotheses and Z-Score test of proportion was computed for the last hypothesis. The study reveals that there is an alarming rate of corruption among the third world countries and that it is not only crumbling the economy but also affecting innocent national's standard of living and image. The study further reveals that the services of the experts (forensic accountants) are more required in developing economies and more especially in the public sector than developed economies.

Enofe, Olorunnuho and Okporua (2016) investigated the effect of forensic accounting on fraudulent financial reporting in Nigeria banks. The study which sampled about 150 professional accountants and employees of banks designed a model to measure the relationship between the role of forensic accounting in fraud prevention, relevance of the audited financial statement and true and fair view of the audited financial statement, using multiple regression analyses. The results show that all the variables but relevance of financial statement exhibit positive relationship with forensic accounting in the Nigerian Banks.

Enofe, Toluwa, Fasua and Ajayi (2016) examined the efficiency and effectiveness of forensic accounting in improving qualitative characteristic of financial reporting in Nigeria using the private sector as a case. Specifically, the study researches on relationship between forensic accounting and financial reporting quality. The methodology employed was a survey and descriptive approach while Pearson Correlation method was used to analyze the collected data. The findings indicate that the main qualitative features (relevance and faithful representation as well as understandability) of financial statements can be significantly improved by forensic accounting.

### **Methodology**

This research paper adopted the survey research design method and data for this research paper is collected from primary sources though the issue of structured questionnaires to the accounting and audit staff of ten commercial banks in Nigeria. These are: First Bank PLC, Guaranty Trust Bank, United Bank for Africa, Eco bank PLC, Access Bank PLC, Fidelity Bank, Diamond Bank PLC, First City Monument Bank, Union Bank, Zenith Bank PLC. Data for the study will be analyzed using Pearson correlation and multiple regression analyses. For the purpose of the research, it is hypothesized that forensic accounting (litigation support services and investigative accounting) have a significant effect on the financial performance (profitability) of commercial banks in Nigeria.

**Profitability = f (investigative accounting, litigation support services) . . . . . 1**

Where investigative accounting is denoted as INVACT, litigation support services is denoted as LTGSVC and profitability is denoted as PROFIT, equation 1 is restated as:

$$PROFIT = B_0 + B_1INVACT + B_2LTGSVC = U . . . . . 2$$

Where:

PROFIT = Profitability

INVACT= Investigative accounting

LTGSVC= Litigation Support Services

**The a priori expectation is that  $B_1$ , and  $B_2 > 0$**

**Data Analyses and Interpretation**

Table 1 below shows the descriptive statistics table for profitability, Investigative Accounting and Litigation Support Services. The table shows that of the 60 questionnaires which we distributed, forty seven (47) were used for the study. This represents the number that was duly completed and returned to the researcher. The further indicate that the mean for Profitability, Investigative Accounting and Litigation Support Services were 0.7695, 0.7418 and 0.7376 respectively while the standard deviation was 0.1014, 0.103 and 0.1172 respectively.

**Table 1: Descriptive Statistics for Profitability, Investigative Accounting and Litigation Support Services**

	Mean	Std. Deviation	N
PROFIT	.76950000	.101398013	47
INVACT	.74184043	.102966243	47
LTGSVC	.7375872	.11725633	47

Table 2 shows the correlation results for the study. From the table, it can be observed that the correlation between profitability and investigative accounting and litigation support services were 0.492 and 0.353 respectively. This result implies that the strength of the relationship between the profitability and investigative accounting and litigation support services 49.2% and 35.3% respectively. Thus, increased implementation of forensic accounting practices is predicted to lead to increase in the profitability of commercial banks in Nigeria.

**Table 2: Correlations matrix for Profitability, Investigative Accounting and Litigation Support Services**

		PROFIT	INVACT	LTGSVC
Pearson Correlation	PROFIT	1.000	.492	.353
	INVACT	.492	1.000	.307
	LTGSVC	.353	.307	1.000
Sig. (1-tailed)	PROFIT	.	.098	.072
	INVACT	.098	.	.068
	LTGSVC	.072	.068	.
N	PROFIT	47	47	47
	INVACT	47	47	47
	LTGSVC	47	47	47

Table 3 shows that the coefficient of correlation (R) for Profitability, Investigative Accounting and Litigation Support Services gave a value of 0.416 with the implication that taken as a unit; the measures of forensic accounting have a strong relationship of about 41.6% with

**LEYIRA C. MICAH, PhD. AND YOUNG ACHESEOMIE SUNNY-JOE**  
**FORENSIC ACCOUNTING AND THE PROFITABILITY OF COMMERCIAL BANKS IN.....**

the profitability of commercial banks in Nigeria. Furthermore, the coefficient of determination (R<sup>2</sup>) gave a value of 0.387 with the implication that investigative accounting and litigation support services taken a unit can explain only about 38.7% of the variations in the profitability of commercial banks in Nigeria.

**Table 3: Model Summary for Profitability, Investigative Accounting and Litigation Support Services**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.416 <sup>a</sup>	.387	.303	.101227558

a. Predictors: (Constant), LTGSVC, INVACT

Table 4 shows the regression results for the relationship between Profitability, Investigative Accounting and Litigation Support Services. From the results, it can be observed that the coefficients of regression (B) gave values of 0.858 and 0.906 respectively for investigative accounting and litigation support services. These results indicates that one unit increase in investigative accounting and litigation support services will lead to a 0.858 and 0.906 units increase in profitability of commercial banks in Nigeria.

**Table 4: Coefficients of Regression for Profitability, Investigative Accounting and Litigation Support Services**

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.586	.126		4.653	.000
	INVACT	.858	.152	.160	1.834	.087
	LTGSVC	.906	.134	.104	1.674	.074

a. Dependent Variable: PROFIT

Table 4 further shows that the T-statistic gave values of 1.834 and 1.674 respectively for investigative accounting (INVACT) and litigation support services (LTGSVC) while the critical T-statistic is 1.960. Furthermore, the probability of the T-statistic gave values of 0.87 and 0.074 with a critical T-probability statistic of 0.05. These results indicate that the relationship between commercial banks' profitability and the implementation of the forensic accounting measures of investigative accounting and litigation support services is not statistically significant. Thus, both null hypotheses are not rejected leading to the conclusion that forensic accounting measures of investigative accounting and litigation support services do not significantly affect the profitability of commercial banks in Nigeria.

### Discussion of Findings

This research paper investigated the effect of forensic accounting measures of investigative accounting and litigation support services on the profitability of commercial banks in Nigeria. The findings of the research paper indicate that there is a positive relationship between investigative accounting and the profitability of commercial banks in Nigeria. With a coefficient of regression of 0.858 for the relationship between investigative accounting and the profitability of commercial banks implying that a unit increase in the implementation of investigative accounting will lead to a 0.858 units increase in the profitability of commercial banks in Nigeria. However, this finding is not statistically significant given that the computed T-statistic of 1.834 is less than the critical T-static of 1.960. Ezeagba (2014) examined the



effectiveness of Forensic Accounting in enhancing qualitative financial reporting in Nigerian commercial banks showed that the fundamental qualitative characteristics (relevance and faithful representation) of financial reporting, accounting and the enhancing qualitative characteristics (understandability) can be significantly enhanced through forensic accounting.

Furthermore, the findings show that there is positive relationship between litigation support services and the profitability of commercial banks in Nigeria. With a coefficient of regression of 0.906 for the relationship between litigation support services and the profitability of commercial banks in Nigeria. This result indicates that a unit increase in the implementation of litigation support services by commercial banks will lead to a 0.906 units increase in the profitability of commercial banks. Again, like in the case of investigative accounting above, the result was not statistically significant as the computed T-statistic of 1.674 was less than the critical T-statistic 1.960. However, in a similar study, Odelabu (2014) showed through an explanatory research design requiring that forensic investigation and forensic litigation was statistically significant in explaining changes in financial performance of commercial banks. The difference in findings is most likely as a result of the differences in the research methods.

### **Conclusions and Recommendations**

Based on the findings of the study, it is concluded that investigative accounting and litigation support services have very little effect on the financial performance of commercial banks in Nigeria in terms of their profitability. This is likely as a result of the fact that fraud is under-reported in the Nigerian commercial banking sector as well as the fact that the services of forensic accountants are not optimally utilized in the industry. Consequently, forensic accounting practices are not an important determinant in the profitability of commercial banks in Nigeria.

From the finding of the study, it has been shown that the application of forensic accounting methods such as investigative accounting do not enhance the financial performance of commercial banks. Thus, on the basis of the findings and conclusions above, the following recommendations are made: Commercial banks must continually improve on and implement investigative accounting practices that have the potential to enhance financial performance. To this end, it is recommended that they study and garner in-depth knowledge of their forensic accounting methods in order to isolate and improve on the methods that enhance financial value the most. Furthermore, such studies should try to underscore the reasons why some of the methods being applied are not yield the desired results and how to remedy the situation.

It is further recommended that commercial banks review their investigative accounting methods in order to establish why it is performing below expectation. We note here that the failure of the method is likely as a result of deficiencies in the depth of knowledge/expertise of their audit staff. In which case it is in their best interest to adequately train and retrain their staff in the best practices in the industry. It is also recommended that close collaboration with relevant institutions and policy making bodies such as Institute of Chartered Accountants of Nigeria (ICAN), Securities and Exchange Commission (SEC), Federal Inland Revenue Services (FIRS) etc. make proposals for strengthening existing laws on auditing processes and policies in order to ensure that the banking industry is better prepared to take on challenges in the industry.

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**LEYIRA C. MICAH, PhD. AND YOUNG ACHESEOMIE SUNNY-JOE**  
**FORENSIC ACCOUNTING AND THE PROFITABILITY OF COMMERCIAL BANKS IN.....**

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**Appendix: Forensic Accounting and Commercial Banks' Profitability Questionnaire**

S/N	ITEMS	SA	AG	UN	DA	SD
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<b>A</b>	<b>INVESTIGATIVE ACCOUNTING</b>					
1	The bank have financial forensic investigators in its payroll					
2	Where fraud is reported, especially at managerial level, the bank forensic accountants are involved in the investigation					
3	Investigative accountants are involved in all categories of fraud in the bank					
4	The misuse of non-financial resources are also investigated by investigative accountants where loss is substantial					
5	Proposals made by the bank's investigative accountants in the course of their job are duly implemented					
6	Fraudulent activities uncovered in the course of their jobs are properly investigated and where necessary litigation processes started					
<b>B</b>	<b>LITIGATION SUPPORT SERVICES</b>					
7	The bank has a well-staffed and funded litigation support unit within the accounting and legal departments					
8	The bank utilize the services of litigation consultant in prosecuting fraud cases					
9	The bank's forensic accountants are routinely involved in reviewing the opposing expert's reports on fraud cases the bank is involved in					
10	The bank incur substantial litigation costs in the course of fraud litigations involving the bank					
11	The bank's forensic accountants routinely function as experts witnesses in the fraud cases involving the bank					
12	The forensic accountants in the bank have been involved in Assisting in securing documentation necessary to support litigation processes					
<b>C</b>	<b>PROFITABILITY</b>					
13	The bank'S performance in terms of profitability has improved as a result of it forensic accounting activities					
14	Investors are impressed with the bank's handling of fraud related problems					
15	Reported case of fraud has reduced considerably as a result of the bank's forensic accounting cases					
16	Depositors' confidence has been on the rise due to the effective handling of their reported fraud cases					
17	The bank's profitability has surpassed industry average in the past three years					