

Chapter 1

Introduction to the Problem of Accounting Fraud

SOLUTIONS

True/False Questions:

1. False
2. False
3. False (The Sarbanes-Oxley Act was passed in 2002.)
4. True
5. False
6. False
7. True
8. False (The Dodd-Frank Act revised and increased the power of the SEC.)
9. True
10. True

Fill-in-the-Blank Questions:

11. Section 404
12. audit
13. banking
14. high-quality
15. 2010
16. corporate fraud
17. Public Oversight Board
18. Volcker
19. familiarity
20. toxic or risky

Multiple-Choice Questions:

21. c

Explanation: The SEC is a government regulatory body and was not complicit in the fraud, nor was its role examined or faulted by the Bankruptcy Examiner.

- Answers a, b, and d are incorrect because Thornburgh found gatekeeping failures in WorldCom's internal audit structure and with its external auditors and its board of directors.

22. b

Explanation: In many cases, senior management compensation agreements included stock options that would provide significant additional remuneration if analysts' earnings expectations were met.

- Answers a, c, and d are incorrect because they were not cited as common reasons to orchestrate frauds.

23. b

Explanation:

- Answers a, c, and d are true statements.

24. a

Explanation:

- Answers b, c, and d are incorrect because Section 301 of SOX mandated the establishment of hotlines for anonymous whistleblowers in the U.S. but ended up causing problems for some American companies with European subsidiaries because very few countries in Europe have laws that protect whistleblowers.

25. a

Explanation: The major objectives of Dodd-Frank are to "reshape the U.S. regulatory system in a number of areas including but not limited to consumer protection, trading restrictions, credit ratings, regulation of financial products, corporate governance and disclosure, and transparency" ("The Laws" 2012).

- Answer a is correct because Dodd-Frank does not attempt to increase the number of audit firms.

26. d

Explanation: All of the changes mentioned, plus others, have resulted from Dodd-Frank.

27. a

Explanation: Through Dodd-Frank's whistleblower program, whistleblowers are offered more protection than under Sarbanes-Oxley, and they can now receive monetary awards from the SEC which is pursuing whistleblower tips very seriously.

- Answers b, c, and d are incorrect because whistleblowers are taken seriously by the SEC and they can receive monetary awards.

28. a

Explanation: The director who works for a competing company, Raining Raisins, may have a conflict of interests.

- The employment status of the other directors would be unlikely to result in conflicts of interest.

29. a

Explanation:

- Answers b, c, and d are incorrect because some of the most outrageous corporate looting prior to SOX occurred via the two-step loan process, as mentioned in statement a.

30. d

Explanation:

- Answers a, b, and c are true statements.