

# By Any

# True Accounting, The Deed Was **Fraud**

*Editor's note: FEI Atlanta Chapter member Jim Wanserski has uncovered fraud multiple times — at Sprint, Telecom USA and MCI — and has assisted some of his consulting clients in ferreting it out. During his Sprint tenure, his success spurred internal clients to seek his help. Those experiences, common sense and a natural skepticism positioned him to uncover a large receivables fraud at MCI, putting the perpetrators behind bars. Here is his first-hand account.*

By Jim Wanserski

**D**ata from the Association of Certified Fraud Examiners (ACFE) indicates outsiders are far down the list in terms of uncovering fraud. My own experience confirms that active managers have the best opportunity to detect fraud and the direct responsibility to do something about it. We need to act more aggressively on our instincts.

I have worked for a variety of large companies, in staff, auditing, management and consulting roles. I have uncovered fraud multiple times. In retrospect, that prior experience prepared me to uncover and deal with a multi-million dollar fraud at MCI Inc.

My observations and descriptions of events are generated or supported by sworn testimony given by me and others in the civil and criminal litigation, supplemented by my own per-

sonal knowledge and experiences. Here is the story:

A decade ago, I was the Director of Customer Financial Services at MCI, responsible for nationwide credit and collections for all commercial customers. One line of business was “carriers,” wholesale customers who established their own customer bases and provided telecommunications services via capacity purchased from facilities-based providers like MCI.

Management of carrier billing and collections came to me in April 1996, on the heels of the two largest disconnections of service experienced at MCI. I was tasked to clean up this portfolio. From April 1996 until his separation, Walter Pavlo, then a senior manager, reported to me.

#### Rules Were in Place

My primary emphasis was on enforcing MCI’s customer contracts. Each carrier contract included payment terms, surety and specific descriptions of all requirements as dictated by contract execution processes. Leverage for straightforward collections action existed. Policy documents addressing

employee behavior, the rules of engagement for committing the company contractually and who was authorized to do so had been distributed in late 1996. The “rules of the road” were vividly clear.

Ultimately, I uncovered the carrier fraud executed by Pavlo and others, dealt with it internally and worked actively with white-collar crime resources. We communicated proactively and regularly with law enforcement. I also prepared for and testified in subsequent litigation, totaling 40 hours under oath.

“Proof-positive” of the fraud was uncovered in February 1997. I confronted the internal perpetrators with the inappropriate transactions they had directed. However, finding the hard evidence was merely the endgame, the “smoking gun.” My own internal control and gut-level suspicions had already peaked due to a number of occurrences, behavior changes in the group and judgment lapses, if not just the difficulty in getting crisp information.

In mid-1996, several sales and business analysis people contacted me, expressing concerns about how

A former financial services manager at MCI recounts what happened in a well-publicized case that he came to know intimately, and offers advice to others about how to deal with fraud and any ensuing litigation.

Jim Wanserski today, nine years after he reported fraud at MCI

## Lessons Learned

☛ You MUST build and maintain multiple, reliable, cross-functional relationships across the organization. You cannot detect fraud in a vacuum. This is the most important realization I have come to and my strongest recommendation.

☛ Hard facts, street-smarts, awareness of behavior changes, inquisitiveness and experience are critical skills. You will need all of these to effectively prevent and detect fraud.

☛ Develop and use recurring but sophisticated reporting to address the “usual suspects” and specialty areas. Go personally to the details. “Sacred cows” deserve special attention. Analytical review techniques still work.

☛ Managers must establish and regularly communicate direction and tone, be it on policy, process, expected behavior or operational results.

☛ If you cannot get crisp answers, probe. People either do not understand, or they are hiding something ... and both are problems.

☛ You cannot rely on memory alone. Document as if you are going to court. Early on in detection efforts, document everything; you will likely need all that material.

☛ “Whistleblowers” are not well-received. Arm yourself with FACTS. Anticipate that you may become the target of potentially desperate acts.

☛ Rely upon knowledgeable legal staff, internal and external. When outside expertise is brought in, take full advantage. Consider the need for your own legal counsel.

☛ Require organizational separation between financial operations and accounting. At MCI, this nearly provided very early insight to suspicious transactions. Vigorously pursue accounting and reporting questions across boundaries.

☛ Expect you will have to push the action. In less than 10 months, I suspected fraud and ultimately uncovered it. According to the ACFE, the average fraud goes undetected for 18 months. On a conference call early in the investigation, an FBI agent told me two things: MCI was “handing this case to authorities on a silver platter,” and “to find fraud, you have to be good, and lucky.”

☛ Managers are responsible for fraud prevention and detection.

**Q: You describe Pavlo’s accounts as “entertaining fiction, at best.” He’s given talks on his fraud...reactions?**

A: The First Amendment is a wonderful thing, and fiction is entertaining. However, the distorted accounts I’ve seen about Pavlo — who has become a speaker at ethics forums and before business students — motivated me to write this article. The wide-ranging stories have multiple inconsistencies.

### Q&A with a whistleblower

According to Pavlo’s accounts, one might even surmise his message was “the environment made him do it!”

Understanding the testimony and facts, however, provides a far different view. This was a willful, active fraud involving a very small group of customers, executed by a very small group of people, some of whom ended up going to jail. Fraudsters typically act deliberately, out of greed, power and perhaps even stupidity... and most ultimately get caught. These perpetrators exhibited many typical fraud behaviors. Because of my experience, I had seen it before, but I had to get “proof positive” to end it, and I did.

I have presented this fraud case in a

certain customers were being dealt with by carrier collections. Their observations mentioned inconsistencies, mishaps explained away as poor communications and difficulties getting needed customer information. However, I also heard about suspicious activities, questionable tactics and inappropriate customer commitments, including occasional references to “deals.”

In the midst of this behavior, I presented the “state of carrier receivables” to my finance bosses in August 1996, at a major review session. I summarized how the carrier marketplace had changed, what the current financial exposure was and what we were doing about it. Consistent and continued support for direct actions to control carrier receivables was expressed from all levels. Messages confirmed at that meeting included: “cash is king;” “take whatever service-disconnection action you deem required;” “impediments to collection will be removed.”

graduate-level, business ethics class at the university where Pavlo got his MBA.

**Q: Give us examples of conflicting events in Pavlo’s commentaries.**

A: His claim of trying unsuccessfully to get MCI to take a \$180 million charge blatantly conflicts with the facts. In a 2002 article, he had claimed the number was \$88 million. Either inflation has increased his number or he didn’t review his earlier stories!

It is fact that during 1996, MCI wrote off \$120 million of carrier receivables and recognized even more exposure by adding to bad debt reserves. So, his claim that MCI “hid” bad debt expense is just bogus. He further claims “his bosses” said the maximum that could be written down would be \$15 million, and that is also senseless.

Finally, the published account that “Pavlo’s crime unraveled when his boss discovered discrepancies between what some of MCI’s customers said they owed and what the company thought they owed,” is also negated by facts. My suspicions had increased over a period of months, but the “proof positive” was the inappropriate recording

Top management support for collections action was clear.

My growing frustrations forced me to take over direct negotiations with key, high-risk customers. During those negotiations, I became convinced that judgments and decision-making by my staff were growing inept, if not worse. Legal direction was not being strictly followed. Finally, after disconnection of one particular customer, Pavlo resigned the first time. I was convinced of fraud, but I had to get him back into the office to lock it down. I convinced him to return under the guise of participating in a “transition period to make organizational changes.”

#### ‘How Much Do You Know?’

In the midst of those changes, the first set of inappropriate transactions was discovered. With hard evidence in hand, I confronted the fraudsters. I vividly recall the phone conversation with Pavlo, especially when he asked,

of a large settlement payment from WorldCom. Pavlo directed \$5 million of the \$41 million payment to be applied against a customer account I had personally negotiated and had disconnected... pretty dumb!

**Q: Describe some comical events.**

A: You’ve heard that rule, “never ask a question you don’t know the answer to?” One attorney interrogated me on a topic where he believed he had all the answers. When I replied far differently than he expected, he tortuously skipped over five pages of further questions! By reputation, he was a tough guy. I enjoyed that one very much.

I recall testifying on a particular event where my account totally conflicted with a defendant’s. His attorney quizzed me about how I could so confidently know the defendant was wrong. I simply said, “Because I asked the person the defendant said he had gotten approval from, and that person told me neither had he given [the perpetrator] approval, nor had he ever seen the document in question.” I liked that one, too — that’s called a “gotcha” in legal terminology.

**Q: Was testifying intimidating?**

A: Anticipation was the worst part. I had been deposed in prior civil proceedings; this was much different. At times, I felt my own integrity was being questioned. Counsel’s recommendation was simply to “own the facts.” I would rate my performances on the stand as a bit stiff to very good. The ultimate compliment, however, was the “high fives” I received from FBI and Treasury agents.

**Q: Any disappointments?**

A: Despite uncovering this fraud in less than 10 months, I

“Well, Jim, so how much do you know?” He quickly resigned a second time and hired legal counsel, first civil, then criminal.

The carrier fraud possessed several components, as the internal perpetrators joined forces with an outside loan broker and a factoring company, who both played significant roles. The base element required the perpetrators to convince a selective, small group of customers to divert payments to other parties. They then manipulated accounting records to camouflage these illicit activities. Unauthorized “agreements” executed by the perpetrators memorialized the deals. One of those concoctions even required MCI to guarantee payments to the factoring company if the customer did not pay. (Obviously, only the fraudsters would gain value from such an illogical arrangement!). Finally, investigative efforts revealed a series of payments improperly directed to a software developer.

I uncovered further dealings with outsiders, drove the internal investigation and dealt with the multitude of auditors and consultants, including one of the most skilled and impressive white-collar crime people I have ever met.

Two things I did not anticipate: the ultimate reactions of certain executives (as opposed to other companies I had worked for); and the unsubstantiated accounts of this fraud subsequently appearing in the press. Based upon my testimony and knowledge, “fiction” has prospered in the media, unfounded, under-researched and unchallenged.

A key reflection on testifying: speak from fact. Presenting the truth is the best offense, and the only defense. Time after time, I had to explain the facts in inordinate detail, yet in their simplest form, all for clarity. Defense attorneys continually “put words in my mouth” (from their clients). Developing a working knowl-

edge of the facts required much time, study and attention. Face it, you must develop a mastery of the data by wading painstakingly through the details.

**Q: “Whistleblowing” has costs, doesn’t it?**

A: Absolutely; be prepared. For example, I was personally named in a far-reaching Racketeer-Influenced and Corrupt Organization Act (RICO) suit, later dropped. Circumstances can get ugly in spite of doing the right thing. At times, I was concerned for my safety, and for my family. I knew my actions to uncover this fraud would have consequences, just not some of the ones that ultimately played out. At Sprint, when I uncovered a fraud against the company in 1984, I received a chairman’s award; at MCI, well... I ended up leaving.

This “whistleblower” experience was very unlike any other. In 2002, Forbes published an article about the MCI fraud in the midst of active litigation. I have noted over 40 inconsistencies, errors or apparent fabrications vs. the sworn testimony and factual knowledge. In 2004, Internal Auditor published an apparently uncorroborated interview with Pavlo. I have an email from the author basically apologizing, though the magazine has declined to publish a “correction.” More recently, someone historically connected with the bank consortium that had originally funded the factoring company caused me to lose consulting opportunities, nearly six years after testifying! So, I felt it was time to disclose the “rest of the story.”

Overall, testifying skills are similar to those developed for negotiating, except you’re on the receiving end. You wait for each question to be presented, state what you know, directly responding to each specific question. You must also admit when you don’t know, and that is sometimes difficult.

Your inclination is to educate the questioner on the topic, which is not your role. I regularly heard, “Wait for the question to be asked and then answer it specifically; fuller explanation can be given during cross-examination, if warranted.” My preparation forced a command of the facts, a requirement for success.

Jim Wanserski ([jorswan@bellsouth.net](mailto:jorswan@bellsouth.net)) is an independent consultant in Atlanta doing work with specialty and turnaround consulting firms.