Thor Industries, Inc. claims to be the world’s largest manufacturer of recreational vehicles and a major builder of buses and ambulances. Its fiscal July 2010 sales were $2.2 billion, and its net income was $110 million. In fiscal 1998, it had sales of $715.6 million and net income of $19.4 million. In October 1999, the U.S. Securities & Exchange Commission (SEC) ordered Thor to cease and desist further violations of securities laws following the coverup of embezzled funds in a subsidiary, which required restatement of results in years ended July 1996 through 1998. In May 2011, Thor became the subject of another SEC order to cease and desist—this time for having poor internal controls that required restating years ended 2004 through 2006.

According to SEC release No. 34-42021, the 1999 case involved Thor subsidiary ElDorado National, Inc. Absence of internal controls enabled Bradley John Buchanan, general manager and controller of ElDorado, to embezzle more than $400,000 in cash over a four-year period. He also overstated ElDorado’s reported income in order to obtain bonuses of $55,297. Without sufficient oversight, Buchanan was able to write checks to himself ($105,000), initiate wire transfers to himself or to his private corporation ($262,000), and direct the issuance of money orders to himself or his corporation ($48,000).

The cooking of ElDorado’s books went undetected by Thor’s corporate management in Jackson Center, Ohio, and its external auditors, Deloitte & Touche (D&T). Apparently, neither visited the ElDorado’s offices where accounting records were kept during the relevant period. D&T used a “rotational” system to select subsidiaries designed to audit those covering at least 70% of consolidated assets, and, as of January 1998, ElDorado amounted to only 5.1% and 2.8% of consolidated sales and net income, respectively, and had only five salaried employees.

The only penalty assessed on Thor by the SEC in 1999 was to “cease and desist from committing or causing any violation, and any future violations” of the relevant sections of the Exchange Act of 1934. The Wall Street Journal reported on May 8, 1998, that Thor hired the forensic-auditing group at Deloitte & Touche to help in “the investigation of this loss and any possible recovery.” (You wonder why the audit committee didn’t choose a different firm.) Buchanan was also charged criminally.

The 2011 case involved a very similar scenario in which poor internal control in a subsidiary again enabled a senior executive to commit fraud. Without admitting or denying the SEC’s charges, Thor agreed to permanently comply with the 1999 cease and desist order that prohibited violations of the books and records and internal controls provisions of the securities laws. The second offense also triggered a $1 million civil penalty, and Thor agreed to hire an independent consultant to review and evaluate internal controls and recordkeeping policies and procedures.

In Litigation Release No. 21966, the SEC charged Mark C. Schwartzhoff, former vice president of Finance at Thor’s Dutchmen Manufacturing, Inc. subsidiary, with securities fraud and other violations. Dutchmen amounted to approxi-
ETHICS

In December 2002, he hid a
was able to engineer was in cost of
largest area of fraud Schwartzhoff
instead of to payroll tax expense.
entries to a balance sheet account
concealed these payments by mak-
knowledge of its computer and
file and manipulated individual
information into a separate computer
subaccounts so the total agreed
with the amounts he had provided
to Thor’s corporate offices.
Schwartzhoff’s career with Thor
may have provided him with the
knowledge of its computer and
accounting systems to lead him to
believe he could commit fraud and
not be discovered. From 1992 to
1995, he served as a corporate inter-
auditor for Thor. He joined
Dutchmen as controller in 1995
and became VP of Finance in 1997.
As VP, he was responsible for
Dutchmen’s financial accounting,
cost accounting, information tech-
nology, human resources, and
product dispatch/shipping func-
tions. He was terminated in January
2007 after admitting to the fraud.

In addition to the 1999 SEC
action, there were other red flags
present during the Schwartzhoff
fraud. D&T’s 1999 management
letter identified the main risk of
fraud at Thor as a lack of segrega-
tion of duties at its subsidiaries.
The July 2004 internal audit of
Dutchmen also found segregation
of duties deficiencies and noted
that an excess number of individ-
uals, including Schwartzhoff, had
access rights to the computer sys-
tem to print checks. These red
flags apparently went unheeded.

Schwartzhoff benefited person-
ally from his fraudulent activity by
receiving unearned bonuses
between 2004 and 2007 that
amounted to approximately
$300,000. He also received a bonus
based on a percentage of Dutch-
men’s pre-tax income under a
management incentive plan. In a
separate criminal action,
Schwartzhoff pled guilty to one
count of wire fraud and agreed to
repay restitution of $1.9 million.
The SEC also barred him from
ever serving again as an officer or
director of a public corporation.

Civil lawsuits have been filed
against Thor, which experienced a
27% drop in its stock price after
the announcement that D&T was
engaged in a review of accounting
methods. About the same time,
D&T decided to manage the 2010
audit of Thor from its Chicago
office and not Dayton, Ohio, as
had been done previously.
Thor was given credit by the
SEC for “self-reporting and signifi-
cant cooperation” in the investi-
gation. Further, the company hired a
new CFO and senior VP in May
2008 and added two new members
to the board of directors: an expe-
rined practicing CPA in March
2010, and the chair and CEO of a
large public company in December
2010. Both have served as public
company audit committee chairs.
The SEC actions against Thor are
subject to judicial review by the
U.S. District Court for the District
of Columbia. Among the factors to
be considered by the Court is
whether the penalties assessed on
Thor were adequate in light of the
fact that the 2011 case was the com-
continued on page 61
pany’s second offense for essentially the same violation of law.

It seems evident that the SEC penalties assessed in 1999 were insufficient. Had Thor learned its lesson from the first incident and acted sooner to implement more effective corporate staff efforts and more rigorous engagement by its audit committee, the fraud at Dutchmen might have been prevented.

Many lessons can be learned from the Thor cases, including:

◆ SEC cease and desist orders alone may not prevent future law violations. Mandatory remediation is necessary.
◆ Thor’s enactment of a code of conduct was insufficient.
◆ Effective operational oversight from senior management and the audit committee is essential when subsidiaries are given entrepreneurial license to be managed independently.
◆ If compensation schemes for financial personnel are tied directly to reported performance, those schemes must be monitored very carefully, if not excluded.
◆ Acquired companies must be integrated into the corporate reporting system and ethical culture.  

Curtis C. Verschoor is the Emeritus Ledger & Quill Research Professor, School of Accountancy and MIS, and an honorary Senior Wicklander Research Fellow in the Institute for Business and Professional Ethics, both at DePaul University, Chicago. His e-mail address is curtisverschoor@sbcglobal.net.