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Litigation Consulting

Update

Forensic Accounting - Fraud - Business Valuation

March 2013

Article:

"The Financial Expert: An Essential Addition to the Litigation Team"

One of the most versatile tools available to the litigating attorney is an experienced financial expert. A few hours with a financial expert often saves hours of work and assists the lawyer in either settling the case or setting a more efficient and direct course towards trial. In those few complex cases that are destined to go to trial, a financial expert is imperative and can make or break a case when presented to the trier of fact.

Quite often, lawyers would rather settle a case than see it go to trial due to the large attendant costs and hours of preparation required. An experienced competent financial expert often presents such a compelling case that, with the use of tangible data, both sides are motivated to settle rather than take a chance on an unpredictable jury. Therefore, the selection of the expert is very important both as a resource value to the lawyer and as a formidable force to contend with for the opposing side. The success of the expert over time is not measured by how many trials he or she has been on the stand to offer expert opinions. The real success in a case is to present such a persuasive opinion and support for that opinion, that there is a settlement and the dispute is resolved. ([click here for article](#))

(as published in "Valley Lawyer," official publication of the San Fernando Valley Bar Association, reprinted with permission)

Recent Case:

"Embezzlement Scheme: Lessons Learned"

"I Can't Believe It Happened to Me - I Should Have Known"

The shock of realization when a victim recognizes that a trusted employee - and even a friend - has stolen from them ranges from sad to tragic. It is a very personal feeling of betrayal and violation. It strikes fear in some, grief in others, and anger in most. In my experience, it is almost always accompanied by a sense that "I should have known this was going on." The evidence of theft sheds a very bright light on the rear-view mirror. Patterns and circumstances take on a clarity that contemporaneous experience either hid or obscured. Sometimes the clarity was there but for a variety of reasons it was ignored.

The following is just such a case - the victim immediately recognized the theft and simultaneously felt incredibly stupid for "allowing it to happen." The lesson cost him several hundred thousands of dollars in uninsured losses. The recognition happened when his bookkeeper unexpectedly missed a few days of work and he ventured into the mail and opened a bank statement. The simple act of thumbing through cancelled checks from one month's bank statement prompted a phone call to his attorney who directed him to a forensic accountant.

What developed was evidence of a simple and devastatingly effective embezzlement scheme. The bookkeeper had set up vendors that were very similar to existing real vendors. For example, if the real vendor was ABC Service Company then a fake vendor was established called ABC Service Co. The bookkeeper went to the bank and set up bank accounts for the fake vendors. That was the hard part. The rest was easy. The business owner signed hundreds of checks to the fake vendors thinking the checks went to legitimate business activity.

Since that worked so well, the bookkeeper began forging checks made payable to pay the vendors, personal expenses, and provide cash gifts to family and friends. And, since all that worked without any notice by the business owner, the bookkeeper got an unauthorized increase in salary. It was bold. It was also easily discovered and should have been easily prevented.

The bookkeeper was pretty quickly arrested and has spent some serious time in jail. The following are **Fraud Prevention 101** steps that were ignored and could have prevented the fraud.

- **Know your employee.** In this particular case the business owner recounted that he knew the prior employer of the bookkeeper really well. He was aware that the bookkeeper had left the prior employer on less than positive terms but figured it was none of his business and hired the bookkeeper because of knowledge of the industry. A phone call to the prior employer/friend after the embezzlement was discovered revealed that the bookkeeper was probably stealing from the current employer to pay off a judgment obtained by the prior employer to recover embezzled funds.
- **Embezzlers tend to be repeat offenders.** This is an obvious follow-up to the prior point. A simple background check is not expensive, easy to do, and in this case would have prevented a really bad hiring decision. It would have confirmed the ill-at-ease feeling of the employer at the time of hiring.
- **Open your own mail.** Let the bookkeeper do the bookkeeping. You cannot abdicate other important (and seemingly unimportant) functions because the clerk is always around and does their job well. Vendor communications, bank statements, and bills from vendors and suppliers are important sources of information.
- **Separate functions and duties.** Many small business owners are so busy that they tend to overlook common sense when assigning work. In this case a bookkeeper was eventually given the responsibility for answering the phones, opening all the mail, writing checks, making deposits, preparing invoices, reconciling the bank statements, and preparing the financial reporting provided to the business owner and his outside tax preparer. As noted above, simply opening the mail would have prevented some of the problems - or would have caught it a lot earlier.
- **Don't accept bad answers to good questions.** When the forensic accountant arrived on-scene, the business owner requested a report showing payments to all vendors. The request was preceded with a long list of qualifications recognizing that it was difficult to put such a report together, would take a long time, and would not be precisely correct. The accountant produced the report in about 90 seconds. The business owner was shocked - and the point was made. His bookkeeper, for a long time, had prevented him from seeing the very report that exposed the whole scheme. He had been given every reason in the book why the report couldn't be produced.
- **Force vacations.** Nobody else had access to the bookkeepers work for over two years. Any other eyes on the accounting records would have exposed everything.
- **Acknowledge your instinct.** If the lifestyle of the employee exceeds what you know about their legitimate compensation there is good reason to look harder. If the bookkeeper can't produce simple reports from "the books" they are keeping there is a problem. If you feel like you are working for the bookkeeper rather than them working for you, something is wrong. If it feels like the business is doing better than ever but there isn't any cash there is good reason to find a reasonable explanation.

All of the bullets were separate points of recognition by the business owner in this case - "I knew something wasn't right. I should have known this was happening." That is never good after-the-fact.

Speeches:

Upcoming Speaking Engagements for Chris Hamilton

Chris Hamilton will speak at the "**National Judicial College**" in Reno, Nevada, March 11 & 12, 2013. Sessions/Topics: *Business Valuation, Damages, and The Courtroom from the Expert Witness Chair.*

Chris will speak in Chicago at the **Forensic Accounting Academy** on the topic "*Interviews and Interrogation,*" March 19, 2013.

"*Buy-Sell Agreements*" will be the topic for Mr. Hamilton's presentation to the **Santa Clarita Valley**

Partner Profile:

Fraud Investigation & Prevention

The ***Fraud Investigation & Prevention*** practice is headed by partner [Chris L. Hamilton, CPA, CFE, CVA, DABFA](#). Mr. Hamilton is a Certified Public Accountant, Certified Fraud Examiner, Certified Valuation Analyst, and a Diplomate with the American Board of Forensic Accounting. He is a licensed life and disability insurance agent and a General Securities Representative. Mr. Hamilton has published articles in several publications, and has made presentations at national conferences, training institutes and seminars on topics including forensic accounting, fraud and business appraisal.

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