

**A QUALITATIVE CASE STUDY OF CHIEF FINANCIAL OFFICER (CFO) FRAUD  
MOTIVATIONS WITHIN COMMON AND UNCOMMON DEMOGRAPHIC GROUPS**

by

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## Abstract

Existing academic studies have historically examined various elements of occupational fraud, particularly the fraud triangle (pressure, opportunity, and rationalization). Studies have additionally considered which demographics are most prevalent in those who commit fraud, in particular the chief financial officer (CFO). This study combines the fraud triangle, specifically the intersection of pressure and rationalization, or motivation, with the demographics of CFOs in answering the research question: for CFOs indicted of corporate fraud, what differences are seen in fraud motivations for CFOs with common fraud demographics (male, younger, lesser-educated) versus lesser common demographics (female, older, more highly educated, or any other combination)? The research methodology used for this study was qualitative case study in the use of secondary public data. This data was extracted from news media and court case files in arriving at CFO fraud motivation. CFOs, indicted by the Securities and Exchange (SEC) and/or Department of Justice (DOJ) were reviewed for this study's population. CFOs that progressed into mature stages of the indictment were included as a sample candidate and cases where fraud motivation detail was available were selected for the 11-person study. Data from the study was coded into broad categories of findings and eventually into research themes. The themes associated with CFO fraud motivations were determined to be financial motivation, internal pressure, and external pressure. Research findings determined that all three fraud motivation themes were consistently present across common and uncommon demographic groups. These findings suggest there are not noticeable differences in fraud motivations across a CFO based purely on their demographic makeup.

## **Dedication**

This dissertation is dedicated to my three biggest life cheerleaders. First, this dissertation is dedicated to my wife, Kathleen, who has always supported my personal and professional aspirations, even if they were not always the most logical or understandable. I appreciate her constant support and actively managing the household during my many weekends studying and writing. Next, this dissertation is dedicated to my little girl, Ryan, for always being aware, even at an early age, of my schoolwork and related studies. Although she will not likely understand and even remember much of my doctoral work, she was continuously my source of motivation to think big and act with purpose. Finally, this dissertation is dedicated to my late father, Bob, who consistently instilled in me to be a greater person and live a higher value life than he had. It was always his hope that his children would be successful and live stably. Thanks, dad, for your motivation from heaven.

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## Table of Contents

|  |     |
|--|-----|
| Acknowledgments.....                             | iv  |
| CHAPTER 1. INTRODUCTION.....                     | 1   |
| Background of the Study .....                    | 1   |
| Need for the Study .....                         | 5   |
| Purpose of the Study .....                       | 8   |
| Significance of the Study .....                  | 100 |
| Research Question .....                          | 17  |
| Definition of Terms.....                         | 17  |
| Research Design.....                             | 19  |
| Assumptions and Limitations .....                | 200 |
| Assumptions .....                                | 200 |
| Limitations.....                                 | 211 |
| Organization of the Remainder of the Study ..... | 222 |
| CHAPTER 2. LITERATURE REVIEW .....               | 244 |
| Methods of Searching .....                       | 244 |
| Theoretical Orientation for the Study .....      | 244 |
| Review of the Literature .....                   | 277 |
| Synthesis of the Research Findings .....         | 51  |
| Critique of Previous Research Methods .....      | 54  |
| Summary.....                                     | 57  |
| CHAPTER 3. METHODOLOGY .....                     | 58  |
| Research Question .....                          | 60  |

|   |     |
|---|-----|
| Research Design.....                                      | 60  |
| Target Population and Sample .....                        | 622 |
| Population .....  | 622 |
| Sample .....  | 633 |
| Procedures.....   | 633 |
| Participant Selection .....                               | 655 |
| Protection of Participants.....                           | 655 |
| Data Collection .....                                     | 656 |
| Data Analysis.....  | 666 |
| Instruments.....  | 677 |
| The Role of the Researcher.....                           | 688 |
| Guiding Interview Questions.....                          | 689 |
| Ethical Considerations .....                              | 699 |
| Summary.....  | 69  |
| CHAPTER 4. PRESENTATION OF THE DATA.....                  | 71  |
| Introduction: The Study and the Researcher.....           | 71  |
| Description of the Sample.....                            | 72  |
| Research Methodology Applied to the Data Analysis .....   | 73  |
| Presentation of Data and Results of the Analysis .....    | 74  |
| Summary .....   | 119 |
| CHAPTER 5. DISCUSSION, IMPLICATIONS, RECOMMENDATIONS..... | 120 |
| Summary of the Results .....                              | 120 |
| Discussion of the Results .....                           | 122 |



|   |        |
|---|--------|
| Conclusions Based on the Results .....                                    | 123    |
| Comparison of Findings with Theoretical Framework and Previous Literature | 124125 |
| Interpretation of the Findings.....                                       | 125    |
| Limitations .....   | 12726  |
| Implications for Practice .....   | 128129 |
| Recommendations for Further Research.....                                 | 129    |
| Conclusion .....  | 131132 |
| References.....   | 133    |

## CHAPTER 1. INTRODUCTION

### Background of the Study

This study examines the motivation of chief financial officers (CFO) in committing occupational fraud within the organization by which they are employed. Specifically, the study strives to better understand the differences in CFO motivations between the common and uncommon demographic groups historically seen in white collar crime. Research suggests that fraud is commonly committed by younger and less-educated male CFOs (Sun, Kent, Qi, & Wang, 2017).

Every other year, the Association of Certified Fraud Examiners (ACFE) publishes the Report to the Nations on Occupational Fraud and Abuse (Dorris, 2018), which outlines reported cases of global occupational fraud spanning multiple industries in nearly every corner of the globe. The report describes the wronged company's size, likely losses by event, types of fraud experienced, information relating to the fraud discovery, potential reasons for the breach, and demographical data of the fraudster. The 2018 ACFE report was a compilation of 2,690 reported cases, inclusive of 125 countries at a total loss of \$7 billion (Dorris, 2018).

In addition to self-reported cases of occupational fraud, the Security and Exchange Commission (SEC) publishes an annual report outlining the governmental actions against specific companies and individuals formally indicted for fraudulent acts (White, 2014; White, 2015; White, 2016). Of interest are instances where executive employees are implicated for fraudulent acts, given their inherent stature and influence with a typical company structure (Lawson & Omer, 2012). Specifically, CFOs wield high level influence over internal and external financial reporting and are allowed access not true of other executives (Bishop, DeZoort, & Hermanson, 2017b). These CFOs exhibit certain pressures that can be unique to their

role, such as CEO pressure toward the CFO, investor pressure and results-driven pressure linked to long-term CFOs tenure. These pressures, collectively or individually, may trigger decisions by CFOs to manipulate financial statements through fraudulent actions (Bishop et al., 2017b).

Occupational fraud, a broader concept than merely financial statement fraud, includes acts that are committed by an employee by virtue of their role in an organization. Occupational fraud is inclusive of financial statement fraud but could also include situations such as asset misappropriation and corruption (Dorris, 2018). For the purposes of this research, occupational fraud is studied because of its widening of the fraud topic, leaving opportunity to study a variety of CFO fraudulent actions beyond only financial statement fraud. However, financial statement fraud tends to be the most commonly indicted scenario by the SEC (White, 2014; White, 2015; White, 2016) and therefore is a point of focus throughout this study's literature review process.

A variety of parties take interest in the outcomes of occupational fraud, as well as its prevention and detection, though likely none more than the investor community. Brazel, Jones, Thayer, and Wayne (2015) reported that investors use their perceptions of fraud in investment decisions and their reliance of fraud red flags in determining whether to apply additional due diligence on a company. This is not a surprise given the U.S. median loss per reported fraud case is \$130,000 and nearly double that amount for Asian companies (Dorris, 2018). Highly publicized cases, such as Enron, WorldCom, and HealthSouth display instances of monumental losses and breaches in internal controls when studied post-incident (Soltani, 2014).

Related to CFO specific fraud, much existing literature centers on a few common themes. First, fraud triangle theory, this study's theoretical basis, establishes the pillars typically present when a fraudulent choice is made, inclusive of pressure, rationalization and opportunity, as it is reported historically. Specifically, the role of power in position as it connects to fraud (Albrecht,

Holland, Malagueno, Dolan, & Tzafir, 2015), the evolution of fraud triangle theory (Dorminey, Fleming, Kranacher, & Riley, 2012), its direct correlation to discovered and indicted fraud (Soltani, 2014), and challenges to the proper geometry of fraud theory (Huber, 2016) have been most actively discussed in historic literature.

Additionally, literature actively discusses fraud motivation – the connection between fraud pressure and rationalization – consistent in executive-level employees, including the CFO, who commit fraudulent acts as inherent by virtue of their high-level positions. This is demonstrated through works discussing financial and external pressures (Bishop et al., 2017), earnings management strategies employed by CEOs and CFOs (Qi, Lin, Tian, & Lewis, 2018), CEOs' pressure influence on CFOs and related financial reporting choices (Bishop et al., 2017a) and how corporate goal setting can implicate fraud (Donegan, Ganon, & Johnson, 2017).

The demographics of participants in situations where fraud has taken place is a common theme in existing literature. Past research studies have looked at a variety of executive level employees' participation in fraud, while overlaying a number of demographical variables. A few examples include CFO/CEO/Audit Committee influences on accruals and reporting, which may create or lead to fraudulent acts (Lawson & Omer, 2012), CFO expertise tied to accounting restatements, a common circumstance of a past fraudulent act (Aier, Comprix, Gunlock, & Lee, 2005), accounting practices employed in relation to a CFOs personal style, which may signal a fraudulent act has or may occur (Ge, Matsumoto, & Zhang, 2011), a CFO's most likely gender in questionable earnings management scenarios, a common way for CFOs to employ accounting practices that are fraudulent (Liu, Wei, & Xie, 2016), and CFO age, gender and education level as it relates to known financial statement fraud (Sun et al., 2017), among others. While these studies have outlined several demographics present through a smattering of results across groups,

they have offered little in terms of organizing the demographics and focusing in on any particular set.

Finally, literature tends to align around morality, ethics and decisions by people who commit fraudulent acts. Fraud research in this space is wide spanning, discussing everything from written deception (Zhou & Zhang, 2008) to common levels of creativity most prevalent in dishonest decision-making (Gino & Ariely, 2012) to how people collaborate with others in deceptive situations (Briggs, Workman, & York, 2013) and even the time of day most subject to fraudulent thinking (Shalvi, Eldar, & Berby-Meyer, 2012). The issues remaining to be understood are a connection between where the literature has gone thus far, namely connecting demographics of those who commit fraudulent acts, with the fraud triangle. Specifically, CFOs in positions of leadership, who commit fraud perceivably, have reasons for doing so, disclosed or undisclosed. These CFOs also exhibit common and uncommon demographics, with common demographics defined in literature thus far as younger males with less education (Aier et al., 2005; Barua, Davidson, Rama, & Thiruvadi, 2010; Liu et al., 2016; Qi et al., 2018; Sun et al., 2017; Troy, Smith, & Domino, 2011). However, a connection between CFO demographics, common and uncommon, has not been merged with CFO motivation (pressure and rationalization) for committing a fraud. As such, this study addresses that gap.

The researcher's interest in this topic extends to his professional certification as Certified Fraud Examiner (CFE) supported by the ACFE. Fraud is an expansive and complex topic, with many varying angles. The interest interacts not only with theory, such as fraud theory (Dorminey et al., 2012) and upper echelon theory (Hambrick & Mason, 1984), but also issues of ethics as it relates to decision making (Ford & Richardson, 1994) and deception, including how and when people deceive others (Briggs et al., 2013; Gino & Ariely, 2012; Shalvi et al., 2012). Finally,

from the perspective of a fraud fighting professional, fraud detection, prevention, and auditing are of great interest and common connection. Before effective fraud controls can be designed, however, the research community must fully understand the topic to address it correctly.

The primary theory used in this study to understand CFO occupational fraud is fraud theory, sometimes referred to as fraud triangle theory. While occupational fraud can be traced back to the 1600s, the fervor of financial statement frauds in the 2000s have contributed most to the preponderance of fraud theory research as of late (Dorminey et al., 2012). Fraud theory is widely viewed as the linchpin of white collar crime in the modern world, migrating from a two to three-dimensional model in the 2000s (Dorminey et al., 2012). While there are any number of factors that can contribute to occupational fraud, such as ethical climate, top at the top, bubble economy, governance and incentive issues, even a post hoc analysis of six large American and European corporate frauds (Enron, WorldCom, HealthSouth, Parmalat, Royal Ahold, and Vivendi Universal) linked back to fraud theory (Soltani, 2014).

More recent studies have challenged elements of fraud theory, including the geometry and variables (Huber, 2016). However, research is consistent that even minimum components of fraud theory link to nearly every fraud circumstance, particularly motivation. As such, this study hopes to advance fraud theory with the potential of discovering demographical versus motivational phenomenon not previously reported.

### **Need for the Study**

Upon discovery of fraud of nearly any kind, a postmortem analysis is often completed on the specific situation and underlying ways in which the fraud was able to begin and continue through to discovery. As is common in fraudulent corporate situations, the analysis of the why and how can be vast, varied, complex, and different situationally. There are any number of

factors discovered in fraud post review such as ethical climate, tone at the top, market pressures, and compensation structure (Soltani, 2014), the use of power by executive-level employees (Albrecht et al, 2015), pressure between and among C-suite employees, for example, CEO to CFO (Bishop et al., 2017b), internal CFO financial pressures and fear of losing their job (Bishop et al., 2017a) and inconsistencies in accounting practices leaving an opportunity for bad behavior (Wustemann & Wustemann, 2010).

These cognitive framing processes may then connect to the common fraud theory elements of pressure, rationalization, and opportunity. In fact, it is often true that while literature grasps for the why and how of fraud occurrence, research consistently comes back to one or multiple elements of fraud theory for its explanation and conclusion. For example, Bishop et al. (2017a) reviewed fraud cases over a 20-year span, focusing on the significant volume of pressures (one arm of the fraud triangle) that CFOs face, namely stock price. Radin (2017) discussed pressures and rationalization, including a situation where a CFO booked a fraudulent entry merely to avoid giving bad news to the CEO. Donegan et al. (2017) spoke to ethics of a fraudulent act while linking the rationale of pressure to report certain positive financial measures publicly. Soltani (2014), who concentrates heavily on other non fraud theory factors linked to six corporate frauds, eventually comes back to pressure and opportunity of executives to commit the ultimate act.

It is true that fraud has many angles and reasons, scenarios and quirks, but time after time, literature tends to come back to the fraud triangle in some fashion. Consistently, motivation, the intersection of pressure and rationalization, is the element most persistent through nearly every fraud situation. On a parallel path, analysis regarding occupational fraud

has studied the players involved in the act itself. This analysis has taken shape across a multitude of industries and includes reviews from all corners of the globe.

Past studies have advised the practitioner community on a myriad of demographics that are present in white collar crime. For example, the most recent ACFE report provided details around level of position, age, gender, and education level most prevalent in discovered fraud cases (Dorris, 2018). Aier et al. (2005) examined CFOs' years of service, experience at other companies, advanced degrees, and certifications as characteristics related to financial restatements of companies. Qi et al. (2018) reviewed age, gender, education level, and financial work experience of top team members in their choices on earnings management strategies. Ge et al. (2011) studied CFO *style* while taking into additional consideration age, gender and educational background in connection to CFO accounting choices and applications. Sun et al. (2017) studied the specific demographics of gender, age, and education level in instances of financial statement fraud reported in China. Xu and Zhao (2016) took fraud research a bit further on the demographics scale in researching the implications of companies who had financial restatements insomuch as knowledge and qualification of CFOs changed, as well as the quality of this change.

In summarizing, the literature suggests those who are younger, male and lesser educated are most likely to engage in an occupational fraud situation, and this tends to align across CFOs, CEOs, board and audit committee representatives (Aier et al., 2005; Barua et al., 2010; Liu et al., 2016; Qi et al., 2018; Sun et al. 2017; Troy et al., 2011;). By default, the uncommon fraud demographic group is any other combination of these three demographics, such as an older, more educated female. Thus far, however, research has not linked the two above concepts together:



fraud theory with the demographics most and least common in executive level employees who commit fraud.

More specifically, one tenant of fraud theory, motivation, a combination of pressure and rationalization, with one specific executive level employee, the CFO, has not historically been connected within the act occupational fraud. This study proposes to do just that; it is a qualitative case study analysis on the motivation of CFOs linking uniquely to the common and uncommon demographical groups of gender, age, and education level. Any noted similarities and differences between the two groups is useful in the further development of fraud triangle theory, as previous literature has suggested a mixed bag of fraud motivation based upon different demographics and circumstances (Troy et al., 2011). Further clarification of the similarities and differences of motivations across the two demographical groups also helps test the fraud triangle for theoretical strength while clarifying motivations potentially helpful in detecting or preventing corporate fraud in the future.

### **Purpose of the Study**

The genesis of fraud theory began with the works of Donald Cressey in the 1950s with his three basic necessary tenants for white collar crime: (a) pressure or incentive, (b) opportunity, and (c) rationalization. This being the basis of fraud theory from the ground roots, fraud triangle theory has undergone a series of criticisms, reviews, and proposed modifications since Cressey's original work. For example, the ways in which the three elements of the fraud triangle interact and the case-by-case situational circumstances that surround each fraud situation cause the fraud triangle to naturally bend and shape with the specific fraud incident. This is demonstrated as simply as understanding that the fraud theme of motivation can be further broken down to rationalization as well as incentive, pressure, or a combination of incentive/pressure (Schuchter

& Levi, 2013). Additionally, tangential issues and new areas of research have begun to form, such as the nature and linkage to fraud collusion and, more broadly, how compliance efforts impact the persistence of fraudulent acts (Free, 2015).

Study of the fraud triangle evolution has been vast but has also seen a higher frequency of discussion in the past decade. These discussions have triggered new questions about the fraud triangle's validity and completeness, sometimes creating new meta-models for the research community to explore and challenge (Dorminey et al., 2012). While the three foundational elements of the fraud triangle exist in real world fraud cases, other aspects cannot be ignored, for instance, ethical climate, tone from the top, public pressures and other such topics (Soltani, 2014). Some recent works have challenged whether the fraud triangle is even a triangle at all, pointing to other added dimensions such as a diamond, hexagon, or even limitless numbers of sides (Huber, 2016).

While the size, shape, and number of characteristics related to the fraud triangle remain under debate, now and likely into the foreseeable future, research has historically aligned around one important component: motivation for a fraudulent act, defined as an intersection of pressure and rationalization, appears persistent in all circumstances. Some may spin the word *motivation* into different elements, such as pressure versus incentive (Schuchter & Levi, 2013), but this creates more an issue of semantics than suggestion that motivation does not exist. That being the case, it seems plausible that fraudster motivation is a ripe area for study, as there remains little debate that motivation is a pillar of fraud theory.

Secondarily, studying who commits fraudulent acts within an organization has cast a wide net across industries, countries, and levels of management. In line with this, research tends to look at fraudster demographics in a variety of ways while cutting through any variety of

situations. This may include post fraudulent events (Sun et al., 2017; Troy et al. 2011; Xu & Zhao, 2016), post financial restatement (Aier et al., 2005), earnings management techniques (Liu et al., 2016; Qi et al., 2018), earnings quality matters (Barua et al., 2010) and a CFO's interpersonal styles connecting to job demands and accounting practices (Ge et al., 2011). When historical research is considered in total, past studies cast light on the demographics most likely present or likely present across a myriad of business situations, when a corporate fraud has been committed as well as when fraud may be an outcome. Additionally, motivational elements link with the CFO demographics in separating those who are more or less likely to participate in such an act. As such, the purpose of this research study is to better understand the intersect between two points: fraudulent CFOs who meet the common demographics of male, younger and less educated (Aier et al., 2005; Barua et al., 2010; Liu et al., 2016; Qi et al., 2018; Sun et al., 2017; Troy et al., 2011) versus those CFOs who do not fit this common demographic (for example, older, more highly educated women) and motivation for committing fraud.

### **Significance of the Study**

Since 1996, the Association of Certified Fraud Examiners (ACFE) has produced an every other year report outlining reported cases of occupational fraud from around the world. The most recent report (Dorris, 2018) captured approximately 2,700 cases of fraud from 125 countries in 23 different industries. These instances of fraud cost investors \$7 billion in losses, with nearly one in four frauds costing more than \$1 million individually. Small businesses were hit especially hard in these frauds, recognizing nearly a 2:1 loss per fraud as opposed to larger companies. Collusion, fraud created by more than one individual working together, saw an explosive effect on median losses, with over a 4:1 loss ratio for collusion of three or more people as opposed to a solo fraudster. Men, particularly those with more than five years of company

tenure, were the most commonly implicated in a fraud; however, only four percent of perpetrators had a previous conviction for a fraudulent act. The ACFE estimated that five percent of company revenues are lost to fraud, based on a survey to 2,000 fraud fighting professionals. If this number, although non quantifiable, is extrapolated to world Gross Domestic Product (GDP), the total loss would be nearly \$80 trillion. For the United States alone, the loss would be \$4 trillion (Dorris, 2018). Additionally, it is worth mentioning that the 2018 ACFE report cited more fraud cases (+280 cases) as well as more total losses (+\$700 million) than the last report in 2016 for the same number of months (Ratley, 2016).

The ACFE is not the only organization monitoring and impacting fraud. The Committee of Sponsoring Organizations of the Treadway Committee (COSO) produces a once-a-decade report with similar types of fraud data, primarily reporting on companies that are implicated or indicted by the SEC. While the data from the COSO's most recent report is not as current as the ACFE, similar escalating numbers are consistent. For example, the 2010 COSO report reflected more than 50 additional fraudulent financial reporting cases and a fivefold dollar magnitude of financial losses from the previous reporting period. The cases involved in the COSO report included those of Enron and WorldCom. In addition, the report noted that fraudulent companies changed auditors nearly twice as frequently as companies without reported financial statement fraud during the reporting period (Beasley, Carcello, Hermanson, & Neal, 2010).

Adding to the culmination of statistical data, the SEC produces publicly viewable annual reports, capturing a section regarding the main objectives the agency has completed for the previous year. Included are the enforcement actions, primarily formal indictments, against companies, and individuals with various levels of occupational fraud, including insider trading, financial/accounting reporting and disclosure fraud matters, abuses of public finance violations

under the Foreign Corrupt Practices Act, and many others. These SEC reports produce valuable information about not only fraud incidences, but actions taken by governmental authorities and potential motivations for the fraud (White, 2014; White, 2015; White, 2016). When it comes to corporate-level, executive-led occupational fraud, there are several impacted parties, by the fraudulent actions themselves as well as the ripple effects of such a choice. This section discusses the foundational groups who stand to see the largest benefits from this research study, as well as the theoretical implications most likely to be impacted by the research results.

### **Investors and Other Interested Parties**

A review of the current fraud literature reveals a distinct group of interested parties outside those of merely passive news followers. The most pronounced grouping tends to be those in the investor community. In fact, Brazel et al. (2015) demonstrated that non professional investors take fraud and fraud red flags quite seriously in investment decisions. This group of novice investors tends to use a myriad of information, such as pending litigation, SEC investigations, management turnover, and risk of non compliance with bank debt covenants, as direct indicators of whether to apply additional scrutiny to investment choices. Yazid and Suryanto (2017) extended on this concept by connecting auditors' natural skepticism of management fraud potential to investor's confidence in a company's financial statements.

Outside of individual investors, institutional investors, such as large conglomerates of mutual fund owners, are also impacted by fraud. Wu, Johan, and Rui (2016) examined the ways in which institutional investors can impact fraud incidences in a company. Because these investors also bring with them political clout, the authors concluded that legal actions linked to fraud are reduced based on merely the presence of institutional investors.

Investors stand to gain or lose portions of their capital based upon the track records of a company, including their probability of committing a fraud in the future. Additionally, the returns they enjoy from company profits through appreciation of stock value or dividends connect directly to company profitability. Company profitability further connects to internal company costs, which is often dependent on past fraud, as those companies with historic fraudulent issues tend to see higher auditor and risk premium costs associated. Zhang, Gong, Xu, and Gong (2018) connected the premise of fraud to bond costs, the costs associated with gaining access to cash flow and liquidity for companies. In fact, the authors noted significant frauds tended to drive up bond costs, and profitability, to similarly high levels, and investors seek out and investigate fraud through use of accounting information and disclosures in financial statements.

Although investors have obvious vested interest in the driving out of fraud in organizations, they are not the lone group mindful of fraud prevention and detection. Regulatory agencies, in particular the Securities and Exchange Commission (SEC), also have a keen interest in what transpires within fraudulent companies. In fact, the process of financial restatement, which occurs when fraud or error has occurred to correct previously published financial statements, is of particular interest to external groups. Cianci, Clor-Proell, and Kaplan (2018) demonstrate investors' trust in company management is driven by previous reputation of management and by how management handles corrective actions and pre restatement communications. Because financial restatements often involve fraud, investors require such management action to discontinue their own personal fraud risk assessments.

The restatement process, considering management's responsibility for pure financial statement reporting, was clarified through actions in the Sarbanes Oxley (SOX) Act of 2002. By

extension, regulatory bodies, such as the SEC, connect to financial restatements through these legal statutes and by applying enforcement actions, if necessary. Chung and McCracken (2014) explained the typical interaction and communication process considering a financial restatement. Through crucial conversation and negotiation, the authors suggested historical financial restatements filter through a process of determining total breadth and scope of the restatement by considering things such as the nature, the party who discovered the issue, reaction from various entities involved in financial reporting and restatements, dissent on accounting topics as to the necessity of restatement, historic communication with the SEC and other regulatory watchdogs, the size of the company, the CFOs personality and internal factors, such as the strength and influence of the audit committee.

One of the SEC's tasks is to monitor and indict fraudulent acts at the federal level. In fact, according to the agency's report from 2016, the SEC filed a record number of actions, nearly 900, against companies and persons responsible for fraud. The result was more than \$4 billion in ordered penalties and claw back gains by wrongdoers with statutory work focused on abusive trading, cybersecurity, and financial statement fraud linked to the spreading of false information into the financial markets (White, 2016).

Regulatory and professional organizations who are tasked with detection, but also preventive fraud control measures exhibit another group of interested persons with respect to white collar fraud. First and foremost are the agents of the company itself, or executive leadership, who are accountable to proper financial reporting. As a result, research such as that by McMahon, Pence, Bressler and Bressler (2016) diligently examined new and innovative ways in which frauds take place, insomuch as preventive measures can be designed to counteract and beat fraudsters to the punch. Similarly, regulators with direct oversight and influence into laws

and statutes targeted at reduction of fraud have an ongoing interest in the impacts of previous regulation, such as SOX, as well as proposed regulation in the pipeline. Research such as that by Gupta, Sami, and Zhou (2018) helps regulators to determine the impact, or lack thereof, of ongoing financial controls regulation. In this circumstance, research suggests that SOX has been an effective measure in increasing the accurate distribution of information through disclosures, thereby enhancing the public interest in financial statement reporting. Fichtner, Rozycki, and Heaston (2015) offered a counter view in issuing a series of legal inquiries wherein the regulations of SOX are unclear or distorted. This level of question brings forth a conflicting stance on the effectiveness of SOX regulations regarding financial reporting and, therefore, brings into question whether fraud prevention has been enhanced. Lowe, Pope, and Samuels (2015) presented a similar perspective with respect to SOX' effectiveness relating to certification of financial statements as it connects to fraud. Regulators, through continuous use of fraud research, stand to gain insights and remain as interested external parties to fraud research in continued refinement of fraud topics and results of regulatory impacts on business financial results.

### **Auditor and Management Responsibility**

A century ago, internal controls were easier than they are today. The founder of Nathan's Famous, the popular hot dog stand, established a low-tech process of monitoring for fraud, with highest risks related to cash skimming, that is still in place (Levy, 2016). However, the types and variations of fraud in today's business world are more complex, encompassing, and bold than a century ago, thus auditors often find themselves in the middle. But what is an auditor's responsibility to detect fraud? Generally Accepted Auditing Standards (GAAS) Section 240 suggests that auditors have a professional responsibility to apply specific audit procedures to



determine if fraud is probable. This requires auditors to use professional judgment and maintain skepticism of management through inquiry and further evaluation about how management may be incited to commit fraud. However, because fraud is often collusive and management overrides internal controls, detection may be difficult (Georgiades, 2015). Furthermore, GAAS statutes are guidance only, not binding. As such, there are often stark differences between an auditor's opinion of their responsibility and public's opinion of an auditor's responsibility.

However, auditors and accountants are still based in the best position to discover fraudulent acts. Under the guidelines of professional auditing standards, auditors have many techniques to examine potential fraudulent issues. For example, auditors may choose to examine high risk items such as related party transactions, high turnover of key executives, historical issues with regulatory offices and large changes in sales and profits. Additionally, auditors should perform high level changes in financial balances, industry ratios and benchmarks, as well as variances between actual and budgeted results (Tschakert, Needles, & Hotzblatt, 2016).

With these issues in view, this study attempts to distill the complications that auditors seek to address in auditing for fraud. Specifically, the study aims to provide the audit community a new data point with reference to the fraud triangle by connecting CFO demographics with motivations. At a minimum, this information may provide auditors with logical and straightforward areas to look for potential fraud or alert them to red flags that may be present when fraud has taken place, given this research study's results.

## **Regulators**

Governmental regulatory agencies also stand to see significance from this research study. The Securities & Exchange Commission (SEC) has a stated mission to “protect investors, maintain fair, orderly and efficient markets, and facilitate capital formation” (White, 2016, p. 4)

as evidenced through the annual SEC report, outlining not only agency's financial performance, but several chapters of regulatory actions taken against those who have committed frauds and other illegal acts in the United States. Investigations and indictments are almost always discovered, investigated and charged post fraud event and frequently take years to resolve through the court system, as suggested in the annual reports (White, 2014; White, 2015; White, 2016). In addition, financial reporting regulatory bodies such as the US Financial Accounting Standards Board (FASB), IASB and Institute of Chartered Accountants are continuously refining accounting standards and practices around the world. However, because of a variety of factors, including U.S. Generally Accepted Accounting Principles (GAAP) conflicting with IFRS, the accounting industry is often providing conflicting and non-standardized guidance about application of accounting principles, thereby creating confusion and opportunity for fraudsters. As such, this research provides new information to regulatory agencies about fraud prevention insomuch as it adds new knowledge about demographics and motivation of fraudulent actions.

### **Research Question**

The research question for this study is stated as: for CFOs indicted of corporate fraud, what differences are seen in fraud motivations for CFOs with common fraud demographics (male, younger, lesser-educated) versus lesser common demographics (female, older, more highly educated, or any other combination)?

### **Definition of Terms**

**Age demographic.** Age demographic is represented by 1 = *Younger*, 2 = *Older*. Age is defined as younger when it is less than or equal to 46 years of age at the time of a fraud and older when it is greater than 46 years of age at the time of the fraud. This is defined as per Sun et al. (2017) as the median age for that study.

**Education level demographic.** Education level demographic is represented by 1 = *Less Educated*, 2 = *More Educated*. Education level is defined as less when CFO has a degree equal to or less than an undergraduate degree. Education level is defined as more when CFO has an advanced degree or certification. This is defined as per Sun et al. (2017).

**Financial statement fraud.** This term is defined as the overstating of assets, revenues and profits and understating of liabilities, expenses, and losses.

**Fraud motivation.** This term is defined as the intersection between fraud pressure/incentive and fraud rationalization.

**Fraud pressure.** This term is defined as a non shareable financial problem (Cressey, 1953).

**Fraud opportunity.** This term is defined as the factors allowing individuals to commit a fraud (Cressey, 1953).

**Fraud rationalization.** This term is defined as an aspect of removing the fraudster from reality and justifying the action (Cressey, 1953).

**Fraud triangle.** This term, also known as fraud theory, is defined as the intersection of fraud motivation, pressure, and opportunity (Cressey, 1953).

**Gender demographic.** This term is represented by 1 = *Male*, 2 = *Female*.

**Indicted fraud.** This term is defined as fraud for which legal action has taken place by the Securities and Exchange Commission (SEC) or Department of Justice (DOJ).

**Occupational fraud.** This term is defined as the use of one's occupation for personal enrichment (Dorris, 2018).

## Research Design

The research methodology chosen for this study is that of qualitative case study based on use of historical records. Because the nature of fraud is inherently sensitive, qualitative case study based on use of publicly available secondary data only allows the researcher to gather information without the need to interact directly with the fraud target in the cases studied. Using the demographics of age, gender, and education levels, in alignment with past research (Aier et al., 2005; Barua et al., 2010; Liu et al., 2016; Qi et al., 2018; Sun et al. 2017; Troy et al., 2011;), companies with indicted fraud were identified through use of SEC databases with fraud cases where CFOs are named catalogued. After identifying the cases, demographical data about CFOs was catalogued using public search records, such as LinkedIn or Bloomberg and other such public domains. A sample of 11 cases was chosen from the fraud cases to complete additional research.

The research approach included a search of public records to determine the perceived motivations for the CFO's fraudulent actions. This search for motivation was captured through public court records and media coverage of the fraud, either during or after the court indictment and conclusion. This data was gathered based upon the Freedom of Information Act (FOIA) in accordance with federal and state jurisdictions, including the use of Public Access to Court Electronic Records (PACER), which is accessible via request. Upon completion of this research step, information regarding motivation was categorized into broad groups to capture motivational components.

Data analysis was completed by use of a keyword search pattern to arrive at general motivational themes. Triangulation was used to arrive at common themes that are communicated

across and within various sources. The corresponding themes were connected to demographic data to arrive at similarities and differences across common and uncommon groups.

### **Assumptions and Limitations**

#### **Assumptions**

Upon examination of the methodological assumptions, specifically ontology, the outcomes of this study presuppose there is only one foundational fraud motivation for the occurrence of fraud under study, unless the CFO indicted states more than one motivation. As stated, the motivational aspects of fraud can be vast and sometimes unexplained. Reliance on court records and media sources may not consider other ontological reasons that the CFO chose to commit fraud, as well as the truthful underlying motivations of doing so. The research is bound by what is revealed through court hearings and other sources as the main reason(s) for the fraud motivation.

The epistemological methodology assumes that CFO motivations can be determined through secondary sources of data and connected to common and uncommon demographics. It further assumes that motivations can be understood through the secondary sources available and, through proper data analysis, research conclusions will adequately address true fraud motivations of CFOs. These motivations are assumed to be triangulated through appropriate data analysis.

The axiological methodology assumes an understanding of values within the research findings that, in turn, help to improve understanding of fraud theory. Because axiology speaks directly to ethics, and the dynamics of ethics commonly weave into and out of fraudulent actions (Donegan et al., 2017), axiology is assumed to be a key aspect of this research study. Ethics as an applicable variable relating to occupational fraud is discussed further in the following chapter.

The researcher further assumes that fraud theory, specifically motivation, can be used to understand and model any fraud case through an examination of pressure and rationalization. While it is not necessary that opportunity is present in the fraudulent act, motivation is a pillar of this research study, and as such, is critical for research conclusions. The researcher goes into the research study acknowledging the various critics of the fraud triangle but presupposes motivation will be present in every situation.

Finally, the research methodology operates under the assumption that court records are, when available, complete and without errors. This suggests that court records are presented in full and with complete records provided by the third-party source. It also assumes no portions of the court case are expunged or otherwise stricken from public records.

### **Limitations**

The way in which this research is designed may create limitations in research results. Specifically, one potential limitation involves the way in which data is gathered. Because the CFO prosecuted for fraud is not questioned directly by the researcher, the CFO is not given an opportunity to give a response to fraud motivations, except through court or other sources. As such, this creates limitation in the opportunity for the researcher to further clarify points of interest and forces the researcher to make inferences based on court records and testimony, which is inherently completed to cast the prosecuted person in the worst possible light. Furthermore, the fraud motivations discovered through testimony may mask the true motivations, or may be incomplete in nature, as discussed in the assumptions section. This may limit the researcher's ability to document actual motivations of the CFO fraudulent act, given the researcher may only use the data presented through a third party, and must rely on it for accuracy.

Finally, cases under study must meet certain minimum thresholds to be used in this study. For example, fraud must be discovered in all circumstances for which to be prosecuted. The discovered case must then be large enough for the government to prosecute. If the government does prosecute, the case must go trial to gather motivational evidence, with any cases settled pre trial not included in this study's sample. Furthermore, evidence presented by the SEC through court filings may cast the accused in a negative light to encourage settlement, thereby hinting at inaccurate fraud motivations. In sum, these factors may create a biased sample.

### **Delimitations**

As stated briefly above, this research study will limit its scope of fraudulent scenarios in several ways. First, only fraud cases brought forward by the SEC or DOJ are within the purview of this study. Cases for which the fraud target was managed more locally or situations where there were no charges brought against the fraud target are not investigated. Furthermore, even if the case was originally indicted by the SEC/DOJ, only cases that went substantially through the process or to trial are included in the case study sample. Cases wherein the CFO settled immediately or over time are not investigated, unless the court process proceeded sufficiently wherein motivational components may have been documented through court records. By virtue of the above, only frauds within the United States border are within scope of this study; companies operating outside the jurisdiction of the SEC/DOJ are not investigated. If a fraud case involved parties other than the CFO, they are not investigated in this study. CEOs, boards of directors, and other internal parties to a fraudulent company are not investigated.

### **Organization of the Remainder of the Study**

Chapter 1 of this document discussed the background and introduction of the research topic, need, purpose and significance of study, research design and assumptions and limitations.

Chapter 2 provides a complete literature review of the topic associated with the research topic. Chapter 3 details the methodology of the research study, including the research question, design, population, sample, procedures, instruments, and ethical considerations. Chapter 4 reveals the findings of the research study, and Chapter 5 discusses the implications and recommendations moving forward, including the summary and discussion of results, conclusions, limitations, and recommendations for further research.



## CHAPTER 2. LITERATURE REVIEW

### Methods of Searching

To identify information on executive-level fraud, the fraud triangle, fraud theory, and occupational fraud, a search strategy was implemented based on reviews in ProQuest, PsychInfo, EBSCO, and Google Scholar. The specific catalogs were scanned for applicable resources using a combination of keywords, as follows: *fraud or financial statement fraud or occupational fraud, fraud triangle or fraud theory, CFO or chief financial officer or CEO or chief financial officer, and fraud*. Results were examined through abstract review to determine applicability to the research topic. These combinations of keywords, particularly when linked in the title or abstract, created a strong lineage to the research topic, providing a rich intersection of fraud, auditing, ethics, theory, and relevant fraud history.

### Theoretical Orientation for the Study

While the topic of fraud can be traced back for many centuries, it was not until the 1950s that Donald Cressey, a criminologist, developed the fraud triangle (Cressey, 1953). Cressey's methodology was straight forward: for a fraud to occur, three things must exist. First, the perpetrator of fraud needed some sort of internal or external pressure, one that was considered non sharable to other people. Typically, this pressure is financial in nature and consists either of motive or incentive. Second, an opportunity must have been present, commonly triggered by a control breach or the perception that detection of the fraud is unlikely. Finally, the fraudster must have been able to rationalize the fraud choice in some fashion. Rationalization tended to further link to the ethical stance of a person and their choices in life (Rodgers, Soderbom, & Guiral, 2015). Cressey's theory was referred to as fraud triangle theory or simply fraud theory when it was hypothesized.

Since that time, and most notably after the series of high-profile frauds in the early 2000s, fraud theory has been analyzed and challenged in the context of many business angles. Specifically, and most profoundly, the shape of the fraud triangle has been brought to question. For example, a fourth component, capability, was proposed in 2004, which emphasized the point that, for a fraud to occur, a perpetrator must have the skill and ability to commit a fraudulent act (Azam, 2018). Around the same time, occupational fraud was explained using the 3-C model (conditions, corporate structure, and choice) to lend a more business-driven methodology to fraud actions (Lokanan, 2018). Dorminey et al. (2012) suggested a new fraud theory meta-model described as MICE (money, ideology, coercion, and ego). MICE was an attempt at expounding upon the pillar of pressure, while taking time to also address the element of collusive fraud, or fraud that takes place among more than one person in a partnership.

Others have suggested that a person's ethics and integrity should be contemplated with respect to how the fraud triangle is analyzed. Most notably, research has proposed that personal integrity replace the pillar of rationalization inasmuch as fraud can be described through an interplay described as a fraud scale (Raval, 2018). Still others have suggested that there is no shape application whatsoever. In fact, the number of dimensions is limitless, and, as such, researchers should cease in boxing fraud theory into a defined set of variables (Huber, 2016).

In addition to the shape, geometry and debate of fraud variables, many other researchers have taken the fraud triangle (or other shape) and attempted to overlay it with tangential theory to explain white collar fraud. This research has set into motion dozens of new models and hybrids of sub-models, some of which are still connected to the fraud triangle at some level, while others have spun off in creating completely new meta-models with variations of the

historic fraud triangle somehow embedded. This research has spanned into criminology, behavioral/social science, ethics, agency theory, and several other areas.

For example, Mui and Mailley (2015) connected the fraud triangle directly to the crime triangle, in linking together how pressure, opportunity, and rationalization attach to the actual criminal act. Similarly, Lokanan (2018) connected the fraud triangle to differential association theory, which connects to how people learn and move forward in committing a crime. Owen Brown, Hays, and Stuebs (2016) pivoted slightly into planned behavior theory, connecting fraudulent acts to whistleblowing and fraud theory. Similarly, Raval (2018) connected elements of disposition based fraud modeling to the fraud theory to explain why fraud may *not* occur in a situation where the fraud triangle elements appear present. The study focused on the behavioral and psychological elements of human behavior considering Cressey's work (Cressey, 1953).

While fraud triangle theory continues to shape, reshape, and connect with other human and company theories, fraud continues to happen globally in hundreds of circumstances (ACFE, 2018). While the SEC examines, investigates, and indicts fraudulent acts (White, 2014; White, 2015; White, 2016), news media sources continue to report new frauds and scams as fast as governmental agencies can respond. More often than not, C-suite employees are implicated, including the CFO. In post mortem analysis, CFO decision-making steps and personal traits are frequently studied. A myriad of research tends to address CFO demographics (Aier et al., 2005; Barua et al., 2010; Liu et al., 2016; Qi et al., 2018; Sun et al., 2017; Troy et al., 2011;) in many aspects, including gender, age, and education level, while connecting to variables such as earnings management (legal or illegal manipulation of revenues), accruals quality, professional style, financial restatements, and outright, indicted and sentenced fraud. Post analysis can also be inclusive of personal reflection in which the CFO expounds on the reasons for and situations

leading up to the decision to commit a crime. Suh, Sweeney, Linke and Wall (2018) described interactions with indicted CFOs in contextualizing the progression, albeit generally slowly, to the acceptance of small bits of fraud that escalated and increased over time to that of a substantial event, including the fraud circumstances both personal and tied to social, corporate factors.

Despite the breadth of published literature on fraud theory in the 2000s and new research challenging of Cressey's original work, this research study largely grounds itself in the original fraud triangle theory, while taking into consideration discussions in literature regarding forward-looking changes. Specifically, this research study is grounded on the three pillars of fraud theory (pressure, opportunity, and rationalization) while collapsing two of the pillars, pressure, and rationalization, into that of motivation. Furthermore, this view of fraud theory is combined with chief financial officer's demographics in examining fraud motivation. The theoretical orientation connects to and aids the research community in the continuing effort to grow and mature fraud theory in concert with active research, described above.

### **Review of the Literature**

The research topic for this dissertation seeks to understand the similarities and differences between the fraud motivations of two distinct groups of people: CFOs in the common and uncommon demographic groups. Common demographic groups include CFOs who are younger, male and lesser educated (Aier et al., 2005; Barua et al., 2010; Liu et al., 2016; Qi et al., 2018; Sun et al., 2017; Troy et al., 2011), while uncommon demographic groups are those with any set of demographics outside of the common group. The section to follow demonstrates a full literature review on the research topic, while organizing existing research about CFO fraud, fraud theory, fraud motivation, and other tangential topics crucial to this study.

The review of literature is organized as follows. To start, the topic of executive level fraud motivation and demographics are discussed. Because fraud motivation and fraudster demographics are the two primary foundations for this research study, the literature review starts with these topics as they relate to existing research. Following motivation and demographics, fraud theory is discussed at length. Given this study's intention to inform fraud theory of new information, and given motivation is a combination of two legs of the existing fraud triangle (pressure and rationalization), fraud theory is addressed early in the literature review section. From there, a background on fraud is explained, beginning with early fraud, and bringing us to current state.

The background section is intended to inform the reader of the gravity of the fraud issue, historically, but also to suggest that fraud has not decreased over time. To provide support to the gravity of occupational fraud, in the past and today, two additional sections discussing how fraud interacts directly with various industries are discussed. The literature review also includes sections on the beneficiaries and impacted groups of fraud. The review then turns to two sections regarding auditor responsibility and internal controls/compliance as it connects to fraud and fraud theory. Of all the interested parties, those in auditing and compliance stand to see the greatest potential practical significance from this research study, as information informing fraud theory may also impact the ways in which auditors and compliance officers adjust for preventive and detective fraud measures in business practice. Ethics, as it addresses fraud and fraudulent behavior is addressed next. Ethics, as discussed in Chapter 1, is often linked to and tries to explain fraudulent actions. Because of this convergence, ethics and fraud are connected briefly in this literature review. The nature of the entire literature review is intended to start with the building blocks of this study (fraud motivation and demographics), add fraud theory, then build a

broad understanding of fraud, concluding with parties who stand to gain theoretical and practice significance from the study while addressing other relevant tangential matters.

### **CFO/C-Suite Motivation and Demographics**

Occupational fraud can take place at any level of an organization, but the executive suite is often front and center in the misdeed. Literature speaks to CEO, CFO, management team, and even the audit committee exercising influence on fraudulent financial reporting decisions. In fact, Lawson and Omer (2012) noted traits of CFOs, CEOs, and audit committee chairs who exhibit authority over a firm's reporting and operational choices from the standpoint of earnings management, or the smoothing of revenues to meet analyst expectations, with accruals seeing an impact. When examining CEOs and CFOs with respect to a fraudulent act, Suh et al. (2018) interviewed executives, who knowingly participated in illegal acts, noting a slow progression toward the fraud. In these situations, the motivation to commit the fraud was not exclusively or entirely financial. Rather, a complex set of societal circumstances presented themselves, marking an incremental progression toward the crime. Time and again, the executives realized the gravity of the circumstance only after the fact, but not when the fraud was progressing. To that end, motivation of C-Suite level fraud is often small and incremental in nature, not always immediate and dramatic.

A subset of the executive suite, the chief financial officer (CFO), is one party of particularly high interest in fraud literature. Likely because of their financial influence, CFOs have been studied closely with respect to occupational fraud. Perhaps this is because once a CFO commits to, and is motivated to, perpetuate a fraud, it is nearly impossible to stop and, in some cases, detect the fraud has occurred (Dinoff, 2015). CFOs, like most other executives, maintain a high level of personal responsibility for the outcomes of a company. Although some fraudulent

CFOs may avoid prosecution and jail time, some do face personal financial ramifications through lawsuits from outside parties (Andrews, 2017; Pileggi, 2016). New claw back provisions, thanks to Sarbanes Oxley provisions, have also ratcheted up incentives for CFOs to ensure proper financial statement reporting. The SEC has the authority to create controls using a comment letter, which publicly forces CFOs to publicly respond to questionable financial reporting or disclosure matters. Comment letters can and often do lead to restatements, which, in turn, can lead to a CFO resignation (Gietzmann, Marra, & Pettinicchio, 2016). And according to Kroos, Schabus, and Verbeeten (2018), CFOs are motivated to properly report financial statements based upon research results. That being the case, the study of CFOs continues to be central to occupational fraud research with a wide variety of motivations in wrongdoing (White, 2014; White, 2015; White, 2016).

From the standpoint of occupational fraud, CFOs have been and still are motivated by external factors such as pressure from the CEO, internal control issues and abnormal accruals (Kroos et al., 2018). Gillett and Uddin (2005) extended this idea, noting that compensation is generally not a good measure of a CFO's intention to commit a fraud through financial reporting. In fact, the decision is much more complex than merely compensation and includes influences from work and non work contacts, as well as size of the company and attitudes about one's self related to beliefs and achievement. This suggests that CFO motivations cannot be easily standardized and neatly organized into a couple of simple categories.

Despite a wide variety of fraud motivations, research attempts to stratify and help frame the demographic components of CEOs, CFOs, and Boards, often aligning to a variety of studied demographics. For example, Han, Zhang, and Han (2015) noted that CEOs and CFOs who have similar educational backgrounds and tenures with the company tend to have more sound

alignment and as such, a positive impact on the firm's financial reporting results. This typically translates into more positive and accurate financial outcomes for a company. Further, this suggests a small incidence of occupational fraud.

Conversely, Troy et al. (2011) examined the type of CEO who is most likely to rationalize a fraudulent act upon the company. Specifically, the authors used upper echelon theory, which connect upper level leadership, including the CEO and CFO, to company decisions, concluding that CEOs who are younger, with less experience and without a business degree are the most likely to rationalize a fraudulent act (Troy et al., 2011). Qi et al. (2018), similarly using upper echelon theory, examined the propensity for CEOs and CFOs to engage in earnings management, a legal but often pre fraud exercise of meddling with earnings numbers. Younger males with higher levels of education were most likely to engage in risky practices according their results.

Examining the CFO singly, Ge et al. (2011) looked at CFO *style*, which was a combination of characteristics and demographics. Characteristics reviewed included risk attitudes and overconfidence, while comparing them against gender, age, and educational levels. Their results suggested that CFOs have a tremendous influence over the accounting practices of their firms, with styles resonating by factors such as job demands, age, gender, and educational background. Furthermore, characteristics, combined with demographics influenced accounting practices and, therefore, financial reporting of firms.

Sun et al. (2017), in a paper pivotal to this research study, examined the demographics of CFOs in situations of known historic fraud within companies in China. Their results suggested CFOs were most likely to commit fraud when they were younger males with less educational background. Similarly, Liu et al. (2016) examined earnings management in Chinese CFOs,



noting males tended to be more aggressive in their application of accounting principles than their female counterparts, highlighting a slippery slope in financial reporting. Earnings quality, another variation of accounting application, was studied by Barua et al. (2010) with a similar outcome of male CFOs exhibiting more aggressive accounting application. Restatements, previously described as a potential fraud within an organization, was studied by Aier et al. (2005) to arrive at common CFO traits. This research concluded that less expertise, specifically those CFOs with less education, were more likely to be involved in the restatement process and outcomes. Finally, in direct alignment with the Aier et al. (2005) study, Xu and Zhao (2016) noted that, following a restatement, a company is most likely to hire a CFO with more financial experience, experience and qualification than the previous outgoing CFO. By extension, this suggests that a company understands that CFO's with less experience present a greater risk of occupational fraud to their organization. Summarized to a singular point, the above research combined to conclude that CFO demographics of fraudulent and activities signaling fraud is more likely to occur aligned with the demographics noted as common in this research study: younger, less educated male CFOs.

Historic literature is rich with information about past frauds, particularly at the C-Suite level. This research study begins to hone in more specifically on the research related to CFOs and the demographics that accompany them while carefully weaving in the motivational factors, through examination of pressure and rationalization, related to the fraud itself. As such, there is a purposeful narrowing down to CFO demographics and the underlying research that describes past CFO fraud.

## **Fraud Theory**

Within the context of a full literature review of fraud theory, it is apparent that there exist many varying conclusions. Research, particularly more recent literature, presents a wide variety of fraud theory shapes (triangle, diamond), sub-models, and meta-models with variations of tangential secondary theories connected directly or loosely to fraud theory. This section is intended to demonstrate the wide variety in schools of thought around fraud theory to demonstrate how cloudy the theory has become. The conclusion, then, discusses which components of fraud theory are used in this research study.

While the theoretical orientation is stated earlier in this chapter, it is worth more in-depth discussion as it relates to the fraud triangle and fraud theory in general. Like a patient with a rare disease, fraud theory has been tested, poked, and prodded with different theories presented over the years. Time after time, especially in the past two decades, researchers have pleaded for additional focus on things such as fraudster rationalization, collusion, and its impacts and the ramifications of whistleblowing regulation (Free, 2015). Researchers commonly make attempts to debunk the existing shape of fraud theory, looking for new geometries or ways to explain the existing shapes, such as Schuchter and Levi's (2013) fraudulent inner voice, which quiets as time progresses, allowing a fraud to get worse and creating a capability element to the newly shaped fraud diamond. This quiet period not only adds a level of complexity about fraud motivation, but turns the fraud triangle into a diamond, thereby casting doubt on the fraud theory itself.

Furthermore, fraud theory tends to remain largely quiet and centered for a short period of time until another corporate fraud erupts, again disrupting the theory post mortem. This is true of real frauds such as Wells Fargo, which reemphasized the importance of internal culture and pressures that cultures can elicit (Albrecht, Albrecht, Sanford, & Rocha, 2017) and through a

comparative analysis of Enron, WorldCom, and HealthSouth, which examined six areas of ethical culture within the companies (Soltani, 2014). When looking deeper at corporate fraud, authors tend to spend time on corporate recruitment efforts in situations where collusion was required, noting common approaches of intimidation and pressure to gain compliance (Albrecht et al., 2015).

On a different peripheral, Murphy and Free (2016) examined the intersection of corporate culture and fraud theory, with key themes emerging. First, a particular climate is often present wherein employees seek to make the company happy, connecting to ethical climate theory. This ethical climate theory further connects to fraud motivation, creating more of a social rationale for committing a fraudulent act. This connection between social theory and today's fraud theory, according to authors, is largely absent (Murphy & Free, 2016). A similar school of thought is expanded by Schuchter and Levi (2013) who examined the slow progression of fraud through company channels while ignoring the internal voice knowing the fraud was morally incorrect. Culture was a large influencer in silencing the internal voice opposed to the fraudulent act. Finally, Rodgers et al. (2015) connected elements of corporate social responsibility to that of the fraud triangle, helping to delineate how individuals act and make decisions based upon corporate tone at the top, further connecting the fraud triangle, primarily within the rationalization leg. These corporate societal aspects of research represent one branch of research connecting to fraud theory that continues to evolve.

Going one step further, researchers also connect fraud theory to several other tangential theories, such as those related to crimes in society. For example, Machado and Gartner (2018) blended agency theory, criminology, and economics to test the fraud triangle, noting solid connection points. Similarly, authors have connected the concepts of criminology and social

behavior to that of fraudulent acts and fraud theory. For example, Lokanan (2018) suggested that there exists within an organization a subculture, one that can be manipulated and convinced to create a criminal act, fraud in this case. In this model, rationalization is assumed to be weighted lighter than opportunity and pressure, while eventual fraudsters are taught and encouraged to go along with fraud. Mui and Mailley (2015) postulated a similar model, wherein the fraud triangle connects most appropriately to the micro situation, or the individual, whereas the crime triangle (pillars required for a crime to take place) connects best with the macro view, or the environmental components. The combination of these two triangles into one model overlaid the crime with the traditional fraud triangle viewpoint.

Additional human elements research has attempted to reshape the fraud triangle in some respects also. This is true with Raval's (2018) work connecting the fraud triangle to the disposition-based fraud model (DFM), which included the human elements of self-control, moral temptation, and judgment. Trompeter, Carpenter, Jones, and Riley (2014) examined a myriad of social aspects to the fraud triangle, noting the pillar of opportunity can be enhanced, particularly through positions of authority, because of access rights, enhanced social networks and understanding of technical elements of fraud. For this reason, proactive management of fraud, such as whistleblowing, is crucial to understand well in advance of the potential of a fraudulent event because having an action plan can noticeably impact the amount of whistleblowing, and therefore fraud avoidance, can be realized (Owen Brown et al., 2016).

Interestingly, in some cases, authors have been able to eliminate portions of the fraud triangle simply based upon personality traits of the fraudster. Epstein and Ramamoorti (2016) argued that certain people, based simply on how they are wired, exhibit traits of a *dark triad*, or narcissism, Machiavellianism, and psychopathy. Given these inherent traits, two legs of the fraud

triangle, namely pressure and rationalization, are not even required. As such, we are left with only one leg, opportunity, in scenarios where these personality traits are present.

Finally, literature is heavily influenced by fraud theory with weight given to one leg: pressure (one element of motivation). While typically not aligned neatly within literature, motivation, particularly that of the CFO, tend to align into two groups. The first group is external pressures that motivate a CFO to take fraudulent actions. Bishop et al. (2017b) spoke to the ways in which CEOs can influence CFOs to participate in a fraud through pressured actions. Inversely, the preventive controls established, specifically those around compliance programs, are generally not great enough to offset pressures from the CEO. And interestingly, once CFOs do commit a fraud, they tend to take accountability for the action rather than place blame on the CEO. Similarly, Bishop et al. (2017b) reviewed actual fraud cases in studying the CFOs formal pressure to cross the line. Pressure from the CEO was listed as the top reason, along with external pressures from the market to hit earnings expectations, pressure to keep stock price high and pressure to keep their jobs.

Internal pressures are frequently the other type of feeling that CFOs manifest to commit a fraud. In this sense, internal motivation tends to align pretty tightly to financial incentives, although there may be other elements at play. Radin (2017) spoke of one CFO who had several motivations, including debt, a failed career and marriage. This eventually led to embezzlement. It is quite common for research to focus on bonuses and other forms of compensation considering fraud motivation such as a specific swatch of fraudulent companies in China (Hass, Tarsalewska, & Zhan, 2016) connecting compensation to fraud motivation. Increases in fraud motivation is also seen through corporate goal setting, wherein employees are rated and compensated against company results, raising pressure and rationalization, and thus motivation, to a fraudulently

bump up the numbers (Donegan et al., 2017). Furthermore, auditors of financial statements have notably factored risk into their pricing for audits when they perceive fraud risk to be greater for CFOs based upon their compensation structure (Billings, Xinghua, & Yonghong, 2014; Kannan, Skantz, & Higgs, 2014).

Adding yet another layer of complexity are the accounting standards that, over time, may remain inconsistent and in the favor of the fraud perpetrator, thus creating a higher level of opportunity for fraud. Wustemann and Wustemann (2010) explained the complexity in a shift from rules-based to principles-based accounting standards. This slide toward principles-based accounting means that company management may apply more judgment to accounting transactions than they had the latitude to do in the past. As such, managers may choose to apply rules most favorable to them in each circumstance, thereby opening the door to higher incidences of fraud. Because of this, authors call for a convergence of accounting standards, particularly given the complexity of business in today's world. Complicating fraud opportunity a bit further yet is the concept of creative accounting practices exercised by many companies today. While not illegal, creative accounting may create financial reporting that is not fair and true of a business and can send a company and its executives down a slippery slope with fraud often resulting at the end. Loopholes in accounting allow creative financial transactions to form, then sometimes fraud to begin, eventually getting a little worse before a large scale fraud has transpired little by little. Most accountants agree that creative accounting is used to gain an unfair advantage that should be considered a serious crime (Lal Bhasin, 2017).

While the above variations related to fraud theory inform this research study, Cressey's traditional and historical components of fraud theory are used as the basis for understanding, inclusive of pressure, opportunity, and rationalization. However, in construction and

determination of the CFOs motivation for a fraudulent act, the pillars of pressure and rationalization are combined to arrive at the CFOs motivation for committing the act in question. Other tangential issues discussed above are used as reference points when reviewing actual CFO fraud scenarios.

## **Background on Fraud**

Having examined the micro topics of CFO motivation, CFO demographics and fraud theory, this section is intended to reorient back to fraud on a grander level by providing information on its severity and frequency along with some of the more common frauds seen in business. Once complete, the literature review will return to more specific elements of importance regarding the research interest. To some parties, the topic of fraud can be elusive and misunderstood, as often only high-profile fraud cases are reported through media channels. However, under the guise of the most basic types of frauds, there are a few consistently seen in business that are well below the level of the large-scale, multi-million-dollar frauds seen on television. For example, employee embezzlement, which is simply money or property stolen from an employer, is common and often kept hidden from public view when discovered (Galletta, 2015). Other schemes such as pump-and-dump, defined as fraudulently filling the sales channel at the end of a reporting period, vendor fraud, often triggered when an employee and vendor collude to commit a fraud, and consumer fraud, which, nowadays, is typically linked to personal credit cards are prominent (Galletta, 2015).

Undoubtedly, based on nothing more than the statistics presented thus far, fraud is a complex topic. While theoretical implications of fraud were addressed earlier, some of the complexity about fraud tends to align with the multitude of options available to a fraudster (Galletta, 2015) but also the ways in which independent fraud can differ from collusive fraud.

Van Akkeren and Buckby (2017) spoke to the differences between solo and collusive fraud situations within an organization and how the situations of fraud differ based upon behaviors, environments, and other social aspects of the fraud situation. Contextually, frauds at individual versus group levels differ dramatically in the ways for which people may interact with one another, particularly if group fraud requires recruitment and coercion to be successful.

Furthermore, the ways in which people choose to interact or progress individually can connect and impact the ways in which compliance and monitoring functions are established (Van Akkeren & Buckby, 2017). When contemplating collusive frauds within organizations, differences in demographics can sometimes emerge, which may be consistent or counter to other research. For example, Bishop, Hermanson and Riley (2017) studied the differences in solo versus collusive fraud from the standpoint of the incident and company impacted, noting those establishing themselves as the leader in a collusive fraud as younger, male with a wheeler dealer attitude and strong ties to external vendor relationships. This gently conflicts the ACFE data (Dorris, 2018) which tends to suggest those with greater than five years of experience, thus a bit older, are responsible for damaging fraud.

Finally, it is worth noting that no particular industry, sector, culture, or geographic is insulated from the potential impacts of fraud. For example, while the ACFE report (Dorris, 2018) noted the Asia-Pacific region as the geographic with the largest dollar loss per fraud, Dessalegn (2014) noted stark fraud implications based on cultural elements. This concept was also true when examining fraud and the business cycle within a single country, Nigeria, noting that economic conditions impacted fraud limitedly with respect to fraud frequency (Isola, Olufadesola, Olabode, & Adeniyi, 2017).



Fleming, Riley, Hermanson, and Kranacher (2016) examined fraudulent financial reporting in public versus private companies, Harris, Petrovits and Yetman (2017) covered not-for-profit fraud while Dean, Vazquez-Gonzales and Fricker (2013) addressed specific healthcare fraud concerns. Even the typically viewed do good industry of sustainability is not free of fraud risk, as Steinmeier (2016) professed. While industry-specific fraud is addressed more precisely in the next section, it is important to highlight that research suggests fraud has no boundaries. In sum, and like fraud theory itself, the research community is left with a gnarled mess of fraud scenarios around the globe with preponderance for it to engage nearly anywhere, anytime and at any level of severity. The sections to follow aid in pulling together the fragmented components of fraud, while connecting to the chief financial officer and fraud theory, discussed above.

### **Fraud Across Industries**

The investor and fraud fighting communities are continuously scanning the environment for potential fraud risks and clues that fraud may be taking place. Research is rich with specific slices of review signaling trouble within a company. For example, Gao, Kim, Tsang and Wu (2017) examined staff turnover circumstances present within organizations at intervals before the fraud, during the fraud but before fraud discovery and after fraud discovery but prior to formal legal action.

Further research reviews are riper in fraud prevention. Harjoto (2017) examined a variety of corporate cultures through formal corporate social responsibility (CSR) programs, connecting formal CSR policies to the outcomes of fraud. Results suggested lower incidences of fraud and lower fraud severity, when it takes places, under CSR-led organizations. Abid and Ahmed (2014) suggested a variety of warning signs historically attributable to a company including executive collusion, executive level greed, upper leadership excess ambition, poor internal controls, and a

corporate culture of aggressive and fast-paced growth that is unachievable. Donelson, Ege, and McInnis (2017) extended this school of thought by connecting company internal controls with fraud presence and communication. These concepts further connect back to fraud motivation.

Research suggests that fraud provides no conclusive identity to any one or even a set of industries, wherein other industries are free of fraudulent actions. The 2018 ACFE fraud report listed a total of 23 industries that fell victim to fraud, and while the number of reported cases was varied by industry, the types of fraud most prevalent by industry were widely varied. For example, while corruption was frequently the fraud circumstance for government entities, religious organizations most often fell prey to billing schemes. And while for-profit organizations made up approximately 7 of 10 fraud cases, not-for-profits could not be eliminated as a possibility (Dorris, 2018).

A segment of business that is particularly prone to fraud is small businesses. Along with a smaller workforce to conduct routine types of fraud checks more prevalent in larger organizations, such as internal audit teams, small businesses tend to be closer knit and most trusting nature (Kramer, 2015). Furthermore, fraud research suggests the 10/10/80 rule to fraud, wherein 10% of employees will steal despite controls, 10% of employees will never steal and 80% will steal situationally. Small business frauds, while less severe than large company frauds, may be underreported because of concealment and reporting issues. And while small businesses tend to suffer different types of fraud, including invoice billing scams, check tampering and cash skimming, controls recommendations are often similar, such as employee surveillance and verification of business transactions. However, trust tends to be greater in small companies, often compounding the fraud problem (Kramer, 2015).

Another debate in literature examines financial reporting fraud in the public versus private sector. Fleming et al. (2016) studied the differences in fraud between these two sectors given historical preference to public entities, with particular risk assessed to private companies in historical fraud reporting. Research results suggested that public companies tended to have larger audit functions, varied fraud methods to avoid detection and frauds were more often detected through formal means, such as an audit. Private companies, with fewer controls, perpetuated more basic types of fraud, but were more likely to be discovered out of luck rather than a formal control or audit process (Fleming et al, 2016). While helpful, it should be noted that the researchers reported fraud in both industries and did not single out one over the other.

Perhaps one of the most at risk organizations subject to fraudulent actions is not-for-profit organizations. Additionally, reported frauds for not-for-profits may very well be understated, given a charity's interest in handling fraud cases quietly, so as not to disrupt any future charitable contributions with bad publicity (Harris et al., 2017). However, recent Internal Revenue Service (IRS) statutes require charitable organizations to disclose significant instances of internal asset diversion, forcing even not-for-profits to ratchet up fraud controls accordingly. Like other industries and organizations, oversight and in-house governance, including board monitoring, independence, internal tone and general oversight have been strong deterrents of fraud (Harris et al., 2017). Furthermore, De Armond and Zack (2017) noted that structuring controls to prevent fraud in not-for-profits includes a system to deal with the human element of fraud, while recommending taking an internal (training of staff) and external (finding organizational advocates of fraud prevention) in thinking like a criminal. The authors noted, however, that resource constraints often hold not-for-profits hostage to proper fraud controls.

The above discussion highlights a key point in fraud: all industries, structures and sizes of business are subject to and at risk for occupational fraud. The frequency and pervasiveness of the fraud environment gives relevance to this study's goal in understanding fraud motivation, while connecting it to key players within the company's infrastructure. In this study, the main key player is inclusive of the role of chief financial officer.

### **Compliance/Internal Controls**

Business is complex with many internal and external parties involved in its success. In situations where a company must restate its financial statement publicly, there is an interplay that develops between many groups, including the CFO, board, audit committee, audit partner, and regulators. This process can be long, complex, burdensome, distracting, and costly to companies, as well as influenced in many ways (Chung & McCracken, 2014). However, before a company gets to the point of an occupational fraud or financial restatement, they will generally employ a layering of internal controls and governance procedures to prevent such an event or detect that it has occurred. Absence of such controls and governance leaves a company completely exposed to the whims of management often with significant consequences (Ilter, 2014).

To aid in the development of governance structures, conglomerates such as the Committee of Sponsoring Organizations of the Treadway Commission (COSO) have published guidance encouraging organizations to design fraud risk policies, perform risk assessments, design preventive and detective controls, conduct investigations and monitor on an ongoing basis for fraud. In addition, COSO recommends that companies take swift action in response to detected fraudulent actions in creation of an information and communication system (Cotton, Johnigan, & Givarz, 2016). Often, companies begin with a form of corporate governance structure to influence management, establish accountability measures and increase the quality of

financial reporting (Waweru & Riro, 2013). However, the actual impact of governance structures was somewhat unknown. Formalized corporate governance in the form of board composition was demonstrated to be most influential in proper earnings management for the companies under study (Waweru & Riro, 2013). Further studies have shown similar results, such as that by Thanh Ngoc Bui and Amaria (2014). This studied suggested a strong association between corporate board structure and fraud outcomes, particularly when the CEO was not board chair and the audit committee functioned independently. Radin (2018) gave a contradictory perspective specific to audit committees, suggesting that they had no noticeable impact on shareholder value. However, Radin did note some perceived benefit in independence and reporting at the board level.

Beyond top-level governance and board oversight, many companies implement a system of preventive and detective controls in order to combat fraud and misuse. Sometimes, these actions are government driven, such as the whistleblower statues through the Frank-Dodd Reforms of 2010. In these circumstances, companies implement whistleblower protocols and offer financial incentives for employees or external parties to come forward with useful information. While such controls can be effective, there is some question regarding the ethicality of such rules (Seitz, Oeding, & Wiese, 2015). McMahon et al (2016) noted that preventive measures are often used by organizations to create the perception that a fraudster will be caught or to create a high hurdle to accomplish the fraud. Preventive measures can be as simple as security controls, locked doors, password protections as well as soft preventive measures such as a corporate culture of intolerance for fraud and the threat of whistleblower actions.

Furthermore, in contemplation that some frauds require the fraudster to convert a company asset to a liquid asset, companies can put controls in place to prevent such a diversion, making the fraud largely useless to the perpetrator (McMahon et al., 2016). Finally, even in the

accounting and auditor realm, preventive controls are often implemented to ensure that this group is managed appropriately. Because accountants often have personality traits that can increase their level of rationalization for fraud participation, Reinstein and Taylor (2017) recommended a system of *fences* or fraud preventive techniques to help save accountants from themselves. These fences create a set of pre determined guidelines to prevent fraudulent behavior from becoming front and center, thereby holding accountants responsible.

Out of the various options of controls, detective controls tends to get the most publicity, possibly because studying fraud after discovery lends itself more cleanly to detective procedures. Although much of the literature examines the techniques of fraud detection from the viewpoint of an external scan of companies, such as using social media language (Dong, Liao, & Zhang, 2018), use of the Beneish Model to detect fraud (Kamal, Sellah, & Ahmad, 2016; Ozcan, 2018) and text mining of financial statements (Dong, Laio, & Liang, 2018), companies should be looking internally for detection techniques that are useful. One of the more popular methodologies in fraud detection is continuous auditing. While the results of research regarding the use of continuous fraud detection are mixed (Gonzalez & Hoffman, 2018), some research results do suggest that the mere presence of monitoring systems do have impacts on behavior. In addition, allowing employees an outlet, such as a whistleblowing program, or anonymous reporting channel, can offer an effective means of fraud detection. Whistleblowing programs, by extension, can offer a preventive and detective fraud benefit (Johansson & Carey, 2016).

Beyond these softer detective controls, procedural and data driven options appear frequently in research literature. Advances in monitoring through data and visualization have become popular ways to examine transactions after the fact. Fraud detection has become more streamlined through visual tools (Simeunovic, Grubor, & Ristic, 2016) as well as through

statistical analysis (Nigrini, 2017; Wuerges & Borba, 2014) and other data mining techniques (Albashrawi, 2016; Liu et al., 2015; Perols, Bowen, Zimmermann, & Samba, 2017). These detective controls are designed to examine the anomalies often present in misstated financial reporting connected to earnings and cash flow of a company (Lee, Ingram, & Howard, 1999).

### **Auditor and Management Responsibility**

A century ago, internal controls were easier than they are today. The founder of Nathan's Famous, the popular hot dog stand, established a low-tech process of monitoring for fraud, with highest risks related to cash skimming, that is still in place (Levy, 2016). However, the types and variations of fraud in today's business world are more complex, encompassing, and bold than a century ago; thus, auditors often find themselves in the middle. But what is an auditor's responsibility to detect fraud?

Generally Accepted Auditing Standards (GAAS) Section 240 suggests that auditors have a professional responsibility to apply specific audit procedures to determine if fraud is probable. This requires auditors to use professional judgment and maintain skepticism of management through inquiry and further evaluation about how management may be incented to commit fraud. However, because fraud is often collusive and management overrides internal controls, detection may be difficult (Georgiades, 2015). Furthermore, GAAS statutes are guidance only, not binding. As such, there are often stark differences between an auditor's opinion of their responsibility and public's opinion of an auditor's responsibility.

Carmichael (2018) further delineates the differences between a financial and fraud audit, noting that a fraud audit is used when a known fraud has occurred, whereas a financial audit is commonly a statutory requirement where fraud has taken place only in rare circumstances. Whereas the fraud audit is focused just on the incident, the financial auditor is only seeking

significant misstatement in the financial statements. This difference creates difficulty in an auditor detecting fraud, and thus, can leave an organization to perpetuate fraud for longer periods of time.

Within the literature, auditors take varying levels of responsibility for fraud detection during audit processes. DeZoort and Harrison (2018) determined a strong linkage between internal/external auditors and their responsibility for fraud detection. Further, external auditors noted a responsibility to detect fraud in financial statements, while internal auditors felt obligation for all fraud types. Jizi, Nehme, and Elhout (2016) gave a counter position, suggesting that most auditors feel no responsibility for fraud detection and highlight the fact that auditors and consumers of financial statements often differ in their opinion of ultimate responsibility. Auditors feel lack of responsibility primarily because of the difficulty in fraud detection, particularly when concealment is easier for a motivated manager.

Albrecht and Hoopes (2014) emphasized GAAS standards even note that “a properly planned and performed audit may not detect a material misstatement resulting from fraud” (p. 14). In many respects, it seems as if the deck is stacked against an auditor’s detection of fraud. Asare, Wright, and Zimbelman (2015) emphasized this in explaining the various reasons that auditors are challenged to detect fraud. First, auditors develop relationships with management that cloud their judgement about management motivations for fraud. As such, effective audit procedures are not formed based on a misperception of fraud risks, creating audit procedures that miss the fraud target.

Added to the issue is the fact that many auditors are not trained in fraud or fraud techniques, and therefore, do not understand how to attach the GAAS guidance on fraud detection to their audit (Asare et al., 2015). The result suggests that many auditors therefore



place unnecessary emphasis on sound controls, but the wrong controls, thereby providing a misguided belief that audit procedures are sufficient. In addition, the problem is compounded in that management place preventive controls that appear effective but miss the fraud risk completely (Hancox, 2014).

Further, in some situations, auditors may actually be penalized for raising awareness of internal company concerns. Eutsler, Nickell, and Robb (2016) demonstrated that audit firms who signal an issue of going concern, or the auditor's assessment that the company may not be financially viable, that are later determined to have fraud are much more likely to see legal action taken against them. This suggests that audit firms may have incentive to underreport certain aspects of their audit to avoid legal suits brought against them at a later date.

However, auditors and accountants are still based in the best position to discover fraudulent acts. Under the guidelines of professional auditing standards, auditors have many techniques to examine potential fraudulent issues. For example, auditors may choose to examine high risk items such as related-party transactions, high turnover of key executives, historical issues with regulatory offices and large changes in sales and profits. Additionally, auditors should perform high level changes in financial balances, industry ratios and benchmarks, as well as variances between actual and budgeted results (Tschakert et al., 2016).

More in-depth analytical procedures have also become commonplace in auditing, wherein auditors gather data that could be crucial in discovering a material misstatement. Furthermore, some research has suggested that a heavy dose of analytical procedures can substantially improve the likelihood that fraud or misstatement review has taken place (Glover, Prawitt, & Drake, 2015). More advanced regression methods using statistics can and have been designed in the auditing industry with implications on fraud prediction models. While these

models may offer some precision, many auditors are not trained to perform such work (McKee, 2014).

If anything, the auditing industry does have the government and regulation on its side. While results have generally been mixed, Sarbanes Oxley statutes have raised the bar with respect to the expectation of management of financial reporting. Gupta et al. (2018) demonstrated SOX may have improved asymmetric information out to the marketplace, though other studies have suggested that certification of results pushed down to lower management levels have been ineffective (Lowe et al., 2015) and that SOX has been incomplete in answering many of the crucial questions that auditors need to understand in performing an adequate review (Fichtner et al., 2015). Just the same, Aikins (2017) suggested the number of hours spent on an audit does have a proportionate effect to the audit outcomes, signaling an increase in audit recommendations, thereby raising the value of the audit.

With these issues in view, this study attempts to distill the complications that auditors seek to address in auditing for fraud. Specifically, the study aims to provide the audit community a new data point with reference to the fraud triangle by connecting CFO demographics with motivations. At a minimum, this information may provide auditors with logical and straightforward areas to look for potential fraud or alert them to red flags that may be present when fraud has taken place, given this research study's results.

### **Ethical Considerations**

Within the context of the literature, incidences of fraud are frequently connected to elements of ethical decision making. In contemplation of fraud theory, specifically, the ways in which people rationalize their behavior, sometimes referred to as ethical fading, is where the components of a business crossroads begin to separate themselves from personal morality and

morph to a business decision (Kirsch, 2018). Considering this, companies are continuously attempting to build cultures of integrity to prevent financial and reputational loss. In this sense, a company wishes to avoid a couple of situations with employees. The first is one of *blindness*, wherein employees purposely ignore ethical behavior because it serves them no benefit to report it. Second, companies wish to avoid the slippery slope of ethics, wherein small ethical choices eventually lead to bigger gaps in judgment, leading to fraud (McFadden, 2016).

In a similar fashion, organizations realize that the fraud triangle elements of pressure, opportunity and rationalization are commonly connected to loose application of accounting standards and a sliding scale of ethical behavior. Chinniah (2015) argued that high levels of pressure and opportunity can lower the level of rationalization required, thus chipping away at ethical beliefs. As challenging as it can be for companies to implement controls that can account for unethical behavior of employees in decision-making roles, it is even more challenging to consider that accountants, those placed in trusted positions, may be corruptible people as well. As Ugrin and Odom (2017) explained, like any other type of employee, accountants can be convinced to act in ways that lack integrity, which suggests that the accounting and auditing industries cannot rely solely on laws and statutes to protect companies from harm, rather, they require a control environment similar to other employees.

Another school of thought related to executives suggests that the behaviors they exhibit outside the office are indicators of subsequent corporate culture as well as risk of fraud in financial reporting. To those in charge of proper fraud controls, this suggests a couple of things. First, the propensity to commit a fraud often suggests the propensity for it to happen again. Additionally, based on the pressure leg of the fraud triangle, people who live lavish lifestyles

outside of work often wish to keep that lifestyle intact through their work efforts, and thus, may be willing to participate in fraud (Davidson, Dey, & Smith, 2013).

Corporations also must be mindful of personal and leadership traits where ethics are lacking or situational. Individually, research has shown a sliding scale morality effect on decision makers based upon the time of day (Kouchaki & Smith, 2014) and the time available to make an ethical versus unethical choice (Shalvi et al., 2012). The topic of responsible leadership is also relevant to companies. As Waldman and Balven (2014) stated, “it is not about whether organizations act responsibly, but about how individuals act and make decisions” (p. 224). Even more concerning to companies is the fact that those leaders who have been put in their positions because they are talented and creative are perhaps the group most likely to be dishonest in workplace situations (Gino & Ariely, 2012).

### **Synthesis of the Research Findings**

In pulling together the themes of occupational fraud, a few common aspects emerge. First, fraudulent acts by individuals and companies continue to be rampant around the globe. As such, the research literature has steadily kept pace with new and emerging theory around fraud topics. Second, fraud can happen to any company, anywhere at any time. Despite a company’s best efforts, there are relatively no companies that can consider themselves insulated from fraudulent acts. Given this, the creation of internal controls, which often lack in all sizes of companies, is a key feature to prevention or detection of fraudulent acts. Finally, the situations in which frauds take place are vast. Company employees at varying levels of the organization can and do step over the imaginary line within a variety of complex circumstances. Vices from person to person can vary; the severity for which they commit a fraud can be different with an

alternative set of circumstances, cultural elements can be present, and different sized companies can address fraud risk very differently (Dorris, 2018).

Given the far and wide reaching implications of fraud, it is necessary for research literature to coalesce around central themes and theory. Through Cressey's early work in the 1950s (Cressey, 1953), fraud theory had a starting place in explaining the actions of those who choose fraudulent actions. However, since Cressey's work, and particularly in response to the most recent incidences of widespread, daring, and collusive fraud, the fraud triangle has been brought into question, as this literature review has suggested. This has meant an attempt at a complete reengineer of fraud theory and the model for which fraud theory has historically been known. Research has contemplated the addition of elements to the existing fraud triangle, such as capability, by simply adding a side (Azam, 2018). It has added completely new elements such as the MICE (money, ideology, coercion, and ego) model, modifying the face of fraud theory completely (Dorminey et al., 2012).

Research has also attempted to take additional models; some historically developed, some newly developed, and merge them with the variations of the fraud triangle. This has created an emergence of new meta-models, hybrids, and new shapes of the fraud triangle, further muddying the theory itself. Unfortunately, these new concepts do not form a basis of congruence and consistency for which to assist fraud theory. Instead, more recent research has tended to examine situational fraud and attempted to force an existing model or create a new one for the purposes of explaining the fraudulent act post mortem.

On a parallel but often disjointed track, researchers, investors, and regulators are interested in knowing who is responsible for the perpetuation of costly fraud within an organization. As demonstrated through the literature review, any person at any level of an

organization can commit a fraud, given a set of characteristics (pressure, opportunity, and rationalization) at any point in time. However, literature does tend to align around the premise that corporate fraud, and especially occupational fraud, is most frequently orchestrated by upper level executives in the organization. While the motivations may be different for executives, they are often responsible or aware of the issue within their organizations.

Specifically, CFOs hold a unique leadership role in a company. Because of their direct interaction and responsibility related to financial statement reporting, CFOs tend to hold the keys when it comes to an opportunity for fraud. Additionally, research tells us that CFOs tend to feel different and heavier pressures that may trigger different and higher levels of motivation to commit fraud with extensions of fraud including not just internal but also external parties. Despite Sarbanes Oxley legislation meant to deter fraud, CFOs, through post mortem analysis, are often implicated and examined as part of a fraudulent act within companies. This has been demonstrated not only through research, but because of the actions taken by the Securities and Exchange Commission (SEC) via their lawsuits against fraudsters. Given CFOs unique role within an organization, and given their prominence within the fraud literature, this research study focuses specifically on the actions and ultimate motivations of the chief financial officer of indicted corporate fraud.

The demographical patterns of those most prevalent and likely to commit fraud represent a final portion of the literature. Like general fraud topics, fraud theory and those most prevalent in the fraud sphere, demographical research tends to be disconnected. Traits displayed in historical research have varied widely, from an attempt to nail down personality characteristics to defining the age of a fraudster. The research could include elements of the fraud triangle or be absent. It could center around one particular group, such as the CFO or CEO, or be

encompassing of a larger group of people participating in a collusive fraud. However, when scraping the literature for common themes, three demographics were noted as frequently studied and similar with respect to results: age, gender, and education level. Throughout literature, the results related to these three demographics were mostly consistent across the C-Suite and the board of directors. Perpetrators tended to be younger, male, and lesser educated in instances where fraud took place.

This research study, therefore, attempts to bind together several themes shared thus far within the literature review. First, the research attempts to unpack and simplify a complex fraud scene around the world. In doing so, the study will focus attention on frauds that have transpired and been indicted by the Securities and Exchange Commission in situations where CFOs were indicted. Next, the research will attempt to aid in the further formation of fraud theory, while acknowledging an assumption that fraud motivation (pressure and rationalization) exists in all situations. Although literature does not align around a common fraud shape or elements, research tends to agree that a motivation is present in a fraud, even if motivation is under a different label. Also, the research study will gravitate around the CFO, who is statutorily, and by virtue of position, given a different level of access to the company's financial records. Finally, this research study brings in important elements of CFO demographics, namely age, gender and education level. In sum, the historic research lacks in providing a complete picture of motivations present across CFO demographics, particularly those most common and least common to commit fraud. This research attempts to do just that.

### **Critique of Previous Research Methods**

For the purposes of review of research methods, several of the most influential articles related to the research question are examined focusing on fraud theory and CFO fraud

demographics. These specific articles are also analyzed from a more global view of the literature as well. To follow are several specific articles studied as part of this study's critique.

The Ge et al. (2011) study examined a CFO's style and demographics, relating the accounting choices made by the company that trickled over into accounting practices. The authors studied a multitude of observable financial values, which suggested judgment in accounting practices as CFOs moved from one company to another. The researchers could not account for differences, both culturally and functionally, within the organization. Accounting choices made by CFOs, therefore, may be more a measure of internal and external forces, such as differences in accounting application, industry standards, or a difference in the financial viability of the company. On a more global level, this study tends to align with previous research and limitations of that research in that motivations of CFOs are rarely consistent, whether the CFO is committing fraud or not. In particular cases of fraud, these motivations can be widely varied, if known at all. Furthermore, fraud motivations are not connected to CFO demographics in any of the studied literature.

Sun et al. (2017) crafted a similar type of intended research outcome examining the demographics of CFOs in fraudulently reported companies. The research design examined reliably reported incidences of fraud in China, extrapolating fraudulent results to CFOs in contemplation of the upper echelon theory, assuming the CFO had a certain degree of power in their position. The study compiled approximately 19,000 firm year incidences, lending credibility to the sample size, while appropriately excluding companies wherein the data was missing. In contemplation of the research design, a few risks present themselves. First, the study only examined incidences of fraud, wherein companies with no known but actual fraud would have been excluded. The study also presumed the CFO was involved or had influence over the



fraud through use of upper echelons theory. While this might be true, although assuming the CFO played an active role may not be accurate in all circumstances. On a more global level, similar studies connecting to CFO demographics to past frauds tended to yield similar results with respect to common genders, age groupings and educational levels. However, in doing so, there was a pervasive issue with the absence of motivation or any connection to fraud theory at all. While the information contained in the studies was useful, it did not extend fraud motivation beyond simply understanding who was most likely to commit fraud, while keeping the reason for it silent. As proposed, this study helps to connect demographics to motivation in this way.

Upon review of the fraud theory literature, a couple notable themes surface. First, relatively little research examines fraud motivation, the intersection between pressure and rationalization. Literature tends to focus on one leg of fraud theory or the entire fraud triangle. Second, fraud theory tends to become blurred with other aspects of theory, including aspects of criminology and ethics. Other research includes or creates other fraud meta-model discussions that move it away from Cressey's original work (Cressey, 1953). This study, however, approaches the questions around fraud differently by including two legs of the fraud triangle (pressure and rationalization) while temporarily calming the challenge of fraud theory by incorporating the element of CFO demographics into the discussion.

Furthermore, this research study is intended to be different from past research in several respects. The analysis of the above studies connected to various theories such as upper echelon, theory of planned behavior and ethical climate theory, whereas this analysis will connect to fraud theory as its sole theoretical context with efforts to impact existing fraud theory. Additionally, much of the research, including the above, considers fraud through quantitative analysis of financial data, primarily financial statements, or qualitative survey. This study, while qualitative

in nature, does not interact directly with CFOs or those who have committed fraud, and is designed to capture case studies of CFO fraud and analyze actual fraud results. As such, much of the data gathered is during or just after the time of the fraud indictment and potentially free of the bias that exists in post mortem surveys well after the fraud event.

### **Summary**

Chapter 2, in particular the literature review, took a broad stroke of fraud in boiling it down to fraudulent CFOs and their underlying demographics and motivations. Along the way, historic research was presented on industry-related fraud, ethical concerns, auditor/management responsibility and compliance topics. In general, literature aligns with younger, male CFOs with less education as the perpetrators of fraudulent behaviors. This common demographic in comparison to their uncommon CFO group would, according to literature, exhibit some sort of pressure (motivation) in committing the fraud. As such, in alignment with fraud triangle theory, this study seeks to understand the similarity or differences of such motivations in the common and uncommon groups. To follow, Chapter 3 takes the reader through the research methodology.

## CHAPTER 3. METHODOLOGY

### Purpose of the Study

When the discovery of fraud breaks in the news media, much of the postmortem analysis focuses on the specific reasons and circumstances of the fraud, including who was responsible, how the fraud was committed, and why the perpetrator took the steps to do so. As a result of this analysis, several outcomes can arise as potential influencers of the fraud including permissive ethical climate, toxic tone at the top, external market pressures, compensation structures that encourage negative decision making (Soltani, 2014), the use of damaging power methods by executives (Albrecht et al., 2015), pressures between executive-level employees (Bishop et al., 2017b), and internally held pressures of CFOs, including fear of losing one's job (Bishop et al., 2017a).

While interesting to the external observer, postmortem analysis is likely more useful to the investor community and fraud fighting industry insomuch as it connects to Donald Cressey's 1950s fraud triangle theory of white collar crime (Cressey, 1953). This theory posits that the presence of pressure/incentive, opportunity and rationalization are almost always a factor when an occupational fraud takes shape. Elements of fraud theory are continuously backed by research connecting fraud theory to actual incidences of fraud, including pressure from the CFO to maintain stock price (Bishop et al., 2017b), a CFO not wanting to give bad news to a CEO (Radin, 2017) and CFO fear of disclosing negative financial measures to the public (Donegan et al., 2017). Time and again, as details of occupational frauds are disclosed to the public, one, two or all three elements of the fraud triangle are present. And consistently, the intersection of pressure/incentive and rationalization, also stated as motivation, are present in fraudulent circumstances.

In the past decade, fraud theory has been hotly debated, particularly with the higher incidence of occupational fraud in the first decade of the 21<sup>st</sup> century. During these recent times, peripheral issues connected to fraud theory have emerged, which have contributed to the fraud theory debate. One issue impacting fraud theory is the concept of collusive fraud, or fraud perpetuated by more than one person (Free, 2015). Another issue is how ethical climate, tone at the top and public pressures contribute to occupational fraud (Soltani, 2014). All of these side issues have consequently caused researchers to challenge the shape of the triangle itself; with new models and meta-models suggesting fraud theory may be a diamond, hexagon, or even a model with unlimited sides (Huber, 2016).

As a result of postmortem analysis, the specific actors who perpetuate the fraud are also discovered and discussed. Because of their unique position as well as perceived power within an organization, CFOs are frequently responsible for, aware of or actively involved in occupational fraud situations in a company. Organizations such as the Association of Certified Fraud Examiners (ACFE) commonly detail out demographic information of fraudsters, including their position, age, gender and educational level in discovered frauds (Dorris, 2018), often citing CFOs as the central responsible party. Scholarly authors also dive more deeply into CFO demographics such as years of service, experience in other organizations and advanced degrees and certifications connected to companies who have financial restatements (Aier et al., 2005). Further, they examine the global footprint of fraud based on age, gender and education in contemplation of earnings management choices (Qi et al., 2018), and age, gender, and education level related to known financial statement frauds (Sun et al., 2017). In this way, literature tends to align around commonality of CFO fraud demographics in being younger male and lesser educated.

While debates ensue about the proper methodology of fraud theory, occupational fraud continues to happen in growing numbers (Dorris, 2018) and in more cases than not, the CFO is targeted and indicted in these situations. On top of that fact, research has mostly aligned on the types of CFO demographics most present, and by default, least present when an occupational fraud is discovered. However, no research to date has married the two together; CFO common and uncommon demographics specifically to fraud theory. To be more precise, the CFO's motivation, defined as the intersection of pressure/incentive and rationalization, for committing a fraud and whether the motivations of CFOs in the common and uncommon demographical groups are similar has not been considered in historical research studies. As such, this study hopes to accomplish just that – determine the motivations, similar or different, between CFOs who commit frauds in the common versus the uncommon demographic groups.

### **Research Question**

The research question for this study is stated as: for CFOs indicted of corporate fraud, what differences are seen in fraud motivations for CFOs with common fraud demographics (male, younger, lesser-educated) versus lesser common demographics (female, older, more highly educated, or any other combination)?

### **Research Design**

This research study methodology is qualitative multiple case study. Because of the sensitive nature of occupational fraud, and given this study seeks to discover the fraud motivations present in CFO's actions, qualitative case study allows the researcher to gather data through public archives rather than establishing direct contact with the fraud target within the cases studied. In turn, this partially protects the CFO population studied as part of occupational fraud.

In consideration of the key demographics stated above (age, gender, and educational level) and in contemplation of past research outlining common demographics (Aier et al., 2005; Barua et al., 2010; Liu et al., 2016; Qi et al., 2018; Sun et al., 2017; Troy et al., 2011;) wherein younger males with lesser education are part of the common demographic and any other combination would be considered uncommon, companies with indicted fraud are identified as a starting point. Securities and Exchange Commission (SEC) daily news bulletins were reviewed to determine if the CFO was a named party within the indictment, with information catalogued if the CFO was a named party. After identifying cases of indicted fraud from which the CFO was implicated, basic demographic data was researched including CFO age, gender, and highest level of education achieved. For the purposes of capturing this data, the SEC indictment often listed CFO gender and age, while general search techniques such as LinkedIn, Bloomberg, or other similar sources often provided information on the CFO's educational background.

Once the CFO information was catalogued, a review of the conclusion of the fraud case was examined and further grouped. Common groups of the indictment conclusion included: settled immediately with the SEC, settled after a lapse of time with the SEC or Department of Justice (DOJ), judgment, plea deal or guilty via trial jury. Generally speaking, the longer the case continued, either via the SEC or DOJ, the better likelihood that media and court transcripts would be available to gather information on CFO fraud motivation.

In instances where information pertaining to CFO fraud motivation was mostly likely discoverable, further public searches were conducted on the CFO, including a general Google search seeking media reports, a LexisNexis search to discover legal articles, a submission of request to the Freedom of Information Act (FOIA) for information at the Federal levels and a search on Public Access to Court Electronic Records (PACER). Each media source or court

record was carefully examined, with keyword and key phrases documented, fraud themes captured, and a summary of the perceived CFO fraud motivation catalogued. At the conclusion of all discovered research by CFO, a final fraud motivation conclusion was prepared, summarizing all the information previously catalogued.

Data analysis was completed by use of a key word or key phrase review in order to arrive at common patterns. These patterns were used to determine general motivational themes, which contributed to the overall CFO fraud motivation conclusion. The corresponding themes and conclusions were connected to the common and uncommon demographic groups to compare and contrast. Triangulation was used across multiple sources to arrive at themes and CFO fraud motivations, while providing support in the fraud motivation conclusions. Triangulation occurred across sources, including media and judicial transcripts, as well as across multiple legal transcripts themselves and by identifying common keywords used frequently within the same legal transcript.

### **Target Population and Sample**

#### **Population**

For the purposes of studying CFO fraud motivation, the population consisted of any instances where the SEC indicted a company's CFO for a fraudulent act. The fraud cases included in the population were those related to a specific financial statement fraud or a securities fraud, such as issuance of illegitimate company stock. Furthermore, because of the amount of time required for a fraud case to step itself through the judicial system, only indicted frauds from 2015 and earlier were studied as part of the target population. There were approximately 150 cases of SEC reported fraud in the population.

## Sample

After determining the population as stated above, each fraud case was reviewed for its conclusion, whether that conclusion was with the SEC or DOJ. The cases were categorized as follows: settled immediately with the SEC, settled after a lapse of time with the SEC or Department of Justice (DOJ), judgment, plea deal or guilty via trial jury. The cases that went to jury trial, received a plea deal or a judgment remained in the sample, while the other cases were removed. The sample remaining represented 11 fraud cases. To determine if the cases would remain in the sample, more intensive research was completed to ensure enough data was discoverable to arrive at a CFO fraud motivation conclusion. Those cases with sufficient data remained in the sample. Secondly, the researcher confirmed the existence of CFO demographics that fit into the common and uncommon fraud groups to have a sufficient sample. The cases were studied until proper saturation of results occurred and results could be arrived at.

## Procedures

The data collection procedures for this research study were as follows.

- A listing of all corporate fraud cases where the CFO was named as an indicted party through SEC filings was catalogued. The cases began in 2015 and went backwards in time and had to be finalized in the court system, with the CFO found guilty.
- The CFO's demographic data was recorded based on public records such as LinkedIn, Bloomberg's, and SEC filings. Data related to CFO age, gender, and educational background was recorded.
- The CFO was categorized as either in a common or uncommon demographical class based on gathered facts of the CFO and the categorization of common/uncommon



given historical research. Within the sample selected, 4 cases were common and 7 cases were uncommon CFO fraud demographics.

- Information was catalogued that determined the outcome of the CFOs case of guilt. The categories documented were settled immediately with the SEC, settled after a lapse of time with the SEC or Department of Justice (DOJ), judgment, plea deal or guilty via trial jury. Cases where the CFO settled with the SEC immediately or later were removed from the eligible population because of lack of data available to form the basis of a CFO's fraud motivation.
- Information was gathered on the CFO's implied or stated motivation for the fraud through public sources, such as initial SEC filings, subsequent court transcripts (either an SEC or DOJ case brought against the CFO), media reports or other documentation supporting the CFO's motivation or actions. The primary data sources were: (a) local media reports; (b) Freedom of Information Act (FOIA) data requests; and (c) Public Access to Court Electronic Records (PACER). Through thorough and careful study of court records, eyewitness testimony, attorney questioning and evidence, CFO testimony and final ruling of the court case, as well as any accompanying media coverage, the information gathered was triangulated with the CFO and circumstances to form as basis of opinion regarding the CFOs implicit fraud motivation.
- Throughout the process steps outlined in the steps above, specific keyword and key phrases were recorded to capture the fraudulent acts that took place as well as information pertaining to the CFO fraud motivation. Additionally, key themes were captured on a case-by-case basis and final fraud motivation conclusions by each piece

of documentary evidence as well as a conclusion based on a combination of all combined evidence was constructed.

- The general groups of motivations, as well as the specific motivations themselves, were connected back to the CFO demographics labeled as common and uncommon with emergent themes classified.

### **Participant Selection**

Because this research was a qualitative case study, there was not an active recruitment of participants in a physical sense. However, to arrive at fraud motivation conclusions for the common and uncommon groups of fraudulent CFOs, consideration was given toward the CFOs age, gender, and educational background when selecting the sample, as described above.

Additionally, the amount and quality of data records, particularly court records, was important in selection of the purposive sample.

### **Protection of Participants**

Because human subjects were not included in this study and information was gathered exclusively via secondary data sources available to the public, protection of participants received less consideration. However, potential ethical issues related to fraudulent CFOs are discussed below. These ethical issues were addressed in part through data analysis techniques also described below.

### **Data Collection**

As noted above, data collection was performed via secondary public records search and through data requests sent to FOIA representatives. Upon receipt of information, documentation was carefully studied with key information highlighted. This data was then transferred into a spreadsheet, which captured the keywords and key phrases most principle to the fraud situation

and CFO motivation. Additionally, fraud themes were captured at the fraud scenario level and conclusive CFO fraud motivation notes were documented per documentation level as well as combining each piece of documentation together in forming a final summary CFO fraud motivation conclusion.

### **Data Analysis**

Because this study does not use research subjects through interviews or focus groups, there is less inherent risk to improper data analysis than other variations of qualitative research. However, it is important that proper reflection and interpretive thinking be applied to data gathered. As such, a strategy to gather and analyze data was followed by a key word / key phrase pattern search based on publicly available secondary data sources, primarily local media and PACER court transcripts. This key words / key phrase process documented the circumstances of the case, a mid-level summary of the fraud scenario and a high-level fraud motivation conclusion. Key words / key phrases were catalogued and linked to the fraud scenarios and conclusions to connect key ideas with written documentation of the court case, court documentation or media source.

Next, a system was used wherein the key words / key phrases were dissected from larger key phrases down into a series of codes. As further data and sources were included, additional codes were added while previously documented codes were added to. The iterative process continued through completion of documentation for each fraud case. Categories and subcategories of data were captured and themes were accordingly coded and catalogued to ensure consistency throughout the process of studying each individual fraud case and CFO circumstance. Through this cataloguing and sorting process, the intent is to ensure the findings and conclusions are consistent, accurate and free of bias.

Upon completion of collection procedures used and described in sections above, a process of sorting and sifting continued, wherein a series of themes emerged from the sorting of fraud motivation key words and phrases. This thematic analysis clustered the common keywords in fraud motivation, such as financial pressures, in order to create meaning across the set of data analyzed. The corresponding themes were then connected to the demographic data of age, gender, and education levels to arrive at similarities and differences across common and uncommon CFO fraud demographic groups. Additionally, this analysis was completed within each case, then across cases within the same demographic group and finally across cases and across groups.

Triangulation, used to clarify the fraud situation and avoid distortions, was also used in order to more soundly analyze each fraud situation. Triangulation was used mostly considering locating various independent sources of data, such as trial transcripts and a media report that are independent of one another. Additionally, triangulation was woven within trial transcripts, for example, across witness and expert testimony, primarily that of the CFOs themselves. Triangulation across trial transcripts has served as the strong basis for adequate data analysis.

### **Instruments**

No instruments were utilized for this research. In the context of this study, where court documentation was the primary source for which data was collected, analyzed, and interpreted, it is useful to better understand the role of the court system and governmental / criminal entities that feed into it. Based on the SEC's annual report (White, 2016; White, 2015; White, 2014) the agency is responsible for researching and seeking enforcement actions against companies and employees of occupational fraud acts. As such, the SEC investigates potential fraudulent situations, indicts those responsible, as necessary, and moves the case through the court system.

The DOJ, independent of the SEC, may additionally opt to take criminal action against company employees. These cases may work in parallel through the courts, or the SEC may pause until completion of the DOJ proceedings. The SEC and DOJ may operate with limitations of staffing as well as objectivity, as both agencies publish annual reports capturing their accomplishments. As such, there may be additional ethical limitations, as described below.

### **The Role of the Researcher**

The role of the researcher is particularly important in qualitative research given the limitations around reliability and accuracy afforded to quantitative researchers. As such, this study and data analysis methods were designed with a rigorous set of techniques including key word / key phrase documentation, sorting, categorizing, theme formation and triangulation, as noted above. In addition, a separate bracketing exercise, wherein the researcher outlined known bias of fraud theory was additionally considered through the data analysis procedures. Finally, the researcher grounded himself within the professional guidelines of professional certification as a Certified Fraud Examiner. The combination of these techniques were structured in such a way as to reduce bias to the lowest possible extent, while offering rich and useful research results.

### **Guiding Interview Questions**

There were no direct interview questions used for this study. Within the SEC and DOJ court systems there are a series of questions from attorneys to witnesses and, in some cases, the CFO, wherein targeted questions are asked. In these circumstances, lawyers are incentivized to offer their side of the story through question and answer, while still bound by professional standards and codes of conduct. In addition, any relevant negative questioning may be offset by additional questioning from the opposing attorney, physical evidence countering the questions

and closing statements. In the context of this study, attorneys in the courtroom conduct the interview questions for the researcher.

### **Ethical Considerations**

Given the research design was non-experimental, inclusive only of publicly available secondary data and not interactive with research subjects, many of the ethical considerations as stated by Capella (2017) regarding selection of human subjects is not applicable. However, care was still taken to protect the privacy of both companies and individuals within those companies during the research, similar to Capella's recommendations for human subjects (2017). Because names were used in reporting of the results some ethical risk is present given the fraudulent CFOs' motivations generally were implied rather than explicitly stated outright. Given this, the researcher has carefully triangulated the facts of the individual fraud circumstance and examined the results for logical themes before drawing substantive conclusions related to motivation.

Additionally, while the researcher is bound to ethical standards of research, attorneys who are indirectly conducting interview questions on behalf of the researcher are not bound by these same standards. These attorneys are bound by their own code of conduct and standards, but they may not be in lock step with the research community's ethics. This factor should be taken into consideration as part of the research results.

### **Summary**

Chapter 3 summarized the basic research design methodology of this research, reminding the reader of the foundational purposes of the study and research question before covering, in detail, the study's design. Chapter 3 also outlined the target population and sample, along with information on how research procedures were conducted and how data collection was handled. It concluded with the primary role of the researcher and ethical considerations. To follow, Chapter

4 will step the reader through the research findings, including a full presentation and summary of results.

## CHAPTER 4. PRESENTATION OF THE DATA

### Introduction: The Study and the Researcher

Chapter 4 of the research study serves as the foundation for this researcher's results and findings. This chapter represents the first indications of what the data tells the researcher about the research problem in contemplation of the literature review presented in Chapter 2. The combination of Chapter 4's research results and Chapter 2's review of past literature is further summarized in Chapter 5. The composition of this chapter begins with information regarding the researcher and the researcher's interest, experience, motivation, and selection of the approach and model of the study. The section to follow provides a description of the sample, comprising a more specific understanding of how this sample was derived. Next, the application of research methodology as it applies to data analysis of the research results is examined and discussed in consideration of the proposed protocols discussed in Chapter 3. Finally, the results of the data analysis are presented, comprising the crux of the chapter.

The researcher for this study has a personal and vested interest in the research results. During the researcher's career, he has worked within the fraud, audit, and internal controls industries as well as taught courses on forensic accounting, audit, and detective/preventive controls at the collegiate level. Additionally, the researcher is a Certified Fraud Examiner (CFE), who speaks on fraud topics around the world. Because of this, the researcher has higher than average knowledge on the topic and has personally experienced the implications of fraud in working with organizations that have experienced it. The researcher has provided consultative advice on how to clean up past fraud occurrences as well as prevent against them in the future. He has seen the personal toll that fraud takes on companies, investors, employees, and the fraudster themselves.



Given the researcher's direct work within the trenches of company fraud, he brings a myriad of applicable experience as to how and why fraud happens. Fraud motivation, the intersection between opportunity and rationalization is mostly understood by the researcher as a narrowly defined set of situations. While this is a strength, it may also interfere with researcher objectivity with respect to new or emerging motivations not previously noted in the researcher's direct line of work. As such, the researcher must be cognizant to follow the methodological approach within the model chosen to perform research considering proper protocols and procedures insomuch as this can help to offset concerns of researcher bias. The researcher proactively completed a bracketing outline and provided a series of known personal biases related to fraud incidences. These known biases were analyzed and referred to during the analysis and conclusion portions of this dissertation.

The research study outcomes will, minimally, create a new basis of knowledge for the researcher that can be used in future pursuits within the fraud fighting industry. The researcher feels optimistic that his background will positively influence the research outcomes, while the constructs and review process of the dissertation will create natural controls for the results presented as unbiased and objective. These control mechanisms are present throughout the remainder of this chapter and modeled in the clearly established procedures to arrive at research results.

### **Description of the Sample**

In sum, 11 fraud cases were studied for this research. Of the 11 cases, each person studied held the office of chief financial officer for the company for which a fraud occurred. The specific population consisted of nine men and two women ages 38-59 with varying educational backgrounds ranging from a community college degree to a master's degree. Most of the CFOs

had an undergraduate degree, one was a certified public accountant (CPA), while two CFOs' educational backgrounds were unknown. By virtue of classifying the CFO in the common versus uncommon fraud demographic, seven were in the uncommon and four were in the common fraud group. The CFOs represented a variety of geographic locales, although most were located in the Eastern half of the United States.

CFOs that were not included in the study and removed during the process included those who were indicted by the SEC yet did not advance far enough in the indictment process for evidence of motivation to exist. CFOs for which little or no court documentation existed were not included in the sample, as motivation would have been nearly impossible to document, analyze, and conclude upon. Additionally, other influences may have been present in a portion of the participants in situations where the CFO accepted a plea or judgment in lieu of testimony against another company executive. This situation was present in four of the eleven cases. In these situations, court testimony and motivation were often more readily available as the CFO tended to be more open with testimony given they were incited and contractually obligated to do so. As such, the results for those CFOs who bore all information as part of plea arrangement may be weighed differently than those who were fighting for their freedom.

### **Research Methodology Applied to the Data Analysis**

Data analysis was completed as per a set of qualitative research friendly procedural steps. This process began with a review of all raw data available for each CFO fraud case with appropriate cataloging of key concepts for each case and each piece of research support connected to the case, be it court records or media reports. This process was followed by a case-by-case coding system to capture major keywords and phrases. This coding process was documented and demonstrated upon review of each case, as shown in the next section below.

During the process of data analysis and review of secondary data sources, 124 individual codes were identified across the 11 CFO fraud cases (See Appendix A). These codes were then distilled, combined, and organized by grouping similar types of coding observations into 17 category/subcategory combinations (Appendix B). Finally, the categories and subcategories were distilled even further into a small number of overarching research themes. These key research themes are discussed later in this chapter as well as highlighted in table format in Appendix B.

### **Presentation of Data and Results of the Analysis**

In line with the research design as described in Chapter 3, this data analysis section progresses through a series of precise steps to take the raw secondary data to distill categories, themes and provide a basis for deeper analysis. This stepwise approach is subsequently described in the following sections and is deliberate in the order and approach herein. Each case summary is included with detail connecting to the secondary research observations.

#### **Case Summary**

The section to follow provides a case-by-case summary of the 11 CFO fraud cases researched as part of this study. Each case is broken down into background, intermediate-level results, and an individual case research conclusion, along with key word/key phrase references. The cases are listed below in alphabetical order based on the CFO's last name.

## **Bartholomew (Younger, Male, Less-Educated) – Los Alamos National Bank**

*Background on the case.* Daniel Bartholomew served as chief financial officer at Los Alamos National Bank from 2003 to 2014. During his tenure, Bartholomew was peripherally involved in a series of fraudulent accounting and banking violations prompting an SEC indictment against him and several other bank officials. The information outlined in this summary comprises actions taken and not taken by Bartholomew, as well as actions taken by others for which he did not take steps to stop. As CFO, Bartholomew settled with the SEC for no penalty in exchange for his testimony and assistance against what appear as the main executive targets in the case. That being the case, the fraud motivations are still captured in this case, despite the CFO not going to trial.

The main components of this case involve some of the more global issues surrounding the bank crisis approximately a decade ago. As is also true in this CFO fraud case, Los Alamos Bank (also referred to as Trinity) was responsible for issues of downgrading certain troubled loans, failing to impair certain toxic assets and failing to capture impairments and other loan issues. The SEC complaint stated that the bank, “refused to downgrade loans...failed to designate loans as impaired...failed to measure impairment properly...purposely overvalued real estate” (Complaint, *Securities and Exchange Commission v. Jill D. Cook and Mark C. Pierce*, 2015). From the viewpoint of executive motivation, the “scheme was motivated...Trinity’s desire to be released from the supervisory agreement, which would only occur after Trinity met specific requirements” (Complaint, *Securities and Exchange Commission v. Jill D. Cook and Mark C. Pierce*, 2015). This suggested motivation stemmed from past regulatory issues driving the bank executives toward fraudulent actions. During a 2009 bank examination, the governing body noted a variety of management and internal controls topics of grave concern stated through

court records as, “(i) employed management who did not have sufficient objectivity and expertise; (ii) had an excessive level of problem and non-performing loans; (iii) did not consistently risk rate loans accurately or identify problem loans” (Complaint, *Securities and Exchange Commission v. Jill D. Cook and Mark C. Pierce*, 2015). Los Alamos Bank’s Chief Credit Officer (Cook) and Senior Loan Officer (Pierce) participated in a series of actions to defraud investors of the bank and conceal the evidence as demonstrated through the SEC documentation as follows, “Pierce instructed loan officers to avoid having loans classified as TDRs” (Complaint, *Securities and Exchange Commission v. Jill D. Cook and Mark C. Pierce*, 2015), “falsely stated the reason for reduced interest rate to avoid having to classify the loan as a TDR” (Complaint, *Securities and Exchange Commission v. Jill D. Cook and Mark C. Pierce*, 2015), “set a tone at the top that created significant pressure for loan officers to avoid having ‘bad loans’” (Complaint, *Securities and Exchange Commission v. Jill D. Cook and Mark C. Pierce*, 2015), “Trinity’s loan department ignored and hid loan weaknesses” (Complaint, *Securities and Exchange Commission v. Jill D. Cook and Mark C. Pierce*, 2015), “During the 2012 OCC Exam, Cook told a loan officer to shred loan guarantees that Waterman had signed that had never been imaged into the Bank’s electronic loan file system” (Complaint, *Securities and Exchange Commission v. Jill D. Cook and Mark C. Pierce*, 2015), and “She implemented and perpetuated the culture of intolerance for downgrading loans” (Complaint, *Securities and Exchange Commission v. Jill D. Cook and Mark C. Pierce*, 2015). The following internal bank emails also support the underlying fraud and culture of Trinity, “[a]s long as we don’t make it appear to be a TDR, we should be good” (Complaint, *Securities and Exchange Commission v. Jill D. Cook and Mark C. Pierce*, 2015), “use the long time good customer matching competing bank offer approach” (Complaint, *Securities and Exchange Commission v. Jill D. Cook and*

*Mark C. Pierce*, 2015), and “I have pretty much exhausted all of my creative ways to cover that here at the Bank,” (Complaint, *Securities and Exchange Commission v. Jill D. Cook and Mark C. Pierce*, 2015).

For his part, Bartholomew was also responsible for portions of the fraud. As CFO, Bartholomew was responsible for implementing adequate internal controls over debt and appraisals, which he did not do. Additionally, he caused many of Los Alamos Bank’s inaccurate and fraudulent reporting as stated through the SEC documentation, “Bartholomew was also a cause of Trinity’s false books and records and the submission of inaccurate reports because he was on notice of certain transactions that failed to comply with generally accepted accounting principles (GAAP), but he failed to correct the accounting errors” (Complaint, *Securities and Exchange Commission v. Daniel R. Bartholomew and Karl I. Hjelvik*, 2015). In so doing, Bartholomew failed to act on several key business functions stated as, “repeatedly saw quarterly grade change reports that indicated loans were not being downgraded timely” (Complaint, *Securities and Exchange Commission v. Daniel R. Bartholomew and Karl I. Hjelvik*, 2015).

Bartholomew took no action when he was ‘dis-invited’ from attending loan department meetings where problem loans were discussed, even though he suspected that he was dis-invited because he thought the loan department wanted to keep information from the accounting department (Complaint, *Securities and Exchange Commission v. Daniel R. Bartholomew and Karl I. Hjelvik*, 2015).

“Bartholomew were...aware of these appraisal irregularities.... took no action to increase controls over the appraisal process” (Complaint, *Securities and Exchange Commission v. Daniel R. Bartholomew and Karl I. Hjelvik*, 2015). Cook and Pierce eventually took a plea deal and paid a small civil penalty of \$30,000 and \$100,000, respectively, with no jail time.

**Intermediate-level results.** Woven throughout this case, although somewhat quietly, is the fact that Bartholomew lacked sufficient experience to be in the role and capacity he assumed at Los Alamos Bank. This is mentioned through formal channels when the bank was examined as well as mentioned again in Bartholomew's cease-and-desist order as, "Bartholomew, Hjelvik, and loan department personnel involved in calculating and reviewing the impaired loan loss calculations did not possess sufficient accounting expertise" (Complaint, *Securities and Exchange Commission v. Daniel R. Bartholomew and Karl I. Hjelvik*, 2015). It is apparent through the SEC indictment actions that the largest targets in the fraud from the standpoint of the SEC were the credit and loan officers. The CFO appeared to be largely complacent and unaware of what was happening. While the SEC does not usually accept complacency as an excuse, in this case, they appeared to give leniency, not formally charging the CFO with a crime, despite indicting him initially.

**Research conclusion.** In this case, there were very few discoverable pieces of court testimony, as all parties settled the claims by the SEC. The CFO arrived at a settlement in lieu of a lengthy court process, and it appears the SEC used this as leverage and threat that the CFO would speak against Pierce/Cook in the case. Overtones in all of the documents lead to some conclusions.

First, the organizational fraud was motivated by executives' desires to release themselves from previous regulatory actions exercised against them. They wanted to get out of regulatory jail and inflated their numbers to do so. Second, the ring leaders appeared to be Pierce and Cook, not the CFO. Third, corporate tone appeared to be largely driven by Pierce and Cook, but especially Cook. She appeared to be the largest target of the SEC, evidenced by the information presented against her in the original complaint and the fact that her judgment fine was larger than

anyone else. Corporate tone appeared to be one of intolerance for bad news (downgrade of loans) and dictated by Cook through her demeanor. This may have had impacts on the decision making and therefore the motivation of the CFO.

Finally, there are overtones throughout the SEC documentation that Bartholomew (CFO) was largely uneducated and was left hung out to the dry by the ring leaders. This claim is mostly supported in reviewing the CFO's LinkedIn, noting that the CFO only had an undergrad degree in religion before and during his time working at the bank, including in the capacity of CFO. He also did not and does not hold a CPA license, common in publicly traded companies. He has, since this incident, received a degree in accounting and did previously have some education in banking, however, this likely left the CFO unequipped to perform reasonable diligence over internal controls, particularly as the perform more acutely responsible for internal control design and monitoring.

Based on this information, the CFO likely acted in a capacity that left him unable to perform his duties and largely not responsible for the fraud. This does not completely relieve him of responsibility, as some of the documentation suggests he was receiving reports and being removed from meetings that should have sent red flags to a reasonably intelligent person; however, with two clear ring leaders, coupled with staff who are untrained on fraud and internal controls, it suggests that lack of education and executive pressure were the main motivators for the fraud, from the perspective of the CFO.

#### **DiMaria (Younger, Male, Less-Educated) – Bankrate, Inc.**

***Background on the case.*** Edward DiMaria served as Bankrate, Inc's CFO from 2006 to 2014, which operated as a bank offering consumers services such as mortgages, insurance, credit cards, and automobile loans. During this time, DiMaria was responsible for appropriate GAAP



accounting and internal controls. DiMaria, in concert with another key accounting official at the bank, orchestrated a common financial statement fraud in which quarterly results for Q2 2012 were stated as more favorable than reality. The fraud included the use of *cushion accounts* also known as *cookie jar accounts*, for which DiMaria used to modify the quarterly financial results of the bank. The SEC and DOJ describe DiMaria's actions, "Bankrate maintained spreadsheets noting various 'cushion accounts' – dubbed 'Ed's Cushion'" (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015), "DiMaria used these cushion accounts to 'tune' Bankrate's financial numbers." (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015), "attaching updated version of the 'cushion' spreadsheet which showed there was \$1.7 million in the cookie jar available to reverse and inflate Bankrate's earnings" (Complaint, *United States of American v. Edward DiMaria*, 2017). In addition, DiMaria fostered an environment of fraud and fear through his actions with accounting staff through various documented actions such as "DiMaria established a corporate culture that condoned using improper accounting techniques to hit the company's financial targets" (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015), "DiMaria also directed that certain unsupported accounting entries be kept 'under the radar'" (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015), as well as internal emails including, "DiMaria asked the vice president to 'review the final balance sheet and the cushion analysis... I may want to tune our numbers...'" DiMaria did, in fact, use the cushion accounts to 'tune' Bankrate's numbers to meet financial targets" (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015), "Charge ALL BILLS TO ACCRUED DEAL COST – I DON'T CARE IF THEY COMPLAIN, WE CAN SAY IT WAS A MISTAKE" (Complaint, *Securities and*

*Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015), “Gamsey immediately emailed the vice president of finance: ‘Better start figuring out an explanation for these’” (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015), “going to rip [the Credit Cards CEO’s] f[\*\*\*]ing head off” and “fire the Credit Cards accountants if they ‘f[\*\*\*] up the accounting” (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015), and “People really have to start using their brains, sometimes I really wonder. Ok why not just write “Hey [Accounting Firm A] – This entry is cushion, please propose an adjusting entry” I really expect this stuff to be managed better” (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015). He also directed staff to make unsupported accounting entries, ignored data to make other necessary accruals, and created documentation to support these instances despite a clear understanding from internal staff that it was not proper and only created more problems in the future. These actions were documented through SEC and DOJ complaints as, “DiMaria...improperly directed two Bankrate divisions...to book additional revenue of \$300,000 and \$500,000...without support or analysis” (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015), “DiMaria further attempted to conceal this fraud by retroactively attributing this revenue to a purported contractual dispute” (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015), “Bankrate intentionally failed to book approximately \$99,000 in known accounting expenses” (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015), with internal dialogue documented as, “Ok go ahead – make it [EBITDA] just over \$30 [million]” (Complaint, *United States of American v. Edward DiMaria*, 2017), “Doesn’t [DiMaria] realize that all this does is put us in a hole to start [the third quarter of 2012] since it

will have to be reversed when the ‘estimate’ is trued up” (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015), “he said there may be some additional good guy adjustments coming and I f[\*\*\*]ing knew that he was going to do something like this” (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015), and “[DiMaria] is treading on very thin ice here” (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015). It is worth noting that DiMaria admitted to all allegations during his change of plea trial testimony.

**Intermediate-level results.** According to the SEC complaint, DiMaria was able to visibly profit from the fraud during this singular quarter demonstrated as “DiMaria sold Bankrate stock, profiting from a stock price that had been artificially inflated by the company’s materially overstated financial results” (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015), “Bankrate’s misstatement of its adjusted EBITDA was material, as it allowed Bankrate to exceed analyst consensus estimates for this key financial metric” (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015), “Bankrate’s stock price rose from \$15.95 to \$17.57 per share. DiMaria sold Bankrate stock during the two-week period following the announcement of Bankrate’s second quarter 2012 financial results” (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015), “DiMaria sold a total of 107,177 shares of Bankrate stock on August 9, August 10, and August 13, for approximately \$2 million” (Complaint, *Securities and Exchange Commission v. Edward DiMaria and Matthew Gamsey*, 2015). It was also apparent that after this one singular quarter of inflationary net operating income, sustaining the fraud was going to get perpetually more difficult as noted through the SEC “his instructions to try and persuade the analysts following Bankrate’s stock to bring their estimates for the Third

Quarter down ‘but don’t worry them’” (Complaint, *United States of American v. Edward DiMaria*, 2017), ‘they could not ‘push’ the analysts ‘more without getting them worried’” (Complaint, *United States of American v. Edward DiMaria*, 2017), “Calls went well now I think maybe we should have widened the range further on the downside to give us more room, damn” (Complaint, *United States of American v. Edward DiMaria*, 2017). As the SEC and DOJ documents outline, DiMaria did precisely what was documented in the indictment paperwork and admitted to it in open court. After DiMaria took the guilty plea, the defense prepared a slew of supportive documentation to demonstrate that DiMaria was a good person, not financially driven in the same way as the ‘bad’ fraudsters and while it was financially motivated, it was not *that bad*.

**Research conclusion.** The defense attorneys make a compelling argument that this fraud case is different than most. This is indeed true. First, the fraud only lasted one quarter. Second, while it created economic losses, it did not bring the company to default like many other fraud cases. Finally, the fraud itself was mostly just rounding errors here and there that added up to a few million dollars.

The concept of financial motivation rippled throughout not only the very early indictment documents but continued to be a verbal theme from both sets of attorneys, prosecution and defense. This was further emphasized in the financial loss number, which was in excess of \$20 million (this also represented the amount of restitution due from DiMaria<sup>9</sup>). In sum, and considering all the facts, a 10-year prison sentence appears to match the implication of the true financial measure of the fraud, further suggesting financial motivation was on the mind of the judge.

Secondarily, the corporate *tone* that DiMaria set at Bankrate adds some additional questions. While it is for obvious reasons, the personal attestations of DiMaria's character are in stark contrast to the corporate culture that DiMaria appeared to exhibit at the corporation. This culture is not merely speculation; the internal email dialogue confirms someone who was thoroughly a tyrant inside the corporate walls. However, it does put into question if this was a top to bottom issue, or simply an issue at the CFO level. As such, there is the potential that corporate culture was at play as it relates to CFO fraud motivation. Furthering this idea, the CFO may have received top-level CEO / Board pressure to ensure the numbers matched analyst expectations, which correspondingly trickled down.

#### **Gibson (Older, Male, Education Level Unknown) – Wilmington Bank**

***Background on the case.*** David Gibson served as the chief financial officer (CFO) of Wilmington Bank from 2002 to 2011. During the years of 2009 and 2010, at the point where the economy was extremely fragile and the banking industry was suffering large losses due to the housing market, Wilmington and several bank executives, including Gibson, participated in a collusive fraud involving the manipulation of troubled loans. This fraud placed known troubled loans into categories on the financial statements suggesting that the loans were current, accruing interest and collectible. Bank executives knew this was not the case and made best efforts to conceal this fact to shareholders. Of interest and concern, Wilmington executives extended a large percentage of their loan portfolio in suggesting to the public and regulators that these loans were not past due and performing as suggested by the DOJ, "Wilmington was forced to execute a 'mass extension' of a staggering \$1.74 billion of past due and matured loans...that constituted 25% of the Bank's outstanding commercial loan portfolio" (Complaint, *United States of American v. David Gibson*, 2014), "With your input, we would like to set a reasonable

goal/game plan for getting these loans renewed/extended and allowing the system to report a true past due number” (Complaint, *United States of American v. David Gibson*, 2014), “could not recall a loan officer ever voluntarily or independently downgrading a loan” (Complaint, *United States of American v. David Gibson*, 2014), and “lenders would simply tell ...Gibson...that the borrower was a ‘good guy’ to avoid any closer review of the assigned loan risk ratings” (Complaint, *United States of American v. David Gibson*, 2014).

Adding a layer of complexity, Gibson requested a public offering for additional bank capital in early 2010 per the SEC and DOJ, “In mid-January 2010, shortly before issuing its year-end 2009 earnings release, Gibson recommended to the Bank CEO that the Bank attempt to raise additional capital by means of a public offering of stock, despite widespread internal awareness of deep problems in the Bank’s loan portfolios” (Complaint, *Securities and Exchange Commission v. David Gibson, Robert V. A. Harra, Jr., Kevyn N. Rakowski and William B. North*, 2015), and “used in connection with Wilmington’s public offering of \$274 million of common stock” (Complaint, *United States of American v. David Gibson*, 2014), despite knowing the financial issues with the bank, including the fraud. In addition, bank executives, those participating in the fraud, were awarded stock options and financial incentives based upon their performance in 2009 as noted by the SEC, “the Bank awarded Gibson stock options and approved salary increases...These awards and salary increases were based on their performance in 2009” (Complaint, *Securities and Exchange Commission v. David Gibson, Robert V. A. Harra, Jr., Kevyn N. Rakowski and William B. North*, 2015). Along with others within the bank executive suite, Gibson was found guilty by jury trial. He was sentenced to six years in prison and a \$300,000 fine. The bank was forced into a fire sale to M&T Bank during the middle months of 2010 because of the fraud stated here.

**Intermediate-level results.** Evidence at trial pointed to several fraud conclusions. Gibson appeared to understand the rules governing the classification of loans. In internal emails, he acknowledged his understanding through the following internal dialogue, “Those are past due! We need those loans where we have executed agreements...the maturity dates are known. These should be done at least 30 days in advance to allow for the documentation process to happen” (Complaint, *Securities and Exchange Commission v. David Gibson, Robert V. A. Harra, Jr., Kevyn N. Rakowski and William B. North*, 2015). Interestingly, this being the case, Gibson did not report the loan classifications appropriately, but also did not ask any bank employees to conceal this fact. Indeed, through trial testimony, no bank employees testified that they were hushed during the reporting process, “as Gibson points out, no former Bank employees testified that he or any other Defendant instructed them to conceal the practice from individuals outside the Bank.” (Complaint, *Securities and Exchange Commission v. David Gibson, Robert V. A. Harra, Jr., Kevyn N. Rakowski and William B. North*, 2015). While this fact remains undisputed, there appeared to be an internal culture shared by bank employees and especially executives; one that created a united front toward achieving financial success, which was one toward growth in the banking market as demonstrated, “the alleged conspirators ‘shared a unity of purpose,’ the intent to achieve a common goal, and an agreement to work together toward a goal” (Complaint, *Securities and Exchange Commission v. David Gibson, Robert V. A. Harra, Jr., Kevyn N. Rakowski and William B. North*, 2015). In addition to this *clan* mentality at all levels of the bank’s infrastructure, there were periodic mentions of financial motivation throughout the court documentation such as, “These accounts make clear that the Officer Defendants...were a tightly knit group of friends who operated as ‘one little clan’” (Complaint, *United States of American v. David Gibson*, 2014), “Bank executives regularly laughed about it in the dining hall”

(Complaint, *United States of American v. David Gibson*, 2014), and "The culture of the bank at the senior level was one of 'we can do no wrong, and our clients don't know anything, so we can do anything we want'" (Complaint, *United States of American v. David Gibson*, 2014). This common thread was presented throughout original complaint and court testimony/evidence.

**Research conclusion.** This case is one that connects cross-case to other banking frauds in industry but carries a different tone within the executive team. While the fraud appears largely financially motivated by the CFO, there is a lot of additional reference triangulated across various sources that suggest corporate culture was at play. Several pieces of documentation allude to a *clan* of corporate executives who were almost forthright in the fraudulent strategy they employed to keep the financials on solid ground from the standpoint of the shareholder.

Of interest and intrigue was the fact that Gibson and other executives did not take actions to hide their actions. While they did not publicly disclose to the public, which is what can elicit a more dramatic response from the SEC, they also did not try to silence internal staff as to what they were doing. Of course, silencing may take place by offering incentives for silence, but as the defense attorneys correctly pointed out, no one from within the bank, at any level, came forward to testify against Gibson that he had asked them to hush the process.

This being true, and in consideration of corporate culture, the fraud community is left with a couple of additional options. It is possible that the executive *clan* exhibited an attitude of arrogance, wherein they thought they would never get caught. This arrogance, fueled by financial motivation, is what started and allowed the fraud to continue. Alternatively, the *clan* mentality may have been fueled by an *everyone is doing it* mindset insomuch as the entire banking sector was crumbling at the time. As such, the fraud motivation may have been simply to survive the hardship and live another day.



## **Lyndon (Younger, Male, Less-Educated) – Left Behind Games (LBG)**

**Background on the case.** Troy Lyndon acted as chief executive officer and chief financial officer of Left Behind Games (LBG) from 2008 to 2012. The company produced a series of religious themed video games for distribution. With Lyndon acting as the company's main executive team, he entered into a rather simple and unsophisticated fraud with a close friend. This fraud involved a series of circular cash transactions that had no real business bearing, yet the company continued to produce financial statements that suggested it was earning revenues as shown in the SEC complaint, "The sales by LBG to Lighthouse lacked economic substance, and were essentially circular, sham transactions" (Complaint, *Securities and Exchange Commission v. Troy Lyndon and Ronald Zaucha*, 2013). Additionally, Lyndon orchestrated stock trade deals to his friend, which while they appeared to be legitimate stock purchases, were largely kicked back to LBG without disclosure of such. Lyndon and Zaucha also entered into consulting and distribution agreements that had no business substance. These agreements were additional ways for Lyndon to circle funds back into the business.

In 2009, Lyndon, acting as CEO and CFO, began to issue stock to his friend, Zaucha, in exchange for *consulting services* suggested in the SEC's court filing, "At Lyndon's direction, Zaucha promptly sold virtually all of this LBG stock, reaping approximately \$4.6M in sales proceeds. Zaucha then kicked back approximately \$3.3 to the company in three ways" (Complaint, *Securities and Exchange Commission v. Troy Lyndon and Ronald Zaucha*, 2013). Once issued, Lyndon would orchestrate a sale of the stock in the open market, thereby creating liquidity for Zaucha. However, Zaucha had to find a reasonable way to give the money back to Lyndon; he did so through fake transactions, including acquisition of inventory (which was subsequently given away), loans to the company, and other measures as stated, "Zaucha kicked

back approximately \$1 million more of his stock sale proceeds to LBG, which payments were characterized in LBG's books in a variety of ways, including as purported 'loans' and 'investments'" (Complaint, *Securities and Exchange Commission v. Troy Lyndon and Ronald Zaucha*, 2013). In another strategy to kick back money to LBG, Lyndon and Zaucha entered into a *consulting agreement for marketing* that was completely made up. As part of the deal, Lyndon could enjoy some liquidity in a company with no real revenues, according to the SEC, "Zaucha also kept portions of the proceeds of the sales, in amounts determined by Lyndon. Finally, Lyndon, who was signatory on all LBG bank accounts, simply treated corporate accounts as his own, withdrawing funds for his personal use" (Complaint, *Securities and Exchange Commission v. Troy Lyndon and Ronald Zaucha*, 2013). LBG also entered into a shoddy distribution agreement with Lighthouse Distributors, a company owned by Zaucha and recognized revenue as part of this agreement. Furthermore, the agreement was concealed to auditors according to the SEC, "Lyndon attempted to conceal Zaucha's relationship with Lighthouse by scheming with Zaucha to instruct the Lighthouse employee to sign the backdated distribution agreement on Lighthouse's behalf" (Complaint, *Securities and Exchange Commission v. Troy Lyndon and Ronald Zaucha*, 2013).

***Intermediate-level results.*** Because this case was taken to trial through the SEC, analysis for this case was performed via use of court transcripts of the SEC case, including trial testimony and trial evidence presented / available to the researcher. However, it should be noted that while trial documentation was available, in many instances, the information was incomplete as there were pages of information missing from court archives. Despite this, with these sources of information, some research conclusions were available.

It is important to note that the business transactions created by Lyndon were discussed and demonstrated to be largely fake in nature through SEC reporting, “Had the auditors known Zaucha’s representations were false, they would likely not have viewed the \$1.38 million in sales to Lighthouse as legitimate revenue” (Complaint, *Securities and Exchange Commission v. Troy Lyndon and Ronald Zaucha*, 2013), “I searched documents produced to the SEC in its investigation to determine whether or not Zaucha or Ron Zaucha Consulting ever submitted invoices to LBG for providing consulting services. I located no such invoices” (Complaint, *Securities and Exchange Commission v. Troy Lyndon and Ronald Zaucha*, 2013), and direct correspondence, “I didn’t respond to your text because I didn’t want a record of the meeting. As for the funds, \$10k for each of us personally (if you remember),” “Yes, I did remember that part ☺” (Complaint, *Securities and Exchange Commission v. Troy Lyndon and Ronald Zaucha*, 2013). It is also the case that Lyndon controlled every aspect of the company, including the company’s bank accounts and financial transactions as demonstrated through email records, “you are holding funds owed to the company, as we both know, in the event your taxes are higher than expected” (Complaint, *Securities and Exchange Commission v. Troy Lyndon and Ronald Zaucha*, 2013). Lyndon acted as a lone wolf in the transactions of the company, and although he did so with a friend, that friend had no company ownership or loyalty to Lyndon as a businessman. As such, the researcher can assume little or no pressure/coercion from outside parties as a key motivation for the fraud. This case ended with a guilty verdict and a summary judgment of \$3.6 million in fines and penalties.

**Research conclusion.** Through documentation of this case, the fraud motivation is largely unspoken. Through the SEC complaint documentation, there is certainly some reference to financial motivation as the main driver in the suggestion that ill-gotten gains from stock

purchases were kicked back and used for personal gain. The SEC documents this as follows, “Zaucha also kept portions of the proceeds of the sales, in amounts determined by Lyndon. Finally, Lyndon, who was signatory on all LBG bank accounts, simply treated corporate accounts as his own, withdrawing funds for his personal use” (Complaint, *Securities and Exchange Commission v. Troy Lyndon and Ronald Zaucha*, 2013). This is the only reference to financial motivation by the CFO in this case, although trial transcripts were largely driven toward evidence that a crime was committed and the defendant, even to this day, denies the allegations.

In fact, the CFO went to great lengths to declare his innocence and file a lawsuit against the United States government for Federal tort claims. This claim as well as appeal documentation and the CFO’s personal website ([www.troylyndon.us/sec.html](http://www.troylyndon.us/sec.html)) gives some doubt as to his mental stability, which may be also be taken into consideration regarding the CFO’s motivation. In sum, this case appears to be financially motivated; however, there may be other factors at play, including the mental capacity of the CFO to conduct normal business transactions.

### **Malone (Younger, Female, Education Level Unknown) – Gepeco, Limited**

**Background on the case.** Trish Malone served as chief financial officer (CFO) of Gepeco, Limited (Gepeco) from 2013 until later in 2014 when the company was suspended from trading. The company purported to specialize in leasing equipment and performed a series of reverse mergers with other companies over the years. Malone is among a long list of defendants named in an indictment by the SEC for what is commonly referred to as a *pump and dump* scheme; one in which a company fraudulently *pumps* or inflates the price of stock and then *dumps* a quantity of stock into the market. This stock is often valueless. Malone, through her access to bank accounts and funds transfers, was responsible for the movement into and out of accounts for

Gepco. The SEC documentation alludes to the fact that Malone was instructed to perform these banking functions with her role as CFO although the documentation suggests she was forced to do so, “Engelbrecht caused Malone” (Complaint, *Securities and Exchange Commission v. Jason Cope et al*, 2015), “Engelbrecht has caused Gepco, through Malone, to issue and transfer more than 38 million shares of restricted common stock” (Complaint, *Securities and Exchange Commission v. Jason Cope et al*, 2015), and “Malone, acting at Engelbrecht’s direction, authorized Gepco’s transfer agent” (Complaint, *Securities and Exchange Commission v. Jason Cope et al*, 2015). Malone settled the charges with the SEC in exchange for her testimony in the Talman Harris trial. She was ordered to pay \$600,000 in penalties and ill-gotten gains based on her part in the fraud as stated, “defendant is liable for disgorgement of \$394,741.24, representing profits gained as a result of the conduct alleged...shall satisfy this obligation by paying \$600,998.74 to the Securities and Exchange Commission” (Complaint, *Securities and Exchange Commission v. Jason Cope et al*, 2015).

**Intermediate-level results.** Through direct and indirect trial testimony at the Talman trial, witnesses were consistent in testimony that Malone acted within a limited capacity wherein she was told to create bank transactions and acted within the interest of intimidating leaders in the organization through statements such as, “I had authority with the bank, but I would never have done anything without his direction” (Complaint, *Securities and Exchange Commission v. Jason Cope et al*, 2015), “Because it was entirely his funds and everything was done at his direction. Nothing was done not at his direction” (Complaint, *Securities and Exchange Commission v. Jason Cope et al*, 2015), “I didn’t know exactly what their position was. I knew they had something to do in the financial field, but I didn’t know their exact positions” (Complaint, *Securities and Exchange Commission v. Jason Cope et al*, 2015), “He’s a very demanding

person” (*Securities and Exchange Commission v. Jason Cope et al*, 2015), and “You didn’t ever not comply with his directions. You always complied with his directions” (Complaint, *Securities and Exchange Commission v. Jason Cope et al*, 2015). However, because of her position, Malone did receive compensation and stock in the various companies for which she did financial work, including Gepco. These benefits as acting CFO were reflected in the financial penalty stated above.

**Research conclusion.** Through both the original SEC indictment as well as trial testimony, there is a consistent theme that the SEC largely included the CFO in this case because of her capital gains for holding stock in the companies deemed to be fraudulent. However, as it relates to Malone’s motivation in the fraud itself, it appears she was mostly complacent in her actions. There is strong implication that Malone was mostly caught in the crossfire of this corporate fraud. She was portrayed, by herself and another third party, as mostly an administrative person who did as she was told. This was suggested in her testimony through the CEO's aggressive actions/words and further suggested when the CEO testified that Ms. Malone did whatever he commanded. The research conclusion is that the *CFO* succumbed to CEO pressure and intimidation as her motivation for committing fraud as well as general complacency in what equated to largely a *bookkeeper* role with a CFO title.

### **Roth (Older, Male, Less-Educated) – ContinuityX Solutions**

**Background on the case.** Anthony Roth served as chief financial officer (CFO) for about 18 months between 2011 and 2012 when he resigned his positions with ContinuityX Solutions, Inc. ContinuityX purported itself as a seller of online information technology management services. ContinuityX, from 2011 to 2012 reported revenues of \$27 million, for which 99% was fraudulent or fictitious. Based upon these reported revenues, ContinuityX’s CFO and CEO

further raised capital through a bond offering, contributing substantially to cash flows for this time period.

To pull off the scam, the CEO and CFO entered into commission agreements with several companies, including AT&T as stated, “AT&T agreed to pay the entire commission to ContinuityX after AT&T accepted a customer order” (Complaint, *Securities and Exchange Commission v. David Godwin and Anthony Roth*, 2015). These agreements typically provided ContinuityX with sales commissions for selling the target company’s products and services to another company. In parallel and without disclosing, ContinuityX would also locate *straw buyers* for which they would market products and services in order to defraud companies such as AT&T. Roth and his co-conspirator would locate companies to *purchase* services and promise them part of the commission stream to participate. These companies had no use for the products and/or could not afford them as the SEC mentions, “straw buyers never used, paid for, or resold the internet services. One straw buyer described his company’s role in the transaction as being a ‘beard,’ meaning his company served to disguise the fraudulent nature of the arrangement” (Complaint, *Securities and Exchange Commission v. David Godwin and Anthony Roth*, 2015), and “Aside from not intending to pay for the services, the straw buyer could not afford the services they purchased. In some cases, the straw buyer agreed to purchase internet services that exceeded their own net worth” (Complaint, *Securities and Exchange Commission v. David Godwin and Anthony Roth*, 2015). When necessary, Roth participated in creating false documentation to aid the straw buyers in passing credit exams from AT&T and other similar customers by, “Roth also prepared and submitted fake financial statements to AT&T to demonstrate the straw buyer’s supposed creditworthiness” (Complaint, *Securities and Exchange*

*Commission v. David Godwin and Anthony Roth, 2015*). Roth went too far as to use one of his own companies, controlled by himself, as a straw buyer.

The final pillar to this fraud involved the company's private bond offering, for which they used the revenue figures of fictitious commissions as the basis as explained, "ContinuityX sold approximately \$6.9 million in bonds to at least 31 investors. The proceeds from the bond offering made up approximately 65% of all ContinuityX's incoming cash" (Complaint, *Securities and Exchange Commission v. David Godwin and Anthony Roth, 2015*). ContinuityX sold millions in bonds to a few dozen investors up until declaring bankruptcy in 2013. Prior to this point, Roth had resigned as CFO.

***Intermediate-level results.*** Some of the overtones of the original filings as well as later paperwork upon Roth's confession and plea deal allude to the CEO directing his actions while several other inferences are made to Roth profiting financially for his fraudulent efforts through statements such as, "At the direction of co-defendant Godwin, defendant prepared the financial statements without the benefit of any factual data" (Complaint, *Securities and Exchange Commission v. David Godwin and Anthony Roth, 2015*), "A primary reason Godwin and Roth concocted the Straw Buyer Transactions and Fictitious Transactions was to enrich themselves" (Complaint, *Securities and Exchange Commission v. David Godwin and Anthony Roth, 2015*), "Godwin and Roth received salaries, bonuses and commissions from ContinuityX. The amount of compensation they were paid each year was based in substantial part on commissions generated from the Straw Buyer Transactions and Fictitious Transactions" (Complaint, *Securities and Exchange Commission v. David Godwin and Anthony Roth, 2015*), and "shortly after he left the company, Roth sold 4,446,675 shares of ContinuityX stock for a net profit of \$456,098" (Complaint, *Securities and Exchange Commission v. David Godwin and Anthony Roth, 2015*).



Roth opted to accept a plea deal in exchange for witness testimony against ContinuityX's CEO and salesperson. Further documentation suggests that Roth was mostly unaware of the fraudulent actions of the CEO and that once he discovered the company was mostly based upon fake sales revenues, he departed the company through SEC statements such as, "defendant realized that co-defendant Godwin's business strategy for ContinuityX was based on false assurances to defendant and the investors in ContinuityX" (Complaint, *Securities and Exchange Commission v. David Godwin and Anthony Roth*, 2015), "Co-defendant Godwin was not signing agreements with companies willing and able to serve as the ultimate end-users of the goods and services provided" (Complaint, *Securities and Exchange Commission v. David Godwin and Anthony Roth*, 2015), and "Defendant learned that...invoices for services were not being paid by ContinuityX, including a company operated by defendant, despite co-defendant Godwin's assurance to the defendant...that they would be paid" (Complaint, *Securities and Exchange Commission v. David Godwin and Anthony Roth*, 2015).

**Research conclusion.** The progression of this fraud case would lead a reader to conclude that CEO Godwin was the true *bad guy* in this case. In fact, the DOJ complaint continues to layer on additional tactics the CEO used to continue his fraudulent actions as shown by the DOJ, "David Godwin, in order to conceal the fraudulent nature...created an email that purported to be from a Telecommunications Company" (Complaint, *Securities and Exchange Commission v. David Godwin and Anthony Roth*, 2015). This, along with the SEC plea documentation is a convenient time for the government to begin backpedaling away from the CFO as its main culprit, and indeed it may be true that the CEO is the bad guy, but that does not explain the financial gain received from Roth.

There are components of the fraud story that may suggest CEO pressure was a motivation of the fraud. In looking at the fraud at a macro level, the CFO did indeed resign, while the CEO continued to man the sinking ship and remained until the company defaulted. Additionally, the CEO took a large salary between the time the CFO resigned and when the company filed bankruptcy.

That said, it would be difficult to explain how the CFO did not benefit financially, particularly when one of the straw buyers was his own company. To suggest that the CFO thought the entire business was legitimate up until he resigned seems far-fetched, suggesting fraud motivation was, at least in part, a factor. Minimally, the CFO has a fiduciary responsibility to ensure reported revenues are, in fact, real revenues. Given 99% of the company's revenues were fake, it would likely not place the CFO in a helpless position in later saying he did not know about it.

**Sabol (Younger, Female, More-Educated) – Commonwealth Bankshares, Inc.**

*Background on the case.* Cynthia Sabol, CPA, served as Commonwealth Bankshares, Inc CFO from 2004 to 2011. In 2008, Commonwealth, through actions from Sabol as well as the bank's CEO and a commercial lender, participated in a series of accounting irregularities to prop up the bank's financial position. The three participants conducted a series of activities to give a false appearance to investors that the bank's balance sheet was strong when, in fact, it was much weaker than anyone realized, given the financial crisis. This was completed through a series of common techniques to hide assets which should be devalued or written down on the balance sheet. Sabol and co-conspirators participated in a series of events to inaccurately reporting financial results to the investing public. Sabol was also exclusively responsible for the internal

controls framework of the organization and held dual responsibility in proper disclosures for the bank as well as signing off on quarterly and annual financial statements.

***Intermediate-level results.*** Through post mortem investigation, it was discovered that Commonwealth participated in a variety of activities to overstate its company assets. This was achieved through materially understating allowance for loan and lease losses (ALLL), materially underreporting non-performing loans, materially understating and underreporting its other real estate owned (OREO) as stated by the SEC, “between in or about November 6, 2008 and August 16, 2010, Commonwealth materially understated on its balance sheet its allowance for loan and lease losses (the “ALLL”), materially underreported Commonwealth’s non-performing loans, and materially understated and underreported its other real estate owned (OREO)” (Complaint, *Securities and Exchange Commission v. Edward J. Woodard, Jr., Cynthia A. Sabol and Stephen G. Fields*, 2013). Additionally, Commonwealth executives provided misleading or inaccurate statements to the investing public about the bank’s asset quality, underwriting practices, and credit monitoring, which deviated from their public claims. According to SEC filings, Sabol was aware of the fraudulent internal practices, how they were concealed, and the effect on the financial statements and was even responsible for large portions of the functions. These SEC statements support those facts, “Sabol knew, or was reckless in not knowing...were experiencing financial difficulties...and that Fields was taking steps to mask this fact” (Complaint, *Securities and Exchange Commission v. Edward J. Woodard, Jr., Cynthia A. Sabol and Stephen G. Fields*, 2013), “at a meeting Sabol attended, Woodard and the Board approved the classification of the PLV loan as non-accrual...also approved classifying the PLV loan as a ‘substandard non-accrual’ loan” (Complaint, *Securities and Exchange Commission v. Edward J. Woodard, Jr., Cynthia A. Sabol and Stephen G. Fields*, 2013), “the internal auditor sent Woodard and Sabol a

report which highlighted the ‘key controls’ exceptions had increased more than sevenfold and ‘many of these exceptions include missing approvals’ (Complaint, *Securities and Exchange Commission v. Edward J. Woodard, Jr., Cynthia A. Sabol and Stephen G. Fields*, 2013), “Sabol oversaw and was responsible for the calculation and accuracy of the ALLL” (Complaint, *Securities and Exchange Commission v. Edward J. Woodard, Jr., Cynthia A. Sabol and Stephen G. Fields*, 2013), and “Woodard and Sabol were ultimately responsible for designing, implementing and monitoring Commonwealth’s internal accounting controls” (Complaint, *Securities and Exchange Commission v. Edward J. Woodard, Jr., Cynthia A. Sabol and Stephen G. Fields*, 2013). As CFO, Sabol had primary responsibility for internal controls infrastructure, financial reporting, including disclosures and other key financial roles.

While the SEC complaint does not directly implicate Sabol as the person who created and orchestrated the fraud, the filings do suggest Sabol was aware of and participated in discussions where decisions were made about classification of assets. The complaint is silent as to Sabol’s participation or approval of the accounting measures.

While the original SEC complaint documents certainly portrayed Cynthia Sabol as a guilty person, with a fair amount of detail as to the crime, the reality of the conclusion of the case suggests otherwise. Sabol was released from all lawsuits, including that of the SEC and DOJ and while she was indicted, she was never formally charged with anything. At the conclusion of the case, she was charged a civil penalty of \$55,000 and settled the remainder of the fraud. However, the penalty for the other two named parties in the SEC indictment suggest that the fraud case was viewed as extremely severe, as Woodard received 23 years and Fields 17 years in prison while Sabol continued to deny wrongdoing. While not explicit in the court documentation, the

Department of Justice (DOJ) hinted that the motivations Woodard and Fields (as well as others charged) were financially motivated.

**Research conclusion.** The buildup and ultimate conclusion of this case from the perspective of the CFO left some doubt as to her ultimate participation in the crime. Based on past fraud cases studied for this research paper, civil penalties are rarely as low as \$55,000 for someone who has actively participated in a crime, unless there are other unusual circumstances of the case. That being the case, a civil penalty does implicate that the CFO was responsible in the fraud, or she would not have paid any penalty and been completely relieved of any wrongdoing. She also would not have been stripped of her accounting licensure and been forbidden to practice in an accounting role for a period of five years.

That said, the harshness of the penalties against the other two originally named in the SEC filing suggests the fraud did take place, was pervasive and severe and created tremendous losses for the public. A sentence of 23 and 17 years, respectively, is a massive punishment. And yet, the CFO was only penalized \$55,000 in civil payments. These wide ranges of penalties appear to be at odds.

Based on the facts presented in the case, it is not possible to conclude that the CFO was outright innocent in the fraud. The civil penalty suggests this is not the case and the fact that the CFO agreed or was not prepared to take the matter to trial to completely exonerate herself of the charges suggests there was guilt also. Just the same, a small civil penalty without formal charges does tell a story.

There was a very small implication by the DOJ that this was financially motivated by those who were formally charged and jailed. That was the only mention to financial incentive detected through all the court and media records. The language felt boilerplate as well. While

financial motivation cannot be ruled out, particularly for those who were held responsible (CEO / loan officer), evidence does not suggest the fraud was financially motivated by the CFO.

Throughout the SEC complaint document, there is reference to the CFO's participation in meetings where decisions were made by the CEO and board. There is not reference to her active participation or formal vote on any matters. Given this, one conclusion may be internal pressure to go along with the crimes. This appears to be the strongest likelihood. In sum, internal pressure by peers (CEO, Board, loan officer) appears to be the most likely fraud motivation in this case.

### **Sanders (Older, Male, Lesser-Educated) – Dewey & LeBoeuf (Dewey)**

**Background on the case.** Joel Sanders was acting chief financial officer (CFO) of Dewey & LeBoeuf (Dewey) from its merger in 2007 until the company saw its spectacular bankruptcy in 2012. During this time, Sanders, along with several others on the company executive team, participated in a large-scale, pervasive and bold set of fraudulent actions that overstated the results of the company. The corporate fraud began as a small event, prompted by the executive's desire to remain within bank covenants. In late 2008, Sanders warned that the company was in financial straits because of revenue issues as mentioned by the SEC, "CFO Sanders...informed...that the firm was in serious jeopardy of breaching the Cash Flow Covenant because the firm's revenue had dried up" (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014) and internal email stated as, "That's precisely what I'm concerned about. The banks will pull our lines in a heartbeat if we don't satisfy covenants" (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014). Because of this, in the final hours of 2008, a group of collusive fraudsters hatched a plan to bring the company right up to the bank covenant requirements while openly communicating on what they had done through email such as, "reverse write-offs for disbursements, which had previously been deemed uncollectible

and totaled \$3.8 million” (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014), “Steve’s copy includes a list of accounting entries made for 2008” (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014), “Great job dude. We kicked ass! Time to get paid” (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014), “Hey man, I don’t know where you come up with some of this stuff, but you saved the day. It’s been a rough year but it’s been damn good. Nice work dude. Let’s get paid” (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014), “I assume you knew this but just in case. Can you find another clueless auditor for next year?” (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014) followed by “That’s the plan. Worked perfect for this year” (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014). Even while employees bragged through email, some became ever more concerned about scrutiny from auditors with statements such as, “Before we close I think we should writeoff at least 1.2 million of the amex charges from Joel’s amex that have been sitting with us in 1211 for so long. I don’t see how we’ll get past the auditors another year” (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014), and “I don’t know anything about [the contracts] and I don’t want to cook the books anymore. We need to stop doing that” (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014). As the fraud continued, executives continued leaving breadcrumbs demonstrating they were documenting not only the fraud itself, but their own payout each time they did with a statement such as, “Keep in mind though that at these levels we will not have cash to pay the partners by Jan 31 since \$25M is fake income” (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014). For 2008, Dewey misstated its net profit by \$36 million, for which \$31 million was used to meet its cash flow covenant.

However, for 2009, the problem only intensified, as sales continued to struggle, plus executives had to find a way to offset the 2008 fraud. While documenting a golden parachute for the executives involved in the scam through SEC references, “Davis approved...receipt of personal lines of credit from Dewey’s bank, backed by updated employment agreements that guaranteed their compensation even if Dewey should ‘enter into dissolution’” (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014), Dewey renegotiated their bank covenant value, while continuing to book fraudulent entries for 2009. Further, at the action of the Board of Directors, Dewey used the fraudulent financial statements to create a bond offering of \$150 million.

***Intermediate-level results.*** After declaring a mistrial during Sanders’ first indictment, Sanders was found guilty on three criminal counts approximately two years later. One of the other co-conspirators was found not guilty in the same trial. In an interesting twist, Sanders received no jail time and was fine \$1 million in restitution for his conviction. Through a series of twists, however, Sanders was jailed for not paying his first installment of \$333,333. In court documentation filed, Sanders exhibited more than enough liquid assets to pay this amount, along with his annual salary of \$375k+. Sander’s lawyers argued for the fine to be dropped through a series of excuses stating, “Defendant Sanders has no assets that he cannot sell” (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014) and “Defendant Sanders has taken care of and provided for his family as the principal wage-earner” (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014), but the judge disagreed due, in part, to the prosecution’s scathing response, “admitting to assets of \$1.5M and income of \$375,000 per year, but claiming that his ‘dire financial circumstances’” (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014), “Sanders is free to support any adult



he chooses, but he is not free to prioritize doing so over satisfying the conditions of his sentence” (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014), “Sanders is making lease payments on a 2018 Audi A3 Premium and car payments on a 2017 Mercedes Benz C300...Sanders has failed to explain why he is maintaining two luxury cars at a time when he knows he has an outstanding fine obligation as part of his sentence” (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014), and “He seems to believe there are and should be two different sets of rules of criminal justice, one for rich people like him, and one for all others” (Complaint, *Securities and Exchange Commission v. Steven H. Davis et al*, 2014). In another interesting twist, Sanders’ employer opted to pay his fine to get him out of jail and satisfy his sentence.

**Research conclusion.** It appears there are likely a number of CFO motivations at play here. At least in the initial stages, there appears a high degree of executive and therefore CFO pressure to make financial results that keep the organization solvent with bank lines of credit intact. In fact, the SEC precisely acknowledges the reason the fraud started to begin with, as executives became aware of the bank line issues and opted to remediate the issue at the final hour. This appears well documented within the evidence.

However, there also appears a secondary undertow as well as a turning point, where the fraud became almost a game to executives, including the CFO. From the outside looking in, the fraud eventually became something bigger; something the executives appeared to almost enjoy trying to trick and deceive. In addition, based on the internal emails, they also appeared to flip a switch toward greed quickly.

This point seems even more emphasized post trial and conviction. Having gotten off with no jail time and a slap on the wrist, Sanders continues to try and play the legal system by

defaulting on his first series of restitution payments, citing severe financial hardship. Yet as the prosecution points out, Sanders is living anything but a frugal life, with oceanfront property, two luxury cars, and is making almost \$400k per year in a salary, all while supporting a wife and grown children. The prosecution would have you believe, and it is hard to deny, that Sanders is financially motivated to live the high life, even at the expense of paying back his sentence obligation.

### **Schwarz (Younger, Male, Less-Educated) – Cay Clubs**

*Background on the case.* David Schwarz served as CFO of Cay Clubs resorts, a company that claimed to be in the real estate development industry. He operated as CFO from 2004 until early 2009. According to its marketing materials, Cay Clubs was in the business of financing the purchase of properties, renovation of the units and further development of luxury resorts with funds raised from investors. However, Schwarz, in collusion with several other executives, fraudulently misrepresented what the company actually did and through deceptive marketing and marginally legal leaseback agreements, Schwarz and co-conspirators orchestrated what turned into an illegal Ponzi scheme as noted by the SEC, “Schwarz began using new investors’ contributions to pay earlier investors their purported returns in Ponzi scheme fashion” (Complaint, *Securities and Exchange Commission v. Barry J. Graham et al*, 2013) and “Schwarz knew the funds sent to investors were not investment returns because they controlled Cay Clubs’ bank accounts” (Complaint, *Securities and Exchange Commission v. Barry J. Graham et al*, 2013). Schwarz, as CFO, maintained control of 150+ bank accounts for which these funds were laundered, and he helped to orchestrate the business marketing, sales transactions and money flows that allowed the fraud to take place. In addition, Schwarz (and co-conspirators) paid themselves high salaries to live lavish lifestyles, including homes, vehicles, planes, boats, and

club memberships as documented through the SEC, “It was the purpose of the conspiracy for the defendant and his conspirators to unlawfully enrich themselves...diverting fraud proceeds for their person use and benefit” (Complaint, *Securities and Exchange Commission v. Barry J. Graham et al*, 2013), “Clark and Schwarz, based on their own accounting, obtained more than \$28 million in proceeds from Cay Clubs, including salary payments, payments to third parties including cash to close condominium unit purchases, cash transfers, and credit card payments” (Complaint, *Securities and Exchange Commission v. Barry J. Graham et al*, 2013). Further to the Ponzi scheme transactions, Schwarz and co-conspirators falsified loan documents and created down payments from people who did not exist. Finally, Schwarz defrauded the United States Treasury by failing to file or filing false tax documentation as stated, “failing to issue any W-2 or 1099-MISC...failing to file any individual tax return...filing false individual tax returns for tax years 2005 through 2007” (Complaint, *United States of America v. David W. Schwarz*, 2016).

***Intermediate-level results.*** During David Schwarz’ early days (prior to Cay Clubs), he worked in the accounting industry and various other ventures, notably, a particular real estate venture that was very lucrative. However, after a good stretch of profitable employment, Schwarz’ wife fell ill, and he was unemployed for more than four years. Schwarz’ trial testimony provided inferences to pressure from colleagues to keep up the fraudulent acts or an unawareness of the actions taking place within the bank accounts he controlled, while admitting guilt on the tax evasion through statements such as, “I was heavily pressured” (Complaint, *Securities and Exchange Commission v. Barry J. Graham et al*, 2013), “I had no control whatsoever over those accounts, except I’ve seen five checks where I signed” (Complaint, *Securities and Exchange Commission v. Barry J. Graham et al*, 2013), and “I’ve never made any bones of the fact that I owed tax...I absolutely owe taxes on it” (Complaint, *Securities and Exchange Commission v.*

*Barry J. Graham et al, 2013*). However, later court documents filed by the Department of Justice (DOJ) reveal pieces of evidence presented by the prosecution, signaling both the types of things acquired because of the fraud as well as the way in which executives cheated investors to gain these funds. Additionally, Schwarz was forced back to the witness stand during arraignment, wherein the judge sided with the government noting Schwarz and his wife were employable. Schwarz was found guilty on four of eight counts he was convicted of and sentenced to 480 months in prison and restitution of \$1,513,030.

**Research conclusion.** While the CFO chooses a variety of defenses during his direct examination (cross examination was not even considered in this case), including blaming others, selective memory, people (IRS) are being unfair, pressure from others and he was set up, there are several pieces of evidence that strongly suggests financial motivation / greed were the drivers of this fraud. This appears supported by a previous *highflyer* lifestyle, then a financial hardship, followed by a reentry into the rich and wealthy lifestyle. Despite the CFO's interest in blaming the CEO and suggesting he was a helpless victim, the IRS' claim that he did not report or pay taxes further suggests a persona of flying above the law. It would appear, based on the verdict and sentence that the court system largely agreed as well.

### **Smyth (Older, Male, Less-Educated) – KIT Digital**

**Background on the case.** Robin Smyth acted as CFO for KIT Digital, a provider of end-to-end video asset management software and related services. Smyth, in conjunction with CEO Tuzman, participated in a series of fraudulent schemes to inject capital into the company as well as illegally recognize revenue throughout the company's history. The first scheme noted in the DOJ documentation is related to creating fraudulent stock transactions for the company stock by purchasing and selling shares in the market with company and personal funds. These trades

created false demand/activity in the market and subsequently drove the price of the stock up artificially. While Tuzman is mostly named as the primary party in this fraudulent act, Smyth is briefly mentioned as a participant in issuing bank wires.

Outside of the illegal manipulation of company stock price, which was mostly blamed on the CEO, Smyth additionally participated in a series of financial transactions that were fraudulent in nature as the DOJ points out, “The defendants knew that KITD had sold perpetual licenses for software that, at the time of sale, was not complete and required substantial future development” (Complaint, *United States of America v. Kaleil Isaza Tuzman and Robin Smyth*, 2015). Further, Smyth worked with clients to confirm with auditors that they owed the amount booked to revenue according to the DOJ, “Smyth directed Employee-1 to ask the TCN CEO to confirm falsely and in writing that KITD had delivered VX Manager to TCN on June 22, 2010” (Complaint, *United States of America v. Kaleil Isaza Tuzman and Robin Smyth*, 2015).

At the same time, KITD had difficulties in delivering the services for the prematurely booked revenue. Smyth recognized that the receivable could not exist past one year of recognizing revenue and informed Tuzman of this. Smyth then, at the direction of Tuzman, created a *loan agreement* from a bank to the customer, took KITD specific funds from an escrow account and routed funds to the customer, who in turn routed the money back to KITD to pay off the receivable as stated, “In the loan agreement, which Smyth prepared at Tuzman’s direction, this repayment date was tethered to an unspecified point in the future called ‘product delivery’” (Complaint, *United States of America v. Kaleil Isaza Tuzman and Robin Smyth*, 2015). Similar concepts of premature revenue recognition and round tripping (using company funds to pay for its own receivables) continued to escalate for Smyth as the concealment continued as discussed in an internal email, “We cannot put restructuring in like this as auditors would expect an

accounting for it if they see this. There really can be no external view” (Complaint, *United States of America v. Kaleil Isaza Tuzman and Robin Smyth*, 2015). The preponderance of the fraudulent behavior was for financial benefit, according to the SEC, “During the relevant time period, Smyth was also awarded a cash bonus and performance-contingent stock” (Complaint, *Securities and Exchange Commission v. Keleil Isaza Tuzman and Robin Smyth*, 2015).

**Intermediate-level results.** During the process of convicting him for his actions, Smyth agreed to a plea agreement (guilty of conspiracy to commit securities fraud) in exchange for testifying at the Tuzman trial. In review of the documentation of this fraud during the trial phase, it appears the government was more interested in getting a conviction for Tuzman and his other co-conspirator, Omar Amanat, than they were for Smyth. Interestingly, during trial, Smyth was asked specifically why he participated in the fraud (after he explained the specific elements of it). He noted that he was asked to do it with his reason was financial, stating explicitly, “I wanted to make money, yes” (Complaint, *United States of America v. Kaleil Isaza Tuzman and Robin Smyth*, 2015). Trial testimony later revealed that Smyth made \$350,000 in annual base compensation and approximately \$900,000 in bonus and stock compensation. There were also undertones of CEO pressure during Smyth’s testimony and internal guilt as the fraud progressed and got more complex. Through cross-examination, we are left somewhat at odds as to the true nature of CEO pressure for committing the fraud.

**Research conclusion.** In reviewing the research and trial transcripts, there appears to be a variety of CFO fraud motivations for this case, including a progression toward each of them. It appears plausible that this fraud was initially motivated primarily as financial. The CFO enjoyed doing what was necessary to cash the bonus and stock option checks at the end of the year. However, as the fraud became a larger, more difficult web of lies and covering tracks, the

motivation may have gone away from being financial and turned toward CEO pressure to keep it up. As more people became involved and the financial transactions became harder to conceal, it appears the CFO felt the heat rise dramatically, wherein money was no longer the motivator. At that stage, CEO pressure appeared front and center, as described in some of Smyth's personal diary excerpts. As such, the research conclusion is that the CFO fraud motivation was multi-pronged: financial and CEO pressure.

### **Toll (Older, Male, More-Educated) – InnoVida**

*Background on the case.* Craig Toll served as CFO of InnoVida, a company whose primary business was to manufacture building panels used in the construction of homes and similar structures to build resistance to fires and hurricanes. Between 2007 and 2010, Toll, along with the company's CEO, Osorio, designed and continued a multi-layered fraud scheme involving two sets financial statements. The first set of financial statements was presented to InnoVida's external auditors and accurately represented the financial status of the company, which was never profitable throughout its history. The second set of financial statements was presented to the board of directors as well as high wealth investors to inject capital into the company. These financial statements were not Generally Accepted Accounting Principles (GAAP) compliant, represented that the company was highly profitable using illegal revenue recognition techniques, and were further used to solicit ongoing investment funds and attract big names (i. e. Jeb Bush) to the board of directors.

Furthermore, Toll and Ororio applied for, solicited and were successful in receiving partial government loans through use of similar production of fake or false documentation. In some instances, Toll doctored invoices sent to the government to demonstrate certain expenditures had been completed when in truth, the monies had been siphoned to Osorio for

lavish purchases. Monies received from newer investors through fraudulent financial reporting were used to pay back older investors in a Ponzi-like scheme while other business funds were used to fund a lavish lifestyle, particularly for Osorio (CEO). For Toll's part in the fraud, he collected a respectable salary; however, he did not receive company stock options or a bonus for his efforts. Craig Toll, CFO, was found guilty by jury trial and sentenced to four years in prison and a \$3.3 million restitution.

***Intermediate-level results.*** Because this case was taken to trial through the Department of Justice (DOJ), analysis for this case was performed via use of the original Securities and Exchange (DOJ) complaint, several pieces of DOJ pretrial as well as in trial documents, including the appeal documentation, which gave more specific information about the case through the eyes of the prevailing judge, as well as DOJ trial transcripts and several media reports. With all these sources combined through interpretation of keyword/key phrase review, several results emerge with triangulation achieved.

First, the CFO was very likely influenced by a CEO who appeared financially motivated even beyond that of the CFO. In fact, the CEO extorted large sums of ill-gotten monies from the company to purchase lavish items, while there is no evidence or suggestion, even by the prosecution, that the CFO did this. Furthermore, the CFO did not own stock; therefore, any financial gains from the company did not provide the CFO additional motivation to commit fraud as stated by Toll's defense attorney, "[Toll] never had one nickel interest in the company" (Complaint, *United States of America v. Claudio Eleazar Osorio and Craig Stanley Toll*, 2012) and "They're not even going to be able to tell you that \$10 of that money went to him other than in his salary" (Complaint, *United States of America v. Claudio Eleazar Osorio and Craig Stanley Toll*, 2012). Finally, court documentation suggests the CFO was purposely cut out of key



financial decisions and access to information that a CFO would normally have access to, such as bank statements and check writing ability, as the CEO as well as CEO's wife, who had no interest in the business, took hold of key financial controls.

Second, the CFO was aware of the fraud and willingly participated in it. Toll used a dual set of financial statements during his CFO tenure, whereby he shared one *real* set with the auditors and an entirely different set of financial statements to investors and the board of directors as stated by the SEC, "Toll maintained two set of financial statements and used one set to mislead investors...the main difference between the statements was how the sets recognized revenue" (Complaint, *Securities and Exchange Commission v. Innovida Holdings LLC, Claudio Osorio and Craig Toll*, 2012). The *fake* set of books lacked proper revenue recognition techniques to show the company as profitable, when, in fact, it was never profitable, according to witness testimony. Further, Toll produced fake documents when a government inquiry was made regarding use of the government loan funds, which Toll knew were false. Toll's background and work professionalism and knowledge were described per witness testimony as quite strong, further suggesting that Toll was not merely an innocent victim, but rather an informed and knowledgeable willing participant.

Finally, court testimony from the defense and lack of response to the defense's argument suggest that while Toll did participate in the fraud, he did not do so with the intent of living a lavish lifestyle. His salary was described as a plentiful; however, the true *bad guy*, as painted throughout trial was the CEO, who used ill-gotten gains for lavish items. The CFO, by contrast, was trying to make a salary in line with his desired lifestyle, which was more mainstream in nature. That said, Toll's participation in the fraud did yield him a salary for many years, most of

which would not have been possible had he not participated in a long standing fraud and lying to investors, the board of directors and the United States Government.

**Research conclusion.** Based on the above presented data and in alignment with the data presented in the table below, the research conclusion is as follows. First, the CFO was influenced based on the CEO, which included intervention by the CEO's wife, and his persistence on making financial greed the center focus of the company's ongoing fraud as stated, "Osorio's wife...became upset with Toll...she reduced both of their salaries, instructed Carness to report directly to her and tried to isolate Toll from the company" (Complaint, *United States of America v. Claudio Eleazar Osorio and Craig Stanley Toll*, 2012). The CEO went to great lengths to lure new investors into the scheme, including forming a high powered board with people such as Jeb Bush and other celebrities. The CEO was also a repeat offender of illegal acts based on media exposure of this fact.

However, the CFO participated in the multi-faceted fraud with full knowledge, education and understanding that what he was doing was illegal. In fact, the CFO was once an auditor whose job was to discover fraudulent situations such as these. The CFO participated in the fraud for reasons of financial motivation. During trial, his salary was mentioned by the prosecution but also the defense as being *decent*, "Yes, Craig got a salary. Yes, he got a decent salary" (Complaint, *United States of America v. Claudio Eleazar Osorio and Craig Stanley Toll*, 2012). This salary would not have been possible for him to continue to collect were it not for the fraud he perpetuated and continued to involve himself in. The punishment handed down through the judgment, especially jail time adds light to the severity of the fraud itself, given other studied fraud cases received only a monetary punishment.

While the CFO's motivation appears financial, this case and the facts gathered do not suggest financial motivation rose to the level of greed; living the high life or living beyond one's means as is seen in other studied CFO cases and exhibited in the CEO's lifestyle in this case as stated, "The hundreds of thousands or millions or whatever Osorio took and spent to feather his lifestyle, to live the high life, never went to Craig Toll" (Complaint, *United States of America v. Claudio Eleazar Osorio and Craig Stanley Toll*, 2012). The research conclusion related to CFO fraud motivation is still ultimately financial, but at a different (lower) level, giving rise to a different kind of variation in financially motivated frauds. Additionally, the CFO appeared to receive internal pressure from that of the CEO and the CEO's co-conspirators, particularly the CEO's spouse in participating in the fraud, and when he stepped out of bounds, was quickly brought back into compliance.

### **Research Themes**

Three key themes emerged directly related to the research question of CFO fraud motivation, with an additional four items included as additionally connecting to the fraud triangle, although more related to fraud opportunity. The themes are presented in order of their relative strength in connecting to CFO fraud motivation inasmuch as the theme tends to appear more frequently in fraud situations. Frequency of fraud motivations can be observed through triangulation in-case as well as cross-case. Data supporting these themes, including relative strength, is presented in the previously discussed appendices.

**Financial motivation.** In most of the fraud cases studied, financial motivation was present as the CFO's frequent form of motivation. Even in cases where there was less court documentation present, in-case triangulation was often present indicating financial motivation was present. The level of financial motivation varied dramatically from case to case. Financial

motivation ranged from situations where CFOs wished to make a livable income only to deliberate inflation and sale of company stock to using the corporate account as a personal bank account. Additionally, there were two cases for which financial motivation appeared to cross into outright greed. Court and media documentation demonstrated, in these cases, not just a motivation to make a living, but to extend into lavish lifestyles, while acquiring items the average person would not possess. In one case, this greed continued beyond sentencing, whereby the CFO refused to pay the first installment of financial penalty, despite having adequate assets to do so.

***Corporate culture/pressure.*** A myriad of internal cultural issues emerged as another key research theme. These culture pressures appeared to fit into three additional subcategories: overall corporate cultures, CEO generated and facilitated cultures and sub-cultures that formed by similarly minded people banding together, also known as clan culture (Kim, 2014), whereby there is a high level of collaboration and loyalty amongst a small set of internal group members. At the higher corporate-level culture, the companies themselves appeared to have certain known rules of engagement, such as condoning poor behavior, accepting certain risks or breaking the law and an inward focus on unrealistic sales growth. These corporate cultures were observed in half of the fraud cases and appeared linked to the CFO fraud motivation.

Outside of a strong corporate pull, CEOs singly provided certain cultural norms or pressures toward the CFOs. These pressures were generally brought in court testimony against the CEO in calling the CEO demanding or suggesting the CFO was under tremendous pressure from the CEO. Thematically, CEO to CFO pressure connects back to the literature review in earlier chapters.

Finally, in a couple of the CFO fraud cases, a small subset or clan culture emerged that provided motivation and pressure to CFOs to commit frauds. In the two cases noted, a strong undertow of fraudulent mindsets were present within a few individuals within an organization; a mindset that allowed fraud to begin and continue due to its collusive nature. In each of the two cases, the clan culture acted in arrogant and defiant types of ways, often acting as if they could do no wrong and would never get caught. In these cases, the CFO got caught up in the clan culture and was instrumental in the fraudulent losses of the company.

**External pressure factors.** While it is possible that internal pressures were also woven into these fraud situations, several of the studied cases experienced some kind of particular external threat or pressure that appeared to create a fraud motivation. The external threat often impacted or connected to cash flow of the business, such as a bank covenant or capital financing. They also included pressure to hit analyst expectations and being captured under a regulatory statute that would somehow impair the business. In several instances, these external pressures appeared to be the main springboard in which the CFO felt motivated to begin and, in some cases, continue the fraud. It is also worth noting that in each of the fraud cases involving this external pressure, an internal corporate pressure also resulted.

Table 1

*Demographic Data of the CFOs Within the Study*

| Name        | Age | Gender | Education | Classification |
|-------------|-----|--------|-----------|----------------|
|             |     | Common |           |                |
| Bartholomew | 45  | M      | Lesser    | Common         |
| DiMaria     | 46  | M      | Lesser    | Common         |
| Lyndon      | 44  | M      | Lesser    | Common         |
| Schwarz     | 46  | M      | Lesser    | Common         |

|         |    | Uncommon |         |          |
|---------|----|----------|---------|----------|
| Gibson  | 52 | M        | Unknown | Uncommon |
| Malone  | 38 | F        | Unknown | Uncommon |
| Roth    | 48 | M        | Lesser  | Uncommon |
| Sabol   | 45 | F        | Higher  | Uncommon |
| Sanders | 49 | M        | Lesser  | Uncommon |
| Smyth   | 56 | M        | Lesser  | Uncommon |
| Toll    | 59 | M        | Higher  | Uncommon |

Table 2

*Presentation of Demographic Classification to Key Research Themes*

| Name        | Classification | Financial | Corporate | External |
|-------------|----------------|-----------|-----------|----------|
| Common      |                |           |           |          |
| Bartholomew | Common         |           | X         | X        |
| DiMaria     | Common         | X         | X         | X        |
| Lyndon      | Common         | X         |           |          |
| Schwarz     | Common         | X         | X         |          |
| Uncommon    |                |           |           |          |
| Gibson      | Uncommon       | X         | X         | X        |
| Malone      | Uncommon       |           | X         |          |
| Roth        | Uncommon       | X         |           |          |
| Sabol       | Uncommon       |           | X         |          |
| Sanders     | Uncommon       | X         | X         | X        |
| Smyth       | Uncommon       | X         | X         |          |
| Toll        | Uncommon       | X         |           |          |

**Themes Linked to Demographics**

Table 1 above classifies the 11 CFOs researched for this study as either common (younger, male, less education) versus uncommon (any other combination) as discussed in earlier chapters. Table 2 cross tabulates each CFO's classification (common or uncommon) with the research themes noted above to the degree that research theme is present for the CFO's individual circumstance. The column heading of "Financial" connects to the "Financial

Motivation” theme, the heading of “Corporate” connects to the “Corporate Culture/Pressure” theme and the heading of “External” connects to the “External Pressure Factors” theme, as described above. This table creates a visual representation for which research themes are present for each case view. For example, the DiMaria case appears to have all three of the fraud motivation themes, while the Roth case only has financial motivation as a connected theme. The table allows the reader to briefly scan for cases in which a singular CFO had one main perceived motivation versus instances where a CFO had several likely motivations based upon research information within court records and media reports.

Table 3

*Presentation of Common CFO Demographic to Key Research Themes - Cross Case*

| Name        | Classification | Financial | Corporate | External |
|-------------|----------------|-----------|-----------|----------|
| Bartholomew | Common         |           | X         | X        |
| DiMaria     | Common         | X         | X         | X        |
| Lyndon      | Common         | X         |           |          |
| Schwarz     | Common         | X         | X         |          |

Table 4

*Presentation of Uncommon CFO Demographic to Key Research Themes - Cross Case*

| Name    | Classification | Financial | Corporate | External |
|---------|----------------|-----------|-----------|----------|
| Gibson  | Uncommon       | X         | X         | X        |
| Malone  | Uncommon       |           | X         |          |
| Roth    | Uncommon       | X         |           |          |
| Sabol   | Uncommon       |           | X         |          |
| Sanders | Uncommon       | X         | X         | X        |
| Smyth   | Uncommon       | X         | X         |          |
| Toll    | Uncommon       | X         |           |          |

Tables 3 and 4 below show the themes cross case by demographic groups of common versus uncommon. These allow the reader to study patterns and trends of research themes based on whether the CFO has common fraud demographics of younger, male and lesser-education or uncommon demographics representing any other demographic combination. Within the common CFO group, the researcher notes all three motivational themes present. In three of four cases, financial motivation and corporate culture issues appear to be at play given the information gathered about the CFO. In one of the four cases, only one theme (financial motivation) is apparent. In one of four cases, all three fraud motivations are present.

A similar outcome is present in the uncommon CFO demographic group. Each of the seven fraud cases has at least one of the research themes and all research themes connect to at least one uncommon CFO fraud circumstance. Additionally, two of the seven cases exhibit only one research theme (financial motivation) while another two of seven cases has all three research themes present.

When comparing the two above tables against one another, taking into consideration a cross-case analysis across demographic groups, no obvious patterns emerge. The fraud motivations detected through the distillation process in arriving at research themes appear to connect to both sets of demographic groups and do so quite evenly. For example, when reviewing the themes of financial motivation and corporate culture issues, this theme presents itself in 75% of the common and 71% of the uncommon cases studied. While external fraud motivation factors were less common in the uncommon demographic group, they were still present in two of seven cases. Then examining the cross-case cross-demographic information, all



fraud motivations appear present within both groups. Stated differently, there is no evidence of a fraud motivation that is present in one demographic group, but absent in the other.

### **Summary**

Chapter 4 presented data gathered in answering the study's research question: for CFOs indicted of corporate fraud, does motivation differ for CFOs with common fraud demographics (male, younger, lesser-educated) versus lesser common demographics (female, older, more highly educated, or any other combination)? Based upon the information presented above, it does not appear that fraud motivations differ between the common and uncommon fraud CFO demographics. Chapter 5 will further advance the research results through discussion, implications and recommendations.

## CHAPTER 5. DISCUSSION, IMPLICATIONS, RECOMMENDATIONS

### Summary of the Results

Historical fraud situations are often studied in context to the fraud triangle, or the tenants of fraud opportunity, pressure and rationalization (Cressey, 1953). Motivation, the intersection between pressure and rationalization, seeks to understand the reasons that people commit frauds. CFOs hold a unique position of power within most organizations, offering them a higher level of fraud opportunity. Past frauds have examined specific CFO demographics present in occupational frauds (Aier et al., 2005; Barua et al., 2010; Liu et al., 2016; Qi et al., 2018; Sun et al., 2017; Troy et al., 2011) in assigning the *common* demographic as younger and lesser-educated male. The need for this study, then, connects historical fraud with CFO demographics in understanding similarities and differences between the *common* and *uncommon* demographic groups.

Several watchdog groups, including the ACFE (Dorris, 2018), COSO (Beasley et al, 2010) and SEC (White, 2014; White, 2015; White, 2016) continuously scan the environment for instances of occupational fraud. Additionally, the SEC has oversight and legal obligations to bring fraud to the forefront as well as hold accountable those responsible for it. In the fraud arena, there are many interested parties, including investors, internal and external auditors, and regulators. Due to this interest, this study has significance to all of these interested groups insomuch as fraud can be better understood, better prevented and more quickly detected.

Considering the research study presented here, historical research was conducted detailing occupational fraud instances, including the persons responsible for it. Past literature on the demographics of those in the center of fraud circumstances was reviewed and understood, in particular those in the corporate CFO role. This literature consistently pointed to instances of

younger, lesser-educated males as the most likely to commit frauds, both individually and through collusion. The most recent literature on challenges to the fraud triangle was also carefully considered in the context of this research study. Taking into account seminal works by Cressey (1953) as well as more recent questions of the fraud triangle (Dorminey et al., 2012; Huber, 2016; Soltani, 2014), this study examined two main areas of the fraud triangle. The elements examined were the intersection between fraud pressure and rationalization, or fraud motivation. The full literature review also discussed the ways in which corporate executives interact on fraud matters, how fraud was seen across industries, how internal controls acted as a form of fraud barrier, and the larger community's interest in the fraud motivation topic, including that of the auditor.

The research methodology used for this research study was qualitative case study based on the availability of historical court transcripts and media reports connected to indicted fraud. This methodology was used as a way to mitigate risk of an inherently sensitive topic of fraud motivation, allowing publicly available secondary data sources to be studied for clues related to perceived motivation. Qualitative case study methodology also allowed the researcher to perform this study without the need to interact directly with those responsible for fraud, thus helping to mitigate and reduce risk in the process.

Based upon the data presented in Chapter 4, the overall research findings suggest no noticeable difference in fraud motivations between those CFOs in the *common* versus *uncommon* demographic group. These data and subsequent findings are based upon a study of 11 fraud cases, 4 of which fall into the common and 7 of which fall into the uncommon CFO demographic groups, respectively. The sections to follow provide a summary of the study's results and findings.

## Discussion of the Results

This research study's question was to determine the differences in CFO fraud motivations across demographic groups; those in the *common* demographic group of younger, lesser-education male versus the *uncommon* demographic group, including any other combination. The expectation, therefore, suggested that the research study would reveal distinct fraud motivation distinctions between these two demographics. The study also aimed to align with historical research related to the overall general fraud motivations that tend to exist at the CFO levels of an organization.

At a macro level, this study provides a strong confirmation of past literature with respect to the motivations generally present when executives commit a corporate fraud. Literature across several spectrums tend to align around a few central reasons for frauds, notably reasons of financial motivation and pressure from others (Bishop et al, 2017; Dorris, 2018; Donegan et al, 2017; Qi et al, 2018). As shown in Table II of Chapter 4, this study's results additionally align with that school of thought, identifying three research themes: financial, corporate, and external. These three themes are further explained as financial motivations, corporate pressure to commit fraud (such as CEO to CFO) and external pressure to commit frauds. Therefore, the research study results do align with and support past research theory on the fraud triangle.

Taking a more micro view and in consideration of the research question, the results support fraud triangle theory that a pressure and rationalization exist, however, the results do not support the hypothesis that there are notable differences between demographic groups. In fact, the results captured in Table 2 demonstrate no clear pattern of fraud motivations within or across groups, suggesting that motivations are varied, and often multiple within the same fraud case.

However, in keeping an inward view of the research results at the forefront, the presented data in Chapter 4 answers the research question posed at the beginning of this study.

### **Conclusions Based on the Results**

As stated in Chapter 2, historical research has not previously examined the ways in which CFOs are motivated to commit fraud acts within their companies. Instead, research has traditionally studied more CFO fraud in two ways. First, CFO demographics have been tabulated and calculated with respect to age, gender and education level, amongst other demographics. These studies have merely looked at a CFO who has committed a fraud in aligning the demographics most commonly present, regardless of perceived guilt or innocence, pressures, opportunities, or motivations for doing so. Secondly and separately, past research on CFO frauds have examined the reasons CFOs choose to cross the line in concluding such reasons as persistent opportunity (Kroos et al., 2018), pressures from higher level executives, such as CEOs (Bishop et al., 2017b) and concerns about losing their job (Bishop et al., 2017a). However, historical research has not typically connected the concepts of fraud theory to CFO demographics. As such, this research does not confirm or dispute previous research, as it is a new basis of learning about the topic.

That being the case, this research leverages traditional fraud theory in combining two elements of the fraud triangle, pressure, and rationalization, into a singular concept of fraud motivation. To that end, it does provide some confirmation of previous theory, as well as contradiction to other aspects. Conclusions of results is broken into two subsections, listed below, beginning first with a connection back to fraud theory. It concludes with an interpretation of the findings.

## **Comparison of Findings With Theoretical Framework and Previous Literature**

As described, fraud theory dates back many centuries (Cressey, 1953) and is based on three pillars: opportunity, pressure, and rationalization. Since that time, and during the last decade, fraud theory has been highly challenged from a variety of angles. These challenges have largely contemplated whether the number of sides, three in Cressey's work, and the classification of the sides are accurate. While some authors have attempted to change the elements of fraud theory, others have suggested more than three and even limitless elements create the entire fraud scenario.

In some respects, the research results herein do challenge standard and largely accepted concepts of fraud theory. The main motivational themes from these research conclusions, comprised of financial motivation, corporate and societal pressures, suggest that the traditional pillars of fraud pressure and rationalization could be collapsed and simply stated as fraud motivation, leaving fraud motivation and fraud opportunity as the two remaining components of fraud theory. This conclusion was garnered based on the presentation of the study data in Chapter 4, which did not detect additional elements of fraud motivation in the eleven indicted cases studied. Furthermore, the study's findings and conclusions are in direct contradiction to the premise that compensation does not represent a good measure of a CFO's intention to commit fraud (Gillett & Uddin, 2005). In fact, in several of the cases studied, the motivation appeared to be precisely connected to compensation. Furthering this idea, some CFOs in this study committed the fraud, according to their own words, merely to earn a common salary and survive. This suggests that, in fact, sometimes CFO fraud does fit neatly into the desire to make a reasonable compensation.

That being the case, this study also supports fraud theory in many ways as well, particularly some of the tangential theories and meta-models coming out of fraud theory. First and foremost, this study gives a strong confirmation related to the pressure element of the fraud triangle, confirming financial incentives and internal/external pressures are nearly always at play in CFO fraud decision making. This is discussed in past literature as well (Bishop et al., 2017a; Bishop et al., 2017b; Hass et al., 2016; Radin, 2017). Of note, CFOs often appear very concerned and therefore more willing to pursue fraud in cases of potential public disclosure of a shaky financial situation, particularly in protection of stock price or a bank financing issue. Consistency of this concept, particularly stock price, is noted in historic literature (Radin, 2017). Further, the connection of fraud theory to corporate culture, discussed in historical literature (Albrecht et al., 2017; Murphy & Free, 2016) aligns with the circumstances of fraud in several of the cases studied. Murphy and Free's (2016) concepts of employees, CFOs in this case, making choices to keep the company happy connects directly to several of the key themes noted in the eleven fraud cases studied. Finally, situations noted by Suh et al (2018) wherein CFOs started from a position of honesty and slowly migrated to one of dishonesty and fraudulent actions is also demonstrated within the research results in this study.

### **Interpretation of the Findings**

In contemplation of the limitations section stated directly below, to follow are several interpretations of this research study related to the findings previously discussed. First, as indicated above, the key research themes of financial motivation, internal pressures and external pressures to commit fraud offer a key confirmation of the most common CFO fraud pressures. These pressures are well documented in literature (Soltani, 2014), but this study's results go further in detecting no additional fraud pressures within the sample studied. While it would be

improper to suggest these are all the fraud pressures present in every circumstance, the results do suggest the key pressures may be relied upon by the parties most interested in fraud prevention and detection.

Second, because the research data connected the eleven CFO fraud cases to all three research motivation themes, this study concludes that demographics bear very little if any influence on the reasons CFOs choose to commit a fraud. This offers shareholders, regulators, and auditors a clue about fraud controls and audits inasmuch as demographics do not matter. CFOs in both the common and uncommon groups are motivated by the same factors and consistently so. This should alert the fraud fighting community that CFOs, whether they are male or female, young or old, lesser or more educated, choose to commit fraud for all the same reasons.

Finally, as discussed in the *Recommendations for Further Research* section below, the additional research themes captured in this study point to strong support and therefore implications related to fraud opportunity. While outside the specific scope of this study's stated research question, findings suggest that there are just as many issues concerning fraud opportunity as fraud motivation, including specific industry concerns, personality issues of CFOs and a wide variety of issues concerning internal controls. Fraud opportunity is discussed in below sections in greater detail.

### **Limitations**

During this study, the researcher noted a couple limitations, discussed here. First, the ability to access documentation sufficient to imply fraud motivation was, at times, a difficult task. To begin, while the Freedom of Information Act (FOIA) appeared to be a reliable and healthy source of court records, in reality, this venue turned out to be without any useful



information for all cases studied. The FOIA is only for a small subset of cases within a specific system of U. S. courts, and therefore, multiple requests came back with no information.

PACER appeared to be a very reliable database of court documentation as an alternative. While PACER did indeed hold valuable information for all of the cases within this study, specific limitations were present within the database. First, each court case often had hundreds or even thousands of records within it. At times, cases spanned across multiple criminal and governmental areas of PACER, creating a complex and often confusing web of related court cases, often difficult to follow. Furthermore, PACER forces a researcher to click on a variety of different links to access data, each of which must be purchased. For particularly expansive cases, it became cost prohibitive to drill into finite detail of the court cases, as the court transcripts and its relative usefulness were hidden until a user agreed to pay to access the records. While there is a system in place to request a PACER fee waiver, multiple attempts to reach governmental agencies to rule on this fee waiver went unanswered.

Finally, while the researcher believed that media reports would assist in triangulation efforts with court documentation, the research study revealed that most media reports were nothing more than carbon copies of government press releases and did not offer much in the way of useful additional data. In sum, data was often difficult to locate as an initial step, then difficult to quantify with relation to value before purchasing it through PACER. Finally, in a few limited cases, while there was information available in PACER for review, trial transcripts were either available but incomplete (pages missing within trial testimony) or certain case files were sealed and not available for viewing under any circumstances. Because of this fact, a moderate number of fraud cases that looked promising for inclusion in this research study were eliminated as

options. Thus, the research conclusions may have differed had greater access to data been available.

Additionally, when court records were available for view, many of the cases were related to CFOs who were testifying as part of a plea deal. In other words, CFOs testified against another indicted party in the same fraud. As such, CFOs were often forced to fully disclose the nature of the fraud, frequently giving details about their motivation. While this offered unique insights firsthand, it was difficult to discern the truthfulness of testimony, when CFOs were fully incited to speak negatively against the defendant. To combat this, cross examination against CFOs was carefully studied, however, it may be seen as a limitation that CFOs were potentially bias in their testimony given these circumstances.

### **Implications for Practice**

From the standpoint of theoretical implications, the research conclusions suggest that the more recent criticisms and critiques of fraud theory are plausible. As mentioned in sections above, this study's conclusions may add value to the argument that the fraud triangle is not in fact a triangle, requiring additional research and analysis. Conversely, the study's results, while not necessarily the main scope, do suggest that fraud opportunity is an ever strong facet of fraud theory. Further, the elements of fraud opportunity were arguably more pervasive and present within the 11 fraud cases studied, with a very large variation of ways in which CFOs carried out their fraud. In nearly all of the fraud cases presented and studied, internal controls issues were consistent, allowing CFOs to expose their companies in countless ways. This study, therefore, offers real theoretical implications, as well as future opportunities, related to the opportunity aspect of fraud theory.

In view of the practical implications, this study helps to confirm to the fraud fighting and other interested communities that fraud is varied, unpredictable, complex and will require continued resources to discover and combat. Although historic researched coalesced around common CFO demographics, this study's results did not confirm consistent fraud motivations based on the common and uncommon demographics noted. Therefore, those who have vested interest in fraud controls, auditing and oversight should understand that, practically speaking, they must align oversights functions consistently across all demographic groups. However, as discussed above, this study's unexpected and consistent research themes related to the pervasiveness of fraud opportunity may offer additional insights that shed light on CFOs fraudulent actions.

### **Recommendations for Further Research**

As this study unfolded, the researcher identified several areas of opportunity for further research. First, the presupposition that the *common* CFO fraud group is younger and lesser-educated males deserves additional research, particularly in the U. S. market. Throughout the research process, the *common* demographic group was difficult to locate in actual fraud cases, while older males appeared to commit fraud more often. This may be because past studies examined frauds having taken place, but did not specifically look at indicted fraud, which was the focus of this study. Committed versus indicted fraud, therefore, may yield a different *common* demographic, and thus, change research results if this study was duplicated.

In addition to further examining the *common* demographics of fraudulent CFOs, two case-specific themes emerged during the study that may warrant additional research. First, within the sample of eleven cases studied, four of the cases emerged as outliers to the other seven. To distinguish a fraud case as an outlier, there existed a circumstance within the fraud case that

made it appear especially severe or egregious. For example, in one of the fraud cases, 99% of the purported revenues were fake, suggesting a higher level of awareness and willingness to participate in the act. In another case, the financial losses were a significant outlier to the losses in the other fraud cases, as well as highly collusive in nature. Although outside the scope of this study, the specific examining of the fraud triangle elements for executive-level staff in these cases may glean interesting new information about how particularly large frauds begin, continue, and unravel. In a similar way, there were four specific fraud cases studied that intersected with the banking industry, with a fairly consistent fraud story behind them all. Given the timeframe of the study was during the financial crisis, this is logical. However, the research community may find value in more deeply studying only the banking industry during this time for clues about how fraud can be understood, detected and prevented in the future.

Finally, through this study, several fraud opportunity-specific themes emerged that may find value in additional study. First, in a few circumstances, the fraudulent CFO appeared to have a particular personal or psychological trait that connected to fraud opportunity. These personal traits were widely varied from case to case. In some situations, the CFO appeared to have a particularly demanding or directive style that allowed them to do what they wished and therefore perpetuate fraud. In other situations, the CFO appeared to be largely unstable from a psychological standpoint or seemingly caved to the pressures of continuing a fraud for which they were responsible. To that end, a study of fraud scenarios connecting to psychology or personal inhibitions of CFOs may be worthy of study.

Secondarily, specific CFO experience appeared to aid in corporate fraud in a couple of the cases studied. In these fraudulent scenarios, there appeared to be a lack of adequate experience on the part of the CFO insomuch as they could realize a fraud was taking place and

take steps to stop it. In one case, the CFO, who worked in the banking industry, did not have an accounting degree and while he appeared to have a banking background, did not seem to have adequate knowledge of accounting. In the other circumstance, the indicted CFO was merely a glorified administrative assistant with bank account access and the title of CFO. Corporate fraud versus CFO experience could be an area of future study.

Lastly, the intersection of fraud opportunity often connects to the specific ways in which CFOs carry out the corporate fraud itself. During this study, a large variety how the fraud took place was noted in the research coding process. Several usual fraud circumstances were present including revenue recognition, stock trading (pump and dump) schemes and kickbacks. However, beyond these common types of fraudulent acts, there was also a wide variety of creativity and other situations created by CFOs that tend to be less common. In some cases, CFOs used a layering of various frauds to sum to a larger overall fraud, creating issues of detection for auditors. Further research in the area of fraud opportunity, potentially connecting with fraud motivation, could provide value to the research community.

### **Conclusion**

As a final reminder to the reader, this research study connected two related but previously unstudied concepts in fraud literature: the intersection of common and uncommon CFO fraudulent demographic groups, confirmed in research studies with the study of CFO fraud motivation. The intent of the study was to determine if CFOs within the common and uncommon demographic groups had the same or different motivations in perpetuating occupational fraud against the company. Through study of eleven cases of indicted CFO fraud, the conclusion is that CFOs, whether common or uncommon, have the same motivations. These motivations align into three key themes: financial motivation, internal pressure, and external pressure. This set of

research conclusion suggest that we, as researchers, interested parties or key stakeholders, must view fraud motivations as consist across the CFO populations and, as such, create a consistent suite of preventive and detective internal controls, regardless of age, gender or education level.

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