

AN ANALYSIS OF FRAUD AT BIG TRAINING CORPORATION

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ABSTRACT

This paper describes an actual fraud case. The names of the organizations and individuals involved have been disguised to preserve anonymity. The fraud was an attempt at asset misappropriation related to employee compensation. The paper describes the corporation and the fraud, then analyzes it in terms of the Association of Certified Fraud Examiners taxonomy of occupational fraud and the ACFE code of ethics. The paper concludes with the resolution of the case.

INTRODUCTION

Fraud can occur in organizations of all types: public and private sector, large and small, service, retail and manufacturing. This paper looks at an actual example of a fraud, relating it to various ideas in the fields of fraud examination and forensic accounting. Although the case described here is real, some details have been changed to preserve the anonymity of the parties involved. The paper is divided into the following sections: description of Big Training Corporation (BTC), description of the fraud, analysis and resolution.

DESCRIPTION OF BIG TRAINING CORPORATION

BTC is a multi-divisional company specializing in providing educational seminars on various business subjects; BTC has divisions throughout the western United States, each with a specific subject area focus. Each division is treated as a profit center; each division has a general manager that enjoys substantial autonomy in decision making.

Dale is the manager of the Los Angeles division of BTC. The Los Angeles division employs a staff of twelve seminar presenters, including Dale's wife; the Los Angeles division specializes in seminars on accounting topics such as financial statement preparation and interpretation, cost management and taxation. BTC has an established policy on nepotism. The policy does not prohibit the employment of immediate family members, it does, however, include the following points:

- No BTC employee may participate in personnel-related decisions involving an immediate family member.
- If a BTC employee works under the direct supervision of an immediate family member, a specific, written plan for addressing the inherent conflict of interest must be developed and approved by the vice president for human resources and ethics.
- The vice president for human resources and ethics must review all decisions on personnel matters involving the employee and his / her supervisor.

Consultants are paid a flat fee for each seminar they give, regardless of the number of participants; most of BTC's seminars filled to capacity. The Los Angeles division's fees and costs are presented below:

Table 1

Fee per student	\$	800
Variable cost per student		300
Fixed cost per seminar		5,000

Variable costs included items such as meals, refreshments, textbooks and other materials; fixed costs primarily comprised the salary of the presenter, but also included minor amounts for allocated overhead. The significant increase in fees per student had reduced demand marginally, but not significantly. Depending on the subject matter, maximum enrollment for each seminar had varied from 30 students to 40 students, with more general seminars having higher maximum enrollments. As division manager, Dale was responsible for setting the maximum size of each seminar and for assigning presenters to each seminar. Dale also had the option of giving up to five seminars throughout the year, for which he received compensation above and beyond his salary as division manager.

DESCRIPTION OF THE FRAUD

Dale had been manager of the Los Angeles division for about a year when the fraud occurred. Without notifying anyone at the corporate headquarters, Dale selectively reduced the maximum seminar size to ten students in the middle of 2011; that is, some consultants continued with the historical maximum enrollments, while others (including Dale and his wife) had their maximum enrollments reduced to the new break-even point. As a result, the Los Angeles division significantly increased the number of seminars offered, but substantially decreased division profits as shown below.

Table 2

	<i>Enrollment</i>	<i>Profit per seminar</i>	<i>Number of seminars</i>	<i>Total profit</i>
Seminar topic		Before the change		
Introduction to financial statements	40	\$ 15,000	1	\$ 15,000
Financial statement analysis	30	10,000	1	10,000
Cost accounting fundamentals	40	15,000	1	15,000
Advanced topics in cost accounting	30	10,000	1	10,000
Introduction to personal taxation	40	15,000	1	15,000
GAAP overview	40	15,000	1	15,000
Totals			6	\$ 80,000
Seminar topic		After the change		
Introduction to financial statements	10	\$ -	4	\$ -
Financial statement analysis	30	10,000	1	10,000
Cost accounting fundamentals	10	-	4	-
Advanced topics in cost accounting	10	-	3	-
Introduction to personal taxation	40	15,000	1	15,000
GAAP overview	40	15,000	1	15,000
Totals			14	\$ 40,000

Anthony was a consultant in the Los Angeles division whose seminar enrollments were not reduced; he was also a certified fraud examiner. He discovered the selective reductions by reviewing information freely available to employees in the accounting information system. Anthony questioned Dale about the selective reductions. Dale replied: “Our consultants get paid by the number of seminars, not the number of participants. I wanted to increase the number of seminars offered so the consultants would earn higher salaries.”

Anthony reported the changes to BTC’s corporate office; he included actual enrollment data as part of his report. BTC’s vice president of finance was alarmed at the changes and confronted Dale about them. Initially, Dale denied making the changes; when the vice president showed him the enrollment data, he quickly confessed to what he had done and promised to make appropriate changes.

ANALYSIS

The Association of Certified Fraud Examiners (www.acfe.com) defines occupational fraud as: “The use of one’s occupation for personal enrichment through the deliberate misuse or misapplication of the employing organization’s resources or assets.” (Association of Certified Fraud Examiners, 2010) Thus, the BTC case constituted occupational fraud; Dale, the division manager, used his position to enrich both himself and a select group of consultants, including his wife, in the Los Angeles division.

The ACFE classifies occupational fraud in three groups: corruption, asset misappropriation and fraudulent statements. (Association of Certified Fraud Examiners, 2010) Corruption comprises conflicts of interest, bribery, illegal gratuities and economic extortion. Asset misappropriation most frequently involves cash as part of a larceny or skimming scheme; it can also involve fraudulent cash disbursements and non-cash assets such as inventory. Fraudulent statements in the ACFE's taxonomy are divided into two subgroups: financial and non-financial. Fraudulent financial statements include many of the items seen in the corporate scandals of the late 20th century, such as Enron and Health South: overstatements of assets and / or revenues, concealed liabilities and the like. Non-financial fraudulent statements include such things as falsified employment credentials.

The BTC fraud fits into the ACFE taxonomy as a corruption case, more specifically as a conflict of interest. Dale had a clear conflict of interest in selectively changing seminar sizes, since both he and his wife would benefit from the change. In addition, Dale had violated BTC's nepotism policy. Although many frauds are initially detected via tips (roughly 40% according to the ACFE), some are detected accidentally (about 8%), as was true in this case. [1]

As a certified fraud examiner, Anthony also had to adhere to the ACFE's Code of Professional Ethics. The code comprises eight points [2]:

- 1) A Certified Fraud Examiner shall, at all times, demonstrate a commitment to professionalism and diligence in the performance of his or her duties.
- 2) A Certified Fraud Examiner shall not engage in any illegal or unethical conduct, or any activity which would constitute a conflict of interest.
- 3) A Certified Fraud Examiner shall, at all times, exhibit the highest level of integrity in the performance of all professional assignments and will accept only assignments for which there is reasonable expectation that the assignment will be completed with professional competence.
- 4) A Certified Fraud Examiner will comply with lawful orders of the courts and will testify to matters truthfully and without bias or prejudice.
- 5) A Certified Fraud Examiner, in conducting examinations, will obtain evidence or other documentation to establish a reasonable basis for any opinion rendered. No opinion shall be expressed regarding the guilt or innocence of any person or party.
- 6) A Certified Fraud Examiner shall not reveal any confidential information obtained during a professional engagement without proper authorization.
- 7) A Certified Fraud Examiner will reveal all material matters discovered during the course of an examination which, if omitted, could cause a distortion of the facts.
- 8) A Certified Fraud Examiner shall continually strive to increase the competence and effectiveness of professional services performed under his or her direction.

Anthony's actions after discovering the fraud most clearly related to the first and fifth points of the ACFE code.

RESOLUTION

After the fraud was discovered, Dale promised the vice president that he would increase the maximum seminar sizes to their historic levels for all staff. A subsequent review of data from the accounting information system revealed that Dale had made the changes shortly after the confrontation, but once again selectively reduced the maximum enrollments once the corporate office had verified the changes. As of this writing, Dale remains a division manager at BTC; his wife continues to work there as well.

References

- [1] Association of Certified Fraud Examiners (2010). Report to the Nations on Occupational Fraud and Abuse (www.acfe.com).
- [2] Hurt, Robert L. (2010). Accounting Information Systems: Basic Concepts and Current Issues. McGraw-Hill / Irwin.