

# MANAGING THE RISK OF FRAUD

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**The expert witness who, because of their knowledge or experience in a specific area, is allowed to give opinion evidence.**

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## Expert Witness Rules of Evidence Part 5

Expert witnesses have been an integral part of the tribunal system and their importance is growing. With that growth comes the need to regulate and control the role and manner in which experts are used and abused by the parties to litigation.

As a result, the professional bodies and the legal jurisdictions have developed rules, standards and codes which the expert must follow. The degree of adherence to these rules will have a direct impact on how the expert's report, testimony and opinions are considered by the trier of fact.

This is the fifth and final part in a series of newsletters that will look at the existing and new rules, standards and codes that are applicable to expert witnesses, including the Standard Practices for Investigative and Forensic Accounting Engagements, the Federal Rules and the new Federal Code of Conduct, the provincial rules of procedure and the new rules in Ontario, British Columbia and Alberta.

In addition, the series will review the Daubert rules in the US and the recent changes to Rule 26 governing the discoverability of experts in the US as well as the US Federal rules, State rules and the American Institute of Certified Public Accountants rules.

The rules applicable to Chartered Business Valuators and the American Society of Appraisers will be examined as well.

As the rules, standards and codes have expanded, so has the focus of the courts on the expert's adherence to these rules, standards and codes. Readers will have a better

awareness of their obligations to the courts and will be prepared to respond in the affirmative when questioned about their methodology and compliance with these rules, standards and codes.

## United States

### PROFESSIONAL RULES AND CODES

#### AICPA CONSULTING SERVICES

#### PRACTICE AID 10 – 1

#### SERVING AS AN EXPERT WITNESS OR CONSULTANT

- The intent of this practice aid is to provide the practitioner with nonauthoritative guidance when serving as an expert witness or consultant for litigation services engagements in the United States of America, although certain parts of this guidance also may be applicable to international assignments.

(Continued from page 1)

10. When forensic accounting services are provided by a practitioner and CPA firms and their employees, they require, at a minimum, adherence to Statement on Standards for Consulting Services (SSCS) No. 1

16. The AICPA Code of Professional Conduct (code) applies to the services rendered by practitioners. The following sections of the code have particular applicability to the practice of forensic accounting services:

- Rule 102, Integrity and Objectivity
- Rule 201, General Standards
- Rule 202, Compliance with Standards
- Rule 301, Confidential Client Information
- Rule 302, Contingent Fees
- Rule 501, Acts Discreditable

17. In some instances, Rule 101, Independence

23. The performance of forensic accounting service engagements as an expert witness or a consultant, either for, or opposed to, a practitioner's or practitioner's firm's attestation client, will impair independence, as defined by the Sarbanes-Oxley Act of 2002;

27. The roles of expert witness and consultant practitioner differ from the role of the attorneys in the litigation process. Because litigation is an adversarial proceeding, each party presents his or her case to the trier of fact. Attorneys must advocate for their clients.

The practitioner, on the other hand, must serve his or her client (the attorney) with integrity and objectivity, as required by the code. Accordingly, forensic accountants should have objective neutrality with regard to their professional opinions and not advocate for the position of the attorneys or the attorneys' clients.

31. The general standards under Rule 201 also apply to practitioners providing expert and consulting services. These standards cover professional competence, due professional care, planning and supervision, and sufficient reliable data.

### OTHER CONSIDERATIONS

- 55. Conflicts of interest
- 61. Engagement Acceptance
- 70. Who is the Client – the attorney or the attorney's client?
- 74. Scope of work
- 75. Timetable
- 76. Fees
- 85. Staffing and Supervision
- 96. Engagement Letter

### AICPA STANDARDS FOR CONSULTING SERVICES (SSCS) No. 1

6. The general standards of the profession are contained in Rule 201 of the AICPA Code of Professional Conduct and apply to all services performed by members. They are as follows:

**Professional competence.** Undertake only those professional services that the member or the member's firm can reasonably expect to be completed with professional competence.

**Due professional care.** Exercise due professional care in the performance of professional services.

**Planning and supervision.** Adequately plan and supervise the performance of professional services.

**Sufficient relevant data.** Obtain sufficient relevant data to afford a reasonable basis for conclusions or recommendations in relation to any professional services performed.

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MANAGING THE RISK OF FRAUD has been prepared for the general information of our clients, staff and other interested parties. The enclosed comments are of a general nature and are not intended to cover all aspects of the subject matter. Prior to implementing any planning based upon information in this publication, the specific facts pertaining to any particular situation should be carefully considered. We will be pleased to assist in this regard and to provide further details pertaining to the matters discussed herein.

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7. The following additional general standards for all Consulting Services are promulgated to address the distinctive nature of Consulting Services in which the understanding with the client may establish valid limitations on the practitioner's performance of services. These Standards are established under Rule 202 of the AICPA Code of Professional Conduct.

**Client Interest.** Serve the client interest by seeking to accomplish the objectives established by the understanding with the client while maintaining integrity and objectivity.

**Understanding with Client.** Establish with the client a written or oral understanding about the responsibilities of the parties and the nature, scope, and limitations of services to be performed, and modify the understanding if circumstances require a significant change during the engagement.

**Communication with Client.** Inform the client of (a) conflicts of interest that may occur pursuant to interpretations of Rule 102 of the Code of Professional Conduct, 2 3 (b) significant reservations concerning the scope or benefits of the engagement, and (c) significant engagement findings or events.

8. Professional judgment must be used in applying Statements on Standards for Consulting Services in a specific instance since the oral or written understanding with the client may establish constraints within which services are to be provided. For example, the understanding with the client may limit the practitioner's effort with regard to gathering relevant data. The practitioner is not required to decline or withdraw from a consulting engagement when the agreed-upon scope of services includes such limitations.

## AICPA AND STATE CODES OF PROFESSIONAL CONDUCT

All of the rules and codes that govern the role of the expert witness will bring the following basic attributes

to the reliance that will be placed upon the expert's opinion. The courts do not consider an expert to be excluded simply because he may not be independent from one of the parties, in the context of a client – professional relationship (e.g. a CPA who acts as an expert for a client of the firm in which he/she is a partner). This potential conflict of interest will impact the weight placed on the expert's testimony by the trier of fact.

### ET Section 91 - Applicability

.01 The bylaws of the AICPA require that members adhere to the rules of the Code of Professional Conduct. Members must be prepared to justify departures from these rules.

### ET Section 92 - Definitions

#### **.29 Practice of public accounting.**

The practice of public accounting consists of the performance for a client, by a member or a member's firm, while holding out as CPA(s), of the professional services of accounting, tax, personal financial planning, litigation support services, and those professional services for which standards are promulgated by bodies designated by council. Such standards include FASB ASC, SASs, and Statements on Standards for Accounting and Review Services, Statements on Standards for Consulting Services, Statements of Governmental Accounting Standards, International Financial Reporting Standards and International Accounting Standards, Statements on Standards for Attestation Engagements, and Statements on Standards for Valuation Services.

### ET Section 52

#### **Article I—Responsibilities**

In carrying out their responsibilities as professionals, members should exercise sensitive professional and

moral judgments in all their activities.

## **Article II—The Public Interest**

Members should accept the obligation to act in a way that will serve the public interest, honor the public trust, and demonstrate commitment to professionalism.

## **Article III—Integrity**

To maintain and broaden public confidence, members should perform all professional responsibilities with the highest sense of integrity.

## **Article IV—Objectivity and Independence**

A member should maintain objectivity and be free of conflicts of interest in discharging professional responsibilities. A member in public practice should be independent in fact and appearance when providing auditing and other attestation services.

## **Article V—Due Care**

A member should observe the profession's technical and ethical standards, strive continually to improve competence and the quality of services, and discharge professional responsibility to the best of the member's ability.

## **Article VI—Scope and Nature of Services**

A member in public practice should observe the Principles of the Code of Professional Conduct in determining the scope and nature of services to be provided.

### **ET §101.05**

#### **Forensic Accounting Services**

For purposes of this interpretation, forensic accounting services are nonattest services that involve the application of special skills in accounting, auditing, finance, quantitative methods and certain areas of the

law, and research, and investigative skills to collect, analyze, and evaluate evidential matter and to interpret and communicate findings and consist of:

- Litigation services; and
- Investigative services.

Litigation services recognize the role of the member as an expert or consultant and consist of providing assistance for actual or potential legal or regulatory proceedings before a trier of fact in connection with the resolution of disputes between parties.

### **AMERICAN SOCIETY OF APPRAISERS STANDARDS**

#### **PRINCIPLES OF APPRAISAL PRACTICE AND**

#### **CODE OF ETHICS**

#### **4.3 Appraiser's Obligation Relative to Giving Testimony**

When an appraiser is engaged by one of the parties in a controversy, it is unethical for the appraiser to suppress any facts, data, or opinions which are adverse to the case his client is trying to establish; or to overemphasize any facts, data, or opinions which are favorable to his client's case; or in any other particulars to become an advocate. It is the appraiser's obligation to present the data, analysis, and value without bias, regardless of the effect of such unbiased presentation on his client's case.

#### **4.4 Appraiser's Obligation to Document Appraisal Testimony**

When a member accepts employment to make an appraisal, or to testify as to value of property before a court of law or other judicial or quasi-judicial forums, the appraiser shall, before testifying, complete an adequate written appraisal report, or have complete documentation and substantiation available in his files.

## 4.6 Agreements and Contracts for Appraisal Services

It is good practice to have a written contract, or at least a clear oral agreement, between appraiser and client, covering objectives and scope of work, time of delivery of report, and amount of fees.

### 7.1 Contingent Fees

Society declares that the contracting for or acceptance of any such contingent fee is unethical and unprofessional.

### 7.2 Percentage Fees

The Society takes the position that it is unprofessional and unethical for the appraiser to contract to do work for a fixed percentage of the amount of value, or of the estimated cost (as the case may be) which he determines at the conclusion of his work.

### 7.5 Advocacy

If an appraiser, in the writing of a report or in giving an exposition of it before third parties or in giving testimony in a court action suppresses or minimizes any facts, data, or opinions which, if fully stated, might militate against the accomplishment of his client's objective or, if he adds any irrelevant data or unwarranted favorable opinions or places an improper emphasis on any relevant facts for the purpose of aiding his client in accomplishing his objective, he is, in the opinion of the Society, an advocate. Advocacy, as here described, affects adversely the establishment and maintenance of trust and confidence in the results of professional appraisal practice and the Society declares that it is unethical and unprofessional.

## 7.6 Unconsidered Opinions and Preliminary Reports

If an appraiser gives an opinion ..... without having ascertained and weighed all of the pertinent facts, such opinion, except by an extraordinary coincidence will be inaccurate. .... and therefore the Society declares the giving of hasty and unconsidered opinions to be unprofessional.

The Society declares it to be unprofessional appraisal practice to omit a proper limiting and qualifying statement in a preliminary report.

## 8: Appraisal Reports

- 8.1 Description of the Property Which Is the Subject of an Appraisal Report
- 8.2 Statement of the Objectives of the Appraisal Work
- 8.3 Statement of the Contingent and Limiting Conditions to Which the Appraisal Findings Are Subject
- 8.4 Description and Explanation in the Appraisal Report of the Appraisal Method Used
- 8.5 Statement of the Appraiser's Disinterestedness
- 8.6 Appraisers Responsibility to Communicate Each Analysis, Opinion and Conclusion in a Manner that is not Misleading.
- 8.7 Mandatory Recertification Statement
- 8.8 Signatures to Appraisal Reports and the Inclusion of Dissenting Opinions

**BUSINESS VALUATION STANDARDS****AMERICAN SOCIETY OF APPRAISERS**

This Standard must be followed in all valuations of businesses, business ownership interests, securities and intangible assets developed by all members of the American Society of Appraisers.

The Standard describes in detail the rules in each of the following areas:

- ◆ Appropriate definition of the assignment
- ◆ Information collection and analysis
- ◆ Approaches, methods and procedures
- ◆ Documentation and retention
- ◆ Reporting
- ◆ Signature and certification
- ◆ Assumptions and limiting conditions
- ◆ Definition of the valuation assignment
- ◆ Business description
- ◆ Financial analysis
- ◆ Valuation methodology
- ◆ Comprehensive written business valuation report format
- ◆ Confidentiality of the report

**Procedural Guideline-1 Litigation Support:****Role of the Independent Financial Expert**

Business valuation professionals are frequently engaged as independent financial experts for purposes of assisting in dispute resolution, litigation, or potential litigation.

This Procedural Guideline incorporates, where appropriate, all relevant Business Valuation Standards and Statements on Standards adopted by the American Society of Appraisers through its Business Valuation Committee.

The expert should maintain custody of the work papers, or make appropriate retention, access, and retrieval arrangements with the party having custody of those work papers. The expert should retain the work papers for a period of at least five (5) years after preparation, or at least two (2) years after final disposition of any judicial proceeding (including arbitration) in which testimony was given, whichever period expires last.

### **Quebec Draft Reform Expert Evidence**

289. Each of the parties can examine a joint expert to obtain clarifications on points covered in the expert's report. In any other case, a party cannot examine an expert it has appointed unless so authorized by the court or unless the purpose of the examination is to obtain the expert's opinion on new evidence introduced in the course of the proceeding.

A party cannot cross-examine an expert appointed by another party except if it is necessary in order to obtain clarifications on the expert's report or on the points on which the experts differ.

## ABOUT LEVI & SINCLAIR

**LEVI & SINCLAIR** is a firm of chartered professional accountants that traces its origin in Montreal to 1970. We pride ourselves on being more than just an accounting firm. We offer an effective blend of personalized service, experience and technological leadership, coupled with a steadfast commitment to consistently deliver excellence.

Our Chartered Professional Accountants and Business Consultants provide advisory services on a broad range of issues to both our individual and corporate clients. The members of our firm possess unique talents, expertise and experience, giving our clients access to a knowledge base of considerable breadth and depth. Together with our support personnel, we share a commitment to developing practical solutions for the business challenges of today, and to devising strategies for tomorrow.

### OUR SERVICES

Our firm takes pride in adding value to every client that we serve through our extensive expertise and proactive approach to your financial needs. We match our dedication to adding value with experience and expertise: we have experience in servicing virtually every type of industry and professional practice.

### TAXATION

Our office has a strong basis in federal and provincial tax issues. Our tax group is highly qualified and experienced. Our accountants work hard to minimize your taxes, yet make sure that you fulfill your tax requirements ethically while working to add value. We can fill a variety of tax needs, both domestic and international as well as corporate and personal. Our specialties lie in tax reporting and representation, tax planning (business, personal, divorce and litigation), tax structuring of entities and transactions and tax research.

### FINANCIAL

**LEVI & SINCLAIR** can meet all of your basic financial needs with our exemplary Accounting Services Group that can truly add value whether it's your business or your personal finances that we are reviewing. We work with business entities as well as non-profits and foundations. Our accounting services include; auditing and compilation review of financial statements, budgets and forecasts, and government reporting. We won't simply process your financial statements, our mission is to add value. We will go the extra mile to help you forecast or locate opportunities that you may be missing.

### BUSINESS CONSULTING

**LEVI & SINCLAIR**'s Business Consulting unit has proven itself as a valuable resource to businesses of all kinds. We can help you plan your future, whether you see it coming or not. We can help you bring seminal business events to life; like mergers and acquisitions, business valuation, leases and contracts, or business development plans, all of which take a huge amount of planning and attention to detail. If there are no big events on your horizon, we can still be of service by helping you to anticipate the unexpected through our forecasting, real estate projections, risk management assessments, or our feasibility studies. We look at your business and all of its many facets, to find both issues and opportunities and bring that valuable insight to you.

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- **Intellectual Property Litigation Support**
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- **Business valuation**
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- **Retail sales audits**
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- **Professional negligence litigation support**
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- **Employee background audits**
- **Financial discrepancy analysis**
- **Divorce litigation support**
- **Insurance claim quantification**
- **Breach of contract quantification**
- **Electronic Discovery and Data Recovery**
- **Computer forensics**

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