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Employee Background Roulette: Hirer, Beware

BY ROBERT TIE

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"People believe what they perceive," says Allen Brown, CFE, CPA, director of internal audit for the Louisiana Community Technical College System in Baton Rouge and an ACFE faculty member.

"That's why public image is so important," he adds. "When an organization recruits staff — especially highly visible senior officials — those selected become part of its image. And this profoundly influences confidence in the organization's ability to fulfill its mission."

Case in point: Congress is scrutinizing the Securities and Exchange Commission (SEC) because of its apparently flawed interpretation

of key background information on a top agency official.

Along with Congress, investors and taxpayers are wondering why the SEC and its chairman, Mary Schapiro, failed to perceive a potential conflict of interest involving now-former General Counsel David Becker.

Becker and his two brothers inherited \$2 million, three-quarters of which was profit, from their deceased mother's innocent investment in the Bernard Madoff Ponzi scheme. He resigned in February after Madoff Trustee Irving Picard sued him to "claw back" those profits, which the suit says were "fictitious" and should be distributed among Madoff investors who incurred losses in the fraud.

The SEC took a seemingly lax approach to the ramifications of Becker's possible conflict. Specifically, Schapiro instructed Becker to consult the SEC's ethics officer. But, as Schapiro knew, the ethics officer reported to Becker. This prevented the officer from being objective in appearance as well as in fact, as required by federal regulations. That approach persisted from the SEC's pre-employment assessment of Becker — who had once before served as the agency's general counsel — on to his being allowed to recommend how Madoff assets should be distributed, a process that could affect Becker's financial interests.

Brown also says that "by their acts and failures to act, those who are hired contribute to the entity's anti-fraud posture, including its internal controls. That is so in all organizations — public or private company, federal regulator or state agency. Of course, everyone with a stake in income or funding is watching. This includes other staff members, business partners, lenders, investors, constituents and fraudsters."

That's why a core recommendation of "Conducting Internal Investigations," the popular ACFE course Brown teaches, is to maximize the perception of detection. The course will be held next in San Antonio May 5-6.

"An organization must continually convince both honest and dishonest observers that it will detect and pursue all forms of fraud," Brown says. "It also should eliminate factors that weaken the perception of inescapable detection and anti-fraud commitment. That's why it's a serious mistake to hire someone who undermines this image, intentionally or not."

FOCUS ON THE BACKGROUND



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Many observers wonder how an organization as large as the SEC wasn't able to properly vet Becker. But it seems that cultural, not technical, factors caused the SEC's flawed evaluation; Becker was a familiar face — he had been the SEC's general counsel from 2000 to 2002.

In many cases, however, effectively screening a prospective employee requires considerable technical expertise not always available in-house. For that reason — and simple economy — many organizations turn to outside experts.

"As most people know, pre-employment screeners aren't all the same," says Thomas Lawson, CFE, CII, and CEO of APSCREEN, Inc., a factual employment screening firm he founded in 1980.

"The problem is that many companies think the most important differences are in price, speed and what passes for convenience," Lawson adds. "Unfortunately for them, it's not that simple. The most important parts of effective screening — quality and reliability — take time."

Lawson says it's critical that the hiring organization engage a screener who can identify risky candidates without running afoul of privacy and other laws that govern access to credit reports and any information useful in ferreting out unsuitable candidates. He often appears as an expert witness in negligent hiring lawsuits.

"Some screening firms can cause you more trouble than they prevent," Lawson says. "Don't do business with one if it tells you it doesn't need your candidate's written authorization to conduct a background check. Agreeing could cost you a lot when a surprised and outraged candidate sues you for violating his or her privacy rights."

Whether you engage a screening firm or vet candidates internally, Lawson offers these key recommendations:

- Formulate a standard employee screening policy, include it in your company procedures manual and mandate adherence to it.
- Design a background check questionnaire that obtains the information you need to conduct a thorough search. A comprehensive form can help you weed out unsuitable candidates who refuse to provide essential information.
- Obtain candidates' written permission to perform credit checks and other inquiries to evaluate their financial history — which can be a measure of integrity. (Though one has to take into account all factors that can have a negative impact on credit scores, such as the recent recession.)
- Search civil litigation indexes and tax court liens. Candidates frequently involved in civil actions — as plaintiffs or defendants — might be more trouble than they're worth. Likewise, candidates sued by tax authorities might have questionable judgment and/or other problems that could make it difficult for them to be productive in your organization.
- When engaging a screening firm, look for membership in certain professional associations, such as the Society for Human Resources Management (SHRM) and the American Society for Industrial Security (ASIS), a professional association for security managers, which may indicate proficiency and integrity.
- When considering a candidate you previously employed satisfactorily — as was the case with Becker at the SEC — update your files with a new background check. Much might have changed — your company, the candidate, the law and other factors — introducing important new (and perhaps negative) dynamics.
- Obtain a criminal history report, and make sure the candidate is who he says he is. Many candidates use aliases; 60 percent of the signed consent and identity disclosure forms APSCREEN receives contain falsehoods or omit important information. Unless you conclusively identify a candidate, you can't be certain your search results pertain to him or her.

The ACFE's "[Fraud Examiners Manual](#)," section 3.507 ff, also discusses background checks. CFEs must remember that anyone who manages cash, inventory, intellectual property or any other valuable commodity also should be closely screened.

CRISIS OF CONFIDENCE

"Stakeholder confidence and financial capital are the lifeblood of all organizations," Brown says. "One or both can evaporate when a company or government agency's management falters, jeopardizing the organization's mission."

In Brown's view, once Becker had been hired, the SEC should have required him to recuse himself from any Madoff-related activities. In addition, Schapiro should have instructed all SEC staff in writing to not approach Becker on such matters.

"Executives know actions speak louder than words," Brown says. "But sometimes they inadvertently permit actual or perceived wrongdoing by their employees. Letting Becker participate in the Madoff case was a major error."

Lawson agrees. "It starts with the hiring decision. There's much more at stake than technical competence. Never scrimp on a background check, particularly with senior staff. You might wind up hiring a technical genius who's unsatisfactory in other important respects. CFEs should emphasize that

to everyone who depends on them for advice, especially CEOs and boards of directors."

ALONE AT THE TOP

When Schapiro appeared before a House oversight subcommittee on **March 10** to discuss pressing matters affecting the SEC's FY 2012 budget request, legislators showered her with questions and lectures about her handling of the Becker affair.

A videotape of the **two-hour hearing** shows some of the SEC's broad array of complex, critical responsibilities and Schapiro's informed grasp of their technical nuances. And although Schapiro is a lawyer, the videotape reveals her command of other legal matters not directly related to securities, such as Becker's potential conflict of interest and how to deal with it, is not as strong.

A **60-second extract** from the hearing videotape presents a portion of the dialogue between Rep. Connie Mack (R-FL) and Chairman Schapiro. The slide Mack mentions cites C.F.R. 200.735-2, which governs federal executive branch agencies and states: "[Employees] must be constantly aware of the need to avoid situations which might result either in actual or apparent misconduct or conflicts of interest..."

Mack's pointed criticism of Schapiro's compliance with this provision highlights the pressures of leadership and how they affect actual and perceived tone at the top.

In many organizations, leaders' attention spans are sometimes spread thin across their multiple responsibilities. And that attention deficit can adversely affect the entire organization's ethical culture. But CFEs can help address leadership's potential shortcomings, such as lax hiring practices. Brown recommends that CFEs first learn what effective vetting entails — who does what, when, how and why. Second, he says CFEs must understand not only what constitutes an actual or potential conflict of interest for a candidate, but also for whomever is vetting him or her.

"CFEs who understand the reporting relationships within their organization can more readily identify conflicts of interest," he said.

RESOURCES

"**Civil Litigation Histories — The Misunderstood Background Check**," Thomas Lawson, CFE, CII, Fraud Magazine, May/June 2008.

"**Conducting Internal Investigations**," ACFE course, San Antonio, May 5-6.

"Conducting Background Checks" from the ACFE's "**Fraud Examiners Manual**," section 3.507ff.

Robert Tie is a New York business writer.

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