The role of forensic accountants in fraud investigations: Importance of attorney and judge's perceptions

Linda Bressler,
University of Houston-Downtown

ABSTRACT

Incidents of fraud can be noted in the media on a weekly if not daily basis. Forensic accountants must be well trained in the rules of evidence, financial data, Accounting Information Systems (AIS) software, communication skills as well as be able to convince a judge that they should be viewed as an expert in their field. Since most of the fraud cases use evidence consisting of accounting data and specifically accounting data retrieved from an AIS system of some sort, not only should these investigators must be well versed in AIS but perhaps also fraud trial attorneys and more importantly, the judges involved with such decisions. Although research does exist on the importance of jury comprehension of statistical and mathematical data, very few studies exist on the importance of jury comprehension of financial data deriving from an AIS nor on the CSI Effect on fraud trails dealing with AIS derived financial data testimony. It would be interesting to note the perceptions of attorneys and judges in the court system as to what might enhance understandability of AIS testimony and the CSI Effect on jurors.

Key Words: Fraud, Accounting Information Systems, CSI Effect,

INTRODUCTION

Incidents of fraud can be noted in the media on a weekly if not daily basis. Fraud could include confidence tricks such as the 419 and Spanish Prisoner, Long Firms or creation of false companies, embezzlement, false advertising or billing, health fraud, bankruptcy fraud, use of tax haven countries for illegal activities etc. Also, marital fraud can be committed by divorcing spouses who do not wish to identify all marital assets (Marden and Darner, 2006; Rosenberg, 1989).

Financial and other fraud cases involve accounting information. Forensic investigators utilize financial information and will need to understand, interpret, discern what is important/not so important, retrieve, identify, safeguard, report, and testify in court financial information retrieved in a fraud investigation (Kahan, 2005; Manning, 2005, Wells, 2005). A fairly new phenomenon in the research deals with the CSI Effect on jurors as well. Researchers discussed the importance of auditors and forensic accountants receiving training on fraudulent methods but also indicate the importance of fraud investigators knowing Accounting Information Systems (AIS) (Bodnar and Hopwood, 2010). In addition, studies also indicate the importance of fraud examiners being able to testify as an expert witness on evidence derived from an AIS (Christensen et al., 2005) and a few researchers even suggest that judges and attorneys might wish to be updated in AIS and forensic evidence (Lowe et al., 2002; Neufer, 2001; Rasmussen and Leauanae, 2004).

TERMS

Accounting Information Systems. Accounting Information Systems can be defined as a collection of resources utilized to transform financial and other data into usable information. (Bodnar and Hopwood, 2010)

Advanced Fee Fraud or 419 fraud and Spanish Prisoner (Adogame, 2009). A scam where the sender requests help in facilitating the transfer of a substantial sum of money usually perpetrated through an email. In return, the sender offers a commission (usually in the millions of dollars) and the scammers will ask that money be sent to pay for some of the costs associated with the transfer. If money is sent to the scammers, they will either disappear immediately or try to get more money with claims of continued problems with the transfer.

CSI Effect. Is a theory which researchers indicate that popular TV crime dramas that focus on forensic science, may affect the behavior and expectations of jurors in real-life cases. The theory also suggests that jurors' perceptions of the need for specific forensic evidence may impact their decisions in the courtroom (http://www.neiai.org/; http://www.jstor.org/pss/20455645; Tyler, 2006).

Computer Forensics. The process of acquisition, restoration and analysis of digital data which could include restoring corrupted or lost data, resurrecting outdated systems and software environments or to simply analyze common security breach activities (Green and Cooper, 2003; Stringer-Calvert, 2002).

Electronic Discovery. Dissecting complicated transactions and revealing important evidence (Hochberg, 2006).

Expert Witness. Specialist in a subject who may present his or her expert opinion such as a forensic accountant or C.P.A. auditor in the case of evidence utilizing AIS data. If the expert is challenged by the defendant's council, evidence of their expertise, training, or special

knowledge can be an exception to the rule against providing an opinion as testimony. The prosecution must prove any experts' qualifications if challenged and the trial judge has the discretion to rule if the forensic accountant is qualified as an expert, or is limited on the subjects that she or he would be an expert (http://www.legal-explanations.com/definitions/expert-witness.htm).

Forensic Accounting. Forensic accounting can be defined as the use of accounting, auditing, and investigative skills to assist in legal matters (Houck et al., 2006).

Fraud Assessment Questioning (FAQ). Questions structured so that the individual being interviewed may not necessarily know that the information they provide is of great significance to the forensic investigation (Buckhoff and Hansen, 2002).

Health fraud. An example would be the selling of products known not to be effective, such as quack medicines (Hyman, 2001).

Long Firms or creation of false companies. (Levi, 2008). This would be the crime of businesses buying on credit, then disappearing.

Red flags. Red flags in AIS would be internal controls within and outside the AIS software that indicated possible suspect transactions (Manning, 2005).

Tax Haven Country. Countries that offer various business services in order for customers to avoid taxes and/or avoid prosecution for illegal acts. Many times individuals intent on fraudulent acts will actively seek tax haven countries to conduct their financial business and/or hide their financial data because of the secrecy laws of certain tax haven countries (Manning, 2005).

FINANCIAL FRAUD AND RISKS

Researchers and practioners agree on the importance of forensic accountants' understanding the elements of fraud which include opportunity, incentive, and rationalization (Buckhoff, 2004; Houck et al., 2006; http://www.osa.state.mn.us/default.aspx?page= 20090724.057). Wolfe and Hermanson, (2004) also believe in the importance of the fraud diamond which includes incentive, opportunity, and rationalization but suggest considering a fourth element. Instead, the authors indicated the forensic accountant should be familiar with the four-sided fraud diamond which would also consider an individual's capability.

In addition to discussing the fraud diamond which offered different ways to think about fraud risks, Wolfe and Hermanson, (2004) noted that fraud examiners should not underestimate the fraud perpetrator because the perpetrator would be smart enough to understand and take advantage of internal control weaknesses (Fiore, et al., 2005). An understanding of AIS would be especially important when investigating fraud and who in the organization might be capable of bypassing or removing financial red flags from the AIS system (Kranacher and Stern, 2004; Weber, 1999).

In order for forensic accountants to be able to identify fraud indicators, they must be trained in the areas of investigation, detection, and various specialized auditing techniques. Many times the forensic investigator will be an experienced auditor and/or accountant. Harris and Brown (2000) suggested that a forensic accountant should be able to demonstrate specialized skills in rules of evidence and the law, analytical and investigative skills, identification of patterns of abuse, excellent interpersonal and communication skills, and outstanding organizational skills. Buckhoff and Hansen (2002) indicate that not only would

excellent communication skills be important, but the fraud investigator should also be asking the right questions and he or she may not know to ask the right questions if not well versed in AIS. The article mentioned the Fraud Assessment Questioning technique (FAQ) and the authors gave sample fraud assessment questions and skills to interpret verbal and non-verbal interviewee responses. However, even if the investigator has excellent interview skills, if she or he is not well versed in accounting information systems, the investigator may not be asking the right questions which is particularly important in this highly-technological business environment (Buckhoff and Hansen, 2002).

Most companies utilize an AIS for financial information processing and reporting. Even entrepreneurial entities (with 5 or less employees) will utilize AIS software such as QuickBooks, Peachtree, or Excel (Buckhoff and Kramer, 2005; Derby, 2003; Williams, 1997). Recently, PricewaterhouseCoopers conducted an audit of HealthSouth Corporation and their findings resulted in the company being charged with fraudulent reporting dealing with inaccurate revenue and expenses and improper accounting business combination activities (Weld et al., 2004). The forensic investigators utilized spreadsheet software and the use of statistical and database analysis for which the investigators needed to understand the AIS system and in addition to other analyses, be able to conduct a detailed analysis of receivables. With these skills, the auditors looked for links between cash flows and several analytical performance measures. Not only does the fraud investigator need to identify links between transactions, but they also need to convince the judge and jury of the validity of their testimony and the investigator should not presume all parties have in-depth knowledge of AIS and other numeric analytic processes (Bodnar and Hopwood, 2010; Buckhoff, 2004).

AIS DATA EVIDENCE RETRIEVAL, PRESERVATION AND TESTIFYING IN COURT

Many times, fraud investigators must explain the data retrieval process for which they are testifying. The forensic investigator must handle and preserve correctly AIS data (Retrieving, 2006). The U.S. Department of Justice released new guidelines regarding the collection and handling of electronic evidence (http://www.ncjrs.gov/pdffiles1/nij/199408.pdf) and this report recommended general forensic and procedural processes when dealing with digital AIS evidence (Volonino, 2003). Once the investigator seizes the evidence and the prosecutor prepares for the trial, it will be important for the forensic accountant to understand the rules of the court and be thoroughly trained in testifying about the AIS fraud trial evidence. Volonino (2003) indicated that when companies do not properly preserve their electronic evidence (Green and Cooper, 2003), severe sanctions by the courts may be experienced and the author mentions that in 1970, Rule 34 of the Federal Rules of Civil Procedure was amended to deal with changing technology and communication.

FORENSIC ACCOUNTANTS TESTIFYING AS EXPERT WITNESSES and FRAUD TRIAL DIFFICULTIES

Testifying

Recently, researchers noted the importance of forensic accountants' understanding and adhering to the Rule 702 of the Federal Rules of Evidence (Craig and Reddy, 2004; Manning,

2005; Rasmussen and Leauanae, 2004; Shmukler, 2005; Wells, 2003; Wells, 2005). Researchers specified specific areas of expertise forensic investigators should possess including investigative accounting, economic loss calculation, and business and intangible asset valuation (Rasmussen and Leauanae, 2004). Jordan (2006) indicated that giving evidence in court deals with communicating information to individuals who often have limited experience and/or previous exposure to such testimony. Lichtman, (2009) stated that the forensic investigator "makes the documents speak" and many times the documents themselves do not tell the whole story and that the fraud investigator must translate what the documentary evidence means. The author suggests backing away from the details and perhaps demonstrating more of the whole picture first or in another words, put the data into context that the listener may better understand.

Understanding & Applying Testimony

Several researchers indicate the difficulty of jurors understanding numerical or statistical data testimony in trials. Neufer (2000) noted that jurors will more often than not possess a limited understanding of statistics and their anxiety dealing with numbers may influence how they process statistical or numerical testimony. Niedermeier et al. (1999) commented that individuals often misunderstand and misapply probabilities, but what should also concern those giving testimony is the fact that even if jurors understand the probabilities, they may fail to apply them accurately. Billings and Crumbly (1996) discussed financial estimates being utilized in tax or financial testifying in court whereby the judge pointed out how one expert's evaluation differed from another which appeared to cause confusion in the testimony. The authors note that creditability of such evidence could be enhanced with an understanding of the phenomenon being measured. If such testimony concerns the judge, the comprehension of the jury will be even less. Kozinski, (2001) mentions the importance of utilizing a specific methodology consistently in testimony because the entire testimony can be challenged and discarded by the judge if the judge does not comprehend or loses faith in the expert witness (Lowe et al., 2002; Rasmussen and Leauanae, 2004).

In regard to judges' understanding of testimony, Kozinski (2001) spoke of a recent survey of the judiciary in Australia noting two important factors that judges consider when comprehending testimony which included a perceived bias by the witness and the ability of the witness to communicate with the court. This becomes particularly important when testifying about digital AIS evidence and explaining the discovery and delivery of data (Rechtman, 2006) and should also be heavily considered in the case of judges who could make rulings without full comprehension of AIS financial information testimony (Craig and Reddy, 2004). Because most companies utilize AIS software, it will be important for juries, judges, attorneys and all involved in a fraud trail to comprehend findings derived from an AIS so that the Forensic Examiner's financial testimony be understood and considered reliable (Lichtman, 2009; Lowe et al., 2002).

CSI Effect

The CSI Effect also known as the CSI syndrome or CSI Infection (http://en.wikipedia.org/wiki/CSI_effect) deals with juries previously being exposed to shows such as *CSI Miami* or *CSI: Crime Scene Investigation* who may demand more forensic

evidence in criminal and fraud trials (http://www.neiai.org/). . Researchers indicate that because of the CSI Effect, judges in order to initiate fairness in the trial process, will many times issue rulings and/or give special instructions to the jury directed at the perceived impact of the CSI Effect at criminal trials (http://www.llrx.com/features/forensicevidencecsieffect.htm).

Although research does exist on the CSI Effect in criminal trials, very few studies exist on the CSI Effect on fraud trails dealing with AIS derived financial data testimony (Brickell, 2008; Podlas, 2006; Schweitzer & Saks, 2007)

Whose Responsibility Is It?

Therefore, whose responsibility would it be to educate all involved in a fraud trial? Craig and Reddy (2004) noted in a recent article that Australian judges indicated expert accounting evidence to be the most difficult evidence to evaluate adequately especially AIS accounting data. The authors suggested ways to improve the process of expert accounting evidence testimony which included communication skills training as well as financial training not only for the forensic accountants but for the judges as well. The authors believed that it would be the forensic accountants' responsibility to communicate accounting and AIS data accurately and clearly to the court. Wells (2005) indicated that although CPA's will usually be regarded as specialists in accounting and AIS, an automatic qualification for an expert witness (www.legal-explanations.com/definitions/expert-witness.htm) does not exist for forensic accountants. Many times, qualifications will be decided on a case-by-case basis with the judge making the expert witness determination at the time of trial and it would be quite a loss for the prosecution if important evidence provided by the expert witness would be set aside because of expert witness competency issues or if the judge who does not understand AIS evidence, makes judgments based upon incorrect presumptions (Heitger and Crumbley, 2005).

FUTURE RESEARCH

It would be interesting to note the perceptions of attorneys and judges in the court system as to what might enhance understandability of AIS testimony and the CSI Effect on jurors. Some researchers believe AIS testimony might be more convincing if forensic investigators were trained better when they "tell the story". Others believe expert testimony might be more convincing if investigators possessed a good background and understanding of the AIS systems for which the fraud has been perpetuated. Still others believe the judges and juries' understanding of testimony on AIS documentation would be more helpful.

Not all researchers agree what would make AIS testimony more convincing. A possible future study could involve conducting a quantitative research project on the perceptions of judges directly involved in validating AIS forensic evidence. It might be especially helpful to inquire as to what AIS evidence was put aside or not allowed as expert testimony and find out why these rulings were made.

CONCLUSION

Fraud investigators will many times spend weeks working on a case to prosecute fraud. Forensic accountants must be well trained in the rules of evidence, financial data, AIS software, communication skills as well as be able to convince a judge that they should be viewed as an

expert in their field. Since most of the fraudulent cases use evidence consisting of accounting data and specifically accounting data retrieved from an AIS system of some sort, not only should these investigators must be well versed in AIS but perhaps also fraud trial attorneys and more importantly, the judges involved with such decisions. Sometimes expert witness testimony validity will be decided on a case-by-case basis with the judge making the expert witness determination at the time of trial. It would be quite devastating to the prosecution if crucial expert witness testimony is discarded because of expert competency issues or unrealistic juror expectations because of the CSI Effect. Or even a worse situation, if the expert witness testimony is thrown out because the judge, not fully understanding AIS evidence, made judgments based upon incorrect presumptions (Heitger and Crumbley, 2005).

REFERENCES

Adogame, A. 2009. The 419 code as business unusual: Youth and the unfolding of the advance fee fraud online discourse. *Asian Journal of Social Science* 37(4): 551-573

Billings, B. and D.L.Crumbley 1996. The use of regression analysis as evidence in litigating tax-related issues. *Journal of Applied Business Research 12:* 3: 97-107

Bodnar, G. H., and Hopwood 2010. Tenth edition. *Accounting Information Systems*. Upper Saddle River, NJ: Prentice-Hall.

Brickell, W. (2008). Is it the CSI Effect or do we just distrust juries? *Criminal Justice 23*(2): 10-16.

Buckhoff, T.A. 2004. Cash: The favorite target of fraudsters. *CPA Journal*: *7:* 63.

Buckhoff, T. A. and J.D. Hansen 2002. Interviewing as a 'Forensic-type' Procedure. *Journal of Forensic Accounting 3*(1): 1-16.

Buckhoff, T. A., and B.K.P. Kramer. 2005. Using Excel to ferret out fraud. *Strategic Finance 86*: 46-50.

Christensen, J., Byington, J.R., and T.J. Blalock 2005. Sarbanes-Oxley: Will you need a forensic accountant? *Journal of Corporate Accounting and Finance 16*(3): 69-75.

Craig, R., and P. Reddy. 2004. Assessments of the expert evidence of accountants. *Australian Accounting Review 14*: 73-81.

Derby, B. L. 2003. Data mining for improper payments. *The Journal of Government Financial Management. 52*: 10-13.

http://en.wikipedia.org/wiki/CSI_effect

Fiore, A.M., H. Jin, and J. Kim. 2005. Hedonic value from image interactivity and responses toward an online store. *Psychology and Marketing 22*: 669-695.

Green, R.P., and S. Cooper. 2003. Computer Sleuth. *California CPA*. *71*(8): 26-27.

Harris, C.K. and A.M. Brown. 2000. The qualities of a forensic accountant. *Pennsylvania CPA Journal 71*(1): 6-8.

Heitger, L.E., and D.L. Crumbley. 2005. Litigation support in antitrust situations. *The CPA Journal 75*: 56-60.

Hochberg, N.E. 2006. When accounting practices go under the microscope. *Financial Executive 22*(1): 53-56.

Houck, M.M., M. Kranacher, B. Morris, R.A. Riley, J. Robertson, and J.T.Wells 2006. Forensic Accounting as an Investigative Tool. *The CPA Journal 76*(8): 68-70.

Hyman, D.A. 2001. The Regulation of managed care organizations and the doctor-patient relationship. *The Journal of Legal Studies 30*(2): 531-567

Jordan, B. 2006. Giving evidence in court. *Chartered Accountants Journal 85*(4): 66-67.
Kahan, S. 2005. Bring 'em back intact. *Accounting Today* 19(18): 14-16.
Kranacher, M., and L. Stern. 2004. Enhancing fraud detection through education. *CPA Journal 4*: 66-68.
Kozinski, A. 2001. Expert testimony after Daubert. *Journal of Accountancy. 2001*: 59-62.
http://www.legal-explanations.com/definitions/expert-witness.htm.
Levi, M. 2008. *The Phantom Capitalists*. Second edition. Andover: Ashgate: 141-153.
Lichtman, S.H. 2009. The power of storytelling. *The CPA Journal 79*(4): 6-8.
Lowe, D.J., P.M.J. Reckers, and S.M. Whitecotton. 2002. The effects of decision-aid use and reliability on jurors' evaluations of auditor liability. *The Accounting Review* 77(1): 185-202
http://www.llrx.com/features/forensicevidencecsieffect.htm
Manning, G.A. 2005. *Financial Investigation and Forensic Accounting*. Boca Raton: Taylor and Francis Group.
Marden, R and T. Darner. 2006. CPAs as Forensic Accountants in Divorce Engagements. *The CPA Journal 76*(5): 62-65.
http://www.neiai.org/
Niedermeier, K.E., N.L.Kerr, and L.A. Messe. 1999. Jurors' use of naked statistical evidence: Exploring bases and implications of the Wells effect. *Journal of Personality and Social Psychology 764*: 553-542.
Neufer, N. L. 2001. *Complex Evidence and Communication: The Good, the Bad and the Ugly*. Section of Litigation, Chicago IL: American Bar Association.
Neufer, N.L 2000. Statistical evidence: How to help jurors understand and use it properly. *Defense Counsel Journal 67*(3): 386-391.
http://www.ncjrs.gov/pdffiles1/nij/199408.pdf
http://www.neiai.org/; http://www.jstor.org/pss/20455645
http://www.osa.state.mn.us/default.aspx?page= 20090724.057
Podlas, K (2006). *Fordham University Publications: Media & Ent. 16:* 429-458.
Rechtman, Y 2006. Forensic computing: A review of a growing technical field. *The CPA Journal 76*(7): 68-69.
Rasmussen, D.G., and J.L. Leauanae. 2004. Expert witness qualifications and selection. *Journal of financial Crime 12*: 165-172.
Retrieving Electronic Data. 2006. *Journal of Accountancy 202*(3): 34.
Rosenberg, C.B. June, 1989. An L. A. lawyer replies. *The Yale Law Journal 98*(8): 1625-1629.
Schweitzer, N.J., & Saks, M. J. (2007). The CSI Effect: Popular fiction about forensic science affects the public's expectations about real forensic science. *Jurimetrics*, *47*(3): 357-364.
Shmukler, E. 2005 February 1. Executives on trial: Scrushy team cross-examines forensic accounting witness. *The Wall Street Journal* (February)1*:* C4.
Stringer-Calvert, D.W. 2002. Digital evidence. *Communications of the ACM 45*(4): 128.
Tyler, T. R. (2006). Viewing CSI and the Threshold of Guilt: Managing Truth and Justice in Reality and Fiction. *The Yale Law Journal, 115*(5): 1050-1085
Volonino, L. 2003. Electronic evidence and computer forensics. *Communications of the Association for Information Systems 12*: 457-468.
Weber, R. 1999. *Information Systems Control and Audit.* Upper Saddle River, NJ: Prentice-Hall

Weld, L. G., P.M. Bergevin and L. Magrath 2004. Anatomy of a financial fraud. *The CPA Journal 74*: 44-50.

Wells, J. 2005. When you suspect fraud. *Journal of Accountancy 199*: 82-85.

Wells, J. 2003. The fraud examiners. *Journal of Accountancy* 196: 76.

Williams, K. Feb, 1997. Safeguarding companies from computer/software fraud. *Management Accounting* 78: 18.

Wolfe, D. T., and D.R. Hermanson December, 2004. The fraud diamond: Considering the four elements of fraud. *CPA Journal* 7: 38-42.