

LINDQUIST FIRST FRAUD COURSE OUTLINE IN AUGUST 1976

Ladies and Gentlemen – We appreciate the opportunity of having discussions with you over the next four days on the subject of white collar crime, a crime which normally is caught by Section 383 of the Criminal Code. And, although we will discuss other sections of the Code, we must point out very strongly that our discussions are limited to actual cases investigated by us and such there are other areas of fraud which will not form a part of our discussions, for example, counterfeit money, as we have had no first hand experience in this very important and critical area of fraud.

The purpose of discussions will be to convey to you some thoughts to enable you to

- A. obtain some idea of white collar crime, its various forms and its contents,
- B. understand the role of professional accountants and the evidential value of that assistance,
- C. understand how the flow of money through a business is accounted and related to supporting documentation.

During our discussions we will make references to some outside reading material which we believe will be of interest and assistance to you.

We have designated ten forms or types of white-collar crime. While this is not a complete list our experience to some degree suggests that most white-collar crimes may be identified with our list:

1. **A Corporate Sham** – that is the objectives of the company are deemed criminal.
2. Where an **Officer** of a company, that is a person in authority has defrauded the owner or owners referred to as shareholders of that company.
3. Where an **Employee** of a company, that is one who has no authority has defrauded the owner or owners of that company.
4. When a company has become **bankrupt**, is it attributable to bad business or a siphoning of funds by an Officer of the company.
5. Where a **non-profit institution** is defrauded by an Officer, Employee or a Supplier.
6. Where **trading-in-the shares** of a company either through a stock exchange or over the counter market is manipulated thereby causing a fraud on the public who are solicited to buy these shares.
7. Where a legitimate company performs a **criminal act** to either maintain or improve its financial position.

8. Where money is paid to a person in authority to influence his decision, normally referred to as a **bribe**.
9. Where **money held in trust** has been misappropriated.
10. **Arson**

We feel that a good discussion of each of these types of white collar crimes will grow from our introduction of actual case work and our accounting role in the respective cases.

CASE DISCUSSIONS

1. Corporate Sham

Dare to be Great
Golden Products
Canadian Blind Associates
Sunway Distributions

Dare To Be Great/Golden Products

These two cases are based on identical principles as both the company and individuals were charged under the Lottery Section #111 of the Code. These shams involved pyramid selling as the Court ruled that the interest of both companies was to recruit leads and not to sell products.

Dare to be Great, apparently the brain-child of Glenn W. Turner, Florida based, offered four levels of tape readings to improve one's self confidence; Golden Products offered soap suds.

o/s comments from brief synopsis and Regina VS information

It was felt that an analysis of the receipts of the company and its disbursement of those receipts might circumstantially show that it was more important to recruit leads than to sell products.

With respect to Dare To Be Great this was our findings:

o/s Brief accounting report.
Then interpret report as to leads, product and commissions.

The second area of interest was the cost to the company of the product they sold relative to the sale price which then could be compared to the commission paid as a result of the sale.

o/s Accounting report

Interpretation

The third area of interest was to show through a pyramid chart that the company would absorb the world population by 1980.

o/s Schedule
Interpretation

The accounting evidence produced the incomes of those charged to show that their source was the commission earned on recruitment of people which was consistent with evidence of the sales brochures and meetings.

In a brief fashion I would like to now touch on Golden Products. The same accounting approach was applied to Golden Products.

o/s Accounting report – source and app interpretation
Individual incomes

Additional information from Golden Products financial records made the theory more conclusive. The commission earned was segregated as to product and people. With respect to very person charged, the product commission evidenced less than 1% of the person's income.

o/s Judge's remarks

Sunway Distributing

Regina VS Lucas and Lipton
o/s Case Synopsis and information

This matter again centered on the theory that the company was only interested in recruiting people; that they were only interested in selling cookie machines. Accounting work was therefore requested to determine if the financial records of the company would support or disprove the theory.

o/s Accounting report and interpretation

Accordingly, we therefore found that the company obtained all their profit through the sale of machines while it incurred a loss on the sale of the cookies. On this basis, eventually the company could not function due to the loss of cookies. The amount of money withdrawn by the principals as a percentage of the total receipts is also noteworthy. As is the length of the company's life – seven months. To substantiate the charge of defrauding the public rather than only the customers and/creditors, examples of the newspaper advertising were obtained.

Canadian Blind Associates

Regina VS Chronics and Corrigan

o/s Brief synopsis and interpretation, information

As accountants we were requested to determine all bank accounts, the source of deposits and disbursements, the benefit derived by the accused, the amount contributed to charity.

o/s Accounting report and interpretation

In the course of our work we were able to show that only 55% of all collections were deposited to the bank. The initial 45% was paid to the telephone solicitors and collectors.

o/s Judgment

The central theme to each of these four cases is that the Court determined that the reason to exist was criminal and that the criminal act resulted in financial reward to varying degrees to the accused. In other words, the public was caused to part with a valuable security, money because of belief in misrepresentations made by the above companies and their people.

2. Officer of a Company

Where an Officer of a company has defrauded the owner or owners (shareholders) of that same company.

Maple Leaf Gardens

o/s Case synopsis and information

The role of the accountants was to identify how each of the fraudulent transactions had been recorded in the records of Maple Leaf Gardens. What is a fraudulent transaction – in a few words, it is a transaction where a personal benefit has been achieved through the expense of others, for example, a shareholder.

o/s Accounting report and interpretation

o/s Judgement

Atlantic Acceptance

o/s Introduction by Hughes & Croft – history

The role of the accountants was simply to determine where the money of Atlantic was spent and to whose benefit. Due to the enormity of the case we have chosen one example which shows Morgan as its President creating corporate shams to cover the fact that he used Atlantic money for his benefit.

o/s Example

The theme is one of greed by someone who enjoys wealth and a betrayal of trust placed in him by fellow Officers, Directors and Shareholders of a company.

3. Employee of a Company

Where an employee of a company has defrauded the owner or owners (shareholders) of that same company.

Smith Transport

Regina VS L. Harvey

o/s Case synopsis and information

The role of the accountants was to determine the total loss to the company, the scheme, and the position of the accused in the company and benefit to the accused. The theory as to the existence of a loss was described by the word lapping.

o/s Definition of lapping

This is a very common method used by employee types i.e. people who have access to the company cash and cheque receipts.

o/s Book Example – theory applied to this matter

Total loss – lapping results in an overstatement of the company's accounts receivable. The acceptable way to determine how much money is due to the company is to communicate directly with the customer.

This communication is done by a letter whereby the company lists each invoice which they believe to be unpaid. The customer acknowledges which of these invoices are either paid or outstanding. This would serve as the basis for determining the amount of the loss.

The next step is to pursue the reason why the customer stated that these invoices are paid while the company's records show them as outstanding. Therefore the company should request that the customer send a copy of their cancelled cheque which paid those invoices which the company still believes to be outstanding, that is not paid.

Then the company should determine whose invoices were paid by this particular customer cheque. Several possibilities exist. The cheque from this customer might not be applied to any of his invoices; maybe to some of his invoices (usually the older

invoices); maybe it is properly applied to all his invoices. Where it is determined that the customer's cheque was not applied entirely to his invoices (i. e. those which the customer intended to pay) than each customer whose invoice was paid by this other customer's cheque should be visited to determine from him how he paid his invoice, when and does he have a receipt (usually cancelled cheque or cash receipt). If any of the invoices were paid by cash, then it could follow that to avoid later detection (the customer might be notified that his invoice is outstanding causing him to communicate directly to the company to someone other than the accused or management in its review of the aged accounts receivable listing, might question why it has not been paid) it would have to be paid. Therefore the accused would take another customer's cheque and rather than applying it to that customer's invoice it could be applied to those invoices which had been paid by cash but not processed through the company's records. Reason: the cash had been diverted.

To confirm this as a method of operation request cancelled cheques from some of the major customers along with a list of which invoices the cheques were paying. Then take a deposit which has no cash, that appears to contain some invoices which are normally cash paid invoices and visit those customers to confirm they paid the cash.

o/s Brief example: (remember to compare invoice totals by customer to cheque amounts shown on deposit slip (after giving consideration to any cash deposit also noted on the deposit slip).

In this matter, the circumstantial evidence was extremely important. Here are some Examples:

- A. Determine position of accused in the daily operation to show access to records and control from an accounting point of view.
- B. Intermediary evidence such as various reports which might identify cash payment to the company.
- C. Were losses reported while accused was sick or on holidays? Was employee dedicated and did employee take work home?
- D. Conduct a complete personal bank analysis of accused and spouse, if applicable. Review both payroll cheques to determine their bank accounts. Obtain search warrants on applicable banks to get various documents – most important is deposit slips.
- E. Where were the "paid" invoices kept by the accused before they were processed through the company's system?
- F. Determine means accused kept track of unpaid invoices (usually aged accounts receivable).

T. Johnson's Case

o/s Synopsis and information

Role of accounting was to identify where and how money was taken by the employee and how it was recorded in the company's records. The obvious was the manipulation and defalcation of documents, namely the company's cheques.

os Examples

Along with the above evidence the position of the accused is very important as she was in control of all accounting and who again was referred to as the trusted employee.

Waddilove and Steel

o/s Regina VS Waddilove and D. Steel
Synopsis and information

The role of the accountant:

- to identify all bank accounts of the customer and bank manager and determine source of deposits to these accounts and the use of the withdrawals.
- Identify the flow of money within all of the above bank accounts to show: lapping and benefits to both the bank manager and customer.
- To cause further searches at lawyers offices to locate legal documents for property purchases.
- To calculate total loss to victim (the bank)

4 .Bankruptcy Due to Poor Management (under-capitalized) or Fraud?

Sometimes, when a bankruptcy occurs, creditors and/or inspectors of the bankrupt suspect that the bankruptcy occurred due to criminal activity on part of the owner/manager. From an accounting point of view, the following factors must be considered:

- A review of cash and cheque disbursements for the previous calendar year to the owner/manager and for the previous three months to the suppliers. This should reveal any unusual siphoning of funds from the company possibly in contemplation of the bankruptcy.
- A review of revenue to determine that all money received was in fact deposited to the company's bank account. This may only be calculated from a material approach and may be determined through inventory calculations.
- A review of inventory for shortages, etc.
- Review of cheque disbursement to determine if personal payments were made by the company on behalf of the owner/manager (O/M).
- Review of short and long term financing of bankrupt to determine if any misrepresentations were made by the owner/manager to acquire credit..

- Has owner/manager provided a personal guarantee for any company indebtedness
- What time period does the insurance cover and when was it last renegotiated and for what coverage.
- If deposits are involved, what was the time period between the date of the last deposit and the date of bankruptcy?
- After interviewing customers who have lost their deposits, determine the difference between the promised date of completion of product and actual date (if produced at all)
- Examine production performance over past three months and compare to orders.
- If some orders were fill was it because:
 - o the customer threatened
 - o the order was small therefore final payment would be forthcoming
 - o dealt with customer on a on-arms length basis.

o/s Drummer Boy judgement

5. **Non-Profit Institution**

Where a Non-profit institution is defrauded by an officer, employee or supplier.

Central Fuel Oil

Regina VS Kitouski

o/s Case synopsis, brief, information

Rose of accountant to graphically illustrate the actual invoicing of fuel oil to the government school compare to the amount of fuel oil which an expert engineer deemed sufficient in view of all variables. Also relevant was the amount of work required to locate copies of documents which the accused had burned.

o/s Actual graph and accounting report

County of Grey

Regina VS D. Parks

o/s Brief synopsis, judgement on precedent of accounting schedule and summaries.

The most important role of the accountant was to identify those transactions of the County of Grey over a five year period which caused the County to be defrauded. On the basis of the initial complaint it was decided to examine all the County's purchase, rental and sale of tractors by serial number. When a serial number arose more than once it was a signal to examine the financial transactions surrounding this tractor.

o/s Brief examples

The investigation led to an examination of the records of those suppliers who had been involved in the movement of the serial numbers noted above. A question of valuation also arose in the matter of the tractors which had been traded-in on the purchase of newer tractors. While it appeared the value had been excessive (to the advantage of the accused) it was difficult to establish due to

- range of equipment condition which can be put by defense to an expert witness who was not there at the time of the trade-in
- supplier cannot remember that particular trade-in as it is one of many.

Another interesting precedent was the use of an overhead projector to enable the jury to view the documents while spoken to by the witness.

West Haldimand General Hospital

Regina VS Van de Ven

o/s Brief Synopsis and information

The role of the accountant was to determine the loss to the hospital by comparison of the day's receipts to the bank deposits and cashed money orders.

o/s Accounting report

6. Manipulation in the Trading of Shares

The purchase and sale of shares called trading is manipulated if the buying and selling does not cause an effective change in the ownership of that share. This particular transaction is termed a washed trade. The person who is the buyer and seller of that share is termed a warehouser, i.e. although he is trading he is hiding it for future gain. The term warehousing is also given to those who purchase any loose stock on the market place to maintain the price. A warehouser will either buy the stock to maintain the price or will buy and sell (wash trade) to create a false impression of unusual activity in order to cause the share price to increase by generating a buying interest amongst the public. Once this interest is generated, the warehouser can then sell (dump) the shares in his possession at a profit.

When more than one person is involved in a market manipulation, the group is said to be running the stock or running a box as they are controlling a material amount of the market activity through all their wash-trading.

Sometimes, especially when the share price is dropping, one member of the group will attempt to sell a portion of his shares (i.e. his warehousing) without the knowledge of the other members and through some other name in order to minimize his loss. This process of chickening-out is termed back-dooring.

As accountants, our role is to secure the necessary documents and produce as much as possible, an analysis of all stock market trading in the stock in question in order to identify several types of information which would, for example, identify the percentage of each day's trading volume which may be attributable to the group who are manipulating the stock.

o/s Working papers for all our (Format) stock analysis and list information we can provide (Somed/Black/Naft)

o/s Information

These stock manipulations almost always involve a salesman of a stock broker who is encouraged to push the stock to this clientele due to the payment of secret commissions by the market manipulators. This commissions are normally cash and are given to the salesman by a bagman. (see Luiano)

7. **Criminal Act**

Where a legitimate company is an owner/manager situation performs a criminal act to either maintain or improve its financial position.

o/s Brief synopsis, information

The role of the accountant was to determine the sales value of those components which were sold with the forged Canadian Standards Association (C.S.A.) labels. Then a value was placed on those forged labels which had not been distributed to the public. Items returned for credit were also considered to properly reflect the net sales value.

o/s Accounting report

MELRAN, a Division of United Products Inc.

o/s Brief synopsis and information

The role of the accountant was to determine which sales invoices which had been factured were in fact false. It was determined that the accused used the same purchase order number when preparing a false invoice. Therefore all invoices bearing the same purchase order number were removed for further investigation. From an examination of the customer's records the false invoice was determined.

o/s Brief example and accounting report

8. **Bribe**

Where money is paid to a person in authority to influence that person's decision, normally referred to as a **BRIBE**.

Royal Commission on the Building Industry

In the course of this inquiry, transactions existed which were identified as BRIBES. From an accounting standpoint the following factors are significant:

- A. The payments were made by cheque and were recorded in the company's records and claimed as an expense for tax purposes.
- B. The disbursement was normally charged to Commissions, Business Promotion or Advertising.
- C. The recipient of the money would open a bank account to deposit his cheque.

Sometimes, the payment was charged to a certain contract as work-in-progress and subsequently billed to the customers. This would require a review of actual job costs as the amount is normally immaterial to the total value of the contract and therefore not obvious if one were to analysis only the unfavourable variances.

o/s Commission report for example and subsequent criminal charges

9. **Trust Funds**

The account's role is to determine what happened to the trust funds to enable the court to compare this finding to the original intent of the funds.

10. **Arson**

From an accounting/financial position a person might put the torch to his premises for the following reasons:

- A. to collect on an insurance policy
- B. to destroy accounting and other records that might prove detrimental in a civil or criminal proceeding

With both A & B, the accountant would know the source of third party information in order to produce evidence such as financial statements with respect to (A) and

evidence of fraudulent transactions with respect to (B) on the basis that this evidence was destroyed in the fire.

The Accounting Course

Debits and credits – forget about these accounting records. Our approach is to logically set out for you in English the simple basis of speaking about the financial records maintained by any company.

3 Types

- Proprietorship - shoe box
- Partnership - records
- Limited Co.s - Business Corporation Act of Ontario
Cda Corporation Act.

- Failure to maintain financial records covered by Criminal Code Section
- Books of Account/General Ledger/ Cash Receipts Journal/ Cheque Disbursement Journal/ General Journal/ Payroll Journal (if applicable)
- Explain each of these in English
- Noting format of information and sequence of recording and supporting documentation
- Their relationship
- Tell them of Posting – how information works its way from supporting documents to the General Ledger

Other Accounting Assistance

1. Attendance at the time of search
 - a. to minimize amount of seized documents
 - b. to assist in interview of person willing to talk
 - c. to determine if other location exist for records.
2. Wording for Search Warrants
 - a. executed at banks
 - b. executed at companies
 - c. executed at brokerage houses
3. Location of documents from 3rd parties to replace documents missing from search.

