

Mannheim, November 2020

Spring Term 2021

ACC 750 Accounting Seminar

The Wirecard Case: How to Prevent Accounting Fraud? The Role of Accounting Standards, Audit and Enforcement

(Der Fall Wirecard: Wie können Bilanzfälschungen verhindert werden?
Die Rolle von Rechnungslegungsstandards, Wirtschaftsprüfung und Bilanzkontrolle)

Lecturers: Professor Jannis Bischof/Professor Jens Wüstemann

I. Admission and Seminar Dates

We accept applications for the seminar until **December 21, 2020**, for the fast close period and until **February 15, 2021**, for the final close period. Please submit your applications via email to Frederik Kohl (fkohl@uni-mannheim.de). You can access the seminar registration form under the following link: <https://www.bwl.uni-mannheim.de/en/wuestemann/teaching/>.

For the seminar writing phase, you can choose between **two eight-week periods**: the **fast close period** spans from **January 4, 2021 to March 1, 2021** and the **final close period** from **March 1, 2021 to April 26, 2021**. Please indicate in your registration document in which period you intend to write your seminar thesis. We will publish the allocation of paper topics via email on January 4, 2021 and on March 1, 2021, respectively (at 12 pm).

The seminar presentations will take place on **May 28, 2021**.

Please consult the relevant examination regulation ("Prüfungsordnung") and module catalog ("Modulkatalog") for information on minimum admission requirements.

II. Seminar Paper and Presentation

1. Motivation & Preliminary Remarks

In June 2020, Europe's formerly "largest fintech" and "answer to Silicon Valley giants", Wirecard AG, filed for insolvency after acknowledging a potential EUR 1.9bn accounting fraud. How has it come to that? Wirecard is founded in 1999 as a payment processor, initially processing payments primarily for online gambling and pornography. The payment processor becomes listed at the Frankfurt stock exchange in

2005 by taking over the listing of a call centre company and thereby avoiding the more sophisticated initial public offering process. After a massive expansion and internationalization period especially across Asia, the Financial Times launches a series of articles questioning Wirecard's accounting practices and operations for the first time in 2015. Yet, Wirecard fends off these allegations by engaging law firms and public relations consultants and relating these charges to short seller attacks. Nevertheless, further accusations follow by an anonymous short seller dossier as well as a German newspaper. Despite these articles and an inside investigation being initiated on the basis of an internal whistleblower, the share price continues to rise and Wirecard enters Germany's most important stock index (DAX) in 2018.

However, the turmoil does not end: Wirecard's long-standing auditor Ernst & Young (EY) receives information about irregularities at Wirecard from a whistleblower. Irrespective, they issue an unqualified audit opinion for the 2018 financial statements. In addition, following further Financial Times reports, BaFin launches market manipulation investigations against the Financial Times and even files criminal complaints against market participants and journalists from the Financial Times. In February 2019, BaFin issues a two-month shortselling ban on Wirecard shares in order to protect the firm from short seller attacks. In an attempt to bring the continuing accusations to an end, Wirecard appoints KPMG to conduct a special investigation. In the end, events come thick and fast: the publication of the KPMG report is postponed several times and BaFin files criminal complaints against Wirecard due to misleading ad-hoc statements in connection with the KPMG report. Despite that, while still conducting the 2019 audit, EY informs Wirecard about forged holdings confirmations on June 16, 2020. Only six days later, Wirecard admits that EUR 1.9bn in bank balances on trust accounts might not exist and files for insolvency on June 25, 2020.

Though the Wirecard case seems to be a very special case of white-collar crime and it is definitely one of the biggest accounting fraud scandals in Germany, white-collar crime happens regularly and several equally prominent cases are known, as for example the Enron case in 2002. In addition, Eugene Soltes (2016) emphasizes that it is not merely greed or hubris leading managers to become white-collar criminals. Instead, he argues that these managers base their decisions on intuition and gut feelings, suggesting that white-collar criminals are not born as criminals but rather engage in criminal actions due to certain circumstances. On the other side, white-collar crime and accounting fraud in particular entail severe consequences in several respects. In the special case of Wirecard, investors likely incur damages of more than EUR 3.2bn of their invested capital. This in turn could significantly damage the reputation of the German capital market and reduce market participation of both international and domestic investors. Against this background, the current political debate on regulatory reform following the Wirecard case seems to be only consequential.

The policy discussion surrounding prior corporate accounting scandals (e.g., Enron, WorldCom) and investment frauds (e.g., Madoff's Ponzi scheme) generally follows a recurring pattern that is primarily concerned with the assignment of responsibilities and identification of deficiencies in existing institutional architectures. As such, Wirecard is a case in point. Following the revelation of its fraudulent activities, media attention has largely revolved around the role of the auditing firm EY as well as the BaFin's failed

line of defense. In an attempt to quickly restore investor confidence, the German Federal Ministry of Finance has therefore formulated a draft bill seeking a general overhaul of the auditing industry including plans to grant more expansive supervisory power to the BaFin.

While certainly well intended, the ministerial draft bill faced a major backlash from Germany's institute of public auditors (IDW), referring to the government's plans as a "knee-jerk reaction". Part of the criticism probably relates to the fact that the German bill largely resembles Michel Barnier's, then EC Commissioner, Green paper on audit policy which was the subject of intense debate in the aftermath of the financial crisis. Given the bill's controversial nature, the seminar aims, *inter alia*, to shed light onto the proposed changes from an evidence-based perspective. Ultimately the goal shall be to distinguish those policy suggestions which have a sound scientific basis from those which are mere political rhetoric.

The first part of the seminar presents a sequential view of typical accounting fraud with a distinct focus on the Wirecard case. It starts by normatively assessing accounting practices that are particularly susceptible to manipulation in the context of financial institutions such as special purpose vehicles, which are frequently used for off-balance sheet banking activities (e.g., ABS). Part A continues by examining manager's motivations for engaging in fraudulent behavior as well as providing an in-depth look into Wirecard's deceptive scheme before concluding with an exploration of the key ways in which fraud may be detected. In the second part of the seminar, we will critically assess some of the proposed changes to the auditing industry in response to the Wirecard case, by drawing from normative and empirical literature. Principal focus will be on the two changes that are arguably of most crucial concern for audit firms, namely auditor liability and mandatory rotation. The final part of the seminar addresses the role of regulatory enforcement and the general institutional framework in constraining white-collar crime. One central question, for example, will be whether large publicly funded agencies are more effective in enforcing securities laws than private enforcement mechanisms available to investors such as class action lawsuits.

For further insights into Wirecard and in general preparation for the seminar session, we recommend reading the following articles and publications:

- McCrum, D., 2020: [Wirecard: the timeline](#), Financial Times.
- Krahenen, J.P., Langenbucher, K., Leuz, C., & Pelizzon, L., 2020. [What are the wider supervisory implications of the Wirecard case?](#) ECON Committee, European Parliament.

2. Topics and Related Literature

Part A: Accounting Fraud: Why They Do It and How It Is Detected

- **Topic 1:** “Critical Assessment of revenue recognition under IFRS 15 with special regards to the performance obligations when other parties are involved in the transaction” / „Kritische Würdigung der Gewinnrealisierungsgrundsätze nach IFRS 15 unter besonderer Berücksichtigung der Leistungspflichten bei der Zusammenarbeit mit Drittanbietern“ (Supervisor: *Marcel Rost*)
 - Wüstemann, J. & Wüstemann, S., 2014. Grundsätze für die Erfassung von Umsatzerlösen aus Verträgen mit Kunden – IFRS 15 „Revenue from Contracts with Customers“. *WPg* 65(18), 929-937.
 - Wüstemann, J. et al, 2017. Grundsätze der Identifizierung von Kundenverträgen und Leistungsverpflichtungen nach IFRS 15 – Anwendung auf Rahmenvereinbarungen und Werklieferungsverträge. *BB* 72(21), 1195-1199.
- **Topic 2:** “Critical Assessment of the Consolidation rules for special purpose entities under German GAAP” / „Kritische Würdigung der handelsrechtlichen Konsolidierungsgrundsätze für Zweckgesellschaften“ (Supervisor: *Marcel Rost*)
 - Becker, C. & Endert, V. 2012. Außerbilanzielle Geschäfte, Zweckgesellschaften und Strafrecht. *ZGR* 41(5), 699-729.
 - Mojadadr, M., 2013. Zweckgesellschaften im Konzernabschluss nach HGB und IFRS. Berlin: Erich Schmidt Verlag.
 - Thelen-Pischke, H. 2010. Die aufsichtsrechtliche Konsolidierung von Zweckgesellschaften unter Berücksichtigung der Auswirkungen des BilMoG. *IRZ* 5(4), 187-195.
- **Topic 3:** “Determinants of Accounting Fraud: Is it merely an Incentive Problem?” (Supervisor: *Clemens Lauer*)
 - *Armstrong, C.S., Jagolinzer, A.D., & Larcker, D.F., 2010. Chief Executive Officer Equity Incentives and Accounting Irregularities. Journal of Accounting Research, 48(2), 225-271.*
 - *Johnson, S.A., Ryan Jr., H.E., & Tian, Y.S., 2009. Managerial Incentives and Corporate Fraud: The Sources of Incentives Matter. Review of Finance, 13(1), 115-145.*
 - *Feng, M., Ge, W., Luo, S., & Shevlin, T., 2011. Why do CFOs become involved in material accounting manipulations? Journal of Accounting and Economics, 51(1-2), 21-36.*
 - *Rezaee, Z., 2005. Causes, consequences, and deterrence of financial statement fraud. Critical Perspectives on Accounting, 16, 277-298.*
 - *Soltes, E., 2016. Why They Do It: Inside the Mind of the White-Collar Criminal, New York.*
- **Topic 4:** ““Inside Wirecard” –Analysis of Critical Accounting Practices” (Supervisor: *Amadeus Bach*)
 - *BMF, 2020. [Sachstandsbericht und Chronologie Wirecard. Bundesministerium für Finanzen \(BMF\).](#) Berlin.*
 - *McCrum, D., Palmer, S., 2019: [Wirecard: inside an accounting scandal](#), Financial Times.*

- McCrum, D., 2020: [Wirecard: the timeline](#), Financial Times.
- KPMG, 2020: [Report: Concerning the independent special investigation](#).
- Fairless, T., Kowsmann, P., Davies, P., 2020. [How Germany's SEC Dismissed a Decade of Warnings about Wirecard](#), Dow Jones Institutional News.
- Krahen, J.P., Langenbucher, K., Leuz, C., & Pelizzon, L., 2020. [What are the wider supervisory implications of the Wirecard case?](#) ECON Committee, European Parliament.
- **Topic 5:** “Accounting Fraud Watchdogs: Whistleblowers, Short Sellers and the Media” (Supervisor: *Amadeus Bach*)
 - Li, Y., & Zhang, L., 2015. Short selling pressure, stock price behavior, and management forecast precision: Evidence from a natural experiment. *Journal of Accounting Research*, 53(1), 79-117.
 - Engelberg, J. E., Reed, A. V., & Ringgenberg, M. C., 2012. How are shorts informed?: Short sellers, news, and information processing. *Journal of Financial Economics*, 105(2), 260-278.
 - Karpoff, J. M., & Lou, X., 2010. Short sellers and financial misconduct. *The Journal of Finance*, 65(5), 1879-1913.
 - Brendel, Janja, and James Ryans, 2020. Responding to Activist short sellers: Allegations, firm disclosure choices, and outcomes, WP.
 - Bushman, R. M., & Pinto, J., 2020. The Influence of Short Selling on the Production and Market Consequences of Negative Press Coverage, WP.

Part B: Implications for the Auditing Practice

- **Topic 6:** “Critical Assessment of the German Ministerial Draft Bill to Expand Auditor Liability” / “Kritische Würdigung des Referentenentwurfs zur Ausweitung der zivilrechtlichen Haftung des Abschlussprüfers” (Supervisor: *Frederik Kohl*)
 - BMF, & BMJV, 2020. *Entwurf eines Gesetzes zur Stärkung der Finanzmarktintegrität*. Bundesministerium für Finanzen (BMF) and Bundesministerium für Justiz und Verbraucherschutz (BMJV), Berlin, Germany.
 - Gietzmann, M. B., & Quick, R., 1998. Capping auditor liability: The German experience. *Accounting, Organizations and Society* 23(1), 81-103.
 - Dye, R. A., 1993. Auditing Standards, Legal Liability, and Auditor Wealth. *Journal of Political Economy* 101(5), 887-914.
 - Quick, R., 1996. The legal liability of auditors in Germany. *European Accounting Review* 5(3), 507-521.
 - Samsonova-Taddei, A., & Humphrey, C., 2015. Risk and the construction of a European audit policy agenda: The case of auditor liability. *Accounting, Organizations and Society* 41, 55-72.

- **Topic 7:** “Critical Analysis of the Proposed Changes to Mandatory Audit Rotation in Germany” / “Kritische Analyse des Vorschlags zur Verschärfung der verpflichtenden Prüferrotation in Deutschland” (Supervisor: *Frederik Kohl*)
 - BMF, & BMJV, 2020. *Entwurf eines Gesetzes zur Stärkung der Finanzmarktintegrität*. Bundesministerium für Finanzen (BMF) and Bundesministerium für Justiz und Verbraucherschutz (BMJV), Berlin, Germany.
 - DeFond, M., & Zhang, J., 2014. A review of archival auditing research. *Journal of Accounting and Economics* 58(2-3), 275-326.
 - Lennox, C. S., 2014. Auditor tenure and rotation. *The Routledge Companion to Auditing*, eds. D. Hay, W. R. Knechel and M. Willekens, 89-106. London, UK: Routledge.
 - Marten, K.-W., Quick, R., & Ruhnke, K., 2020. *Wirtschaftsprüfung*. 6th ed. Stuttgart, Germany: Schäffer-Poeschel.
 - Public Company Accounting Oversight Board (PCAOB), 2011. *Concept Release on Auditor Independence and Audit Firm Rotation: Notice of Roundtable*. Release No. 2011-006. (August 16). Washington, DC: PCAOB.

Part C: Implications for Regulatory Enforcement

- **Topic 8:** “Private versus Public Enforcement: Complements or Substitutes?” (Supervisor: *Clemens Lauer*)
 - Jackson, H.E., & Roe, M.J., 2009. Public and private enforcement of securities laws: Resource-based evidence. *Journal of Financial Economics* 93(2), 207-238.
 - La Porta, R., Lopez-de-Silanes, F., & Shleifer, A., 2006. What Works in Securities Laws? *The Journal of Finance* 61(1), 1-32.
 - Schantl, S.F., & Wagenhofer, A., 2020. Deterrence of financial misreporting when public and private enforcement strategically interact. *Journal of Accounting and Economics* 70(1), Article 101311.
- **Topic 9:** “Enforcement Transparency: What’s in it for Firms and Investors?” (Supervisor: *Patricia Breuer*)
 - Aobdia, D., & Shroff, N., 2017. Regulatory oversight and auditor market share. *Journal of Accounting and Economics* 63(2-3), 262-287.
 - Christensen, B.E., Glover, S.M., Comer, T.C., & Shelley, M.K., 2016. Understanding Audit Quality: Insights from Audit Professionals and Investors. *Contemporary Accounting Research* 33(4), 1648-1684.
 - Duro, M., Heese, J., & Ormazabal, G., 2019. The effect of enforcement transparency: Evidence from SEC comment-letter reviews. *Review of Accounting Studies* 24, 780-823.
 - Nagy, A., 2014. PCAOB Quality Control Inspection Reports and Auditor Reputation. *AUDITING: A Journal of Practice & Theory* 33(3), 87-104.
 - Shroff, N., 2020. Real Effects of PCAOB International Inspections. *The Accounting Review* 95(5), 399-433.

- **Topic 10:** “The Interaction between Institutional Design, Regulatory Oversight and Market Efficiency from a German Financial Market Perspective” / „Die Wechselwirkung zwischen institutionellem Rahmen, Aufsicht und Markteffizienz im Kontext des deutschen Finanzmarkts” (Supervisor: *Frederik Kohl*)
 - Ball, R., 2001. Infrastructure Requirements for an Economically Efficient System of Public Financial Reporting and Disclosure. *Brookings-Wharton Papers on Financial Services*, eds. R. Litan and R. Herring, 127-169. Washington, D.C.: Brookings Institution Press.
 - La Porta, R., Lopez-de-Silanes, F., & Shleifer, A., 2006. What Works in Securities Laws? *The Journal of Finance*, 61(1), 1-32.
 - Leuz, C., & Wüstemann, J., 2004. The Role of Accounting in the German Financial System. *The German Financial System*, eds. J. P. Krahnert and R. H. Schmidt, 450-481. Oxford, UK: Oxford University Press.
 - Wüstemann, J., Bischof, J., & Wüstemann, S., 2012. The Economics of Private Law: Consequences of Choice and Application of Accounting Standards from Institutional, Theoretical and Empirical Perspectives. *Privates Recht*, eds. C. Bumke and A. Röthel, 157-186. Tübingen, Germany: Mohr Siebeck.

III. Administration and General Information

1. Supervision

In general, you should contact your assigned supervisor shortly after the allocation of topics to discuss the general direction of your topic and the principles of writing an academic seminar paper. In addition, we expect that you present and discuss the structure and content of your term paper at one or two more meetings with your supervisor. Please check the list of topics and the chair's website on how to get in contact with your supervisor.

2. Formal Guidelines

Please check the "Guidelines for Academic Writing" („Richtlinien für die Anfertigung wissenschaftlicher Arbeiten“), which are available for download on the relevant chair's website. Seminar papers need to be written in English (seminar papers of topics 1, 2, 6, 7 and 10 can be written in German). Please note that students in the English-track of the MMM program must write their seminar papers in English. In general, seminar papers consist of 14 to 16 text pages, excluding indices and appendices. You should start your paper with a clear and concise introduction that motivates the topic and derives the main research question of your paper. The introduction should be approximately 1-1.5 pages in length and conclude with a short outline of the course of your study. Accordingly, your seminar thesis shall end with a conclusion that summarizes the main findings of your paper. You can find further details in the "Guidelines for Academic Writing".

3. Submission of Seminar Papers and Presentations

Please submit two printed copies of your written seminar thesis to Silke Frankl (office assistant to Prof. Wüstemann) or Julia Peemöller (office assistant to Prof. Bischof) during the regular office hours. Seminar papers must not be bounded by hard- or paperback; stapled copies are sufficient. In addition, please submit a digital version of your paper to your supervisor. The digital version shall include, if applicable, all relevant digital content of your thesis (such as MS Excel files, internet resources, etc.). Seminar papers need to be submitted until 12 pm on the ending date of either the fast or final close period (*vide supra*). Extensions of the submission deadline are only possible in accordance with the examination regulation if you can present a medical certificate. Please note that it is not possible to extend the working period beyond the date scheduled for the seminar presentations. In addition to the written seminar thesis, you are required to prepare a presentation based on your submitted seminar paper. The language of the seminar is English. Details on the content and structure of your presentations will be available from your supervisors only after the submission of your written papers. The presentation slides have to be handed in on May 14, 2021 at the very latest.

4. Grading

Grading is based on the written paper (60%), the presentation and active seminar participation (40%). Attendance at all seminar sessions is mandatory, and all participants are expected to participate in the seminar discussions.

5. *Seminar Preparation and Materials*

To effectively prepare for the seminar and the discussions, we will provide all participants with relevant introductory literature as well as the final presentations via ILIAS. Further information on the availability of additional material will be announced in time.

6. *Examiner/Supervisor*

The students will be examined / supervised by the following Professor / Research Assistant:

Topic 1 (part A)	Prof. Wüstemann / Marcel Rost
Topic 2 (part A)	Prof. Wüstemann / Marcel Rost
Topic 3 (part A)	Prof. Bischof / Clemens Lauer
Topic 4 (part A)	Prof. Bischof / Amadeus Bach
Topic 5 (part A)	Prof. Bischof / Amadeus Bach
Topic 6 (part B)	Prof. Wüstemann / Frederik Kohl
Topic 7 (part B)	Prof. Wüstemann / Frederik Kohl
Topic 8 (part C)	Prof. Bischof / Clemens Lauer
Topic 9 (part C)	Prof. Bischof / Patricia Breuer
Topic 10 (part C)	Prof. Wüstemann / Frederik Kohl