CASE STUDIES: LEARNING FROM THE SUCCESS OF OTHERS
THE KICKBACK MINE: VENDOR FRAUD WITH A KICKBACK TWIST

What at first appeared to be a straightforward vendor invoice scheme with one suspect turned into a corruption scheme involving multiple insiders and collusion, with a vendor pressured to provide kickbacks to keep his business afloat. Taken from the ACFE’s new Bribery and Corruption Casebook, follow the case as the investigation leads to some difficult lessons learned for the victim company.

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Mr. Christopher is also a graduate of the FBI Academy in Quantico, Virginia, and served as an FBI Special Agent in the Birmingham and San Diego divisions. While in the FBI, he investigated white-collar crime, including embezzlement, bankruptcy fraud, cyber-crime, public corruption, and bank fraud. He also investigated a wide variety of other federal crimes, including violent crime and civil rights violations, and was a case agent on the Alabama Church Arson investigation, in which three men burned nine rural Alabama churches in early 2006. The case garnered national attention and involved the coordination of more than 100 law enforcement officers from a dozen different agencies. Prior to serving in the FBI, he began his career in public accounting with Arthur Andersen, LLP, PricewaterhouseCoopers, LLP, and Deloitte, auditing large, publicly traded companies in the software development and telecommunications industries.

In addition to his teaching duties, he leads a private practice that focuses on providing fraud examination, tax, bookkeeping, and payroll services for his small-business clients. He is active in his community, having served on the board of his local Habitat for Humanity chapter, as the chair of his church audit committee, and leader of a mission trip to Rwanda. He is the author of “The Kickback Mine: Vendor Fraud with a Kickback Twist,” which was published in Bribery and Corruption Casebook: The View from Under the Table, edited by ACFE founder and Chairman, Dr. Joseph T. Wells, and Laura Hymes.
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The Kickback Mine

J. AARON CHRISTOPHER

It was a typically slow day at the Bellville, West Virginia, Residency Agency of the FBI where I served as a Special Agent. Being the only agent with an accounting background, I was the designated white-collar specialist when new cases arose. I received a call from Crimson Mine’s general counsel, George Brent, who told me about the recent discovery that one of their vendors had been overbilling them and he wanted to prosecute. My first thought was that this would be a routine matter of greed by a vendor and I would just need to look at how much was taken and try to get the vendor to confess. However, during the course of my investigation, additional suspects were developed, the scheme took a turn in a new direction, and the “bad guy” turned out to be likable and as much a victim as he was a suspect. It would also be one of the largest frauds to ever occur in Bellville.

The Crimson Mine had been a major employer in the region for more than 40 years. However, recently two of the three mines had closed, which resulted in a loss of jobs in the area. Crimson had been purchased a couple of years prior by a large public company, Diversified Holdings, Inc. It had its own hotline, and the new telephone number was posted in the break room and other places at the mine. Moreover, it subcontracted out mine support construction to local vendors so that Crimson could focus on mining. Over the years, the company had several different vendors, but for the past five years, it exclusively used Richardson Construction because of its prompt response and excellent work.

Keith Richardson moved to Bellville eight years earlier to start a small construction company dedicated to providing specialized metal fabrication to the Crimson Mine and manufacturing companies in the area. When Keith started, he only had one employee, but over the years he had developed the company into a thriving business with 30 workers. Keith was proud of his success but also felt a great sense of responsibility to his employees to earn work to keep them busy and employed. He knew that his success was
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providing for 30 families, and this responsibility weighed on him more than anyone knew. Because of the limited industries in the area, his work came primarily from half a dozen businesses. The Crimson Mine was his largest account, comprising 30 percent of his total billings.

Because of the substantial amount of work and long-standing relationship Richardson had with Crimson, they established a “blanket purchase order (PO)” agreement. Under the arrangement, when mine supervisors needed work done, they could call Richardson and order it at a prearranged labor rate plus the cost of materials, without the need to obtain competitive bids. The mine supervisor would then approve Richardson’s time sheets and materials list and forward the documents to the accounts payable department based on the blanket PO agreement. Crimson reserved the right to review Richardson’s time sheets, payroll records and materials invoices at any time without notice.

A few months prior to my call from George, Diversified received a message on its hotline. The tipster stated that Keith Richardson’s company had been overbilling Crimson for work done at the mine and that “it had been going on for years.” Diversified’s response was to seek assistance from the forensic accounting practice of its Big Four external audit firm. The auditors obtained documents from Richardson and performed a review of all of the last two years of billings and compared them to the vendor’s actual payroll records.

What they uncovered were overbillings totaling nearly $550,000 over the past two years. This was accomplished through overstating the actual hours reported on the time cards submitted to Crimson for payment. They also found ghost employees listed on time sheets who had either never worked for Richardson or were working on other jobs on the days billed to Crimson. As a result of these findings, Crimson immediately ended its relationship with Richardson, and George Brent called the FBI.

Taking a Gamble

After receiving George’s call, my partner and I headed out to the mine to get the whole story. George told us about the message from the tipster and about the work the external audit firm had completed. He had met with Richardson the day before to let him know that they would no longer be using his services but did not detail the audit findings to him. George appeared personally hurt by Keith’s betrayal and greed. He had known Keith for a number of years and liked him very much. He knew Crimson had substantially made his company what it was today and also valued the work Keith’s company had done at the mine. No safety violations or injury accidents had ever occurred from their work and, as the general counsel, that was very important to him. While he was saddened by the wrongdoings of
his friend, George also had a responsibility to the company, and Diversified instructed him to pursue prosecution of the case.

When I arrived at George Brent’s office at mine headquarters, he provided me with a two-page summary of findings along with five examples of overbillings. He also told me about his meeting with Keith the day before and that while he didn’t accuse him directly, he was confident that Keith knew that the auditors had discovered the fraud. He also told me that all of the audit evidence and working papers were at the auditors’ offices back in Texas.

At this point, I had a decision to make. Do I subpoena the detailed audit evidence and spend time wading through several boxes of invoices, time sheets and payroll records, or do I go ahead and interview Keith with the information I have?

I chose to interview Keith. To be honest, this was a bit of a gamble. Keith could tip off other conspirators or destroy evidence. However, I decided not to wait because after George spoke with Keith, he knew the fraud had been discovered. Also, he was no longer in a position to continue the fraud or do further damage. As far as destroying evidence, I knew the auditors already had most of what we needed, and the rest would be found by a subpoena of his bank account. At the time, I was not aware of any co-conspirators, but if they were going to be tipped off by Keith, likely it had already happened.

Special Agent Trace Burrows was the only other agent in the Bellville Resident Agency. Trace had been an FBI Special Agent for 18 years and was enjoying being close to home as his retirement date approached. Prior to joining the FBI, he worked for the Baltimore Police Department and had developed a specialty in violent crimes within the Bureau. While Trace wasn’t an expert in white-collar crime, he was an expert at criminal behavior and was a great asset to have on interviews. Typically when we interviewed together, we would strategize and decide who would take notes. For our interviews on this case, Trace took the notes to allow me to focus on developing the questions, introducing the evidence and confronting our interviewee with the fraud allegation. His help and guidance on the case would prove invaluable.

Trace and I asked George to call Keith and arrange a meeting at George’s office. Since Keith’s office at Richardson Construction was nearby, he arrived about 15 minutes later. He was very surprised to see two FBI agents there but knew why we wanted to speak with him and agreed to sit down and visit with us. I first built a rapport with him and got to know him a little bit. I asked him to tell me about his business and was genuinely interested in learning more about the coal industry and what his company did at the mine. Next I had him tell me about how he got started working with Crimson. By the time I asked him about the fraudulent billings, I presented it as if the allegation of fraud was a fact and just part of the story. I would periodically ask clarifying questions, but for the most part I just let him tell me what happened. I did not want to be confrontational and adversarial
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with him by leading with an accusation that would be difficult for him to accept and admit to. Instead, by building rapport with him over 30 minutes or so of nonthreatening discussion, when we finally did introduce the fraud allegation, he just incorporated that into his story and proceeded to confess the details of the scheme.

As Keith began to explain the fraud, he started about five years earlier. He was reluctant to involve anyone but himself, but eventually described the first time that the mine manager, Rich Bowden, asked him for some tickets to a big college football game the upcoming weekend. After that, Bowden began asking for money — reminding Keith of all the work Crimson did with Richardson and how much Keith’s company would suffer without it.

The revelation that someone on the inside at Crimson was involved was news to me, but I didn’t let Keith know that I was surprised to learn it. Along the way, I showed Keith some of the billing documents the external auditor had identified as part of their forensic audit. He admitted that they were false and that he had inflated them to provide cash to Rich. At first Rich would ask for money infrequently, but beginning a couple of years ago, he started asking for money on a regular basis and would almost always stop by Keith’s office to get an envelope with the cash in it.

As Keith talked, I focused my questions on the “why” of the scheme. As someone who had studied various fraudsters and other white-collar schemes, I had always been interested in that first decision to cross the line and commit fraud. I assumed that he had debts or wanted to buy something and “needed” the extra money. However, as Keith detailed his reasons for the fraud, I actually began to feel sorry for him and his situation. Rich threatened to end his contract with the mine, which would have forced Keith to lay off a number of his workers who depended on him to provide work to support their families. Also, because he was taking large amounts of cash out of his business account and did not have a legitimate business reason or receipts, he had to pay taxes on the withdrawals as if he personally had received the money. Therefore, a significant portion of the overbillings went to the IRS to pay the additional taxes he incurred.

At the end of our interview, Keith promised to cooperate fully with our investigation and answer further questions upon request. Our next step was to go to Bowden’s house. We knew it was possible that Keith could have second thoughts about his confession and tip Bowden off to our investigation, so Trace and I wasted no time in trying to interview him.

The Cold Shoulder

As we drove up the driveway to Rich’s house, we saw the large industrial building that was rumored to hold his collection of 20+ antique cars. To the left of the house, we noticed a large above-ground pool with a huge deck built around it and a hot tub under a cabana. It quickly became obvious that
he was living well beyond his mine supervisor’s salary. Bowden was a gruff,
mine-hardened man who at 6′8″ could be pretty intimidating. He reluctantly
invited us inside to talk at his kitchen table. Unlike Keith, Rich was not in
a talking mood. He told us about his 28-year career at the mine and how
he was looking forward to retirement. When we turned our attention to his
relationship with Keith, he became quiet and seemed to be listening to find
out how much we knew. When we directly asked about the bribe payments
Keith made to him, he quickly stated, “I don’t want to talk about the money.”
I provided him with my card in case he changed his mind and let him know
that we did not need his cooperation with the evidence we had. It was up to
him if he chose to cooperate or not. We left shortly thereafter.

Rich’s quick, tight-lipped response when accused of taking bribes told
me two things:

1. There was money to be talked about.
2. He did not want to cooperate.

This verified Richardson’s claim that Bowden was involved, but I still
needed evidence to prove it. My next step would be to conduct many more
interviews and begin reviewing documents.

Fortunately for me, the external forensic auditors had already done an
outstanding job of proving that Keith had been overbilling Crimson. They
compared all of the vendor’s billings, which included time cards submit-
ted for approval to Richardson’s actual payroll. The vast majority of the
overbillings had been approved by Bowden, but I began to notice another
supervisor’s signature on other inflated invoices — Steve Crosby.

As I interviewed other mine workers, they relayed rumors that Bowden
had pressured other vendors in the past. They detailed how one vendor had
his workers build the deck at Bowden’s house and how another had installed
the hot tub. They were also suspicious of Bowden’s relationship with Keith
Richardson and stated that they believed he was also taking money from him.

Since I did not have to do the forensic work on the overbillings, I focused
my attention on Richardson’s bank statements. The inflated checks from
Crimson were deposited into Keith’s business checking account, so that was
a logical place to look to see where the money was going. What I found
surprised me. I saw only small checks payable to Keith personally and on
an infrequent basis. Typically, one would expect to find a large amount of
money coming out of the account to the primary subject’s benefit. I did,
however, find regular checks made payable to “cash” approximately every
two or three weeks. Richardson’s office manager told me in an interview that
Bowden would come by Keith’s office every two or three weeks and leave
with a brown manila folder. She suspected that the envelopes contained cash
but never questioned Keith about them. Again, it was more circumstantial
evidence of Bowden receiving bribes, but I needed something concrete.
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In my search to determine what Keith spent his ill-gotten gains on, I found a few checks made payable to a local credit union. The checks were suspicious and in the amount of $473.54. A subpoena to the credit union revealed that the checks were loan payments on a truck owned by Rich Bowden. Finally I had hard evidence that Bowden had been receiving bribes. He had Keith directly make truck payments for him.

I also found checks made payable to Eugene and Bobby Crosby. The name “Crosby” caught my eye and I remembered the other mine manager, Steve Crosby, who had approved a few of the inflated invoices. It was time to interview Steve.

The Benefits of Cooperation

Unlike Bowden, Steve was very humble and contrite when he came to the FBI office to speak with us. He had been keeping this secret for too long and just wanted to get it off his chest. He told me about how Bowden had promoted him as an individual mine supervisor when he became the area manager. He then detailed how Bowden pressured him to approve false invoices for Richardson and not to ask too many questions. Eventually he too began accepting cash from Richardson. The checks I had discovered were payments made to his two grade-school-age sons. Crosby was completely truthful and fully cooperated. He said he was relieved to have the entire episode behind him and agreed to testify against Bowden if needed.

In reviewing the evidence against Richardson and Crosby, the over-billings and other documents alone would have been enough to convict them at trial. Crosby had no reason to receive checks from Richardson, and the fact that they were made payable to his young sons was even worse. The clear evidence of billing Crimson for workers who were not even Richardson’s employees or were working on other jobs on the day billed to Crimson was sufficient evidence against the vendor. However, because they had been truthful and confessed the scheme to Trace and me, they both agreed to plead guilty to a federal information of mail fraud. An information is used in federal court when a subject agrees to plead guilty to a criminal charge instead of being indicted by a grand jury. The federal mail fraud statute was used because the subjects in this case caused the proceeds of their fraud to be mailed by Crimson to Richardson Construction through the U.S. Postal Service. (The mail fraud statute, because it is so broad, is considered the workhorse of federal fraud prosecutions.) As a result of their cooperation, the defendants avoided arrest and were allowed to self-report to court for their hearings. Also, the U.S. Attorney agreed to recommend sentencing on the low end of the Federal Sentencing Guidelines to the judge.

Bowden never took me up on my suggestion that he cooperate with the investigation. As a result of the statements of Crosby, Richardson and Richardson’s office manager; Bowden’s signature on the false invoices; and,
more important, the checks Richardson wrote for Bowden’s truck payments, Bowden was indicted by a federal grand jury on multiple charges of mail fraud. I arrested him at his home and took him before a U.S. magistrate for his initial appearance. He was granted release with conditions pending trial.

After reviewing the substantial evidence against him, including his signatures approving the false invoices, Keith’s payments on his truck loan and the witness who saw him regularly leaving Keith’s office with a thick envelope, Bowden’s attorney recommended that he plead guilty to the charges against him. He ultimately did, and all three defendants avoided a trial. The judge sentenced Richardson and Crosby to 12 months in prison, which they served at a minimum security federal prison camp. Although they were given a lenient sentence, the judge explained that they deserved to serve a year in prison because they did not come forward and stop the fraud when they had the opportunity. The judge had harsher words for Bowden, who betrayed his lifelong employer, for failing to take responsibility for his actions. Bowden was sentenced to 36 months in prison, which he served in a maximum security federal penitentiary in another state. All three of the defendants were held jointly liable for restitution for the full $550,000 amount of the fraud.

After sentencing I learned that, out of his feelings of guilt, Richardson arranged to close his business and gave all of its assets, including the real estate, to Crimson in full settlement of the restitution order.

### Recommendations to Prevent Future Occurrences

**Fraud Hotline**

The tip from the anonymous whistleblower led to the initial discovery of the fraud. Had Crimson Mine had a hotline in place prior to the acquisition by Diversified, the scheme could have been discovered much sooner and losses would have been greatly minimized. As discussed in the Association of Fraud Examiner’s 2010 Report to the Nations, organizations that have fraud hotlines in place suffer significantly smaller losses and discover fraud schemes on average seven months sooner than organizations without such a reporting tool in place.

**Early Interview**

Often investigators are leery to approach a subject until they have all the facts. This strategy can be useful, but it can also lead to wasted investigative resources and looking for evidence in the wrong places. Because the subject of this investigation was already aware of it and was not in a position to do more harm to evidence or the victim company, interviewing Richardson early paid dividends in investigating the case. Investigators have to evaluate when they have enough evidence to approach a subject with an accurate and knowledgeable accusation.

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Investigative Myopia

Naturally investigators form an initial theory of a case. (In the Fraud Examiners Manual [ACFE, 2012], this is known as the fraud theory approach.) However, we must remain open to following the evidence and challenging our initial theory. Rather than being a case of a greedy contractor (Richardson) bilking a customer, this was a case of the greedy supervisor (Bowden) extorting the contractor to pay for his own kickbacks. Richardson profited nothing and ultimately lost everything as a result of the fraud.

Internal Audit

In this case, the internal auditors of the parent company did not provide adequate oversight at this relatively small subsidiary, providing additional opportunity for fraud to occur. Proper internal controls and regular audit procedures might have prevented the fraud or uncovered the losses sooner.

Scope

When a fraud has occurred over a long period of time, it is important to work with prosecutors (presuming criminal prosecution is warranted) early to develop a scope for the investigation. In this situation, even though the fraud was thought to have occurred during the last five years, developing evidence more than the past couple of years would not have added anything to the prosecutor’s case. Additionally, complete records older than two years were not available, and only a partial audit trail could have been traced. By limiting the scope of the investigation, I was able to focus on providing clear and logical findings to the grand jury and thereby not overcomplicating the case.

About the Author

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