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Internal Audit

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We Are In this Together: CPAs in Industry and Public Practice Raising Their Awareness to Prevent Fraud

Sam Antar, a former CPA with the now-defunct Crazy Eddie's electronic chain, would be the first to agree that CPAs need to learn more about fraud. That's because Antar, now a convicted felon, helped engineer a half-billion dollar financial statement

fraud that was made possible by taking advantage of the company's independent auditors.

Antar, along with a half-dozen other fraudsters, are featured in a new 8-hour self-study program designed to teach CPAs in industry and public practice the basics of how fraud is committed against organizations.

The interactive CD, *Fraud and the CPA*, features video clips of criminals describing their schemes. It was jointly produced by the AICPA and the Association of Certified Fraud Examiners (ACFE) as part of both organizations' efforts to increase CPE offerings in fraud prevention, detection and deterrence.

Barry C. Melancon, president and CEO of the AICPA, put it bluntly. "CPAs must join together to restore the profession's reputation. One of the ways CPAs can lead the way in fraud prevention and detection is to commit more time to CPE in this area and ensure that their skills and understanding are up to date."

The new course (see article in this issue) covers the following major topics:

The Cost of Fraud. As recent headlines about multi-billion dollar cases such as Enron and WorldCom show, the cost of illegal corporate conduct is staggeringly high and covers myriad nefarious activities ranging from expense account abuse to financial statement fraud. And this is not just for the largest corporations. Companies of all sizes are severely damaged by fraud.

In the ACFE's 2002 *Report to the Nation on Occupational Fraud and Abuse*, it is estimated that the average organization will lose about 6% of its revenues to all forms of occupational fraud. Moreover--as recent high-profile cases have shown—not only do investors lose billions, but employees lose their jobs and pensions, and the erosion of confidence in capital markets can have a devastating effect on the economy.

The CPA's Fraud-Related Responsibilities. Controlling fraud is a collaborative effort between the CPA and corporate America. Nonetheless, independent auditors have certain responsibilities when it comes to detecting fraud and other illegal acts. Moreover, other CPAs may have legal obligations to report suspected fraud. It is important for CPAs to know what to do if they believe a fraud may have occurred. It also is important, especially if they work in business and industry, that they understand the new responsibilities under the Sarbanes-Oxley Act, which requires CEOs and CFOs to certify company financial statements.

Who Commits Fraud and Why. From the mailroom to the boardroom, people who choose to commit fraud usually believe they are justified in doing so. It is vital for the CPA to understand the factors that motivate this type of conduct. Actual offenders like Sam Antar, in video clips, describe what they did and why.

- Kay Lemon, the bookkeeper for a Midwestern lighting store, stole \$416,000 in cash, which she used to greatly improve her lifestyle
- Tim Sasak, a former CPA, defrauded investors of over \$40 million in a classic real estate Ponzi scheme. His motivation was to cover bad investments he had made.
- Barry Minkow, the reputed "boy wonder" in the now-classic \$100 million ZZZZ Best fraud, fooled his independent auditors. He describes the simple tricks he used.

These case studies illustrate that "ordinary" people commit fraud. The culprit could be a coworker or a trusted client. To detect and deter fraud, CPAs must have a heightened sense of professional skepticism.

Fraud Schemes. There are three principle types of occupational fraud: fraudulent statements, corruption and asset misappropriations. For each type, there are specific schemes that CPAs must know. Several schemes are commonly used to manipulate financial statements, two involving corruption, and four major schemes are used to misappropriate assets. For each, there are also numerous variations and sub-schemes. CPAs in business and industry who are familiar with the ways fraud is committed against organizations are in a much better position to recognize their unique red flags and minimize or avert fraud losses.

Fraud Prevention. Preventing fraud goes far beyond internal control. There are three main factors that control the risk of fraud: pressure, opportunity and attitude. By understanding and applying the three elements of what has become known as the "fraud triangle," CPAs can start developing a more complete picture of the causes and cures for fraud. Accountants have a unique and important role in preventing fraud, but they can't do it alone. This concluding section puts fraud prevention in its proper context, and offers suggestions for improving fraud detection and deterrence.

" The objective of this course is to raise awareness of fraud within the accounting profession and corporate America," said Melancon. "This information is vital, because to find fraud, we must understand the human element—why people commit fraud and what opportunities and factors aid in their decision. By advancing our knowledge in this area, we can help solve the problem."

Toby J.F. Bishop, president and CEO of the ACFE, said that the jointly produced video is but one of several projects planned by the two associations. "Education is the cornerstone of fraud prevention. In Dec., the AICPA and ACFE released a free interactive CD entitled *How Fraud Affects You and Your Organization*. The one-hour training program is designed to educate employees of all organizations about fraud." The training program is viewable, free of charge, at www.aicpa.org/antifraud.

Melancon said that the AICPA will also be working with universities to survey the current state of fraud education, and with textbook publishers to integrate appropriate

fraud-related material. In addition, the AICPA will assist the ACFE's ongoing efforts to provide free educational resources to colleges and universities.

" Joseph Wells, the ACFE's founder and chairman of the board, was one of the first to act on the need for antifraud education by providing materials without charge to institutions of higher learning. It is important that tomorrow's accounting graduate enters the workforce better prepared to fight the battle against fraud," Melancon said.

For CPAs in practice and in industry, *Fraud and the CPA* represents a major effort to reshape the way the accounting profession views the phenomenon of fraud. In the words of ACFE's Bishop, "We CPAs are very adept at our knowledge of accounting concepts. But books and records don't commit fraud; people do. And in the war on fraud, this course helps us recognize who the enemy is."

Live Webcasts for Financial Professionals

Chief financial officers and other top financial professionals have teamed up with the AICPA and CFO.com experts to help you manage complex issues pertaining to off-balance-sheet financing, auditing, ERISA, XBRL, corporate disclosure, financial reporting, treasury management and more. The quarterly CFO Roundtable Series, which began in Oct. 2002, is a cost-efficient and time-efficient way to stay plugged in to professional developments in this turbulent economic and regulatory climate while earning continuing education credits.

Here is the schedule for the remainder of the CFO Roundtable Series:

Jan. 16, 2003 1:00 p.m. – 2:55 p.m., ET

May 15, 2003 1:00 p.m. – 2:55 p.m., ET

July 17, 2003 1:00 p.m. – 2:55 p.m., ET

A single event costs \$79 with 8 CPE credits per subscription. Registrations cannot be accepted after noon Eastern Time on the day of the Webcast.

For ordering information, visit www.cpa2biz.com/webcasts or call 888/777-7077.

AICPA and Association of Certified Fraud Examiners Issue CD-ROM Primer on Fraud

In an effort to help educate the U.S. business community about the economic consequences of fraud, the AICPA and the Association of Certified Fraud Examiners have developed a one-hour training program on CD-ROM, entitled *How Fraud Hurts You and Your Organization*.

The CD takes the user through the definition of fraud, examples of fraudulent activity, real-life case studies, the psychological aspects of fraud, warning signs, and the people who are responsible for preventing fraud. It also includes a 13-minute video featuring interviews with three people who were convicted of fraud, including Sam Antar, who was the Chief Financial Officer of Crazy Eddie Electronics.

"The first line of defense to prevent or detect fraud is to deploy effective antifraud programs and controls within every business in America," said Barry C. Melancon, AICPA President and CEO. "It's imperative that everyone understand the motivation for fraud and how frauds are committed."

"According to a study we conducted, internal fraud may cost as much as \$600 billion a year, or \$4,500 for every worker," said Joseph Wells, Chairman of the Association of Certified Fraud Examiners. "Fraud harms both the company and the individuals who work there."

How Fraud Hurts You and Your Organization is the latest installment in the AICPA's multifaceted antifraud campaign, which Melancon announced in a Sept. 4 speech at the Yale Club in New York. It began in October with the release of a new standard that gives auditors expanded guidance in detecting fraud. Last month, the Institute, along with six other professional organizations, produced a set of antifraud programs and controls for boards of directors and management. Currently in development are a fraud summit and an Institute for Fraud Studies with the Association of Certified Fraud Examiners and the University of Texas.

"The potential for fraud is always present," Melancon said. "As such, we must continually update our knowledge, skills and standards."

How Fraud Hurts You and Your Organization is available free of charge. The CD may be obtained by contacting Member Satisfaction; see the main section of this CPA Letter for ordering instructions. Include \$8.00 for shipping and handling. Or, the program may be viewed from www.aicpa.org/antifraud.

From the AICPA and the Association of Certified Fraud Examiners

NEW! Fraud and the CPA

All CPAs have a responsibility to be diligent in preventing and detecting financial statement fraud. Whether you are a preparer of financial statements, an auditor, or just want to help your company or your clients, this course will help you be more effective in preventing and detecting such devastating frauds. In today's environment, this is knowledge you can't afford not to have.

Objectives

- Gain insights from fraud specialists that will deepen your fraud knowledge, enhance your professional skepticism and improve your decision processes
- Understand the different ways people "cook the books" and learn what to watch out for
- Go beyond the checklists and learn to think like a fraudster so you can catch them

Prerequisite: None

Estimated CPE Credit*: 8

QAS Credit: TBD

Level: Intermediate

Format: CD ROM

No. 731730hs CPA01

15% Discount!

AICPA Member Special Introductory Offer

\$98.60 (Regular price \$116)

Non-member Special Introductory Offer

\$123.25 (Regular price \$145)

* CPE credit for this course is estimated and will be finalized when the course is published. Recommended CPE Credit is based on pilot testing. Order by phone and a Member Satisfaction representative will confirm credit and price. You will be able to order this course online when recommended CPE credit and price are final.

Enewsletter Designed for Members in Business and Industry

The New Finance Team, which supports AICPA members in business & industry, communicates with members through a twice-per-month electronic newsletter called BusIndNews. This newsletter is written specifically for the perspective of CPAs practicing the profession in business & industry. It is text-only and to the point, and provides an up-to-date look at the field of accounting and the current state of the

profession, as well as a quick look at where we will be tomorrow. However, we can't reach you unless we have your e-mail address!

If you would like to receive BusIndNews, please send us your e-mail contact information to: [BusIndNews@ aicpa.org](mailto:BusIndNews@aicpa.org) with the subject line "Send BusIndNews."

Seven Professional Associations Jointly Issue Antifraud Programs and Controls to Help Management Combat Fraud

Seven professional associations have taken an important step towards restoring public confidence in financial reporting. Together, these organizations have developed a set of recommendations specifically to help boards of directors, audit committees and management prevent and root out fraud. These recommendations are contained in a new document titled *Management Antifraud Programs and Controls: Guidance to Help Prevent, Deter, and Detect Fraud*.

The organizations that sponsored the document are the American Institute of Certified Public Accountants, Association of Certified Fraud Examiners, Financial Executives International, Information Systems Audit and Control Association, Institute of Internal Auditors, Institute of Management Accountants, and the Society for Human Resource Management. Other organizations that participated in reviewing and offering advice include American Accounting Association, Defense Industry Initiative, and the National Association of Corporate Directors.

"Antifraud research suggests that the most effective way to implement measures to reduce wrongdoing is to base them on a set of core values that are embraced by the entity," states the introduction to *Management Antifraud Programs and Controls*.

The document identifies the measures an organization can take to prevent, deter and detect fraud, which can range from falsified financial statements to employee theft. Antifraud programs and controls, the document maintains, evolve from three fundamental actions:

- **Creating a culture of honesty and high ethics.** Directors and officers of corporations set "the tone at the top" for ethical behavior within any organization. Senior financial officers hold an important and elevated role in corporate governance. As members of the management team, they are uniquely capable and empowered to ensure that all stakeholders' interests are appropriately balanced, protected and preserved.
- **Evaluating antifraud processes and controls.** Neither fraudulent financial reporting nor misappropriation of assets can occur without a perceived opportunity to commit and conceal the act. Organizations should be proactive in reducing fraud opportunities by:

- identifying and measuring fraud risks
- taking steps to mitigate identified risks
- implementing and monitoring effective internal controls
- **Developing an appropriate oversight process.** To prevent or deter fraud, an organization should have an appropriate oversight function in place. The audit committee should evaluate management's identification of fraud risks, implementation of antifraud measures and creation of the right "tone at the top." It should also make sure that senior management, particularly the CEO, has antifraud measures in place to protect investors, employees and other stakeholders. The audit committee also plays an important role in helping the board of directors fulfill its responsibilities to oversee the company's financial reporting procedures and system of internal controls.

Strong antifraud programs and controls, such as those described in this document, should help companies save revenue, enhance their market value, avert civil lawsuits and maintain a positive image.

Management Antifraud Programs and Controls is available from any of the sponsoring organizations and can be accessed at:
www.aicpa.org/antifraud/management/.