FORM A: ABDC 2013 JOURNALS LIST REVIEW  
NEW ACADEMIC JOURNAL SUBMISSION

*** PLEASE NOTE THAT: FORM A is designed to formalise requests to the ABDC Journals Review Panel 2013 seeking the inclusion of an academic journal which is currently omitted from the ABDC 2010 list. Previously unrated journals should only be nominated in this form where a clear case can be made for them (a) achieving a minimum “business element test” and (b) satisfying a minimum threshold of research quality. Please complete a separate form relating to each journal for which you wish to make a submission of this type.

Journal Title: Journal of Forensic & Investigative Accounting

| QA1. FIELD of RESEARCH (FoR) PANEL to which this request is directed (tick one box only): |
|---------------------------------|----------------|
| 0806 Information Systems        |     X 1501 Accounting |
| 1401-1499 Economics             | 1502 Finance |
| 1501 Accounting                  | 1503 Management |
| 1502 Finance                     | 1504-07 Marketing/Tourism/Logistics |
| 180105/1801025 Business and Taxation Law |

<table>
<thead>
<tr>
<th>QA2. WHAT ABDC 2013 RATING DO YOU PROPOSE FOR THIS JOURNAL?</th>
</tr>
</thead>
<tbody>
<tr>
<td>A*</td>
</tr>
<tr>
<td>A</td>
</tr>
<tr>
<td>B</td>
</tr>
<tr>
<td>C</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>QA3. IN ERA 2010, WHICH FoR GROUP WAS THIS JOURNAL ASSIGNED?</th>
</tr>
</thead>
<tbody>
<tr>
<td>0806 Information systems</td>
</tr>
<tr>
<td>1401-1499 Economics</td>
</tr>
<tr>
<td>1501 Accounting</td>
</tr>
<tr>
<td>1502 Finance</td>
</tr>
<tr>
<td>1503 Management</td>
</tr>
<tr>
<td>1504-07 Marketing/Tourism/Logistics</td>
</tr>
<tr>
<td>180105/1801025 Business and Taxation Law</td>
</tr>
<tr>
<td>OTHER: please specify</td>
</tr>
<tr>
<td>New journal not previously ranked</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>QA4. WHAT ERA 2010 RATING WAS THIS JOURNAL ASSIGNED?</th>
</tr>
</thead>
<tbody>
<tr>
<td>A*</td>
</tr>
<tr>
<td>A</td>
</tr>
<tr>
<td>B</td>
</tr>
<tr>
<td>C</td>
</tr>
<tr>
<td>not applicable</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>QA5. NOMINATE “THE BEST” COMPARATOR JOURNAL (journal from the ABDC 2010 list that is most similar in research quality):</th>
</tr>
</thead>
<tbody>
<tr>
<td>Journal of Forensic &amp; Investigative Accounting</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>QA6. JOURNAL INFORMATION</th>
</tr>
</thead>
<tbody>
<tr>
<td>Publisher: E.J. Ourso School of Business and the Department of Accounting</td>
</tr>
<tr>
<td>Frequency: 2</td>
</tr>
<tr>
<td>Current Volume: 5 Current Issue: 2 ISSN: 2165-3755 First Year Published: 2009</td>
</tr>
<tr>
<td>Refereed (please tick one): [ ] yes [ ] no</td>
</tr>
<tr>
<td>Editor’s Name: D. Larry Crumbley Institution: Louisiana State University</td>
</tr>
<tr>
<td>Web Address: <a href="http://www.bus.lsu.edu/accounting/faculty/lcrumbley/jfia/Default.htm">http://www.bus.lsu.edu/accounting/faculty/lcrumbley/jfia/Default.htm</a></td>
</tr>
</tbody>
</table>

NATURE OF SUBMISSION

<table>
<thead>
<tr>
<th>QA7. Primary submitter type (tick one box only)</th>
</tr>
</thead>
<tbody>
<tr>
<td>[ ] Higher Education Institutional Submission (e.g. formal submission from Business Faculty/School)</td>
</tr>
<tr>
<td>[X] Peak Body Submission (e.g. AFAANZ, ANZAM)</td>
</tr>
<tr>
<td>[ ] Individual Submission</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>QA8. Primary submitter: ABDC Panel</th>
</tr>
</thead>
<tbody>
<tr>
<td>Institutional Affiliation:</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>QA9. Are there other signatories to this submission? [ ] Yes [ ] No</th>
</tr>
</thead>
<tbody>
<tr>
<td>If yes, how many signatories are there (including the primary submitter)?</td>
</tr>
</tbody>
</table>
As shown in the appendices to this submission, Journal of Forensic & Investigative Accounting:
* has a mix of academic representation on its Editorial Board (refer to App A2)
* is primarily an accounting journal as reflected in its title and description of journal (refer to App A3)
* relates to accounting and business as reflected in recent tables of content (refer to App A8)
SUPPLEMENTARY INFORMATION: APPENDIX CHECKLIST

The ABDC invites further supplementary and supporting information to be submitted by way of appendices.

**QA11. Mandatory “substantive business element test” (please tick one box only):**

☐ **Appendix A1:** Substantive business element test

- Simple metrics that demonstrate a substantive “business” element relating to the relevant FoR Panel e.g. > 50% of articles over 3 years written by business faculty or > 50% of articles over a recent 3-year period are of a business nature. For the purposes of this test, a research area is deemed to be “business” related provided that it meaningfully relates to (at least) one of the FoR Panels established for the ABDC journal list review.
- The Editorial Board list and clearly establish that many academics on the board have meaningful links to the relevant area of business-related research.

☐ ERA 2013 FoR code is the same as the requested FoR designation (i.e. answer for QA1 = QA3) – **Appendix A1 is NOT required.**

**QA12. What supplementary information are you supplying (by way of appendices) to support your submission?** (these appendices should be seen to be optional – you have discretion over those that you choose to supply and those that you choose to ignore).

The following documents are attached in support of this application (please tick boxes as relevant):

- ☒ **Appendix A2:** List of Editorial Board Members
- ☒ **Appendix A3:** Description and Scope of Journal
- ☐ **Appendix A4:** Recommendations from eminent scholars in the relevant field
- ☐ **Appendix A5:** Comparisons with existing rated journals
- ☐ **Appendix A6:** Coverage in review articles
- ☐ **Appendix A7:** Impact Factors: SSCI or others
- ☒ **Appendix A8:** Other supporting documentation
- ☐ **Appendix A9:** Signatory Details – in cases where there are more than one signatory to the submission, list all signatory names and their university or relevant affiliations (this appendix should articulate with the answer given to QA8 above).
APPENDIX A2

EDITORIAL BOARD
Editorial Advisory Board

A

Husam Abu-Khadra, Ph.D., Roosevelt University

B

Charles Barne-Aldred, Ph.D., Northeastern University

Richard A. Bernardi, Ph.D., Roger Williams University

Linda Bressler, University of Houston-Downtown

Len Brooks, B.Com., MBA, FCA, University of Toronto

Thomas Buckhoff, Ph.D., CPA, CFE, CFF, Georgia Southern University

Priscilla Burnaby, Ph.D., Bentley College

C

James Cali, CPA, University of Missouri

A. J. Cataldo II, Ph.D., CPA, CMA, West Chester University

Natalie Tatiana Churyk, Ph.D., CPA., Northern Illinois University

D

Ronald J. Daigle, Sam Houston State University

James A. D'Gabrielle, CPA/ABV/CFF, CFE, Cr.FA, CVA, Montclair State University

Cindy Durtschi, Ph.D., DePaul University

E

Dana A. Forgione, Ph.D., CPA, CMA, CFE, University of Texas at San Antonio

Thomas Freeka, Ph.D., University of Notre Dame

Ross D. Fuerman, JD, Ph.D., Suffolk University

F

Brian Greenstein, Ph.D., University of Delaware

H

Carol A. Hartley, Providence College

Lester E. Hetiger, Ph.D., Missouri State University

Tanweer Hasan, Roosevelt University

Robert Holtflether, Ph.D., Central Washington University

Wm. Dennis Huber, JD, DBA, MBA, MA, MS, EdM, CPA, CMA, CIA, CISA, CFSA, CFM, CFE, CCP, Capella University

K

A. K. M. Waresul Karim, Saint Mary's College of California
J. Edward Ketel, Ph.D., Penn State University
Linda A. Kidwell, Ph.D., University of Wyoming
Katherine Kinkela, Iona College

L

Chih-Chen Lee, Ph.D., CPA, Northern Illinois University
Constance M. Lehmann, Ph.D., CISA, University of Houston, Clear Lake
Tim J. Louwers, James Madison University
Patrick M. Lynch, CPA, CFF, CrFA, CFE, Loyola University, New Orleans

M

Charles A. Malgwi, Ph.D., CFE, Bentley University
Diane A. Matthews, Ph.D., CPA, CFE, CFF, Carlow University
Dorothy A. McMullen, Ph.D, CPA, CFE, FCPA, CICA, Rider University

Jeffrey E. Michelman, Ph.D., University of North Florida
Santana Mitra, Ph.D., FCA, MBA, M.Com, Wayne State University, Detroit
Jackie Moffitt, Ph.D., CPA, Louisiana State University
Janice Taylor Morris, Ph.D., CPA, Sam Houston State University
Philip W. Morris, Ph.D., CPA, CFE, Sam Houston State University
Roselyn E. Morris, Ph.D., CPA, Texas State University-San Marcos

N

Thomas G. Noland Ph.D, CPA, CMA, CDFM, University of South Alabama

P

Carl Pacini, Ph.D., CPA, CFSA, Florida Gulf Coast University
Deborah D. Pavelka, Ph.D., CPA, Roosevelt University
Timothy Pearson,Ph.D., CPA, CFF, West Virginia University
Kelly R. Pope, DePaul University
Scott Porter, CA, DIFA, The Institute of Chartered Accountants of Ontario

R

Sridhar Ramamoorti, Ph.D., ACA, CPA/CITP/CFF, CIA, CFE, CFFA, CFSA, CGAP, CGFM, CRP, CICA, FCPA; School of Accountancy & Center for Corporate Governance, Kennesaw State University
Kenneth Reichelt, Ph.D., CA, Louisiana State University
Zabihollah Rezaee, CPA, CMA, CFE, University of Memphis
Nazik Roufaiel, Ph.D., CPA, CIA, CMA, CFM, CFE, State University of New York, ESC-CDL

S

Jeremy T. Schwartz, Ph.D., Hampden-Sydney College
Mike Seda, Ph.D., Shaw University
Debra T. Sinclair, Ph.D., CMA, AVA, University of South Florida - St. Petersburg
Tommie Singleton, Ph.D., CISA, CMA, CPA, CITP, CFS, University of Alabama Birmingham
Charles Smedmor, Smedmor & Associates
The Journal of Forensic & Investigative Accounting (JFIA) publishes creative and innovative studies employing research methodologies that logically and clearly identify, describe and illuminate important academic forensic accounting, fraud, and litigation services issues; tests and improves forensic accounting research skills, tools, and techniques; stimulates discussion and experimentation in instructional means, methods, and materials in the field of forensic accounting and research in general; exchanges of ideas and findings about developments related to instruction, learning, and curricular issues in forensic accounting and fraud education.

The Journal of Forensic & Investigative Accounting solicits unpublished manuscripts not currently under consideration by another journal or publisher. Each article will be published electronically as soon as the editor, based upon advice from referees, determines that the manuscript meets the objectives and standards set forth by the editor and the journal's editorial board.

Review Process

Each manuscript submitted to The Journal of Forensic & Investigative Accounting is subject to the following review procedures:

1. The manuscript is screened by the editor for general suitability.
2. If the manuscript passes the initial editorial screening, it will be blind-reviewed by at least two reviewers.
3. In light of the reviewers' recommendations, a decision will be made by the editor as to whether the article will be accepted as is, revised, or rejected. It is anticipated that the decision will be communicated to the author within four to six weeks after submission.

The process described above is a general one. The editor may, in some circumstances, vary this process at his or her discretion. Through its constructive and responsive editorial procedures, the journal aims to render research efforts relevant and rewarding for all concerned.

Submission Requirements

Manuscripts are expected to be original research that has not been previously published and is not currently under review by another journal. If measurement instruments (questionnaires, case, interview plan, etc.) have been developed by the authors and are an integral part of the study, copies should be included with the manuscript. Manuscripts are to be submitted via email to dcrumbl@lsu.edu as a MS Word file. A nonrefundable $50 fee must be paid to the editor. Checks are to be made out to Larry Crumbley - editor. Please indicate how the submission fee requirement has been satisfied when you submit your manuscript. Revisions must be submitted within 12 months from notification; otherwise the manuscript will be considered a new submission.

Style


Format

1. All manuscripts should be double-spaced, except for indented quotations.
2. Margins settings should provide for at least one inch top, side, and bottom margins.
3. A cover page should include the title of the paper, the author's name, title and affiliation, any acknowledgments, and a footnote indicating whether the author is willing to share the data (see policy statement below).
4. All pages, including tables, appendices, and references, should be serially numbered.
5. Spell out numbers from one to ten, except when used in tables and lists, and when used with mathematical, statistical, scientific, or technical units and quantities, such as distances, weights and measures. For example:
The Effects of Communication Media and Client Familiarity on Auditors' Confidence in Deception Detection

Meghann Cefaratti
Reza Barkhi

Abstract: Auditors collect audit evidence through client inquiry. When auditors incorporate audit evidence gathered via client inquiry, they must be able to detect deception to be effective. Detection of deception, in the information that is communicated, may be more difficult with the proliferation of web-based communication applications. These applications represent an efficient approach to facilitate the exchange of information between auditors and audit clients. However, the effectiveness of the information exchange between auditors and audit clients may be more challenging for audit clients that are unfamiliar (i.e., new clients). We collected data from 84 participants (upper level accounting students) to study the influence of communication mode and familiarity with the client on auditors' perceived ability to detect deception. We find that, consistent with Media Richness Theory and Channel Expansion Theory, leaner forms of communication media and less familiarity with the audit client lead to a diminished confidence in ability to detect deception. Our study provides support for auditors’ consideration of the most appropriate form of communication before gathering information from a client.

Keywords: Auditing, deception, deception detection, familiarity, media richness.

Download: Abstract [PDF] Full Article [PDF]

Wi-Fi Hotspots: Secure or Ripe for Fraud?

Richard G. Brody
Kyle Gonzales
Dustin Oldham

Abstract: This paper explores the threats involved with accessing public wireless fidelity (Wi-Fi) hotspots, and how sensitive information can be compromised by malicious users to commit fraud. Every network contains a service set identifier (SSID), which can be exploited to conduct an attack on a wireless unprotected public network. Since unprotected wireless networks are susceptible to attacks, security mechanisms surrounding wireless networks are necessary. Older wireless encryption algorithms such as Wired Equivalent Privacy (WEP) have become deprecated due to malicious users successfully cracking the key. Presently, Wi-Fi Protected Access (WPA & WPA2) is the industry-best standard for maintaining a secure wireless connection to mitigate any attempts of acquiring information from other users on the network. Attackers can use various techniques to harvest critical information from users on the same network, which can be used to commit fraud. The most common fraudulent actions by the attacker includes activities such as obtaining authentication credentials, conducting social engineering attacks, and acquiring sensitive information for personal gain. This article will examine the technology associated with Wi-Fi, vulnerabilities associated with using public Wi-Fi, methods for exploiting vulnerabilities to commit fraud, and preventative measures that can be taken to avoid becoming a victim of fraud.

Keywords: Wireless fidelity, service set identifier, wired equivalent privacy, Wi-Fi protected access, wireless security.

Download: Abstract [PDF] Full Article [PDF]
+ Fraud-Risk Factors and Audit Planning: The Effects of Auditor Rank

   - David S. Kerr

Abstract: This research examines the association between external auditors' position in their firm (rank) and their consideration of fraud risk factors when planning an audit. Included in this examination is a study of the relationship between rank and judgmental agreement among auditors concerning the effects of risk factors on the extent of substantive testing.

Results reveal that, when planning the extent of testing, audit managers place greater relative importance on tone-at-the-top than do senior auditors, who give it greater importance than auditing students. Results also reveal a significant relationship between auditor rank and inter-auditor judgmental agreement in audit planning in the early stages of auditors' careers. In contrast, however, rank above the senior level is associated with decreased levels of judgmental agreement when planning the audit. An analysis of auditor rank and sources of judgmental agreement among auditors at different ranks in their firm reveals significant relationships between rank and factor-weighting agreement among auditors, but does not find significant relationships between rank and judgmental consistency or agreement on the appropriate degree of configural factor processing. Finally, results reveal that pair-wise mean absolute differences between participants' judgments are a more sensitive measure of inter-auditor judgmental agreement than the traditional measure of consensus—the product-moment correlation coefficient.

Keywords: Tone-at-the-top, internal control, fraud risk, audits planning, auditor rank, audit experience, auditor judgment, decision making.

Download: Abstract [PDF] Full Article [PDF]

+ The Effects of Wrongdoer Motivation and Internal Versus External Reporting Channel on Intention To Report Fraud

   - Blaise M. Sonnier

Abstract: Using an experiment, this study examines the impact of the motivation of the wrongdoer and characteristics of the corporate reporting channel on the likelihood that in-house accountants will report fraudulent financial reporting to an employee hotline. The results indicate that in-house accountants are more likely to report a fraudulent financial misstatement when motivated by the wrongdoer’s personal gain. In addition, the study provides evidence that in-house accountants are more likely to report to a hotline managed by the internal audit department than to a hotline managed by a third-party contracted by the corporation. Employees may be hesitant to report wrongdoing to an external channel given the traditional duty of loyalty and obligation of confidentiality of corporate employees. In addition, the education, training, and codes of conduct of accountants all place an emphasis on confidentiality. Based on the results of the study, corporations should explore implementing an employee reporting hotline managed internally for reporting accounting or auditing irregularities.

Keywords: Employee hotline, fraudulent financial reporting, reporting intentions, whistle blow, whistleblowing.

Download: Abstract [PDF] Full Article [PDF]

+ Manipulating Sales Revenue to User Reference Points in Pre- and Post- Sarbanes-Oxley Eras

   - Charles E. Jordan
   - Stanley J. Clark

Abstract: Cosmetic earnings management occurs when unmanipulated income falls just below a user reference point (e.g., $395 million) and management increases earnings just across the threshold (e.g., to slightly above $400 million). Extant research shows this form of earnings management routinely occurred prior to but not after the Sarbanes-Oxley Act (SarB0X). The current study examines this same type of biased reporting but with sales revenue as the object of manipulation instead of earnings. Results indicate clear signs of cosmetic sales management in the pre-SarB0X period examined but no evidence of it in the post-SarB0X era, thus providing further evidence of an increased commitment by managers and accountants in recent years to provide more transparent reporting.

Keywords: Revenue manipulation, earnings management, Sarbanes-Oxley Act, Benford’s Law.

Download: Abstract [PDF] Full Article [PDF]

+ An Empirical Evaluation of Graham’s Model of Principled Organizational Dissent in the Whistleblower Context Post-SOX

   - Blaise M. Sonnier
   - Walfried M. Lassar

Abstract: Using an experiment, we empirically examine the applicability of Graham’s Model of Principled Organizational Dissent on the intention to report corporate wrongdoing in a post-SOX environment. We establish that the perceived seriousness of the wrongful act, the employee’s level of personal idealism, and the perceived duty to report wrongdoing as part of one’s job directly influence an employee’s perceived responsibility to report. Contrary to extant literature that perceived seriousness is directly related to reporting intention, our data establishes that it has only an indirect impact by increasing one’s perceived responsibility to report. We also find that while the threat of adverse job action if management discovers the whistleblower’s identity increases the perceived personal cost of reporting, the potential that management will discover his/her identity did not impact the perceived personal cost. The prohibition against retaliation against employee whistleblowers by Section 806 of SOX had no impact on
the perceived personal cost of reporting; however, it directly increased the likelihood of reporting.

We also demonstrate that factors that influence reporting intention vary depending on whether the employee is required to provide his/her name when reporting. The perceived personal cost and perceived responsibility both impact reporting intention when the employee is not required to provide his/her name to the hotline. However, these factors have no impact on intention to report when the employee is required to provide his/her name when reporting. The protection afforded employees against retaliation by Section 806 of SOX predominates reporting intention in this situation.

Keywords: Employee hotline, fraudulent financial reporting, reporting intentions, Sarbanes-Oxley Act, whistleblowing, whistleblower, Graham’s Model of Principled Organization Dissent.

+ Chinese Reverse Mergers: Accounting Fraud and Stock Price Collapse

Brittany Lang
John R. McGowan

Abstract: Investing in stock is a risky business. However, Chinese reverse mergers (CRM) have introduced a new level of risk. Research has shown that many Chinese reverse merger companies have used the process as a way to gain access to U.S. markets without having their financial statements inspected. Many Chinese companies are corrupted by fraudulent accounting practices and have taken advantage of the reverse merger method to mislead investors. This article highlights many common fraudulent accounting practices, which have led to the downfall of many CRM firms. The second objective of this article is to look at the role that investigative research companies play in revealing these companies’ true financial condition. For example, CRM firms’ stock prices commonly exhibit significant decline when Muddy Waters Research announces CRM firms’ fraudulent accounting practices. We examine seven CRM firms to highlight both the incidence of fraudulent accounting practices and the markets reaction when these practices are brought to light. Finally, this article seeks to enlighten and encourage unsuspecting investors to pursue due diligence procedures before investing in Chinese reverse merger companies. Many CRM companies engage in unethical business and accounting practices. Investors should be wary before investing in these firms.

Keywords: Chinese reverse mergers, accounting fraud, Muddy Waters research, risk.

+ Market Reactions to the Reform of Shareholder Derivative Litigation in Japan

Shingo Kawashima
Fumiko Takeda

Abstract: This paper investigates how stock prices of high-litigation-risk industries reacted to the news on legal changes in shareholder derivative suits in Japan. Specifically, we focus on two amendments to the Japanese Commercial Code. The 1993 Commercial Code amendments lowered the filing fees required to bring derivative actions, while the 2001 Commercial Code amendments attempted to reduce abusive shareholder derivative suits. We find stock prices of the pharmaceutical industry tended to react negatively to the news that increased the likelihood of the passage of the 1993 amendment, while stock prices of the retailing and electronics industries tended to react positively to the news that increased the likelihood of the passage of the 2001 amendment.

Keywords: Litigation, shareholder lawsuits, event study.

+ Does Financial Reporting Fraud Recognize Borders? Evidence From Bank Fraud in Iran

Zabihollah Rezaee
Gholamhossien Davani

Abstract: Reliable and high quality financial information is the lifeblood of the global capital markets and that quality can be adversely affected by the existence and persistence of financial reporting fraud (FRF). The 2007-2009 global financial crisis caused by subprime loan mortgage shenanigans has also provided incentives and opportunities for management to engage in FRF. Fraud in general and FRF in particular (Enron, WorldCom, Satyam, Madoff, Olympus) are global phenomena. The September 2011 discovery of Iran’s biggest bank fraud, totaling 2.6 billion USD, resulted in the arrest of more than 50 suspects, including some government officials. This bank fraud involved the use of forged documents to secure credit at one of Iran’s top financial institutions to acquire companies, conduct fraudulent business, and transfer money abroad. This article concludes that FRF does not recognize borders and can occur in any country. In the end, fraud does not yield rewards but rather result in severe consequences such as death sentences of the four fraud perpetrators in the bank fraud case in Iran.

Keywords: Financial reporting fraud, bank fraud in Iran, fraud prevention, detection.
Announcements, Correspondence, and Book Reviews

$34 Million Embezzlement at Koss over 12 Years: Case Study

Hugh Grove *

John C. Koss is recognized for creating the stereo headphone industry in 1958 with his first stereo headphone. Koss Corp. (KOSS) was incorporated in 1971 in Milwaukee, Wisconsin and manufactures stereo headphones, speaker phones, computer headsets, telecom headsets, noise reducing headsets, and wireless headsets. Koss Corp. went public in 1965 at $5 per share. Over the last eleven years, its stock price has ranged from $8 in July 2002, to its peak at $15 in July 2006 to its low at $4 in July 2010. It currently trades at approximately $5.50 per share. Accordingly, its market capitalization has ranged from $3.4 million to $12.8 million to its current level of $5.1 million. Thus, it was below the $75 million market value cutoff for a full implementation level of the Sarbanes-Oxley Act (SOX) and, accordingly, did not have an audit of its internal controls over its financial reporting. The Chief Executive Officer (CEO), Michael J. Koss, the founder’s son, and his family directly or indirectly own in excess of 70 percent of the company’s 851,000 shares. A $34 million embezzlement of cash from the Koss Corp. occurred and went undetected over a 12 year period from 1997 through December 2009 even though unqualified audit reports were issued every year by a Big Five audit firm.

Accounting and Auditing Enforcement Release (AAER) No. 3330, 10/24/11

SEC v. Koss Corporation and Michael J. Koss, Civil Case No. 2:11-cv-00991

Excerpts

On October 24, 2011, the SEC filed a Complaint (this AAER) against, and proposed settlement with, KOSS and Michael J. Koss (MJK), its CEO and former CFO, based on KOSS’s preparation of materially inaccurate financial statements, books and records, and lack of adequate internal controls from fiscal years 2005 through 2009. During this period, Sujata (Sue) Sachdeva, KOSS’s former Principal Accounting Officer, Secretary, and Vice-President of Finance, and Julie Mulvaney, KOSS’s former Senior Accountant, engaged in a wide-ranging accounting fraud to cover up Sachdeva’s embezzlement of $34 million from KOSS. The SEC Complaint alleges that:

- The yearly amounts stolen were significant to KOSS’s 2005-2009 financial statements. For example, during the fiscal year ending June 30, 2009, Sachdeva stole approximately $8.5 million, while KOSS reported total sales of $38.2 million, net income of $2.0 million, cash of $1.7 million, total assets of $28.5 million, total equity of $23.6 million including retained earnings of $21.6 million, basic/diluted earnings per share of $0.54, and dividends per share of $0.52.

- Sachdeva and Mulvaney were able to hide the embezzlement in KOSS’s financial records in part because KOSS and MJK did not adequately maintain internal controls to reasonably assure the accuracy and reliability of financial reporting. The $34 million embezzlement started in 1997 and ran until December 2009.

- While KOSS’s internal controls policy required MJK to approve invoices of $5,000 or more for payment, its controls did not prevent Sachdeva and Mulvaney from stealing $34 million from KOSS to pay for Sachdeva’s personal purchases (lavish shopping sprees at Neiman Marcus among others) without seeking or obtaining MJK’s approval.

- MJK knew that KOSS’s computerized accounting system was almost 30 years old, and he twice deferred proposals for a new system. Access to the accounting system could not be locked at the end of the day or month and there was no audit trail. Sachdeva and Mulvaney were thus able to make undetected post-closing changes (false journal entries) to the books and bypass an internal control requiring Michael J. Koss to authorize those changes.

- KOSS did not regularly change the password to access the computers and accounting terminals were not locked when unattended. KOSS did not have information technology (IT) security policies and controls to log and monitor network and application security violations or to report incidents to management.

- Due to the limited number of people working in KOSS’s accounting department, many critical duties were combined and given to a few employees. Based upon the fraudulent accounting books and records prepared by Sachdeva and Mulvaney, KOSS prepared, and MJK certified, materially inaccurate audited financial statements and materially inaccurate current, quarterly, and annual reports for the fiscal years 2005 through 2009.

Epilogue

When the embezzlement accusations were made public on December 21, 2009, the Nasdaq stock exchange halted trading in Koss shares at the company’s request. Koss shares had then traded at $5.51, down from an adjusted 52-week high of $7.89 in April 2009. MJK testified that Sachdeva’s thefts had threatened the company’s stability and that KOSS was forced to cut profit sharing and pay...
Sujata Sachdeva was arrested in December 2009 after the results of an internal investigation were turned over to authorities. She is in her mid-40s and was paid $173,734 by KOSS in total compensation in fiscal 2009 and $206,462 in fiscal 2008. Her embezzlement ran in spurts. There was a flurry of check-writing over three days in August 2006 totaling $478,735. On August 1, $154,021 was paid to Valentina Inc., an exclusive clothing store. On August 2, $181,000 was paid to Neiman Marcus and $10,120 to Saks Fifth Avenue. On August 3, $296,494 was paid to American Express on her personal credit card. Over a five-year period, Sachdeva spent more than $5 million at the Valentina boutique whose owner said the figure seemed high. Concerning more spending spurts, on February 3, 2006 checks were written to American Express for $204,287 and from July 11 to 17, 2003, $20,182 was spent at Marshall Fields, $26,420 at Saks Fifth Avenue, and $104,738 went to American Express.

Sachdeva used the money from KOSS to buy personal items, including women’s clothing, furs, purses, shoes, jewelry, a 2007 Mercedes Benz and other automobiles, china, statues, household furnishings, and a vacation ownership interest in Kauai, Hawaii resort property. She also paid for hotels, airline tickets and other personal travel expense for herself and others, renovations and improvements to her home, and personal services for her and her family. She never even took the tags off of many of the items and rented two storage spaces because she couldn’t fit them all in her house. Investigators seized more than 22,000 items she may have bought with company money. Prosecutors did not dispute her lawyer’s defense that Sachdeva likely suffered from bipolar disorder and compulsive shopping, but they said that it was an explanation, but not an excuse, for her behavior. In the U.S. District Court on November 17, 2010, Sachdeva pleaded guilty to six counts of fraud, was ordered to pay $34 million in restitution (would selling all of her 22,000 purchases be sufficient?), and was sentenced to 11 years in prison.

Required

1. Describe methods that Sachdeva and Mulvaney could have used to steal $34 million in cash over 12 years under KOSS’s existing internal control system.

2. Describe various false journal entries that Sachdeva and Mulvaney could have used to cover up the $34 million theft of cash over 12 years.

3. Recommend internal controls that KOSS should implement to prevent future cash thefts.

*The author is Professor at University of Denver. Solution to the case can be obtained from the author (hgrove@du.edu)

Books Reviews

**Detecting Fraud in Organizations**
John Wiley
11 River Street
Hoboken, N.J. 07030

Filled with cartoon, pictures, motivational quotes, and one-minute mysteries that creatively help readers to see beyond numbers and instead focus on open, proactive communication with organizational staff, the author looks at the people in today’s organizations and identifies how and where the value within your organization may potentially be exposed to fraud.

Drawing from the author’s thirty years providing fraud training and prevention/detection services for professionals, this book is designed to get you proactively thinking about fraud from a new perspective. Straightforward, simple, and entertaining in presentation, this unique book focuses on the people in today’s organizations and on pinpointing how the value within those organizations is exposed to fraud.

Featuring a companion website with additional fraud case studies and business process maps, this practical, hands-on guide explores:

- Fraud and why it keeps happening.
- How to get a handle on transactions.
- What happens when someone decides to commit fraud.
- The six Ps of successful fraudsters: passion, philosophy, planning, persistence, patience, and prison.
- How to build a case – document organization, data analysis, and lifestyle analysis.
Fraud control points in the organizational process.

Faces of Fraud
Cases and Lessons from a Life Fighting Fraudsters
John Wiley
11 River Street
Hoboken, N.J. 07030

Fraud is an evil with a life of its own that shows no sign of abating. The aura of fraud comes not from how a person looks or where they come from but from their criminal intent and the resulting self-serving actions, ruthlessness, and arrogance. The faces of fraud run the gamut from simple schemes that hit and run, like advance-fee loan scams, to long running and complex financial accounting frauds, such as the high-profile crimes that occurred at Enron, HealthSouth, and WorldCom. The author helps you detect fraud and prevent this evil from taking hold in your organization.

Sharing his 40 years of international fraud-fighting experiences, cases, and best practices, Martin Biegelman breaks down the key lessons he has learned in fighting fraud. Written for fraud investigators, auditors, and managers, he reveals the essential characteristics of fraudsters and the skills you need to spot and stop scammers in their tracks. Biegelman profiles the key traits fraudsters share, as well as the skills good forensic accountants must possess to be successful in thwarting fraud before it takes root.

Topics included in the book include:

- The Fraudster Mindset
- Silver-Tongued Devils
- Fraud Theories
- A Short History of Fraud in America
- Rise of Boiler Rooms and Bucket Shops
- Use Your Imagination in Fighting Fraud
- The Mob Strings Fraudsters
- Fraudster Stupidity Is Your Friend
- One Man’s Trash Is an Investigator’s Gold
- If You Don’t Ask, You Will Never Know
- New York State of Fraud
- Good Humor Ice Cream Scandal
- Bad Hams and Bribes
- Arrogance and Recidivism
- Informants and Whistleblowers
- Managing Confidential Informants
- A Tale of Deceitful Pitches and Vendor Kickbacks
- Cruise to Nowhere
- A Story of Vanity and Deception
- The Making of a Fraudster
- Scoundrels without a Conscience
- Why I Love Liars
- Fraudsters Love Expense Report Fraud
- San Francisco Meter gate
- Fraud Prevention for Individuals and Business Organizations.

The Forensic Accounting Deskbook
American Bar Association

In the preface the author, who is both an attorney and CPA, states that the book was written for both the experienced and less experienced family law practitioner. For the more experienced, the deskbook connects the dots and fills gaps among the inter-related topics of subrosa practice. accountin
concepts, depositions, reports, methodology, financial statements, tax returns, reports, and testimony. For the less experienced family law practitioner, the author provides a basic introduction to core divorce concepts, such as asset identification, classification and valuation, income determination, and expenses. He provides a step-by-step explanation of basic “how to” mechanics and explores higher-level strategic concerns appropriate for high-asset and high-conflict cases.

The book is useful to a solo practitioner, the partner in both the small and large law firm, an associate who needs a primer for his/her own edification, and the associate assigned to read the book for the benefit of the partner to whom he/she reports.

Mr. Mason suggests that forensic accountants can help clients keep money that might otherwise be taken from them by a difficult and confusing divorce. Some interesting chapters are:

- The Hunt for Hidden Assets – Red Flags, Schemes, Scams, Lies, and Damn Lies
- Discovery – Documents, Details, and Transactions
- Methodologies, Investigation, and Techniques
- Determining Income
- Lifestyle Analysis
- Reports and Testimony

The 2013 Annual Fraud and Forensic Accounting Conference

Mark your calendar for July 29 and 30, 2013, for the Louisiana State University Fraud & Forensic Accounting Conference in Baton Rouge, LA. For more information about the 2013 conference, go to: http://business.lsu.edu/Accounting/fraud/Pages/2013-Fraud-and-Forensic-Conference.aspx

Advertise in the JFIA

Would you like to advertise in this journal? Full page advertisement is $300. Half page ad is $150. Contact Larry Crumbley (dcrumbl@lsu.edu) Checks are to be made out to Journal of Forensic and Investigative Accounting and sent to Larry Crumbley at 2833 Business Education Complex, Dept. of Accounting, L.S.U., Baton Rouge, LA 70803.
Summary Witness Testimony in Federal Tax Litigation Cases as Identified in Court Opinions

Brigitte W. Muehlmann
Priscilla Burnaby
Martha Howe

Abstract: In U.S. tax litigation, there are three types of summary witnesses that may be called by both parties in a case. Their use provides insights into how large volumes of evidence and empirical research complex issues are presented in tax cases. To determine how witnesses are used during tax trials, this is the first to review the 109 tax opinions published through 2010 that disclose the use of summary witnesses. This paper first discusses the Federal Rules of Evidence related to summary witnesses: Rule 1006 primary evidence, Rule 611 pedagogical device and hybrid or secondary-device summary witnesses. Then the court cases are surveyed to determine: the trends in the use of summary witnesses; who presents the summary witness; how many cases are Rule of evidence 1006 versus Rule 611; the demographics of the summary witnesses; if they serve as more than one type of expert during the trial; and the reasons for which their testimony was challenged in courts of appeals. A detailed review of the opinions led to the master list of 109 cases. The majority of the summary witnesses (57.1%) presented Rule 611 pedagogical-device summaries, 26.5% presented Rule 1006 primary-evidence summaries, and only 10.2% provided the hybrid 1006 and 611 secondary-evidence summaries. The vast majority of the summary witnesses (65.3%) were IRS revenue agents or IRS special agents (10.2%). Fifty percent of the summary witnesses served dual roles before the introduction of the Daubert standard, but only one summary witness did so after the standard was introduced. The summary witnesses’ testimony was challenged in 22 court cases and six verdicts were overturned due to problems with their testimony.

Keywords: Tax, summary witness, expert witness, primary evidence summary, pedagogical-device summaries, secondary-evidence summaries.

Validating Early Fraud Prediction Using Narrative Disclosures

Chih-Chen Lee
Natalie Tatiana Churyk
B. Douglas Clinton

Abstract: This study documents a model building and validation process for the purpose of early fraud prediction based on asynchronous communication contained in the narrative disclosures of annual reports. Following Churyk et al. (2009), we apply content analysis to the management discussion and analysis section of the annual report to determine and examine significant qualitative fraud risk factors. A detailed review of the opinions led to the master list of 109 cases. The majority of the summary witnesses (57.1%) presented Rule 611 pedagogical-device summaries, 26.5% presented Rule 1006 primary-evidence summaries, and only 10.2% provided the hybrid 1006 and 611 secondary-evidence summaries. The vast majority of the summary witnesses (65.3%) were IRS revenue agents or IRS special agents (10.2%). Fifty percent of the summary witnesses served dual roles before the introduction of the Daubert standard, but only one summary witness did so after the standard was introduced. The summary witnesses’ testimony was challenged in 22 court cases and six verdicts were overturned due to problems with their testimony.

Keywords: Tax, summary witness, expert witness, primary evidence summary, pedagogical-device summaries, secondary-evidence summaries.
+ Fraudsters and the Form 1099 Technique

Christine Crawford Cheng
D. Larry Crumbley

Abstract: This paper discusses a technique employed by firms to recoup money and property stolen from a business by employees. Under the Form 1099 technique the firm supposedly uses the threat of filing a Form 1099 with the IRS for the amount stolen, unless the fraudster signs an installment note agreeing to a payback. This article discusses various aspects of this Form 1099 technique, including anecdotal evidence regarding the use of this technique, and the incentives of the firm, the employee who committed the fraud, and the IRS perspective of this technique.

In general, a company prefers the Form 1099 technique as a recoupment method when the probable amount collected from the employee exceeds the amount the firm would receive through insurance and tax recoupment. The employee should prefer to have the amount stolen reported to the IRS, unless the employee’s potential tax liability exceed the amount stolen from the firm. The IRS should prefer delayed reporting of the fraud when the company has sufficient net income to offset the amount of the fraud. The IRS should prefer the immediate reporting of the fraud when the company does not have sufficient net income to offset the amount of the fraud. Based upon our discussions and the unlikelihood of full repayment by a fraudster, the Form 1099 technique may not be a valuable approach. However there are instances where the Form 1099 technique is preferable to immediate tax reporting. Congress may wish to consider a tax rule which would protect a firm’s ability to use this technique for these instances.

Keywords: Form 1099, fraud, incentives, illegal income, embezzlement.

+ Influence of Leadership Positions on Internal Controls and Reported Fraud In Religious Organizations

Robert M. Cornell
Carol B. Johnson
William C. Schwartz, Jr.

Abstract: This study examines the extent to which particular leadership positions and governance bodies within churches are associated with the presence of internal controls and/or the absence of fraud. Our study is motivated by Marquet’s (2011) chronicle of 21 high-profile church embezzlements in the first half of 2011; Ventura and Daniel’s (2010) finding that church members tend to trust their leaders in spite of the absence of internal controls; and discoveries by Booth (1993) and Conway (1999) that clergy tend to be ill-disposed to utilize secular accounting and internal control practices. We surveyed 131 individuals who were responsible for financial management within their respective churches. The survey was conducted through in-person, structured interviews. After removing duplicate interviews, we analyzed a sample of 129 responses. The subjects were affiliated with churches that varied widely in size, age, and denomination. Our results indicate that the leadership position most closely associated with the presence of internal controls in the church is a financial expert on the board of directors. Consistent with the findings of Booth (1993) and Conway (1999), paid clergy tend to traverse in the opposite direction. We fail to find any indication that presence of the leadership positions or governance bodies we examined are associated with a reduced incidence of reported fraud. These results suggest that future research should go beyond simply looking for internal controls in churches and should establish whether there are characteristics or viable practices of churches (internal controls or otherwise) that can indeed reduce the incidence of fraud.

Keywords: Fraud, governance, internal audit, internal control, nonprofits, religious organizations.

+ Effects of Alternative Short-Session Training Methods on Fraud Detection: A Performance and Efficiency Assessment

W. Eric Lee
Vairam Arunachalam
Dennis Schmidt

Abstract: Many novice accounting professionals and current accounting students receive limited training in fraud detection, often restricted to a short CPE course or a short module in an accounting course. Therefore, it is important to investigate the effects of alternative short-session training methods on fraud detection. This study reports the results of a short-session experiment that employed two widely used training methods: lecture and experiential. By comparing to a control group who received no training, we assess the relative performance effectiveness of the two training methods with respect to both fraud cue identification and fraud cue justification. We also assess efficiency, in terms of effort and time, relative to performance. Except for the experiential group,
with no significant identification performance improvement, we find that either training method increases
performance and efficiency compared to no training. Regarding both performance and efficiency for fraud cue
identification, we observe slightly better results for lecture training over experiential training, but no significant
difference between the two methods. With respect to both performance and efficiency for fraud cue justification,
we find significant support for experiential training over lecture training. Our results should help accounting
educators decide which approach to use when designing a short-session fraud detection training module.

**Keywords:** Fraud detection training, fraud cue identification, fraud cue justification, efficiency.

**Abstract:** A fundamental argument that has persisted throughout the modern history of accounting concerns
whether the primary measurement basis in financial reporting should be input-based (historical cost) or outcome-
based (fair value). The key issue hinges on the trade-off between the relevance and reliability of the numbers
reported under these two measurement bases, with fair value measures viewed as more relevant, but historical
cost measures considered more reliable. This article provides a background and discussion of these two
measurement bases and explains the FASB’s gradual shift from historical cost toward fair value reporting. More
importantly, through the application of Benford’s Law, which has become an important forensic analytical
tool for detecting earnings management and other forms of fraudulent financial reporting, the study provides
an empirical examination of the reliability of all three levels of fair value disclosures required by SFAS No. 157. The
findings suggest a significant amount of manipulation occurs in each of the three levels of fair value disclosure,
including Level 1, which should be based on objectively determined external marketplace data. Thus, the results
of the forensic procedures performed in this study call into question the reliability and credibility of the fair value
information currently reported in the financial statements.

**Keywords:** Fair value reporting, SFAS No. 157, reliability, manipulation, Benford’s Law.

**Abstract:** A fundamental argument that has persisted throughout the modern history of accounting concerns
whether the primary measurement basis in financial reporting should be input-based (historical cost) or outcome-
based (fair value). The key issue hinges on the trade-off between the relevance and reliability of the numbers
reported under these two measurement bases, with fair value measures viewed as more relevant, but historical
cost measures considered more reliable. This article provides a background and discussion of these two
measurement bases and explains the FASB’s gradual shift from historical cost toward fair value reporting. More
importantly, through the application of Benford’s Law, which has become an important forensic analytical
tool for detecting earnings management and other forms of fraudulent financial reporting, the study provides
an empirical examination of the reliability of all three levels of fair value disclosures required by SFAS No. 157. The
findings suggest a significant amount of manipulation occurs in each of the three levels of fair value disclosure,
including Level 1, which should be based on objectively determined external marketplace data. Thus, the results
of the forensic procedures performed in this study call into question the reliability and credibility of the fair value
information currently reported in the financial statements.

**Keywords:** Fair value reporting, SFAS No. 157, reliability, manipulation, Benford’s Law.

**Abstract:** A fundamental argument that has persisted throughout the modern history of accounting concerns
whether the primary measurement basis in financial reporting should be input-based (historical cost) or outcome-
based (fair value). The key issue hinges on the trade-off between the relevance and reliability of the numbers
reported under these two measurement bases, with fair value measures viewed as more relevant, but historical
cost measures considered more reliable. This article provides a background and discussion of these two
measurement bases and explains the FASB’s gradual shift from historical cost toward fair value reporting. More
importantly, through the application of Benford’s Law, which has become an important forensic analytical
tool for detecting earnings management and other forms of fraudulent financial reporting, the study provides
an empirical examination of the reliability of all three levels of fair value disclosures required by SFAS No. 157. The
findings suggest a significant amount of manipulation occurs in each of the three levels of fair value disclosure,
including Level 1, which should be based on objectively determined external marketplace data. Thus, the results
of the forensic procedures performed in this study call into question the reliability and credibility of the fair value
information currently reported in the financial statements.

**Keywords:** Fair value reporting, SFAS No. 157, reliability, manipulation, Benford’s Law.

**Abstract:** A fundamental argument that has persisted throughout the modern history of accounting concerns
whether the primary measurement basis in financial reporting should be input-based (historical cost) or outcome-
based (fair value). The key issue hinges on the trade-off between the relevance and reliability of the numbers
reported under these two measurement bases, with fair value measures viewed as more relevant, but historical
cost measures considered more reliable. This article provides a background and discussion of these two
measurement bases and explains the FASB’s gradual shift from historical cost toward fair value reporting. More
importantly, through the application of Benford’s Law, which has become an important forensic analytical
tool for detecting earnings management and other forms of fraudulent financial reporting, the study provides
an empirical examination of the reliability of all three levels of fair value disclosures required by SFAS No. 157. The
findings suggest a significant amount of manipulation occurs in each of the three levels of fair value disclosure,
including Level 1, which should be based on objectively determined external marketplace data. Thus, the results
of the forensic procedures performed in this study call into question the reliability and credibility of the fair value
information currently reported in the financial statements.

**Keywords:** Fair value reporting, SFAS No. 157, reliability, manipulation, Benford’s Law.

**Abstract:** A fundamental argument that has persisted throughout the modern history of accounting concerns
whether the primary measurement basis in financial reporting should be input-based (historical cost) or outcome-
based (fair value). The key issue hinges on the trade-off between the relevance and reliability of the numbers
reported under these two measurement bases, with fair value measures viewed as more relevant, but historical
cost measures considered more reliable. This article provides a background and discussion of these two
measurement bases and explains the FASB’s gradual shift from historical cost toward fair value reporting. More
importantly, through the application of Benford’s Law, which has become an important forensic analytical
tool for detecting earnings management and other forms of fraudulent financial reporting, the study provides
an empirical examination of the reliability of all three levels of fair value disclosures required by SFAS No. 157. The
findings suggest a significant amount of manipulation occurs in each of the three levels of fair value disclosure,
including Level 1, which should be based on objectively determined external marketplace data. Thus, the results
of the forensic procedures performed in this study call into question the reliability and credibility of the fair value
information currently reported in the financial statements.

**Keywords:** Fair value reporting, SFAS No. 157, reliability, manipulation, Benford’s Law.

**Abstract:** A fundamental argument that has persisted throughout the modern history of accounting concerns
whether the primary measurement basis in financial reporting should be input-based (historical cost) or outcome-
based (fair value). The key issue hinges on the trade-off between the relevance and reliability of the numbers
reported under these two measurement bases, with fair value measures viewed as more relevant, but historical
cost measures considered more reliable. This article provides a background and discussion of these two
measurement bases and explains the FASB’s gradual shift from historical cost toward fair value reporting. More
importantly, through the application of Benford’s Law, which has become an important forensic analytical
tool for detecting earnings management and other forms of fraudulent financial reporting, the study provides
an empirical examination of the reliability of all three levels of fair value disclosures required by SFAS No. 157. The
findings suggest a significant amount of manipulation occurs in each of the three levels of fair value disclosure,
including Level 1, which should be based on objectively determined external marketplace data. Thus, the results
of the forensic procedures performed in this study call into question the reliability and credibility of the fair value
information currently reported in the financial statements.

**Keywords:** Fair value reporting, SFAS No. 157, reliability, manipulation, Benford’s Law.

**Abstract:** A fundamental argument that has persisted throughout the modern history of accounting concerns
whether the primary measurement basis in financial reporting should be input-based (historical cost) or outcome-
based (fair value). The key issue hinges on the trade-off between the relevance and reliability of the numbers
reported under these two measurement bases, with fair value measures viewed as more relevant, but historical
cost measures considered more reliable. This article provides a background and discussion of these two
measurement bases and explains the FASB’s gradual shift from historical cost toward fair value reporting. More
importantly, through the application of Benford’s Law, which has become an important forensic analytical
tool for detecting earnings management and other forms of fraudulent financial reporting, the study provides
an empirical examination of the reliability of all three levels of fair value disclosures required by SFAS No. 157. The
findings suggest a significant amount of manipulation occurs in each of the three levels of fair value disclosure,
including Level 1, which should be based on objectively determined external marketplace data. Thus, the results
of the forensic procedures performed in this study call into question the reliability and credibility of the fair value
information currently reported in the financial statements.

**Keywords:** Fair value reporting, SFAS No. 157, reliability, manipulation, Benford’s Law.

**Abstract:** A fundamental argument that has persisted throughout the modern history of accounting concerns
whether the primary measurement basis in financial reporting should be input-based (historical cost) or outcome-
based (fair value). The key issue hinges on the trade-off between the relevance and reliability of the numbers
reported under these two measurement bases, with fair value measures viewed as more relevant, but historical
cost measures considered more reliable. This article provides a background and discussion of these two
measurement bases and explains the FASB’s gradual shift from historical cost toward fair value reporting. More
importantly, through the application of Benford’s Law, which has become an important forensic analytical
tool for detecting earnings management and other forms of fraudulent financial reporting, the study provides
an empirical examination of the reliability of all three levels of fair value disclosures required by SFAS No. 157. The
findings suggest a significant amount of manipulation occurs in each of the three levels of fair value disclosure,
including Level 1, which should be based on objectively determined external marketplace data. Thus, the results
of the forensic procedures performed in this study call into question the reliability and credibility of the fair value
information currently reported in the financial statements.

**Keywords:** Fair value reporting, SFAS No. 157, reliability, manipulation, Benford’s Law.

**Abstract:** A fundamental argument that has persisted throughout the modern history of accounting concerns
whether the primary measurement basis in financial reporting should be input-based (historical cost) or outcome-
based (fair value). The key issue hinges on the trade-off between the relevance and reliability of the numbers
reported under these two measurement bases, with fair value measures viewed as more relevant, but historical
cost measures considered more reliable. This article provides a background and discussion of these two
measurement bases and explains the FASB’s gradual shift from historical cost toward fair value reporting. More
importantly, through the application of Benford’s Law, which has become an important forensic analytical
tool for detecting earnings management and other forms of fraudulent financial reporting, the study provides
an empirical examination of the reliability of all three levels of fair value disclosures required by SFAS No. 157. The
findings suggest a significant amount of manipulation occurs in each of the three levels of fair value disclosure,
including Level 1, which should be based on objectively determined external marketplace data. Thus, the results
of the forensic procedures performed in this study call into question the reliability and credibility of the fair value
information currently reported in the financial statements.

**Keywords:** Fair value reporting, SFAS No. 157, reliability, manipulation, Benford’s Law.

**Abstract:** A fundamental argument that has persisted throughout the modern history of accounting concerns
whether the primary measurement basis in financial reporting should be input-based (historical cost) or outcome-
based (fair value). The key issue hinges on the trade-off between the relevance and reliability of the numbers
reported under these two measurement bases, with fair value measures viewed as more relevant, but historical
cost measures considered more reliable. This article provides a background and discussion of these two
measurement bases and explains the FASB’s gradual shift from historical cost toward fair value reporting. More
importantly, through the application of Benford’s Law, which has become an important forensic analytical
tool for detecting earnings management and other forms of fraudulent financial reporting, the study provides
an empirical examination of the reliability of all three levels of fair value disclosures required by SFAS No. 157. The
findings suggest a significant amount of manipulation occurs in each of the three levels of fair value disclosure,
including Level 1, which should be based on objectively determined external marketplace data. Thus, the results
of the forensic procedures performed in this study call into question the reliability and credibility of the fair value
information currently reported in the financial statements.

**Keywords:** Fair value reporting, SFAS No. 157, reliability, manipulation, Benford’s Law.
Abstract: This case involves damages for the infringement of two patents owned by Salsa, Inc. The patents are for (a) the design and (b) the method of manufacture of concrete walls for containing construction noise caused by the building or widening of highways. By containing this noise, the state highway construction authority saves on the cost of compensation paid to nearby business owners and homeowners disturbed by the noise of highway construction. This patent has been infringed by other highway construction companies. Therefore Salsa has sued the infringing companies in order to recover compensatory damages for its lost profits due to patent infringement. The case requires students to calculate compensatory damages for lost profits from lost sales, lost profits from margin erosion, lost profits (if any) from convoyed sales, and interest on all lost profits.

Keywords: Patent, infringement, compensatory, damages, lost profits, lost sales, margin erosion, convoyed sales

Announcements, Correspondence, and Book Reviews

Advocacy vs. Objectivity

As provided by Rule 702 of the Federal Rules of Evidence, an individual qualified as expert by knowledge, skill, experience, training or education (e.g., the forensic accountant), may offer “expert testimony” to assist the trier of fact (judge or jury or arbitrator) to understand the evidence. The court, of course, needs assurance of the expert's objectivity. This assurance may be a problem for an expert because the court, as well as the opposing attorney, may assume that advocacy has supplanted the expert's objectivity.

Consider, for example, the following characterization of forensic accounting experts (FA) testifying in a business valuation case by Judge David Schwartz, of the U.S. Court of Claims: "The trier must first judge the qualifications of the opposing experts, then try to understand their presentations, pass on their sincerity and credibility, and finally choose between opposing conclusions. Throughout, there is the uneasy doubt as to an appropriate discount for partisanship. Have the witnesses ... anticipated a discount by the trier and hiked their opinions twice, once for discount and once for loyalty to their client, or only once, or even not at all?"

Sometimes, the FA must deal not only with the court's and the opponent's assumptions about their advocacy, but also with the real difficulty of maintaining objectivity that is posed in some cases. Conclusions about technical and professional issues are sometimes based on probability rather than certainty. The determination of the value of closely held stock, for example, is a matter of judgment, rather than just mathematics. In such instances, the FA needs to be particularly careful to maintain objectivity and avoid becoming an advocate for an unwarranted position or conclusion.

A testifying expert’s role (and duty) should be qualified during the engagement interview. At this point, the FA needs to clarify the nature and scope of the engagement and proposed limitations. Because of time and monetary constraints, for example, counsel may wish to limit the scope of the expert’s involvement or make that involvement conditional in anticipation of expanding or curtailing the scope of the expert's involvement. As the case progresses, the expert’s scope of involvement may change from providing services as a consultant to testifying as expert witness. The FA needs to ensure that the scope of the engagement, including any changes, is documented in the case file and that all expert opinions offered fall within the scope of the engagement.

Each of the six segments of a litigation services engagement (engagement interview, investigation process, attorney communications, reporting, depositions, and testimony) is a progression built upon the prior segment. However, the investigation process is perhaps the key to keeping the expert an objective witness. A strong, thoroughly executed investigation gives the support needed to withstand the pressures and outright manipulations inherent in the rest of the litigation process.

Data Issues

As the investigation progresses, certain issues can arise that make it difficult for the FA expert to keep the investigative process objective. Attorneys and clients come to the FA with their own view of the facts. Inadvertently or deliberately, they may provide inaccurate information, or they may withhold information. This problem creates an opportunity for opposing counsel upon cross examination to compromise or discredit even the most seasoned expert witness. To avoid such impeachment, the FA needs to recognize that attorneys and their clients are biased. The FA needs to keep an open mind and avoid reaching conclusions prematurely. For example, the FA may use the scientific method of forming a hypothesis. Then the FA carefully follows well established investigative steps and develops forms, procedures, and processes that will ensure proving or disproving the hypothesis and that he or she will not neglect or overlook critical data, or be taken in by inaccurate data.

Even after the FA has thoroughly investigated the facts of the case and has objectively reached a supportable conclusion, he or she is still vulnerable to subtly shifting from objective expert to advocate. Sometimes, the expert's conclusion can fall within a range on a continuum of conclusions that at one end support the client-attorney's goals and at the other end support the opponent's goals. Wherever the FA expert's conclusion falls on that continuum, he or she needs to return to the data to be sure that the results, in fact, is supported by the data.

Communications between the attorney and the FA expert are necessary to ensure that everyone on the
Communications between the attorney and the FA expert are necessary to ensure that everyone on the team is aware of all facts and the direction of the case. Such communications also provide opportunities for the expert to learn of new or contradictory data (e.g. alternative explanations) and to assess challenges to the conclusions he or she has reached.

At this point, the expert needs to avoid becoming attached to the original conclusion if it is attacked by the attorney or other team members. Understandably, an expert who has invested considerable time and effort in reaching this conclusion may be reluctant to change it. That said, the expert must maintain an objective point of view, realistically assessing challenges to opinions and remaining open to the possibility of flaws in the initial approach. A change may or may not be warranted, depending on the supporting data. Again, the expert needs to return to the data to see which conclusion it best supports.

Investigative Issues

An investigation that fails the mandates of Rule 702 (sufficient facts /data and the application of reliable methods) puts the expert's opinion in jeopardy. The FA expert needs to be careful, for example, when using a purchased software program (such as valuation and economic damage software) as part of the investigation to reach a conclusion. The conclusion may be subject to many variables unaccounted for by the software, making the expert's credibility vulnerable.

In general, the FA expert can help to avoid having testimony discredited by reviewing the investigation carefully before testifying. The FA should review records of time and research to make sure they agree with the case file reports. The FA also should review the files to make sure his or her conclusions are supported with documentation.

Although the FA expert can advocate his or her position based on the findings of an investigation, as an expert witness, he or she must be objective whether or not those findings support the goals being advocated by the attorney. This objectivity is required not only to provide services ethically, but also to ensure attracting the right kind of referral sources and clients.

*Bill Barrett, CPA/CFF/ABV, has investigated fraud and misfeasance in governments, corporations, boards of directors and professional practices; and has directed federal teams investigating multi-defendant money laundering, illegal income, tax evasion and white-collar fraud. He is the current vice president of practice for the American Accounting Association Forensic and Investigative Section. Contact him at bill.barrett@barrettpc.com

Books Reviews

**Cyber Forensic**  
A. J. Marcella, Jr., F. Guillosoi, 2012, $80  
John Wiley  
201.748.6358

The authors begin by explaining the origins of data. From there, the authors address concepts related to data storage, boot records, partitions, volumes, and file systems and how each of these is interrelated and essential in a cyber forensic investigation. They then analyze the roles these concepts play in an investigation and what type of evidential data may be identified within each of these areas.

Ronelle Sawyer and Jose McCarthy – two fictional characters – are used throughout the book to illuminate specific IT and cyber forensic concepts and discuss critical cyber forensic processes. Their activities and actions bring cyber forensic concepts to life by providing you with specific examples of the applications. Cyber Forensics also examines endianness and time—two important yet often overlooked topics—that drastically impact almost every cyber-based investigation.

Providing a through foundation to this emerging field, this step-by-step reference covers:

- Converting binary to decimal
- The power of HEX
- Forensics and encrypted files
- Master Boot Record (MBR)
- Volume versus Partition
- FAT filing system limitations
- New technology file system
- Forensic Investigative Smart Practices
- MS-DOS 32-bit time stamp: date and time
- Characteristics of a good cyber forensic report
- A cyber forensic process summary
This book teaches readers how to identify and interpret verbal and nonverbal behaviors of deceptive or truthful people, and how to move toward obtaining solid confessions from guilty persons using the Reid Technique. The Reid Technique is built around basic psychological principles and presents interrogation as an easily understood nine-step process. Separated into two parts, What You Need to Know About Interrogation and Employing the Reid Nine Steps of Interrogation, this book will help readers understand the effective and proper way that a suspect should be interrogated and the safeguards that should be in place to ensure the integrity of the confession.

Key Features

- An abridged book covering the state-of-the-art technique of interviewing and interrogation.
- Designed for criminal investigation students, law enforcement personnel, corporate security officers, and attorneys.
- Includes real-world scenarios and examples.
- Contains fascinating insights into how people behave when they are trying to lie.
- Teaches proper and effective ways to interrogate and safeguard against false confessions.

The author identifies the sources of electronic document leakage in terms non-teches can understand, as well as the many threats to confidential e-documents across a wide range of digital platforms, including e-mail, instant messaging, mobile devices, cloud computing, and social networks. Then he offers proven solutions for proactively defending against each of those threats.

While Smallwood describes proven technological fixes that can be implemented right away, he is careful to explain why technology alone cannot fix the problem. Real e-document security, the author explains, begins at the top, with clear, rigorously enforced Information Governance (IG) policies. Drawing upon his more than a quarter-century of experience, Smallwood provides step-by-step guidance on how to establish a set of IG protocols appropriate to your organization and for developing an organization-wide program of total life-cycle security for critical electronic documents, from their creation to their eventual archiving or destruction.

The 3rd Annual Midyear Forensic and Investigative Accounting Conference

The Annual Mid-Year Forensic and Investigative Accounting Conference will be held March 22-23, 2013, jointly with the Public Interest Section in New Orleans, LA. The conference will be consist of keynote speakers, concurrent sessions dealing with a wide variety of fraud, forensic and investigative accounting topics, panel discussions, case work, and film previews.

The 9th Annual Fraud and Forensic Accounting Conference

Mark your calendar for July 29 and 30, 2013, for the Louisiana State University Fraud & Forensic Accounting Conference in Baton Rouge, LA. For more information about the 2013 conference, go to: http://business.lsu.edu/Accounting/fraud/Pages/2012-Fraud-and-Forensic-Accounting-Conference.aspx

Advertise in the JFIA

Would you like to advertise in this journal? Full page advertisement is $300; Half page advertisement is $150. Contact Larry Crumbley (dcrumbl@lsu.edu). Checks are to be made out to Journal of Forensic and Investigative Accounting and to be sent to Larry Crumbley at 2833 Business Education Complex, Dept. of Accounting, L.S.U., Baton Rouge, LA 70803
The opinions of the authors are not necessarily those of Louisiana State University, the E.J. Ourso College of Business, the LSU Accounting Department, or the Senior Editor.

©2011, ISSN: 2165-3755, Louisiana State University.