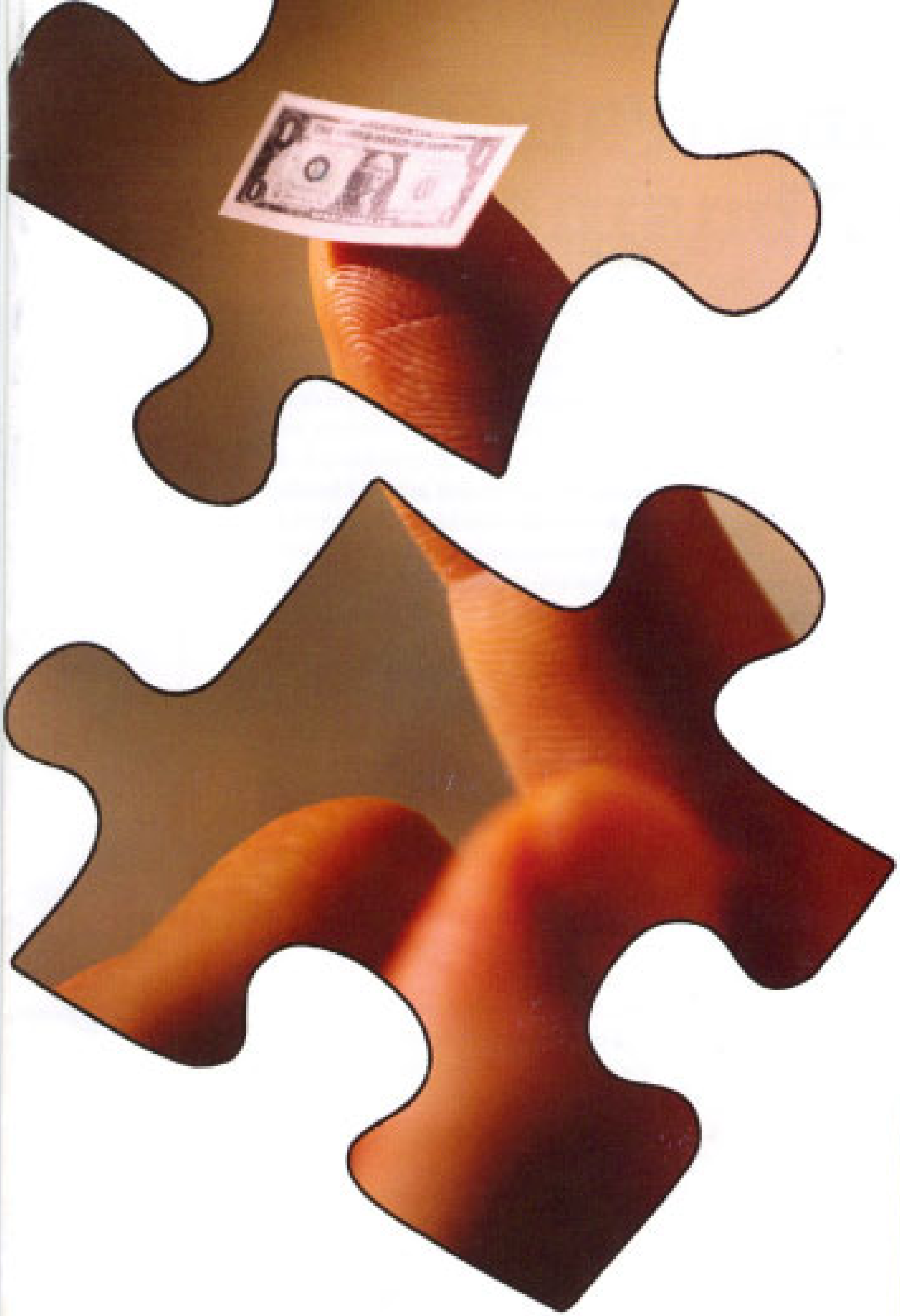

fraud alert

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How to spot insurance fraud against businesses

Insurance fraud is a crime that happens every day in every state. It costs the industry and, in turn, policyholders, a lot of money — at least $80 billion a year, according to the Coalition Against Insurance Fraud.

Unscrupulous individuals sometimes target businesses and their insurance companies as "deep pockets" of wealth. The two largest categories of insurance fraud against businesses are workers' compensation fraud, in which an employee fraudulently alleges an injury on the job, and property-casualty fraud, in which a claimant alleges personal or property damage resulting from an action by the business.

Costly problem

Workers' compensation fraud costs $5 billion each year and property-casualty fraud costs $20 billion, according to estimates by the National Insurance Crime Bureau.

Spotting inflated or fraudulent claims takes vigilance on the part of insurers, claims adjusters and insured companies. Fraud experts have identified red flags that indicate which claims deserve special scrutiny for the possibility of insurance fraud.

Workers' compensation fraud

Workers' compensation fraud can take several forms. Employees may falsify claims, use unnecessary medical services, miss work after an injury has healed or report an off-hours injury as an on-the-job accident.

Although none of the circumstances described below is conclusive in itself without further investigation, prudent employers should be on the lookout for the following common signs of workers' compensation fraud:

An employee reports an on-the-job injury Monday morning, with no witnesses. Workers who get hurt over the weekend pursuing leisure activities sometimes try to turn their injuries into cash by faking an accident at work.

An employee reports an injury just before a seasonal layoff or other work stoppage. A worker who claims an injury just before a strike, layoff or regular shutdown may be looking for a way to collect income during the closing.

A new employee reports an injury. Workers' compensation abusers sometimes have little intention of doing any actual work. Their goal is to get hired and report an injury after very little time on the job.

An employee on recuperative leave is hard to reach. The employee may be "double dipping" — working another job while collecting benefits for an injury that supposedly makes work impossible.

Accounts of the accident differ. The worker may describe the accident differently to the employer than to doctors. Sometimes, accounts by accident witnesses differ from the injured worker's account.

Irregularities mark medical treatment. The injured employee may refuse a diagnostic procedure to confirm an injury or change medical providers frequently.

Property-casualty scams

In property-casualty insurance fraud schemes, telltale behavior or circumstances may alert businesses that they are being set up. Sometimes the clue lies in the details of the incident underlying the claim and sometimes hints come in the way the report is filed. Red flags include:

Witnesses to a reported accident are unavailable. In variations of this situation, an overly enthusiastic witness or a witness related to the claimant comes forward. Details in the account may suggest that the claimant created the so-called hazard that caused the alleged accident.

The claimant pushes for a quick settlement or accepts a reduced settlement. Sometimes, the claimant threatens the insured with adverse publicity if the claim is not settled quickly.

The claimant is difficult to reach or has a suspicious address. The claimant may use a post office box, an answering service or an unconventional business address to receive communications. Related behavior that may provide a tip-off includes frequent changes in home address and telephone number, a preference for handling business in person, or reluctance to use the U.S. mail.

The claimant can't or won't produce solid identification. Further investigation may show that the claimant has an active claims history under various aliases.

A food poisoning claimant is the only person to become ill. Another suspicious circumstance in claims of illness after eating is the failure to produce any foreign or contaminated substance as supporting evidence.

A food product liability claimant can't produce evidence showing contamination. Typically, the only evidence offered is the package wrapper, can or box.

Soft or hard, insurance fraud costs everyone

Insurance fraud can be "hard" or "soft." The two approaches may differ in technique and sophistication, but either way, insurance fraud means higher premiums for everyone.

Hard fraud is deliberately faking an accident, injury, theft, arson or other loss to collect money illegally from insurance companies. Hard fraudsters often act alone, but activities involving organized crime rings are increasing. In these schemes, criminals conspire to carry out concerted efforts to defraud insurance companies.

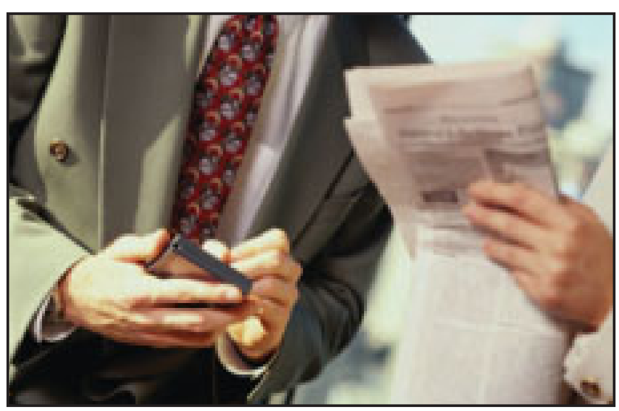
Soft fraud is the attempt by usually honest people to deceive their insurance companies with "little white lies." The perpetrators like to think of their deceit as harmless fudging. On the contrary, soft fraud is a crime — one that costs everyone.

Best defense

Many insurance claims are legitimate, but fraudulent claims built on false or inflated accounts of injury cause significant harm to businesses and consumers. Staying alert to the signs of potential insurance fraud is the best defense against this form of fraud.

Investigating fraud in a limited partnership

Suspicions frequently arise of mismanagement, self-dealing or fraud by the general partners or sponsors of a limited partnership. In a limited partnership, one or more general partners (GPs) manage the business while limited partners (LPs) contribute capital and share in the profits.



No control

LPs do not participate in running or managing the business, and if they do participate in making management decisions they lose their limited partnership status. They nominally have the power to vote to remove the GP, but the partnership structure usually makes removal virtually impossible — unless the GP in question has committed fraud.

Since LPs have no control over the partnership, they should make sure going into the agreement to have considerable knowledge about the GP's reputation and record and the type of business being considered.

Potential losses for LPs are limited to their capital contributions. The GP alone is subject to claims, debts in bankruptcy and lawsuits.

But LPs and those considering such an investment should be aware of a less-recognized form of investor fraud: limited partnership abuse. Many limited partnerships perform very poorly and GPs give various explanations for this poor performance, never blaming themselves.

Self-enrichment

Since LPs do not participate in day-to-day business operations and no board of directors reviews management decisions, the GP has almost complete control of the partnership. With their superior operational knowledge and exclusive day-to-day control, GPs could enrich themselves at the expense of the business.

One example of this kind of abuse is self-dealing — payment of exorbitant fees and benefits to the GP at the direction of the GP. For instance, instead of simply drawing one fee for managing the company, the GP may purport to provide additional services to the limited partnership and be paid separately for these services.

Other examples of fraud may be difficult to detect. For example, a GP may control or own another company that provides goods or services to the limited partnership at inflated or unconscionable rates.

In a deal like this, the GP is working both sides, acting for both the company providing the services and the company paying for them. This puts him or her in a position to approve contracts that charge the partnership exorbitant fees.

Advance investigation

Investors considering a limited partnership should determine in advance whether the GP provides goods or services to the partnership, either directly or indirectly. If so, they should find out how much the limited partnership is paying for those goods or services, and be sure the transactions are at arm's length and in line with market rates.

LPs who want to follow up on suspicions of GP mismanagement often call on forensic accountants to analyze financial records and determine the facts surrounding suspicious activities.

Cases in point

Here are two cases that illustrate the kinds of mismanagement, self-dealing and fraud possible:

Marriott. Thousands of limited partnership investors throughout the United States and abroad brought a case against Host Marriott, Marriott International and their affiliates, on the formation and operation of six partnerships.

Marriott, acting as GP in the partnerships, raised money from investors with the promise that they would share in the success of a group of hotels. But Marriott used investors' funds as a financing technique, taking essentially all the income and leaving investors nothing.

Marriott was charged with knowingly burdening the partnership with excessive fees and debts. The case was settled for $434 million.

Chaparral Investments. The Commodity Futures Trading Commission filed charges against Max E. Walters of Kansas City, Mo., alleging that Walters, GP in Chaparral Investments, LP, defrauded the limited partnership of more than $1 million in connection with commodity futures and option trading.

The complaint alleged that Walters failed to disclose commissions paid him on partnership trades and that partnership funds were misappropriated for Walters' personal expenses. An administrative law judge imposed a civil money penalty of $2.4 million and restitution of more than $1.64 million.

Never too late

These cases show that it is never too late for LPs to investigate the GPs when they suspect mismanagement, self-dealing or fraud. The services of a forensic accountant can determine the facts in the case.

Fraud investigation reports: A science unto themselves

Uncovering and documenting facts in a fraud case is just the precursor to what may prove to be the most important part of an investigation: writing a report that will stand up in court.

Unlike an audit report, a fraud investigation report is not written for shareholders or boards of directors. It is for attorneys, juries, witnesses and the media — a skeptical audience that will be looking for holes, inaccuracies and inconsistencies.

Writing a fraud report that can withstand this scrutiny can be tough, but not nearly so tough as watching a case disintegrate in a courtroom attack.

Fraud examiners know that judges and juries are neither understanding nor forgiving when the report includes errors and omissions. Misspellings, imprecise dates, improperly recorded numbers and other signs of carelessness can taint a report — with no second chances to correct mistakes.

Precision counts

Findings must be documented throughout the investigation. The examiner should write a dated memorandum of every interview — as soon as possible after the interview. Prompt attention to this task not only meets evidence standards but also protects against later assertions that memories of the interview had become faulty by the time the report was written.

Interview memorandums should include the identities of the investigator and witness, the time and location of the interview, and any other relevant details. The memo also should note whether the interview was tape-recorded and should state the time that elapsed between conducting the interview and drafting the memo.

The investigator should prepare a separate memo for each interview. Combining reports of several interviews into one narrative may seem like a good way to save time, but the convenience comes at a risk. With a combined document, an opposing attorney asking to see one interview can gain access to all interviews.

Any evidence collected during the interview should accompany the memo. Examples include documentation of phone calls, notes or letters, computer disks or CDs, and date books.

Investigators' opinions do not belong in interview memos or final fraud reports. These documents are intended to detail facts. They should be impartial accounts, including only information relevant to the case at hand.

Presentation matters

Effective, clear presentation is an important part of a good fraud report. A summary of basic issues covered in the report should appear at the beginning. Then, presenting a list of witnesses and exhibits in chronological order makes it easier to understand the sequence and significance of events.

Another helpful organizational device for any report 10 pages or longer is an index listing evidence collected during the investigation, names of everyone involved and visual aids that help clarify the fraud.

Savvy investigators avoid a question-and-answer format. This approach enables defense attorneys to inquire why one question was asked but another was not, or why a question was phrased in a certain way. Diversions like this can sidetrack a jury, drawing attention to how the investigation was conducted rather than the facts of the case.

Finally, fraud investigation reports should be understandable. Language should be neither too casual nor overly formal, and facts and ideas should be clearly stated. Charts and diagrams can help clarify complex information or provide a guide to a circuitous money trail.

Quality pays off

In the end, a fraud examiner's report is as critical to the eventual conviction and punishment of perpetrators as is the investigation that identifies them. A well-structured, complete and accurate report can do much to enhance a case. A substandard report can provide the defense with a similar advantage.

When stockbroker misconduct needs a specialist's attention

When stockbrokers misbehave, tracking their shenanigans can be challenging — whether their wrongdoing results from simple negligence or outright fraud. But with skilled investigation by accountants trained to uncover misconduct, investors have a better chance of recovering losses suffered at the hands of unscrupulous brokers.

Common ploys

The most common forms of stockbroker misconduct are:

Misrepresentation. Brokers are forbidden to say they believe a stock is a good buy if they know it to be bad. Yet it happens all the time — and it's fraud all the time. Brokers are also forbidden to imply they have inside knowledge about a company. And they can't recommend stock of an issuer that pays the broker or brokerage firm without disclosing those payments.

Churning. When brokers buy and sell excessively to generate commissions for themselves, investors do not benefit. Many of these transactions may be completed at virtually the same price with no loss or gain for the investor.

Unsuitable trading. Brokers have a duty to advise investors to purchase securities appropriate to the investors' objectives and risk tolerance. Brokers may not, for example, recommend heavy investment in speculative stocks to senior citizens primarily interested in preserving principal and receiving income. Even if a misguided investor wants to speculate, brokers may not recommend investment strategies inconsistent with the investor's financial profile.

Unauthorized trading. To prevent unauthorized trades made to generate commissions, brokers must obtain permission from an investor before a trade, unless the investor has provided advance written discretionary authorization.

Manipulation. Brokers may not use investors' money to influence the market price of a security.

Excessive markups. Broker markups for securities sales or discounts for securities purchases may not exceed fair market standards.

Victims of any of these practices can seek compensation through arbitration forums of the National Association of Securities Dealers (NASD) or the New York Stock Exchange (NYSE).

First step

Attorneys representing investors in these proceedings often turn to forensic accountants to supply specialized accounting, auditing and investigative skills. As a first step, forensic accountants usually conduct preliminary investigations to determine the objectives and procedures and establish an action plan.

Once the action plan is determined, the accountant obtains necessary evidence for analysis. Details depend on the nature of the dispute, but forensic accountants typically calculate economic damages, trace assets, determine present values with appropriate discount rates and analyze the impact of changing key values.

Brokerage liability

When investigations reveal broker misconduct, the brokerage house employing the broker may also be liable. Under the rules of both NASD and NYSE, a brokerage house is required to supervise its brokers to be sure they don't break the rules of professional conduct.

If the firm has not established or enforced a proper system of supervision and internal control, it may be liable to the same extent as the broker.

No guarantees

Brokers can't — and are, in fact, forbidden to — guarantee clients' investments. But a broker's license is not a license to lie, cheat and steal.

Chances to recover losses inflicted on investors by unscrupulous brokers improve markedly with the specialized skills of accountants trained to uncover and analyze misconduct.

Fraud to watch for:

Phoenix companies may turn to ashes

Strategic bankruptcy, or strategic liquidation, can be a valid business tool when properly structured and pursued. Unfortunately, it also offers an avenue for less-than-honest businesspeople to profit at the expense of their creditors.

Take the case of phoenix companies that rise from the ashes of failed companies, trading on the goodwill of the original firms and perhaps adopting similar names. Sometimes, these new companies abuse the second chance.

Deliberate mismanagement

In these situations, company directors purposely run a business into the ground to buy the assets from liquidators at knockdown prices. They then go right back into the same line of business. In other cases, directors who mismanaged a business into bankruptcy form a phoenix company and use the same inept procedures to ruin that firm as well.

Phoenix companies often are undercapitalized to begin with and leave a trail of unpaid debts to mark the end of their short life spans. In worst cases, creditors of the phoenix operators do business with the new company under the mistaken impression that they are dealing with the original company because of its similar name.

At the same time, creditors of the original company also remain unpaid even as they watch the phoenix company continue in business.

Legitimate asset sales

It is legal for an insolvent company to sell its assets to another party at market value. It is also legal to sell a business to existing management. Specialists are needed to structure legitimate phoenix companies, and specialists are required to unravel those that aren't legitimate.

The difficulty is in determining whether the decision to sell assets is made in good faith or in an effort to avoid liability. Forensic accountants make such distinctions, looking beyond the numbers to assess the business realities of situations. They examine evidence in light of assertions of fact and established standards to prepare reports and analyses designed to withstand courtroom scrutiny.

Don't Let Fraud Ruin Your Business

Occupational fraud and abuse costs American businesses an estimated $600 billion annually — roughly $4,500 per employee. Small businesses are the most vulnerable to these crimes. But you don't just have to stand there and be victimized by them.

Let Rogers, Lynch & Associates LLC assist you in combating fraud and abuse. We offer a wide range of forensic accounting, and fraud-related services, including:

- Litigation Consulting and Support
- Expert (Witness) Services
- Fraud Detection and Deterrence
- Insurance Claim Analysis: Loss Profits, Business Interruption, Surety Bond Claims, Fidelity Bond Claims
- Divorce/Community property Partition
- Evaluation of Internal Control Systems
- Financial Statement Analysis and Interpretation
- Bankruptcy and Reorganization
- Asset Recovery
- Track and Locate Assets Misappropriated

Since our firm's founding in 1989, we have been committed to providing our clients professional service of the highest quality. Our clientele includes family and closely held businesses, public corporations, and commercial lenders throughout the United States.

We would welcome the opportunity to help you prevent, detect, or prosecute fraud. Please call us at 504-282-1441 or visit our Web site: www.rlastars.com, and let us know how we can be of assistance.

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Managing member has over 30 years experience in fraud detection and deterrence and has testified as an expert witness in US Bankruptcy Court.

Penny Rogers, CFE, DABFA, CrFA
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