

Instrument

Notes for Reviewer:

- These pages below present screen shots of the online study in chronological order.
- A “Screen”, below, indicates what participants could see at one time (with the potential need to scroll down).
- Participants saw each “screen” below unless noted otherwise.
- The “Initial Instructions” screens held embedded video instruction. The text of this instruction is presented below.
- The labels for each “Screen” and table of contents were not provided to participants.

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Initial Instructions

Note for Reviewer:

- Viewed once by all participants at the beginning of the study

Screen 1 – Initial Instructions

Welcome and Initial Instructions

Click to play the video below to view an introductory guided tour of the first part of this study.

- The video states the following text while simultaneously visually demonstrating what is being said:
“Thank you very much for participating in our research study. This research investigates innovative methods for detecting red flags and fraud. Specifically, this study investigates the ability to detect fraud and red flags in a company’s financial results by listening to the company’s CEO respond to questions in a quarterly earnings conference call. Your participation is vital to the success of this research. Your responses are completely anonymous. Thus, neither the researchers, nor their universities, nor your current or former firm will have the ability to match these responses to you.

This study should take less than two hours.

- Please complete the study in **one** sitting. That is, please complete the entire study at this time. If you cannot complete the entire study at this time, please close your browser now, and come back when you can.
- Please **do not** click your browser's "Back" or "Forward" buttons or the "refresh" button (F5).
- Finally, please **do not** access any outside information while completing this survey. For example, please do not access any information about the companies you will be asked to evaluate. We will intentionally and purposefully give you less information about these companies than you would normally have.

If you have any problems or questions, please contact Professor *expunged* at the email address listed below (*expunged*).

After you finish watching this video, you will click “Next” to proceed.

The next screen, as you can see here, presents the standard consent form. You will click here and then click “Next” to start the study. Please also indicate if you are currently a college student.

Then, you will see an introductory screen that describes what we are asking you to do today.

After reading this introduction, you will click “Next” to view a detailed example. If you have this error, click “Yes.” As you can see here, there are additional Guided Tours to walk you through this example.

Please proceed when you are ready.”

Screen 2 – Initial Instructions

Letter of Information & Informed Consent

Consent Form

Screen 3 – Initial Instructions

Introduction

Your Task

Your task in this study is to use the first several minutes of CEO responses to analyst questions in a quarterly earnings conference call of a public company and do the following two things: (1) determine whether you think the results being discussed are fraudulent and (2) identify potential red flags in the audit of the company. You will do this four times for four separate public companies.

Presence of Fraud

These four companies were taken from a larger set of companies. In this larger set, 50% of the companies had to restate their earnings due to fraud. Specifically, in half of the companies in this larger set, the quarterly and/or yearly financial results being discussed in the conference call were later restated due to one or more of the following: fraudulent financial results, a regulatory investigation, or a class action lawsuit. Since you have a sample of only four companies, you will not know for sure how many of these companies committed fraud. The most likely scenario is that you will evaluate two fraud companies and two clean companies. However, you could have any combination of fraud and clean companies, including all fraud companies or all clean companies.

Structure of This Study

Next we will provide you with a guided tour of an example of how to evaluate a company. Then you will evaluate your four companies. Finally, you will answer a few wrap-up questions. Please complete the entire study at this time. Thank you again for your participation.

Screen 4 – Initial Instructions

Instructions
(Instructional Example Only)

You will be presented with the first several minutes of CEO responses to analyst questions in a quarterly earnings conference call of a public company. Your task is to (1) determine whether you think the results being discussed are fraudulent and to (2) identify potential red flags in the audit of this company.

Note: Research indicates that certain cues in what a CEO says and how s/he says it can help in the detection of deception. One cue found to be useful in detecting deception in these CEO responses is cognitive dissonance. Cognitive dissonance is the negative, uncomfortable emotion a person feels when they are saying something that they know is not true. Those experiencing cognitive dissonance feel uncomfortable, uneasy, and bothered.

This screen consists of 3 main parts.

(1) Background Company Information
This section lists background company information and financial statements.

(2) Conference Call Presentation and Red Flag List
In this section, you are presented with the first few minutes of the question and answer period from a quarterly earnings conference call. You are then asked to record each red flag you detect.

(3) Fraud Assessment
On the next screen, you will be asked to assess the likelihood that this company had to restate their earnings. You will also be asked a few other questions about this company.

[Click below to view a guided tour of the first part of this example.](#)

- Participants in the “**unaware of cognitive dissonance**” condition viewed all of this screen with the exception that the box above that starts with “Note:” said the following:
“Note: Research indicates that certain cues in what a CEO says and how s/he says it can help in the detection of deception.”
- The video states the following text while simultaneously visually demonstrating what is being said:
“Now that you have been given an overall introduction to the study, we will go through a simple, illustrative example. This example is intentionally light-hearted, and serves only to demonstrate how this online survey works, and what we are asking you to do. After you have finished this example, you will be asked to evaluate four real, public companies.

First, please read the instructions that appear directly above where you clicked on this video. Pause this video by clicking on it, and take time to read the instructions if you have not already done so. When you are ready to proceed with this Guided Tour, click on the video again to un-pause.

Next, I will demonstrate what you will need to do to evaluate each of your four companies by going through each of the three parts of this intentionally unrealistic example. I will start by demonstrating the first part of the evaluation process.

Part One

In part one, starting here, we give you background company information. As you can read here, you may wish to use the following information about this company. Again, please do not access any other information. It is critical that you do not do so. We have intentionally given you less information than you would normally have. This complies with the principles of good scientific research.

First, we give you the company name and the relevant quarter. In our example, the company is called Kermit The Frog, Incorporated. The conference call excerpt that you will hear reports on the 4th Quarter and year-end 2006 results.

Next, we give you a business overview. This is a brief summary about the company you are evaluating. Pause this video and take a moment now to read our fictional example.

Next, we provide you with portions of a Balance Sheet, an Income Statement, and a Statement of Cash Flows. Pause this video and take a moment now to look over our fictional examples. After you have done so, scroll down to Guided Tour of Example #2.”

Company Information

First, you may wish to use the following information about this company. Please do not access any other information. It is critical that you do not do so. We have intentionally given you less information than you would normally have. This complies with the principles of good scientific research.

Company Name and Relevant Quarter

Kermit The Frog, Inc. (NYSE: kerm)

"Kermit Announces Fourth Quarter and Year End 2006 Results"

Business Overview

Kermit the Frog, Inc. provides three main products and services as follows: (1) swamp restoration and beautification ("green swamping"), (2) television, movie, and music production, and (3) general dream fulfillment. We are...

...

...We were formed in January 1961 when our legendary founder, Kermit Frog...We were incorporated on January 7, 1974 in Delaware....Our principal executive offices are located at 1313 S Harbor Blvd, Anaheim, CA 92802, and our telephone number is (407) 939-1289.

Balance Sheet

Kermit The Frog, Inc. Condensed Consolidated Balance Sheets (In Thousands, Except Share Data)

	December 31, 2006	December 31, 2005
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 800,000	\$ 400,000
...
Total current assets	1,300,000	600,000
Property, equipment, and equipment, net	60,000	30,000
...
Total Assets	\$ 1,600,000	\$ 800,000
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	8,000	4,000
Other accrued expenses	170,000	50,000
...
Total current liabilities	900,000	350,000
Long-term debt	154,021	55,461
...
Total liabilities	1,100,000	500,000
Stockholders' Equity:		
Common stock	400	390
...
Retained earnings	260,000	120,000
Accumulated other comprehensive income
Total stockholders' equity	500,000	300,000
Total Liabilities and Stockholders' Equity	\$ 1,600,000	\$ 800,000

Income Statement

Kermit The Frog, Inc. Condensed Consolidated Statements of Income (In thousands, except share and per share data)

	Year Ended December 31,	
	2006	2005
Revenues:		
Total revenues	3,000,000	1,800,000
Expenses:		
Selling, general and administrative	400,000	250,000
Depreciation and amortization	17,000	9,000
...
Total expenses	2,750,000	1,700,000
Income before income taxes	250,000	100,000
Income tax expense	87,000	33,000
Net income	\$ 163,000	\$ 67,000
Net income per share:		
Basic	\$ 3.50	\$ 1.40
Diluted	\$ 3.40	\$ 1.30

Statement of Cash Flows

Kermit The Frog, Inc. Consolidated Statements of Cash Flows (In Thousands)

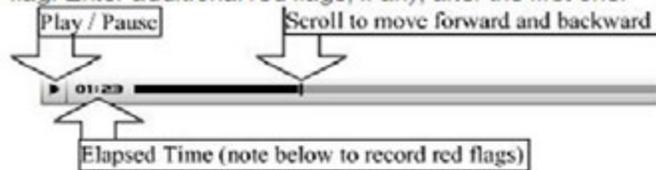
	Year Ended December 31,	
	2006	2005
Cash from operating activities:		
Net income	\$ 139,000	\$ 51,000
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	17,000	9,000
...
Deferred taxes, net	13,000	7,000
...
Net cash provided by operating activities	500,000	80,000
Cash from investing activities:		
Proceeds from sale and maturities of investments	110,000	200,000
Purchases of investments	(140,000)	(200,000)
...
Net cash used in investing activities	(91,000)	(60,000)
Cash from financing activities:		
Proceeds from common stock issuance, net	21,000	-
...
Purchase of treasury stock	(700)	(200)
Net cash provided by financing activities	120,000	2,000
Cash and cash equivalents:		
Increase during the period	529,000	22,000
Balance at beginning of period	431,000	409,000
Balance at end of period	\$ 960,000	\$ 431,000

Conference Call Presentation

Instructions

Below, you are presented with the first few minutes of the question and answer portion from a quarterly earnings conference call from the CEO of the company listed above. Your task is to listen to this audio and identify red flags. A red flag, in our study, exists any time you feel that the CEO's comments are suspicious, give you pause, or require additional investigation. You may follow along using the written transcript appearing below, but you must listen to the full audio recording before proceeding.

Note the elapsed time of each red flag and as much detail about the red flag as possible. Do this by looking at the elapsed time of the audio on the far left. If you detect a red flag, type the elapsed time of the occurrence of the red flag in the box below with a note about what was being discussed and why it is a red flag. Enter additional red flags, if any, after the first one.



When you are ready, click the play arrow below. You can pause and scroll at any time.

Call Presentation and Red Flag List



(Caution: Click Expunged to access audio, *only* if it fails to play above.)

(List Red Flags below)

0.24 - 0.26: when Kermit speaks about flies and mosquitoes (add description of why)
1.14 - 1.32: When Kermit describes the characters of the movie (add description of why)

- The screen above is for the **Audio condition**
- The video states the following text while simultaneously visually demonstrating what is being said:

“Part Two

I will now discuss part two of the evaluation process—“Conference Call Presentation and Red Flag List.”

Recall that your task is to use the first several minutes of CEO responses to analyst questions in a quarterly earnings conference call of a public company and do the following two things: (1) determine whether you think the results being discussed are fraudulent and (2) identify potential red flags in the audit of this company. Here you will listen to the entire audio excerpt and list red flags. On the next page, part three, you will answer some additional questions about fraud.

Please pause the video now and read the instructions provided above, if you have not already done so. When you are finished, un-pause to view the rest of this video.

I will now demonstrate how to play the audio and, importantly, how to list red flags.

- Play the audio by clicking on the play arrow.

- Pause the audio by clicking here. As you can hear in our intentionally light-hearted example, Kermit is being questioned by an analyst. Note that all analyst voices are computerized. This will also be the case in the four real companies that you evaluate; however, while the voices may be computerized, the questions, names, and responses in those four companies will be real.
- Please note the elapsed time directly to the right of play arrow. As you can see, 10 seconds have now elapsed. You may be able to view the time remaining on the far right. Please ignore this and only use the elapsed time, listed on the left, here.
- I will now play the audio from the beginning by dragging this slider back to the starting position. Notice that the elapsed time has now changed to zero.
- Now, I will push play and listen for red flags. Obviously, in this light-hearted example, there are no actual red flags, but for the sake of explanation, assume that I detect two.
 - Assume that the first red flag occurs in the time range of 0:24 to 0:26, when Kermit discusses flies and mosquitoes.
 - In order to precisely determine the range, I will move the slider back and forth to replay the section of interest.
 - Having found the suspicious range, I will jot it down in this box.
 - Also, if this were a real company, I would add a description of why I felt this was a red flag.
- Assume that I continue to listen and that I find another red flag in the range of 1:14 to 1:32. I will jot this down as well. You can list as many red flags as necessary in this box.

You must listen to the entire audio excerpt at least once.

Notice, that if you scroll down, you can follow the written transcript of the conference call excerpt.

Take a moment now to practice and become comfortable with this task. After you have done so, click next to move to the third and last part of the evaluation process and the Guided Tour of Example #3. Please note, that you must certify that you have listened to the entire audio clip before you can proceed.”

Transcript

Susie Greenberg, Morgan Swampy- Analyst

Good afternoon. I have a question about your salary, Mr. Frog. You are paid basically nothing for your role as CEO, movie and television talent. Could you elaborate on the relatively low amount you are paid and why you have decided to go this route?

Kermit Frog, Kermit the Frog, Inc. - Chairman and CEO

Well, well, I get flies and mosquitoes, and things like that. You mean money? No, I'm, I am not actually, I don't actually do this for the bucks. You see, I do this because I enjoy it.

Well, you know, I suppose I could. I sort of gave that up. I don't really have pockets to put it in. You don't need it so much when you live in the swamp. I mean I, I know you are a vegan, and I, I apologize, but my lunch just flies by.

Mike Forbin, Tadpoles and Co. - Analyst

You have a new movie on the horizon. I would like to know more about the plot. What is the basic set-up and scheme that you are going for? Also, how do you think this will translate to a new generation of viewers?

Kermit Frog, Kermit the Frog, Inc. - Chairman and CEO

Well, the plot of the film, basically, it starts out with, ah, a character named Gary, who is played by, uh, Jason Segel, and Walter, who is played by Walter. And, then, there is Amy Adams who plays Mary. And Gary and Mary are, are, are about to get married, or so Mary thinks, but Walter is kind of the third wheel, you, ya see, because his is Gary's childhood friend. So, they all decide to go to L.A. Uh, Mary hoping to get married to Gary, and Walter hoping to meet the Muppets.

We're just so thrilled that a whole generation of, of, now, adults, who grew up with us as the Muppet Show Muppets, can, uh, now meet us again with their own kids. I think it is just wonderful.
<< time limit reached >>

Next, you will answer a few more questions about this company. You will not be able to revisit any of the information above.

Are you ready to proceed? You **must** listen to the full audio recording before continuing.

"I have listened to the audio recording in its entirety."

- The screen above is for the **Audio condition**

Conference Call Presentation

Instructions

Below, you are presented with the first few minutes of the question and answer portion from a quarterly earnings conference call from the CEO of the company listed above. Your task is to read the transcript and identify red flags. A red flag, in our study, exists any time you feel that the CEO's comments are suspicious, give you pause, or require additional investigation. You must read the entire transcript before proceeding.

Note the line number of each red flag and as much detail about the red flag as possible. Do this by looking at the line number on the far left. If you detect a red flag, type the line number where the red flag occurred in the box below with a note about what was being discussed and why it is a red flag. Enter additional red flags, if any, after the first one.

(List Red Flags below)

Line 1: when Kermit speaks about flies and mosquitoes {add description of why}
Lines 6-9: When Kermit describes the characters of the movie {add description of why}

- The screen above is for the **Transcript only condition**
- The video states the following text while simultaneously visually demonstrating what is being said:
“Part Two
I will now discuss part two of the evaluation process—“Conference Call Presentation and Red Flag List.”

Recall that your task is to use the first several minutes of CEO responses to analyst questions in a quarterly earnings conference call of a public company and do the following two things: (1) determine whether you think the results being discussed are fraudulent and (2) identify potential red flags in the audit of this company. Here you will read the entire excerpt, below, and list red flags in this box. On the next page, part three, you will answer some additional questions about fraud.

Please pause the video now and read the instructions provided above, if you have not already done so. When you are finished, un-pause to view the rest of this video.

I will now demonstrate how to list red flags.

- First, read the transcript excerpt.
- As you can see in our intentionally light-hearted example, Kermit is being questioned by analysts. Note that for the four real companies that you evaluate the questions, names, and responses will be real.
- Please note that each line of the CEO's responses is numbered, to the left of the text.
- I will now look for red flags. Obviously, in this light-hearted example, there are no actual red flags, but for the sake of explanation, assume that I detect two.
 - Assume that the first red flag occurs on line 1, when Kermit discusses flies and mosquitoes.
 - Having found the suspicious line, I will jot it down in this box.
 - Also, if this were a real company, I would add a description of why I felt this was a red flag.

- Assume that I continue to read and that I find another red flag on lines 6 through 9. I will jot this down as well. You can list as many red flags as necessary in this box.

You must read the entire transcript at least once.

Take a moment now to practice and become comfortable with this task. After you have done so, click next to move to the third and last part of the evaluation process and the Guided Tour of Example #3. Please note, that you must certify that you have read the entire transcript excerpt before you can proceed.”

Transcript

Susie Greenberg, Morgan Swampy- Analyst

Good afternoon. I have a question about your salary, Mr. Frog. You are paid basically nothing for your role as CEO, movie and television talent. Could you elaborate on the relatively low amount you are paid and why you have decided to go this route?

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8 Adams who plays Mary. And Gary and Mary are, are, are about to get married, or so Mary
9 thinks, but Walter is kind of the third wheel, you, ya see, because his is Gary's childhood
10 friend. So, they all decide to go to L.A. Uh, Mary hoping to get married to Gary, and Walter 11 hoping
to meet the Muppets.

12 We're just so thrilled that a whole generation of, of, now, adults, who grew up with us as the
13 Muppet Show Muppets, can, uh, now meet us again with their own kids. I think it is just
14 wonderful.

<< time limit reached >>

Next, you will answer a few more questions about this company. You will not be able to revisit any of the information above.

Are you ready to proceed? You **must** read the entire transcript before continuing.

"I have read the transcript in its entirety."

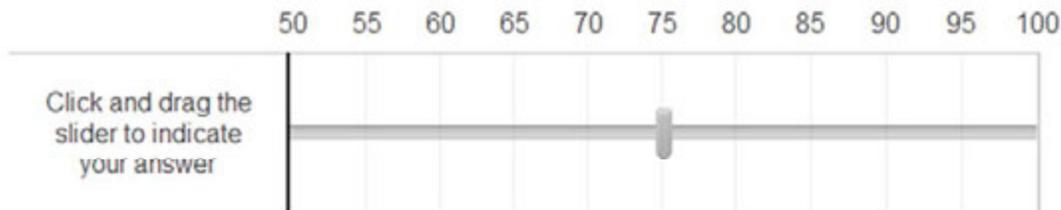
- The screen above is for the **Transcript only condition**

Screen 5 – Initial Instructions

Next, provide an overall judgment of whether it is more likely than not that fraud was being committed at this company during this quarter. That is, did this company later restate this quarter's financial results due to one or more of the following: fraudulent financial results, a regulatory investigation, or a class action lawsuit?

- Yes, fraud was likely being committed during this quarter.
- No, fraud was not likely being committed during this quarter.

What is the probability that your judgment above is correct?



Assume you are the partner in charge of the financial statement audit of this company. Indicate below which (if any) audit areas appear to be problematic and will require additional attention and testing during the course of the audit. Check more than one box if desired.

	Overstatement	Understatement
Assets	<input type="checkbox"/>	<input type="checkbox"/>
Liabilities	<input type="checkbox"/>	<input type="checkbox"/>
Revenues / Gains	<input type="checkbox"/>	<input type="checkbox"/>
Expenses / Losses	<input type="checkbox"/>	<input type="checkbox"/>
Other / Additional (Please elaborate in the space provided below.)	<input type="checkbox"/>	<input type="checkbox"/>

- A video states the following text while simultaneously visually demonstrating what is being said:
 “Part Three
 Finally, please answer a few more questions about the company.
- Once you have reached these questions, you will not be able to return to the prior screen to examine the conference call again or to look at the financial information.
- The first question asks you about fraud. As you can see, it says the following:

1. Next, provide an overall judgment of whether it is more likely than not that fraud was being committed at this company during this quarter. That is, did this company later restate this quarter's financial results due to one or more of the following: fraudulent financial results, a regulatory investigation, or a class action lawsuit?

- Yes, fraud was likely being committed during this quarter.
- No, fraud was not likely being committed during this quarter.

- After you have answered these and a few more questions, you will move on to evaluate the next company. After evaluating four companies, you will move to a short exit survey.
- Thank you again for helping us investigate this important audit topic. Your responses are very important. We very much value your time.”

Screen 6 – Initial Instructions

Next, indicate how much cognitive dissonance the CEO felt during this excerpt of the conference call. Cognitive dissonance is the negative, uncomfortable emotion a person feels when they are saying something that they know is not true.

No Cognitive Dissonance Very High Cognitive Dissonance

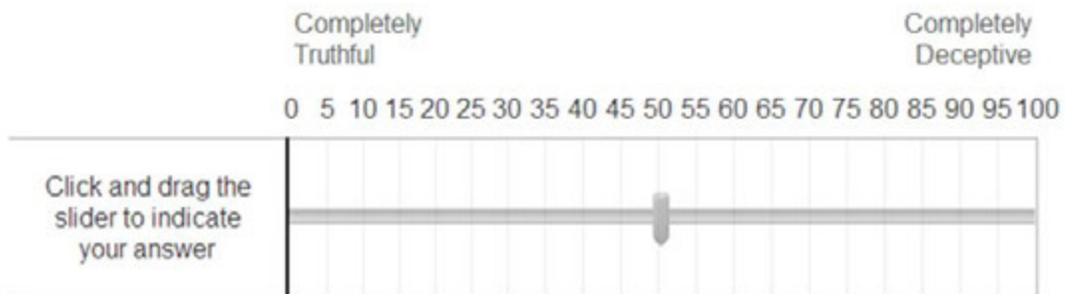
0 1 2 3 4 5 6 7 8 9 10

Click and drag the slider to indicate your answer

- Only participants in the “**aware of cognitive dissonance**” saw this screen. No comparable screen was provided to participants in the “unaware of cognitive dissonance” condition.

Screen 7 – Initial Instructions

What is your impression: was the CEO being truthful or deceptive?



Would you please succinctly but specifically list cues that gave you this impression? (If no cues gave you an impression, please type "none" in the box below.)

Screen 8 – Initial Instructions

This company may or may not have had to restate this quarter's financial results due to one or more of the following: fraudulent financial results, a regulatory investigation, or a class action lawsuit. **Before** participating in this study, were you aware of any financial improprieties for this company?

- Yes
- No

What general level of familiarity did you have with this company **before** doing this study?

Very Low Very High

0 1 2 3 4 5 6 7 8 9 10

Click and drag the slider to indicate your answer

During the course of this study did you look up any additional information about this company, outside of the information we provided for you?

- Yes
- No

Click below when you are ready to move on to the next company. You will not be able to change any of your answers above.

- "I am ready to evaluate the next firm."

The Experiment: Example Screen Shots for One Company (PKTR)

Notes for Reviewer:

- Participants evaluated four out of 10 possible companies.
- For all four companies, instructions and the data collected from participants (i.e., the “red flags” and screens 3-5) were identical.
- These are screen shot taken from the “**audio**” (versus “**transcript only**”) condition and the “**aware of cognitive dissonance**” (versus “**unaware of cognitive dissonance**”) condition. Differences between these conditions are indicated below.

Screen 1 – The Experiment: Screen Shots for One Company (PKTR)

Instructions

You will be presented with the first several minutes of CEO responses to analyst questions in a quarterly earnings conference call of a public company. Your task is to (1) determine whether you think the results being discussed are fraudulent and to (2) identify potential red flags in the audit of this company.

Note: Research indicates that certain cues in what a CEO says and how s/he says it can help in the detection of deception. One cue found to be useful in detecting deception in these CEO responses is cognitive dissonance. Cognitive dissonance is the negative, uncomfortable emotion a person feels when they are saying something that they know is not true. Those experiencing cognitive dissonance feel uncomfortable, uneasy, and bothered.

This screen consists of 3 main parts.

(1) Background Company Information
This section lists background company information and financial statements.

(2) Conference Call Presentation and Red Flag List
In this section, you are presented with the first few minutes of the question and answer period from a quarterly earnings conference call. You are then asked to record each red flag you detect.

(3) Fraud Assessment
On the next screen, you will be asked to assess the likelihood that this company had to restate their earnings. You will also be asked a few other questions about this company.

- Participants in the “**unaware of cognitive dissonance**” condition viewed all of this screen with the exception that the box above that starts with “Note:” said the following:
“Note: Research indicates that certain cues in what a CEO says and how s/he says it can help in the detection of deception.”

Company Information

First, you may wish to use the following information about this company. Please do not access any other information. It is critical that you do not do so. We have intentionally given you less information than you would normally have. This complies with the principles of good scientific research.

Company Name and Relevant Quarter

Packeteer, Inc. (NASDAQ: PKTR)

"Packeteer, Inc. Announces Fourth Quarter and Full Year Financial Results"

Business Overview

Packeteer provides wide area network, or WAN, Application Delivery systems designed to deliver a set of visibility, Quality of Service, or QoS, control, compression, application acceleration and branch office service capabilities. Their product family includes PacketShaper, iShared, SkyX and Mobiliti Client products that can be deployed within large data centers, smaller branch office sites and software clients on PCs for mobile and Small Office/Home Office, or SOHO, users throughout a distributed enterprise. They use an "intelligent overlay", which bridges applications and IP networks, adapts to customers' existing infrastructure and addresses the demands created by a changing application environment in to deliver applications across all WAN and Internet links. The company was founded in 1996 and is headquartered in Cupertino, CA.

Packeteer helps package the internet for business use. Packeteer, Inc. develops bandwidth management systems that enable businesses and ISPs to find and classify network traffic, analyze network performance, control traffic, and prioritize Web site access. Its products help network managers reduce congestion that can result from heavy internet traffic.

WAN Application Delivery products are designed to solve network and application performance problems that provide visibility into application performance and network utilization, control over network performance and network utilization, compression and protocol acceleration to accelerate performance and increase WAN capacity. PacketShaper is designed to provide application traffic monitoring, bandwidth provisioning and management. The PacketShaper family currently includes the 1400, 1700, 3500, 7500, and 10000 models. iShared is suited for environments with large amounts of collaborative traffic (files, email, and large documents). It provides Wide Area File Services, or WAFS, with CIFS acceleration, general WAN optimization technologies, Web object caching and TCP acceleration. It also has the ability to deliver Microsoft-based branch office services and integrate with Microsoft security and management frameworks. SkyX enhances the performance and efficiency of Internet and private network access. The product line includes the PX250 and PX750 models. Mobiliti software products provide solutions for the mobile and SOHO users.

Balance Sheet**PACKETEER, INC.
CONSOLIDATED BALANCE SHEETS**

	December 31,	
	2006	2005
	(In thousands, except per share amounts)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 39,640	\$ 36,221
Short-term investments	25,681	81,228
Accounts receivable, net of allowance for doubtful accounts and sales returns of \$3,010 and \$1,800, as of December 31, 2006 and 2005, respectively	31,743	15,759
Other receivables	216	207
Inventories	3,957	4,979
Prepays and other current assets	3,249	2,148
Total current assets	104,486	140,542
Non-current assets:		
Property and equipment, net	3,968	2,681
Long-term investments	11,236	5,228
Goodwill	58,656	9,527
Purchased intangible assets, net	11,045	5,606
Other non-current assets	27,577	5,073
Total assets	\$216,968	\$168,657
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 3,014	\$ 2,808
Accrued compensation	9,567	6,551
Other accrued liabilities	8,431	4,716
Income taxes payable	7,164	3,520
Deferred revenue	23,931	18,986
Total current liabilities	52,107	36,581
Non-current liabilities:		
Deferred revenue, less current portion	5,173	3,129
Deferred rent and other	179	340
Total liabilities	57,459	40,050
Commitments and contingencies (Notes 4 and 5)		
Stockholders' equity:		
Preferred stock, \$0.001 par value; 5,000 shares authorized; no shares issued and outstanding as of December 31, 2006 and December 31, 2005	—	—
Common stock, \$0.001 par value; 85,000 shares authorized; 35,400 and 34,197 shares issued and outstanding as of December 31, 2006 and December 31, 2005, respectively	36	34
Additional paid-in capital	212,961	188,046
Deferred stock-based compensation	—	(567)
Accumulated other comprehensive loss	(18)	(182)
Accumulated deficit	(53,470)	(58,724)
Total stockholders' equity	159,509	128,607
Total liabilities and stockholders' equity	\$216,968	\$168,657

Income Sheet**PACKETEER, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS**

(In thousands, except per share amounts)	2006	2005
Net revenues:		
Product revenues	\$110,164	\$ 85,590
Service revenues	34,959	27,351
Total net revenues	145,123	112,941
Cost of revenues:		
Product costs	26,028	19,575
Service costs	10,907	8,163
Amortization of purchased intangible assets	2,150	1,557
Total cost of revenues	39,085	29,295
Gross profit	106,038	83,646
Operating expenses:		
Research and development	30,646	21,778
Sales and marketing, includes amortization of purchased intangible assets of \$791 in 2006, and none in 2005 and 2004	57,889	38,276
General and administrative	13,949	7,222
In-process research and development	1,800	—
Total operating expenses	104,284	67,276
Income from operations	1,754	16,370
Interest and other income, net	3,932	2,913
Income before provision (benefit) for income taxes	5,686	19,283
Provision (benefit) for income taxes	782	125
Net income	\$ 4,904	\$ 19,158
Basic net income per share	\$ 0.14	\$ 0.57
Diluted net income per share	\$ 0.14	\$ 0.55
Shares used in computing basic net income per share	34,848	33,823
Shares used in computing diluted net income per share	35,740	35,065

Statement of Cash Flows

PACKETEER, INC. CONSOLIDATED STATEMENTS OF CASH FLOWS

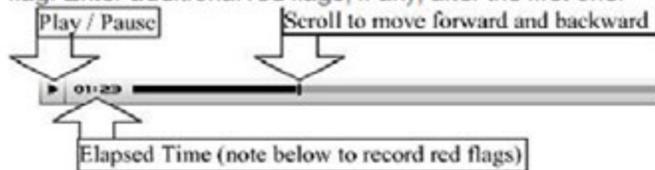
(In thousands, except per share amounts)	2006	2005
Cash flows from operating activities:		
Net income	\$4,904	\$19,158
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	2,630	2,414
Amortization of purchased intangible assets	2,941	1,557
Provision for (reversal of) allowance for doubtful accounts	292	(45)
Write-down of inventory	568	89
Stock-based compensation related to Mentat acquisition	484	901
Stock-based compensation related to stock options and ESPP	13,311	—
Excess tax benefit from stock-based compensation plans	(981)	—
Tax benefits from employee stock option plans	2,829	1,191
Deferred income taxes	(5,794)	(2,967)
Loss on disposal of property and equipment	9	20
In-process research and development	1,800	—
Changes in operating assets and liabilities, net of acquired assets and assumed liabilities:		
Accounts receivable	(14,324)	1,114
Other receivables	(9)	1,680
Inventories	680	(1,962)
Prepays and other current assets	(522)	(186)
Accounts payable	206	6
Accrued compensation	2,397	84
Other accrued liabilities	(247)	(1,163)
Income taxes payable	2,846	1,082
Deferred revenue	6,476	5,958
Other	(68)	(50)
Net cash provided by operating activities	20,428	28,881
Cash flows from investing activities:		
Purchases of property and equipment, net	(3,626)	(2,049)
Purchases of investments	(66,834)	(109,851)
Proceeds from sales and maturities of investments	120,156	104,945
Acquisitions, net of cash acquired	(66,930)	(1,750)
Funds deposited into escrow in connection with acquisition	(7,850)	—
Net cash used in investing activities	(25,084)	(8,705)
Cash flows from financing activities:		
Proceeds from issuance of common stock, net of repurchases	4,583	3,027
Sale of stock to employees under the ESPP	2,511	2,346
Excess tax benefit from stock-based compensation plans	981	—
Proceeds from repayment of notes receivable from stockholders	—	—
Payments of notes payable	—	—
Principal payments of capital lease obligations	—	—
Net cash provided by financing activities	8,075	5,373
Net increase (decrease) in cash and cash equivalents	3,419	25,549
Cash and cash equivalents at beginning of year	36,221	10,672
Cash and cash equivalents at end of year	\$39,640	\$36,221
Non-cash investing and financing activities:		
Issuance of restricted common stock, net of repurchases, to former Mentat employees	\$—	\$—
Options assumed in acquisition of Tacit	\$2,482	\$—

Conference Call Presentation

Instructions

Below, you are presented with the first few minutes of the question and answer portion from a quarterly earnings conference call from the CEO of the company listed above. Your task is to listen to this audio and identify red flags. A red flag, in our study, exists any time you feel that the CEO's comments are suspicious, give you pause, or require additional investigation. You may follow along using the written transcript appearing below, but you must listen to the full audio recording before proceeding.

Note the elapsed time of each red flag and as much detail about the red flag as possible. Do this by looking at the elapsed time of the audio on the far left. If you detect a red flag, type the elapsed time of the occurrence of the red flag in the box below with a note about what was being discussed and why it is a red flag. Enter additional red flags, if any, after the first one.



When you are ready, click the play arrow below. You can pause and scroll at any time.

Call Presentation and Red Flag List



(Caution: Click Expunged to access audio, *only* if it fails to play above.)

(List Red Flags below)

- Audio condition

Transcript

Troy Jensen, Piper Jaffray - Analyst

Just to go back on the gross margin line, how much of the gross margins being down was maybe the mix with a whole bunch of the 1400 models versus pricing discounts or erosion on the legacy side?

Dave Cote, Packeteer, Inc. - President, CEO

But I'm, but I think I want to make sure that we do also say the mix was a factor, I mean, the 1400. Um, and, and, and frankly that is we view that as very good news. It means bigger deployments. So we did see, as I said, 75% of our, our units were Edge. And, and that does have a slightly, you know, lower gross margin on it.

Troy Jensen, Piper Jaffray - Analyst

Dave, a follow-up for you. Can you talk about Tacit a little bit? Competitively, maybe give us some understanding when you win a competitive deal with Tacit, why do you win, and vice versa when you lose where the key reasons why you would lose a deal?

Dave Cote, Packeteer, Inc. - President, CEO

You know, if I look at the, the wins, it's, it's some of the things I talked about. I mean people that have, ah, clearly people who have, ah, an important, ah, focus on a Microsoft environment and our ability to operate in that environment and deliver native CIFS acceleration, our virtual file system, I mean, what I would consider a traditional WAFS, true WAFS solution, I think we have a very, very competitive product and, and win our unfair share there. Um, I think as I mentioned that in pure, what I call pure acceleration deals, we're actually seeing the Shaper, and in some cases like in data center replication the SkyX product, be really our point product against a Riverbed, where the TCP acceleration is the primary factor. Um, and, and so I guess, you know, it, it, it isn't so much, um, iShared versus Riverbed, sometimes it is PacketShaper versus Riverbed.

Matt Robison, Ferris, Baker Watts - Analyst

What is -- why was R&D sequentially down? I missed that. And also the percentage of sales from Edge? And then the last -- then I have one brief follow-up.

Dave Cote, Packeteer, Inc. - President, CEO

Let me cover the Edge stuff, while David pulls up the other data. Um, eh, essentially it was just a higher, higher number of, ah, I mean, led, led by 1400, but just a higher number of deals that involved, ah, lots of branch locations.

Matt Robison, Ferris, Baker Watts - Analyst

In the past you had been more like 70% core on the revenue side, right?

Dave Cote, Packeteer, Inc. - President, CEO

70, yeah.

Matt Robison, Ferris, Baker Watts - Analyst

Then what gives you -- you said a lot -- and a lot of things that sound very promising. But what are the top two or three things that give you the confidence of being able to duplicate that revenue growth number, especially given that a portion of your revenue growth in '06 was inorganic?

- Audio condition

Dave Cote, Packeteer, Inc. - President, CEO

That was a relatively, yeah, relatively small amount, if you look at it. Um, but beyond that I think that we have, um, as David alluded to, made a significant set of changes in our organization from a people standpoint, ah, heavily in, in sales where we have new sales leadership in three out of four geographies. We have added 50%, ah, to our sales organization. And all of that being done through the course of a very successful year. Now I think we hit the ground running with a much more powerful, larger and effective sales organization.

Um, our product pipeline, ah, is, as I said, the strongest we've had in the history of the Company. And you will see in the first-half a number of product announcements that, um, either enhance our current position or actually open up some new opportunities for us. Um, and that pipeline continues beyond that. It is just that, ah, you know, in the next 6 months there will be some, I think, some very good stuff.

Um, I think some of our big partnerships that, ah, came to us as a result of the, ah, the Tacit acquisition. Ah, Microsoft. I think, ah, in a number of different ways, both product, sales and marketing, represents an opportunity for partnership with a very, very major player that has a, v, a strong vested interest in this ongoing server consolidation strategy. And we are the only native, ah, Microsoft application, which not only helps us from a joint marketing standpoint, but from a technology standpoint we know what Microsoft is, is doing. We're working with them to make sure that our products complement what they do. And, ah, I think that, that will benefit us.

I think related to that is our partnership with Brocade, which really, you know, helps us into a, ah, a segment of the marketplace that is somewhat new for us in storage, and to some degree server. Um, you know, their business is ramping, and that will be a more meaningful part of, ah, of our business, you know, in, in '07.

Ah, so I think there is just a number of different, um, and, and then the overall market itself. I think the awareness of what is going in the marketplace, um, and, and the importance of these technologies. And, and not just the acceleration technology, the, the buzz around acceleration is only one factor. There is the ongoing and increasing complexity associated with, you know, MPLS and voice video convergence. Um, I think video is going to be a very important phenomenon moving forward, because it is a huge, ah, amount of bandwidth. Um, at the same time, customers have, have got to be able to manage it.

So I think the market in general, ah, is, is improving. Our product pipeline is stronger. Our solution is broader than anybody in the market. And we've got the resources in our sales organization to really drive the revenue.

Jonathan Curtis, JMP Securities - Analyst

From JMP Securities. Can you help us understand what drove your decision into the quarter to offer the two-for-one pricing on Tacit? And then obviously you have extended it into the March quarter. What is driving that decision?

And then it looks like the performance of Tacit, I guess you guys have guided it to a range of about \$4 million to \$5 million. Are you happy with the performance of it this quarter, and what was your internal target for the quarter?

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So let me take your first question. I think that the two-for-one is, is really just a way to build some awareness into the marketplace, ah, particularly with our installed base. And, ah, in many respects it represents more of a trial opportunity than anything else. So here's a way to sort of, you know, put a, put a little bit of a promotion out there on the, on the technology. And, and I think we continue to, to want to do that, along with a number of things. Ah, I mentioned in our, um, ah, in, in my prepared remarks that, um, Microsoft announced an extension of their branch office promotion, and we joined that to offer 30% off on our Flexinstall product. Really just trying to, ah, continue to take advantage of the growing awareness in the marketplace and, and build trial. That is what is behind the, ah, network assessment that we're offering
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"I have listened to the audio recording in its entirety."

- **Audio condition**

Conference Call Presentation

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62 is behind the, ah, network assessment that we're offering
<<experiment time limit reached>>

Next, you will answer a few more questions about this company. You will not be able to revisit any of the information above.

Are you ready to proceed? You **must** read the entire transcript before continuing.

"I have read the transcript in its entirety."

- **Transcript only condition**

Screen 2 – The Experiment: Screen Shots for One Company (PKTR)

Next, provide an overall judgment of whether it is more likely than not that fraud was being committed at this company during this quarter. That is, did this company later restate this quarter's financial results due to one or more of the following: fraudulent financial results, a regulatory investigation, or a class action lawsuit?

- Yes, fraud was likely being committed during this quarter.
- No, fraud was not likely being committed during this quarter.

What is the probability that your judgment above is correct?

50 55 60 65 70 75 80 85 90 95 100

Click and drag the slider to indicate your answer

Assume you are the partner in charge of the financial statement audit of this company. Indicate below which (if any) audit areas appear to be problematic and will require additional attention and testing during the course of the audit. Check more than one box if desired.

	Overstatement	Understatement
Assets	<input type="checkbox"/>	<input type="checkbox"/>
Liabilities	<input type="checkbox"/>	<input type="checkbox"/>
Revenues / Gains	<input type="checkbox"/>	<input type="checkbox"/>
Expenses / Losses	<input type="checkbox"/>	<input type="checkbox"/>
Other / Additional (Please elaborate in the space provided below.)	<input type="checkbox"/>	<input type="checkbox"/>

Screen 3 – The Experiment: Screen Shots for One Company (PKTR)

Next, indicate how much cognitive dissonance the CEO felt during this excerpt of the conference call. Cognitive dissonance is the negative, uncomfortable emotion a person feels when they are saying something that they know is not true.



- Only participants in the “**aware of cognitive dissonance**” saw this screen. No comparable screen was provided to participants in the “**unaware of cognitive dissonance**” condition.

Screen 4 – The Experiment: Screen Shots for One Company (PKTR)

What is your impression: was the CEO being truthful or deceptive?



Would you please succinctly but specifically list cues that gave you this impression? (If no cues gave you an impression, please type "none" in the box below.)

Screen 5 – The Experiment: Screen Shots for One Company (PKTR)

This company may or may not have had to restate this quarter's financial results due to one or more of the following: fraudulent financial results, a regulatory investigation, or a class action lawsuit. **Before** participating in this study, were you aware of any financial improprieties for this company?

- Yes
- No

What general level of familiarity did you have with this company **before** doing this study?

Very Low Very High

0 1 2 3 4 5 6 7 8 9 10

Click and drag the slider to indicate your answer

During the course of this study did you look up any additional information about this company, outside of the information we provided for you?

- Yes
- No

Click below when you are ready to move on to the next company. You will not be able to change any of your answers above.

- "I am ready to evaluate the next firm."

Exit Survey

Notes for Reviewer:

- These screens were viewed once by all participants after evaluating four companies.
- The exit survey did not vary by condition.

Screen 1 – Exit Survey

Exit Survey

These final few questions will improve the quality of our analysis. Please take a few more moments and answer to the best of your ability.

Questions About Your Professional Experience

1. How many years have you worked in audit, assurance, and/or fraud/forensic services?
2. How many years of public company audit experience do you have?
3. What is your current or final position or job title (e.g. student, senior, manager, partner, lecturer, etc.)?
4. For how many years did you work (have you worked) with your most recent (current) employer?
5. What is the highest level of education you attained?
6. If your work was concentrated in one (or a few) industry(ies), please list it (them).
7. Please list all of your professional certifications / designations (if any), such as CPA, CFE, etc.
8. If different from #3 above, what was your highest position or job title in a public service firm (e.g. senior, manager, partner, etc.)?

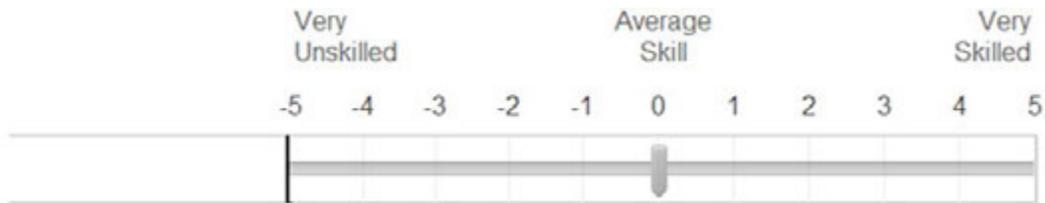
9. Gender

Male Female

10. How much experience do you have detecting fraud and deception?



11a. Compared to your peers, how skilled are you at detecting fraud and deception?



11b. Do you classify yourself as more of an audit or fraud/forensic professional?



12. Please explain, in as much detail as possible, all of the training you have received on deception detection. Please make sure to indicate
(1) the frequency of the training,
(2) the content and extent of the training, and
(3) and whether the training came while working at the current accounting firm, a prior accounting firm, or some other source.

Is there anything else you would like to tell us that might help us improve our analysis or interpret our results?