



Global
Business Leadership

SHAKING THE GLOBE NEWSLETTER

Courageous
Decision-making in
a Changing World



Be Alert to Fraud

Volume 4, issue 6

Usually a day does not pass without a story about fraud in The New York Times. Many of the conditions that **prevent** fraud are the same conditions that make good business sense. So the first lesson in staying alert to bad practices is: **trust, but verify**. In any business, trust creates the environment necessary for people to ask questions and is a major indicator of effective leadership. Linda A. Hill and Kent Lineback writing in *Harvard Business Review* say, "trust has two components: belief in your competence and belief in your character."

*To be trusted is a greater compliment
than being loved.*

— George MacDonald

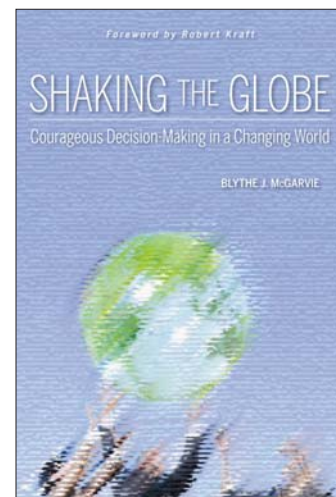
Yet, trust can also create complacency. Too often people become distracted from recognizing indicia of untrustworthiness. There are many lessons from the 2002 film, *Catch me if you Can*, in which an FBI agent tracked down and caught a young con artist who successfully impersonated an airline pilot, doctor, assistant attorney general and history professor, cashing more than \$2.5 million in fraudulent checks in 26 countries. (In today's terms, adjusting at the CPI rate, that is \$15 million.) In one scene, the father Frank Abagnale Sr. asks his son, "You know why the Yankees always win, Frank?" Frank Jr. says, "'Cause they have Mickey Mantle?" His father answers, "No, it's 'cause the other teams can't stop staring at those damn pinstripes." We must not allow ourselves to be distracted or looking solely at the surface. So, the second lesson is: think about **what is driving the success or weakness of an internal control or procedure**.

Let's survey the resurgence of corporate fraud. Highlights from Kroll's 2010/2011 **Global Fraud Report** published in CFO magazine (March 2011) provide insights.

1. Business losses due to fraud increased 20% in 2010, from \$1.4 million to \$1.7 million per billion dollars of sales. These frauds were discovered in 2010, but most were going on for several years. With tighter economic conditions and more failed businesses, many of these frauds are now revealed.
2. The **most likely targets**, by industry, are financial services, media, technology, manufacturing and health care. These industries in 2009 represent 35% of the US GDP and respectively, 8.3%, 3.9%, 4.2%, 11.2% and 7.5% of the GDP.
3. Various forms of embezzlement, outright theft and the growing risk of information theft constitute traditional forms of fraud. Recently, two new versions of corporate malfeasance have arisen: fraud in the business model and fraud in the business process.



Sopranos Nicole Cabell and Renée Fleming display their talents with the **Lyric Opera** Board.



Blythe McGarvie's **Shaking the Globe**, with a foreword by Robert Kraft, was published by John Wiley & Sons in February 2009.



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1-757-345-3595
bmccgarvie@LIFgroup.com

Fraud in the business model is defined by selling illegal or worthless wares. For example, this happens in the pharmaceutical industry with drugs not FDA approved. In the media industry, bootlegged films or illegal copies of music, programming and other content constitute fraud in the business model. Fraud in the business process ranges from ignoring environmental or safety laws to “window dressing” results at quarter-end.

***Rather fail with honor
than succeed by fraud.***

— Sophocles

What can we do to create the conditions that discourage bad practices? Here are three ideas:

1. **Start at the top.** Boards and top management set the tone and establish the culture. In addition, listen when someone is trying to tell you something. It’s important to perceive the entire communication, paying attention to verbal and body language. Do not let your own concerns and priorities blind you to what is being communicated. Again, from Catch me if you Can, Frank Abagnale Jr. reveals the truth to his fiancée Brenda.

Frank says: Brenda, I don’t want to lie to you anymore. All right? I’m not a doctor. I never went to medical school. I’m not a lawyer, or a Harvard graduate, or a Lutheran. Brenda, I ran away from home a year and a half ago when I was 16. Brenda Strong says: Frank? Frank? You’re not a Lutheran?

2. **Educate others about what constitutes fraud.** Most fraud is uncovered by whistle-blowers or by accident. No one should wonder if what he or she does or is observing is wrong. Find out what happens in other industries. If you think that what you are doing doesn’t seem right, it probably is not.
3. **Surprise audits work.** Fewer than 30% of victim organizations in a 2010 survey by the Association of Certified Fraud Examiners (ACFE) had surprise audits. 22% of the 1662 cases resulted from perpetrators in Accounting, 18% in Operations, followed by Sales and Executive Management each with 14% of the cases. When I was a CFO, internal audit would periodically put through duplicate invoices to see who would catch it and then recognize the person who did. If the invoice was not caught, a review of procedures was in order for the team. The person who failed to catch the duplication could only hope to be rotated into a different job.



Winemaker Stephanie Gallo and McGarvie participate with KIN in Napa Valley.

So, watch out for the “Catch me if you Can” types. And at the same time, build trust. • • •

Global Perspective: Items of Note



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FTI Journal interviews Blythe McGarvie in an article on “Pressure Points,” in which corporate directors discuss the best ways to respond and a board’s proper role in helping companies compete and prosper ([PDF](#)).

LIF Affiliate [Laura Martin](#) publishes her latest report on the [Pricing Strategies in a Digital World](#) on her [Capital Knowledge](#) website.

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The *Shaking the Globe* Newsletter is written for decision-makers who recognize the critical importance of the interconnected world for financial stability and growth. Blythe speaks internationally about how to strengthen the global community.

(URLs: www.BlytheMcGarvie.com and www.LIFgroup.com)