

Chapter 2: Introduction to Asset Misappropriations

Sharon Curry, CFE

What is a Misappropriation?

- *Misuse* of a company asset for personal gain
- Includes more than theft or embezzlement
 - Use of company computer to surf the net
 - Company car for personal trips, etc.
 - Steal cash
 - False invoicing, etc.

Defining Assets

- Assets = resources owned by the organization
- Two categories:
 - Intangible Assets
 - Tangible Assets

Intangible Assets

- Not physically identifiable
- Usually represented by contractual right
- Examples:
 - Patents, trademarks, leaseholds
 - Goodwill
 - Trade secrets

Tangible Assets

- Five principal types:
 - Cash
 - Accounts receivable
 - Inventory

- Plant and equipment
- Investments
- Most asset misappropriations involve tangible assets (especially cash)

How Asset Misappropriations Affect Books of Account

- Assets = Liabilities + Owner's Equity
- Asset Misappropriation causes \$ for \$ set-off to owner's equity
- Affects balance sheet via income statement
- Revenue – expenses = profit
- Asset misappropriation essentially an expense of doing business
- But we don't know how big the expense is or when it occurs

The Accounting Entry for Fraud

<u>Debits</u>	<u>Credits</u>
Expense	Cash
Asset	Cash
OR:	
Revenue	
Liability	Cash
Equity	

Concealing Asset Misappropriations

- Out-of-balance Conditions
- False Debits
- Forced Balances
- Omitted Credits

Concealing Asset Misappropriations

False debits

- To expenses (most common)
 - Expenses are not tangible (can't be inventoried)
 - Expense accounts closed to zero at end of year
- To assets
 - Commonly debit accounts receivable
 - Debit to asset easier to detect
 - Stays on books

Concealing Asset Misappropriations

- Omitted credits
 - Concealment technique for cash skimming
 - Pocket cash, no credit to sales
- Out-of-balance conditions
 - Asset removed from business (debit)
 - No corresponding credit
 - Perp hopes nobody notices

Concealing Asset Misappropriations

Forced balances

- Variation of out-of-balance technique
- Instead of a false entry to cover loss, perp simply adds wrong, carry false totals
- Used by perps with access to the books

Classifying Asset Misappropriation Schemes

Median Losses - Cash v. Non-Cash

- Median cost of non-cash schemes was higher than that of cash schemes
- Non-cash schemes: thefts of inventory, equipment, proprietary information, etc.

Classifying Cash Schemes Cash Schemes - Median Losses

- Among cash schemes, fraudulent disbursements have the highest median loss.
- Larceny is both the least common and least costly method of cash fraud, on average.