



THE INSTITUTE OF INTERNAL AUDITORS
**INTERNATIONAL
CONFERENCE**
DUBAI, UAE / 6-9 MAY 2018



Ethics and the Mindset of the Fraudster

8 May 2018

Allan Bachman, CFE
Former Education Manager [retired]
Association of Certified Fraud Examiners
Anti-Fraud Consulting and Training

Agenda

- **Fraud, an Example of What Personal Behavior?**
- **Ethics Fundamentals 101**
- **Us (Personal) versus Them (Organizational)**
- **Guidelines for Professionals (CPA, CIA, CFE)**
- **Tackling Ethical Dilemmas and Lapses**
- **Understanding Fraudster Models**
- **Fraudster Stories**
- **Closing & Questions**

Agenda

- **Fraud, an Example of What Personal Behavior?**

**What word
can we substitute
for “addiction”
in this video?**

Agenda

- Fraud, an Example of What Personal Behavior?
- **Ethics Fundamentals 101**



Why Do We Need Ethics?

- To maintain personal integrity and credibility.
- To make the right decisions and prevent further harm when confronted with ethical problems.

Ethical Values



Two categories:

- Personal ethics
- Organizational ethics

Personal Ethics

- *Personal ethics* include an individual's **basic notion of right and wrong**.
- Shaped from many sources, such as upbringing, religion, personal experience, and other cultural factors.
 - We are not born liars and deceivers.
 - Learned behaviors.
- Always evolving?

Your children
will become
who you are;
so be
who you
want them to be.

Dear Wife what
did you get Lily

for a surprise ~~at~~
again. I forgot. aiga
Please Reply here _____

Love : Don



THE INSTITUTE OF INTERNAL AUDITORS

**INTERNATIONAL
CONFERENCE**

DUBAI, UAE / 6-9 MAY 2018



Personal Ethics

- This category prompts the most disagreement, as each individual can have their own ethical perspective.
 - These evolve and are carried throughout our lives.
 - Influences vary resulting in individual perspectives.
- Clashes in ethical values often result because of a difference in personal ethics with organizational ethics.

Organizational Ethics



- *Organizational ethics* are those **defined by an organization**, such as a corporation, agency, or association.
- Established to promote consistent integrity in the members of the organization.

Organizational Ethics



- When a person agrees to become an employee at a company or joins an association with a code of ethics, there is typically a commitment to follow the established ethical policies.

Agenda

- Fraud, an Example of What Personal Behavior?
- Ethics Fundamentals 101
- **Us (Personal) versus Them (Organizational)**

Personal Ethics vs. Organizational Ethics

- Understanding the distinction between personal and organizational ethics is important.
- There might come a time when an individual's personal ethical values clash so much with an organization's values that it is best to end his/her association with it

Personal Ethics vs. Organizational Ethics

- However, the reality is that the individual may not be able to simply quit when faced with an “unethical” choice.

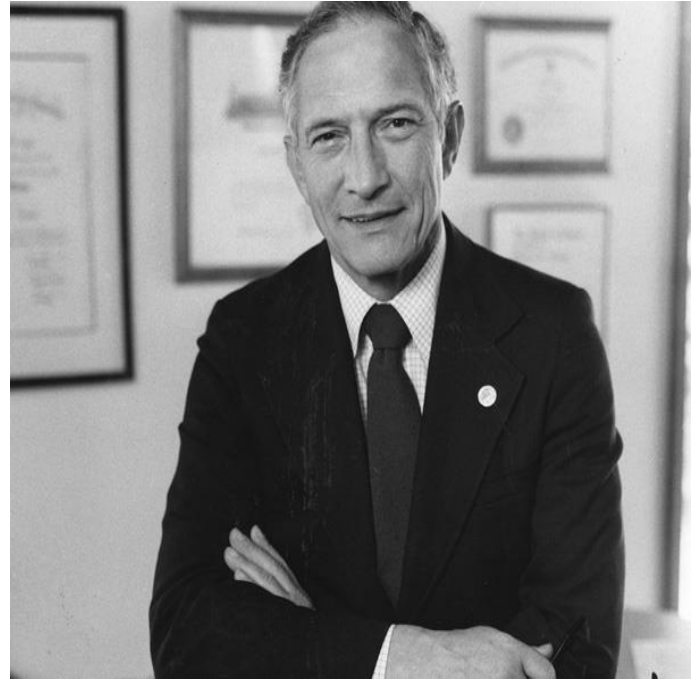
Why Employees Don't Report Unethical Conduct

- No (real or perceived) corrective action by management
- No confidentiality of reports
- Potential for retaliation
 - By superiors
 - By coworkers
- Unsure of who to contact

Words of Wisdom

***“If ethics are poor at the top,
that behavior
is copied down
through the organization.”***

*Robert Noyce
Co-founder
Intel Corporation*



Corporate Culture and Ethics

Important Steps to Take



- Set an ethical tone at the top
- Establish a code of ethics
- Carefully screen job applicants
- Assign proper authority and responsibility
- Mandate fraud and ethics training for staff
- Implement effective disciplinary measures



Important Steps to Take

- Implement a confidential hotline
- Establish a whistleblower policy
- Follow through with reports of misconduct and promote effective internal controls
- Prevent reprisals
- Create a culture of doing the right thing

Corporate Codes of Conduct

**“culture
always
trumped the
code”**

Legal Considerations

- Ethics has a large role in shaping the law, and what is lawful also *partly defines* what is ethical.
- Occasionally, a seemingly ethical choice conflicts with legal standards.
- However, for most ethical dilemmas, *laws establish the minimum standard* for how you should conduct yourself.

Agenda

- Fraud, an Example of What Personal Behavior?
- Ethics Fundamentals 101
- Us (Personal) versus Them (Organizational)
- **Guidelines for Professionals (CPA, CIA, CFE)**

AICPA Ethics Codification

Preface

0.100.000 **Overview of the Code of Professional Conduct**

0.200.000 **Structure and Application of the AICPA Code**

0.300.000 **Principles of Professional Conduct**

0.400.000 **Definitions**

0.500.000 **Nonauthoritative Guidance**

0.600.000 **New, Revised, and Pending Interpretations and Other
Guidance**

0.700.000 **Deleted Interpretations and Other Guidance**

Part 1

Part 1

Members In Public Practice - Topics

1.000 INTRODUCTION

1.100 INTEGRITY AND OBJECTIVITY

1.200 INDEPENDENCE

1.300 GENERAL STANDARDS

1.310 COMPLIANCE WITH STANDARDS

1.320 ACCOUNTING PRINCIPLES

1.400 ACTS DISCREDITABLE

1.500 FEES AND OTHER TYPES OF REMUNERATION

1.510 CONTINGENT FEES

1.520 COMMISSIONS AND REFERRAL FEES

1.600 ADVERTISING AND OTHER FORMS OF SOLICITATION

1.700 CONFIDENTIAL INFORMATION

1.800 FORM OF ORGANIZATION AND NAME

Independence Sub-Topics

1.210 Conceptual Framework Approach

1.220 Accounting Firms

1.224 Affiliates, including Governmental Units

1.226 Reissued Reports

1.228 Engagement Contractual Terms

1.230 Fees

1.240 Financial Interests

1.245 Trusts and Estates

1.250 Participation in Employee Benefit Plans

1.255 Depository, Brokerage and Other Accounts

1.257 Insurance Products

1.260 Loans, Leases, and Guarantees

1.265 Business Relationships

1.270 Family Relationships with Attest Clients

1.275 Current Employment or Association with an Attest Client

1.277 Former Employment or Association with Attest Client

1.279 Considering or Subsequent Employment or Association with Attest Client

1.280 Memberships

1.285 Gifts and Entertainment

1.290 Actual or Threatened Litigation

1.295 Non-attest Services

1.297 Independence Standards for Engagements Performed in Accordance with SSAEs

Financial Interest

- 1.240.010 – Overview of Financial Interests
- 1.240.020 – Unsolicited Financial Interests
- 1.240.030 – Mutual Funds
- 1.240.040 – Retirement, Savings, Compensation, or Similar Plans
- 1.240.050 – Partnerships
- 1.240.060 – Limited Liability Companies
- 1.240.070 - Section 529 Plans

IIA Code of Ethics — Principles

- **Integrity:** The integrity of internal auditors establishes trust and thus provides the basis for reliance on their judgment.
- **Objectivity:** in gathering, evaluating, and communicating information about the activity or process being examined; make a balanced assessment the relevant circumstances and are not unduly influenced by their own interests or by others in forming judgments.

IIA Code of Ethics — Principles

- **Confidentiality:** Internal auditors respect the value and ownership of information they receive and do not disclose information without appropriate authority unless there is a legal or professional obligation to do so.
- **Competency:** Internal auditors apply the knowledge, skills, and experience needed in the performance of internal audit services.

ACFE Code of Professional Ethics

Basic principles of ethical CFE behavior to guide members in fulfilling their duties:

Article 1: Commitment to Professionalism & Diligence

Article 2: Legal & Ethical Conduct & Conflict of Interest

Article 3: Integrity and Competence

Article 4: Court Orders and Testimony

Article 5: Reasonable Evidential Basis for Opinions

Article 6: Confidential Information

Article 7: Complete Reporting of Material Matters

Article 8: Professional Development

ACFE Code of Professional Ethics

- Article 1: Demonstrate a commitment to professionalism and diligence in the performance of his or her duties.
- Article 2: Shall not engage in any illegal or unethical conduct, or any activity which would constitute a conflict of interest.

ACFE Code of Professional Ethics

- Article 3: Exhibit the highest level of integrity in the performance of all professional assignments and accept only assignments for which there is reasonable expectation that the assignment will be completed with professional competence.
- Article 4: Comply with lawful orders of the courts and will testify to matters truthfully and without bias or prejudice.

ACFE Code of Professional Ethics

- Article 5: Will obtain evidence or other documentation to establish a reasonable basis for any opinion rendered. No opinion shall be expressed regarding the guilt or innocence of any person or party.
- Article 6: Shall not reveal any confidential information obtained during a professional engagement without proper authorization.

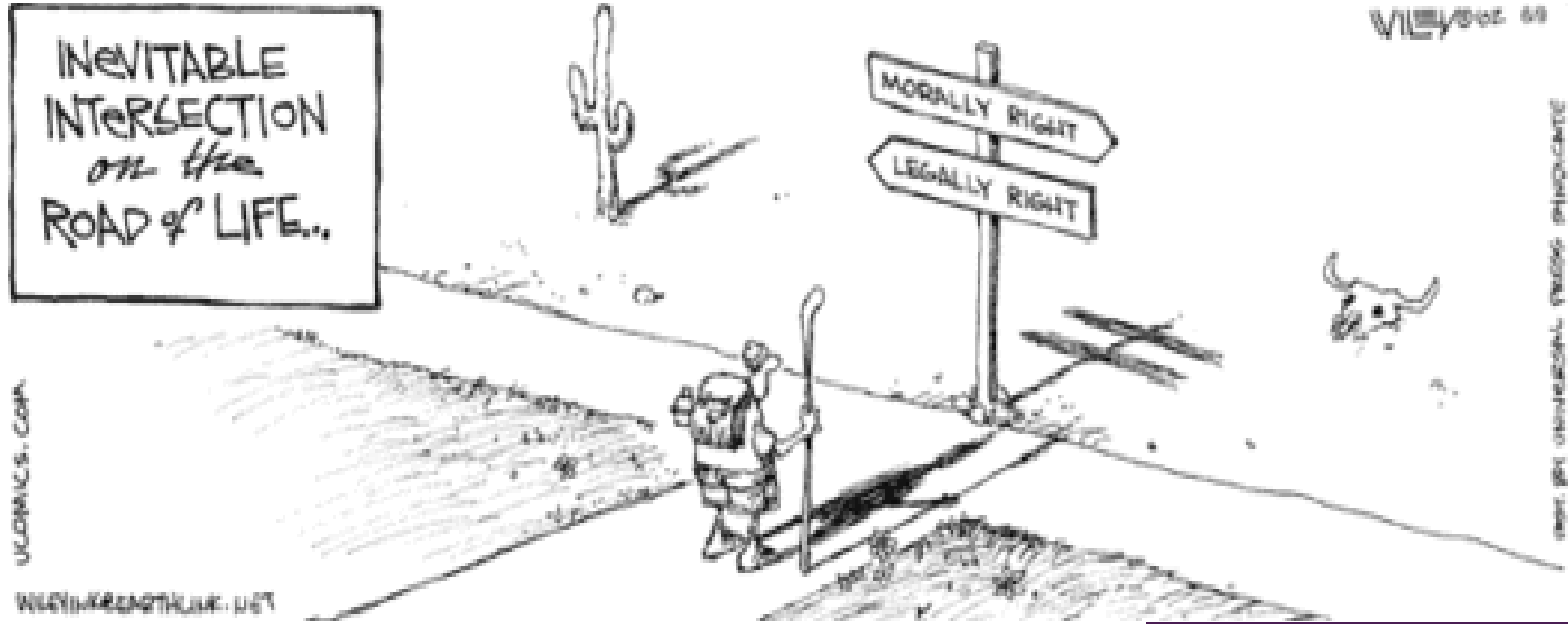
ACFE Code of Professional Ethics

- Article 7: Reveal all material matters discovered during the course of an examination which, if omitted, could cause a distortion of the facts.
- Article 8: Continually strive to increase the competence and effectiveness of professional services performed under his or her direction.

Agenda

- Fraud, an Example of What Personal Behavior?
- Ethics Fundamentals 101
- Us (Personal) versus Them (Organizational)
- Guidelines for Professionals (CPA, CIA, CFE)
- **Tackling Ethical Dilemmas and Lapses**

Choices When There is no Choice



What Is An Ethical Problem?

“An ethical problem is a situation involving conflict about an ethical choice that needs to be resolved.

Ethical problems challenge or threaten individuals’ moral duties and values.”

– ACFE.com



Ethical Dilemma Defined

- An *ethical dilemma* is a complex situation with no predetermined answer that involves a conflict between ethical values.
- Difficulty arises not from ignorance about what is obviously right or wrong, but rather from being forced to choose from a flawed set of options.
 - Choosing the “best of the worst.”



9 Types of Ethical Lapses

1. Conflict of Interest
2. Discreditable acts
3. Professional incompetence
4. Professional misconduct
5. Misrepresentation of self
6. Poor governance
7. Unethical billing
8. Unethical use of another's information
9. Violating rules of other organizations

Conflict of Interest

Use of Data

Sources of Ethical Lapses

- Opportunity + Judgment Influenced by:
 - Greed
 - Ignorance
 - Ambition
 - Financial Pressures
 - External Pressure
 - Selectivity



Getting the Facts Straight

- When dealing with a potential ethical dilemma, the first thing you should do is get your facts straight.
- The more reliable information you have, the more accurately you can determine whether an ethical dilemma does in fact exist.

Analysis

- Look at any applicable ethical codes
- What does the law say?
- Seek advice or counsel



Resolution

- There is no approach that will provide you with an automatic solution to your ethical dilemma.
- Resources can guide you as you deliberate on the issue for yourself, exploring important considerations, and finally coming to your own resolution.

Resolution

- The right thing is not necessarily the easy thing. You might experience pressure from various sources to act in an unethical manner.
- This is where your strength of character will present itself.
- Do you have what it takes to behave in an ethical manner despite the potential negative repercussions of doing so?

Additional Resources for Ethical Guidance

In dealing with ethical issues, you might also find the following resources to be helpful:

- The law
- Attorneys
- State boards or commissions
- Codes of ethics
- Professional trade organizations
- Industry trade organizations
- Wisdom from cultural or religious traditions

In Summation

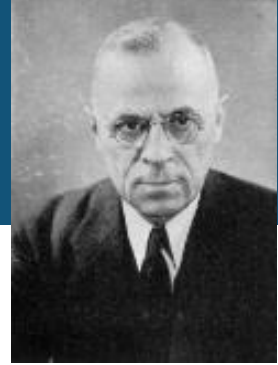
- Making good ethical decisions in your professional engagements requires that you:
 - understand ethical values,
 - exhibit sensitivity to ethical issues, and
 - display a strong ability to see a situation from various perspectives.
- Ultimately, it will be your willingness and desire to do the right thing that drives you to make good ethical choices in all of your professional engagements.

Client Ethical Violations

Agenda

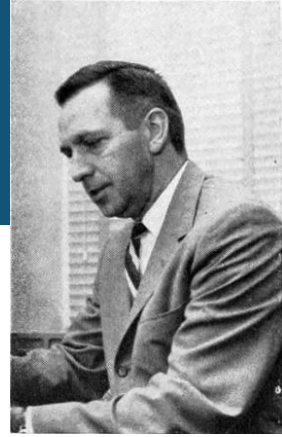
- Fraud, an Example of What Personal Behavior?
- Ethics Fundamentals 101
- Us (Personal) versus Them (Organizational)
- Guidelines for Professionals (CPA, CIA, CFE)
- Tackling Ethical Dilemmas and Lapses
- **Understanding Fraudster Models**

Edwin H. Sutherland, 1939



- Crime is ***learned*** from intimate personal groups.
- These groups teach "definitions" (including the skills, motivations, attitudes, and rationalizations) either favorable or unfavorable to the violation of the law.
- Criminal behavior results when one is exposed to an ***excess of definitions favorable to the violation of the law over unfavorable definitions.***

Donald R. Cressey, 1953



- A criminologist who studied embezzlers
- Why people become “trust violators”
- Developed the Fraud Triangle
- Cressey’s three learning principles

Dr. Donald Cressey

Richard C. Hollinger, 1983



Surveyed 10,000 workers:

- 1/3 had committed some form of fraud.
- Many stole because of job dissatisfaction.
- Employee perception of detection is important.
- Employee-thieves exhibit other deviances
 - Sloppy work, sick leave abuses, etc.
- Increased security & controls may slow, but not deter acts.

Gottfredson & Hirschi's General Theory of Crime, 1990

Michael R. Gottfredson and
Travis Hirschi

A GENERAL
THEORY OF
CRIME

- Individuals **choose the behavior** that they wish to perform rationally.
- Weigh the **potential pleasure** of performing a behavior against the **potential pain** of the behavior.
 - When a behavior is judged to be **more pleasurable than painful**, an individual is likely to perform the behavior.

Agenda

- Fraud, an Example of What Personal Behavior?
- Ethics Fundamentals 101
- Us (Personal) versus Them (Organizational)
- Guidelines for Professionals (CPA, CIA, CFE)
- Tackling Ethical Dilemmas and Lapses
- Understanding Fraudster Models
- **Fraudster Stories**

Diann Cattani

Walt Pavlo

Walt Pavlo

Aaron Beam

Aaron Beam

Mark Whitacre

Nathan Mueller

Mark Whitacre

Agenda

- Fraud, an Example of What Personal Behavior?
- Ethics Fundamentals 101
- Us (Personal) versus Them (Organizational)
- Guidelines for Professionals (CPA, CIA, CFE)
- Tackling Ethical Dilemmas and Lapses
- Understanding Fraudster Models
- Fraudster Stories
- **Closing & Questions**



Questions?

Thank you

Contact Information

+1 512-934-4018

ABachmanCFE@gmail.com

LinkedIn: Allan Bachman, CFE