Forensic Accountants: The Fraudbusters

Presented by: Thomas Buckhoff, Ph.D., CPA/CFF, CFE
GASBO Presentation on November 6, 2013
Augusta Marriott Hotel

Forensic Accountants

“The bloodhounds of bookkeeping sniff out fraud and criminal transactions in corporate financial records.”

Source: U.S. News & World Report

Auditors vs. Forensic Accountants

Auditors:
- Prevent
- Deter
- Detect

Forensic accountants:
- Investigate
- Resolve
- Litigate

“Today’s auditors are not forensic accounting investigators.”
Tom Golden, PwC
Forensic Audits vs. Financial Statement Audits

- Forensic audits assess the risk and/or existence of fraud within a company.
  - Most internal frauds do not cause the financial statements to be materially misstated.
- Financial statement audits determine if the financial statements "present fairly" a company's financial position.
  - Few frauds discovered this way.

Auditors and Fraud

- External auditors maintain that management is responsible for detecting fraud (see SAS 99).
- Public expects that the external auditors should detect fraud.

The AICPA defines forensic accounting as the application of accounting to facts at issue in a legal dispute.
What is fraud examination?

“A methodology for resolving fraud allegations, which involves obtaining and analyzing evidence, taking statements, writing reports, testifying to findings, and detecting and preventing fraud.”

Fraud Theory Approach

1. Think like a criminal.
2. How could someone steal and get away with it?
3. Collect evidence to test your theory.

Phases of a Forensic Audit

1. Understand controls over cash flows
2. Identify weaknesses
3. Generate fraud theories
4. Collect and evaluate evidence
5. Estimate losses
6. Report findings
7. Assist in filing charges and/or claims
Case #1: Forensic audit

- Steve was a highly-trusted, upper-level project manager for a $40 million construction company owned by his best friend, Robert.
- After 15 years together, Robert receives a 'tip' from Steve's wife that Steve has an ownership interest in two vendors.
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Forensic Accountants: The Fraudbusters
Steve’s fictitious vendor scheme

North Central Construction → Invoices sent → Industrial Supply
Industrial Supply → Invoices paid through Specialty Supply → nothing is received

Fraud loss is total amount of payments made: $170,000

Invoices sent

Invoices paid through nothing is received

Fraud loss is total amount of payments made: $170,000
Case Resolution

- Steve confessed to the scheme and was fired.
- Steve was convicted of felony “theft by deception” and given a 12-month suspended sentence.
- Owner filed employee dishonesty insurance claim.

What is litigation support?

Forensic accountant lends his/her accounting expertise to assist in resolving a matter under dispute in a court.

Litigation Support Service Areas
Testifying as a Forensic Accounting Expert

The effective expert connects with the jury so that the jury understands, is persuaded by, and remembers the expert’s testimony.

Act 14: Economic Loss Incurred

It is my opinion that the total economic loss incurred by CVHL as a result of Act 14 by Dr. Parson is US$17,649,981 computed as follows:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
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<tbody>
<tr>
<td>BKF Valuation of Point Lepeux Block*</td>
<td>US$ 98,387,450</td>
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<tr>
<td>Lower end of range</td>
<td>US$113,040,900</td>
</tr>
<tr>
<td>Upper end of range</td>
<td>US$105,714,175</td>
</tr>
<tr>
<td>Midpoint of range</td>
<td>CVHL’s ownership interest in asset x 17.5%</td>
</tr>
<tr>
<td>Fair market value of CVHL asset</td>
<td>US$18,499,981</td>
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<tr>
<td>Less amount asset was sold for</td>
<td>US$ (850,000)</td>
</tr>
<tr>
<td>Economic loss incurred by CVHL</td>
<td>US$17,649,981</td>
</tr>
</tbody>
</table>
*Source document: WP 57

Defendant’s Bank Balances

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The Role of Expert Witnesses

➢ In professional negligence cases: To explain the infraction against professional by-laws or principles.
➢ To clarify technical or complex schemes involving accounting manipulations.
➢ To assist the court in resolving fraud-related disputes.

Case #2: Litigation support

**Plaintiff:**
MDMS is a provider of short-term, ‘pay day’ loans

**Defendant:**
Smith & Buckley is a Top 50 CPA firm with 12 offices in four states.

**Complaint:**
MDMS is suing SB for failing to uncover a $2 M fraud over eight years.
Case Background

1. Beverly, bookkeeper, embezzled $2 million and ‘hung her debit’ in loan receivables.
2. Jennifer, office manager, knew about it but did nothing, except earn a 5% commission.
3. Robert, supervisor, discovered irregularities and visited the SF office.

Auditing expert needed to determine:

1. Whether SB owed MDMS a duty to exercise due care.
2. Whether SB breached that duty, and
3. Whether the breach of duty caused the Plaintiff’s damages.

Case Resolution

1. Not surprisingly, opposing experts had opposite opinions.
2. Defense expert was disqualified for falsely claiming the CPA credential.
3. Parties reached a confidential, out of court settlement.
Testifying vs. Consulting Expert

<table>
<thead>
<tr>
<th>Testifying Expert</th>
<th>Consulting Expert</th>
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<tbody>
<tr>
<td>Review documents</td>
<td>Review documents</td>
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<tr>
<td>Express opinion</td>
<td>Express opinion</td>
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<tr>
<td>Testify</td>
<td>Litigation strategy</td>
</tr>
<tr>
<td>Subject to discovery</td>
<td>Exempt from discovery</td>
</tr>
</tbody>
</table>

Summary

An effective forensic accountant is...
- A lawyer,
- An accountant, and
- A detective
All rolled into one person.

Employment prospects:
Demand > Supply = Job openings

Who has the first question?

Oh, Oh! Pick me!
Contact info

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