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Auditors' Perspectives on Financial Fraud in Pakistan – Audacity and the Need for Legitimacy

Keywords: Audit, shenanigans, legitimacy, fraud, financial reporting, Pakistan.

1. Introduction

This study reports the findings from a series of interviews with corporate auditors in Pakistan regarding fraud in financial reporting. Analysis of this type of behaviour in an emerging nation setting, where incentive and reward processes are often defined by opaqueness and informal relationships (Wanyama et al., 2009; Josiah et al., 2010; Chanda et al., 2017). However, detailed investigation of the opinions of auditors, a critical party in such contexts (Wanyama et al., 2013), is rare and the lack of evidence of this type represents a potentially significant gap in understanding.

Financial statement dishonesty is a substantial risk for corporate stakeholders, including commercial lenders and equity investors, with its discovery typically leading to major declines in organisation value (D'Agostino and Williams, 2002; Hoogs et al., 2007). The importance of independent auditors is therefore critical as capital providers require the ability to identify financial statement fraud rapidly and effectively to alleviate the risk of substantive investment losses (Karpoff & Lott, 1993; Neu 2013). In order to be of practical use to stakeholders, detection techniques must be both robust to practical conditions and sufficiently transparent to permit comprehension of the foundations upon which they are based (Persons, 1995; Hoogs et al., 2007) as incorrect claims of dishonesty can have consequences as severe as cases where fraud goes undetected.¹ Studies such as the present one, which attempts to develop understanding of how auditors perceive the manifestation of such behaviour, can therefore generate insights of value to all those with a current or potential financial interest in a corporate entity. This is especially the case in a developing nation where, as Deegan (2019) notes, reporting practices are likely to differ from those of developed nations as the influence of a range of institutional influences vary, notably regarding the rule of law, individual freedoms, governmental control (formal and informal) and media independence.²

Deegan argues that the way in which these forces manifest themselves reflects differences in the three key pillars of institutional order set out by Scott (2014), Palthe (2014) and others and recognition of these is central to the present study's contribution. We address Deegan's call for more nuanced understanding of the role compulsion plays in driving legitimising propensity by demonstrating that Pakistani auditors' views are suggestive of significant fragility in the three institutional pillars which are normally viewed as generating the need for organisational legitimacy (O' Donovan, 2002). However, **despite evidence of professional views that point to**

financial reporting practices so rooted in a culture of habitual corruption that the drivers of the need for legitimacy appear to be particularly weak, Pakistani auditors continue to play a key role in providing an outward appearance of systemic robustness and veracity that goes well beyond what is required by forces on the ground. As Abid et al. (2018) note, audit opinions in Pakistan are not, as a matter of course “issued in response to the earnings management activities being employed by firms” (p. 1)³ and it is therefore apparent that some type of social contract has allowed the current Pakistani reporting and auditing system to persist and operate with apparent impunity - even when the institutional forces conventionally argued as generating the need to legitimise the parties’ behaviour are weak at best.

In the world’s developed economies, scandals such as those at Maxwell, WorldCom, and Enron⁴ have led investors to lose trust in corporate governance norms. As a result, regulatory bodies have been required to sanction new regulations clarifying the duties and responsibilities of senior management, external auditors, and corporate boards in order to re-establish investor confidence (Bai et al., 2004). Whilst the cases receiving most global media attention and ongoing academic analysis are based in the developed world, Jeanjean & Stolowy (2008) and Hasan et al. (2017) argue that earnings management in emerging economies requires detailed contemporary examination, not least because many of the purported benefits of IFRS implicitly assume strong regulatory frameworks and enforcement mechanisms (Hasan et. al., 2017).⁵

The present study focuses on auditors’ perceptions regarding the use of accounting manipulation techniques in the developing nation of Pakistan;⁶ as detailed in Section 2.2 below, the country’s corporate sector has witnessed numerous large-scale financial scandals in recent years and the issues are therefore likely to be relevant for stakeholders attempting to identify financial fraud and insulating themselves from exposures to risk. The research explores the attitude of auditors in Pakistan regarding the use, likely existence, and impact of such actions/omissions with the over-riding goal of generating information of use to investors and other parties with a potential interest in transparent and robust financial disclosure practices. To achieve this aim, two specific issues are addressed: (i) the factors motivating and enabling fraudulent financial reporting; and (ii) the ways in which such impulses manifest themselves in practice. What emerges is a pattern of widespread malpractice, lacking the subtlety evidenced in high profile scandals in developed nations and often involving deliberate misreporting of underlying financial realities. The rest of the study is structured as follows. The next section provides a review of relevant literature in the area, while Section 3 outlines the

methodological approach. Section 4 then presents and discusses the findings of the interviews before Section 5 concludes the paper.

2. Literature Review

2.1 Motivations and Propensity for Fraudulent Behaviour

The 3Cs model of Rezaee (2002) identifies three possible motivations for fraud at an institutional level: (i) choice; (ii) conditions; and (iii) corporate structure, with fraud itself having two categories: ‘management’ and ‘employee.’⁷ On this basis, Rezaee argues that financial statement fraud, the focus of the present study, is at the discretion of management (rather than employees) since managers and accountants are more closely involved in the process of preparing financial statements than are employees.⁸ Rezaee (2002) suggests that economic pressures can also motivate organisations to become involved in financial fraud and, when conditions are sufficiently difficult, the need to demonstrate corporate strength often overwhelms any moral imperative for honest reporting.⁹ Whilst the existence of powerful internal controls can dissuade managers from dishonesty (Jackson et. al., 2001), in practice many of the underlying systems are brittle - often, but not exclusively, in emerging nations - (Edwards, 2004). A CIMA report prepared by Doody (2009) characterises the ‘fraud triangle’ as containing three elements: opportunity, rationalization and perceived pressures,¹⁰ a disaggregation that builds on insights from several earlier lines of enquiry where competition and pressure from shareholders have been suggested as drivers of financial statement fraud (Watts and Zimmerman 1986; Merchant and Rockness, 1994; Tsui et al., 1996; Guidry et al., 1999; Krishna & Paul, 2003; Sholeh et al., 2018).¹¹

According to Healy (1985; 1999) the principal driver of executive inclination to undertake financial fraud is greed, with performance-linked benefits often driving conscious misstatement of the relevant data.¹² In this regard, Holthausen et al. (1995) and Bergstresser & Philippon (2006) demonstrate that executives who receive the largest proportion of their emoluments on this basis are most inclined to manipulate the underlying data.¹³ The possibilities offered by (illegal and legal) creative accounting and other financial fraud make it relatively straight-forward to generate financial rewards well beyond any fair entitlement, without necessarily drawing the attention of regulators that might lead to criminal or civil charges (Fudenberg & Tirole 1995; Graham et al. 2005; Doody, 2009).¹⁴ Lambert (1984) argues that the proclivity for creative accounting is also linked to the expertise of board

members in the fields of auditing, accounting, and finance; specialised knowledge is therefore required in making judgements about the veracity of financial statements, an issue that motivated the decision to focus on auditors' opinions in the present study.

A series of papers published in a special issue of Accounting, Organizations and Society (AOS) in 2013 demonstrated the breadth of contemporary research taking place around fraud in modern financial reporting processes. For example, Neu et al. (2013) explore a fraudulent state-funded sponsorship scheme and mobilize Bourdieu's work on institutional sociology to illustrate the potential for accounting processes to interact with collective structures to facilitate the development of corruption networks. **In a paper focussing on ontological positioning, Power (2013) argues that while renewed academic discourse around broader governance-related matters has driven an increase in the level of attention paid to the risk of fraud, the revitalised debate has in fact emerged "from the world of auditing" (p. 541) with work emphasising the latter providing an important role in contributing to knowledge in the area.**

An alternative theoretical perspective is offered by Davis and Pesch (2013) who develop a model where two types of fraud-propensity exist, one which tends towards stability and another which is defined by individual tendencies for fraudulent behaviour that alters over time. The analysis concludes by suggesting that "it may be inappropriate for auditors to evaluate fraud prevention and detection mechanisms in a uniform manner" (p. 481) again suggesting the multi-faceted complexity of the audit process and the apparent need for engagement with those directly involved. In reflecting on the contents of the special issue the editors (Cooper et al., 2013) argue that while there is now "... an extensive research literature on how auditors might recognize fraud and how audit procedures can mitigate against acts of fraud" (p. 453) the contributions to the debate so far have primarily been normative, with their view remaining that "... the actual means used in carrying out fraud is an area where more accounting research is warranted" (p. 438). The latter argument suggests that detailed empirical work focussing on the perspectives of auditors around fraudulent accounting behaviour is important.

In the present study we focus on Pakistan because, as noted below, a range of accounting-driven scandals suggest that the profession's ability to ensure accurate reporting of financial realities has been heavily compromised. The prevalence of financial reporting scandals is reflected in the recent development of a literature on accounting fraud in Pakistan. In this context, Dilshad et al. (2020) argue that forensic audit procedures should be subject to statutory

mandating, with specialisation in the area a priority for the nation's business schools. This conclusion is consistent with Khan et al.'s (2020) argument, based on quantitative analysis of nearly 300 questionnaires sent to members of firms listed on the Pakistan Stock Exchange, that the internal audit function in the nation would benefit from greater independence and a more "rigorous" (p. 49) hiring process. Another recent study, Iqbal and Aslam (2020), supports the contention that the problems in financial reporting outcomes are widespread, with significant growth across Pakistan in digital and white-collar crime levels more generally the result. The authors suggest that one of the main problems is that a majority of the nation's company accountants are inexperienced, lacking professional qualifications and therefore unable to fully understand new financial reporting standards. These more recent contentions are consistent with an earlier study by Shahid (2016) exploring the manufacturing sector in the Punjab, where governance failures are reported to be an important influence on accounting practices with the inherent agency problems requiring regulatory attention. Again, however, this literature almost entirely ignores the issue highlighted by Cooper et al. (2013) as critical i.e., the 'means' of carrying out fraud, concentrating instead on broader systemic failures and issues in modern-day Pakistan. The present study therefore places specific accounting techniques at the centre of the enquiry, exploring in detail auditors' views regarding their prevalence. The discussion now turns to the Pakistani context, linking the empirical backdrop to the role of institutional failures and debate around the impetus for legitimising behaviour.

2.2 Pakistani Context and Institutional Legitimacy

Salvioni (2002) argues that the existence of financial fraud is partly explained by the fact that income figures provided by companies are 'loose', often based on estimates¹⁵ and presumptions that are easy to manipulate. A report from the ACFE (2008) suggests that a wide range of techniques are employed in this regard, including (*inter-alia*): deliberate exclusion of disclosures relating to accounting policies and principles (and associated financial quantities); misrepresentations or (intentional) exclusion of certain accounts, transactions and substantive events where an unfavourable financial impact is likely; recording fabricated revenues by generating bills to existing and/or bogus customers for fictional sales; and manipulating asset valuations by improperly recording inventory and other asset details.¹⁶ Whilst the literature on financial fraud has been dominated by research focussing on the world's largest financial markets, primarily the US, evidence relating to emerging economies is scarce, as is examination of the views of those charged with attesting to the accuracy of financial reports, i.e. professional auditors. This is a particular concern in a country such as Pakistan, where the

extent of financial fraud has grown to the extent that it is often characterised as the norm (Salman & Siddiqui, 2013; Siddiqui & Fahim, 2013; Rizwan, 2019). According to PWC (2020), 47% of Pakistan companies had experienced fraud in the prior two-year period. The worst of the recent scandals include events at Mehrangate, Taj Company, KASB Bank, the National Savings Scheme, Nestle and numerous microfinance banks (Awan et al., 2016; Kemal, 2019) where investors faced massive losses as a result of widespread reporting fraud (Rizwan, 2019). The present study is therefore cited in Pakistan, in an effort to establish the nature of auditors' perspectives regarding financial deception and thereby provide a robust indication of how and where the institutions charged with attesting to the reliability of firms' accounting disclosures see the malign practices as manifesting themselves most often.

A number of recent contributions to the critical accounting literature have explored financial reporting in Pakistan, but these typically focus on change processes in internal management systems. For example, Ashraf and Uddin (2015) employ a case study method to explore state actors' roles in the nation's aviation industry and expose the importance of social blocks' (relative) dominance in facilitating change. An earlier study by Munir et al. (2013) examines the institutional catalysts for change in Pakistani banks' performance measurement systems, with financial pressures, regulatory change and managerial leadership (including changes therein) all being identified as important. While the literature on financial reporting Pakistan has developed significantly in recent years, the focus remains on investigation of internal dynamics and shifts in structures whereas in the present study we provide the first detailed exploration of auditors' perspectives, i.e. those tasked with affirming the quality of the information reported externally.

Contemporary examination of organisations' financial reporting behaviour is vital, as legitimacy can be seen as representing communication between continuously moving societal limits (Vaara & Joutsenvirta, 2015). Modern applications of legitimacy theory in a reporting context build on early analyses such as that of Dowling and Pfeffer (1975) who suggest that the notion of organisational legitimacy represents the: "condition or status which exists when an entity's value system is congruent with the value system of the larger social system of which the entity is a part" (p. 122). Thus, from a legitimacy theoretical perspective, firms will be predisposed to report on their operations on the basis of standards required by the communities in which they operate (Deegan, 2002). The need for legitimacy itself reflects the 'social contract' existing between a company and the society in which it operates (Deegan, 2000;

Deegan, 2002; Patten, 1992). According to Shocker and Sethi (1973), such contracts have two key elements: (i) the delivery of desirable outcomes to society in general; and (ii) the distribution of economic, social, or political benefits to the groups from which it derives its power. While Shocker and Sethi do not directly link the social contract with organisational legitimacy, Patten (1992) and Deegan and Rankin (1996) argue that the manifestation of social contracts signifies the multiplicity of implicit and explicit expectations regarding how an organisation should conduct and report on its operations. The legitimacy of an organisation is therefore likely to be challenged when it fails to fulfil its social contract responsibilities, creating a legitimacy gap (Lindblom, 1994).

Palthe (2014, p. 61) notes that while leading researchers ‘differ in terms of the primacy’ they attribute to the three pillars of institutional theory - the regulative, normative and cognitive (see, e.g., Scott, 2014)¹⁷ - each of these elements aligns with a particular variety of organisational legitimacy (legal/moral, ethical and cultural respectively).¹⁸ Irrespective of the extent of independence, Alexander (2012) notes the applicability of the three pillar structure when the task at hand - as is the case here with the Pakistani financial reporting system - involves understanding nation-level institutions. We demonstrate that Pakistani auditors’ widespread perception of audacious fraud represents evidence that each of the three pillars have been dismantled. As a result, the existence of factors normally argued as generating the obligation for institutions to maintain legitimacy via social contracts appears to be questionable in Pakistan - and yet the system itself continues, despite the perceptions of malfeasance being generated here by auditors, the very individuals tasked with testifying to the veracity of financial reporting in the nation. In offering this evidence, novel insights are suggested regarding some of the central issues set out by Deegan (2019) as gaps in understanding around institutional legitimacy outcomes that require urgent attention, in particular the conventional notion that compulsion for legitimising behaviour is founded on the existence of the three institutional pillars. Cooper et al. (2013) argue that there is a need for a stronger understanding of the factors that drive “the promotion, persistence and prevention of fraud” (p. 452) in practice. Whilst a literature on these issues (including in the aforementioned special issue of AOS edited by Cooper et al. themselves) has developed, this debate often emphasises normative contention, meaning that the link between contemporary empirical evidence and theoretical modelling remains poorly understood. In the present study, we attempt to address this issue by setting out the implications of our findings regarding the existence of the regulatory, normative and cultural/cognitive institutional pillars as the drivers of the need for

legitimacy, with the focus on the views of auditors, i.e. those who play a key role in establishing and maintaining the validity of the nation's financial reporting system.

We provide empirical indication of an apparently complete breakdown of the three pillars in Pakistan, a society characterised by precisely the types of forces pointed to by Deegan (2019) i.e. embedded power imbalances, a lack of plurality and the silencing of critical voices.¹⁹ As a result, we are able to address Deegan's related identification of the need for better understanding of the role of compulsion and obligations around breakdowns in institutional foundations, with legitimacy theory failing to provide an answer when observed behaviour departs from that predicted. In demonstrating the apparent frailty of any meaningful compulsion for firms to demonstrate legitimacy in the financial reporting system in Pakistan - without apparently challenging society's tacit sanctioning of the nation's long-established financial reporting system - we provide a relevant contribution to this debate. Abid et al. (2018) argue that a range of malign factors, including inter-party 'economic bonding' are embedded in the system, leading to opportunistic behaviour on the part of the profession. Auditors - themselves part of the system as attesters to the authenticity of financial statements - are shown here to have extremely cynical views about motives and outcomes within the Pakistani financial reporting system. When considered alongside the complete breakdown of the three institutional pillars that our work demonstrates, it becomes apparent that Deegan (2019) is right to call for further understanding of the way in which attempts to legitimise and maintain social contracts are driven by compulsion as the latter appears to be notable by its fragility in Pakistan.

3. Research Design

3.1 Data Collection

The empirical research involved interviews with 50 Pakistani auditors about various matters relating to financial fraud in the nation's corporate sector.²⁰ The interviews sought views on two issues: (i) the means of recording revenue, expenses, assets, liabilities and capital permitted by accounting rules operating in Pakistan; and (ii) the reasons why, and ways in which, Pakistani organisations and individuals distort information in the financial statements. The first of these was intended to serve as an icebreaker, as the accounting techniques outlined in the relevant standards are on public record, but the discussion also allowed the auditors to outline any de-facto practices and innovations not formally mandated.²¹ Sample selection was deliberately purposive with the main objective being to seek out individuals with distinct

relevant knowledge and experience of taking part in audits in a variety of organisations.²² A semi-structured guide reflecting the major issues was developed based around a series of questions that reflected both the study's aims and the most common themes in the related literature.²³ As per Schilit (2002)²⁴ the potential devices used to manipulate accounting data were set out as: recording bogus revenue; boosting income with one-time gains; recording revenue too soon or when of questionable quality; shifting current revenue to a later period; failing to record or improperly reducing liabilities; shifting future expenses to the current period as a special charge; and shifting current expenses to a later or earlier period. The findings relating to the specific techniques employed are therefore structured on this basis in the next section of the paper.

Ten interviews were conducted in four major cities of Pakistan, lasting 35 minutes on average in Islamabad, eight in Karachi, eighteen in Lahore and fourteen in Peshawar. Face-to-face interviews were conducted in Islamabad and Peshawar with the remainder conducted by telephone for practical reasons.²⁵ In addition to geographical diversity, the sample included individuals from a range of backgrounds, suggesting that a potentially rich span of opinions was being captured. For example, the age of the respondents varied from 23 years to 78 years, with professional experiences ranging from 2 to 55 years. The interviewees were all fully - or partly - qualified members of the Institute of Chartered Accountants of Pakistan as well as, in many cases, being in possession of additional professional qualifications.²⁶ Details regarding the participants are shown in Table 1. Seven of the participants worked for the world's top 5 firms, with a further 18 employed in the top 10 and another 11 in the top 20. The rest of the interviewees worked in local chartered accountancy firms licenced by the Institute of Chartered Accountants of Pakistan (ICAP) and holding QCR (Quality Control Reviewer) status.

3.2 Data Analysis

Analysis of the interview data was based around development of thematic codes. This process facilitates a systematic approach to categorisation, one that is ideal for exploring large amounts of textual information in order to determine trends, frequency of use, relationships, recurrent structures and discourses in communication (Mayring, 2004; Kitto, 2008). Development of the interview guide and analysis of the data involved a number of stages. First, a draft of the guide was prepared based on examination of prior literature in the area. Following a series of pilot interviews with chartered accountants a number of adjustments were made to the document. The guide was employed as a basis for the discussions, but with each interviewee allowed to

set out their views in detail and raise issues not explicitly included in the document. After the interviews, the text was transcribed, and the data interrogated using Excel to identify common phrases and terms. We employed the coding scheme in Gibbins et al. (1990) and Beasley et al. (2009) to categorise the data, beginning with the creation of a vocabulary within the interview text followed by analysis of the transcripts, highlighting of significant words and sorting of the latter into categories on the basis of similarity. Using this coding scheme, we developed unique categories that captured the participants' responses. The first of these involved two broad emergent categories: propensity for involvement in financial fraud and manifestation of financial fraud. In the next phase, the data relating to the second of these high-level groups was re-coded on the basis of the seven specific classes of financial fraud suggested by Schilit (2002) that had both informed the configuration of the interview guide and closely matched the thematic structure of comments made. Finally, we examined a number of 'qualified'²⁷ audit reports to explore whether the perceptions of the participants were in line with the attested veracity of financial reports in Pakistan. In broad terms, the points highlighted by the auditors in the interviews were consistent with the qualified reports,²⁸ but suggested that the malpractice is likely more widespread - and certainly more shameless - than simple reading of the latter would indicate.

4. Results

4.1 Propensity for Involvement in Financial Fraud

The majority of the interviewees were clear in asserting that certain types of institutional characteristics are associated with an increased proclivity for financial fraud; these pointed in most cases to weaknesses at best in (at least) one of the pillars on which Scott (2008) and others suggest that institutional legitimacy is based. Notably in this context, a weak internal control system was widely thought to be one of the main drivers of financial statement falsification. The views of interviewee A3, a highly experienced auditor based in Islamabad, were typical in this regard, suggesting an underlying problem whereby:

“Companies usually do not focus on the internal control system and fall prey to frauds and misstatements by their most trusted employees.”

This perspective suggests the questionable evidence regarding the existence of any meaningful regulative impulse for institutional legitimacy. As Palthe (2014) notes, this pillar is based on rudimentary respect for policies and rules with “fear and coercion” sustaining its impact. If a firm's “most trusted” employees are prone to financial fraud then clearly this particular force

(also identified by Scott, 1995; Thornton et al., 2012 and others) is very limited in impact in the Pakistani financial reporting system. Most of the interviewees believed that the problems caused by fragile internal control processes in Pakistan are exacerbated by flexibility in accounting rules. In this context, issues relating to commercial processes, arrangements designed to protect asset values and certification of the records needed for external reporting were all seen as significant. In the absence of controls targeting such actions, pervasive fraud was considered likely. A further perception shared by most of the interviewees was that the propensity for financial fraud is considerably higher in newly formed companies; several interviewees asserted that such firms employ dubious accounting methods in order to demonstrate rapid growth to potential investors. The point was articulated most clearly by interviewee A42, a CA finalist from Peshawar, who noted that: "... as new organisations [these firms] do not have high profits, but they manipulate information to satisfy all the stakeholders" with the behaviour driven by: "pressures from government, investors [and] shareholders ... to use such techniques as make everyone happy."²⁹

The principal-agent relationship and behavioural issues linked to it were implicit in many of the comments made, but pressures placed by owners on management to generate desired financial outcomes was seen as a major independent catalyst for fraudulent acts. One of the interviewees, A17, provided a stark example of just how insidiously this motivation could manifest itself:

"Once I audited an organisation where the management was facing extreme internal pressure to increase the dividend and [therefore] the profitability level. Management had to hire a chartered accountant on the extraordinary salary of Rs. 1,500,000 to manipulate the financial information."

Another interviewee, A7, suggested that external pressure on firms was also an issue, effectively normalising deliberate misstating of financial figures, auditors having to come to terms with the pervasive nature of the behaviour:

"In the beginning some of the practices involving the misrepresentations in the financial statements seemed to me to be the organization trying to deceive us and the general public for which I tried to correct them, but with the passage of time and experience with more organizations I came to understand that these practices are the new normal and the firms have to make such misrepresentations in order to survive in the market and compete with those who are also involved in such practices" (A7).

Palthe (2014) argues that the normative aspect of institutional legitimacy reflects a sense of duty and responsibility that builds morality into organisational behaviour. The observation

made by the auditor here suggests that neither the firm (in targeting potentially unprincipled professional accountants) nor the latter individuals themselves are moved by the type of ethical obligation on which this pillar is built. This interviewee elaborated on the incident by noting the way in which it exposed the tension between shareholders' focus on short-term dividend income and management's need for long-term investment via retained earnings. Whilst most of the comments made reflected this type of conflict (explicitly or implicitly), a number of other specific spurs for fraud were identified by respondents, including financial distress and its tendency to motivate companies to provide a (false) impression of stability to potential investors.

There was broad consensus that the primary driver of such practices was the moral hazard faced by Pakistani managers as agents³⁰ in a society where regulatory obedience is far from the norm in many arenas. The temptation to prioritise personal benefits over the desires of any owners - contrary to the assumed role of moral responsibility in the normative pillar of institutional legitimacy - was believed to dominate decision-making in a straightforward manner, as interviewee A39 stated:

“Management are hired by the shareholders and are paid by them as well. In instances where the rewards are performance related, the management manipulate information so that they are paid higher remuneration.”

Whilst many of the interviewees were keen to point out the lack of subtlety in response to individualistic motivations, deception driven by a need to ensure that outside investors' desires are met - irrespective of the reality - was also alluded to. For example, interviewee A44, a CPA based in Peshawar, noted that:

“All organisations are formed for the purpose of profit making. They try to earn enough profit to keep the investors happy. For this purpose, they sometimes manipulate information if they fear that showing the correct information may reduce investors' interest in the organisation.”

The impact of funding requirements more generally on the likelihood of misleading financial reporting was also mentioned by a number of the interviewees.³¹ For example, a Lahore-based auditor (A20) asserted that:

“Organisations operate on money and for money they have to get financing in the form of debt or equity depending on their need and requirements. To attract financiers, they must have good standing in the market [and to] achieve that, organisations get involved in financial shenanigans to portray strong financial statements and higher profits.”

Scott (2008) suggests that from a normative standpoint, an individual's affectation, driven partly by a desire to avoid shame, should counter any temptation to behave in the way suggested by the interviewees quoted above. What these perspectives indicate is that in practice this institutional force can be overcome by a need to portray a falsely favourable impression to external parties. Given their proximity to the process, the views of the auditors regarding technological developments were of particular relevance to a study of contemporary reporting practices. The general view was that advancements in technology have made it easier for organisations and individuals to commit fraud without detection, a process that began with the move away from paper trails some years earlier. The thoughts of a Certified Information Systems Auditor, interviewee A49, shed light on the particular issues faced by the audit profession in the digital information age - even relative to accountants as a whole - in arguing that:

“Technology is useful on one hand but a hindrance on the other as it is very easy today to be an accountant but very difficult to be an auditor. All the entries are one click away with the help of updated software but tracking the origin of an entry is a long, hectic process.”

This concern implies a weakness regarding the cognitive foundation of institutional legitimacy. As Cashmore and Wejs (2014) and Palthe (2014) note, this pillar is based on issues such as social identity, beliefs and assumptions, but in this case an experienced auditor is suggesting that transformation in reporting system mechanisms, as part of a broader move to digital processes, brings with it challenges to professional skills that are far from trivial, thus compromising the cultural foundation of this particular legitimising feature.

In addition to the widely held perceptions reflected above, a number of other motivations for financial fraud were identified by several participants. Interviewees A1, A2, A7, A18 and A19 all pointed to taxation as an impetus for the widespread frauds that Pakistan has witnessed in recent years. Again, the highlighted behaviour was blatant and unashamed in nature, with revenues hidden and expenses exaggerated. Interviewee A1 emphasised that this type of ‘distortion’ was ‘usual’ in practice, with the moral issues surrounding this behaviour (and any suggestion that such practice might represent a victimless crime) addressed by a hugely experienced auditor from Lahore (A32) who argued that:

“Taxation is a vital organ for society as the tax helps individuals’ avail of the basic necessities of life, but in [Pakistani] society, taxation is considered to be a burden, and everyone tries to get rid of its payment. For that purpose, organisations try to hide their incomes so that they pay less taxation while not

considering the fact that such payment of taxation is ultimately used by the government to give facilities to them.”

In this case, fragility in both the normative and cognitive elements of institutional theory set out by Alexander (2012), Palthe (2014), Scott (2014) and others is suggested, as the view expressed implies the irrelevance of the social pressures often associated with the former pillar and, via the implicit suggestion of a cultural aversion to taxation exposure, the cognition-driven element as well. This contention also provides support for the notion put forward by Braithwaite (2013) that certain markets: “... can demand managers who reject the view that paying tax is normative; it rewards managers who construe a tax liability as a problem that aggressive management should eliminate.” This leads Braithwaite to argue that ‘qui tam’ regulation might be required - in other words, when the two institutional pillars that conventionally generate what Braithwaite characterises as a “virtue” market both have marginal bearing at best (as appears to be the case in Pakistan), rationality around the societal benefits of taxation disappear from mindsets such that a complete restructuring of the judicial basis of enforcement might be required.

Finally, and of significant concern given the extent of corporate failures in Pakistan, several interviewees suggested that worries regarding the loss of going concern status was a major influence on behaviour. The views expressed in this context are reflected in the following comment made by respondent A35, which points to the perceived lack of any need for discernment in practice and, again, the failure of any institutional regulative constraint:

“The going concern phenomenon tells investors whether the organisation will survive for the longer period or not. The investors take out their investments from the organisations if they feel any threat of losing their money ... this is why organisations manipulate their financial statements.”

4.2 Manifestation of Financial Fraud

While the interviewees had much to say about individual and organisational propensity to commit reporting fraud, most of the comments made related to the particular techniques employed. The latter all appeared to represent one of the seven types outlined by Schilit (2002) although in each case the perceived behaviour was unashamedly straightforward, both in absolute terms and relative to that reported in the high-profile scandals in the West alluded to earlier. As with the evidence relating to the tendency to become involved in fraudulent reporting behaviour, in most cases the views expressed suggested a breakdown of one (or more) of the three elements underpinning institutional legitimacy.

4.2.1 Recording Bogus Revenue

To rely on financial reports, investors have to assure themselves that the information regarding revenue generation is presented fairly and accurately (Mulford & Comiskey, 2011). One of the issues raised most often by the interviewees relates to situations where customers receive a shipment of goods but are not required to keep or pay for them, thereby opening up the potential for the whole transaction to be reversed at a future date. Companies in Pakistan were seen by the auditors as using such arrangements to shield income from their (the auditors) view by modifying the terms of sales contracts via "side agreements"³² that grant customers the right to return unsold goods. The original sales lack economic substance³³ as they typically involve reciprocal agreements in which the company commits to buy something from its customer, or to simply refund the income received on an agreed basis. In any case, the original revenue from such activities is then wiped out in net terms, for example:

“I once came across an organisation that had side agreements with the customers under which the customers had to return the product after a stipulated period for some portion of the investment to be returned. In reality, the organisation used to record the whole amount as revenue without making an allowance for the refund” (interviewee A8).

Given the apparent involvement of customers in this particular manipulative device, key elements in all three of the institutional pillars that are normally associated with the need to legitimise are notable by their (at best) fragility. As regards the regulative component, the lack of respect for the rules on either side of the transaction indicates that the extent to which this motivation exists is questionable. Equally, the ostensible lack of meaningful ‘social obligations’ (Scott, 2008) and/or sense of ethical duty suggest that any need for the outward legitimacy offered by Pakistan’s reporting system is not founded on any normative pillar. Finally, the apparent self-interest underlying this interviewee’s observations point to a local culture that reflects pervasive financial fraud, such that any cognitive compulsion for legitimacy at a higher level that goes beyond the rules of the game is not a feature in Pakistani financial reporting. However, the persistence of a system with superficial symbols of strong legitimacy such as (growing) adherence to IFRS and a well-developed system of professional accreditation for auditors suggests that some form of impulse exists, one that motivates attempts to project legitimacy beyond that required by social obligation norms, regulatory outcomes or extant culture.

Whilst the financial fraud at Enron was primarily attributable to the use of a myriad set of special purpose entities, evidence subsequently emerged of the firm recording loan receipts as operational revenue.³⁴ The findings here suggest that although nothing as subtle as the off balance-sheet financing schemes developed at Enron were involved, the latter practice is an established feature of corporate reporting in Pakistan. In this context, participant A2 – a highly experienced auditor from Islamabad – noted that “people confuse loan income with revenue as both transactions are in monetary form, but their substance is different which needs to be understood and differentiated.” However, the extent to which confusion could explain any such misreporting was very limited in most interviewees’ minds; for example, respondent A11 contextualised his belief in this process via a specific example of a telecommunications company where: “... to achieve targets they were providing money to customers to buy connections in their name and recording such money as revenue.” Again, it was the crude nature of the underlying behaviour that was often most remarkable; interviewee A37 acknowledged that, based on his observations over three decades, the following basic principle was being ignored by many firms and required reiterating: “sales of fixed assets ... are not revenue and recording them as such will give the wrong impression.”

In contrast to most of the fraud perceived by the interviewees to be common features of Pakistani reporting practice, deceptive recording of related party transactions³⁵ was seen as more subtle in terms of exploiting ambiguity in accounting rules. Whilst respondent A1 simply outlined that: “related party transactions are the most common and most difficult method of fraud to detect,” Interviewee A47, an FCA with 8 years’ experience, acknowledged the complexities involved:

“Related party transactions are not against the law ... It may be possible that such companies are facing a hard time in catching up with the competition, losing investment opportunities and maybe facing being wound up. In such cases these transactions violate the accounting and auditing standards and become questionable.”

This was one of many points made by participants in the study relating to the exploitation of ambiguity in particular accounting rules in certain situations. Scott (2008) argues that one of the founding elements in the cognitive institutional pillar relates to ‘affect’ around the certainty/confusion relationship. What is clear from the evidence accumulated here is that equivocality in rules drives much of the objectionable behaviour attested to, with the certainty required to support this particular pillar of legitimacy apparently lacking.

4.2.2 Boosting Income Using One-Time Gains

Whilst the recording of one-off events³⁶ does not necessarily involve the breaking of particular accounting rules, the interviewees expressed serious concern about the motives underpinning much of this behaviour in Pakistan. Respondent A2 pointed to the problems caused by agency relationships in such cases:

“One-time gains boost profit – this may please the bosses, but those who invest in the organisation or finance the organisation and rely on the deceptive financial statements will be disappointed.”

This type of comment was typical of several related to moral hazard and the incongruence of objectives between various parties. The prevalence of this issue again suggests major limitations in the strength of one of the critical drivers of the need for a legitimate financial reporting system in Pakistan. In this case, there appears to be questions surrounding the extent to which ‘moral obligations’ and ‘values’ - the factors that Palthe (2014) points to as underpinning normative and cognitive institutional legitimacy respectively - manifest themselves in Pakistan.

A particular issue was raised relating to the ad-hoc recording of gains and losses from activities unrelated to on-going operations such as the sale of land or buildings. Several respondents pointed to the proliferation of this practice in Pakistan with the suggestion that those responsible were either acting out of a deliberate desire to misrepresent financial realities or an extraordinary failure to grasp the basic accounting notion that onetime gains are shown separately in income statements. In this regard, the interviewees were keen to point out the basic nature of the rules that those responsible for this behaviour appeared to be unaware of, including respondent A47, who suggested that a benevolent interpretation of the malpractice would have to centre on a lack of knowledge that:

“Investment income is to be separated from revenue income as revenue is from operations while investment is separate from operations of the organisation. Setting gains and losses from investment against revenue is fundamentally wrong because their nature is different, and they should therefore be accounted for under different headings.”

Apparent ignorance regarding the related need to differentiate between recurring and non-recurring expenses was also advanced as the most generous interpretation of this type of reporting misdemeanour, with participant A13 suggesting that such conduct would have to involve unfamiliarity with the most basic concepts in accounting. In terms of specific devices,

the technique perceived to be adopted most widely involved selling undervalued assets (which remain recorded at cost or book value) at inflated amounts. Again, the implicit fraud involved is notable by its sheer brazenness, but concern emerged that this type of behaviour was partly facilitated by the weak nature of any external mitigating pressure.

4.2.3 Recording of Revenue Too Soon or When of Questionable Quality

As Douppnik & Perera (2011) note, revenue should not be recognised unless reliable indication of the arrangement is present, and assessment of the client's creditworthiness has taken place. Therefore, when money is received in advance of the provision of a service or product, it represents unearned revenue (i.e., a liability) and should remain so until the service is provided in full (Bauman, 2000). Again, both the practice and motivation behind this behaviour was seen as strikingly straight-forward by Pakistan's auditors, with any need to legitimise behaviour on a regulative basis via observance of rules, or any fear of legal sanction entirely non-existent. For example, interviewee A37, an accountant based in Peshawar with 30 years of practical experience, noted that:

“When the year end is approaching and profits are sagging, companies ship goods and record revenue before the sale has taken place. The merchandise is sent out of the warehouse to customers before their demand is received.”

Whilst this opinion accorded with most of the views expressed on the issue, the motivation seen as underpinning this behaviour was summed up most succinctly in the comments of respondent A16, who believed that: “whenever operating cash flow starts to lag behind declared net income, it is a clear sign that unearned revenue is being recorded.” Whilst in other contexts this contention might be seen as overly cynical, it is entirely consistent with the picture that emerged of Pakistani financial reporting practices more generally.

4.2.4 Shifting Current Income to a Later Period

Unlike most of the other categories of reporting misdemeanour outlined in the present study, fraudulently delaying the reporting of income is often found in organisations in a relatively stable financial position (Schilit, 2002). Whilst much of the literature links this type of timing decision to questionable – but not strictly prohibited – accounting choice,³⁷ the interviewees again pointed to the brazen nature of the rule-breaking in Pakistan. The desire to portray smooth income growth to providers of capital was central in the opinions put forward in this regard, a point made most concisely by interviewee A18 who contended that:

“Organisations carry out such practices as investors and creditors are keen to invest in stocks with stable and probable earnings, as compared to the stocks where earnings fluctuate” (A18).

Prevalence of this underlying motivation again challenges the role of social obligations in Scott’s conceptualisation of the normative institutional pillar and the role it ascribes to morals and ethics in establishing the need for legitimacy. Particular concern was raised regarding practices around mergers and takeovers that are agreed close to the end of an accounting period, where acquiring companies typically ask the acquired firm to temporarily halt the recording of revenue until the deal is finalised. In this context, interviewee A25 pointed to the vested interests at work, simply stating that: “... mergers and acquisitions provide room for fraud and misstatement for both parties who benefit themselves as much as they can during the process.”³⁸

4.2.5 Failing to Record or Improperly Reducing Liabilities

When liabilities are recorded, organisations may prefer not to disclose the full extent of their exposure (Schilit, 2002). Whilst some flexibility exists for organisations in choosing the timing and method of recording certain transactions, as reflected in certain elements of the Maxwell and Enron cases (Clarke, 1993; Vinten, 2002), organisations must be able to justify discretionary choices that affect the reporting of amounts owed (Doupnik and Perera, 2011).³⁹ Many of the comments made by the interviewees when discussing issues relating to under-reporting of liabilities in Pakistan⁴⁰ related to the exploitation of ambiguity in rules albeit in the context of an apparently lower need for complexity than in cases documented in the developed world. For example, participant A7 was keen to make the point that:

“Accounting is all about judgement and assumptions which make it easy for organisations to manipulate the data. Accounting assumptions can be used to misstate the financial statements as changing an estimate can change the overall picture and depiction ... manipulation in many such ways is possible.”

These points – made by a representative of the audit profession – again indicate the lack of any cognitive foundation for legitimacy around the financial reporting system in Pakistan; as Palthe (2014) notes, assumptions play a critical role in this institutional characteristic. Given that, according to interviewee A7, assumptions are exploited by the nation’s firms for perverse ends, Scott (2008)’s contention that ‘certainty’ relative to ‘confusion’ buttresses the cognitive pillar is indicative of a reporting system in Pakistan that is not founded on any such robust basis. However, the views expressed here also indicate the presence of the type of interplay suggested

by Deegan (2019) around the three pillars with, for example, no apparent ‘fear’ of legal consequences – central to the regulative pillar – evident.

Interviewee A20 described a scenario based on his own experiences where firms structure transactions in a way that principally reflect a desire to manipulate the timing of expenses but with implications for liability and asset figures:

“Assume that you agree to purchase Rs. 100,000 inventories in the next year from a supplier but reach agreement for a rebate of Rs. 20,000. You therefore reduce the expense by Rs. 20,000 which will increase the profit in the current period. Actually, what should be done is a reduction in inventory price by Rs. 20,000 which will mean that the benefit accrues in the current period instead of later when it is sold.”

Notwithstanding the managerial indifference to financial deception evident in this perception – arguably as concerning as any of the points made by participants in the study – suggests a complete lack of the certifiable confirmation driving normative institutional pressure.

4.2.6 Bringing Future Expenses Forward to an Earlier Period as a Special Charge

Schilit (2002) argues that while bringing forward the recording of expenses may not contravene formal accounting regulations, in practice it takes place primarily to serve the interests of corporate management. Murphy & Zimmerman (1993) and Pourciau (1993) point to the concentration of such activity around top executive changes in the US and the views of the interviewees here suggest that similar ‘big-bath’ outcomes exist in Pakistan albeit – again – with little indication of any attempt to mask the underlying motivation. Participant A1 offered the following example to illustrate the point:

“Let us assume that a new CEO is hired, and they take drastic steps to improve the financial performance of the organisation; downsizing, restructuring and shifting future expenses to the current period will be their priority. Doing this means a decrease in tax liability for the current period and a big increase in future profitability. Investors, on the other hand, won’t recognise the big charge, due to its non-recurrent nature and so it’s win-win for the managers.”

Whilst this type of behaviour suggests deficiencies relating to elements in several institutional pillars, it is most obviously at-odds with Palthe (2014, p. 61)’s assertion that where the cognitive foundation exists, “personal desire” will establish cultural legitimacy rather than, as appears to be the case here, individuals are unhindered by any concerns for the impression that might be generated. Other inter-temporal fraud of this type attested to by the auditors included the treatment of research and development costs around takeover activity, with a perception that firms in Pakistan have a tendency to write off acquisition costs prematurely by deeming

them to be ‘in process’ thereby reducing expenses and raising operating profits. The absence of any personal concern regarding institutional pressure for legitimacy was again notable.

4.2.7 Shifting Current Expenses to a Later or Earlier Period

Major acquisition activity or managerial changes can motivate the bringing forward of expenses and costs, but the auditors’ views suggested that artificial delaying of expense recording is also a common feature in Pakistani financial reporting. As Schilit (2002) notes, if charges against income are recorded later than accounting rules or principles suggest, profitability increases and higher taxes have to be paid, implying that shareholders have good reason to be wary of such activity. The primary issue that concerned the interviewees here regarded circumventing of the spirit, if not the letter, of IFRS by treating certain operating costs as investments and extending the profit impact over time via amortisation. Examples pointed to included interest, marketing and R&D expenditures, although there was acknowledgement that flexibility – and lack of familiarity – with accounting rules drove some of this behaviour. Interviewee A22 made this point in the context of a failure to grasp the concept of impairment⁴¹ which, he noted with concern: “is not very widely used in Pakistan.” Similarly, interviewee A1 argued that an element of the observed behaviour might reflect ambiguity in the attendant rules – and a further apparent compromise of any regulative or cognitive institutional foundation for legitimacy – contending that it underpinned (widespread) problems in this regard:

“... it (capitalising certain operating costs) is allowed in standards to a certain extent, making it difficult to question and the most popular way to commit fraud. One should sense the existence of fraud if the policies are being changed near to the closing dates.”

However, several interviewees took the view that the behaviour ran counter to basic accounting norms in such a stark manner that perverse intent was almost certainly involved, suggesting that the main issue in terms of the institutional pillar construction relates to a breakdown of the regulative element, reflecting the apparent lack of any fear in Pakistan regarding “sanctions” for rule breaking (Thornton et al., 2012, p. 37).

4.3 Relationships between Fraudulent Acts

Whilst manifestations of each of the seven types of fraud identified above was evident in the auditors’ comments, Schilit (2002) argues that overlap and relationships amongst these is likely; given their apparent prevalence in Pakistan, it is unsurprising that the perceived extent of interaction was non-trivial. For instance, situations were pointed to where organisations

accept payment in advance from customers for the future provision of services but record the revenue immediately, thus involving the third and fifth example outlined in Section 4.2 (i.e., “Premature recording of revenue” and “Failing to record or improperly reducing liabilities”). Similarly, the issues raised in sections 4.2.4 and 4.2.1 are clearly allied as an organisation that has deliberately held back the recording of revenue in the current period will subsequently recognize that revenue (wrongly) in a future period. Additionally, the mechanisms set out in 4.2.5 and 4.2.6 (i.e., failures relating to recording liabilities and bringing future expenses forward) will be linked when an organisation restructures and releases reserves in a future period upon the charge being credited. These associations increase the potential for harm to be caused to those wishing to access reliable information about Pakistani firms’ financial performance. However, from an investor point of view, some cases of accounting fraud can prove more dangerous than others. For example, the bloating of revenue is potentially more harmful than manipulation of reported expenses (Spathis, 2002). Notwithstanding this type of differentiation, Grove & Basilico (2011) report that when organisations use conspicuous fraud, associated stock price deterioration lasts longer.⁴² Hence, whilst financial fraud can provide some benefits for (self-interested) corporate parties in the short run, over longer time periods misleading reporting can have an effect on organisational credibility that impacts all parties adversely.

5. Conclusion and Reflection

The present study has provided detailed evidence regarding the opinions of Pakistani auditors regarding the manifestation of accounting fraud within the nation, illustrating a widespread view that such practices are both common and unashamed. In approaching the issue in this way, we have attempted to address Cooper et al. (2013)’s concern that while much highly productive normative theorising has taken place in the area, ‘the means’ by which such activity manifests itself requires more extensive empirical enquiry. The picture that emerges regarding behaviour in Pakistan’s financial reporting system provides the basis for a contribution to the broader debate regarding the forces prompting attempts to develop institutional legitimacy. In particular, the unashamed corporate behaviour outlined here by Pakistani auditors – the gatekeepers in the reporting system – regarding the prevalence of financial fraud has been demonstrated to represent a collapse of all three main pillars of institutional theory.

The financial reporting profession in Pakistan presents an outward appearance of legitimacy to the world, with international accounting standards mandated and professionally-qualified auditors attesting to the veracity of the system's outputs. However, as the evidence in this paper indicates, auditors themselves appear to believe that a 'moral economy' exists within the nation, centred on (unashamed) corruption and open contempt for rules and standards. Thus, while the 'rules of the game' reflect widespread embedded malfeasance, the financial reporting system's (superficial at least) projection of robust legitimacy appears to go well beyond what is required to address de-facto pressures for authenticity and robustness on the ground. An apparently very limited need for the type of outward legitimacy that Pakistan's financial reporting system continues to portray is suggested by our evidence regarding the weakness of each of the three institutional underpinnings of strong legitimacy, i.e: (i) the normative pillar - as the type of societal compulsions driving a need to project legitimacy appear to be weak at best in Pakistan; (ii) the regulatory pillar - with both reporting firms and public gatekeepers appearing to operate on the basis of norms that involve cursory regard for regulation; and (iii) the cognitive pillar - given that cultural systems in Pakistan suggest that social identity does not require adherence to what might reasonably be considered best practice in reporting behaviour.

As Palthe (2014) notes, each of the three pillars can be seen as representing a "basis for" the need for legitimacy, a view consistent with Deegan's (2019, p. 2318) argument that the pillars "provide an over-arching system within which organisations operate." **In short, our findings suggest that the Pakistani financial reporting system provides an external impression of legitimacy that goes well beyond what is necessitated by national conventions, norms and culture.** In suggesting this possibility we believe that Deegan (2019)'s call for further analysis of these forces is well-timed, with the evidence presented here addressing Deegan's call for 'incremental' building of theory around institutional financial reporting practices. Whilst Deegan (2019, p. 2321) argues that "we could perhaps elect to abandon legitimacy theory (perhaps in favour of some form of institutional theory given that it might seem no longer appropriate to use legitimacy theory, in its simple form)" he ultimately rejects this call by suggesting that the need for models which are "... accounting focussed and developed and refined by people who have a specific interest in, and knowledge of, various aspects of accounting" remains critical. In any case, the complex nature of the modern theoretical debate around the manifestations of (and requirements for) particular institutional influences indicates

that studies such as the present one, set firmly in the views of practising accountants, are important.

Our findings also provide contemporary empirical support for earlier contentions that legitimacy, stakeholder and relate theories may not represent relevant explanatory frameworks for studies of reporting outcomes in non-Western countries with unique cultural settings and weak democratic institutions. In particular, recent literature on Bangladesh points to the important role of traditional local norms and culture. Uddin and Choudhury (2008) report that “familial and political connections” within the nation often conflict often with “the state’s rational and legal power” (p. 1045) while Uddin et al. (2018) point to support for Weber’s notion that traditional links between political and familial forces are critical in determining conventions in Bangladeshi firms’ corporate social reporting (CSR) practices. We have added to this body of knowledge by providing detailed evidence relating to the specific perceptions and lived experiences of those actually charged with attesting to the legitimacy of external reported outcomes amongst listed firms. In so doing we have demonstrated that a moral economy reflecting a pervasive lack of adherence to regulation can co-exist with an outwardly legitimate financial reporting system. Further work is needed to develop an understanding of the forces at play here, to help identify the means by which this type of systemic dissonance can be challenged. As it stands, the findings are consistent with a scenario where the superficial appearance of strong legitimacy persists for the purposes of reassuring investors and other stakeholders beyond national/cultural borders, while widespread disdain for rules and statutes in day-to-day commercial behaviour and regulatory pursuits continues to manifest itself in practice. Any work exploring the extent to which this inward/outward dichotomy is embedded would be insightful in this context as it would permit exploring the relevance to financial reporting more broadly of Uddin et al. (2018)’s contention that attaining “ ‘legitimacy’ globally” (p. 425) irrespective of local traditionalism may be a concern in a CSR context.

In addition to its theoretical contribution the present study points to a number of issues relating directly to accounting practice, in particular its regulatory aspects. In identifying trends in the perceptions of Pakistani auditors, the research reported here should be of use to organisations responsible for overseeing financial reporting regulation in the nation. Given the role that such issues played in motivating much of the perceived behaviour, it is clear that a stronger corporate governance framework - with robust enforcement - and a broader understanding of the harmful

effects of poor ethical standards are needed in modern-day Pakistan. The apparently deeply embedded nature of the fraud attested to by the nation's auditors means that the problems are unlikely to be resolved by regulation alone. Whilst accounting bodies now regularly publish detailed ethical codes and guidelines, a cultural change in attitude is likely to be required in Pakistan to address the existence of an institutional and cultural environment where malpractice in financial reporting is considered normal. As Cooper et al. (2013) note: "Disparate cultural frameworks thwart or enable practices such as bribery and corruption" (p. 452). The evidence presented here suggest that systemic factors in Pakistan currently work to 'enable' rather than 'thwart' in this regard and so the type of whistleblowing initiative as noted by Okafor et al. (2020) may have a role to play in increasing systemic transparency and accountability. This type of change would almost certainly require establishment of an (anticorruption-focussed) institutional environment based on cultural and religious values that are supportive of national unity, equity, transparency and fairness, with robust accountability discharge required to hold corrupt officials responsible for their actions. In this context, the use of accounting technologies to combat fraud has been proposed by Everett et al. (2007) and, as part of a broader package of structural changes, this proposal might have merit in drawing attention to bottom-line performance as a measure of efficiency. An awareness campaign strategy designed to engage stakeholders - including the institutions and religious bodies that have historical and cultural hegemonic influence - could help build understanding of the importance of notions of ethics and morality. Ultimately, the results of the present study support the type of contention in the wider literature on corporate governance in developing countries made by Wanyama et al. (2013) and others whereby the need for ethical behaviour, transparency and honesty in all spheres of life must be emphasised from the earliest days of an individual's education, if the type of entrenched forces supporting the status quo are to be challenged meaningfully. The improvements in the quality of accounting information and ethics that should result will aid not only investors, but all potential users of financial statements in emerging markets, by increasing transparency, reliability and the extent to which trust can be placed in reported information.

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Table 1. Participants' Profile

Interviewees	Age	Qualification	Experience (Years)	Location	Category of Firm ⁴³
A1	52	FCA	30	Islamabad	Top 10
A2	55	ACA, CMA, CISA	32	Islamabad	Top 10
A3	50	ACA, ACMA	32	Islamabad	Top 10
A4	43	CA part-qualified	25	Islamabad	Top 10
A5	72	FCA, CIA	30	Islamabad	Top 10
A6	25	CA part-qualified	3	Islamabad	Top 10
A7	23	CA part-qualified	2	Islamabad	Top 20
A8	25	CA part-qualified	3	Islamabad	Top 20
A9	47	ICAEW	16	Islamabad	Top 20
A10	51	ICAEW	21	Islamabad	Top 20
A11	23	CA part-qualified	2	Karachi	Top 5
A12	33	CA part-qualified	6	Karachi	Top 5
A13	40	CA part-qualified	10	Karachi	Top 5
A14	69	FCA, CMA	30	Karachi	Top 5
A15	33	CA part-qualified	4	Karachi	Top 10
A16	39	CA part-qualified	6	Karachi	Above Top 20
A17	65	FCA	25	Karachi	Top 10
A18	65	FCA	30	Karachi	Above Top 20
A19	56	ACA, CISA	23	Lahore	Top 20
A20	43	ACA	15	Lahore	Top 20
A21	62	FCA	28	Lahore	Top 20
A22	29	CA part-qualified	5	Lahore	Top 5
A23	67	FCA	30	Lahore	Top 5
A24	35	CA part-qualified	10	Lahore	Top 5
A25	67	CISA	15	Lahore	Top 10
A26	64	ACCA	20	Lahore	Top 10
A27	38	ACCA	3	Lahore	Top 10
A28	66	ICAEW	20	Lahore	Top 20
A29	29	CA part-qualified	5	Lahore	Top 20
A30	72	FCA, CISA	40	Lahore	Above Top 20
A31	58	FCA	32	Lahore	Above Top 20
A32	70	FCA	37	Lahore	Top 20
A33	53	ACCA	20	Lahore	Top 20
A34	55	ACCA	24	Lahore	Top 10
A35	32	CA part-qualified	4	Lahore	Above Top 20
A36	53	ACCA	26	Lahore	Top 10
A37	60	FCA, FPFA, FAIA	30	Peshawar	Top 10
A38	78	FCA, FCMA	55	Peshawar	Top 10
A39	32	CA part-qualified	7	Peshawar	Above Top 20
A40	26	CA part-qualified	4	Peshawar	Above Top 20
A41	30	CA part-qualified	5	Peshawar	Top 10
A42	40	CA part-qualified	9	Peshawar	Top 10
A43	75	FCA	50	Peshawar	Above Top 20
A44	48	CPA	18	Peshawar	Above Top 20
A45	45	CA part-qualified	10	Peshawar	Above Top 20
A46	56	FCA	12	Peshawar	Above Top 20
A47	45	FCA	8	Peshawar	Above Top 20
A48	43	FCA, CMA	9	Peshawar	Top 10
A49	32	CISA	4	Peshawar	Above Top 20
A50	61	FCA	29	Peshawar	Above Top 20

Note: This table provides background information about the interviewees. CA = Chartered Accountant (The Institute of Chartered Accountants in Pakistan); CA part-qualified = Passed at least 4 exams; FCA = Fellow Chartered Accountant; FPFA = Fellow of Pakistan Institute of Public Finance; FAIA = Fellow of the Association of International Accountants; FCMA = Fellow of Chartered Institute of Management Accountants; ACA = Associate Chartered Accountant; CPA = Certified Public Accountant; CMA = Certified Management Accountant; and CISA = Certified Information System Auditor.

ENDNOTES

¹ When relayed to commercial lenders or investors such ‘false positives’ can result in the passing up of valuable investment opportunities (Glaum et al., 2004).

² See also Tilt (2018).

³ As noted below, our interviewees are drawn from a range of accounting firm backgrounds, although Abid et al. suggest no difference in ‘big 4’ and other accounting firms in this regard.

⁴ See, e.g., Clarke (1993); Stiles and Taylor (1993); Vinten (2002).

⁵ Pakistan has at the time of writing in 2021, adopted all extant IFRS Standards other than IFRS 1 (First-time Adoption of International Financial Reporting Standards) and IFRS 14 (Regulatory Deferral Accounts). Most recently, the nation adopted IFRS 9 Financial Instruments (with an effective date of 1 July 2018). See <https://www.ifrs.org/-/media/feature/around-the-world/jurisdiction-profiles/pakistan-ifrs-profile.pdf>.

⁶ Under the Companies Act 2017 (formerly the Companies Ordinance 1984), all companies in Pakistan are required to undergo statutory audits based on standards adopted by the Institute of Chartered Accountants of Pakistan (ICAP) under the supervision of the independent Audit Oversight Board (AOB). The AOB was established in 2016 by the Securities and Exchange Commission of Pakistan (SECP) via an amendment to the Security and Exchange Commission of Pakistan Act of 1997. The functions of the AOB include: (i) overseeing and monitoring the work of ICAP’s Quality Assurance Board (QAB) and Quality Control Review (QCR) program; (ii) registering all firms that have achieved a satisfactory QCR rating via the QAB - and deregistering firms where this is not the case; and (iii) ensuring that auditing standards adopted by ICAP are aligned with IAASB standards. See <https://www.ifac.org/about-ifac/membership/country/pakistan> and Abid et al. (2018). ICAP adopted the revised 2016 ISAs as issued by the International Auditing and Assurances Board (IAASB).

⁷ According to Rezaee (2002), management fraud includes misrepresentation of material facts in financial reports, asset misappropriation, and the concealment of material facts, illegal acts, bribery and conflict of interests. In contrast, employee fraud involves embezzlement of property, breaches of fiduciary duty, theft of trade secrets and/or intellectual property, and illegal acts.

⁸ In particular, managers tend to exploit the flexibility provided by accounting principles and assumptions to report ‘expected results’ (Tiscini, et. al., 2006). Most researchers now acknowledge that the opportunities and incentives for individual gains by managers drive much of the malign activity observed in corporate reporting (Brown and Higgins; 2001; Graham et. al., 2005).

⁹ See also Glaum et al. (2004).

¹⁰ An earlier analysis by Sutherland et al. (1992) proposed a similar three-stranded model based around motive, opportunity and rationalisation. In this context, several authors suggest that as all executives are susceptible to pressures and rationalisations, the propensity to commit fraud is at its highest when the latter two characteristics combine with perceived opportunity (see Albrecht et. al., 1995; Dellaportas, 2013).

¹¹ The opportunity to minimise taxes via the exaggeration of incurred expenses that goes beyond exploitation of accounting rule ambiguity has long been recognised as a major contributing factor in financial fraud (Scholes et al., 1992) although Jennings et al. (1983) and Graham et al. (2005) note that the propensity for deliberate misstatement can also be attributed to the ease with which stock valuations can be manipulated.

¹² See also Merchant and Rockness (1994); Bergstresser & Philippon (2006) and Nelson & Below (2012).

¹³ See Watts & Zimmerman (1978); Lambert (1984); Moses (1987); Balsam (1998); Healy (1999); Nelson & Below (2012).

¹⁴ An additional spur for deliberate misreporting of financial information relates to firms’ tendency to reduce earnings figures before entering pay negotiations with labour unions (Liberty & Zimmerman, 1986; Waterhouse et al., 1993; D’Souza et al., 2000).

¹⁵ Accounting estimates are rough approximations of amounts that are to be credited or debited, but for which no accurate measurement is present; they are therefore grounded on exclusive knowledge and judgments based on training and experience (Salvioni, 2002).

¹⁶ These examples broadly overlap with earlier evidence provided by Bonner et al. (1998) who study the Auditing and Accounting Enforcement pronouncements made in the US by the Securities and Exchange Commission. See also Hemraj (2004a,b) and Beasley et al. (2000); Bell and Carcello (2000); Rezaee (2002) and Hoogs et al., (2007).

¹⁷ Palthe adopts the same terminology around the three pillars as Scott (1995). In later work (e.g. Scott, 2001; 2008) Scott changes the name of the third pillar from “cognitive” to “cultural-cognitive”, but with the same basis for its role in underpinning legitimacy (see Thornton et al., 2012).

¹⁸ Deegan (2019) suggests that there “will conceivably be an interplay” (p. 2322) between the three elements; our evidence provides some empirical support for this as set out later in the manuscript.

¹⁹ See, e.g., Bashir et al. (2011) and Nawaz et al. (2012).

²⁰ McNamara (1999), Gill et al. (2008) and others argue that interviews are particularly useful in investigations such as this, where the issues involved are complex and detailed individual perceptions required.

²¹ The use of ‘icebreaker’ questions in interviews is recommended by a number of authorities on the conduct of qualitative research, including Lofland & Lofland (1996) and Krauss (2005).

²² Etikan et al. (2016, p. 2) and others point to the appropriateness of this technique when knowledgeable responses are required, as it encourages “... expressive and reflective ...” narratives.

²³ A copy is available from the authors on request.

²⁴ Merchant (1994, p. 511) argues that Schilit “overstates” the value of his approach, particularly in an investment context, with the “basic” nature of the analysis the fundamental problem. Whilst we acknowledge the accuracy of Merchant’s criticism, Schilit’s framework is referred to in leading academic journals in varied contexts linked to financial reporting failures (see, e.g., Spathis, 2002; Defond & Hung, 2003 - who specifically cite Schilit’s arguments regarding the validity potential of cash flow figures around accruals management; Rosner, 2003; Kirkos et al., 2007; Zhou & Kapoor, 2011; Basilico et. al., 2012; and Hasan et al., 2017). The present study does not claim that the seven categories are exhaustive or represent an ideal basis for sophisticated analysis of accounting technicalities. Rather, we employ them as a basis for classification of activity types in the interview guide (and explicitly acknowledge their interactions in the narrative). The primary contribution of the paper lies instead in the audacity with which such activities appear to take place in Pakistan and the theoretical implications of the fact that it is auditors who are attesting to this behaviour despite their role in the broader financial reporting system.

²⁵ Telephone interviews provide a range of advantages relative to face-to-face interviewing (Tucker & Parker, 2019). For instance, using telephone interviews helps participants who would be inhibited in face-to-face interactions.

²⁶ The Chartered Accountant qualification in Pakistan is very challenging and time-consuming, especially for students who struggle to afford education expenses (Sulehri, 2012). Whilst students are entitled to work for an audit firm after passing four professional exams (ICAP, 2015) many students engage in an articleship in a CA firm that begins at the commencement of their accountancy schooling in order to bear the costs. Many accounting trainees in Pakistan are thus involved in audits of organisations from an early stage in their career, developing substantial practical experience even before completing their professional examinations. After working four years in practical audit, students are eligible for the award of a CA articleship from the Institute of Chartered Accountants of Pakistan although they cannot own a CA firm (see Sulehri, 2012; ICAP, 2015 and TSB, 2019). We therefore believe that inclusion of some individuals who had still to complete their professional education is consistent with our desire to seek out the views of those with substantive audit experience.

²⁷ In Pakistan, audit practice reflects ISA 700 “Forming an opinion and reporting on financial statements” which states that an audit report should be qualified if the statements do not provide a true and fair view (see Gold et. al., 2012).

²⁸ While examining the qualified reports we found reference to several of the financial frauds suggested by the auditors in the interviews. For instance, one audit firm declared in their qualified report that “...these conditions lead us to believe that the going concern assumption used in preparation of these financial statements is inappropriate; consequently, the assets and liabilities should have been stated at their realisable and settlement amounts respectively.” This reasoning indicates that proscribed behaviour around claims of ‘going concern’ status would lead to an adverse opinion being given.

²⁹ Interviewee A10 suggested that “fast-growth” firms more generally tend to “disregard ethical and moral restraints.”

³⁰ The smaller (typically family-owned) firm sector in Pakistan was not seen as immune to the emergence of financial gimmicks although the perceived extent was lower than where agency relationships were in place, given the reduced need to attract external shareholders. Several interviewees made the point that, since personal and family money is involved, there is little incentive to ‘deceive’ investors. In this context interviewee A32, a Lahore-based FCA, pointed out that: “No one would ever want to lose money or business and this [desire not to] lose their own money keeps private companies away from such gimmicks.”

³¹ Whilst many of the comments in this regard emphasised the use of financial deception to attract and retain capital, reference was also made to the propensity to complement the fraud by laying off significant numbers of employees and cutting salaries (consistent with the contention in Abrahamson and Park, 1994).

³² A “side agreement” or “side letter” is a mutually agreed document that is unrelated to any original negotiated contract, relating instead to additional transactions and obligations (Mulford & Comiskey, 2011).

³³ The economic substance notion relates to the need for a transaction to have both a substantial purpose (aside from the reduction of tax liabilities) and an economic effect (also aside from the tax effect) in order to be considered valid (Mulford & Comiskey, 2011).

³⁴ See Benston & Hartgraves (2002).

³⁵ Any entity or person related to the entity or person who is in the process of preparation of financial statements is termed a “related” or “affiliated” party and the extent to which any such transactions are “arm’s length” is relevant (IAS 24.9, 2016). The latter concept permits the market to certify that the parties to the contract are performing in their personal interest and are not under any duress from the other party (Kieso et. al., 2010).

³⁶ i.e. infrequent events that do not arise from an organisation's ordinary course of business, including losses or gains from selling a division or fixed asset, the implications of a change in accounting standards, discontinuations of operations and special write-offs (see, e.g., Pourciau, 1993; Detzler & Machuga, 2002; Doukakis, 2010; Sek & Taylor, 2011).

³⁷ Typically through the timing of special write-offs and commitment to major expenditure programmes with long-term orientations (Murphy & Zimmerman, 1993; Pourciau, 1993).

³⁸ For this type of behaviour to achieve its aims, bidder companies need to coordinate cash policies, internal control systems and corporate culture with sellers in order to avoid loopholes and fully embrace the fraudulent practices involved (Klein, 2006).

³⁹ Furthermore, International Financial Reporting Standards require organisations to prepare financial statements retrospectively in the event of changes in accounting policy, including those relating to the reporting of financial obligations (see Kieso et al., 2010).

⁴⁰ The appropriateness of accounting estimates, their application and any change in their nature inevitably relies upon the judgement of the accountant (McSweeney, 1997). Interviewees did discuss this issue in more general terms (i.e. not just in so far as it relates to liabilities) regarding financial reporting practices in Pakistan which, despite malign intention, do not necessarily violate extant rules. For example, participant A47 stated that: "Accounting assumptions can transform the overall view of financial statements; for instance, depreciation methods give different results, so using improper methods can change the whole presentation of financial statements."

⁴¹ Where the carrying value of the asset is more than its selling value (or the benefits that can be derived from the use of asset) then the asset is said to be impaired, and a provision is required for this 'impairment' loss (Kvaal, 2005).

⁴² The authors suggest two reasons for this. First, organisations that are involved in such practices try to delay investors' discovery of the questionable practices until later; and second, the behaviour lessens the degree of trust placed in the firms concerned by investors, causing difficulties in the future when attempts are made to raise new capital.