

Part of Chapter 27
27. SHORT STORIES
(All true)

In December 1995 I attended a class for CPAs that I needed for continuing education requirements in order to keep my CPA license. There were about 100 students attending. I sat in the second row from the back. I turned around and talked to the auditor behind me. He said he was an employee for one of the big CPA firms. I asked him what he did there. He said he audited banks. I found him interesting. I asked him if he could teach me a few things. He said, "Sure, what can I teach you."

I replied, "On a \$100,000 bank loan, how much legal tender does the bank have to loan in order for the bank to legally own the bank promissory note?"

He responded, "That's easy, \$100,000."

"Does the bank record a loan from the borrower in the amount of \$100,000?" I asked.

He said no. "Why would you loan the bank \$100,000? You are the borrower. You are going to the bank for the loan, not the reverse."

I said, "I get it. I loan the bank the promissory note and they loan me something, am I right?"

He wanted to know where I graduated from. He said, "The bank loans you \$100,000 from other depositor's money."

I asked, "Is a check money, or merely an order pay money?"

He responded, "It doesn't matter, you can get cash for the check."

I responded back, "Legally, what is it, money or merely an order to pay money?"

He again replied, "We think of it as money."

I said, "I do not care what you think. I want to know the law. Do you have the competence to know?" I knew he had to say he did because he did the audit.

He responded, "Legally it is not money."

I asked, "Does the bank record legal tender as a bank asset?"

He answered yes.

I asked, "Does a bank liability mean that the bank owes legal tender?"

He said yes. Then he asked, "Why are you asking all these questions?"

I said that several CPA bank auditors I knew had said that bank loans were a fraud, and I wanted to know more. He exploded and said that whoever was selling those manuals and tapes should be put in jail. I thought to myself, "I never mentioned a manual or tapes." I realized he knew about them from some other source. He demanded to know who I was. I gave him my CPA business card.

He looked at my name and said, "I have seen this name before."

I suggested we go on with our discussion. I asked, "Does the bank disclose all material facts?"

He said, "Yes, they have to or it is fraudulent concealment."

I asked, "Does the bank deny borrowers equal protection under the law?"

He said no.

I said, "On the \$100,000 bank loan, if the bank refused to loan \$100,000 of other depositors' money or legal tender, does the bank legally own the promissory note?"

He said no, because the bank never fulfilled the agreement to loan the money.

I asked, "Does the bank have to follow the Federal Reserve Bank policy and procedures when granting loans?"

He said, "Of course they do, it is the law. They have no choice"

I asked, "What are the bank bookkeeping entries for a loan?"

He said, "The bank replaces the other depositors' cash with the promissory note."

I asked, "Is the promissory note recorded as an asset, and the bank gives the borrower cash?"

He said yes.

"Does the bank give the borrower a bag of cash?"

He said, "Get real, it is a check."

I said, "What happens with the check?"

He said, "If you are buying a house and the bank finances it, the seller of the house deposits the check in his checking account."

I asked, "What is the bank bookkeeping entry?"

He said the check was recorded as a bank asset and a Demand Deposit Account was recorded as a bank liability.

I asked, "Does the check cancel out because it was recorded as a liability and then as a bank asset?" He agreed it cancels out. I said, "What do you have remaining?"

He said, "A bank asset called a promissory note and a new bank liability." Then he got the most horrid look on his face and said, "I never realized it before, but every bank loan is a fraud." He asked me where I found this out. I told him I was an expert witness, it was my job to know.

He said, "No one is to find out, no one is to know this! Do you realize what will happen if people find out? The auditor will get sued and maybe put in jail. Now I have to reissue the audit opinions. If I do this, I will get sued for sure. If I do not, and someone finds out...oh, I don't know what to do." The key thing was, he knew that I knew the bank bookkeeping entries and he could not get away with lying. He knew that if he insisted that the loan money came from other depositors, the bank could never, under any circumstances, record the promissory note as a bank asset. If other depositors' money was loaned, the bank assets and liabilities would have to decrease. The opposite had happened, the bank assets and liabilities increased, showing that the borrower funded the loan. He knew as an auditor he had to perform tests to be sure the bank fulfilled the agreement. Everything he said earlier meant he agreed that the bank did not own the promissory note. Believe me he was not happy. He wanted me to return his business card. I said, "No, one of my clients may want to sue you some day." I told him, "Now that you have admitted to a fraud, will you revise the audit opinion and expose it?"

He would not respond and I thanked God that I had never audited a bank.

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About the author

Tom Schauf has a diverse background. He graduated from Northern Illinois University with a Bachelor of Science with double majors in accounting and finance.

After graduation, he worked as a staff accountant for Motorola. He worked for a small certified public accounting firm, owned and operated his own business brokerage firm and certified public accounting practice.

Over a period of nearly ten years, he has testified in a number of cases as an expert witness in business valuation, and has taught the arts of business acquisition and negotiations to buyers, CPAs, and lawyers on a national level in colleges and major universities.

He has taught lawyers and thousands of CPAs the art of valuation and negotiations in his copyrighted course designed to meet continuing education requirements.

He has been a controller, and head of purchasing and personnel for a major manufacturing company. He was also a real estate broker and aircraft flight instructor (CFII).

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