

Fraud: Ensuring Integrity in Financial Reporting

Table of Contents

Chapter 1 – The Need for Financial Reporting Reform	1
Learning Objectives	1
Manipulation of Financial Performance	1
Improper Revenue Recognition	1
Inappropriate Earnings Management Practices	3
Concealed Liabilities and Expenses	4
Stock Option Backdating	5
Under-Reporting of Stock-Based Compensation	6
Overstated Pension Plan Assumptions	6
Use of Pro Forma Results	6
Errors and Violations	8
Financial Restatements	8
SEC Staff Comment Letters	10
SEC Enforcement Actions	12
Poor Corporate Governance	13
Audit Failures	13
Ineffective Board Oversight	15
Review Questions	17
Review Answers	18
Chapter 2 – Protecting Investors	21
Learning Objectives	21
Accounting for Stock-Based Compensation	21
Background	21
The Measurement Basis	22
Alternatives to Stock Options	26
SEC Regulations	27
Analyst Conflicts of Interest	27
Mutual Funds' Broker Rewards	28
Insider Trading Disclosures	28
CFA Institute Research Objectivity Standards	29
Research Objectivity Policy	29
Public Appearances	30
Reasonable and Adequate Basis	30
Investment Banking	30
Research Analyst Compensation	30
Relationships with Subject Companies	31
Personal Investments and Trading	31
Timeliness of Research Reports and Recommendations	31
Compliance and Enforcement	31
Disclosure	31
Rating System	32
Review Questions	33
Review Answers	34
Chapter 3 – Restoring Investor Confidence	37
Learning Objectives	37
Key Features	37
Oversight of Accounting Firms	39
Section 102: Mandatory Registration	39
Section 103: Cooperation with CPA Groups	40
Section 104: Annual Inspections	40
Section 105: Investigations	40
Section 105: Enforcement	40
Section 106: Foreign Public Accounting Firms	40

Table of Contents

Reforms of Corporate America.....	40
Section 303: No Lying to the Auditor	41
Section 301: Audit Committee Responsible for Public Accounting Firm	41
Section 301: Audit Committee Independence	41
Section 301: No Listing on National Exchanges for Violators.....	41
Section 304: Forfeiture of Bonuses and Profits.....	41
Section 305: Equitable Relief	41
Section 306: Prohibition of Insider Trading During Pension Fund Blackout Periods.....	41
Section 401: Enhanced Financial Disclosures	41
Section 402: No Personal Loans	42
Section 403: Disclosures of Transactions Involving Management and Principal Stockholders	42
Section 404: CEOs & CFOs Must Enact Internal Controls	42
Section 404: CEOs & CFOs Required to Affirm Financials	42
Section 406: Code of Ethics for Financial Officers	42
Section 407: Financial Expert Requirement.....	42
Section 409: Real Time Disclosures.....	42
Section 803: Debts Not Dischargeable in Bankruptcy.....	42
Section 840: Expanded Statute of Limitations for Securities Fraud	42
Section 906: Criminal Liability of Corporate Officers	42
Improvements in Audit Quality	44
Strengthening Auditor Independence	44
Section 201: Most Consulting Banned for Audit Clients	44
Section 202: Disclosure to Investors	45
Section 203: Audit Partner Rotation Required	45
Section 204: Auditor Reports Directly to the Audit Committee.....	45
Section 206: Conflicts of Interest.....	45
Adopting Auditing Standards.....	46
Internal Control Reporting Requirements	48
General Rules.....	48
The Principles of ICFR.....	49
Responsibilities.....	49
Significant Deficiencies and Material Weaknesses	53
Role of the Audit Committee	56
Disclosure Controls and Personal Accountability.....	59
Certification of Financial Reports.....	59
Crime Penalty Enhancements	61
Cybersecurity Systems and Risk Reporting Act.....	62
Review Questions.....	64
Review Answers	66
Chapter 4 – Promoting Accountability and Transparency.....	71
Learning Objectives	71
Business Ethics	71
Factors Influencing Business Ethics.....	71
Corporate Ethical Development Model	72
Codes of Ethical Conduct.....	73
Corporate Social Responsibility.....	76
The Concept of Social Responsibility	76
Principles of Social Responsibility	76
Legal Aspects of Social Responsibility	79
Principles of Good Governance.....	81
NYSE Corporate Governance Standards	83
Code of Conduct for Management Accountants	84
Review Questions.....	86
Review Answers	88
Glossary.....	91
Index	95