

WHITE-COLLAR CRIME

FIGHTER

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YOUR SECRET WEAPON IN THE WAR ON FRAUD

IN THE NEWS

Bribe At Your Own Risk

The number of bribery investigations initiated by the US Department of Justice (DOJ) more than tripled from nine in 2003 to 29 in 2007. And this year, more than 80 US companies are under investigation for alleged violations of the Foreign Corrupt Practices Act (FCPA).

Key areas in need of improvement: While most companies (84%) have formal FCPA and anti-corruption policies, whistleblower hotlines and anti-corruption training programs, less than 70% distribute these policies in written form to all employees. Moreover, while three-quarters of companies have hotlines in place, just over one-quarter (27%) promote the use of them among vendors, joint venture partners and other third parties whose actions could put the company on the wrong side of anti-bribery laws.

Essential message: All major companies must initiate "frank discussions and quick action...around the necessity of appropriate compliance programs and activities to lower the risk of violating the FCPA and other anti-bribery and anti-corruption laws."

White-Collar Crime Fighter source: KPMG 2008 Anti-bribery and Anti-corruption Survey. For further information and to obtain the full survey, contact KPMG and www.kpmg.com or Richard H. Girgenti, Forensic National Practice Leader at rgirgenti@kpmg.com.

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Judge William Wilkins, Nexsen, Pruet, LLC

Criminal Fallout from The Financial Crisis

How to Protect Your Organization



William W. "Billy" Wilkins, Ronald Reagan's first selection in the nation for a federal judgeship and former Chief Judge of the U.S. Court of Appeals for the Fourth Circuit, subsequently served as the first Chair of the U.S. Sentencing Commission (USSC). The Guidelines crafted by the USSC have had a profound impact on white-collar crime litigation since they went into effect in 1991.

Judge Wilkins recently returned to private practice in Greenville, SC. He maintains an avid interest in the role of fraud in US and international business.

We recently spoke with him about his views on the impact of fraud on the current economic crisis and how companies with potential culpability can minimize their risk of damaging legal consequences...

I'm no economist, but having spent 40-plus years in the legal world of white-collar crime, I am certain that criminal conduct played a significant role in getting our financial and economic systems into their current state of unprecedented crisis.

The problem: We won't understand the real extent to which different types of fraud were instrumental in bringing the financial system to the brink of collapse. However, you can be sure that an explosion of allegations of criminal conduct is inevitable. They will involve (among many others) such

activities as...

- **Fraudulent financial reporting**—to conceal the dramatic deterioration of mortgage-related assets on financial institution balance sheets.

- **Misrepresentation of the value of asset-backed securities** by investment banks, securities brokers and related parties.

- **Deception of prospective investors** as to the safety of many of the arcane derivative securities whose

riskiness no one really understood.

- **Mortgage fraud**—perpetrated by a small army of unscrupulous mortgage brokers, collusive appraisers, attorneys, lenders and home builders.

RISKS FOR ORGANIZATIONS

There is no doubt that much of the criminal action initiated in the wake of the financial crisis will target individuals among the groups mentioned above. How successful plaintiffs will be in suing these people is anyone's guess.

More worrisome: The impending legal assault on banks, investment banks, pension funds, insurance companies, hedge funds and similar institutions for fraud, conspiracy, earnings manipulation and other crimes.

Already, the FBI has initiated high-profile investigations of the insurance giant AIG, as well as Lehman Brothers, Fannie Mae and Freddie Mac. And FBI Director Robert Mueller recently testified before Congress, stating that his agency was already investigating more than 25 cases

You can be sure that an explosion of allegations of criminal conduct is inevitable

of alleged corporate fraud related to the collapse of the mortgage industry.

Separately—and perhaps indicative of the type of criminal action that will be making headlines with increasing frequency in coming years—are the convictions in September of four top AIG executives. Former AIG CEO, Ronald Ferguson, faces life imprisonment for his role in a sham transaction going back to 2000 to fraudulently add \$500 million to the insurer’s loss reserves. The latest FBI probe is a clear indication of a history of fraud-related problems facing AIG which

is now front and center in the financial crisis.

COMING CLEAN

As these latest developments indicate, the depth and breadth of the current crisis—coupled with the intensity of consumer outrage over the “greed factor” on Wall Street that they attribute at least in part to their own financial woes—is already spurring prosecutors to aggressively scrutinize companies believed to have culpability for the financial mess.

Several prosecutors in the New York area have already ramped up their investigations of mortgage fraud and securities law violations and white-collar defense attorneys have expressed concern about a rash of indictments that might not have been handed down if the financial and economic crisis had never occurred.

Prediction: Companies that have committed illegal acts related to the mortgage and credit crisis still have some time to gird themselves against the prosecutorial onslaught that is gathering steam with each passing day. However, it may take a couple of high-profile convictions of companies and/or executives in connection with the current crisis to motivate other guilty companies to take action to mitigate the risk of being targeted by aggressive prosecutors.

Key: Executives of corporations who know that their organizations have or may have committed fraud related to the current “meltdown” should do themselves a favor and immediately initiate their own internal investigations.

Reason: While woefully inadequate investigative and prosecutorial resources at all levels of government provide high odds that a culpable organization will “get away with” financial wrongdoing, if they don’t the consequences could all but ruin the organization as it is subjected to increasingly aggressive investigation and prosecution, and potentially devastating punitive measures.

Essential: Cooperate fully with prosecutors. If an internal investigation reveals substantive evidence of wrongdoing, take prompt corrective measures and self-report the wrongdoing to the appropriate prosecutorial office.

Doing so may result in a decision not to prosecute...or to offer a deferred prosecution, where your organization’s admission of wrongdoing results in a

Where A Fraud Risk Assessment Can Go Wrong

There is practically an unlimited variety of ways to conduct a successful fraud risk assessment (FRA). However, there are critical elements of a FRA that if not well-executed can render the exercise flawed at best and useless at worst. *Examples...*

- **Not having the proper personnel involved in the process.** Most FRAs require the participation of at least the CFO, CIO, general counsel, business unit managers, a senior human resources manager, the accounting manager, chief internal auditor and representatives of the board and the audit committee. (See also page 3.)

- **Limiting the FRA to risk factors**—such as motives, opportunities and incentives to commit fraud—while failing to identify the critical fraud schemes and scenarios that potentially threaten the organization.

- **Failure to identify potential perpetrators.** This usually means insufficient consideration of management override of internal controls.

- **Failure to assess the risk of collusion** between insiders and vendors, customers or other external parties.

- **Failure to obtain management “buy-in.”** Without the unqualified support of the CEO, COO and other top executives, your FRA will not be taken seriously and may prove inadequate as a tool for strengthening the organization’s anti-fraud defenses.

White-Collar Crime Fighter source:

Jim Lombardo, CFE, Director in the Enterprise Risk Services practice, Deloitte & Touche LLP, and Mohammed Ahmed, CPA, Senior Manager, Deloitte Financial Advisory Service LLP’s Forensic & Dispute Services practice. www.deloitte.com.

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Mission Statement

White-Collar Crime Fighter provides information of maximum practical value to organizations and individuals involved in all facets of investigating, detecting and preventing economic crime.

This community includes law internal auditors...fraud examiners...regulatory officials...corporate security professionals...senior executives...private investigators...and many more.

The editors of *White-Collar Crime Fighter* strive to gather and compile the most useful and timely information on economic crime issues.

Comments, suggestions and questions are welcome. Please fax us at 203-431-6054, or E-mail us at editor@wccfighter.com. Visit us on the Internet at www.wccfighter.com.

period of “probation” monitored by the authorities, thereby avoiding the damaging fallout of a criminal conviction.

At worst, many companies that voluntarily disclose their financial misconduct will end up with sentences much lighter than what they would get had they chosen not to cooperate with prosecutors. That’s because the US Sentencing Guidelines recommend significantly lower penalties for organizations that meet some or all of the seven key compliance criteria of the Guidelines...


- Oversight by high-level personnel.
- Due care in delegating substantial discretionary authority for implementing and enforcing a compliance program.
- Effective communication to all levels of employees.

Cooperate fully with prosecutors. If an internal investigation reveals substantive evidence of wrongdoing, take prompt corrective measures and self-report the wrongdoing

Essential: For a compliance program to be recognized as effective, it must include periodic training of all employees at all levels within the organization regarding the responsibility of everyone to act ethically and lawfully at all times. These periodic educational programs must be designed to ensure that all employees understand what is legal and what is not.

- Substantive measures to achieve compliance, which include implementing systems for monitoring, auditing and internally reporting suspected wrongdoing without fear of reprisal.

Key: An anonymous hotline that employees can use to report criminal conduct without fear or reprisal.

- Consistent enforcement of compliance standards including disciplinary action.
- Meaningful steps to respond to and prevent further repeat offenses upon detection of a violation. 

White-Collar Crime Fighter source:

Judge William Wilkins, member and chair of the White-Collar Crime, Appellate Advocacy, and Corporate Compliance/Crisis Management practice groups at Nexsen, Pruet, LLC, a Columbia, SC-based law firm, www.nexsenpruet.com.

ROLES AND RESPONSIBILITIES

Nidhi Gupta, CPA, CFE, CIA, *BDO Consulting*

ELIMINATING THE CONFUSION

Defining the Roles of the Board, Audit Committee and Senior Management in Fraud Prevention



The public outrage and increased enforcement actions by regulatory and legislative bodies resulting from the mega-frauds at Enron, Tyco, Worldcom, HealthSouth and dozens of other multi-billion dollar companies has raised public expectations regarding the responsibilities of the board of directors, audit committee and senior management.

When an organization is in the news due to fraud, among the most frequently heard questions are, “Where was the board of directors?...Where was the audit committee?... where were the honest executives?”

DEFINING ROLES

Key lesson:

Some of these organizations may not have become household names had the roles of the board of directors, audit committee and senior management been clear with regard to identification, monitoring and response to fraud risks.

To reduce the confusion, listed below are a few best practices describing these critically important roles in the four key areas essential to an effective fraud prevention program...

- Tone at the Top
- Fraud Risk Assessment
- Fraud Prevention Controls
- Mechanisms for Reporting and Investigating Fraud

TONE AT THE TOP

The board of directors is responsible for establishing this tone by ensuring that it is in a position to exercise adequate oversight over senior management and the overall organization.

Example: If a majority of the board is comprised of owners, senior executives and/or parties related to these individuals, then the board has no independence and both Tone at the Top and board oversight responsibilities are severely compromised.

Important: As part of its oversight responsibilities, the board also must ensure that management implements policies that promote ethical behavior throughout the organization. To accomplish this, the board must

As part of its oversight responsibilities, the board must ensure that management promotes ethical behavior throughout the organization

review, help fine-tune and approve the corporate vision and mission statements, the company’s code of ethics and the communication process used to distribute this message throughout the organization as well as to vendors, customers and shareholders.

Example: Enron’s 65-page code of conduct was thorough and well-written but was by no stretch of the imagination an integral part of the organization’s culture. Had the Board been doing its job, it would have detected not only management’s lack of a company-wide communication system for ethics, but also management’s own egregious disregard for the code itself.

FRAUD RISK ASSESSMENT

The board also has responsibility to ensure that management designs effective fraud risk management procedures. Often, the board delegates this oversight responsibility to the audit committee.

Important: The board should detail these responsibilities in the audit committee’s charter as well as its own.

To ensure that appropriate steps are taken to identify and prioritize

Continued on pg. 4