The 2014 AICPA Survey on International Trends in Forensic and Valuation Services
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EXECUTIVE SUMMARY

As part of its commitment to serving member needs, the AICPA Forensic and Valuation Services (FVS) Section regularly surveys FVS professionals to get a sense of the state of practice today and of the trends these professionals will be facing in the short term. The FVS Section undertook a landmark survey that gathered input from a range of sources. This is the first survey that has been distributed to both AICPA and CPA Canada members, marking its debut as an international study.

Forensic accounting services generally involve the application of specialized knowledge and investigative skills possessed by CPAs to collect, analyze and evaluate evidential matter and to interpret and communicate findings in the courtroom, boardroom or other legal/administrative venue. Valuation services are the application of specialized knowledge, approaches and methods to establish a determination of value. Professionals specializing in forensics and valuation provide services to their clients, who are often attorneys and businesses across an array of industries.

One of the most notable findings in the 2014 survey was the appearance of electronic data analysis — or big data — at the head of the top issues list. While technology concerns weighed in at No. 5 on the list in the 2011 survey, it was surprising in 2014 to see a tech issue replace hiring and retaining qualified staff, a perennial concern throughout the profession and in the specialized FVS sector in particular, in the No. 1 spot. Staffing, in fact, dropped to No. 5 on the most recent survey list. Since by all accounts conditions in the CPA hiring market have only tightened in the last two years, it is possible that big data moved to the top of the list due to greater public awareness of the subject, which has prompted deeper attorney and client awareness of its potential uses.

Overall, the survey indicated healthy demand for forensic and valuation services and strong prospects for their future. A total of 76% of forensic and 54% of valuation respondents expected their practices to grow with the majority expecting growth of between 10% and 50% over the next two to five years.

The vast majority of respondents to this survey has experienced or is expecting to experience increased demand for their services. For example:

▶ Thirty-eight percent of survey respondents expect a jump in prepackaged bankruptcies in the next two to five years

▶ In the family law area, 35% reported taking on more divorce cases

▶ Within valuation services, 21% of respondents experienced a 10% to 25% increase in services during the last year
In some cases, the survey asked respondents to make predictions about trends in specific practice areas. To that end, 29% thought valuation of assets carried at fair value would be the most prevalent financial statement misrepresentation issue in the next two to five years, while 26% cited inadequate disclosures of material transactions and fraud, and 23% pointed to revenue recognition. Within the fraud arena, 58% thought financial statement fraud committed by company personnel would increase in the next two to five years, about one-third predicted fraud by company personnel in collusion with third parties, and 10% expected a rise in fraud by third parties.

Regarding professional requirements, when asked what credentials respondents require of those providing forensic accounting services, a CPA was the most frequently required credential. The CPA, coupled with the Certified in Financial Forensics (CFF®) credential, provides the most desirable combination of credentials in the areas of: fraud prevention, detection and response; financial statement misrepresentation; damages calculations; bankruptcy; and electronic data analysis. Likewise, the CPA coupled with the Accredited in Business Valuation (ABV™) credential was the most widely desired combination of credentials for valuation engagements.

The AICPA FVS Section also commissioned a study of professionals in business and industry (B&I) to gather their feedback on working with forensic and valuation professionals. The survey results provide valuable information for CPAs on the trends affecting their clients, how they are responding to those trends, and which services they may need from outside experts.

More than half of the survey respondents (53%) had experienced fraud in the past year. Among other insights about FVS professionals in B&I, the survey offered a unique opportunity to gauge what kinds of fraud prevention techniques are being used. Given the variety of approaches, the most popular response was general internal controls (83%), followed by division of responsibilities (77%) and appropriate oversight by management and directors (76%).
THE RESPONDENTS

Who Participated

There were 443 professionals who responded to the survey; 182 were dedicated FVS practitioners and 261 professionals in business and industry. Of the dedicated FVS practitioners, 55% worked in public accounting or consulting firms. The second largest group — 23% — worked in business and industry. Exhibit 1 provides a complete overview.

The respondents were an experienced group, with two-thirds or more having 10 or more years of experience in their niche and 36% having 20 years or more on the job. Respondents in firms offered a range of services, but the top categories were:

- Fraud prevention, detection and response (44%)
- Valuation (37%)
- Economic damages (31%)

Exhibit 1

PARTICIPANTS

- Public Accounting or Consulting Firm 55%
- Business and Industry 23%
- Education 3%
- Government, including regulatory bodies 9%
- Law Enforcement 1%
- Other 9%
The largest group — 30% — came from organizations with one to five accounting professionals and a total of 48% worked in organizations with 20 or fewer accounting professionals. In 79% of all the organizations represented, the accounting professionals spent no more than 25% of their time on forensic and valuation services. Only 15% of the professionals worked full time on forensic and valuation services. A total of 31% said that up to 25% of their individual total hours were generated from forensic and valuation services during the past year, while at the opposite end, 28% said that more than 75% were. About 30% used a third party to support and supplement their resources in providing forensic and valuation services.

Optimism About the Future

The respondents were very enthusiastic about the opportunities for forensic and valuation services. A total of 76% of forensic and 54% of valuation respondents are expecting growth with most anticipating between 10% and 50% growth in their practice over the next two to five years. Of the 76%, roughly 33% overall expected up to a 10% increase in demand for their services in the coming two to five years. Another 30% anticipated up to a 25% rise in demand, and about 13% were looking to a 50% or higher spike. Twenty percent foresaw no change, and about 4% expected a decline in demand.

No doubt one contributing factor was the belief — held by two-thirds of respondents — that there would be an increase in litigation and regulatory enforcement during the next two to five years.

Exhibit 2

What Services Were Offered?

AREAS OF PRACTICE

- Bankruptcy and Insolvency 12%
- Electronic Data Analysis 13%
- Economic Damages 31%
- Family Law 16%
- Financial Statement Misrepresentation 27%
- Fraud Prevention, Detection and Response 44%
- Valuation 37%
- None of these 29%
TOP ISSUES

One of the hallmarks of every FVS Trend Survey is the respondents’ opinion on the top five issues facing forensic and valuation professionals over the next two to five years. The major issues this year were a departure from those identified in the 2011 survey, and they may be a surprise for many FVS professionals. The comparison between the two surveys can be found in Exhibit 3, but here are some key points.

- **Electronic data analysis** — another term for the buzzword “big data” — did not appear on the list in 2011 but jumped to number one this year. (For one practitioner’s take on big data, see Case Study 2 on page 9.) As shown in Exhibit 2, only 13% of respondents said they practiced in this area, but electronic data analysis may be called for in a variety of other engagements.

- **Attracting and retaining qualified staff slipped to number five from number one last time.** Although this seems like a dramatic change, there are many reasons to believe that hiring and retention are still critical concerns for FVS practitioners. The CPA profession as a whole is seeing more demand for talent as the economy rebounds and the baby boomers head into retirement. (For a look at smart succession steps in an FVS practice, see Case Study 1 on page 7.) At the same time, the need to find the right people can be particularly acute in specialized areas such as forensic and valuation services. While staffing may have slipped from the top place, it undoubtedly remains a key concern for those in this practice area.

- **Increased complexity and scrutiny remain as challenges for CPAs** as their approaches and methodologies come under greater scrutiny by judges and governing bodies. Taking second place in this year’s survey, this issue replaces a somewhat related issue — keeping abreast of regulatory changes — from 2011.

- **Although concerns about the economy dropped off the list this year,** competition and fee pressure remain important issues for FVS practitioners.

Exhibit 3

Top Five Issues Facing Forensic and Valuation Professionals Over the Next Two to Five Years

<table>
<thead>
<tr>
<th>2014 ISSUES</th>
<th>2011 ISSUES</th>
</tr>
</thead>
<tbody>
<tr>
<td>Electronic data analysis</td>
<td>Attracting and retaining qualified staff</td>
</tr>
<tr>
<td>Increased complexity and scrutiny in engagements</td>
<td>Keeping abreast of regulatory changes</td>
</tr>
<tr>
<td>Competition and fee pressure</td>
<td>The economy</td>
</tr>
<tr>
<td>Regulatory changes</td>
<td>Competition and fee pressure</td>
</tr>
<tr>
<td>Attracting and retaining qualified staff</td>
<td>Technology</td>
</tr>
</tbody>
</table>
Case Study 1: Succession Planning in a Niche Practice

Getting an early start is the key to succession planning at The Koerber Company PA, a boutique business valuation and forensic accounting practice in Hattiesburg, MS. As an example, the six-person firm has one young professional who was hired directly out of college and who has been with the firm for six years. “We’ve worked with him over time to ensure he gets the training and skills he needs,” including attendance at the AICPA Expert Witness Skills Workshop, says Jim Koerber, CPA/ABV/CFF, CVA, CFE. To enhance their skills and confidence, Koerber likes to start young professionals with small but important projects, such as straightforward divorce or court-appointed work.

But the firm’s outreach begins before students graduate from college. “Hiring interns who are in school allows you to evaluate their work ethic and their aptitude for this work and to introduce them to it,” he says. “It has worked very well for us.” The firm is about to hire a woman who has just completed her master’s degree and who has worked for the firm as an intern for two years. Koerber is also considering expanding his outreach beyond students in accounting programs, to include those getting master’s (degrees) in subjects such as economics or finance.

Reputation is an important element in the success of an FVS practice, which is why Koerber has encouraged young professionals to speak before Beta Alpha Psi chapters, to present continuing legal education seminars and to write articles that have been published in the Mississippi Society of CPAs newsletters. Finally, when Koerber goes on site visits, he brings a young professional along so that clients get to know them and so that they have first-hand experience working with them. “Don’t look at the short term,” he advises other practitioners. “It can take up to five years before people really master this area.”

Koerber also works to educate students and prospective candidates about forensic and valuation services, with which many are unfamiliar. His firm accomplishes this through the presentations for accounting students and through classes Koerber has taught at LSU in Baton Rouge. In his class, Koerber tries to build a sense of excitement by, for example, dividing the group into plaintiffs and defendants and having them work through a case. “After each class, I would get emails inquiring about openings at the firm,” he says.
INSIGHTS INTO PRACTICE AREAS

Electronic Data Analysis

The research company Gartner Inc. defines big data as “high-volume, high-velocity and high-variety information assets that demand cost-effective, innovative forms of information processing for enhanced insight and decision-making.” In simple language, it’s about accessing and analyzing voluminous amounts of information. At the end of 2013, International Data Corporation forecasted that the big data technology and services market would grow at a 27% compound annual growth rate to $32.4 billion through 2017, which would be roughly six times the growth rate of the overall information and communication technology market.

This year’s results clearly indicate that this surge is having an impact on FVS professionals, even if they don’t work directly in this practice area. Much of the interest may be driven by clients. A full 53% reported that their clients were developing in-house capabilities to address electronic data analysis needs. Not only did electronic data analysis lead the top issues list this year, but also 85% of respondents expect to see an increase in time spent on electronic data analysis.

Information security is another critical concern for FVS professionals. The survey asked respondents about looming threats in this area, and their answers are shown in Exhibit 4.

Exhibit 4

Over the Next 2 to 5 Years, What Will Be the Biggest Information Security Threat for Organizations?

<table>
<thead>
<tr>
<th>SECURITY THREAT</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cybersecurity</td>
<td>40%</td>
</tr>
<tr>
<td>Malicious insiders</td>
<td>14%</td>
</tr>
<tr>
<td>Personal devices in the workplace</td>
<td>14%</td>
</tr>
<tr>
<td>Cloud computing</td>
<td>11%</td>
</tr>
<tr>
<td>Social networking</td>
<td>8%</td>
</tr>
<tr>
<td>Big data repositories</td>
<td>6%</td>
</tr>
<tr>
<td>Remote access</td>
<td>4%</td>
</tr>
<tr>
<td>Other</td>
<td>2%</td>
</tr>
<tr>
<td>Supply chain security</td>
<td>1%</td>
</tr>
</tbody>
</table>
Case Study 2: Big Data Moves to Center Stage

Although the buzz about big data has certainly been growing, electronic data analysis, which topped this year’s list of top issues for FVS practitioners, is not new to CPAs in this area. “It’s something we’ve been dealing with for some time,” notes Tim Bryan, CPA/CFF/CITP, CISA, EnCE, a forensic accounting and technology services senior manager at Crowe Horwath in Sacramento, CA. The important changes that have moved it to center stage include new technologies that support greater data mining and the fact that clients have developed a more sophisticated understanding of its potential. “They are demanding a higher level of data analysis capabilities,” Bryan says.

He describes one recent engagement that involved a governmental agency whose investigation of a company required an analysis of all sales data for that entity over a three-year period. “With every transaction, the company is going to generate a lot of data, so we were working with about 60 million lines of data that had to be synthesized into something the attorney could use to defend the client,” he explains. Key considerations include data validation. “Tying the data to a source that you know is complete and accurate is the biggest challenge, followed by getting it into a useable format.” This case required taking the data out of a SQL server (a database that implements the structured query language) and moving it to the firm’s own SQL server.

New Skills Required

This work requires a broader set of skills. “Spreadsheet tools are no longer good enough,” Bryan says. “Database experience is vital for CPAs in these cases. At our firm, we have invested in people with this experience and given them database training opportunities and encouraged obtaining certifications. Spreadsheet tool capabilities stop at around 1 million rows of data, which is powerful but not enough for a case like this one.”

CPAs also must be able to slice and dice all that data to make sense of it. “We are running queries and sampling data by query to understand it and make sure we have a good understanding of the data,” he says. “The analysis is driven by the need to answer a query or test a theory raised by your side or a claim from the other side. We are analyzing massive amounts of data, trying to synthesize it to validate or invalidate a theory.”

The availability of big data is behind several new cases that Bryan has seen in wage and hour litigation. State and federal labor laws require employers to offer workers a certain amount of break time and an uninterrupted lunch break. Employees must clock in or out before and after each break or lunch, but if they are required to do so five minutes early, say, that could add up to significant overtime during a year. In one case, “we’re downloading years and years of timeslip-level data on every single employee,” Bryan says. “It will all be used to determine trends and whether the employees are getting their breaks and meal times.” Wage and hour litigation is not new, but there is a new demand for an analysis of raw data. “At the end of the day, data is going to tell the truth,” he notes.

Gearing Up

In his hiring, Bryan is seeking people who can add IT abilities to their CPA skill set. “In addition to a CPA, I look for course work or minors in information systems,” he says. “We also offer internal training. We have one person doing continuing education in university-level classes in R, a programming language.”

One potential stumbling block for organizations is the failure to have the requisite systems to efficiently and effectively manage data analytics. “You have to beef up your systems and hardware and know how to use them,” he says. New approaches require taking a more holistic approach that goes beyond sampling to consider every transaction. Bryan recommends taking some data analysis courses related to big data which can easily be found online and are often free. “It’s a great way to introduce yourself to the subject, and the price is right,” he says. “When clients need data analysis, they think of CPAs, and they expect us to have the skill set to get it done.”
Bankruptcy

When it came to prepackaged bankruptcies, a healthy 38% expected an increase over the next two to five years. What are respondents working on now? A total of 7% said that corporate bankruptcy made up 76% to 100% of their practices, while another 9% said it made up 11% to 40%. Personal bankruptcies made up a much smaller portion of their work.

The top five roles being performed in bankruptcy practices demonstrate the range of roles that FVS professionals can play in this area. They were:

- Expert for receiver/trustee
- Expert for creditors’ committee
- Expert for debtor
- Restructuring consultant
- Fresh-start accounting

Case Study 3: The Advantages When Bankruptcy and Fraud Teams Join Forces

FVS practitioners are used to working with attorneys and other professionals. One CPA has seen the value of combining the knowledge from two areas, bankruptcy and forensics, under the FVS umbrella. Corey Anne Bloom, CPA/CFF, CA, CA-IFA, CFE, a partner of the firm of MNP LLC in Montreal, Canada, believes that there often is an assumption that bankruptcy is due to mismanagement. But it can also be a result of fraud, or even a combination of both.

She believes that the complexity and/or magnitude of the fraud or suspected fraud can be a factor in determining when bankruptcy professionals should turn to forensic examiners to assist with the mandate. In these situations, the role of the CFF or IFA may vary. It may include: the gathering and securing of the evidence, including electronic evidence; performing forensic analysis; identifying improper or irregular transactions; and assisting in the recovery of the funds. “The forensic team may also assist with technology and call upon its forensic technology services to secure evidence and protect data,” Bloom says.

In a case involving the bankruptcy of a large complex real estate investment company, the trustees suspected that fraud may have been present and invited the forensic team to review detailed information. The forensic team assisted in the determination of whether fraud indicators were in fact present and whether fraud had played a key role in the company’s bankruptcy.

Bloom’s advice is simple. She advises professionals to get the right team and expertise in place in a bankruptcy case where fraud is suspected. That may include the team having knowledge of a variety of areas including, amongst others, forensic IT, accounts receivable and payroll. She concludes, “If you’re not sure if you’re dealing with fraud in a bankruptcy situation, bring in the forensic experts. There are a lot of benefits when offices encourage bankruptcy and forensics professionals to work together.”
Damages Calculations

To offer FVS professionals an overview of what their peers are doing in practice, the survey questions in this area generally focused on practical approaches. For example, the survey found that when it comes to damages calculations, 64% are using a hybrid approach, 20% ex ante and 16% ex post.

The survey also asked whether respondents calculated damages for:

<table>
<thead>
<tr>
<th>Time Period</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 year</td>
<td>11.32%</td>
</tr>
<tr>
<td>1 year</td>
<td>3.77%</td>
</tr>
<tr>
<td>3 years</td>
<td>22.64%</td>
</tr>
<tr>
<td>5 years</td>
<td>35.85%</td>
</tr>
<tr>
<td>10 years</td>
<td>4.72%</td>
</tr>
<tr>
<td>In perpetuity</td>
<td>21.70%</td>
</tr>
</tbody>
</table>

When discounting future damages back to present value, 76% used both assumptions and a discount rate. Sixteen percent used only the discount rate and 8% used assumptions. Forty-one percent were involved in damages cases involving breach of contract, 31% business torts, 27% mergers and acquisitions, 24% intellectual property, 24% each for personal injury and employment, 16% wrongful death and 15% unfair competition. Thirty-nine percent said that economic factors had changed their approach to the damages assessment.

In predicting future demand, 35% foresaw more interest in breach of contracts, 32% in intellectual property, 27% increase in business torts cases, 22% in mergers and acquisitions, 19% in employment, 13% in unfair competition, 12% in personal injury and 7% in wrongful death. Forty-six percent of respondents said the cases in which they were involved never went to trial.

Family Law

This remains a solid practice area, with many professionals seeing growth. In fact, within the last year, 35% saw a jump in divorce cases and another 60% maintained the same number of engagements. When asked the reason for that increase, the most popular choice was the economy, which was cited by 19% of respondents. This may be because a stronger economy has enabled couples to afford two households and made them more willing to split or sell assets now that asset values have risen again.

Daubert Doings

Among those to whom it applied, 83% had found 10% or fewer of their cases subject to a Daubert challenge, while 6% had faced these challenges in 14% to 49% of their cases and 3% in 50% to 100%. In cases where an opinion or testimony had been challenged, the most likely causes were methodology (21% of participants), lack of evidence (8%) or qualifications (7%).
Among other key findings:

- 40% have seen an increase in alternative dispute resolution, with the largest jump in the use of mediation, followed by arbitration, collaborative resolution and binding arbitration.

- Thirty-four percent had seen greater use of mutually agreed upon experts and 14% had seen a rise in court-appointed experts. A total of 27% had spent up to 25% of their time serving as a joint expert.

- Forty-four percent spent up to 25% of their time tracing separate property as a key component of their tasks. The majority of cases in which respondents were involved (66%) never went to trial.

Exhibit 5

In Family Law Cases, What Types of Analyses Do You Perform?

<table>
<thead>
<tr>
<th>Analysis</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Valuation</td>
<td>40%</td>
</tr>
<tr>
<td>Equitable distribution</td>
<td>19%</td>
</tr>
<tr>
<td>Marital vs non-marital</td>
<td>16%</td>
</tr>
<tr>
<td>Separate vs community property</td>
<td>13%</td>
</tr>
<tr>
<td>Standard of living</td>
<td>11%</td>
</tr>
</tbody>
</table>
Valuation

This was another area in which strong growth was expected. Ten percent had a 25% increase in services during the last year, and 11% enjoyed a 10% rise. A total of 54% of respondents expected more demand for valuation services over the next two to five years.

When asked an open-ended question about areas in which they had seen issues emerge during the last year, areas they cited included:

- Changes in estate tax provisions
- Closely held systematic risk premium determinations
- Competitive bidding for work
- Contributory asset charges
- Cost competition
- Fair value (including the impact of new private company reporting standards)
- Incorporating the recession into both current data and future assumptions
- Intangible assets
- Municipal property assessment fluctuations
- Purchase price allocations
- Risk scoping
- Shareholder disputes
- Valuation of complex financial instruments
- Technical requirements for contingent analysis (especially for contingent consideration in purchase price allocations and use of simulations)
- Emerging use of quantitative models for discounts for lack of marketability on tax engagements

Respondents had seen a rise in demand for:

- Shareholder or partner dispute cases 49% (see Case Study 4 on page 20 for more on these disputes)
- Contractual disputes 44%
- Litigated valuations 40%
- Gift and estate 36%
- Family law/marital dissolution cases 35%
- Industry specialization 32%
- Fair value for financial reporting 30%
- Bankruptcy, insolvency and reorganization 22%
- Non-cash compensation valuation 18%
- Employee stock ownership plans 17%

Areas they believed were most likely to experience increased demand in the next two to five years were:

- Shareholder/partner disputes 34%
- Litigation services 29%
- Contractual disputes 25%
- Family law/marital disputes 25%
- Gift and estate taxes 18%
- Bankruptcy, insolvency, reorganization 15%

Thirty-five percent of valuation respondents had 10 or more years of experience in valuation. Thirty-seven percent, the largest group, worked in firms with up to five professionals, and a total of 56% worked in firms with 20 or fewer. The largest segment, 42%, had devoted up to 25% of their individual hours to valuation in the past year. Thirty-four percent used help from an outside third-party to provide services.

In considering how their valuation practices had changed their uses of resources:

- 16% had increased their use of third-party resources
- 16% had added valuation professionals

Only 13% had noticed more law firms bringing valuation professionals in house, and among that group, 21% had seen a resulting impact on the engagements they received from those firms.
Most did not believe their practices would be affected by standards being proposed by the Private Company Council (65%), but 32% thought they would be somewhat affected and 3% highly affected.

**Financial Statement Misrepresentation**

What kinds of misrepresentation did respondents expect to see in the near future? Twenty-nine percent believed valuation of assets carried at fair value would be the most prevalent financial statement misrepresentation issue in the next two to five years. Another 26% cited inadequate disclosures of material transactions and fraud, 23% tapped revenue recognition and 14% the treatment of off-balance-sheet assets and liabilities. Seventy-four percent expected that allegations of inadequate control over financial reporting would be a prevalent issue in conjunction with other issues in the next two to five years, while 14% saw it as a prevalent standalone issue. The rest did not believe it would be significant. Investing and wealth management entities were most likely to experience the most allegations of financial statement representations in the respondents’ opinion (43%), followed by lending institutions (15%), service organizations, such as health care (11%) and high tech companies (10%). Seventy percent of respondents said their financial statement misrepresentation cases never went to trial.

**Fraud**

Fifty-eight percent expected that financial statement fraud committed by company personnel would increase in the next two to five years, 32% anticipated fraud by company personnel in collusion with third parties, and 10% expected a rise in fraud by third parties. During the same period, another 55% thought that embezzlement committed by company personnel would rise, 37% expected more embezzlement by company personnel in collusion with an outsider and 8% foresaw more from third parties.

In the cases in which respondents were involved, fraud was detected using:

- Internal inquiry or tipoff 39%
- Whistleblowers 36%
- By accident 35%
- Internal audit 20%
- External inquiry or tipoff 14%
- External audit 12%
- Law enforcement investigation 11%
- Regulatory investigation 9%

Looking ahead over the next two to five years, respondents thought there could be significant improvements in preventing fraud by using internal computer-based tools (86%), internal new employee screening (73%), an internal fraud risk management program (70%), internal physical controls (68%) and internal whistleblower hotlines (56%). Among external controls, respondents thought improvements would be seen due to external whistleblower hotlines (56%), external (SEC or IRS) computer-based controls (55%), external (SEC or IRS) increased and better trained internal audit (44%), an external fraud risk management program (44%), external enforcement of comprehensive vendor and employee codes of conduct (37%), external new employee screening (36%), external physical controls (35%) and external current employee screening (30%).

In the wake of the new SEC whistleblower rules and recent fraud cases, 48% did not use an investigative response plan, 35% did not plan changes and 17% did. Forty-one percent of the organizations did not provide fraud risk training, but 36% had increased this training because of recent developments. The training they believed was most useful was forensic accounting and investigative procedures (51%), the nature and vulnerability of technology, including computers (20%), knowledge about internal control in general and fraud risk in particular (13%), knowledge about computer-driven internal controls (9%) and auditing standards (6%). Fifty-eight percent of the fraud cases in which respondents were involved did not go to trial.
BUSINESS AND INDUSTRY RESPONDENTS

Where Did They Work?

A total of 56% of business and industry respondents worked in privately held U.S. companies, 22% worked in public companies, 13% in government, education or not-for-profits, 5% worked for foreign employers and 4% for others.

Twenty-five percent were employed by organizations with revenues of $1 billion or more, while 22%, the next largest segment, worked for companies with $10 million to $50 million in revenues. Twenty-one percent were in companies worth $10 million and under, while 11% worked for those worth $50 million to $100 million. The largest percentage — 17% — worked in manufacturing, followed by 12% in finance or insurance, 7% in banking and 6% for a health care provider. The organizations involved employed CPAs with valuation skills in the accounting/controller function (51%), corporate finance (30%), tax (20%), treasurer (12%) and acquisitions (9%). A total of 53% of the organizations used third-party vendors to provide valuation services. Thirty-eight percent of those were chosen based on a referral from the external auditor, 21% based on a referral from an internal auditor and 14% from a referral from external counsel. Twenty-six percent used other methods, including audit committee selection, working relationships and referrals from bankers or board members. The largest number of the external valuation specialists — 41% — was employed by a business valuation firm. Another 30% worked for a CPA firm, 16% for a consulting firm and 5% for an investment banking firm.

Fraud Prevention

The survey offered a unique opportunity to gauge what kinds of fraud prevention and detection techniques are being used (see Exhibits 6 and 7). Respondents’ employers used a wide range of methods. The most popular prevention response was general internal controls (83%), followed by division of responsibilities (77%) and appropriate oversight by management and directors (76%). For detection, the top choices were general internal controls (85%), appropriate management oversight (81%) and physical controls (69%).
Exhibit 6

What Methods Does Your Organization Use to Prevent Fraud?

<table>
<thead>
<tr>
<th>Method</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>General internal controls</td>
<td>83%</td>
</tr>
<tr>
<td>Division of responsibilities</td>
<td>77%</td>
</tr>
<tr>
<td>Appropriate oversight by management and directors</td>
<td>76%</td>
</tr>
<tr>
<td>Background investigation of new employees</td>
<td>69%</td>
</tr>
<tr>
<td>Computer-based controls</td>
<td>67%</td>
</tr>
<tr>
<td>Physical controls</td>
<td>67%</td>
</tr>
<tr>
<td>Employee and vendor codes of conduct</td>
<td>61%</td>
</tr>
<tr>
<td>Internal audit function including conduct of fraud risk assessments</td>
<td>49%</td>
</tr>
<tr>
<td>Anti-fraud education programs</td>
<td>27%</td>
</tr>
<tr>
<td>Mandatory vacations</td>
<td>25%</td>
</tr>
<tr>
<td>Rotation of duties</td>
<td>17%</td>
</tr>
<tr>
<td>Background re-investigation of current employees</td>
<td>12%</td>
</tr>
<tr>
<td>Cybercrime prevention training</td>
<td>12%</td>
</tr>
</tbody>
</table>
Exhibit 7

How Did Respondents Detect Fraud?

<table>
<thead>
<tr>
<th>RESPONSE</th>
<th>RESPONSE</th>
</tr>
</thead>
<tbody>
<tr>
<td>General internal controls</td>
<td>85%</td>
</tr>
<tr>
<td>Appropriate oversight by management and directors</td>
<td>81%</td>
</tr>
<tr>
<td>Physical controls</td>
<td>69%</td>
</tr>
<tr>
<td>Computer-based controls</td>
<td>62%</td>
</tr>
<tr>
<td>Internal audit function including conduct of fraud risk assessments</td>
<td>47%</td>
</tr>
<tr>
<td>Whistleblower hotline</td>
<td>44%</td>
</tr>
<tr>
<td>Cyber information security procedures</td>
<td>25%</td>
</tr>
</tbody>
</table>
Virtually none of the organizations had seen an emergence of the use of virtual currencies (such as bitcoin), and none had seen fraud associated with that use.

More than half of the survey respondents (53%) had experienced fraud in the past year. Among the most common types of fraud, 15% had been victims of check fraud, 12% of employee expense fraud, 10% of the misuse or diversion of assets, 8% of false or fictitious vendor invoices.

### Exhibit 8

**What Types of Fraud Did Your Organization Experience in the Past Year?**

<table>
<thead>
<tr>
<th>RESPONSE</th>
<th>RESPONSE</th>
</tr>
</thead>
<tbody>
<tr>
<td>We did not experience any fraud</td>
<td>47%</td>
</tr>
<tr>
<td>Check fraud</td>
<td>15%</td>
</tr>
<tr>
<td>Employee expense fraud</td>
<td>12%</td>
</tr>
<tr>
<td>Misuse or diversion of assets</td>
<td>10%</td>
</tr>
<tr>
<td>False or fictitious vendor invoices</td>
<td>8%</td>
</tr>
<tr>
<td>Fraudulent billing or credit scheme</td>
<td>6%</td>
</tr>
<tr>
<td>Contract or vendor fraud</td>
<td>5%</td>
</tr>
<tr>
<td>Cybertheft — external</td>
<td>4%</td>
</tr>
<tr>
<td>Theft of intellectual property/ trade secrets</td>
<td>3%</td>
</tr>
<tr>
<td>Fictitious employees and other forms of payroll fraud</td>
<td>2%</td>
</tr>
<tr>
<td>Financial statement misrepresentation</td>
<td>1%</td>
</tr>
<tr>
<td>Cybertheft — internal</td>
<td>0%</td>
</tr>
</tbody>
</table>
Internal inquiry or tipoff was the top method of detecting fraud (17%), followed by internal audit (16%), external inquiry or tipoff (8%), accident (7%), whistleblowing (6%), law enforcement investigation (3%) and regulatory investigation (2%).

When it occurred, 89% of the time fraud was committed by an employee below the senior management level, with 8% at that level and 3% at the officer or director level. The aggregate financial amount fell below $10,000 61% of the time and between $10,000 and $49,999 13% of the time.

Frauds typically occurred in a wide variety of parts of the organization. The highest responses were in sales and marketing (9%), purchasing and accounts payable (8%) and customer service (6%).

**Economic Damages**

A total of 63% of respondents’ organizations had not been involved in an economic damages case during the past year. Among those that were, the cases most frequently involved employment (9%), personal injury (6%) and breach of contract (5%).

In the largest percentage of cases, organizations relied on a referral from external counsel in selecting the expert who testified in an economic damages case (8%). Five percent used a referral from internal counsel and 3% from their external auditor.

The qualifications for these expert witnesses included the CPA (7%), MBA (4%), CPA/ABV (3%), ASA (2%) and CPA/CFF (2%).

**Financial Statement Misrepresentation**

Only 3% of the organizations involved experienced financial statement misrepresentation during the past year. For those affected, the cases involved an overstatement of accounts receivable, inventory, securities or other assets (29%); fictitious or overstatement of revenues (12%); or intentional omissions or improper disclosures (6%). The cases were most often detected through an internal audit (17%), in an external audit or by accident (11% each) or through whistleblowing (6%).
Shareholder Dispute

Two percent of the organizations had experienced a shareholder dispute. The cases cited involved dissenting shareholders, oppressed shareholders and, in one situation in the “other” category, a large shareholder purchase. Fair market value was the standard of value used 75% of the time and investment value in the other cases.

Case Study 4: Two CPAs Weigh in on Shareholder or Partner Disputes

Will the ongoing retirement of the baby boom generation and an improving economy spur more shareholder or partner disputes? “There is not a bright line connection, but it’s certainly true that as the economy and and enterprise values improve, things are often more worth fighting over,” says Ron Seigneur, CPA/ABV/CFF, CGMA, ASA, CVA, managing partner of Seigneur Gustafson, LLP, in Lakewood, CO. He reports seeing a spike in interest from attorneys or from partners or shareholders who aren’t getting along.

Ron DiMattia, CPA/ABV, CMA, president of Corporate Value Partners in Rocky River, OH, believes that CPAs and attorneys are doing a better job of talking about valuation issues with clients, which makes them more aware of the need to hire a professional to help them navigate the process.

Get It in Writing

In these disputes, Seigneur often sees corporate legal documents that don’t adequately set forth what will happen if the owners differ on critical issues or decide to split. “The operative legal documents often don’t adequately define the standard of value that should be used or how qualified business appraisers will be chosen,” he says. He recommends a book by valuation expert Chris Mercer, Buy-Sell Agreements: A Ticking Time Bomb or Reasonable Resolution?, because it offers examples of workable and flawed agreements.

The lack of satisfactory buy-sell agreements is an opportunity for CPAs, Seigneur observes. “You can review the legal documents with your clients before they are going through a triggering event, such as a business divorce, when the partners are getting along or even at the point of business formation,” he advises. “Look for details on how a dispute or split will be handled and for language on triggering events, so that a dispute will not have to occur down the road.” Seigneur’s firm does a great deal of exit-planning work, and he often finds that an owner who has not saved enough for retirement who now has unrealistic expectations about what they should be able to take out of a business, will typically lead to a dispute. A well-structured buy-sell agreement can help prevent the problem.

DiMattia advises CPAs to have regular contact with their clients and to talk about valuation issues as part of those conversations. “The business is relationship-based and trust-based,” he says. “The client or key people who influence the client have to know you.” In discussing the service with clients, he emphasizes the goal of making the best of a transaction, rather than the potential for disputes and he spends time with clients discussing how valuation concepts relate to their operations. “An understanding of valuation is a gift that clients can use in their businesses every day,” he says.
The Standard of Value

One sticking point in disputes is often the standard of value to be used. The possibilities might be fair market value, investment value or fair value, and the choice is a legal issue that is not determined by a CPA. In a merger or acquisition, the standard of value used is investment value, Seigneur says. “Most CPAs live in a fair market value world, because that’s what’s used in estate planning and other tax related engagements.” He notes that when working with investment value, there’s not as much reliable empirical data available. He recommends GF Data as one less costly source of empirical values.

The Client Viewpoint

Outside of business considerations, DiMattia advises maintaining some perspective on what the issues mean to the client. “Any transition is emotional,” he says. “For the seller, it may be the only transaction of this magnitude in his or her life. The asset they are selling may be as important to them as their family. On the other hand, the buyer may have a great deal of uncertainty about the deal, especially if it will be highly leveraged.” Unlike in engagements that are largely compliance driven, it may be difficult for each side to remain economically impartial in a buyout or sale.

One complication is the lack of any real market test for the ownership interests. In the absence of this test, the valuation can offer comfort and reassurance about the proper values. DiMattia notes that valuations are not necessarily the final determination. “In many cases, the two sides will use the valuation to negotiate,” he says. “That’s why a well-documented valuation is so important. You’re educating the buyer and seller about the issues involved.”

Deal structure is another critical concern and one that can offer chances for negotiation. He cites a hypothetical case in which the ownership interest is worth $1 million. The buyer can only borrow $600,000, so the seller carries a note for $400,000. “That note will differ from one given by a bank,” DiMattia says. “The seller may agree to terms that a bank would not, such as an interest-free loan for the first few years.” Other options might allow a moderate interest rate in exchange for a seat on the company board of directors. “The seller often wants to maintain some kind of involvement in the business, so they may be willing to negotiate terms in exchange for some sense of connection and control.”

Pumping Up the Practice Area

Seigneur offers this advice for those who are interested in this practice area:

- Get training in expert witness services. These disputes are often litigation engagements that will involve rendering an opinion in court. “I often get hired based on my reputation as a testifying expert as much as my reputation in business valuation,” Seigneur says. “The attorneys know we have the credentials. They also want to be sure we can defend our opinion in court and articulate our positions.” One training resource is the AICPA Expert Witness Skills Workshop.

- Pump up your intellectual property expertise. “A lot of value relates to intellectual property,” Seigneur notes. Beyond patents and trademarks, these engagements may also include workforce in place, proprietary processes, artistic endeavors and logos.

- Market yourself to attorneys. “That’s where work comes from,” he notes. He recommends making the most of chances to write for legal publications or speak to attorney groups.