

THE IMPACT OF BOARD'S CHARACTERISTICS ON INTERNAL CONTROL WEAKNESSES AND FRAUD IN FINANCIAL STATEMENTS BASED ON THE FRAUDULENT INCENTIVE OF MANAGEMENT

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ABSTRACT

Control over financial reporting and reporting weaknesses with internal significance based on the statement of Tehran Stock Exchange Organization, and designing an effective internal control system to realize the micro and macro objectives of the company is very important. The individual and social characteristics of the board of directors are very significant factors in accomplishing their goals and tasks at the level of company and society. In this research study, the impact of board characteristics on the relationship between internal control weaknesses and fraud in financial statements has been examined. To this aim, the data of 113 companies which were members of the Tehran Stock Exchange from the years 2012 to 2017 have been used based on the limitations. In this investigation, in order to examine the subject of the research, two main hypotheses have been used, which included 12 sub-hypotheses. Research hypotheses have been investigated using the Eviews software version 10 at 95% confidence level and the results have been presented. Research variables include (dependent-independent-control and moderator). Based on the results obtained from testing the hypotheses, it can be concluded that there is a direct and significant relationship between the weakness of internal controls and fraud in financial statements, and there is an inverse and significant relationship between the characteristics of independence and financial expertise of the board of directors and fraud in financial statements.

Keywords: Board characteristics, internal control weaknesses, fraud in financial statements

INTRODUCTION

One of the major concerns of managers, board of directors, business owners and internal auditors is how to establish an internal control system and deal effectively and efficiently with the risk of fraud at the level of organization and company. An efficient internal control system is the primary tool for identifying and revising fraud. The extension of activities of business units and organizational complexity has led the managers of these groups to rely on internal controls to achieve the goals of the organization and prevent fraud and collusion and waste of the organization's resources and ensure the optimal allocation of resources.

Issues related to the characteristics of the board of directors, internal controls and their weaknesses, fraud in financial statements and examining its various factors and aspects have always been challenging topics for investors and financial analysts.

The existence of internal auditing is an undeniable necessity for strengthening corporate governance, improving the internal control system, assisting strategic risk management, and ensuring transparency in reporting at the internal and external levels of the organization.

Management authority is allowed to choose the criteria for the importance of the company's internal control. In this regard, financial statements assist users to make economic decisions to achieve the expected output by providing an image of the financial situation and performance of the companies. Profit and loss statement is of importance for users of financial information because of the useful information it provides about the profitability of business units.

Detecting fraud has long been regarded by independent internal auditors and professional institutions and accordingly, the emphasis of these professional institutions and auditing standards is on correcting the organizational structure and the improvement of the internal control system and the performance of continuous and regular audits to reduce the risk of fraud and increase the validity of financial reports.

According to the audit standard no.240, fraud is any intentional act by one or more executives, management bodies, employees or third parties that entails cheating to attain an illegitimate or illegal advantage. Fraud often occurs in three forms: financial corruption, misuse of assets, and fraud in financial reporting.

Recent development in research studies on the structure and decision-making process of the board of directors require further study of the impacts of behavior and the characteristics of the board on organizational outputs. Research studies conducted on the characteristics of the board of directors also confirm the significance of these features in adjusting issues arising from agency and corporate governance, realizing the rights of stakeholders, reducing agency costs and financial costs, adjusting financial leverages, the role of deterrence against financial scandals and also its important role in corporate governance issues. This research can be useful in scrutinizing the economic impacts of financial events and operations, the status and performance of the business unit, predictions and decisions, for investors and the stock exchange organization, as well as policy-making institutions in adopting investment and management policies. Additionally, this study can be useful for other people such as small investors and organizations such as the privatization organization, etc. This research also makes it possible to compare companies with specific characteristics chosen in this research with other similar and non-similar companies in different time intervals.

Based on the studies conducted on research records in universities as well as scientific sites, although several studies have been conducted in and outside the country on the variables tested in this study, but the effect of board characteristics on internal controls and fraud in financial statements (the subject of the present study) has not been specifically and directly addressed in any research. Clarifying the various dimensions of the present study seems to be a useful step towards to complete the literature related to this issue in the economic environment in the Iranian market.

The main purpose of this study is to explain the effect of board characteristics on the weaknesses of internal controls and fraud in financial statements. In other words, this study answers the question of what is the impact of the board's characteristics on internal controls and fraud in financial statements?

THEORETICAL FRAMEWORK OF THE RESEARCH



The board of directors is the most important factor in controlling and supervising the company's management and is responsible for protecting the interests of stockholders (agency theory). Also, the major responsibility of the board of directors is to create an efficient management of the company's affairs in line with the interests of stockholders and make the balance in the interests of different stakeholders, including customers, employees, investors and local communities.

In fact, the financial crisis is the failure of risk management in business relationships. Studies conducted by financial institutions in the United States indicate that the characteristics associated with the board's decision-making process have a negative impact on risk management decisions. Calstein et al. (2009) argue that recent research advances in the structure and decision-making process of the board of directors require further study of the effects of the board's behavior and characteristics on organizational outputs.

It is widely believed when the board has more independence, it more effectively supervises over executives. Internal controls and the effective characteristics of the board of directors are major components of a strong corporate governance that can be seen as a control tool that limits management's incentives to manipulate, falsify, and fraud financial statements.

Internal control is a fundamental and dynamic process that constantly makes itself harmonious and consistent with the changes fronting the organization. Management and employees at all levels are required to be associated with this process in order to identify risks and gain reasonable assurance of achieving the organization's mission and overall objectives. In other words, internal controls are a set of actions that managers take to ensure relative reliability and compliance with established regulations and policies to increase the efficiency and effectiveness of operations and attain predetermined objectives. Weaknesses in internal control include anything that affects or interrupts an organization's objectives and management decisions.

Numerous criteria have been suggested to examine internal controls and assess weaknesses related to these controls. One of the most important criteria mentioned in this study is the fraudulent management incentive. Implementing stronger internal controls and the board of directors, with specific features and characteristics, including independence and financial expertise, leads to the presentation of better reports and improved disclosure of notes and explanations, as well as financial statements.

The subject of the current study is the impact of the characteristics of the board of directors on the weaknesses of internal control and fraud in financial statements in companies accepted in the Tehran Stock Exchange. According to the studies conducted in this field, it can be stated that companies that have stronger and more efficient internal controls have provided more reliable and convincing financial statements and there has been less distortion and fraud in such companies. Numerous studies have also pointed to the characteristics of the board of directors that affect fraud in financial statements and the weakness of internal controls, and it has been mentioned that independence is the most important feature. These studies declared that there was a significant and inverse relationship between board independence and fraud in financial statements.

RESEARCH METHODOLOGY

This research is descriptive and correlational and is applied regarding its purpose. In this research study, the statistical population including all companies in all industries and disciplines



listed in the Tehran Stock Exchange has been extensively studied. Statistical information and data is related to the companies considered in the statistical sample in the period of 2012 to 2017. In this research, a systematic removal method has been used for sampling that the criteria applied for sample selection are as follows:

- A. Companies should be among the companies present in the Tehran Stock Exchange.
- B. Companies must have been listed in the stock exchange before 2012.
- C. The required information from 2012 to 2017 should be available.
- D. The fiscal year of all companies should be ended on March 20.
- E. Companies should not be among banks and financial institutions (financial intermediation companies, investment companies, insurance companies and holdings, etc.).
- F. Companies should not have a trading break of more than six months.

Finally, after applying the limitations and related filters, 113 sample companies were selected for investigation.

Regression models to test hypotheses:

Model 1

Model 2

Model 3

Model 4

Data collection methods and tools

To collect information about the research literature, library and documentary studies have been conducted, and information on the financial statements of companies listed on the Tehran Stock Exchange has been used to obtain the information needed to process research hypotheses. Using the Rahavard No software, Codal, Tedan and other resources systems, including Tehran Stock Exchange technology management, the required data has been extracted and then the variables have been calculated in Excel.

Measuring Independent variable (internal control weakness with the symbol of Control weakness):

In order to measure weakness in internal controls, as an independent variable, important weaknesses of internal controls are used, which are obtained from the report of independent auditors. According to the checklist of internal controls prevailing the financial reporting of the Stock Exchange Organization, since 2012, the company's auditor has been required to investigate the internal controls of the company and to disclose the cases that indicate that the internal controls are not observed or not to properly implemented in the audit report. Thus, the focus of the current study is on the following clauses of the legal responsibilities of companies' auditing reports.

Measuring moderator variables (board characteristics):

First Feature: Board independence with the symbol of BOARDIND: The ratio of non-executive board members to total members

Second Feature: Financial expertise of the board with the symbol of BOARD Knowledge: The ratio of members in the board with financial expertise to all members

Third Feature: the tenure of the CEO with the TENURE symbol: the number of years that a manager has been the CEO in the company.

Control variables and how to measure them

Company size: In several studies, it shows various aspects of the company. The size of the company can indicate a competitive advantage. The size of the company can indicate the management ability and the quality of accounting plans. In the current study, the size of the company is equal to the logarithm of the book value of the total assets of the company shown with the symbol of SIZE.

Financial leverage: The simplest definition of financial leverage is that financial leverage is the amount of debt that a company undertakes to buy more assets. In fact, this ratio determines the extent to which the company has met its financial needs from other sources. The financial leverage is equal to the sum of the company's debts divided by the company's assets shown with the symbol of LEV.

Asset Efficiency: Return on assets (ROA) indicates how much a company's profitability is related to its total assets. So, it is equal to the net profit divided by the sum of the company's assets shown with the symbol of ROA.

Loss: means the loss of all or part of an asset or an increase in debts. In this study, if the company reported a loss, the value is equal to one, otherwise, the value becomes zero, shown with the symbol of LOSS.

Dual responsibility of the CEO: If the CEO is also the chairman of the board of directors simultaneously, the value number is one and otherwise, the value is zero shown with the symbol of DUALL.



Conceptual (schematic) model of the research

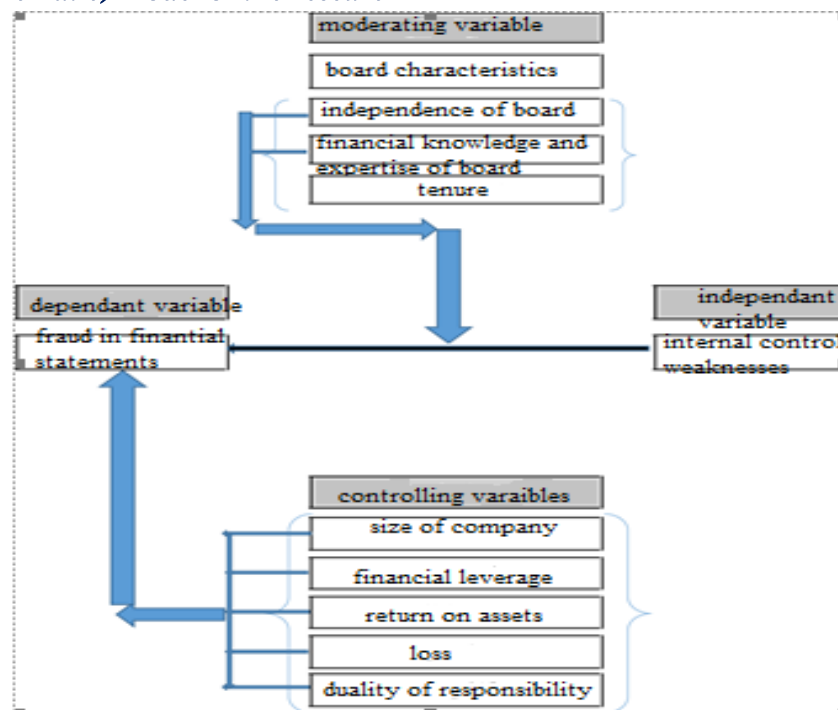


Figure 1- Conceptual model of the research

Data analysis method

In this study, the data related to the companies listed on the Tehran Stock Exchange after being collected from reputable sources, was entered in the Excel software for the relevant calculations, and it was analyzed by Eviews software using mathematical models and presented in two sections of descriptive statistics and inferential statistics. In the section of descriptive statistics, the minimum, maximum, average and standard deviation values of the variables were examined, and a distribution table was presented for the qualitative variables. In the section of inferential statistics, regression estimation models and fitness criteria were first evaluated. Data is executed through Eviews software version 10 at 95% confidence level and the results are presented. In each of the regression tests, the method of selecting appropriate method for estimating and establishing the basic assumptions of regression has been considered in order to achieve valid results.

RESULTS AND FINDINGS**Descriptive Findings**

In order to examine the general characteristics of the variables and analyze them accurately, it is necessary to get familiar with the descriptive statistics related to the variables. Table (1) displays the descriptive statistics of the data related to the variables used in the research. Descriptive statistics are related to 113 sample companies over a period of 6 years (2012-2017).

Table 1. Descriptive Statistics of Research Variables

Variable Name	Number	Mean	Minimum	Maximum	Kurtosis	Standard Deviation	Skewness
First Criterion of Fraud							These values do not make sense for a qualitative variable
Second Criterion of Fraud							
Third Criterion of Fraud							
Internal Control weakness							
Independence of the board							
Knowledge of the board							
Tenure of the CEO							
Size of the company							
Financial Leverage							
Return on Assets							
Loss							These values do not make sense for a qualitative variable
Duality of responsibility							

The average value for the variable of return on assets is equal to (0.162), which indicates that most of the data is concentrated around this point. In other words, most of the examined companies made about 16 percent of their profits. The value of the standard deviation for the size of the company is equal to 1,541 and for the return on assets, it is equal to 0.124, which shows that these two variables have the highest and lowest standard deviations; respectively. The minimum and maximum amount of independence of the board of directors is zero and one. This means that there are companies in which there are no dormant member and all members are executive.

Inferential findings

Reliability test

Table 2. The reliability test of non-qualitative (quantitative) variables

Variable Nmae	Test statistic of (Dickey-Fuller)	Significance Level (prob)	result
Independence of the board			is reliable
Knowledge of the board			is reliable
Tenure of the CEO			is reliable
Size of the company			is reliable
Financial Leverage			is reliable
Return on Assets			is reliable



As can be seen in Table 2, the significance level of the variables is less than 5% and indicates that the variables are reliable.

Results of Research Hypothesis

In the following, the results of each of the research hypotheses have been presented with a logistic model.

Null Hypothesis: There is no relationship between weak internal control and fraud in financial statements.

Opposite Hypothesis: There is a relationship between weak internal control and fraud in financial statements.

As three criteria have been used to measure the weakness of internal control, the first main hypothesis has been tested in the form of three sub-hypotheses.

- Sub-hypothesis: There is a relationship between internal control weakness and fraud in financial statements (the criterion of fraudulent management incentive).

Analysis of control variables: The control variables of the size of the company and the duality of the CEO's responsibility have a significant level of more than 5%, so they do not have a significant effect on the dependent variable. The variables of financial leverage, return on assets and loss have a direct and significant effect on the dependent variable.

Table 3. Final estimation of sub-regression model 1

Variables	Coefficients	Standard Deviation Coefficients	z-Statistic	Significance level	result
Internal Control weakness					is significant
Size of the Company					is not significant
Financial Leverage					is significant
Return on Assets					is significant
Loss					is significant
Duality of responsibility					is not significant
intercept					is significant

According to the results of Table 2, it is observed that the weakness of internal control has a positive coefficient and a significance level of less than 5%, therefore, it can be claimed that there is a direct and significant relationship between the weakness of internal control and fraud in financial statements (the criterion of fraudulent management incentive) and sub-hypothesis 1-2 is accepted.

Analysis of control variables: Control variables of company size, return on assets and loss have a significance level of more than 5%. So, they do not have a significant effect on the dependent variable. The variables of financial leverage and dual responsibility have a direct and significant effect on the dependent variable.

Null hypothesis: Board characteristics have no impact on the relationship between weak internal control and fraud in financial statements.

Opposite hypothesis: Board characteristics have an impact on the relationship between internal control weakness and fraud in financial statements.

Considering that three criteria have been used to measure the weakness of internal control and 1 criterion has been used to measure the characteristics of the board of directors, therefore, the second main hypothesis has been tested in the form of 3 sub-hypotheses.

- Board independence has an impact on the relationship between internal control weaknesses and fraud in financial statements (the criterion for fraudulent management incentive).
- Financial expertise of board members has an impact on the relationship between internal control weaknesses and fraud in financial statements (criteria for fraudulent management incentive).
- The tenure of the CEO has an impact on the relationship between internal control weaknesses and fraud in financial statements (the criterion for fraudulent management incentive).

Table 4- Final estimation of sub-regression model 2

Variables	Coefficients	Standard Deviation Coefficients	z-Statistic	Significance level	result
Internal Control weakness					is not significant

Independence of the board					is not significant
Independence of the board and Internal Control weakness					is significant
Size of the Company					is not significant
Financial Leverage					is significant
Return on Assets					is significant
Loss					is significant
Duality of responsibility					is not significant
intercept					is significant

According to the results of Table 4, it is observed that the moderating effect (board independence * internal control weaknesses) has a negative coefficient and a significance level of less than 5%. So, it can be stated that the independence of the board of directors has an inverse effect on the relationship between internal control weaknesses and fraud in financial statements (the criterion of fraudulent management incentive).



Table 5- Final estimation of sub-regression model 2

Variables	Coefficients	Standard Deviation Coefficients	z-Statistic	Significance level	result
Internal Control weakness					is significant
Knowledge of the board					is not significant
knowledge of the board and Internal Control weakness					is significant
Size of the Company					is significant
Financial Leverage					is significant
Return on Assets					is significant
Loss					is not significant
Duality of responsibility					is not significant
intercept					is significant

According to the results of Table 5, it is observed that the moderating effect (board knowledge * internal control weaknesses) has a negative coefficient and a significance level of less than 5%.

So, it can be stated that the knowledge of the board of directors has an inverse effect on the relationship between internal control weaknesses and fraud in financial statements (criteria for fraudulent management incentive).

Table 6- Final estimation of sub-regression model 3

Variables	Coefficients	Standard Deviation Coefficients	z-Statistic	Significance level	result
Internal Control weakness					is significant
Tenure of the CEO					is significant
Tenure of the CEO and Internal Control weakness					is not significant
Size of the Company					is not significant
Financial Leverage					is not significant
Return on Assets					is significant
Loss					is not significant
Duality of responsibility					is not significant
intercept					is not significant

Based on the results of Table 6, it is observed that the moderating effect (Tenure of the CEO * Internal Control Weaknesses) has a significant level of more than 5%, therefore, it can be stated that the tenure of the CEO does not affect on the relationship between internal control weaknesses and fraud in financial statements (criteria for fraudulent management incentive).

Goodness of fit tests

When the dependent variable is of two values, there are different criteria for assessing the goodness of fit of the models, which have been examined below.

McFadden coefficient and the statistic of LR likelihood

The value of the McFadden coefficient is always between zero and one, and its larger size means the higher fit of the model. Also, if the value of the statistic of likelihood has a significant level of less than 5%, at the 95% confidence level, it can be stated that the fitted model has sufficient validity.

Table 6. The results of McFadden coefficient and the statistic of LR likelihood

It is observed that in Hypothesis 1 of the research, independent and control variables have been able to explain 39% of the changes in the dependent variable, also, the significance level of the statistic of likelihood is less than 5%, so it can be stated that the fitted models have sufficient validity.

Hosmer-Lemshow and Andrews Test

Another goodness of fit measure in two-value dependent variables is Hosmer-Lemshow and Andrews test. In this test, the class of observations is classified based on the value of fitness of the dependent variable (divided by the desired number), such as ten decimals (and in each classification, the actual values of the dependent variable are compared with the adjusted values). The statistical rule of this test is as follows:

Null Hypothesis: Optimal fitness (actual values = fit values)

Opposite hypothesis: Non-optimal fitness (actual values \neq fit values)

Table 7. The Results of Study Hypotheses

Model Name	Hosmer-Lemshow Test		Andrews Test	
	Significance level	Test statistic	Significance level	Test statistic
Sub-hypothesis (model) 1				
Sub-hypothesis (model) 2				
Sub-hypothesis (model) 3				

Based on the results of Table 7, it is observed that the significance level of Hosmer test is more than 5% and it indicates the optimal fitness of the model.

DISCUSSION AND CONCLUSION

Behavioral, individual, and social characteristics of the board of directors play an important role in stock pricing and the expectations of investors and stockholders. Internal controls and their related weaknesses, as stated in the reports of the board of directors and other reports of the economic unit, are also interesting for investors, stockholders and other interested parties and help them very much in making decisions. In this research, it was tried to investigate the effect of board characteristics on the weaknesses of internal controls and fraud in financial statements to find out the relationship between them and explain and measure this relationship using various tools.

The controlling variables of company size and the duality of the CEO's responsibility have a significance level of more than 5% and therefore do not have a significant effect on the dependent variable. Financial leverage variables have an inverse effect, return on asset and loss have a direct and significant effect on the dependent variable.

Based on the results of the research, it is observed that the weaknesses of internal control have a positive coefficient and a significance level of less than 5%. So, it can be said that there is a direct and significant relationship between the weaknesses of internal control and fraud in financial statements (the criterion of fraudulent management incentive) and the sub-hypothesis is confirmed.

Based on the obtained results, the moderating effect of (board independence - internal control weaknesses) has a negative coefficient and a significance level of less than 5%. Therefore, it can be stated that the independence of the board of directors has an inverse effect on the relationship



between internal control weaknesses and fraud in financial statements (criteria for fraudulent management incentive).

Based on the results of the research, the moderating effect of (knowledge of the board of directors-weaknesses of internal control) has a negative coefficient and a significance level of less than 5%. Therefore, it can be said that the knowledge of the board of directors has an inverse effect on the relationship between internal control weaknesses and fraud in financial statements (criteria for fraudulent management incentive).

Also, the moderating effect of (CEO's tenure - internal control weaknesses) has a significance level of 5%. Therefore, it can be stated that the CEO's tenure does not affect the relationship between internal control weaknesses and fraud in financial statements (criteria for fraudulent management incentive).

The structure of the board of directors and the composition of its members in relation to the issue of corporate governance has been the focus of much research, because the activities of the board of directors and their decisions are directly related to the financial and economic performance of the organization. Therefore, explaining the structural factors and characteristics of the board of directors is a significant question for company owners.

In 2016, Beglou and Mahmoudi conducted a study entitled "The Impact of Internal Controls on Financial Violations of the Executive Bodies in West Azerbaijan Province". In this study, the effect of five components of internal controls including: control environment, risk assessment, control activities, information and communication and monitoring along with the main limitation of internal controls (establishment costs) on the amount of financial violations of West Azerbaijan province organizations has been investigated. The results of testing the hypotheses show a significant effect of the establishment costs and all components of internal control on financial violations, which have the greatest impact on the control environment, establishment cost, control activity, monitoring and risk assessment; respectively.

In 2017, Hajiha, Oradi and Salehabadi conducted a study entitled "Weakness in Accounting Controls and Delay of Audit Report ". The purpose of this study is to investigate the effect of weakness in internal controls on the delay of audit reports in companies listed on the Tehran Stock Exchange. To this end, the research data were tested between 2012 and 2015. The research findings reveal that there is a significant relationship between weakness in internal controls and delays in audit reports. In other words, the lack of weakness in internal controls is related to the timely audit reporting.

In 2017, Dadashi, Kord Manjiri and Baradaran, conducted a study entitled "The impact of internal audit structure on the probability of fraud in the financial statements of companies listed on the Tehran Stock Exchange". The purpose of this study was to investigate the effect of structural features of the internal audit unit on the probability of fraud in financial statements. The findings indicated that the experience and tenure of the internal auditor have negative and positive effects on the probability of fraud in the financial statements of the examined companies; respectively. However, no significant effect was observed by other internal audit characteristics on the probability of fraud in financial statements.

In 2017, Amiri and Hajiha have conducted a study entitled "Investigating the relationship between the activities of the audit committee and the quality of the internal control system in companies listed on the Tehran Stock Exchange". The results of the 95% confidence level survey presented that there is a significant relationship between the size of the audit committee and the



type of audit firm with the quality of internal control. Also, the number of members of the audit committee has had a significant relationship with the quality of internal control (weakness at the general level). Finally, the type of audit firm adjusts the relationship between the activities of the audit committee (the number of members of the audit committee) and the quality of internal control (weakness at the general level and weakness at the income level). Based on the results of testing the hypothesis, it can be concluded that the size of the audit committee and the type of audit firm affect the quality of internal control. Though, considering the number of members of the audit committee, this impact has not been effective in the internal control criteria and its indicators. Therefore, it is suggested that the number of members of the audit committee be increased and stricter laws be legislated to require all companies to have an audit committee.

In 2017, Saedi and Dastgir have conducted a research study entitled "The impact of weak internal controls and the disagreement between control stockholders on the investment efficiency of companies listed on the Tehran Stock Exchange". The statistical population of this study is the companies listed on the Tehran Stock Exchange from 2009 to 2015. The results indicated that there is a significant relationship between the disagreement between control stockholders and investment efficiency. In other words, as the disagreement between control stockholders increases, so does investment inefficiency. There is also a significant relationship between the weakness of internal controls and the efficiency of investment, in the sense that if there is a weakness of internal controls or an increase in its number, the inefficiency of investment will increase.

In 2018, Hemmati and et al., conducted a study entitled "Internal controls: a continuous link to the financial reporting chain". In this study, the role of internal controls in the financial reporting chain has been explained and a new model in relation to internal control of financial reporting environment has been presented. This study considers the financial reporting process as a three-step activity and examines the impact of internal controls on each component of the process.

A study was conducted by Kao and Lou from China on individual characteristics of board members and internal control weaknesses. In this study, the relationships between the individual characteristics of the board of directors and the weaknesses of internal control are examined using data from companies listed in China from 2007 to 2018. The results reveal that the individual characteristics of board members, including training, experience, certification, integrity and training, are related to the lack of internal controls. These results also show that the individual characteristics of the CEO of the board are related to internal problems. These results also indicate that the individual characteristics of the CEO of the board are related to internal problems. The overall results show when the quality of internal control is better, weaknesses in internal control are reduced, and weaknesses are more corrected in companies where board members and CEO have greater degree (capability). In addition, ownership has a moderating effect on the relationship between board characteristics and internal control. However, the behavior of the board does not mediate the relationship between the board members and the internal control.

Wu and Wang's (2018) study was conducted entitled as "Important measures of management's weaknesses in internal control and corporate fraud". The present paper examines the determinants and consequences of the first-accepted decisions of Chinese companies regarding important criteria for the weakness of internal control that can be seen from the 2011 annual



report. Although pre-tax income is the most common measure of importance, income is used as a popular option. Income is more subject to manipulation because it has a larger financial value compared to pre-tax income. We contend that immoral managers do not disclose significant weakness through manipulating the standards to justify not disclosing potentially significant weakness.

Based to the results of this research study, and stating that the characteristics of the board of directors affect on the weaknesses of internal control and fraud in financial statements, it is suggested that in selecting the members of the board of directors, the features mentioned in this research and the general assembly of the companies should be considered by the stockholders.

Due to the fact that the characteristics of the board of directors affect on the weaknesses of internal controls and fraud in financial statements, investors and creditors are advised to consider the characteristics of the board of directors in this research in making their decisions.

Based on the results of this research, there is a relationship between the characteristics of the board of directors and the weaknesses of internal control and fraud in financial statements. It is suggested that in the ranking of companies which are the members of stock exchange, the characteristics of the board of directors (effective and significant factors) should be considered as an important factor.

Due to the impact of the research model and based on the hypotheses and results of the research, it is suggested that the impact of other features of the board of directors on internal controls be considered in the future research studies.

Also, based on the results of the research, it is suggested that in the future research, the effect of the characteristics of the board of directors on the quality of financial statements and its dimensions be discussed.

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