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FRAUD AND ITS EFFECT ON BANKING INDUSTRY: A STUDY OF SELECTED BANKS IN NIGERIA

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ABSTRACT

This research work investigates Fraud and its effect in the banking industry: A study of selected banks in Nigeria. The main objective of this study is to determine the effects of Fraud and financial crimes on the Nigerian banking industry. Three research questions and three research hypotheses were raised. A sample size of 80 was utilized for the study. Primary data gotten from a well-structured research questionnaire was used for the study. The data were analyzed using frequencies, percentages, weighted mean, and z-test. The analysis was conducted based on the objectives of the study, which include; To determine the effects of fraud and financial crimes on the profitability of the Nigerian banking industry and examining the effects of fraud and financial crimes on the bank customers' confidence in the Nigerian banking industry. From the analysis it was established that; Fraud and financial crimes have a significant effect on the profitability of Nigerian banking industry. Fraud and financial crimes negatively affect the confidence of bank customers in the Nigerian banking industry. The study recommends amongst others that Nigerian Banks must follow a global pattern by identifying and reporting transactions of a suspicious nature to the financial intelligence unit in the respective country.

Keywords: fraud, stability, crime, profitability.

1.0 INTRODUCTION

Economic and financial crimes in whatever form and nature have potentially devastating impacts on the economy, security, and social wellbeing of the people. It is perhaps pertinent to stress that as modern financial system encourages and facilitates local and international commerce, antithetically, financial criminals are also enabled by modern financial global liberalization to transfer millions of dollars around the world instantly through available information communication infrastructures such as the internet, electronic money transfer (wire transfer) and the rest.

Money laundering among other forms of economic and financial crime requires an existing financial system and operation. Money is laundered in Nigeria through currency exchange houses, stock brokerage houses, casinos, automobile dealerships, and trading companies.

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These institutions are capable of masking proceeds from illegal criminal activities. The overall effects of these activities on the socio-political lives and economic wellbeing of the people of the developing countries and Nigeria, in particular, could be well imagined (Ribadu, 2004).

In the developed economies of the West, evidence emerged (which was at first difficult to believe) that the criminal manipulation of Company balance sheets created a much more favorable picture of their finances than was the reality. The Enron Company which unexpectedly went bust is probably the best-known example of accounting book manipulation in our time. Here in Nigeria, the Lagos state government funds are trapped while there was also a crisis in the US in the management of mortgages that were inflated. It was a boom and investors.

1.1 Statement of the Problem

Banks generally have been experiencing fraud since its evolution. This affects the performance and the profitability of banks and may possibly lead to distress. The inability to identify Fraud is a major challenge to the entire banking industry; no bank is immune to it in all facets of life (Olorunsegun, 2010). The banking public expects accountability, fairness, and transparency in their daily operation for effective intermediation.

Though there were known cases of fraud in the sector, one major question still remains unanswered which is what is the nature and different ways through which fraud can be perpetuated in banks. It is asserted by Adeyemo (2012) that fraud in the bank is possible with the corroboration of an insider. The banks are expected to ensure that they carry out their responsibilities with sincerity of purpose which is devoid of fraudulent practices. This is relevant if the banking sector is to gain public trust and goodwill.

The government and its agencies have not put enough effort in the prevention and control of bank fraud in Nigeria; otherwise, the level of bank fraud would have reduced to a bearable level. Agencies like the Economic and Financial Crimes Commission (EFCC) which helps to place surveillance on any account through which such excess cash deposits or withdrawals are made, Independent and Corrupt Practices Commission (ICPC) which is involved in managing financial crimes.

In view of the above development, this research work seeks to investigate the effects of fraud in the Nigerian banking industry.

1.2 Objectives of the Study

1. Determine the effects of fraud and financial crimes on the profitability of Nigerian banking industry
2. Examine the effects of fraud and financial crimes on the bank customers confidence in the Nigerian banking industry

1.3 Hypotheses

H01: Fraud and financial crimes have no significant effect on the profitability of Nigerian banking industry

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H02: There is no significant negative relationship between fraud, financial crimes, and the confidence of bank customers in the Nigerian financial industry

2.0 MATERIAL AND METHODS

2.1 The Concept and Extent of Economic and Financial Crime

The term "economic and financial crime" refers broadly to any non-violent crime those results in a financial loss. These crimes thus comprise a broad range of illegal activities, including fraud, tax evasion and money laundering. The category of "economic crime" is hard to define and its exact conceptualization remains a challenge. The task has been further complicated by rapid advances in technology, which provide new opportunities for such crimes (UN Office on Drug and Crime, 2005).

Financial crimes are crimes against property, involving the unlawful conversion of the ownership of property (belonging to one person) to one's own personal use and benefit. Financial crimes may involve fraud (cheque fraud, fraud, mortgage, medical fraud, corporate fraud, securities fraud (including insider trading), bank fraud, market manipulation, payment (point of sale) fraud, health care fraud); theft; scams or confidence tricks; tax evasion; bribery; embezzlement; identity theft; money laundering; and forgery and counterfeiting, including the production of Counterfeit money and consumer goods.

2.2 Types of Financial Crimes

White-collar crimes are nonviolent crimes committed in commercial situations by individuals, groups, or corporations for financial gain. They include but are not limited to the following types of fraud (Lawshop, 2015):

Antitrust fraud includes the use of practices such as price-fixing and monopolies to stifle competition.

Bankruptcy fraud is committed by businesses or individuals who conceal assets, mislead creditors, falsely claim bankruptcy, file multiple bankruptcy claims, or launch petition mills.

Bribery is a crime in which money, a favor, or something else of value is promised to, given to, or taken from an individual or corporation in an attempt to sway his or its views, opinions, or decisions.

Computer fraud involves the use of a computer to engage in illegal activity.

Credit card fraud refers to the unauthorized use of a credit card to make purchases.

Counterfeiting is the act of manufacturing fake currency or altering genuine currency.

Embezzlement occurs when one who has been entrusted with funds steals them for his own benefit.

Environmental fraud is the illegal release of potentially harmful pollutants into the air, water, or soil.

Government fraud is any fraud committed against the U.S. Government or one of its contractors, including public housing, educational programs, and agricultural programs.

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Identity fraud refers to the theft of one's personal information so as to use it for opening credit card accounts, applying for loans, purchasing cellular phones, or committing serious crimes.

Insider trading occurs when someone who has confidential information uses it to reap profits or avoid losses on the stock market.

Insurance fraud is the filing of artificial or exaggerated claims to an insurance company.

Mail fraud involves the use of the U.S. Postal Service or another registered mail service to commit a crime.

Securities fraud, or investment fraud, is the intentional deception of investors that financially benefits the perpetrator. Numerous tactics of manipulation and misrepresentation can constitute securities fraud.

Trade secret fraud is the theft of a confidential plan, formula, idea, or collection of information that could benefit a business.

2.1.2 Money Laundering and Fraud

Money laundering is the integration of illicit funds into the mainstream of legitimate finance in order to conceal the criminal sources and nature of such funds and ultimately make the funds look clean. It is the smuggling of funds with criminal intention into the channel of the legitimate financial system.

Black (1979) defines fraud as all multifarious means that human ingenuity can devise, and which are resorted to by one individual to get an advantage over another by false suggestions or suppression of the truth. It includes all surprises, tricks, cunning or dissembling, and any unfair way in which another is cheated. Under common law, three elements are required to prove fraud; a material false statement made with intent to deceive (scanter), a victim's reliance on the statement, and damages.

The criminal code section 380 sub-section one stated that everyone who, by deceit, falsehood, or other fraudulent means, whether or not it is a false pretense with the meaning of this Act, defrauds the public or any person, whether ascertained or not, of any property, money or valuable security, or any service.

Edelherz (1977) defines fraud as an illegal act or series of illegal acts committed by nonphysical means and by concealment or guide to obtaining money or property, to avoid the payment or loss of money or property, or to obtain business or personal advantage. Also, Webster's collegiate dictionary of current English defines fraud as deceit, trickery, specifically; intentional pervasion of truth in order to induce another to part with something of value or to surrender a legal right. Fraud is a feature of every organized culture in the world.

The interaction process theory of deviant behavior or trust violation involves a non-shareable financial problem; knowledge of how to violate; and rationalizations about the violations. Non-sharable financial problems include business failure through an unsuccessful gamble or speculation and important socio obligations such as emergency expenditure which involve the person's social status. Those who violate trust believe that they can resolve these

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problems secretly by violating their positions of trust, and they are confident that they have the knowledge of the technique to do so. They rationalize their behavior, not as a trust violation but they were "only borrowing" and hope to pay back but something then happens which makes it impossible for them to refund what they were only borrowing. Trust violations are usually put in the position they violate precisely and they were regarded as trustworthy with other people's money or property.

Table 2.1 Cross-border illicit financial flows

Global Flows	Low (US$ M)	%	High (US$ M)	%
Drugs	120	11%	200	12.5%
Counterfeit goods	80	7.5%	120	7.5%
Counterfeit currency	3	0.2%	3	0.2%
Human trafficking	12	1.1%	15	0.9%
Illegal arms trade	6	2.0%	10	0.6%
Smuggling	60	5.6%	100	6.3%
Racketeering	50	4.7%	100	6.3%
Crime subtotal	331	3 1 .2%	549	34.3%
Mispricmg	200	18.9%	250	15.6%
ABUSIVE transfer pricing	300	28.3%	50	31.2%
Fake transactions	200	23.9%	250	15.6%
Commercial subtotal	80	66.0%	1,000	62.5%
Corruption	30	2.8%	50	5.1%
Grand Total	1,472%	203.2%	2,697	198.6%

Source: Capitalism's Achilles Heel, Baker 2019. Based on a review of studies of transnational crime

Van (2003) and his coworkers' work is in general very critical and ask the question about the state of our present knowledge about organized crime and/or money laundering, which can be dealt with in a very simple manner: There is no hard or proven knowledge of the size and development of money laundering or organized crime. Neither the FATF (Financial Action Task Force), the US administration nor the FIU (Financial Intelligence Unit) has invested in converting the image of speculation into approaching scientific insight into the phenomenon of money laundering and organized crime (Van, 2003). Van argues that every member state portrays the laundering and organized crime phenomenon as a global means, but none has thought of a multi-country integrated strategic information management system (Van and Demiranda (2002).

3.0 METHODOLOGY

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3.1 Research Design

The research method is the general research strategy that outlines the way in which a research project is to be undertaken and among other things identifies the methods to be used in it. The method comprises the research design, area of the study, population, sample and sampling technique, instrument for data collection, and as well as procedure for data analysis.

3.2 Sources of Data

Primary Sources of Data

Primary data was obtained from the targeted respondents through a carefully constructed questionnaire. The questionnaire was designed to capture the demographic data of the respondents and their opinions with respect to the research questions. The questionnaire was divided into two (2) sections: Section A: personal bio-data and Section B: questions on the effects of commercial bank nonperforming loans on bank performance

Secondary Sources of Data

The secondary sources from which data were collected include textbooks several materials in Nnamdi Azikiwe University, Awka, library, and journals from the internet.

3.3 Population of the Study

The population of the study was composed of staff of Nigerian commercial banks in Awka South Local Government Area of Anambra State. The entire staffs of the 3 branches of First Bank PLC and 3 branches of UBA PLC, two (2) branches of Enterprise Bank Plc, and two (2) branches of diamond banks constitute the population of the study.

3.4 Sampling size and Sample Techniques

The researcher employed a convenient random sampling technique in picking 100 staff for this study. Thus, 10 staff were picked from each of the three (3) branches of UBA PLC, three (3) branches of First Bank PLC, two (2) branches of Enterprise Bank, and two (2) branches of Diamond Bank Pic making it a population of 100.

The sample size is a proportion of individuals drawn from a population. Determining the sample size from the population, the researcher will make use of the Taro Yamani's 1964 formula. The formula is;

$$n = \frac{N}{1+N(e)2}$$

Where;

n = Sample size.

N = Population,

e = Tolerable error.

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1 = Constant.

Taking into consideration of the following;

n =?

N=100

e =0.05

By

Substituting the formula;

$$n = \frac{100}{1 + 100(0.0025)}$$

$$n = \frac{100}{1.25}$$

$$n = 80 \text{ (sample size)}$$

3.5 Method of Data Collection

The method of data collection used by the researcher on this topic is the questionnaire administered. Questionnaires are used when factual information is needed; it is a list of questions given to individuals to fill by answering stipulated and structured questions as honestly as possible. The questionnaires used for this research work have multiple opinions for the questions, where respondents were provided with opinions of answers to choose from within a range of how they feel based on the questions presented.

This form of research plan was chosen in order to ease the work of the researcher in the area of classifying and analyzing individuals (respondents') opinions. The questionnaires were distributed to the staff of UBA and First Bank Plc, Enterprise Banks Plc, and Diamond Bank Plc within Awka metropolis, which had enough knowledge about the subject, and the questionnaires were collected back afterward.

The questionnaire was divided into two different sections section A contains questions on the demographic characteristics of the respondents. It bears age, educational qualification as well as length of service. While the second part bears questions bordering on the objectives of the study.

3.6 Decision Rule

The decision rule for accepting the null hypothesis will be if Z-calculated < Z-critical two-tail value at 5%.

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The decision rule for rejecting the null hypothesis will be if Z-calculated> Z-critical two-tails value at 5%.

3.7 Data Presentation and Analysis

This chapter presents the statistical analysis and interpretations of the data collected from the respondents for the study on the topic of banking reforms as a tool for economic growth and stability in Nigeria. The first part of the chapter dealt with an analysis of the demographic characteristics of the respondents, presented in tables of frequencies and percentages respectively. The second part deals with the presentation and analysis of the research questions while the third part deals with the test of the hypothesis and discussion of findings.

3.8 Analyses of Research Questions Analysis of Research Question One

The first objective of this study was to determine the effect of fraud and financial crimes on the profitability of the Nigerian banking industry. Tables 4.6 indicated the questionnaire items and the opinions of respondents on the effect of fraud and financial crimes on the profitability of the Nigerian banking industry

Table 4.6 Effect of fraud and financial crimes on the profitability of Nigerian Banking industry

s/n	Items	SA	A	DA	SD	UD	Mean	Decision
1 . How would you agree with the following statements on effect of fraud and financial crimes on the profitability of Nigerian banking industry?								
A	Financial fraud affect bank profitability negatively	10	40	10	5	5	3.64	Agree
B	Financial fraud leads to costly legal battles	42	4	12	9	1	4.0	Disagree
C	Financial fraud reduces bank customers	55	4	1	8	2	4.5	Disagree
D	Financial fraud reduces bank capital base	1	9	9	50	1	2.41	Disagree

Source: Field Survey Report January 2022

Table 4.6, item la with a mean score of 3.64 indicates that the respondents agree that financial fraud affects bank profitability negatively.

Item Ib having a mean score of 4.0 shows that the respondents agree that financial fraud leads to costly legal battles.

Item Ic having a mean score of 4.5 shows that the respondents agree that financial fraud reduces bank customers.

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Item Id with a mean score of 2.41 shows that the respondents disagree that financial fraud reduces bank capital base

Analysis of Research Question Two

The second objective of this study was to examine the effect of fraud and financial crimes on the confidence of the Nigerian banking industry. Tables 4.7 indicated the questionnaire items and the opinions of respondents on the effect of fraud and financial crimes on the confidence of the Nigerian banking industry.

Table 4.7: The effect of fraud and financial crimes on the confidence of the Nigerian banking industry

s/n	Items	SA	A	DA	SD	UD	Mean	Decision
2. How would you rate the following statements on the effect of fraud and financial crimes on the confidence of Nigerian banking industry?								
A	Fraud and financial crimes lead to loss of confidence in the banking sector.	50	10	3	3	4	4.41	Agree
B	Fraud and financial crimes leads to loss of valuable customers.	4	55	1	5	5	3.69	Agree
C	Fraud and financial crimes leads to loss of foreign investors in the bank.	7	49	4	1	9	3.63	Agree
D	Fraud and financial crimes lead to frustration of bank customers.	8	51	1	6	4	3.76	Agree

Source: Field Survey Report January 2022

Table 4.7, item 2a with a mean score of 4.41 indicates that the respondents agree that fraud and financial crimes lead to loss of confidence in the banking sector.

Item 2b having a mean score of 3.69 shows that the respondents agree that fraud and financial crimes lead to the loss of valuable customers.

Item 2c having a mean score of 3.69 shows that the respondents agree that fraud and financial crimes lead to the loss of foreign investors in the bank.

Item 2d with a mean score of 3.76 shows that the respondents agree that fraud and financial crimes lead to frustration among bank customers.

3.9 Test of Hypotheses

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In this section, the researcher tested the hypotheses using the z-test. The test of hypothesis values of the respondents was categorized into two with "strongly agree" and "agree" as agree, while "disagree" and "strongly disagree" was categorized as disagree. Z-test was used to test the hypotheses.

Hypothesis One

H0: Fraud and financial crimes have no significant effect on the profitability of Nigerian banking industry

HI: Fraud and financial crimes have a significant effect on the profitability of Nigerian banking industry

Table 4.9; Z-test computation for hypothesis one

	AGREE	*DISAGREE*
Mean	17	59.2
Known Variance	366	7.36
Observations	5	5
Hypothesized Mean Difference	0	
Z	4.88353	
P(Z<=z) one-tail	5.21E-07	
z Critical one-tail	1.644854	
P(Z<=z) two-tail	1.04E-06	
z Critical two-tail	1.959964	

Key z-calculated < z-critical =accept; z-calculated > z-critical= reject

The result indicated in table 4.9 revealed that z-calculated (4.88) is greater than z-critical (1.95). Therefore we reject the null hypothesis and accept the alternative which states that Fraud and financial crimes have a significant effect on the profitability of Nigerian banking industry

Hypothesis Two

HQ: There is no significant negative relationship between fraud, financial crimes, and the confidence of bank customers in the Nigerian financial industry

HI: There is a significant negative relationship between fraud, financial crimes, and the confidence of bank customers in the Nigerian financial industry

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Table 4.10; Z-test computation for hypothesis two

	AGREE	*DISAGREE*
Mean	57.8	6 0.4
Known Variance	3.76	
Observations	5	5
Hypothesized Mean Difference	0	
Z		
P (Z<=z) one-tail	56.508951	
Z Critical one-tail	1.6448540	
P (Z<=z) two-tail z Critical two-tail	1.959964	

The result indicated in table 4.10 revealed that z-calculated (56.50) is greater than z-critical (1.95). Therefore, we reject the null hypothesis and accept the alternative, which states that there is a significant negative relationship between fraud, financial crimes, and the confidence of bank customers in the Nigerian financial industry

4.0 DISCUSSION OF FINDINGS

The first objective of this study was to determine the effect of fraud and financial crimes on the profitability of the Nigerian banking industry. Findings indicate that fraud and financial crimes have no significant effect on the profitability of Nigerian banking industry. Responses from the respondents indicate that fraud and finical crimes affect bank profitability negatively but the respondents disagree that fraud and financial crimes reduce bank customers, and reduce bank capital base.

The second objective of this study was to examine the effect of fraud and financial crimes on the confidence of the Nigerian banking industry. Findings indicate that there is a significant relationship between fraud and financial crimes and the confidence of bank customers in the Nigerian financial industry. Responses from the respondents indicate that fraud and financial crimes lead to loss of confidence in the banking sector, loss of valuable customers, loss of foreign investors in the bank, as well as the frustrations of bank customers.

5.0 CONCLUSION

Fraud, financial crimes, money laundering, and Corruption have grown with Nigeria as a country. It gets more and more ingrained, especially as the economy deteriorates and the rate of crime increases. There is hardly any day a newspaper will not carry stories of corruption and/or financial crime. Financial crimes are not only in the public sector/civil service but also in the banking sector. Almost anywhere a service is to be provided the service is not freely obtained.

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Money laundering and financial crime have negative consequences on the economy as well as the banking sector, which include; loss of revenue to the government, worsening criminal rate in the society, political instability, and internal insecurity of the nation. On the part of the banking institution, money laundering has led to the loss of confidence in the banking sector as well as the loss of foreign investors due to the bad image of the banking system.

6.0 RECOMMENDATIONS

1. Banks should adhere to stipulated rules and regulations guiding their operations, especially with lending. This will reduce sharp practices and incidence of fraud and improve on their profitability.
2. The confidence of the bank customers should be restored by putting in place measure like anti-fraud software to reduce the susceptibility of bank customers to fraudulent attacks especially ATM and online users.

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