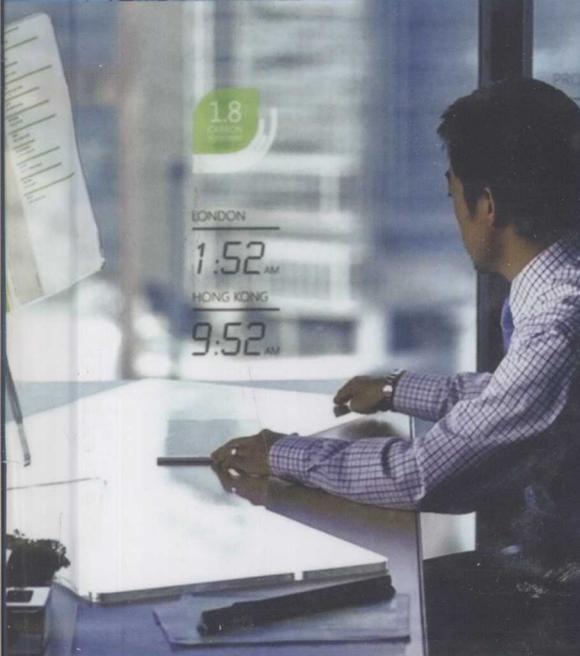


Second Edition



Forensic Accounting *and* Fraud Examination



William S. Hopwood

Jay J. Leiner

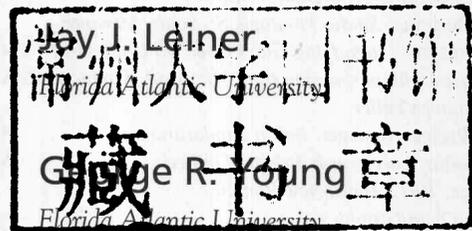
George R. Young

Forensic Accounting and Fraud Examination

Second Edition

William S. Hopwood

Florida Atlantic University



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FORENSIC ACCOUNTING AND FRAUD EXAMINATION, SECOND EDITION

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To all the faculty and staff in the Forensic Accounting Masters Program at Florida Atlantic University.

William Hopwood

I dedicate this book to my family and friends; to my wife, Diane; my sons, Victor and Peter; and Mom and Ezio for always believing in me; to my real friends and partners, the old interdiction team (you know who you are), thanks for being there for me and pushing me that little extra step; to my coauthors, Bill and George, for supporting me and asking me to join them as a coauthor; and last, but not least, to the Broward County Sheriff's Office for giving me the opportunity to investigate cases and to Florida Atlantic University for the opportunity to educate others.

Jay Leiner

I dedicate this book to my father, George, and my mother, Wilma; my wife, Sherry, and my sons, Joshua and Angelo.

George Young

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Preface

WHAT'S NEW IN THE SECOND EDITION

Because of a general increase in the demand for fraud investigation services, the second edition adds five new chapters relating to fraud investigation processes. The result is that, as revised, Part II (Chapters 5–12) covers the entire fraud investigation process over the span of eight chapters. Parts III and IV (Chapters 13–18) follow up with various types of fraud applications that range from employee and vendor fraud to anti-money laundering and counterterrorism.

A major distinction of the second edition is that it follows a process-oriented approach. This means that fraud investigation is presented as an organized sequence of steps that start at some point and end at some other point. Flow diagrams are presented throughout Part II (Chapters 5–12) to graphically illustrate the sequence of steps followed in fraud investigations.

The process-oriented approach differs significantly from taxonomy-based approaches commonly followed in the literature. Taxonomy-based approaches tend to focus on classifying fraud investigation methods. Although useful, taxonomy approaches in and of themselves do not provide the most basic guidance needed by a fraud investigator, namely what to do first, second, and so on, and when to end a given phase of an investigation.

TEXT ORGANIZATION

The text seeks to provide comprehensive coverage of fraud examination and forensic accounting through a wide range of topics relevant to all types of students, regardless of their major, concentration, or level of studies. The chapters are organized into five major parts. Part I deals with topics primarily relevant to the fraud examination and forensic accounting environment. Part II introduces the theory, processes, and methods of fraud examination. Part III focuses on occupational and organizational fraud. Part IV deals with various specialized nonoccupational areas of fraud. Part V highlights forensic accounting services whose applications are typically outside the area of fraud examination.

PART I INTRODUCTION TO FORENSIC ACCOUNTING AND FRAUD EXAMINATION

This part covers various foundational areas of importance to fraud examination and forensic accounting. Chapter 1 provides a general overview. Chapter 2 focuses on the legal procedures that are frequently relevant to forensic accounting work. Both criminal and civil procedures are covered, with a special emphasis on criminal procedures because they are often ignored in the typical business law courses.

Chapters 3 and 4 provide comprehensive, self-contained units in accounting information systems and auditing. Inclusion of these chapters makes the text accessible to nonaccounting majors and even to nonbusiness majors.

PART II FRAUD EXAMINATION THEORY, PRACTICE, AND METHODS

This part discusses basic and advanced fraud examination and investigation processes. The flow of chapters in this section corresponds to the entire fraud investigation process: fraud prevention (Chapter 5), fraud detection (Chapter 6), fraud investigations and the engagement process (Chapter 7), the fraud evidence collection process (Chapter 8), physical,

documentary, and observational evidence (Chapter 9), interview methods (Chapter 10), forensic science and computer forensics (Chapter 11), and fraud reports, litigation, and the recovery process (Chapter 12).

PART III OCCUPATIONAL AND ORGANIZATIONAL FRAUD

This part features specific areas of occupational and organizational fraud. Chapter 13 deals with employee and vendor fraud. Chapter 14 focuses on financial statement fraud. Chapter 15 highlights fraud and the Sarbanes-Oxley Act.

PART IV SPECIALIZED FRAUD AREAS

This part focuses on specialized areas in which frauds typically originate from specific types of individuals outside of the organization. Chapter 16 deals with tax fraud; Chapter 17 with frauds relating to bankruptcy, divorce, and identity theft; and Chapter 18 with organized crime, money anti-money laundering, and counterterrorism.

PART V OTHER FORENSIC ACCOUNTING SERVICES

This part discusses forensic accounting services not directly related to fraud. Chapter 19 deals with business valuation, and Chapter 20 focuses on dispute resolution and litigation services.

TEACHING APPROACHES AND THE SELECTION OF CHAPTERS

Chapters are written in a modular, self-contained fashion so that instructors can select chapters from each of the five major parts according to specific course requirements. Some basic teaching approaches are as follows:

Comprehensive Focus

Following this approach, an instructor can cover all, or almost all, chapters over a single school term. The auditing and accounting systems chapters could be skipped if students have completed prerequisite courses in these areas.

Fraud and Auditing Focus

Following this approach, the instructor would cover the following chapters in Part I: Chapters 1 (introduction) and 2 (legal) and Part II, Chapters 5–12 (fraud investigation processes). These chapters can then be followed by selected fraud-related applications from Part IV, Chapters 13–18 (fraud applications).

Forensic Accounting Focus

Following this approach, the instructor would cover Chapters 1–2 (introduction and legal), Chapters 5–12 (fraud investigation processes), and Chapters 19–20 (forensic accounting services).

Eclectic Focus

Because the chapters are self-contained and modular, the instructor can select any desired set of chapters to meet particular course needs. Furthermore, the chapters in Part III can be covered in almost any order.

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The authors would like to thank the following forensic accounting educators for their input during the development of the first and second editions of *Forensic Accounting and Fraud Examination*. The feedback from these knowledgeable instructors provided the authors valuable assistance in meeting the needs of the forensic accounting classroom.

Second Edition

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Part I

Introduction to Forensic Accounting and Fraud Examination