

# FORENSIC ACCOUNTING

THE WHATS, WHYS, AND HOWS OF FORENSIC ACCOUNTING

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## FORENSIC ACCOUNTING: STOPPING TODAY'S FINANCIAL CRIMINALS IN THEIR TRACKS

Enron, Worldcom, Tyco, Bernie Madoff, Stephen Cohen - These names have special meaning in today's business culture, just like John Dillinger, Baby Face Nelson, and Bonnie and Clyde were recognized names in the 1930s. But instead of recognition for robbing banks, these subjects and companies are all recognized for a different crime: committing massive frauds that caused catastrophic losses. Like the Depression-era bank robbers, these frauds also resulted in the enactment of new federal legislation that changed our business environment forever.

We all know how those notorious bank robbers were ultimately caught, but how were these disastrous financial frauds discovered, investigated and prosecuted? Who possessed the unique skill set necessary to track down these complex accounting frauds and then trace and locate the proceeds of the illegal activity? Welcome to the exciting world of forensic accounting, a relatively new and rapidly growing profession dedicated to investigating complex financial crimes and frauds.

## WHAT IS FORENSIC ACCOUNTING?

When we hear the word forensic, we usually think of popular TV shows like CSI, NCIS, or Law and Order, where a crime is committed and detectives and investigators use various forensic techniques (fingerprints, DNA analysis, blood splatter analysis, tool mark identification, hair and

fiber comparisons, etc.) to solve the crime, usually within 60 minutes! On the other hand, the word accounting reminds us of debits, credits, financial statements, tax returns and auditing. How do these two terms fit together?

Well, the word forensic is derived from the Latin word "forum," which means of, or relating to, the legal system or court. The broader definition of forensic simply means applying scientific knowledge to legal issues. Forensic accounting melds special scientific and mathematical skills in accounting, auditing, risk analysis, quantitative methods and research with investigative techniques, law, courtroom procedure and digital forensics.

**Forensic accountants are accountants specially trained as financial investigators and fraud experts.**

Synonyms for forensic accounting include financial investigation, investigative accounting and fraud examination. In fact, the term financial investigation or fraud examination is often preferred by some educators and authors because those words are better understood by the general public and more descriptive of what forensic accountants actually do.

## WHY DOES BUSINESS NEED FORENSIC ACCOUNTING?

Fraud is theft by deceit, misrepresentation and trickery. The costs are staggering. The most recent statistics

estimate that \$3.7 trillion (5 percent of all revenue) is lost annually to fraud with most of that cost being ultimately passed on to the consumer and the taxpayer – all of us.

In reality, the cost of fraud is probably both unknown and unknowable because, by its very nature, fraud involves concealment and deceit. But, in its 2014 Report to the Nations on Occupational Fraud and Abuse, the Association of Certified Fraud Examiners estimates the median loss due to fraud in 2013 at \$155,000 per case or incident.

Although the specific category for “financial statement fraud” only accounted for 9 percent of all fraud incidents, it had the greatest median loss — more than \$1 million per incident. “Corruption” was the next category, totaling 37 percent of total fraud incidents reported with a median loss of \$200,000. Finally, asset misappropriation was the largest category of all fraud incidents reported with a median loss of \$130,000.

**These dramatic statistics demonstrate the need for financial investigators and forensic accountants with an expertise in fraud matters.**

Sadly, 58 percent of all fraud victims never recover any of their losses, according to the association’s study. For example, all the innocent employees who dedicated their careers working for Enron lost years of their

accumulated retirement savings because the company executives convinced them to invest it in Enron stock, which was ultimately worthless as the result of fraud and the resulting bankruptcy.

## WHAT DOES A FORENSIC ACCOUNTANT DO?

The work of a forensic accountant/financial investigator is exciting and varied. No two days are alike and job satisfaction is very high.

Forensic accountants do not spend their workdays sitting in a cubicle staring at a computer screen. Forensic accountants plan, coordinate, and direct financial aspects of investigations in cooperation with prosecutors, attorneys and other investigators. Forensic accountants investigate complex financial crimes involving all types of fraud including corporate fraud, financial institution fraud, securities fraud and insider trading, health care fraud, money laundering, commodities fraud and governmental fraud.

Federal law enforcement agencies also use financial investigators in counterterrorism, public corruption, bribery, counterintelligence, cybercrime and organized crime matters. Today’s complex cases and prosecutions always include a thorough financial investigation regardless of the nature or type of crime committed.

Forensic accountants also develop profiles of individuals and groups, conduct interviews of subjects and witnesses,



gather evidence and prepare affidavits for use in court. A forensic accountant will often conduct a detailed financial analysis of business and personal records in a never-ending quest to follow the money. They summarize their findings and conclusions in financial investigative reports and exhibits and frequently testify about their financial investigations before grand juries and as a fact or expert witness at criminal and civil trials.

Because of their unique skill set, forensic accountants are in high demand in private industry and with governmental agencies such as the Federal Bureau of Investigation, Internal Revenue Service, Securities and Exchange Commission, Treasury Department and the various offices of the Inspector General.

A little known fun fact is that when the United States Bureau of Investigation (later to be renamed the FBI) was originally formed in 1908, it hired 20 accountant/bank examiners as its first special agent investigators. Because it has jurisdiction over most complex financial crimes and corruption, the FBI still seeks this unique skill set and has

continued to hire large numbers of forensic accountants throughout its history.

## WHAT SKILLS AND TRAINING DO TODAY'S FORENSIC ACCOUNTANTS NEED?

Today's financial investigator must also have a strong working knowledge of both digital and web forensics as well as cybercrime awareness. Cybercrime is often just garden-variety fraud that is perpetrated using the internet and a computer as instruments to commit the crime.

**The essence of fraud has not changed; just the communication method or means has evolved from the mail and telephone to the e mail because of technological advances.**

Gathering the evidence of crime, as discussed above, usually includes seizing information stored in digital form in computer hard drives or in the cloud.

The successful and well-trained forensic accountant/financial investigator must know how to seize and preserve digital information regardless of how it is stored or where it is located. Since e-mails commonly contain explanations of criminal conduct, if not outright incriminating evidence (the proverbial smoking gun), forensic accountants also learn web forensics and how to trace and retrieve digital information as it flows around the world through the internet. Forensic accounting students who desire a deeper knowledge in digital forensics are encouraged to enroll in classes offered through the Florida Center for Cybersecurity at USF.

Technology and greed have combined to change the corporate landscape and environment and business crime over the past few decades.

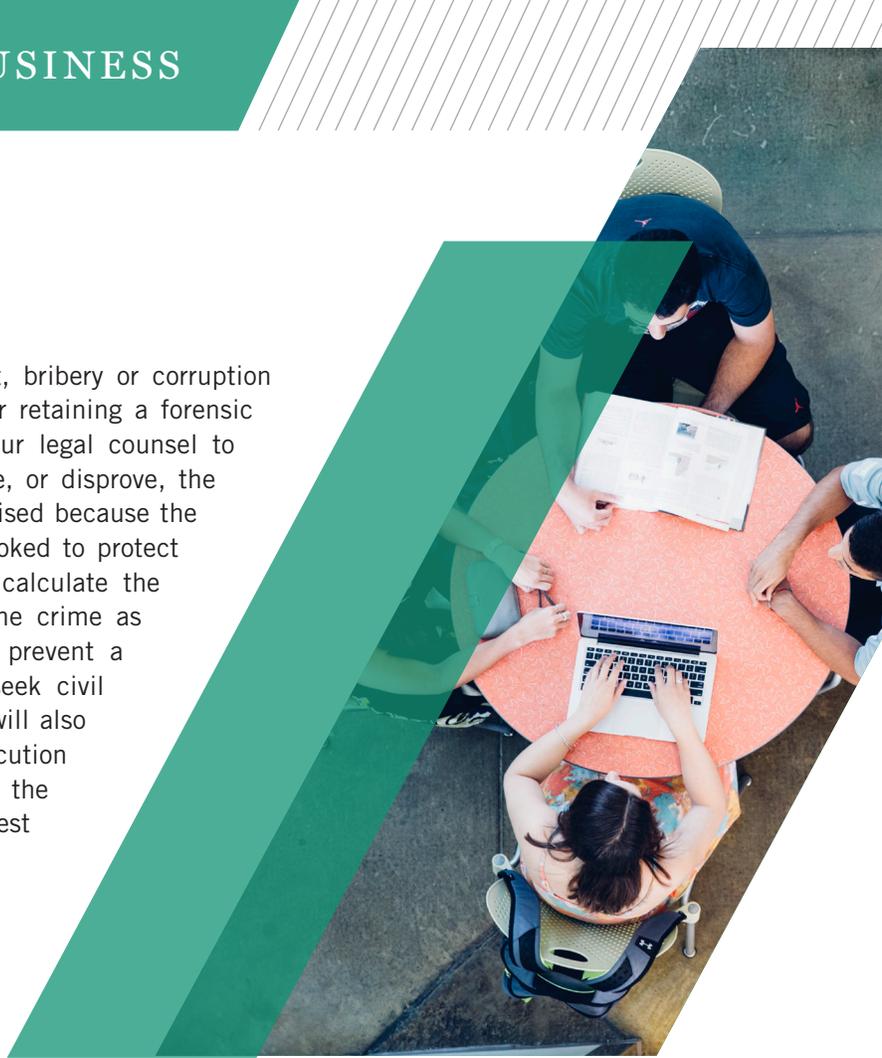
**Today's financial experts require skills that were not contemplated even 20 years ago.**

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## HOW CAN FORENSIC ACCOUNTING BENEFIT YOUR BUSINESS?

If you suspect that any type of financial fraud, theft, bribery or corruption is occurring at your organization, you should consider retaining a forensic accountant. A forensic accountant can work with your legal counsel to conduct the financial investigation necessary to prove, or disprove, the occurrence. Working through your legal counsel is advised because the protections of the attorney-client privilege can be invoked to protect the investigation. The forensic accountant can also calculate the damage sustained by your business as a result of the crime as well as recommend improved control procedures to prevent a reoccurrence in the future. Your organization may seek civil restitution of the loss. The professional investigation will also increase the probability of a successful criminal prosecution should your organization want to proceed against the perpetrators criminally. Preventing fraud is in the interest of every business owner, taxpayer and consumer.



## ABOUT THE AUTHOR



Kerry Myers is a clinical professor in the USF Lynn Pippenger School of Accountancy and is also part of the Florida Center for Cybersecurity. He teaches graduate classes on forensic accounting, drawing from his 25 years as both an attorney and an accountant with the Federal Bureau of Investigation. He was one of the original members of the Tampa Bay Bank Fraud Task Force and served on the Tampa Joint Terrorism Task Force. He was also certified as a bomb technician with the FBI and worked the Oklahoma City Bombing, Centennial Park Bombing in Atlanta, and the TWA Flight 800 crash off of Long Island Sound. Myers received the Federal Law Enforcement Officers' Association Annual Award for Bravery in 2008 for his work in Afghanistan with improvised explosive devices, and a Director's Award from then-FBI Director Louis Freeh for leading a national terrorism undercover operation.

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