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EVALUATING LEGAL AND GOVERNANCE FRAMEWORKS IN PREVENTING ARTIFICIAL INTELLIGENCE-RELATED FRAUDULENT ACTIVITIES IN PUBLIC COMPANIES

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Abstract

Artificial Intelligence (AI) has become a cornerstone of technological advancement, driving innovation across industries. The rapid growth of AI in companies requires a robust framework focusing on accountability, transparency, fairness and security. The framework should be able to address potential biases and errors within the AI systems. AI should facilitate innovation, allowing faster and more accurate responses to business challenges whilst increasing efficiency, improving decision-making, reducing cost and enhancing customer experience. Past studies mostly discovered that AI governance is in the infancy stage. Absence of adequate security measures may lead to risks of potential fraud as the companies may lack the monitoring or knowledge to properly handle emerging vulnerable management. This study examined the role of corporate governance mechanisms in regulating the use of AI in public companies with a specific focus on preventing, detecting and mitigating AI-enabled or AI-related fraudulent activities. This study adopted a doctrinal research methodology involving a critical examination of primary and secondary legal sources as well as examining the current legal, regulatory and governance relating to the usage of AI. Findings revealed a significant regulatory inadequacy in Malaysia, where current laws lack decisive provisions to address AI-related fraud. Traditional corporate governance mechanisms may fail to identify, monitor, or respond effectively to fraud. There is a need to update an AI-related legal and governance framework, aligning with global best practices to reduce cases of fraud. This paper contributes to the literature on the governance of AI, and assists legislators and policymakers in balancing accountability, transparency and trust in corporate practices.

Keywords: Artificial Intelligence, corporate governance, fraud, public companies.

1. INTRODUCTION

With the rise of Artificial Intelligence (AI) in the world of digital technology, the world has become increasingly advanced in the day-to-day business. AI can be described as a computer system that is able to imitate human intellectual abilities. It can understand, identify, make decisions and solve complex problems quickly and efficiently (Aici-umg, 2024). One of the usages of AI is its role in detecting and preventing of investment scams which threaten an organisational integrity and stakeholder trust. With the rise of digital financial platforms and complex investment products, companies face challenges in identifying fraudulent activities that can occur both internally and externally (Ezekiel et al., 2024).

Scammers can use publicly available videos and audio to train the AI to impersonate multiple senior executives in a video call convincing a clerk to authorise large funds transfers. Such a case happened in Hong Kong where a finance clerk at a Hong Kong branch of a multinational corporation fell victim to a deepfake scam resulting in a loss of over \$25 million (Shelwell, 2024). In Malaysia, a former CFO of Maybank Malaysia almost fell victim to a deepfake where the perpetrators used AI to conduct a Zoom call impersonating a colleague from Singapore and Whatsapp messages requesting her to make a transfer of US\$985,426 (about RM4.77 million) to Maybank Singapore via JP Morgan (Shanmugam, 2025). There was no financial loss since JP Morgan manage to hold back the transaction (Ramasamy, 2025)

AI-driven systems enhance governance frameworks by providing real-time monitoring, analysing behavioural patterns, and detecting anomalies that may signal fraudulent investment schemes. By automating the surveillance of financial transactions and communication channels, AI supports compliance with regulatory standards and promotes transparency within corporate structures (Efunniyi et al., 2024). As part of a governance strategy, the integration of AI not only reduces the risk of financial misconduct but also reinforces ethical decision-making and accountability across all levels of an organization.

Corporate governance refers to the mechanisms and processes in which a company is structured and manages how its decision-making processes are organised (Musa et al., 2015). The goal of corporate governance is to balance the interests of several stakeholders while concentrating on the long-term viability and prosperity of the business. Typically, corporate governance offers a structure for accomplishing the organisation's objectives, guaranteeing responsibility and safeguarding the interests of all parties involved, namely stakeholders. By introducing the AI technology, the development and acceptance of AI technology have radically changed the conventional corporate governance model. The main elements of AI, including machine learning and data analytics which can help companies in making better decisions, improve operational efficiency and enhance their risk management capabilities by helping extracting insights from massive volumes of data (Briere et al., 2022).

MCCG documents published by Securities Commission Malaysian on 28 April 2021 did not cover any AI issues and neither the documents entitled Corporate Governance Monitor issued in year 2024. MCCG which operates on a "comply or explain" basis means that public companies must either adhere to its principles or provide reasons for any deviations. Public companies are expected to integrate these MCCG's governance principles into their operations to maintain investors' confidence and ensure ethical conduct. Although MCCG highlights the key governance areas such as board leadership, risk management, and stakeholder engagement, reflecting the growing need for strong governance frameworks in an evolving business landscape, it failed to refer to any risk that will arise from AI technology.

Past studies mostly discovered that AI governance is in its infancy, signifying a lack of well-established norms, evolving understanding of the technology, limited expertise and the absence of comprehensive frameworks for oversight (Birkstedt, 2023; Oberholzer, 2024). Security measures should adequately be in place to properly handle emerging vulnerable management. Lack of knowledge or monitoring of security together with governance immaturity in AI technology may lead companies to risks of potential fraud. Security flaw raises serious concerns since companies might not have the monitoring tools and specialist skills needed to recognize AI issues. Companies become more vulnerable and easier to data manipulations and exploitation of AI system complexity when they lack skill (Hossain et al., 2024), strong governance frameworks

and security procedures, which eventually makes them more vulnerable to fraudulent activity. Thus, this study examined the role of corporate governance mechanisms in regulating the use of AI in public companies with a specific focus on preventing, detecting and mitigating AI-enabled or AI-related fraudulent activities.

2. LITERATURE REVIEW

Corporate governance refers to the system and framework that determines how companies are directed and controlled. It encompasses the responsibilities and roles of management, the board of directors, and shareholders, aiming to promote transparency, accountability, and fairness within the organization itself. Decisions should align with the long-term interests of stakeholders to enhance the integrity of corporate operations. Corporate governance in Malaysia is shaped by the Malaysian Code on Corporate Governance (MCCG), which serves as a benchmark for best practices among public companies (Bhatt & Bhatt, 2017).

Apart from MCCG, other regulatory frameworks such as Companies Act 2016 and Bursa Malaysia Listing Requirements also enforce the need for transparency, accountability, and proper risk management (Mohd-Sulaiman & Rachagan, 2016). These guidelines strongly suggest the adoption of effective corporate governance structures while balancing innovation with ethical considerations and stakeholder interests, hence, ensures that public companies in Malaysia operate responsibly and sustainably. Since there is a growth in adopting AI in public companies, AI technology continues to shape the corporate environment, therefore, there is a need for a strong governance framework (Chatterjee, 2020; De Almeida et al., 2021). Corporate governance will help to mitigate the risks that are associated with AI, such as data breaches and misuse of technology, while at the same time ensuring AI-driven innovations to be aligned with general goals of corporate accountability and public trust.

AI is increasingly and slowly being adapted by public companies across various industries. AI will enhance and upgrade the efficiency of the companies' operations and eventually will improve innovation and decision making (Chui & Francisco, 2017). AI tools are being used to automate the usual routine task, analysing large amounts of dataset for strategic insight or predicting the movement of market behaviour (Okeleke et al., 2024). Despite its growing adaptability, the organisation lacked standardisation protocols or rules for ethical AI usage thus exposing them to risks like breach of data and potentially fraudulent activities. An AI implementation in public companies raises a significant issue towards governance concerns, especially due to absence of the standard and proper accountability mechanisms (Wirtz et al., 2020).

Many organisations recognize the importance of AI in transformative potential and its implementation; however, they did not fully understand the corporate governance risk (Pirson & Turnbull, 2011). Absence of proper controlling mechanisms and regulatory frameworks will contribute exposure to big data manipulation and misuse of AI tools for fraudulent activities. The status of AI usage in public companies, even though it looks promising, will remain in its beginning of the implementation. Many public companies are gradually incorporating AI into their business processes, upgrading it for predictive analytics, customer relationship management, and enhancing the operational efficiency (Al-witwit & Ibrahim, 2020). However, the adoption rate is uneven across industries, with some sectors investing heavily in AI-powered solutions, while others remain cautious due to governance, legal, and reputational concerns.

Financial services firms utilise AI-driven algorithms for fraud detection and customer profiling,

whereas healthcare-related public companies employ AI for diagnostics and patient care improvements (Bohr & Memarzadeh, 2020). Retail and e-commerce giants leverage AI for personalized marketing and inventory management, reflecting the broad applicability and potential of AI in public companies. Generative AI offers seemingly endless potential to highlight both the nature and the scope of fraud against financial institutions and their customers; it is limited only by a criminal's imagination (Satish et al., 2024).

There have been many cases of fraudulent activities that has been known that have been involving AI, but what need to be identified first is what could be classified as fraudulent activities using AI specifically, the ready availability of new generative AI tools can make deepfake videos, voice cloning, and fake documents easily (Sholademi, 2024). Deepfakes videos are already being used to bait potential victims by using an interesting video for "click bait" to attract people into a malicious website to get their card payment details. Others like voice cloning are used to mimic other people's voice to engage a conversation with a person and convince them of their details. Fraudulent activities such as generating fake documents can be used to create tailored emails and image content to create a fabricated accident to claim an insurance scam (Sholademi, 2024). However, past study show that AI can contribute to benefits the public (O'Keefe et al., 2020). Thus, companies should implement their ethical guidelines to mitigate the risk of AI being used in fraudulent activities (Cihon et al., 2021).

Companies dealing with copyrighted works while using AI maybe at risk of infringing works of others. The case of *Andersen v. Stability AI Ltd.* (2024) was the landmark case in United States (US) concerning copyright implication concerning AI-generated arts. The plaintiff claimed that an AI image generation tool infringed the copyright and rights of publicity of artists. The court concluded that there was copyright infringement based on previous cases of fraudulent activities in involving the infringement of other people copyright (Awoyomi, 2024). Lawsuits are expected when corporate works involved AI and its possibilities of infringing copyrights, but there is little evidence to suggest that AI availability will shake up intellectual property and corporate law in a dynamic sense in the short term. The maturity of AI is still in an early stage to pose a significant risk in the short term. A company that has integrated AI in their governance may cause an issue of pinpointing responsibility (Santoni de Sio & Mecacci, 2021).

3. METHODOLOGY

This study applied the doctrinal legal research approach methodology. Secondary data were collected from journals, rules, guidelines to comprehend and analyse legal doctrines and rules. Such research approach either explains the legal rules governing a specific area of law or assesses the relationship between different legal rules, principles and case laws. (Majeed et al., 2023). This library-based research design involves a critical examination of legal sources as well as examining the current legal, regulatory and governance relating to the usage of AI. This method helped to achieve the research aims of examining the role of corporate governance mechanisms in regulating the use of AI in public companies.

4. RESULTS AND DISCUSSION

Findings revealed a significant regulatory inadequacy in Malaysia, where current laws lack decisive provisions to address AI-related fraud. Traditional corporate governance mechanisms may fail to identify, monitor, or respond effectively to fraud. There is a need to update an AI-related legal and governance framework, aligning with global best practices to reduce cases of fraud. On the matter of AI, the Malaysian legal system is still left behind as compared to the

United Kingdom or US. While other countries have used AI in legal practice such as prioritising crimes to be prosecuted, filtering through a large quantity of documents and establishing reasonable suspicion, the Malaysian legal system is still struggling on procedure or guidelines in admitting evidence given by or produced from AI.

With regards to personal data, the statute of Personal Data Protection Act 2010 (PDPA) is relevant because of AI usage generally requires collecting and processing of personal data in commercial transactions. A data user who is defined as a person who processes any personal data shall have to comply with PDPA (Razak et al., 2020). Consent is needed when processing personal data. The data user must ensure that the AI used will not process personal data beyond the scope of the data subject's consent. Security and integrity of personal data are important when AI is used to process personal data. Compliance with the PDPA will likely minimise exposing the data user to liabilities when using AI to process personal data. Malaysia's PDPA lacks such specific restrictions and advice, but country such Singapore has particular prohibitions that allow organisations to use personal data to develop AI systems without authorisation under certain scenarios (Skrine. 2024). Singapore's advisory guidelines make it clear that, under specific circumstances, companies can use the "business improvement exception" to create AI systems that improve an already-existing good or service and the "research exception" to carry out for-profit research to create AI systems that benefit the general public (Skrine, 2024) Although Malaysia provides an exception for research, there is not much complete guidance on how to use the PDPA's exceptions.

The use of generative AI in corporate governance also revolves around the patent of the intellectual property that it has generated. In the context of patent law in Malaysia under the Patents Act 1983 and Patents Regulations 1986, the main issue is whether an AI is the original creator of the document it produces. Whether AI-Generated works are safeguarded by Copyright Act 1987 also remains in the grey area, as the current law in Malaysia is still inadequate in specified current AI utilisation (Razak et al., 2020). In the context of Copyright Act in Malaysia, it specifies the requirement for a human author, which makes it not probable for copyright to apply to any content that are generated by AI. Therefore, whether products qualify for copyright protection would depend on whether they meet the criteria outlined in section 7 of the Copyright Act 1987, which involves assessing whether sufficient effort has been expended to make the work original in character.

Be that as it may, numerous Malaysian ministries, agencies and sector-specific entities have roles or interests related to AI. While each of these organisations may engage in AI related activities or initiatives, they often prioritise their institutional objectives and lack a cohesive framework to guide their efforts (Tan et al., 2025). The current government capability to successfully applying its policies and achieve its objectives is vital for a good governance. This is because there is a notable shortage of professionals' public servant in AI system assessment and this problem is not only unique to Malaysia, but it is a worldwide issue (Tan et al., 2025). The rapid pace of technological advancement highlights the lack of monitoring and evaluation of AI application.

5. CONCLUSION

This paper explores the role of corporate governance mechanisms in regulating the use of Artificial Intelligence (AI) in public companies, with a focus on mitigating AI-related fraud and enhancing accountability, transparency, and trust. The rapid integration of AI in public companies has created both opportunities and challenges. On the one hand, AI can drive innovation, improve efficiency, and enable better decision-making processes. On the other hand, the absence of a

detailed legal and governance framework will expose companies to risks such as potential biases in AI systems, security breaches, and AI-enabled fraudulent activities. Without periodic reassessment, policy makers will not be able to ensure that AI systems remain compliant with ethical standard. Translating policies into enforceable legislation requires empirical evidence before the legislation can take effect. Since this study limited to the legal and governance framework using doctrinal analysis, future study should explore qualitative research design and obtain further information from AI users.

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