IOSR Journal of Business and Management (IOSR-JBM)
e-ISSN: 2278-487X, p-ISSN: 2319-7668. Volume 22, Issue 4. Ser. III (April. 2020), PP 05-11
www.iosrjournals.org

Effect of Internal Reconciliation Strategies on Fraud Prevention in Listed Insurance Firms in Nairobi City County, Kenya.

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Abstract: *Insurance industry play a key role in advancing the socio-economic of the country. Besides reinstating the social and economic status of the insured citizenry after a loss occurs, the sector contributes significantly to the national economy through, employment of thousands of Kenyans and paying taxes to the Exchequer. This study sought to determine the effect of internal reconciliation strategies on fraud prevention among listed insurance firms operating in Nairobi City County. The fraud triangle theory guided the study. A cross-sectional research design and quantitative approach were adopted. A total of 147 staff working with the aforesaid insurance firms constituted the study population. Out of this population, a sample of 108 respondents calculated using Yamane's formula was obtained using stratified sampling technique. A structured questionnaire was used in data collection. In addition to the facilitation of the Statistical Package for Social Sciences, descriptive and inferential statistics were used to analyze the collected data. The results of the analysis were presented in form of tables. According to the study findings, there existed a positive, strong and statistically significant relationship between internal reconciliation strategies and fraud prevention ($r = 0.965$; $p = 0.00$) at p-value = 0.05. The effect of the aforementioned strategies on fraud prevention was also established to be statistically significant ($F_{1, 54} = 722.128$; $p = 0.00$). Therefore, as further indicated by the results of the t-statistics ($t = 26.872$; $p = 0.00$) the null hypothesis was rejected. It was concluded that insurance firms gave all their employees performance targets in addition to carrying out frequent internal reconciliations with the objective of minimizing fraud risks. Additionally, it was inferred that internal reconciliation strategies had significant effect on fraud prevention. It is recommended that insurance companies should put in place and implement sound internal reconciliation strategies in order to prevent fraud more effectively.*

Keywords: *Fraud, fraud prevention, fraud triangle theory, internal reconciliation strategies, listed insurance firms,*

Date of Submission: 22-03-2020 Date of Acceptance: 09-04-2020

I. Background

Fraud is defined as an act that involves deceit which is purposed to gain an unfair advantage over another in order to secure something of value or deprive another person of their right (Duffield & Grabosky, 2001). It occurs when a perpetrator communicates false statements with the intent of defrauding a victim of property or something valuable. Fraud prevention, therefore, is the responsibility of every employee, vendor, supplier, contractor, service provider, or any agency doing business with the company to ensure there is no fraudulent activities being perpetrated. As fraud prevention practices may not stop all potential perpetrators, organizations have put systems in place with the view of highlighting occurrences of fraud in a timely manner. This is achieved through fraud detection (Duffield & Grabosky, 2001).

Reconciliation refers to the process of comparing transactions and activity to support documentation. It involves resolving any discrepancies that may have been discovered with the view of coming up with truce between conflicting parties or issues (McKone, 2015). The process of reconciliation ensures the accuracy, validity of financial information and unauthorized changes have not occurred to transactions during processing. The key concepts of reconciliation are accuracy of activity, error correction, documenting the process, completion and matching the source. Reconciliation strategies thus are steps taken to reconcile the activities of a firm so that it can realize its objectives and mission.

According to the Insurance Regulatory Authority (IRA), fraud is one of the major bottlenecks insurers face. It threatens the survival of firms as it increases the cost of doing business. If fraud is not detected early, it eventually has a huge financial implication. Due to its white–collar nature, eliminating it becomes both difficult and expensive. Companies are really threatened by fraud risk since it affects their liquidity position and eventually drives them out of business. The greatest effect of this risk is the loss of customers' goodwill and customer loyalty. On the same note, it is emphasized that businesses (insurance firms included) should take stock of the risks they are presently exposed to or foreseeing to face. This would enable them to put in place both control and preventive measures of addressing potential risks including fraud risks(Mose, Osiemo, & Kuloba, 2013).

Statement of the Problem

Insurance firms play a critical role in the socio-economic development of the country. however, these companies are oftentimes exposed to risks emanating from fraudulent activities. Fraud is mostly perpetrated by the organizations' employees, insurance agents or other people who work in cahoot with the insurance firms' staff or their agents to defraud these companies. Statistics from the Insurance Regulatory Authority (IRA) indicated that there were a total of 143 cases of medical insurance fraud reported in 2012. The foregoing led to a loss of Ksh 253.6 million with only Ksh 5.2 million being recovered(Association of Kenya Insurers, 2013). Recent statistics indicated that approximately 25.0% of insurance industry income in Kenya is fraudulently claimed(Deloitte, 2019). The foregoing necessitates the actions of insurance firms to prevent fraud. It is on this premise that the study was conducted with the view of determine the effect of internal reconciliation strategies on fraud prevention in listed insurance firms in Kenya.

Objective of the Study

The objective of the study was to determine the effect of internal reconciliation strategies on fraud prevention in listed insurance firms in Nairobi City County.

Research Hypothesis

H_{01}: There is no signficant effect of internal reconciliation strategies on fraud prevention in listed insurance firms in Nairobi City County.

Theoretical Framework

The study was guided by fraud trinngle theory (FTT) which is one of the classical fraud theories. The FTT was proposed by Donald Cressey in 1950(Cressey, 1953). In his theory, Cressey, a criminologist, argued that there must be a reason or motive behind everything people do, including fraud. Queries like why people commit fraud pursuaded him to examine the impetus of trust violation by people. Accordingly, the theory states that there must be a presence of three factors for an offense to take place. These are pressure, opportunity, and rationalization. These three factors form a triangle, hence the fraud traingle theory(Cressey, 1953). As such, every fraudulent act stems from perceived pressureor motive, perceived opportunity and rationalization(Wells, 2011).

Perceived pressure constitute of factors which result in unethical behaviour or tendencies. It is stated that every fraud is motivated by certain pressure to commit unethical act (Abdullahi & Mansor, 2015a). The pressure may be financial or non-financial. However, the pressure may be unreal hence its reference to being perceptible. It is further asserted that approximately 95% of fraud cases are occasioned by perceived financial pressure of the fraudsters(Albrecht, Albrecht, & Albrecht, 2008).

Perceived opportunity results from ineffective control or governance system which gives a perpetrator space to commit fraud in an organization. The presence of perceived opportunity often encourages people to take advantage of prevailing circumstances(Kelly & Hartley, 2010). The opportunity exists in the perception or belief of the perpetrator. The chances of being caught are inversely proportional to the probability of committing fraud. Hence when the risk of being caught is perceived to be lower, there are higher chances of committing fraudulent activities.

Rationalization occurs when the perpetrator attempts to justify (by say, giving excuses) why he or she should engage in unethical behaviour such as embarking on commmitting the fraudulent activities. In the event that perpetrator is unable to justify dishonest actions, there is little, if any, likelihood of engaging in fraud(Cressey, 1953). Therefore, engaging in fraudulent activities in insurance firms is likely to stem from pressure on the part of perpetrators, say employees. Then there is opportunity presented by weak internal controls or governance system or both in the insurance firms which the perpetrators believe they can seize and conduct fraud. Lastly, the justification that it is deserving for them to embezzle funds or carry out other related fraudulent activities, pushes the perpetrators to actually commit the fraud. Therefore, in order to prevent fraud, it is imperative for the management of insurance firms to address both financial and non-financial needs of all their employees so that they will not be motivated or pressurized to commit fraudulent activities.

Empirical Review

A research study on the relationship between innovation capability, innovation type, and firm performance was conducted by Rajapathirana and Jayani (2018) in Amsterdam. The main objective of the study was to explore the relationship among innovation capabilities, innovation types and different aspects of firm performance. The sample size of 379 senior managers of insurance companies wasused. The study revealed that effective management of innovation capability helped the delivery of more effective innovation outcomes to generate better performance .

In Ghana, a research study was conducted by Amissah (2017) to investigate the effect of internal control systems on performance of companies in the insurance industry. The sample sizecomprised 91 respondents. The data were analysed using descriptive statistics and regression analysis. The study established that lost adjustor and reinsurrance firms had low levels of performance and weak internal control systems, whereas brokerage, life and non-life insurance firms had strong internal control systems and high levels of performance. The study further revealed that there was a significant difference between the risk assessment procedures of non-life and brokerage firms. The study recommended that non-life and brokerage firms should adopt risk assessment procedures based on their organisational context.

An empirical study conducted in Kenya sought to examine insurance fraud risk management practices and performance of motor vehicle underiting firms(Nyanga, 2018). The objective was to determine the effect of insurance fraud risk management practices on performance of the aforesaid firms. A descriptive research design was adopted where a total of 35 motor vehicle underwriting companies were targeted. According to the study findings, preventive, detective and responsive fraud practices were significantly related to performance of the aforementioned firms. It was concluded that the stated practices were instrument in influencing the performance of motor vehicle underwiting companies in Kenya. Therefore, these firms were recommended to deliberate on the extent to which they ough to adopt and implement the studied insurance fraud risk management practices.

II. Methodology

The study adopted a cross-sectional research design given that the study was conducted at a given point in time. This is in tandem with the assertion that cross-sectional studies are carried out at a specified time period where a snapshot of event is observed or taken for analysis (Hemed, 2015). Additionally, a quantitative approach was employed where the data collected were numerical. The target population comprised all staff working with insurance firms in Kenya. However, the study or accessible population was delimited to the 147 staff working with the six insurance firms listed on the Nairobi Securities Exchange (NSE) and based in Nairobi City County. The listed insurance companies included Jubilee Insurance, CIC Insurance, Britam Insurance, Sanlam Kenya, Liberty Kenya and Kenya Re.

The sample size was determined using Yamane's formula as illustrated below (Yamane, 1967).

$n = N/1+N\,(e)^2$

Where:

n represents the sample size

N represents the population under study (147)

e represents the error margin (0.05)

The above equation is substituted as follows:

$n = 147/1+147(0.05)^2$

$n = 107.5$

$n = 108$ respondents

Therefore, as shown above, the sample that was used in the study constituted 108 staff working with listed insurance firms operating in Nairobi City County. A simple random sampling technique was employed to ensure fair and equitable distribution of respondents across the 6 listed insurance firms.

A structured questionnaire was used in data collection from the sampled respondents. The questionnaire was consistent to the quantitative approach and survey design adopted by the study. The data items captured in the questionnaire and which addressed the study objectives (internal reconciliation strategies and fraud prevention) were on a 5-point Likert scale ranging from strongly disagree to strongly agree. The data were collected after obtaining a research permit from the National Commission on Science, Technology and Innovation (NACOSTI). Additionally, the consent of the senior management of the listed insurance firms was obtained prior to data collection.

The collected data were analyzed using both descriptive statistics and inferential statistics and with the assistance of the Statistical Package for Social Sciences (SPSS). The descriptive statistics used included percentages, means and standard deviations. On the other hand, Pearson's Product Moment Correlation Coefficient and simple linear regression analysis constituted the inferential statistics which were used. The results of the analysis were presented in tabular form and were accompanied by pertinent interpretation and discussion.

III. Findings and Discussions

This section presents the results of analyses with regard internal reconciliation strategies and fraud prevention. Essentially, the data collected and subsequently analyzed were on a 5-point Likert scale where values of 1 to 5 were represented by a scale ranging from strongly disagree (SD) to strongly agree (SA) respectively. The results were in form of both descriptive statistics and inferential statistics. Descriptive statistics included percentages (%), means, and standard deviations (Std Dev.). inferential statistics were Pearson's Product Moment Correlation Coefficient (PPMCC) and simple linear regression analysis. The results are accompanied by pertinent interpretations and discussions.

Descriptive Results of Internal Reconciliation Strategies

The studies sought to determine the various internal reconciliation strategies present in insurance companies. The pertinent results are outlined in Table 1 below.

Table 1: Descriptive Statistics for Internal Reconciliation Strategies

	SA (%)	A (%)	N (%)	D (%)	SD (%)	Mean	Std. Dev.
All employees are given performance targets which they are expected to achieve.	71.4	28.6	0.0	0.0	0.0	4.71	.456
Internal reconciliations are frequently carried out by the management with the view of minimizing risks that can result in fraud.	42.9	51.8	1.8	3.6	0.0	4.34	.695
There is a supervisor who controls whatever goes on daily in the organization.	44.6	46.4	7.1	1.8	0.0	4.34	.695
The management has a criterion for ascertaining the most critical risks.	35.7	57.1	0.0	3.6	3.6	4.18	.897

The findings revealed that all (100%) of the surveyed respondents admitted that all employees were given performance targets which they were expected to achieve. Regarding the argument that internal reconciliations were frequently carried out by the management with the view of minimizing risks that could result in fraud 94.7% of the respondents were in agreement with the assertion while only 3.6% refuted the argument. It was also ascertained that a significant number (91.0%) of the participating respondents registered their agreement that there was a supervisor who controlled whatever went on daily in the organization. However, 7.1% of the respondents were uncertain regarding the opinion. In addition, the study found that most (92.8%) of the sampled staff concurred that the management had a criterion for ascertaining the most critical risks.

It was further ascertained that on average the respondents were in admission that all employees were given performance targets which they were expected to achieve (mean = 4.71) and that internal reconciliations were frequently carried out by the management with the view of minimizing risks that could result in fraud (mean = 4.34). In addition, the participating staff generally agreed that there was a supervisor who controlled whatever went on daily in the organization (mean = 4.34) and that the management had a criterion for ascertaining the most critical risks (mean = 4.18). Regarding internal reconciliation strategies the respondent's views were largely similar (stddev< 1.000).

Descriptive Results of Fraud Prevention

The study examined the views of the sampled employees on fraud prevention in insurance companies in Kenya. The results are presented in Table 2.

Table 2: Descriptive Statistics for Fraud Prevention (2)

	SA (%)	A (%)	N (%)	D (%)	SD (%)	Mean	Std. Dev.
Both internal and external auditing of all transactions is conducted on a regular basis in order to identify any cases of fraud in our company.	66.1	19.6	0.0	10.7	3.6	4.34	1.149
In order to prevent some employees from engaging in fraudulent activities, performance evaluations are ensured that they are correct, fair and communicated.	33.9	57.1	5.4	1.8	1.8	4.20	.773

There is controlled access to documents which can otherwise be abused by certain employees for their individual persuasions.	16.1	80.4	0.0	3.6	0.0	4.09	.549
Our firm always conducts background screening to exclude new employees who are higher risks for fraud.	21.4	71.4	0.0	7.1	0.0	4.07	.710
Our firm conducts interviews on all employees exiting the company with the objective of establishing their awareness on past and current fraud cases.	3.6	35.7	3.6	44.6	12.5	2.73	1.183

The results as illustrated in Table 2 reveal that 85.7% of the participating management staff admitted that both internal and external auditing of all transactions was conducted on a regular basis in order to identify any cases of fraud in the firms. Regarding the argument that in order to prevent some employees from engaging in fraudulent activities, performance evaluations were ensured to be correct, fair and were communicated, majority (91.0%) of the sampled respondents agreed to the view. It was further noted that 96.5% the respondents concurred that there was controlled access to documents which could haveotherwise been abused by certain employees for their individual persuasions, only 3.6% of the respondents held contrary opinions. More so, a significant number of respondents (92.8%) were in agreement that the firms always conducted background screening which exclude new employees who were higher risks for fraud. Moreover, 44.6% of the sampled respondents disputed the argument that their firms conducted interviews on all employees who exited the company with the objective of establishing their awareness on past and current fraud cases. However, 39.3% of the staff agreed to the view.

The respondents in general were in admission with the view thatboth internal and external auditing of all transactions was conducted on a regular basis in order to identify any cases of fraud in the firms (mean = 4.34). The respondent's opinion regarding the foregoing proposition varied significantly (stddev> 1.000). It was further noted that on average the respondents concurred with the views that in order to prevent some employees from engaging in fraudulent activities, performance evaluations were ensured to be correct, fair and were communicated (mean = 4.20); that there was controlled access to documents which could have otherwise been abused by certain employees for their individual persuasions (mean = 4.09) and that their respective firms always conducted background screening which exclude new employees who were higher risks for fraud (mean = 4.07). The views of respondents regarding the aforestated views varied insignificantly (stddev< 1.000).Furthermore, the participating staff were uncertain in relation to the view that their firms conducted interviews on all employees who exited the company with the objective of establishing their awareness on past and current fraud cases (mean = 2.73). The opinions of the participating respondents were unrelated (stddev> 1.000).

Results of Correlation Analysis

The relationship between internal reconciliation strategies and fraud prevention was ascertained. The pertinent PPMCC results are as shown in Table 3.

Table 3: Correlation betweenInternalStrategiesandFraud Prevention

		Fraud Prevention(2)
Internal ReconciliationStrategies	Pearson Correlation	.965**
	Sig. (2-tailed)	.000
	n	56

****. Correlation is significant at the 0.01 level (2-tailed).**

According to the results shown in Table 3, there existed a positive, strong and statistically significant relationship between internal reconciliation strategies adopted by insurance firms and fraud prevention in the aforesaid entities ($r = 0.965$; $p = 0.00$). The results meant that when tested at p-value = 0.05, the correlation between internal reconciliation strategies and fraud prevention was established to be significant. Therefore, the aforesaid strategies were inferred to have the potential of greatly influencing prevention of fraud in insurance companies.

Results of Simple Linear Regression Analysis

The study further linearly regressed internal reconciliation strategies against fraud prevention. The collected data were first assumed to be linearly distributed. The results of the aforestated regression analysis are presented in Table 4, Table 5 and Table 6 respectively.

Table 4: Model Summary on Internal Reconciliation Strategies on Fraud Prevention

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.965[a]	.930	.929	.20327

a. Predictors: (Constant), Internal Reconciliation Strategies

The key results illustrated in Table 4 are those of the coefficient of determination (R2 = 0.930) which indicate that internal reconciliation strategies could explain 93.0% variability in fraud prevention. The findings emphasized on the importance of insurance firms to adopt and implement the aforementioned strategies in order to prevent fraud more effectively.

Table 5: Test Significance Results of Internal Reconciliation Strategies on Fraud Prevention

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	29.837	1	29.837	722.128	.000[a]
	Residual	2.231	54	.041		
	Total	32.069	55			

a. Predictors: (Constant), Internal Reconciliation Strategies

b. Dependent Variable: Fraud Prevention

The results of F-statistics shown in Table 5, that is, $F_{1, 54} = 722.128$; p = 0.00 indicated that the effect of internal reconciliation strategies on fraud prevention was statistically significant at p-value = 0.05. The findings were interpreted to mean that the sample data collected and subsequently analyzed fitted the adopted simple linear regression model ($Y= \beta_0 + \beta_1X_1 + \varepsilon$). Therefore, the model was feasible to be used to illustrate the effect of internal reconciliation strategies on fraud prevention in insurance firms as shown in Table 6.

Table 6: Regression Coefficients of Internal Reconciliation Strategies on Fraud Prevention

	Unstandardized Coefficients		Standardized Coefficients		
Model	B	Std. Error	Beta	t	Sig.
(Constant)	-1.262	.193		-6.521	.000
InternalReconciliation Strategies	1.172	.044	.965	26.872	.000

a. Dependent Variable: Fraud Prevention

According to the results shown in Table 5 ($Y= -1.262 + 1.172X_1$), a change of 1 unit in fraud prevention (Y = 1) was subject to 1.172 unit change ($\beta_1 = 1.172$) in internal reconciliation strategies when other factors were duly held constant ($\beta_0 = -1.262$). The effect of the aforesaid strategies was further established to be statistically significant (t = 26.872; p = 0.00) at p-value = 0.05. The results led to the rejection of the null hypothesis (H_0) which stated that: There is no significant effect of internal reconciliation strategies on fraud prevention in insurance firms in Kenya. The results underlined the sheer importance of internal reconciliation strategies in addressing fraud issues in insurance firms in Kenya.

IV. Conclusions and Recommendations

From the study findings it was concluded that insurance firms gave all their employees performance targets in addition to carrying out frequent internal reconciliations with the objective of minimizing fraud risks. To this end, the firms have supervisors who conducted oversight on the daily activities. The firms' managers were inferred to have specific criteria of assessing most critical risks. With the view of establishing fraud cases, the insurance firms audited all transactions. The study further concluded that performance evaluations were conducted correctly and fairly and the pertinent feedback communicated as part of the measures laid down to curtail employees from engaging in fraudulent activities. Additionally, it was inferred that internal reconciliation strategies had significant effect on fraud prevention, a fact that underscored the critical role they played in insurance firms. It is recommended that insurance firms ought to closely examine all activities being undertaken by the employees as a way of mitigating fraud. Insurance companies are further advised to put in place and implement sound internal reconciliation strategies if they are seeking to prevent fraud more effectively.

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Gachuru George. "Effect of Internal Reconciliation Strategies on Fraud Prevention in Listed Insurance Firms in Nairobi City County, Kenya.". *IOSR Journal of Business and Management (IOSR-JBM)*, 22(4), 2020, pp. 05-11.