

Analysis of financial fraud cases based on Fraud Triangle Theory

-- A Case Study of Blue Mountain Technology

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Abstract: In recent years, the frequent occurrence of financial fraud in listed companies has caused a huge impact on enterprises and investors. In this paper, Beijing Blue Mountain Technology Co., LTD. (hereinafter referred to as "Blue Mountain Technology") as an example, through the fraud triangle theory, from the pressure, opportunity, excuse three aspects of in-depth analysis of the financial fraud of Blue Mountain Technology motivation, and put forward targeted preventive measures.

Keywords: Blue Mountain Technology, Fraud triangle theory, Financial fraud.

1. Financial Fraud and Fraud Triangle Theory

1.1. Financial fraud

Financial fraud refers to that enterprises intentionally alter the data or notes listed in financial statements in order to deceive the users of financial reports. Financial report fraud includes forgery, fabrication and falsification of the financial statements of the voucher data and other behaviors. Internal control defects, frequent related transactions, frequent management changes, excessive concentration of equity are the main manifestations of corporate financial fraud.

1.2. Fraud triangle theory

Fraud triangle theory mainly refers to the enterprise with pressure factors and opportunity factors and excuse factors to achieve financial fraud, the relationship between the three is mutual, the pressure can be understood as the enterprise input financial fraud motivation, can be understood as the opportunity to implement financial fraud conditions, excuse is self-rationalization excuse, its essence is the lack of loyalty. To find a more reasonable explanation for their forgery.

1.2.1. Pressure factors.

Often, stress comes from a combination of internal and external factors. Internal pressure refers to the financial situation of the enterprise is difficult at the same time the operating condition is poor, leading to the break of the enterprise capital chain, and the enterprise is in urgent need of development, will have the motivation to implement financial fraud. The external pressure usually comes from the capital market. If enterprises want to further develop in the capital market, they are in urgent need of a large amount of financing. However, due to the poor financial operation condition, it is difficult to obtain financing, which greatly increases the possibility of enterprise fraud.

1.2.2. Opportunity factor.

Enterprise internal opportunities usually refer to the ownership structure is not reasonable, the internal control system in a vacuum, the professional quality of financial personnel is not enough, internal audit system loopholes and other aspects of the enterprise caused by the conditions of

fraud. External opportunities usually refer to the existence of audit loopholes in external audit institutions, adverse supervision by external regulators, and imperfect capital market system.

1.2.3. Excuse factor.

It refers to the financial personnel under the pressure of fraud, find the appropriate opportunity, find a reasonable excuse, the implementation of financial fraud. The usual rationalized excuses are: everything is done for the long-term development of the company, in order to maintain the company's motives and ignore ethics, and in the capital market supervision loopholes, financial personnel have the opportunity to follow.

When the three elements of opportunity, motivation and rationalization exist at the same time, it will form a "fraud triangle", inducing individuals or enterprises to commit fraud. Therefore, in terms of preventing fraud, it is not only necessary to strengthen internal control and supervision, but also to guide people at the institutional and cultural levels to form correct values and codes of conduct.

2. Summary of financial fraud cases of Blue Mountain Technology

2.1. Case review

Blue Mountain Technology was listed at the basic level of the New Third Board in 2014, and entered the innovation level in 2016 after meeting the entry standards of the innovation level of the New Third Board, and remained there until 2019. On April 29, 2020, in order to further enhance the company's market recognition and highlight the enterprise value, Blue Mountain Technology began to submit data to the selected layer. Compared with the investor admission standard of RMB 2 million and RMB 1 million for the basic layer and the innovation layer of the New Third Board, the investor admission threshold of the selected layer is as low as RMB 500,000. In order to protect the legitimate rights and interests of small and medium-sized investors, the information disclosure requirements of the selected layer are stricter. In the face of more stringent information disclosure review, Blue Mountain Technology was suspected of the authenticity of the company's information disclosure when it conducted the

review of information disclosure access of the selected layer.

After a series of examination and evidence collection, China Securities Regulatory Commission made a punishment decision on November 22, 2021 on Blue Mountain Technology: a fine of 4 million yuan, ordered correction and gave a warning. Four intermediary agencies related to Blue Mountain Technology were also placed under investigation, the Blue Mountain Technology fraud case officially ended.

2.2. Analysis of financial fraud means of Blue Mountain Technology

2.2.1. Inflated bank balances

When auditing the financial statements of enterprises,

auditing institutions should pay attention to whether the balance of bank deposits and other monetary funds of enterprises is true, so as to reflect the real situation of the changes in sales income and cash flow of enterprises. Monetary fund audit is an important way for audit institutions to find fraudulent clues such as false income, which should be paid attention to. Through the audit of the bank deposits in the financial statements of Blue Mountain Technology, it is found that the balance of the company's bank deposits in 2017-2018 was substantially inflated, as shown in Table 1:

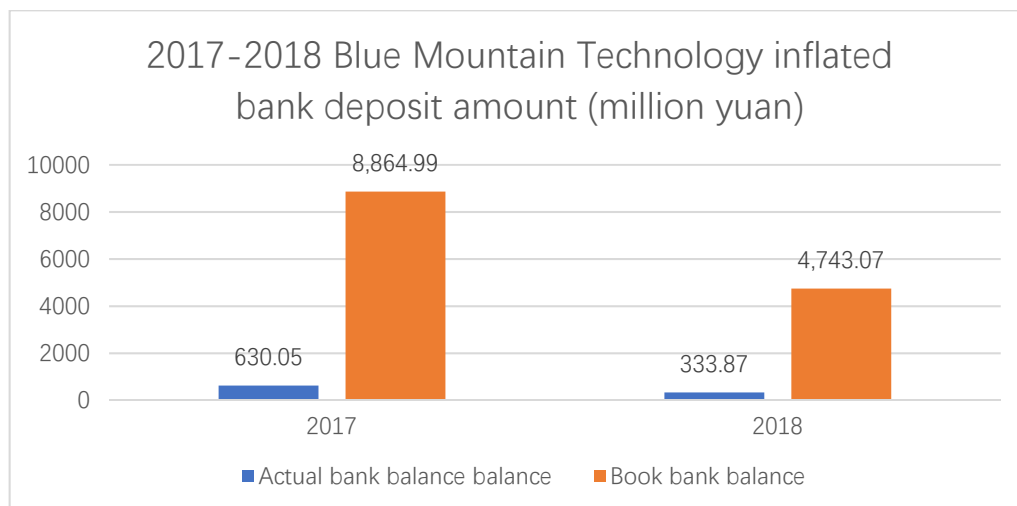


Figure 1. 2017-2018 Deposit balance fraud of Blue Mountain Technology Bank

2.2.2. Fictitious circular buying and selling business

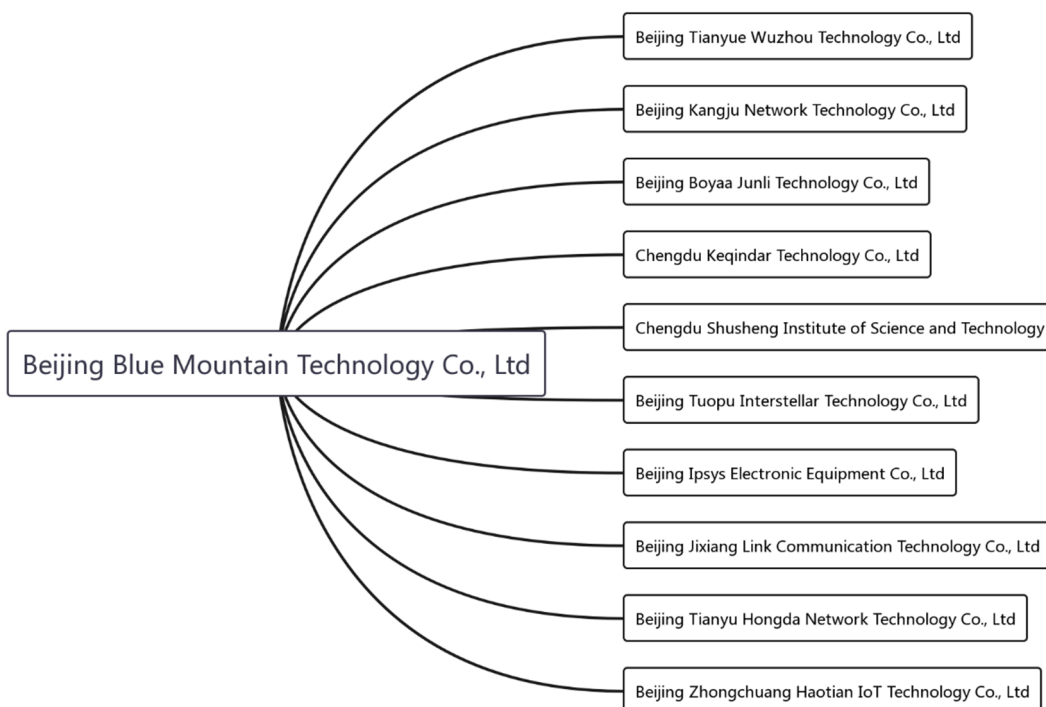


Figure 2. Related parties of Beijing Blue Mountain Technology Co., LTD

As shown in Figure 2, the above 10 companies are all controlled by the actual controller of Blue Mountain Technology, but Blue Mountain Technology did not truthfully disclose its association relationship, and used its false

association relationship to carry out fictitious cycle business to facilitate its fraud. According to the disclosure, Blue Mountain Technology has fictitious procurement sales cycle business and other full chain of financial fraud, including but

not limited to the use of related parties, external customers and suppliers to implement financial fraud. These behaviors

involve procurement, production, sales, logistics and transportation, financial accounting and other links.

Table 1. Situation of Blue Mountain Technology and its wholly-owned subsidiary Beijing Zhongjing CyberTech Co., LTD.'s conspiracy to fabricate cycle business during 2017-2019 (Unit: Ten thousand Yuan)

Reporting year	Inflated sales revenue	Inflated sales profit	Inflated inventory	Inflate accounts receivable
2017	29,224.26	10,031.72	6,070.71	400.39
2018	18,740.36	5,449.07	4,539.97	2,768.77
2019	33,127.64	9,078.17	0.00	3,134.17
total	81,092.26	24,588.96	10,610.68	6,303.33

Data source: China Securities Regulatory Commission Administrative Penalty Decision (Blue Mountain Technology)

As shown in Table 1, from 2017 to 2019, Blue Mountain Technology and its wholly-owned subsidiary Beijing Zhongjing Cyber Technology Co., LTD falsely increased its revenue by RMB 810,922,600, its sales profit by RMB 24,589,600, and its inventory by RMB 10,610,680 through fictitious purchasing and sales cycle business. The total amount of fictitious receivables is 63,033,300 yuan.

2.2.3. Fictitious R&D expenditure

R&d expenditure represents the core competitiveness of

the enterprise, and the level of R&D expenditure directly or indirectly affects the sustainable development ability of the enterprise. From the penalty decision of China Securities Regulatory Commission, it can be seen that the management of Blue Mountain Technology is obviously aware of the effect of R&D investment on the enterprise. From 2017 to 2019, Blue Mountain Technology fictitious research and development contracts and payments with Chengdu Shusheng and Topu Interstellar, and its fictitious research and development expenditure totaled 24,858,000 yuan.

Table 2. The fictitious R&D expenditure of Blue Mountain Technologies during 2017-2019

Reporting year	Fictitious R&D expenditure	Inflated administrative expenses	Inflated total assets
2017	5,144.39	4,682.12	462.27
2018	13,172.78	3,032.16	10,602.89
2019	6,541.63	3,534.44	13,610.08

Data source: China Securities Regulatory Commission Administrative Penalty Decision (Blue Mountain Technology)

2.2.4. Fictitious freight expenses

According to the investigation, Nanshan Technology increased the freight by 41.467,500 yuan in total from 2017 to 2019, which was a fictitious freight to and from Beijing Crescent United Automobile Co., LTD., its only logistics enterprise, without the actual business matters involved in the cost. The amount of false freight is mainly in order to

cooperate with the false income for joint fraud, so that the false income seems more reasonable, to mislead auditors. At the same time, the behavior of falsely increasing the freight and reporting it in the financial statements can not only mislead auditors, but also deceive investors and market supervision, so that Blue Mountain Technology can avoid market supervision and punishment while gaining more interests.

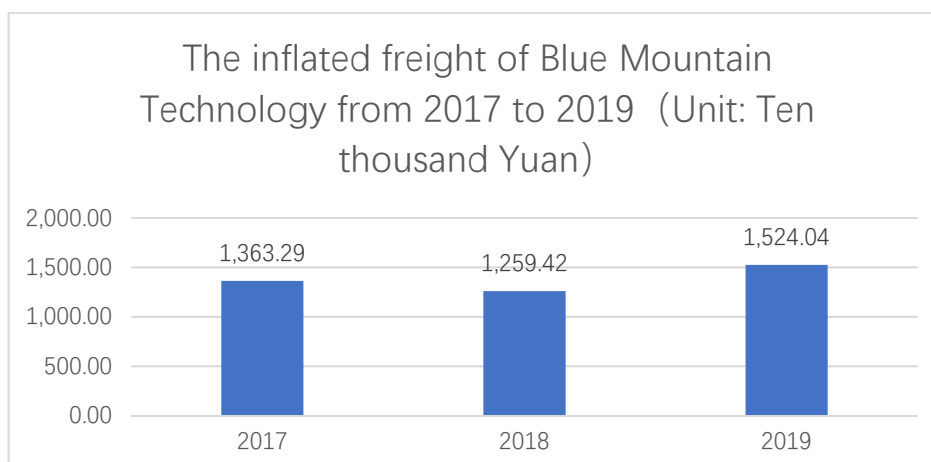


Figure 3. The inflated freight of Blue Mountain Technology from 2017 to 2019

2.2.5. Fictitious disposal assets

In December 2019, Blue Mountain Technology and its wholly-owned subsidiary Zhongjing Cyberine adjusted their production mode and sold production equipment, with sales volume of RMB 4,383,180 (tax included). The audit agency

investigated and verified that the sale business was fictitious, and the purchaser Ipseth was actually a related party of Blue Mountain Technology, and Blue Mountain Technology did not actually receive the proceeds from the sale. Based on this, Bluemannshan invented the disposal and sale of production

equipment business of RMB 4,383,1,800 yuan (tax included), accounting for 4.89% of the net assets at the end of 2019.

3. Analysis of Financial Fraud Motivation of Blue Mountain Technology Based on Fraud Triangle Theory

3.1. Pressure element analysis

First of all, the impact of the new Third Board innovation layer pressure. The New Third Board is divided into three layers: selection layer, innovation layer and foundation layer. Blue Mountain Technology was listed on the New Third Board in 2014, and from 2016 to 2019, it has remained in the innovation layer of the New Third Board. If Blue Mountain Technology can enter the selected tier, then for Blue Mountain Technology, the investor capital threshold will be lowered, greatly enhancing its financing ability. However, the innovation layer of the New Third Board has higher requirements on the financial situation and corporate

governance of listed companies. So Blue Mountain technology in order to promote itself to meet its requirements, began to operating income, net profit, bank deposits, research and development expenditure and other aspects of the financial fraud.

Secondly, the internal financial pressure of the enterprise. As a listed company, Blue Mountain Technology faces market competition, performance pressure and other factors. Due to its poor financial condition, it needs to increase its performance and financial indicators through fictitious data to attract more investors and market attention.

As can be seen from Table 3, the actual bank deposit balance of Blueshan Technology in 2017 was 6.305 million yuan, and the book balance after inflated was 88,649,900 yuan, with the inflated amount up to nearly 92.89%. In 2018, the actual balance of the bank deposit was 3,338,700 yuan, and the book balance was 4,743,700 yuan after the increase, with the increase amount as high as 92.96%. From the above data, we can see that the fund situation of Blue Mountain technology is poor, and the fund pressure is also the pressure factor of Blue Mountain technology for financial fraud.

Table 3. Increase of deposit balance of Blue Mountain Technology Bank (Unit: ten thousand yuan)

Reporting year	Actual deposit balance	Balance of book deposit	Inflated amount	Inflated ratio
2017	630.05	8,864.99	8,234.94	92.89%
2018	333.87	4,743.07	4,409.20	92.96%

Data source: China Securities Regulatory Commission Administrative Penalty Decision (Blue Mountain Technology)

3.2. Opportunity element analysis

First of all, Blue Mountain technology internal control effectiveness is insufficient. According to the annual report of Blue Mountain technology appeared a large number of financial data fraud, it can be seen that the company's internal control system is flawed. Meanwhile, Blue Mountain Technology made false records in major documents, illegally inflated a large amount of bank deposits, revenues and profits,

failed to disclose its related parties in a timely manner, and used its related parties to carry out insider trading. At the same time, Blue Mountain Technology has not established a complete risk management system and internal audit system, which makes its internal management and supervision mechanism unable to effectively prevent and detect financial fraud, and the overall increase in false value is shown in Table 4:

Table 4. The falsely increased revenue, profit and total assets of Blue Mountain Technology from 2017 to 2019 (unit: ten thousand Yuan)

Reporting year	Inflated sales revenue		Inflated total profits		Inflated total assets at the end of the year	
	Inflated amount	Inflated ratio	Inflated amount	Inflated ratio	Inflated amount	Inflated ratio
2017	29,224.26	43.20%	3,966.29	51.90%	15,148.29	13.69%
2018	18,740.36	29.18%	1,019.05	22.16%	22,062.63	20.56%
2019	33,127.64	49.17%	3,862.98	80.67%	16,062.11	14.20%

Data source: China Securities Regulatory Commission Administrative Penalty Decision (Blue Mountain Technology)

In addition, the external intermediary in this case failed to fully perform its duty of diligence. Blue Mountain partnered with four intermediaries, including Hualong Securities, Zhongxing Caiguanghua Accounting Firm, Tianyuan Law Firm and New Century Asset Appraisal Company. As can be seen from the administrative punishment of Zhongxing Caiguanghua CPA Firm issued by China Securities Regulatory Commission, its auditors did not implement the auditing procedures in place, and did not find any abnormality in the inflated amount of bank deposits, the inflated amount of income and profits. Not maintaining proper professional suspicion. Zte Caiguanghua accounting firm failed to implement auditing procedures in strict accordance with auditing standards, creating favorable conditions for Blue Mountain technology to carry out financial fraud.

Finally, regulators failed. Blue Mountain Technology was listed on the New Third Board in 2014, and has been on the innovation board for four consecutive years from 2016 to 2019. It is because of the strict screening of the selection layer that the financial fraud case of Blue Mountain Technology was uncovered. But the company's financial fraud has existed for many years, but the new third board in the disclosure of information did not find any problems, indicating that although the new third Board between each level of audit intensity differences, but insufficient supervision, and punishment is not enough, to Blue Mountain technology to provide convenience for financial fraud.

3.3. Excuse element analysis

The management of Blue Mountain Technology falsified

financial data by falsely increasing bank deposits, fictitious circular purchase and sales business, falsely increasing R&D expenditure, freight and other means to cover up the actual operating and financial conditions of Blue Mountain Technology. At the same time, Blue Mountain Technology uses various accounting methods and policies to distort financial data, such as the phenomenon of fictitious increase or decrease in operating costs, expense advances, etc., so as to make the financial statements seem more real and reasonable.

Secondly, Bluemagnite incorporated non-existent revenues and profits into its financial statements by means of fictitious transactions and contracts, thus covering up its real performance and financial position. At the same time, Blue Mountain Technology used fictitious customers and accounts and other means to cover up the truth of actual sales and turnover, in order to achieve profit fiction and cover up financial fraud.

According to the investigation, as early as 2016, there were discrepancies between the purchasing data ledger of Blue Mountain Technology and the data of several suppliers, and there were cases of exaggerating the purchase and sales scale by real customers. However, it was not discovered in the following years, which greatly strengthened the lucky mind of Blue Mountain Technology.

4. Financial Fraud Prevention Measures Based on Fraud Triangle Theory

4.1. Pressure factor level

As mentioned above, the main pressure of implementing financial fraud in Blue Mountain Technology is the impact of the selected layer and financial pressure. In the final analysis, because of the enterprise's own management problems. So how to make enterprises improve their operating conditions:

first of all, to develop specific and operable targets. The tragedy occurred because of the behavior of Blue Mountain Technology beyond its capacity. It was clear that it had not met the conditions to impact the selected layer, but it still took risks to carry out financial fraud for benefits. Enterprises should reasonably evaluate their own operating conditions, make reasonable planning for enterprises, and improve their operating conditions. For example, in the aspect of product operation, it pays attention to the core competitiveness of products and constantly improves the innovation and research and development ability of the enterprise. From the inflated R&D expenditure of Blue Mountain Technology, it can be seen that the enterprise does not pay attention to its own research and development ability, which leads to the poor financial condition of the enterprise.;

Secondly, optimize their own financing channels. The reason why Blue Mountain Technology is struggling to hit the selected layer is also the hope that after reaching the selected layer, the enterprise can have more financing channels. In fact, in the capital market, the most able to attract the attention of investors is their own business conditions, false statements will always be exposed one day, their own strength is the absolute truth. Through continuous market research, understand the latest trends of the market, timely adjust the development strategy of enterprises, improve their competitiveness, so as to attract investors and expand financing channels.

4.2. Opportunity factor level

First of all, enterprises should strengthen internal control and audit supervision, establish a sound risk management system, timely discover and correct possible loopholes. Enterprises to strengthen internal control, set up good and effective internal control system is the basis of preventing fraud, enterprises should combine their own characteristics, optimize the control environment, clear control objectives, improve control technology, and constantly improve the internal control system in practice, improve the effectiveness of internal control.

Secondly, external audit institutions should improve their professional quality, strengthen the study of audit laws, regulations and professional knowledge, avoid being tempted by the interests proposed by enterprises, and avoid allowing enterprises to be audited due to the limitations of their own professional capabilities.

Finally, China Securities Regulatory Commission should strengthen the supervision of enterprises, increase the punishment, so that enterprises dare not cheat, do not want to cheat, can not cheat. Strengthen the supervision and management of external audit institutions, improve the legal standards of the audit industry, and establish a favorable market environment.

4.3. Excuse element level

In order to avoid enterprises to find reasonable excuses for financial fraud, it is necessary to build a good faith ethical environment. Enterprises should improve the integrity consciousness of the management, lead all employees to strengthen the integrity consciousness of the values through the example of the management, increase the punishment for dishonesty and trustworthiness, and implement the responsibility to every employee of the enterprise. Can promote the long-term development of the enterprise.

At the same time, the state should also introduce relevant laws and regulations and policies, reward honest and trustworthy enterprises, increase the punishment for dishonest and trustworthy enterprises, create the situation that the cost of fraud is far higher than the interest, from the source to curb the idea of corporate financial fraud, jointly create a good social atmosphere.

5. Conclusion

Through the analysis of the financial fraud case of Blue Mountain Technology, it can be found that the occurrence of fraud is the result of pressure, opportunity and excuse. In terms of pressure factors, the management is faced with multiple pressures such as market competition, performance pressure and interest demands, which form the motivation to commit fraud on financial data. At the level of opportunity elements, there are such opportunity factors as lax internal control and inadequate audit supervision in Blue Mountain Technology, which provide opportunities for the occurrence of fraud. At the level of excuse elements, the management makes up various excuses to cover up their financial malpractices and rationalize them.

Therefore, the prevention of financial fraud requires a comprehensive consideration of the role of three elements. In terms of pressure factors, enterprises should strengthen internal governance, establish a reasonable assessment mechanism, and provide a good working environment and profit return for the management. In terms of opportunity

factors, enterprises should strengthen internal control and audit supervision, establish a sound risk management system, and timely discover and correct possible problems. At the level of excuse elements, enterprises should establish and improve audit procedures and processes, ensure the independence and effectiveness of audit work, and reduce the possible space for making up excuses.

To sum up, the prevention of financial fraud requires a comprehensive consideration of pressure, opportunity and excuse, and corresponding measures should be taken to prevent and contain it. Only in this way, enterprises can ensure the true, accurate and reliable financial data, establish a good corporate image, enhance the confidence of investors and the market, and promote the sustainable development of enterprises.

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