

ACCT 542 – ANALYTICS FOR DETECTING
FINANCIAL FRAUD



Syllabus – SUMMER 2019
Day of week 5:00 PM - 7:00 PM— Location JFF 331
June 24 – July 29

Professor: Douglas Farrow

Office Phone: 213-955-8389

Office Hours: *Office hours by appointment and also available via email and pre-scheduled phone conversations.*

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Course Description

Auditors are required to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, as part of forming an opinion on the financial statements. The auditors are also required to obtain reasonable assurance about whether material weaknesses exist as of the date specified in management's assessment as part of forming an opinion on Internal Controls Over Financial Reporting (ICOFR) for publicly traded companies.

The purpose of the course is to help the students develop an understanding of fraud risk from an auditor's perspective and develop a practical skillset to perform analytics in detecting financial fraud risk.

Course Learning Objectives

Through discussions, lectures, data analytics projects, case studies and a significant group project, you will learn the concepts and attain the technical knowledge that is expected of a second year financial statement auditor in the context of auditor responsibilities around the risk of fraud, as well as apply such theories and methods while analyzing real world fraud schemes. Students will, by the conclusion of the course, should be able to explain the following concepts:

- 1 A basic understanding the different types of fraud and its impact on the financial statements and internal controls.
- 2 Role of management and audit committee responsibilities around fraud risk management and governance over an entity's compliance programs.
- 3 Auditor responsibilities around assessment of risk of fraud and the specific procedures required to comply with the professional auditing standards.
- 4 Knowledge of qualitative and quantitative factors in helping external auditors identify fraud red flags (including industry specific issues) and the appropriate auditor response to those risk factors.
- 5 Hands on data analytics exercises on general ledger information to identify specific anomalous transactions and identify appropriate follow up procedures in the context of the audit.
- 6 Complete a group case study on a fraud investigation and review the auditor responsibilities in the context of the investigation, its results, remedial actions and its impact on the financial statements and controls.

Graduate Program Student Learning Outcomes

Below are the five Learning Outcomes developed for this program by the USC Leventhal faculty and administration and filed with the AACSB, the accrediting body for accounting and business schools. This course will deal primarily with Outcome #1—**Technical, Conceptual, Problem-Solving**. To a lesser extent, this course will support Learning Outcomes #2 – **Professional Development** and #4 – **Ethical Principles and Professional Standards**

1. Technical, Conceptual, Problem-Solving - Students will be competent in and be able to apply discipline-specific knowledge and skills in the fields of accounting. This learning outcome includes the development of critical thinking and problem-solving skills, as well as an understanding of the strategic role of accounting in business organizations and society.

2. Professional Development - Students will learn to communicate clearly and strategically, after considering the relevant audience, situation, and purpose of the communication. Students will learn to demonstrate the ability to work productively with others to accomplish established goals.

3. Research/Life-Long Learning - Students will be able to use relevant research databases and academic/professional literature to gain new knowledge and analyze business situations.

4. Ethical Principles and Professional Standards - Students will be able to apply ethical principles and professional standards in analyzing situations and making informed decisions.

5. Globalization and Diversity - Students will be able to demonstrate an international perspective and appreciation for diversity and cultural differences, along with their significance in global business.

Reading Materials

- **(Required)** *Financial Statement Fraud Prevention and Detection 2nd Edition* by Zabihollah Rezaee and Richard Riley, 2010.
- **(Required)** *United States Securities and Exchange Commission v. Mathias Francisco Sandoval Herrera, et al.* --- Case 1:17-cv-20301-JAL – *Order on Defendants’ Motion to Compel Production from Non-Party Law Firm* -- (“ML [law firm] contends that even the actual physical product of work product to a company’s auditors does not waive work-product protection because an independent or outside auditor typically shares a common interest with the corporation for purpose of the work product and waiver doctrines. The Undersigned [US District Court] agrees with ML [law firm] that documents shared with [auditors] Deloitte are protected from disclosure”)
- **(Required)** *Accounting Literature*
 - AU 317 – *Illegal Act by Clients*,
 - AUC 250 – *Consideration of Laws and Regulation in an Audit of Financial Statements*
 - *Section 10A of The Securities Exchange Act of 1934 (Audit Requirements)*
 - *IESBA – Responding to Non-Compliance with Laws and Regulations*
- **(Supplementary)** *Managing the Risk of Fraud and Misconduct: Meeting the challenges of a Global, Regulated, and Digital Environment* by Gircenti and Hedley, 2011.
- **(Supplementary)** *The Smartest Guys in the Room: The Amazing Rise and Scandalous Fall of Enron* by Bethany McLean and Peter Elkind, 2004
- Various class handouts, including PowerPoints, supplementary resources, cases, problems, examination materials, etc. Note: all materials are copyrighted and may not be reproduced, distributed, or displayed without express written consent of the author.

You are encouraged to bring the textbooks to each class, as part of your participation grade includes being called on in class to describe key concepts in the pre-requisite reading. Textbooks are available through Amazon.com or the USC bookstore.

ASSIGNMENTS AND GRADING DETAIL

Grading components and relative weights are as follows:

	Points	% of Total
Participation	100	10%
Presentation	250	25%
Case Study Report/Memo	200	20%
Quiz	150	15%
Final Exam	300	30%
Total	1,000	100%

Final grades represent how you perform in the class relative to other students. Your grade will not be based on a mandated target, but on your performance. Three items are considered when assigning final grades:

1. Your average weighted score as a percentage of the available points for all assignments (the points you receive divided by the number of points possible).
2. The overall average percentage score within the class.
3. Your ranking among all students in the class.

Extra Credit: 150 points (submitted any time during the semester)

Read *The Smartest Guys in the Room: The Amazing Rise and Scandalous Fall of Enron* by Bethany McLean and Peter Elkind, 2004. Submit a five-page essay answering the following questions:

- 1) Why did Enron fall? Who was impacted by this event?
- 2) In your opinion, who should be responsible for the failure of Enron?
- 3) What did you learn from this reading? Any additional observations or thoughts?

Topics and Assignments

A weekly schedule is at the end of the syllabus and includes course coverage on a weekly basis together with the exam and other important dates throughout the semester. Please note that this syllabus and assigned readings are subject to change. The field of detecting of financial fraud requires that you deal with constant change and uncertainty and our class will incorporate aspects of this uncertainty. Changes will be indicated on Blackboard and an updated course schedule will be posted. You are required to check the contents of the Content Folder at the conclusion of each week to determine course coverage, readings, assignments, guests, etc. for the upcoming week. In the absence of any changes indicated on Blackboard, follow the attached course schedule. Any updates, as well as all course-related information, will be posted on the “Course Information” folder and should be available by Friday for the coming week.

Class Participation and Professionalism

Students will be graded on their participation in class. Students who miss class will earn zero points for participation on that day and attendance is tracked by sign-in sheet. It is your responsibility to sign in for each class session and attendance only counts when a student arrives on time and stays until the end of class. Attendance does not equate to participation but attendance is required for all six class meetings.

Except for the first class, students are expected to come prepared to discuss the pre-requisite reading material and explain concepts at a high level as they are called on in class (versus volunteering). Participation points are awarded for substantive contributions to class discussions.

Presentations

Each group will be requested to identify one fraud case that impacted financial reporting and/or auditors. At the beginning of each class, the assigned group will present the case to the classmates. The length of the presentation should be 10-15 minutes. The presentation shall include but not limited to discussions on the background of the case, associated parties, investigations, and case outcomes.

Data Analytics Exercises

There will be at least one substantive data analytics in-class assignment that will introduce the students to the concept of journal entry testing through use of relevant computer assisted auditing techniques. The exercise will include the students receiving a full download of a fictitious company's journal entries, writing and applying queries against the data to identify anomalous journal entries for additional analysis.

Case Study Report and Group Evaluation

The Case Study is a significant investigation loosely based on individual and team performance. The class will be divided into groups. Each group will be provided materials for the Case Study including business background information, financial information, and data. Your group assignment will answer the questions and writing the memo outlined in the Case Study.

You will also be required to provide an evaluation of each member of your group, including yourself, to help ensure that all members of your group are full and active contributors in this assignment. You will receive materials and more details during the second class. Peer evaluations may reduce an individual score on the group project.

Quiz and Final Exam

The exam will be based on the cumulative material covered up to the point of the exam. Materials include lectures, readings, and class discussions. There will be questions based on material covered in the lectures that is not available in the text. The learning experience in this class is designed to be effective and efficient. Accordingly, content covered in reading material may not be covered in the lectures. Conversely there will not be a requirement to read the chapters that cover the lectures. Please note that there are no book chapters associated for some of the lectures and therefore attendance to all classes is critical. Both the reading material and lectures will be covered in the mid-term and final exams.

- **Quiz: 7/8/19**
- **Final Exam: 7/29/19**

Exam Make-Ups

Make-up exams will be given only if the instructor determines an extraordinary circumstance, justified by a legitimate excuse, and supported by appropriate and adequate documentation.

Assignment Submission Policy

Assignments must be turned in at the START of class on the due date reflected in the Weekly Schedule. Should you have to miss class that day, the assignment must be uploaded to Blackboard by 1:30PM on the date the assignment is due. For all types of graded material, late work will not receive full credit. A hard copy assignments are required to be turned in at the beginning of the class. Please also email all assignments to both instructors prior to the start of the class.

ADDITIONAL INFORMATION

Add/Drop Process

You may be asked to withdraw from the class if you have missed one or more classes. In addition, the professors can ask that your enrollment from the class be dropped by the program office should you miss the first class.

These policies maintain professionalism and ensure a system that is fair to all students. The following is the schedule of important dates that you should be aware of:

1	Summer mid-semester classes begin	Monday, June 24
2	Last day to add	Monday, July 1
3	Last Day to Drop without “W” and receive refund	Monday, July 1
4	Independence Day, University Holiday	Thursday – Friday, July 4 - 5
5	Quiz	Monday, July 8
6	Last Day to Drop without “W” or change pass/no pass	Monday, July 8
7	Last day to drop with a mark of “W”	Monday, July 22
8	Final Exam	Monday, July 29

Retention of Graded Coursework

Final exams and all other graded work that affected the course grade will be retained for one year after the end of the course *if* the graded work will not be returned to the student.

Technology Policy

Laptop are allowed but Internet usage is not permitted during academic or professional sessions unless otherwise stated by the respective professor and/or staff. Use of other personal communication devices, such as cell phones, is considered unprofessional and is not permitted during academic or professional sessions. ANY e-devices must be completely turned off during class time. Upon request, you must comply and put your device on the table in off mode and FACE DOWN. You might also be asked to deposit your devices in a designated area in the classroom. Videotaping or audiotaping faculty lectures is not permitted due to copyright infringement regulations and the type of content covered in class. Use of any recorded or distributed material is reserved exclusively for the USC students registered in this class.

Academic Conduct

Students enrolled in any class offered by the Leventhal School of Accounting are expected to uphold and adhere to the standards of academic integrity established by the Leventhal School of Accounting Student Honor Code. Students are responsible for obtaining, reading, and understanding the Honor Code System handbook. Students who are found to have violated the Code will be subject to disciplinary action as described in the handbook. For more specific information, please refer to the Student Honor Code System handbook, available in class or from the receptionist in ACC 101.

Plagiarism

Plagiarism – presenting someone else’s ideas as your own, either verbatim or recast in your own words – is a serious academic offense with serious consequences. Please familiarize yourself with the discussion of plagiarism in SC Campus in Part B, Section 11, “Behavior Violating University Standards” <https://policy.usc.edu/scampus-part-b/>. Other forms of academic dishonesty are equally unacceptable. See additional information in SC Campus and university policies on scientific misconduct, <http://policy.usc.edu/scientific-misconduct>.

Support Systems

Free and confidential mental health treatment for students, including short-term psychotherapy, group counseling, stress fitness workshops, and crisis intervention. <https://engemannshc.usc.edu/counseling/>

National Suicide Prevention Lifeline - 1-800-273-8255

Provides free and confidential emotional support to people in suicidal crisis or emotional distress 24 hours a day, 7 days a week. <http://www.suicidepreventionlifeline.org>

Relationship & Sexual Violence Prevention Services (RSVP) - (213) 740-4900 - 24/7 on call

Free and confidential therapy services, workshops, and training for situations related to gender-based harm. <https://engemannshc.usc.edu/rsvp/>

Sexual Assault Resource Center

For more information about how to get help or help a survivor, rights, reporting options, and additional resources, visit the website: <http://sarc.usc.edu/>

Office of Equity and Diversity (OED)/Title IX compliance – (213) 740-5086

Works with faculty, staff, visitors, applicants, and students around issues of protected class. <https://equity.usc.edu/>

Bias Assessment Response and Support

Incidents of bias, hate crimes and microaggressions need to be reported allowing for appropriate investigation and response. <https://studentaffairs.usc.edu/bias-assessment-response-support/>

Student Support & Advocacy – (213) 821-4710

Assists students and families in resolving complex issues adversely affecting their success as a student EX: personal, financial, and academic. <https://studentaffairs.usc.edu/ssa/>

Diversity at USC – <https://diversity.usc.edu/>

Tab for Events, Programs and Training, Task Force (including representatives for each school), Chronology, Participate, Resources for Students

Students with Disabilities

USC is committed to making reasonable accommodations to assist individuals with disabilities in reaching their academic potential. If you have a disability which may impact your performance, attendance, or grades in this course and require accommodations, you must first register with the Office of Disability Services and Programs (www.usc.edu/disability). DSP provides certification for students with disabilities and helps arrange the relevant accommodations. Any student requesting academic accommodations based on a disability is required to register with Disability Services and Programs (DSP) each semester. A letter of verification for approved accommodations can be obtained from DSP. Please be sure the letter is delivered to me (or to your TA) as early in the semester as possible. DSP is located in GFS (Grace Ford Salvatori Hall) 120 and is open 8:30 a.m.–5:00 p.m., Monday through Friday. The phone number for DSP is (213) 740-0776. Email: ability@usc.edu.

EMERGENCY PREPAREDNESS/COURSE CONTINUITY

In case of a declared emergency if travel to campus is not feasible, the *USC Emergency Information* web site (<http://emergency.usc.edu/>) will provide safety and other information, including electronic

means by which instructors will conduct class using a combination of USC's Blackboard learning management system (blackboard.usc.edu), teleconferencing, and other technologies.

WEEKLY SCHEDULE/READINGS/ASSIGNMENTS

Date	Topic	Readings								
1	6/24/19	Overview of class and syllabus, group assignment, and presentation schedule and introduction to Fraud (fraud types, sources, fraud triangle, etc.)								
	<table border="1" style="margin-left: auto; margin-right: auto;"> <tr> <td>Cisco Systems</td> <td>MiniScribe</td> </tr> <tr> <td>Tyco</td> <td>Bristol-Myers Squibb</td> </tr> <tr> <td>Baptist Foundation of Arizona</td> <td>McAfee, Inc.</td> </tr> <tr> <td>Rite Aid</td> <td>Cendant Corporation</td> </tr> </table>	Cisco Systems	MiniScribe	Tyco	Bristol-Myers Squibb	Baptist Foundation of Arizona	McAfee, Inc.	Rite Aid	Cendant Corporation	Assignment: Please read chapter 1 and 2 in <i>Financial Statement Fraud Prevention and Detection</i> .
Cisco Systems	MiniScribe									
Tyco	Bristol-Myers Squibb									
Baptist Foundation of Arizona	McAfee, Inc.									
Rite Aid	Cendant Corporation									
2	6/27/19	Financial Statement Fraud – management responsibility; auditor’s fraud risk responsibility; fraud risk assessment procedures; soft v hard indicators of fraud; detecting the risks and red flags of external fraud; etc.								
	In-class group exercise: Case 1: <i>BoneFix Inc.</i>	Assignment: Please read chapter 3, 4, and 5 in <i>Financial Statement Fraud Prevention and Detection</i> .								
3	7/1/19	Presentation on the fraud cases:								
	<table border="1" style="margin-left: auto; margin-right: auto;"> <tr> <td>Cisco Systems</td> <td>MiniScribe</td> </tr> <tr> <td>Tyco</td> <td>Bristol-Myers Squibb</td> </tr> <tr> <td>Baptist Foundation of Arizona</td> <td>McAfee, Inc.</td> </tr> <tr> <td>Rite Aid</td> <td>Cendant Corporation</td> </tr> </table>	Cisco Systems	MiniScribe	Tyco	Bristol-Myers Squibb	Baptist Foundation of Arizona	McAfee, Inc.	Rite Aid	Cendant Corporation	Assignment: Please read chapter 6, 7, 8, and 9 in <i>Financial Statement Fraud Prevention and Detection</i> .
Cisco Systems	MiniScribe									
Tyco	Bristol-Myers Squibb									
Baptist Foundation of Arizona	McAfee, Inc.									
Rite Aid	Cendant Corporation									
	7/4/19	Independence Day Holiday								
4	7/8/19	Quiz								
	In-class group exercise: Case 2: <i>Tax Fraud</i>	Assignment: Please read chapter 10, 11 and 12 in <i>Financial Statement Fraud Prevention and Detection</i> .								

5	7/11/19	Introduction of the case study ---- NW Residential, Inc. <ol style="list-style-type: none"> 1) Investigation overview 2) Shadow investigation (s) (privilege issues) 3) Client relationships 4) Preparation for discussion with senior management on 7/15 5) Discussions regarding the documentation/memo that will be submitted to OGC by 7/18. (i.e. structure/format of the memo, information/material to include in the documentation/memo, etc.) 	Assignment: United States Securities and Exchange Commission v. Mathias Francisco Sandoval Herrera, et al. --- Case 1:17-cv-20301-JAL – Order on Defendants’ Motion to Compel Production from Non-Party Law Firm Read the Required Accounting Literature before class: AU 317, AU-C 250, Section 10A Securities Exchange Act, and IESBA
6	7/16/19	8:00 AM CLASS Case Study – NW Residential, Inc. – Guests – CFO, Legal Counsel, and VP of Internal Audit of NW Residential, Inc. <ol style="list-style-type: none"> 1) Finalize your interview questions 2) Class interviews regarding a reported fraud 3) Preparation of documentation/memo to be submitted to OGC on 7/22 	Assignment: Please prepare the memo to DPP/OGC regarding fraud, implications on controls, financial statements, audit implications, and planned procedures to complete the audit. This assignment is due on 7/22/19
7	7/18/19	Journal Entry Data Analytics – Session #1	Assignment: Please read chapter 13 and 14 in <i>Financial Statement Fraud Prevention and Detection</i> .
8	7/22/19	Journal Entry Data Analytics – Session #2	
9	7/25/19	Session with DPP, OGC – DPP and OGC question individual groups on their documentation/memos. In-class group exercise: Case 3: <i>Darpa Company Fraud</i>	
10	7/29/19	Final exam	