

## TOSHIBA

### Accounting Fraud – Case Study

#### 1. How can the fraud triangle be applied to explain Toshiba's fraud and reveal the motives behind it.

Looking at the fraud triangle we can identify for each aspect a couple of facts that were contributing elements in the Toshiba accounting fraud case.

##### **FINANCIAL PRESSURE:**

From the investigation report, it is obvious the fact that the incompetent accounting policies were initiated during the 2008 global financial crisis, which stimulates the CEO at that time to take steps that could draw the corporation during the tough times. The pressure culminated and dimmed itself and evidently went out of the sphere of correct policies and procedures and gravitated towards the last resort, which was to achieve the target in exchange of anything.

The subsequent CEO and directors were put into the shoes and designations which was not only colossal to live upto, but also submerged into the fraudulent activities, that continuing in the same direction seems easier than enabling some ground breaking changes, as always the culture of the corporation proved to live upto.

##### **OPPORTUNITY:**

Indulging into malpractice found the global crisis to be a perfect platform, as the fear on unemployment and laying off arise in the minds of the workers and employees, it was a step easier to enforce harsh policies that demanded profits no matter what, with the knowledge that it will eventually

lead to fraud policies adaptations and inflated results. Eventually, it embedded itself as a hardcore system, with little to no room for sophistication and following culprits harvest the forbidden fruit.

### **RATIONALIZATION:**

The difficulties of the global crisis became excessive, for a corporation of 140 years history, intended to flourish and leave behind a legacy of centuries. It was an impediment for the corporation to handle without removing its significant market share, therefore in order to hinder the same, the CEO found it in the best interest of the company to ultimately salvage it from the crisis, irrespective to the damage it may possess on its accounting policies, procedures and practices.

### **PROBABLE REASONS BEHIND THE ACCOUNTING SCANDAL:**

The 2008 financial crisis threw everyone out of their games, including Toshiba, but the legacy and enormous market share was at risk and at stake, the situation demanded tremendous steps. Forgetting where the boundaries stood, the CEO, in full awareness, took steps and enforced policies which were clear, to be the stepping stones into the fraudulent practices that spread over the whole organisation.

When the scandal was brought to light, we saw that CEO Hisao Tanaka and seven other directors took forceful resignations. The report of the investigation committee clearly points that the initial footprints were laid down during the time of CEO Atsutoshi Nishida during the financial crisis of 2008.

The subsequent leaders and directors were living the glorified mirage that was pre-established, and once they came to realizing the truth, it was too difficult to present in any other way, given the incapability of the workers to raise their voices against the management, was motivation enough to lead Toshiba in the direction it was heading in the context of the financial crisis of 2008.

It is difficult to believe that there have been no early signs that did not indicate towards the building scandal or misappropriation that had the complete potential to magnify in the face of the top management. Toshiba Corporation accumulating profit should have raised some red flags while the

competitors ran in losses and decline. Moreover, the faulty accounting practices over the period of 2008 to 2015 makes it crystal clear that the people next in the leadership indulged themselves further rather than bringing the matter onto light, way before it actually came into the spotlight.

The negligence or purposeful negligence on the part of the security controller or the exchange of Japan also comes up, as they took action too late to point fingers at a situation which had already gone beyond the grandiose proportions.

## **2. What are the issues at Toshiba from the point of view of its stakeholders (especially the investors).**

In my opinion, Toshiba did not maximize the 400.000 shareholders wealth by reporting revenue numbers that were much higher than actual numbers. This strategy may have profited stockholders in the short-run, but in the long run did not profit stockholders because they were forced to report their losses, which drove stock prices down. They did not act within the constraints of the law by illegally reporting fake numbers, and incorrectly using the percentage-of-completion accounting principle. For these reasons, Toshiba's actions can be declared unethical.

Overall, Toshiba's stakeholders are unhappy, then the consumer electronic employees who lost their jobs because of this scandal, along with their families, are the unhappiest. Not to mention the customers who bought those consumer electronic products because they will no longer be able to buy Toshiba products.

Toshiba's stockholders are disappointed because the fraud caused the stock price to drop 38% over eight months. The Toshiba executives along with their criminal actions that resigned because they were traced into the scandal being exposed and forced to apologize to their stockholders and customers are another example of unhappy stakeholders. Due to Tanaka's managerial policy of personnel rotation after every few years regardless of the situation in their department, Toshiba allowed their successors to take charge and be accountable for the losses of projects in a system obviously based on losses and not on setting goals that probably brought high levels of frustration internally. Most likely, the

employees in the accounting department are unhappy because their seven yearlong scheme was exposed and corrected.

Probably the only relatively happy stakeholder is Japan's Securities and Exchange Surveillance Commission because they successfully identified and reported Toshiba's accounting errors.

Overall, the interests of the stakeholders were not met and therefore their happiness was not intended, by these unethical actions.

### **3. What are the ethical issues in this case? What would you do if you were in the same situation as the Toshiba employees?**

Investigators found evidence of inappropriate accounting techniques that were booking future profits early, pushing back losses, pushing back charges, and other similar techniques that resulted in overstated profits. From the Toshiba case we learn how the corporate leadership handed down strict profit targets to business unit executives, often with the clear message that failure would not be accepted. For example, quarterly Challenges were handed down near the end of the quarter when there was no time left to materially affect unit performance. It is clear within individual business units that the only way to achieve these Challenges was to do so through the use of inappropriate accounting techniques. To meet its profit targets, Toshiba implemented a plan to carry over and overstate profits by adjusting profit and losses, used a cash-based method instead of accrual method for its accounting.

I believe that this case has to be analysed and looked carefully from the cultural perspective as it has an essential role in allowing the fraud to expand and remain unrevealed. Toshiba's corporate culture demanded obedience to superiors, an important factor enabling the emergence of fraudulent accounting practices. They operated on the level of business unit executives and every level of authority down the chain to the accountants who ultimately made use of the accounting techniques.

The ethical theories overlook the position of the accounting department employees, who were being left to choose between acting ethically and maintaining their job. No employee should ever be in such

a position. For that reason, I do not fault the accounting department employees for the fraudulent activity they obeyed to carry out.

#### **4. What options are available for the company moving forward? How can it prevent such fraud in the future?**

- Toshiba should consider a reformation of the corporate culture, elimination of the profit targeting system, reestablishment of internal controls and strong corporate governance and promote a secure environment where people have no fear, feel free to raise the flag and confess any abnormality encountered.
- Employee Reporting Systems in order to have full knowledge and access to employee's information. Their reporting, working hours, capacity, result orientation and their level of interest in the organization should be known to the executives and accounting managers.
- Clear Standards that should act as a motivator, and not as a threat, because the difference between the two, changes the mindset of the employees working to achieve the same. They represent a tool to work with and not against them.
- Independent internal control audit is a must for Toshiba to assist in internal check, highlighting the areas that need further improvement or assistance. It is of extreme importance, that the internal check imposed in a corporation of such size is subjected to independent third party audit, which can provide to the management a honest report.
- Marginal costing or management accounting that proved to be efficient and result oriented methods to achieve desired result, without compromising standard rules or accounting policies.