



The use of red flags in financial fraud prevention

A utilização de red flags na prevenção de fraudes financeiras

Luana Vitória Molina Leite da Silva

Nilton Cezar Carraro

Keywords: Red flags, Financial fraud, Prevention.

1 INTRODUCTION

Financial fraud has been plaguing the market for more than a century. As a result, mechanisms are created for protection and one of them has been the independent audit, safeguarding *stakeholders* from possible fraud through a systematic review of the accounts of a particular company and period. Among so many tools, one of the most used by auditors has been the *red flags*, which can be technically called flags (REINSTEIN; MCMILLAN, 2004). The *red flags* use as a principle to identify evidence of errors and fraud, and can be conceived basically through the analysis of cause and consequence. One of the most feasible ways to create and use *red flags* is through the use of key performance indicators (financial and non-financial) via information systems, seeking the largest possible volume of data, since the audit always works with samples.

2 OBJECTIVE

To test the feasibility and adherence of a new key performance indicator as a *red flag* from the evidence of risk drawn by large companies at the beginning of the year 2023.

3 METHODOLOGY

This is an exploratory research using the deductive method, seeking to test through hypotheses the construction of this new indicator. According to Creswell (2010) when combining this search with quantitative methods in multivariate analysis, there is a greater propensity for satisfactory results. To this end, several companies will be analyzed that showed signs of fraud arising from drawn risk in the year 2023. A timeline will be defined for the temporal analysis in which a survey of the growth rate and perception by independent auditors of accounting errors and frauds reported in recent years that are



related to drawn risk will be carried out, as well as the impacts that the findings of frauds have influenced the reliability of a given sector. After applying the key performance indicator objective of this work year by year, multivariate statistical tests will be applied to prove its adherence.

4 DEVELOPMENT

Initially, a broad theoretical review will be conducted on fraud involving drawn risk in the national and international literature to identify the state and stage of knowledge on the subject. According to Albrecht (2011) this is the principle for a study of this nature. After this step, the main publicly or privately held companies will be identified, listed or not on the B3 (Brazilian Stock Exchange), which presented some indication of fraud in this regard, and then the financial statements, management reports and audits will be surveyed in order to conduct a fundamentalist analysis. Seeking a relationship between cause and consequence the creation of the indicator will be proposed, given that there is already an inference for the same allowing a conception about it. Subsequently, the procedures described in the previous section will be applied to prove the adherence of this new indicator that intends to be launched to the market as a new possibility of use by independent auditors as a *red flag*. Finalizing the research and supported by the findings of Carraro et al. (2020), the use of more and new *red flags* in the information systems used by auditees will allow amplitude to the auditors' work and consequently greater reliability to their reports.

5 CONCLUDING REMARKS

This contribution is expected to allow a new way of evidencing errors and frauds in drawn risk, since the existing taxonomy, among them the current legislation, was not enough to restrain abusive practices by certain companies, generating billionaire losses to several *stakeholders* and mainly casting new doubts on the practices exercised by the market, especially that of the independent auditors. Therefore, the use of *red flags* proves to be an important tool to detect scenarios that are favorable to the emergence of fraudulent acts, in addition to signaling risk situations before they become an aggravating factor and cause financial damage.



REFERENCES

ALBRECHT, S. Fraud Examination. Editora South-Western College Pub, 2011.

CARRARO, N. C.; ALMEIDA, O. A. I.; SIQUEIRA, L. C.; SOUSA, M. A. B. Construto para utilização prática de red flags em auditoria. Revista Científica Hermes, v. 27, p. 361-377, 2020.

CRESWELL, J. W. O projeto de pesquisa: métodos qualitativo, quantitativo e misto. 3. ed. Porto Alegre: Artmed, 2010.

REINSTEIN, A.; McMILLAN, J. The Enron debate: more than a perfect storm. Critical Perspectives on Accounting. Article in the press, 2004.