



**TCTC 2024**  
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# ***Fraud Brainstorming and Interviewing Techniques for Auditors***

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**CHAIRMAN EMERITUS, COTTON & COMPANY**

Dave Cotton is founder and Chairman Emeritus of Cotton & Company, Certified Public Accountants, headquartered in Alexandria, Virginia. Cotton & Company was founded in 1981 and has a practice concentration in assisting Federal and State agencies, inspectors general, and government grantees and contractors with a variety of government program-related assurance and advisory services. Cotton & Company has performed grant and contract, indirect cost rate, financial statement, financial related, and performance audits for more than three dozen Federal inspectors general as well as numerous other Federal and State organizations, programs, activities, and functions. In April 2022, Cotton & Company became a wholly owned subsidiary of Sikich LLP.

Cotton & Company's Federal agency audit clients have included the U.S. Government Accountability Office, Public Company Accounting Oversight Board, U.S. Navy, U.S. Marine Corps, U.S. Transportation Command, U.S. Defense Security Cooperation Agency, U.S. House of Representatives, U.S. Capitol Police, U.S. Small Business Administration, U.S. Bureau of Prisons, Millennium Challenge Corporation, U.S. Marshals Service, and Bureau of Alcohol, Tobacco, Firearms and Explosives. Cotton & Company also assists numerous Federal agencies in preparing financial statements and improving financial management, accounting, and internal control systems.

Dave received a BS in mechanical engineering and an MBA in management science and labor relations from Lehigh University in Bethlehem, PA. He also pursued graduate studies in accounting and auditing at the University of Chicago Graduate School of Business. He is a Certified Public Accountant (CPA), Certified Fraud Examiner (CFE), and Certified Government Financial Manager (CGFM).

Dave served on the Advisory Council on Government Auditing Standards (the Council advises the United States Comptroller General on promulgation of **Government Auditing Standards**—GAO's yellow book). He served on the Institute of Internal Auditors (IIA) Anti-Fraud Programs and Controls Task Force and co-authored **Managing the Business Risk of Fraud: A Practical Guide**. He served on the American Institute of CPAs Anti-Fraud Task Force and co-authored **Management Override: The Achilles Heel of Fraud Prevention**. Dave is the past chair of the **AICPA Federal Accounting and Auditing Subcommittee** and has served on the **AICPA Governmental Accounting and Auditing Committee** and the **Government Technical Standards Subcommittee of the AICPA Professional Ethics Executive Committee**. Dave chaired the Fraud Risk Management Task Force, sponsored by COSO and ACFE and is a principal author of the **COSO-ACFE Fraud Risk Management Guide**. Dave co-chaired a task force to update the **COSO-ACFE Fraud Risk Management Guide**. In May 2022, Governor Glenn Youngkin appointed Dave to the Virginia Board of Accountancy.

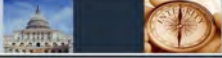
Dave served on the board of the Virginia Society of Certified Public Accountants (VSCPA) and on the **VSCPA Litigation Services, Professional Ethics, Quality Review, and Governmental Accounting and Auditing Committees**. He is a member of the Association of Government Accountants (AGA) and past-advisory board chairman and past-president of the AGA Northern Virginia Chapter and past Vice Chair of the **AGA Professional Ethics Board**. He is also a member of the IIA and the Association of Certified Fraud Examiners. Dave is presently serving on the National Association of State Boards of Accountancy (NASBA) Regulatory Response Committee.

Dave has testified as an expert in governmental accounting, auditing, and fraud issues before the United States Court of Federal Claims, the Armed Services Board of Contract Appeals, and other administrative and judicial bodies.

Dave has spoken and written frequently on cost accounting, professional ethics, and auditor fraud detection responsibilities. He has been an instructor for the George Washington University Master of Accountancy program (**Fraud Examination and Forensic Accounting**) and has instructed for the George Mason University Small Business Development Center (**Fundamentals of Accounting for Government Contracts**).

Dave was the recipient of the **ACFE 2018 Certified Fraud Examiner of the Year Award** ("presented to a CFE who has demonstrated outstanding achievement in the field of fraud examination ... based on their contributions to the ACFE, to the profession, and to the community"); **AGA's 2012 Educator Award** ("to recognize individuals who have made significant contributions to the education and training of government financial managers"); and **AGA's 2006 Barr Award** ("to recognize the cumulative achievements of private sector individuals who throughout their careers have served as a role model for others and who have consistently exhibited the highest personal and professional standards").

## **Disclaimer**

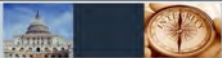


**The views expressed in this presentation are my views and do not necessarily align with the views of the Virginia Board of Accountancy.**

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1

## **SAS 99: Consideration of Fraud in a Financial Statement Audit**



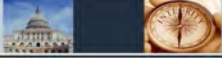
- Issued October 2002
- Codified in AU-C Section 240
- SAS 99 superseded SAS 82, *Consideration of Fraud in a Financial Statement Audit* (Issued February 1997)
- SAS 82 Superseded SAS 53, *The Auditor's Responsibility to Detect and Report Errors and Irregularities* (Issued April 1988)

2

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2

## Is SAS 99 Making a Difference?



- Evaluating how the entity responds to identified fraud risks
- More emphasis on professional skepticism
- **Discussions among engagement personnel (brainstorming)**
- **More inquiries of management and others within the entity**
- Reorganized and modified fraud risk factors
- Expanded fraud risk assessment approach
- Expanded guidance on revenue recognition as a likely risk
- Linkage between identified risks and the auditor's response
- Looking at the risk of management override of controls

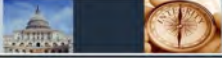
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## Let's ...



- Look at some fraud brainstorming concepts and techniques
- Look at some fraud inquiry concepts and techniques
- Apply these concepts and techniques to solve a crime

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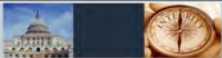


# Fraud Brainstorming



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## “Discussion Among the Engagement Team”



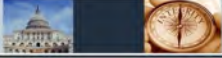
- “should include an exchange of ideas or brainstorming among the engagement team members about how and where the entity's financial statements ... might be susceptible to material misstatement due to fraud, how management could perpetrate and conceal fraudulent financial reporting, and how assets of the entity could be misappropriated.”
- “setting aside beliefs that the engagement team members may have that management and those charged with governance are honest and have integrity...”

6



6

## “Discussion Among the Engagement Team”



- Focus on the “fraud triangle” (incentive/pressure; opportunity; rationalization)
- Consider risk of management override of controls
- Consider earnings management or manipulation
- Maintain professional skepticism
- Consider auditor responses

7

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## Fraud Discussions Among Engagement Personnel

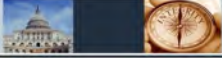


- During audit planning *and throughout the audit*
- Interactive exchange of ideas ... *brainstorming*
- Insights of more experienced team members with creativity of less experienced team members
- How and where the financial statements might be susceptible to fraud
- Emphasize importance of proper state of mind (professional skepticism) during the audit
- Include the risk of management override of controls
- Include risk of earnings manipulation

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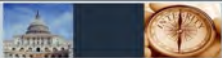
## Fraud Discussions Among Engagement Personnel



- Thoroughly probe the possible fraud issues
- Consider audit responses to fraud susceptibility
- Summarize known fraud risks and control strengths and weaknesses
- Brainstorm ways that fraud might be committed by someone within the entity (by management or employees) or on the entity (by an outsider)
- Evaluate fraud schemes deemed viable or possible
- React by modifying planned audit tests to ascertain if fraud is occurring

9

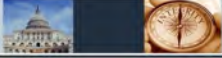
## Fraud Discussions Among Engagement Personnel



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- **React** by modifying planned audit tests to ascertain if fraud is occurring

10

## *The Purpose of Brainstorming ...*



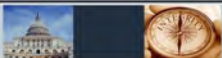
*...is to get as many ideas as possible from a group of people in the shortest possible time. Quantity and not quality is the order of the day. It does not matter if the ideas are thought to be unworkable, or crazy, or outlandish by anybody within the group. Sometimes these ideas are the very ones that are adapted into other forms that solve the problem adequately.*

*--<http://www.mindbloom.net/brain.html>*

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11

## *The Four Principles of Brainstorming ...*



- 1. Quantity over quality.** The idea is that quantity will eventually breed quality as ideas are refined, merged, and developed further.
- 2. Withhold criticism.** Team members should be free to introduce any and all ideas that come into their heads. Save feedback until after the idea collection phase so that “blocking” does not occur.
- 3. Welcome the crazy ideas.** Encouraging your team members to think outside of the box and introduce pie in the sky ideas opens the door to new and innovative techniques that may be your ticket for success.
- 4. Combine, refine, and improve ideas.** Build on ideas and draw connections between different suggestions to further the problem-solving process.

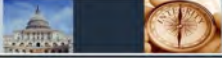
Source: [MindManager.com](http://MindManager.com)

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12



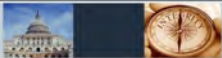
## The Sole Practitioner Dilemma



- ✓ *How does a sole practitioner meet the SAS 99 brainstorming requirement?*

13

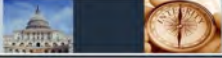
## The Documentation Dilemma



- ✓ *How much should we document?*
- ✓ *Follow audit organization policies ...*
- ✓ *Follow SAS 103, Audit Documentation ... “record of procedures performed, relevant audit evidence obtained, and conclusions the auditor reached.”*

14

## Brainstorming Documentation Per SAS 99 (AU-C 240)

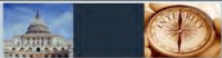


- Significant decisions reached
- How and when brainstorming was done
- Who participated
- Identified and assessed risks of material misstatement
- Auditor responses to identified/assessed risks of material misstatement (overall and risk-specific)
- Reasons for concluding that revenue recognition is not a risk (if applicable)

15



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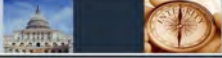


# Fraud Inquiries



16

## *Fraud Interviewing Techniques for Auditors*

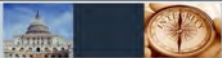


- Why? (What do standards require?)
- Integrate brainstorming and interviews
- Characteristics of a “good” interviewer
- Logistics
- Types of questions
- Question sequence
- Overcoming resistance or hostility
- Recognizing deception
- Interviews versus interrogations



17

## **Why do I have to talk to people?**

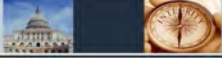


Let's look at what SAS 99 requires.



18

## Why do I have to talk to people?



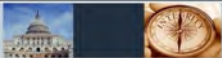
*The auditor should make inquiries [of management, internal audit, and those charged with governance] **and others within the entity as appropriate**, to determine whether they have knowledge of any actual, suspected, or alleged fraud affecting the entity.*

[AU-C 240]

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19

## Why do I have to talk to people?



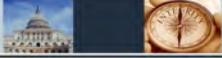
*The auditor's inquiries of management may provide useful information concerning the risks of material misstatements in the financial statements resulting from **employee fraud**. However, such inquiries are unlikely to provide useful information regarding the risks of material misstatement in the financial statements resulting from **management fraud**.*

[AU-C 240]

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20

## Why do I have to talk to people?



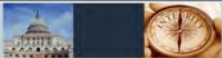
*Making inquiries of others within the entity, in addition to management, may provide individuals with an opportunity to convey information to the auditor that may not otherwise be communicated. It may be useful in providing the auditor with a perspective that is different from that of individuals in the financial reporting process.*

[AU-C 240]

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21

## Why do I have to talk to people?



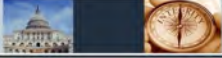
*The responses to these other inquiries might serve to corroborate responses received from management or, alternatively, might provide information regarding the possibility of management override of controls.*

[AU-C 240]

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22

## Why do I have to talk to people?



*Examples of others to whom the auditor may direct fraud inquiries to include:*

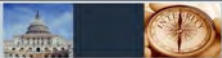
- *Operating personnel not involved in accounting and financial reporting*
- *Employees at different authority levels*
- *Employees involved in complex or unusual transactions*

[AU-C 240]

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23

## Why do I have to talk to people?



*Examples of others to whom the auditor may direct fraud inquiries to include:*

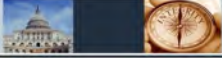
- *In-house legal counsel*
- *Chief ethics officer or equivalent*
- *Person(s) charged with dealing with fraud allegations*

[AU-C 240]

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24

## Why do I have to talk to people?



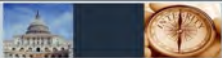
*Management is often in the best position to perpetrate fraud. Accordingly, when evaluating management's responses to inquiries with professional skepticism, the auditor may judge it necessary to corroborate responses to inquiries with other information.*

[AU-C 240]

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25

## Representation Letters?



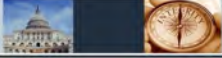
For key interviews and interviews that reveal information essential to audit objectives, consider requesting written representations from interviewees.

Not required by standards, but not prohibited, and might be valuable in assuring an accurate understanding of facts obtained.

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26

## Integrate Brainstorming and Fraud Inquiries

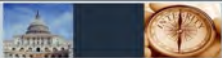


- Brainstorming yields a list of potentially viable fraud scenarios that MIGHT be occurring
- What is the most efficient way to determine if such scenarios might actually be happening?
- Often, the most efficient way is through carefully planned fraud inquiries
  - Who would be in a position to see a particular fraud scheme?
  - What questions can we ask her/him to determine if that fraud might be happening?



27

## Integrate Brainstorming and Fraud Inquiries



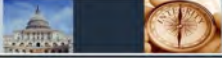
- Our brainstorming session revealed the following fraud vulnerability:
  - ????
- Who should we consider interviewing and what questions should we ask?



28



## Characteristics of a “Good” Interviewer

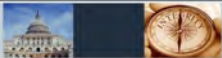


- Efficient, prepared, courteous, and careful with language used
- Don't talk down
- Businesslike; friendly, but not social
- Do not be authoritarian; do not dominate the discussion
- Avoid technical jargon
- Don't use an accusatory tone or demeanor

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29

## Interviewing Logistics

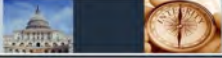


- Meet in the interviewee's office (so she or he can access records if need be)
- Social distance (4-6 feet apart)
- Ideally, nothing between interviewer and interviewee
- One interviewee at a time
- In private
- Minimize note-taking; maintain eye contact

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30

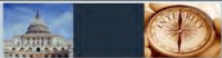
## Types of Questions



- Closed questions—can be answered with one word
  - “You’ve worked here for two years, is that correct?”
  - “What day of the month are closings done?”
  - “Are vendor files organized by month or by vendor?”

31

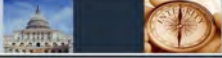
## Types of Questions



- Open questions—cannot be answered with one word
  - “Please describe your job responsibilities.”
  - “Please describe the process used when paying a vendor.”
  - “What did you think when your manager asked you to award the contract even though only one bid had been solicited but you thought the price was way too high?”

32

## Types of Questions

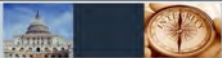


- Leading questions—contain the answer as part of the question
  - “Isn’t it true that your job responsibilities require you to interact frequently with vendors?”
  - “You are one of just a few employees with access to the warehouse on weekends, isn’t that correct?”
  - “You would have noticed any large or unusual payroll transaction, right?”

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33

## Types of Questions

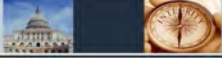


- Double-negative questions—confusing, don’t use
  - “Didn’t you suspect that something wasn’t right?”
- Complex questions—avoid using
  - “What are your responsibilities in this job and how long have you worked here?”

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34

## Question Sequence



- Introductory questions
  - Break the ice
  - Establish commitment to assist
  - Basic introductions and interview purpose
  - Set the tone; establish rapport
  - *Calibrate*

35

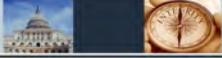
## Question Sequence



- Informational questions
  - Non-confrontational, designed to gather basic information; go over facts
  - Proceed from general to specific
  - Start with closed questions; move to open questions
  - Proceed from non-sensitive to sensitive

36

## Question Sequence

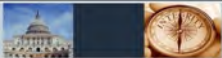


- Closing questions
  - End on positive note
  - Confirm key points discussed
  - Leading questions are okay
  - Keep communication lines open for future follow-up (in both directions)



37

## Question Sequence

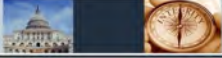


- Assessment questions (Used when you suspect the interviewee has not been honest or complete in her or his answers. Usually only used when a specific instance of fraud is suspected.)
  - “Why do you think an employee might feel that stealing from this company is justified?”
  - “What do you think should happen to someone who steals from her or his employer?”
  - “Have you ever felt justified—even though you did not go through with it—in taking advantage of your position?”
- Admission-seeking questions (Only used when you think it is highly likely that the interviewee has done something dishonest. Only used when a specific instance of fraud is suspected.)



38

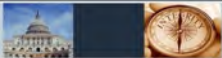
## Question Sequence and Types



- Introductory.....closed questions OK
- Informational...open questions are best
- Closing .....closed and leading questions OK

39

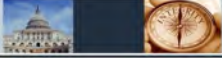
## Develop Some Good Fraud Questions to Use at the End of the Informational Phase



- *If someone wanted to steal from the company, how do you think they could do it?*
- *If management wanted to cook the books, how do you think they could do it?*
- *What are the greatest fraud risks this company faces?*
- *Is there anything that happens around here that you think is strange or unusual?*
- *Have you ever seen anyone circumvent control procedures?*
- *Are there any tasks that are only allowed to be performed by certain individuals?*
- *Are you aware of any improper or fraudulent activity?*
- *Are there any questions I have not asked you that you think I should ask?*
- *Who else do you think I should talk with?*
- *Will you get in touch with me if you think of anything else you think I should know about possible fraud?*

40

## Overcoming Resistance

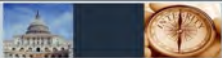


- Better to schedule interview in person than by phone
- *"I'm too busy"* Respond by stressing:
  - The interview will be brief
  - The interview will not be difficult
  - I'm here now, let's get it done
  - The interview is very important
  - I really need your help
- *"I don't have any information that will be useful"* Responses:
  - *"I see, What do your duties involve then?"*
  - *"Yes, that's what I wanted to find out; do you know anything about control procedures in your area?"*



41

## Overcoming Resistance

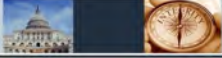


- *"I don't remember"* Responses:
  - *"I understand that you probably don't remember every detail; let's start with the parts that you do remember."*
  - *"Sure, that's understandable. Do you recall who else was around at the time?"*
- *"What do you mean by that?"* Response:
  - *"Sorry if that's confusing. Let me clarify."*



42

## Overcoming Hostility



- Do not react to anger from interviewees
- Don't reason; disarm (*"Thank you for sharing that viewpoint with me."*)
- Change tactics (*"I understand how you feel, but what would you do if you were me?"*)
- Make it easy to say "yes" (*"Yes, I see your point; and I am sure you understand my position, don't you?"*)
- Make it difficult to say "no" (*"We both are concerned about this company and its stakeholders, right?"*)



43

## Recognizing Deception



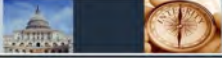
- It is important to calibrate—observe demeanor during introductory and routine questions
- Be alert for **verbal** clues indicating increased stress
  - Changes in speech patterns
  - Repetition of the question
  - Complaints about heat/cold/light/noise
  - Selective memory
  - Excuses (*"I'm always nervous"*)
  - Oaths (*"to be honest ..."* *"I swear to God ..."*)
  - Testimonials (*"You can ask anyone ..."* *"You can ask my minister..."*)
  - Answering with a question
  - Overuse of formality/respect



44



## Recognizing Deception

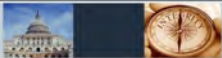


- It is important to calibrate—observe demeanor during introductory and routine questions
- Be alert for ***non-verbal*** clues indicating increased stress
  - Full body motions/shifts
  - Anatomical physical responses (sweat, increased heart rate, shallow or labored breathing)
  - Illustrators (change in use of hands to illustrate points)
  - Hands over mouth
  - Manipulators (picking lint from clothes, playing with an object)
  - Fleeing position
  - Crossing arms or feet
  - Lip movements (tight/pursed lips, closed mouth, biting lips/tongue, chewing on object)



45

## Interviewing in an Audit Versus Interviewing in an Investigation?



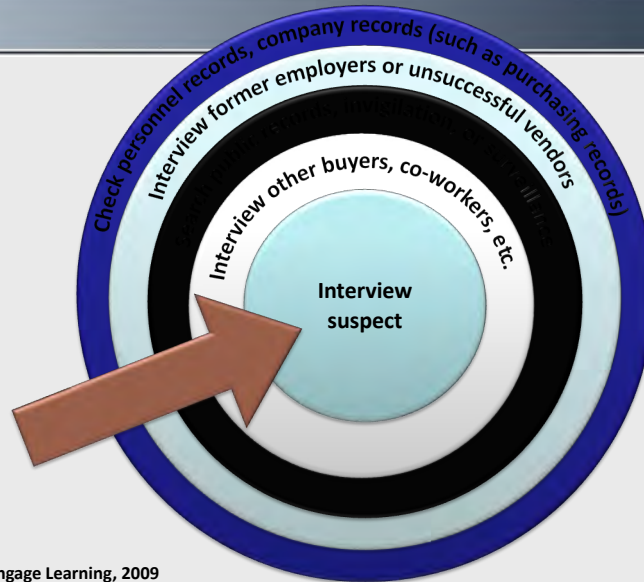
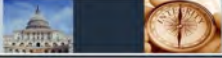
**In an audit, you are seeking information and knowledge.**

**In an investigation, you know or suspect that fraud has occurred and are trying to determine the perpetrator.**



46

## Theft Act Investigative Methods



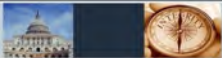
47

Fraud Examination, 3<sup>rd</sup> Edition, Cengage Learning, 2009



47

## Inquiries About Fraud ...

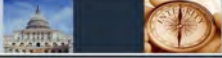


- SAS 99 clearly envisions that auditors will develop and maintain some new skills ....
- We have always been good at “fact-finding” interviews
- SAS 99 requires “information-finding” interviews
- Ideally, “knowledge-finding” inquiries are what we need to be able to make



48

## Inquiries About Fraud ...

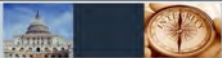


Being a good *professional* interviewer will prepare you for when your audit turns into an investigation

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49

## Okay ...



Let's apply these skills and see if we can figure out who took what ... when ... why ... where ... and how ...

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50



# *W. I. S. E.*

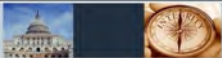
## *A Case Study in Fraud*

Cotton

333 John Carlyle Street | Alexandria, VA 22314  
[www.cottoncfe.com](http://www.cottoncfe.com)

51

### **NOTE:**

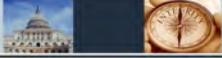


- The names of the organizations and characters in this case study have been changed, and are not the real names of the organizations and persons involved in the case from which this story was derived.
- Any similarity between the organizations, characters, and events depicted in this case study and organizations, persons, and events with which you may be familiar is entirely deliberate.

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52

## **NOTE:**

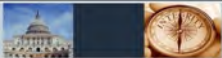


- We will need 7 volunteers to assist in the presentation of this case study.
- Your assistance, if you volunteer, will not be difficult; it will not be embarrassing.
- It will be educational, challenging, and hopefully, fun.
- Trust me; you can count on me; I am an accountant.
- ***If you volunteer, you will receive the acclaim of your peers!***

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53

## **Worldwide Institute for Situational Ethics, a Not-for-Profit Organization**

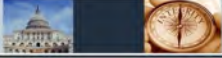


Susan Purduper, Executive Director  
Robin Plundar, Chief Financial Officer  
Helen Weels, Programs Director  
Otto Krattic, Board Chair  
Salvatore Amander, IT Director  
Lewis Skannon, New Board Member  
Talia Watt, Receptionist

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54

## Worldwide Institute for Situational Ethics, a Not-for-Profit Organization

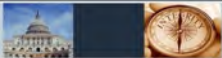


- As we learn a little bit about our ~~perpetrators~~ I mean volunteers, see if you can identify any fraud risk factors or vulnerabilities that might indicate a higher risk of fraud.
- **Fraud Risk Factor:** A characteristic that provides a *motivation* or *opportunity* for fraud to occur; a *rationalization* for fraud; or an *indicator* that fraud may have occurred

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55

## Susan Purduper, Executive Director

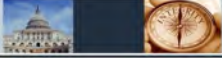


- Sue has been WISE's executive director for 4 years.
- She was selected for the position by WISE's founder, Otto Krattic, who is now chairman of the board. Sue and Otto work well together and confer frequently about policy.
- During Sue's tenure
  - membership has risen over 220%
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56

## Susan Purduper, Executive Director

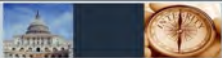


- Sue is responsible for all hiring and firing decisions including all purchasing and contracting; but she delegates most of what she considers “administrative minutia tasks.”
- Everyone—particularly the board of directors—agrees that Sue has done an outstanding job of meeting the organization’s mission goals and objectives.



57

## Robin Plundar, Chief Financial Officer



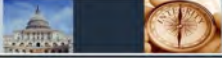
- Robin is a retired senior manager from a CPA firm, Hay, Wood, Jubusoff & Company.
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- As WISE grew, Robin helped Sue manage the growth, and became a trusted and key advisor to her.
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58



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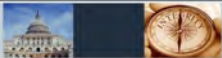


- Robin works long hours during the week and on most weekends, s/he is always cheerful; a true team player.
- Robin has always been very satisfied with the modest annual pay increases Sue has recommended for him/her over the years.
- Everyone agrees that Robin does a terrific job; Sue always gives her/him a great deal of the credit for WISE's success; Robin is very happy working for WISE and has, in fact, turned down offers to work for larger organizations for substantial pay increases

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59

## Helen Weels, Programs Director



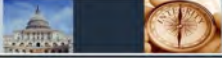
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60



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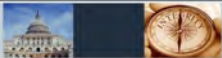


- Publication sales at conferences initially increased along with the increased attendance, but then leveled off and started declining slightly.
- Helen even added two more conferences to WISE's annual schedule.
- Helen's success in expanding WISE's conference programs has been recognized by both the board and the executive director.

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61

## Otto Krattic, Board Chair

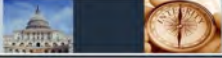


- Otto is a former senior Federal executive and gained prominence for his groundbreaking work in advanced situational ethics applications.
- Otto founded WISE eight years ago and initially served as both executive director and board chair.
- Otto hired Susan Purduper as executive director 4 years ago so that he could spend more time speaking at conferences and consulting on political campaigns.

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62

## Otto Krattic, Board Chair



- Otto has semi-annual Board meetings at which the executive director and the programs director give updates on operational and programmatic activities and achievements, and the CFO gives updates on financial matters, primarily focusing on the annual budget and tracking actual-to-budget performance.



63

## Salvatore Amander, IT Director

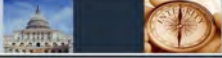


- Sal joined WISE three years ago. His previous job was as a senior IT manager for Hay, Wood, Jubusoff & Company, a CPA firm.
- When Sal arrived, the WISE IT structure was a mess. Most of the organization's computers were obsolete, the network was slow and inefficient, and WISE was not even using a broadband internet connection. WISE did not even have any sort of virus protection system; Sal found all of the entity's PCs infected with multiple viruses.
- Within the first six months, Sal upgraded all of WISE's systems to state-of-the-art hardware and software, installed appropriate firewalls and virus protection, and arranged for a high-speed T-1 connection.



64

## Salvatore Amander, IT Director

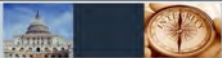


- Sal also implemented several linked databases that integrate accounting, fundraising, membership, and conference registration information.
- Sal prepared a report that estimated that the cost savings from the more efficient systems more than offset the additional IT budget costs.
- The executive director, Susan Purduper, has been very pleased with Sal's work, and WISE has given Sal generous performance bonuses the past two years.

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65

## Lewis Skannon, New Board Member

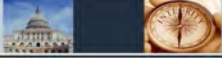


- Lew is considered to be a rising star in the field of situational ethics, having gotten his start working as campaign manager for Bill Clinton, during Bill's unsuccessful bid for governor of Alaska in 2012.
- Lew met Otto Krattic, WISE's founder, at a conference where Lew had delivered a talk entitled "*If It Sounds Good, Say It!*"
- After Otto asked Lew to join the WISE board six months ago, Lew quickly immersed himself in WISE details.

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66

## Lewis Skannon, New Board Member



- Lew has asked many questions about WISE operations:
  - Why are we spending so much on information technology?
  - Why is publications expense rising faster than publications revenue?
  - Why have on-site conference registrations decreased so drastically in the past two years?
  - Why can't the programs director or the IT director or the CFO give me straight answers to any of my questions?
  - Why doesn't the board meet monthly?
  - ... and so forth ...



67

## Lewis Skannon, New Board Member

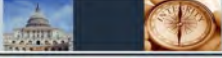


- Otto, who was initially supportive, seemed to become impatient with Lew. At Lew's first board meeting three months ago, Otto said to Lew "Maybe you should take a few months to get to know the organization better." Everyone laughed.
- Susan, however, has been very patient with Lew's questions. At the board meeting, she directed staff to get answers to each of Lew's questions "immediately, if not sooner."



68

## Talia Watt, Receptionist

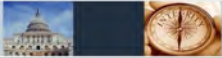


- Talia is outgoing, talkative, effervescent, and pleasant at all times.
- Callers and visitors often comment to the executive director, Susan Purduper, about Talia’s cheery attitude, pleasant manner, and helpfulness.
- Talia was hired by the WISE founder, Otto Krattic, not long after WISE started.
- In addition to answering the phones and greeting visitors, Talia manages office supplies, and coordinates deliveries.
- Talia also opens and sorts the mail, including invoices from vendors. She also keeps a log of accounts payable and, when she mails out checks, she notes accounts as “paid.”



69

## WISE Selected Financial Information

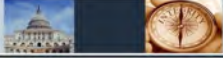


	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>
<b>Members</b>	55,295	61,899	91,756	109,873	121,985
<b>Dues Revenues</b>	\$30,412,250	\$34,044,450	\$50,465,800	\$60,430,150	\$67,091,750
<b>Program &amp; Grant Revenue</b>	239,075	256,098	635,987	724,589	843,575
<b>Conferences Revenues</b>					
Pre-registrations	7,208,734	7,307,543	8,102,355	8,765,419	9,359,887
On-site Registrations	764,097	865,322	871,098	880,981	859,031
<b>Publications</b>	2,543,009	2,759,080	2,657,087	2,875,018	2,810,876
<b>Total Revenue</b>	<u>\$41,167,165</u>	<u>\$45,232,493</u>	<u>\$62,732,327</u>	<u>\$73,676,157</u>	<u>\$80,965,119</u>



70

## WISE Selected Financial Information

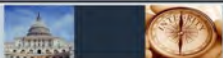


	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>
Fundraising Costs	\$7,603,063	\$8,511,113	\$12,616,450	\$15,107,538	\$16,772,938
Program & Grant Expenses	255,810	266,342	648,707	731,835	818,268
Research Costs	17,713,312	20,104,208	31,699,722	40,799,324	46,588,278
Publications Costs	1,986,543	2,155,333	2,338,464	2,537,156	2,752,730
Conferences Costs	5,320,987	6,032,642	6,649,415	7,153,519	7,583,493
<b>Administrative Costs</b>					
Salaries	985,609	1,024,541	1,063,472	1,102,404	1,141,335
Expenses	6,848,948	6,246,310	6,733,733	5,167,589	4,137,348
IT Costs	398,876	870,998	985,321	1,097,623	1,198,526
<b>Total Expenses</b>	<b>\$41,113,148</b>	<b>\$45,211,486</b>	<b>\$62,735,284</b>	<b>\$73,696,987</b>	<b>\$80,992,915</b>
Surplus/(Deficit)	\$54,017	\$21,007	(\$2,957)	(\$20,830)	(\$27,796)



71

## Brainstorming to Find Fraud

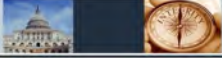


- Gather into brainstorming teams of 4-5 people
- Select a scribe
- Using the information you know about this case so far, brainstorming ways that fraud might be happening at WISE
- Following the rules for effective brainstorming
- Take ~10 minutes
- Following the brainstorming session, use ~5 minutes to decide on questions to ask our panelists. Each team is limited to asking only 5 questions, so select your questions and targets for those questions wisely (no pun intended)



72

## *The Purpose of Brainstorming ...*



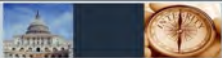
*...is to get as many ideas as possible from a group of people in the shortest possible time. Quantity and not quality is the order of the day. It does not matter if the ideas are thought to be unworkable, or crazy, or outlandish by anybody within the group. Sometimes these ideas are the very ones that are adapted into other forms that solve the problem adequately.*

--<http://www.mindbloom.net/brain.html>



73

## *The Four Principles of Brainstorming ...*



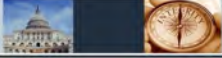
- 1. Quantity over quality.** The idea is that quantity will eventually breed quality as ideas are refined, merged, and developed further.
- 2. Withhold criticism.** Team members should be free to introduce any and all ideas that come into their heads. Save feedback until after the idea collection phase so that “blocking” does not occur.
- 3. Welcome the crazy ideas.** Encouraging your team members to think outside of the box and introduce pie in the sky ideas opens the door to new and innovative techniques that may be your ticket for success.
- 4. Combine, refine, and improve ideas.** Build on ideas and draw connections between different suggestions to further the problem-solving process.

Source: [MindManager.com](https://www.mindmanager.com)



74

## Fraud Discussions Among Engagement Personnel

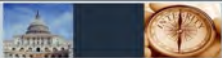


- Thoroughly probe the issues
- Consider audit responses to fraud susceptibility
- Summarize known fraud risks and control strengths and weaknesses
- **Brainstorm** ways that fraud might be committed by someone within the entity (by management or employees) or on the entity (by an outsider)
- **Evaluate** fraud schemes deemed viable or possible
- **React** by modifying planned audit tests to ascertain if fraud is occurring

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75

## Who Did It? (And What Did He or She Do?)



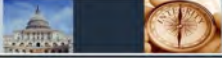
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76



## In this Case ....



- The symptoms (fraud risk factors) were discernible via
  - Careful analysis of internal control weaknesses
  - Careful analytical review
- Brainstorming—focused on these symptoms—should have lead to the potential fraud schemes
- Careful inquiries should have narrowed the focus to our two suspects
- Good audit work from there should have revealed evidence of the frauds

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77

# ***Fraud Brainstorming and Interviewing Techniques for Auditors***

Dave Cotton, CFE, CPA, CGFM

Cotton

333 John Carlyle Street | Alexandria, VA 22314  
[www.cottoncfa.com](http://www.cottoncfa.com)

78

## Worldwide Institute for Situational Ethics

### **Susan Purduper, Executive Director**

- Sue has been WISE's executive director for 4 years.
- She was selected for the position by WISE's founder, Otto Krattic, who is now chairman of the board. Sue and Otto work well together and confer frequently about policy.
- During Sue's tenure
  - membership has risen over 220%
  - revenue from fundraising and grants is up over 350%
  - administrative costs have dropped from 20% to 8% of the annual budget
  - total staffing has increased by 150% while administrative staffing has only increased by 15%
- Sue is responsible for all hiring and firing decisions including all purchasing and contracting; but she delegates most of what she considers "administrative minutia tasks."
- Everyone—particularly the board of directors—agrees that Sue has done an outstanding job of meeting the organization's mission goals and objectives.

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- Otto is a former senior Federal executive and gained prominence for his groundbreaking work in advanced situational ethics applications.
- Otto founded WISE eight years ago and initially served as both executive director and board chair.
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## Worldwide Institute for Situational Ethics

- Otto has semi-annual Board meetings at which the executive director and the programs director give updates on operational and programmatic activities and achievements, and the CFO gives updates on financial matters, primarily focusing on the annual budget and tracking actual-to-budget performance.
- Due the WISE's success and growth under Susan's management, the Board has given her great latitude in day-to-day management and decision-making. Susan makes all hiring and firing decisions and is responsible for all purchasing decisions.

### **Salvatore Amander, IT Director**

- Sal joined WISE three years ago. His previous job was as a senior IT manager for Hay, Wood, Jubusoff & Company, a CPA firm.
- When Sal arrived, the WISE IT structure was a mess. Most of the organization's computers were obsolete, the network was slow and inefficient, and WISE was not even using a broadband internet connection. WISE did not even have any sort of virus protection system; Sal found all of the entity's PCs infected with multiple viruses.
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- Sal also implemented several linked databases that integrate accounting, fundraising, membership, and conference registration information.
- Sal prepared a report that estimated that the cost savings from the more efficient systems more than offset the additional IT budget costs.
- The executive director, Susan Purduper, has been very pleased with Sal's work, and WISE has given Sal generous performance bonuses the past two years.

### **Lewis Skannon, New Board Member**

- Lew is considered to be a rising star in the field of situational ethics, having gotten his start working as campaign manager for Bill Clinton, during Bill's unsuccessful bid for governor of Alaska in 2012.
- Lew met Otto Krattic, WISE's founder, at a conference where Lew had delivered a talk entitled "*If It Sounds Good, Say It!*"
- After Otto asked Lew to join the WISE board six months ago, Lew quickly immersed himself in WISE details.
- Lew has asked many questions about WISE operations:
  - Why are we spending so much on information technology?
  - Why is publications expense rising faster than publications revenue?
  - Why have on-site conference registrations decreased so drastically in the past two years?
  - Why can't the programs director or the IT director or the CFO give me straight answers to any of my questions?
  - Why doesn't the board meet monthly?
  - ... and so forth ...
- Otto, who was initially supportive, seemed to become impatient with Lew. At Lew's first board meeting three months ago, Otto said to Lew "Maybe you should take a few months to get to know the organization better." Everyone laughed.
- Susan, however, has been very patient with Lew's questions. At the board meeting, she directed staff to get answers to each of Lew's questions "immediately, if not sooner."

### **Talia Watt, Receptionist**

- Talia is outgoing, talkative, effervescent, and pleasant at all times.
- Callers and visitors often comment to the executive director, Susan Purduper, about Talia's cheery attitude, pleasant manner, and helpfulness.
- Talia was hired by the WISE founder, Otto Krattic, not long after WISE started.
- In addition to answering the phones and greeting visitors, Talia manages office supplies, and coordinates deliveries.
- Talia also opens and sorts the mail, including invoices from vendors. She also keeps a log of accounts payable and, when she mails out checks, she notes accounts as "paid."

Worldwide Institute for Situational Ethics  
Selected Financial Information  
2013 to 2017

Attachment 2

	<u>2013</u>		<u>2014</u>		<u>2015</u>		<u>2016</u>		<u>2017</u>	
	<u>Amount</u>	<u>% of Rev.</u>	<u>Amount</u>	<u>% of Rev.</u>	<u>Amount</u>	<u>% of Rev.</u>	<u>Amount</u>	<u>% of Rev.</u>	<u>Amount</u>	<u>% of Rev.</u>
<b>Members</b>	55,295		61,899		91,756		109,873		121,985	
<b>Dues Revenues</b>	\$30,412,250	73.88%	\$34,044,450	75.27%	\$50,465,800	80.45%	\$60,430,150	82.02%	\$67,091,750	82.87%
<b>Program &amp; Grant Revenue</b>	239,075	0.58%	256,098	0.57%	635,987	1.01%	724,589	0.98%	843,575	1.04%
<b>Conferences Revenues</b>										
<b>Pre-registrations</b>	7,208,734	17.51%	7,307,543	16.16%	8,102,355	12.92%	8,765,419	11.90%	9,359,887	11.56%
<b>On-site Registrations</b>	764,097	1.86%	865,322	1.91%	871,098	1.39%	880,981	1.20%	859,031	1.06%
<b>Publications</b>	2,543,009	6.18%	2,759,080	6.10%	2,657,087	4.24%	2,875,018	3.90%	2,810,876	3.47%
<b>Total Revenue</b>	<u>\$41,167,165</u>	100.00%	<u>\$45,232,493</u>	100.00%	<u>\$62,732,327</u>	100.00%	<u>\$73,676,157</u>	100.00%	<u>\$80,965,119</u>	100.00%
<b>Fundraising Costs</b>	\$7,603,063	18.47%	\$8,511,113	18.82%	\$12,616,450	20.11%	\$15,107,538	20.51%	\$16,772,938	20.72%
<b>Program &amp; Grant Expenses</b>	255,810	0.62%	266,342	0.59%	648,707	1.03%	731,835	0.99%	818,268	1.01%
<b>Research Costs</b>	17,713,312	43.03%	20,104,208	44.45%	31,699,722	50.53%	40,799,324	55.38%	46,588,278	57.54%
<b>Publications Costs</b>	1,986,543	4.83%	2,155,333	4.77%	2,338,464	3.73%	2,537,156	3.44%	2,752,730	3.40%
<b>Conferences Costs</b>	5,320,987	12.93%	6,032,642	13.34%	6,649,415	10.60%	7,153,519	9.71%	7,583,493	9.37%
<b>Administrative Costs</b>										
<b>Salaries</b>	985,609	2.39%	1,024,541	2.27%	1,063,472	1.70%	1,102,404	1.50%	1,141,335	1.41%
<b>Expenses</b>	6,848,948	16.64%	6,246,310	13.81%	6,733,733	10.73%	5,167,589	7.01%	4,137,348	5.11%
<b>IT Costs</b>	398,876	0.97%	870,998	1.93%	985,321	1.57%	1,097,623	1.49%	1,198,526	1.48%
<b>Total Expenses</b>	<u>\$41,113,148</u>	99.87%	<u>\$45,211,486</u>	99.95%	<u>\$62,735,284</u>	100.00%	<u>\$73,696,987</u>	100.03%	<u>\$80,992,915</u>	100.03%
<b>Surplus/(Deficit)</b>	<u>\$54,017</u>	0.13%	<u>\$21,007</u>	0.05%	<u>(\$2,957)</u>	0.00%	<u>(\$20,830)</u>	-0.03%	<u>(\$27,796)</u>	-0.03%