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# Fraud Fighters

*Be on the forefront of the fraud offensive.*

By Sheryl Nance-Nash

"When times are good people steal, and when times are bad, they steal," says Ellen Zimiles, co-founder and CEO of Daylight Forensic & Advisory, a New York City fraud risk management firm. "Fraud is a never-ending battle. There's never a significant downturn."

According to the 2006 Association of Certified Fraud Examiners (ACFE) *Report to the Nation on Occupational Fraud & Abuse*, survey participants lost 5 percent of annual revenues to fraud. Applied to the estimated 2006 US Gross Domestic Product, this translates to about \$652 billion—an increase of 63 percent over 1996's estimate of \$400 billion.

Other surveys indicate that nearly 75 percent of individuals have observed some form of fraud or misconduct in the workplace over a 12-month period. This number has remained about the same despite the passage of Sarbanes-Oxley and the spotlight shone on compliance issues, says Kenneth Neumann, a CPA, Certified Fraud Examiner and director of business valuation and technology services at RGL Forensic Accountants & Consultants in Chicago.

Three factors contribute to the proliferation of white-collar crime. "It's extremely profitable, complex schemes by sophisticated individuals make detection difficult, and the remote likelihood of prosecution and the resulting punishment encourages such activity," says Bill Brown, a partner in the forensic accounting firm of Weaver and Tidwell in Dallas.

Indeed, it's a good time to specialize in fighting fraud. "The field of forensic accounting is exploding now, and will for the next 20 years," says Brown.

As demand rises faster than supply, salaries jump. The average compensation for Certified Fraud Examiners (CFE) can be more than \$100,000, and for non-CFEs about \$80,000, surmises Robert Brennan, a CPA, CFE and director with CBIZ Accounting, Tax & Advisory in Plymouth Meeting, Pa.

More generally, says Neumann, forensic accountants can earn 15-20 percent more than regular auditors/accountants. That higher income, however, requires a specific set of skills and additional training, among other qualifications.

Does your future lie in fighting fraud?

**Defining forensic accounting** "Forensic accounting bridges the gap between auditing and investigative disciplines, and provides the necessary resources to effectively deal with fraud," says Brown. "The key element of forensic accounting is the development of evidentiary material that establishes intent, which is defined as motivation behind a particular act, and is evidenced by material which frequently is beyond the scope of a routine audit," he explains.

Deborah Adkins, a CPA who offers forensic accounting and financial investigation services in Winter Park, Fla., says forensic accountants need to focus their training on four critical areas:

- Understanding the relationships behind the numbers and being able to see visual patterns.
- Knowing and understanding key fundamentals of the criminal or civil justice system.
- Understanding the people who commit fraud, along with the various psychological and social process theories.
- Developing investigative and examination skills to source public information and information not part of the public domain, to interview prospective witnesses, and to evaluate the potential for deception.

Usually, an audit uses sampling techniques and doesn't evaluate every transaction. However, a forensic examination will focus on one activity and look at each of the transactions, says Adkins.

Furthermore, "Because each assignment is unique, each case requires a fresh, open-minded approach to the facts and circumstances. It's important for forensic accountants to maintain a skeptical mind regarding the methodologies, assumptions and data used," says Neumann. "Although similar investigative techniques are used and similar issues often arise, it's vitally important for the forensic accountant to ask the probing questions on each case, which ultimately will uncover the facts and appropriately quantify the issues."

"My mindset is, what extraneous accounts or information may make the information I've discovered misleading? I look for a motive for bias and for intent. I gather testimonial evidence through interviews," says Brown. "A client may have a contract with an equipment vendor and the year-end inventory reveals the equipment isn't there. Either it was stolen or never got there. An interview of purchasing department personnel could reveal important information, like the purchasing director's brother works at the equipment company, or someone in the department is having financial problems," he explains. "If you're just looking at a general ledger you wouldn't learn this kind of information. I establish links, relationships and motives."

There are often red flags, says Richard T. Balog, CPA, a Jacksonville, Fla. forensic accountant who developed and leads the Forensic Accounting course for the American Management Association. "Financial ratios alone don't work. If a company is showing earnings growth but cash flow from operations is negative, look out. It can happen for one or two quarters, but not year after year; that's not right."

Another sign that someone may be doctoring the books is a financial statement that shows results of operations that are significantly different than industry peers. "There are ranges that are usually stayed within, which is why it's important to know industry standards," says Balog. Also, watch for continuous outpacing of competitors. "Companies rarely outperform peers for long periods. If someone's financials say they are top dog forever, you better check it out," he warns.

**Prevention efforts increase** Today's companies are beginning to understand that fraud prevention—rather than reaction—is a necessary evil. "Five years ago prevention wasn't prevalent. Business doesn't like to

acknowledge fraud; it's commonly referred to as the "F" word," says Brown.

Zimiles adds, "It makes sense to hire us before there's a problem. Preventative measures are cheaper. Once there's fraud, there's loss. People don't like to spend money upfront."

"There's a lot of emotional distress with fraud. Somebody wasn't paying attention. There's criticism and fear, so companies don't like to talk about fraud," says Brown.

The reality of the problem has created not only heightened awareness, but also a greater sense of urgency, especially in the age of Sarbanes-Oxley. Consequently, forensic accounting is much more than after-the-fact sleuthing.

Generally, "We will review an organization's internal controls and look for gaps, like overlapping duties that should be segregated," says Bill Kresse, CPA, Certified Forensic Accountant, CFE and professor at Saint Xavier University in Chicago (which offers graduate programs in Financial Fraud Examination & Management). "Fraud awareness is essential. Training employees about what to look for is critical, as is creating and disseminating a code of ethics. A good work environment and a positive culture takes away the common rationale for stealing—to get back at the company because the employee is disgruntled," says Kresse.

Employee assistance programs are also helpful, he explains, because they can address issues, like drug and alcohol addiction or gambling, that might be the root cause of fraud. It's not always just about greed.

Claudia Wolf, a Chicago-based partner with Deloitte Financial Services LLP, says her firm uses software and technology-based tools that can look at financial data, such as accounts payable and payroll, and match and analyze that data to identify relationships that aren't obvious, therefore detecting anomalies and spotting questionable trends. Electronic and investigative tools are necessary to get the most comprehensive results for clients, she explains.

Companies shouldn't be shy about revealing all the weapons in their fraud-fighting arsenal. "Let it be known that detection processes are in place. That alone will eliminate some fraud," Wolf advises.

That said, you can't stop everybody. "A padlock will keep many out, but a small group will have a bolt cutter to get it off," says Brown.

A huge aide in the fight against fraud is an anonymous tip hotline. Organizations with these hotlines suffered a median loss of \$100,000, compared to \$200,000, says Neumann of recent studies. Let vendors and customers know about the hotline, as well as employees. In fact, "I suggest to my clients that they include the hotline number on all check stubs, as well as customer invoices. It's also been my experience that ex-spouses, ex-boyfriends and ex-girlfriends will utilize the hotlines," says Adkins.

Neil Fishman, a CPA in Deerfield Beach, Fla. and a director of the National Conference of CPA Practitioners, says fraud is also detected through internal and external audits, periodic checks of policies and procedures (like running a dummy deal to see how rules and procedures are adhered to) and, frequently, entirely by accident.

"There are a wide range of events that warrant a company's suspicion," says Fishman. For example, employees being secretive about their work and responsibilities; employees that appear to be living beyond their means; checks clearing for unusually large amounts; checks clearing on long-dormant payables; numerous invoices from the same vendor, and invoices without proper supporting documentation."

Companies must be vigilant, says Peter D'Arruda, president, Capital Tax Advisory Group in Cary, NC. "Keep good track of files and records. Nobody should have more than one file at a time. If you have a stack on your desk, somebody could steal one and you wouldn't know it. Files, including CDs and DVDs, should have to be checked out like a library," he says.

Furthermore, fax machines should not be left unguarded when in use. "Unattended fax documents can be ripe for corporate espionage," D'Arruda explains. Careful computer monitoring is important, too. He recommends eight-digit passwords, preferably with lower case letters and numbers that are hard to crack. Codes should be changed frequently. When computers are tossed, D'Arruda advises taking the hard drives and smashing them into pieces; otherwise they can be retooled by the wrong person.

**Scrambling to meet demand** Brennan, a former IRS agent who spent more than a decade investigating tax crimes, explains how, "It never ceases to amaze me the ways and schemes people use to commit financial crimes, and how they rationalize their behavior."

Consequently, forensic accounting departments are popping up in firms everywhere; and demand for forensic accountants is at an all-time high.

There are a variety of paths to a career in financial sleuthing, including law enforcement. Brown, for example, got his training working in the FBI for nearly a decade. The AICPA offers courses on topics like money laundering and occupational fraud. The Association of Certified Fraud Examiners is the granddaddy of educators on fraud detection, while state accounting associations offer courses on topics that pertain to detecting, controlling and avoiding fraud.

If you're already in the field, look out for the competition nipping at your heels. To keep an edge, Neumann suggests "obtaining and maintaining relevant professional certifications, and participating as a teacher or a student in the certification's professional education programs. Participate in professional associations and networks related to forensic accounting, and offer to write articles and present on the topic at association meetings. Lastly, read extensively in the field."

What does it take to succeed? "You have to be analytical, a 'Doubting Thomas' type, always questioning. You should also be someone who can think outside the box and not be afraid to be confrontational when you need to be. You have to be able to work outside your comfort level," says Brennan.

"I've been told Sherlock Holmes was an accountant. If that's true, he should be the poster boy for forensic accounting," he adds.

Not that forensic accounting needs marketing. Your job may never be obsolete, says Fishman, "Fraud can happen anywhere." □

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