

CASE STUDY: HARD DRIVES AND BAD LUCK²

Someone had stolen 1,400 hard drives from a computer warehouse in Toronto. That much was certain. But the question remained: who took them? The answer was more than academic; it could mean the difference between the distributor's continuing operation and a total crash. Swainler's Technology averaged \$8–\$9 million a year in sales, but with an 8 percent

profit margin, the company didn't have much financial room to maneuver. The company was a joint venture, overseen by a group of investors who were, to put it mildly, nervous. They had theft insurance, but with a particularly sticky clause that said that the policy wouldn't cover theft committed by a Swainler's employee. In order to collect on the \$600,000 worth of disk drives missing from the warehouse, the investors had to show that the theft was an outside job.

²Several names and details have been changed to preserve anonymity.

Their report showed just that. Employees and management agreed that the skids bearing the equipment had been safe and sound until the week that a competitor of Swainler's, Hargrove Incorporated, had sent delivery drivers over for an exchange. Evidently, some of Hargrove's people had swiped the equipment during the several days they were working in the Swainler's warehouse. Hargrove and Swainler's worked together when they had to, but they were in hot competition, and at different times each company had lost business—and employees—to the other. Since all Swainler's employees checked out, management concluded that the theft must have been committed by someone from Hargrove.

Doug Andrews was an independent adjuster hired by Swainler's Technology's insurance company. Besides conducting routine loss estimates, he's also a certified fraud examiner who is willing, as he puts it, "to see things other people either don't see or choose to ignore." Although the Swainler's board assured Andrews this was a simple case, he wasn't convinced: "I wasn't sure it wasn't an inside job. Too many questions were left hanging. How did the Hargrove people get the stuff out without being seen? The date management was setting for the loss seemed awfully convenient. It seemed like at the least someone at Swainler's had to be involved," Andrews remembers. He needed some help chasing down these hunches, so Andrews hired Harry D'Arcy to assist. D'Arcy worked for the Canadian Insurance Crime Prevention Bureau as a CFE and investigator. He and Andrews interviewed everyone at the warehouse and on the investors' board, returning two or three times if necessary to get their questions answered. They traced serial numbers and possible distribution routes to turn up some sign of the hard drives. D'Arcy says, "We met at least twice a week to come up with a way to solve this. It was like a think tank, bouncing ideas and options off each other: 'What tack should we take now? Should we call out to California? Do we need to go to that shop in Ottawa?' We knew we were being stymied. We just had to find a way around the blocks they put in front of us."

The main thing bothering Harry D'Arcy was that the board was presenting them with what appeared to be an open and shut case. Everyone's stories matched like precision parts. "It was too good to be true, too neat," D'Arcy says. The board members had seen the material on the Friday before Hargrove came; they noticed it was gone afterward; they had reason to suspect their competitor was behind it. Yes, they knew their insurance policy wouldn't pay if an employee did the hit, but that was beside the point. The board trusted its employees. Many of the people at Swainler's, from clerks to warehouse personnel, were either related to, or friends of, the management. D'Arcy and Andrews were encountering what Andrews later described as "an active campaign of misinformation."

Once he got a sense of the system of operation at Swainler's, D'Arcy had some material for a new round of questioning. He noticed that as skids of equipment were prepared for shipping, the entire apparatus was wrapped in a thick plastic sealant and moved from the warehouse floor into the shipping dock.

"Now," he asked one of the investors, "if those disk drives were ready for shipping on the Friday you say, then they would have already been wrapped, right?"

"Sure."

"Then, how did you know what you were seeing if the wrapping was already on? You can't see through the wrapping."

"I knew that batch was supposed to go out for the next week," the man replied.

"Then the skids should have been moved to the loading dock," D'Arcy interjected.

"I don't see your point."

"You said you saw them in the warehouse," D'Arcy reminded the man. "You couldn't have seen them in the warehouse if they had been moved to the dock for shipping." The witness, feeling stymied himself, shifted and said, "Well, maybe they hadn't been taken over yet."

D'Arcy had a full house of questions for the initially talkative managers. Why would they notice a particular skid of drives on a particular day? Why were their memories so specific on this one shipment? How often did management tour the warehouse for an informal inventory? D'Arcy reports, "Once I had them shaken up, I would ask them point blank, 'Are you parroting something you heard somebody else say?'" The men would declare that, no, they'd seen the material themselves.

"Did you discuss this with other board members?" D'Arcy asked.

"We talked about it in board meetings, sure," came the answer.

"And did you all agree on what you would say when you gave a statement?"

"No."

"But your statements all match."

"We agreed that we remembered the drives being there on the same day."

Doug Andrews was feeling fed up: "We were getting this string of nonanswers. I felt like we were coming up dry."

Swainler's had hired a private investigator of its own to work the case. Harry D'Arcy talked with the man, who was convinced he had the material to show an outside job. The PI had been to Hargrove and spoken with employees there, including a man who had once worked for Swainler's. "I don't know if somebody here took the stuff or not," the man said. "But those guys at Swainler's deserve everything they get." He claimed Swainler's required its employees to work long hours with little pay or benefits, that workers were little more than switches on a processing board. To Swainler's investigator, then, this was a classic case of employee resentment, a common excuse for fraud.

D'Arcy said he disagreed, but the investigator persisted. Swainler's Technology was now claiming its expenses for the investigation, finally totaling \$125,000. During one week alone, the PI billed \$45,000 when he conducted a stakeout in another city. An anonymous tip to the executive vice president at Swainler's placed the stolen disks at a storage facility in

London, Ontario. The investigator took a team of people and equipment, and after a weekend of surveillance, it observed a man opening the unit. When the team approached, it found nothing inside but the man's personal belongings.

Meanwhile, D'Arcy and Andrews pursued their own strategy. They notified the manufacturer's representatives throughout Canada and the United States to be on the lookout for a set of serial numbers. Sure enough, a call came in from a dealer in California; one of the disk drives had shown up for repair. Invoices showed the drive had been shipped from upstate New York and was purchased in Ottawa, Canada. The Ottawa shop had received the drive from a distributor in Montreal. Doug Andrews went to the Montreal warehouse but found it empty. Canvassing the neighborhood, he was told the people renting the warehouse had moved to another area in northern Montreal.

When Andrews got to the new address, he questioned four or five of the workers there about his case. They had never heard of Swainler's and knew nothing about the stolen drives. But when Andrews pressured them to look through their records with him, he found documents matching his serial numbers. Then, one of the missing drives turned up inside the warehouse.

Andrews wasn't ready to celebrate, though. "I was feeling beat. We'd been spending all this time, running back and forth, interviewing and reinterviewing. I said, 'I don't know, we may not get this one.'" The invoices he'd looked at were dated five weeks earlier than the time Swainler's had listed the theft. The discrepancy might help disprove the company's outside perpetrator theory, but could also be used to throw Andrews's largely circumstantial case into further confusion. As he was driving back to Toronto, Andrews got a call from Harry D'Arcy. "I've been doing some work based on what you found there," D'Arcy told him excitedly. "When you get back they'll be in chains."

Since D'Arcy now knew that at least some of the merchandise had gone through the warehouse in Montreal, he had looked for phone calls from that city in the phone logs at Swainler's. The marketing manager, Frederic Boucher, had not only received a large number of calls from Montreal, the calls were coming from the warehouse Andrews had just visited, the one claiming it had never heard of Swainler's. D'Arcy spoke again with people in the warehouse, one of whom admitted that the skids had disappeared much earlier than first reported. He guessed the actual date was about a month earlier than the one management had given. This, of course, coincided with the invoices Andrews had found in Montreal. At a special meeting, the board of directors reviewed D'Arcy's findings and confronted Frederic Boucher with the evidence pointing toward him. Boucher denied any involvement, and the board supported his story.

The next morning, Boucher told a different story. He had talked with his wife and a lawyer and was ready to come clean.

He said he'd met the people from the Montreal warehouse at a conference. Together they worked out a deal in which Boucher would provide them with a supply of hard drives at a sweet price. With the help of a Swainler's shipping clerk, Boucher sent sixty low-end drives to Kingston, halfway between Montreal and Toronto, for \$20,000 paid in cash. The atmosphere at Swainler's was ripe for this sort of offense. Harry D'Arcy recalls, "The bookkeeping system wasn't controlled. It was nothing to find things going out with no receipts. The operation was mainly run on trust. The men who headed up the company were all old friends, and they hired people they knew or to whom they were connected in one way or another. It ran on blind trust and nepotism." Encouraged by their first success, Boucher and his accomplices then arranged to make the big sale: 1,400 top-quality hard drives for a \$600,000 take. They didn't have to worry about covering their tracks, because management was eager to point the finger outside the company and collect on their insurance.

With Boucher's confession, Doug Andrews could make a happy report to his client that they weren't liable for the claim. Boucher was sentenced to make restitution for the theft, and to two years' imprisonment, while the shipping clerk and the Montreal distributor were given one year each. All the sentences were suspended and the defendants placed on probation. The executives at Swainler's were, according to Harry D'Arcy, "cautioned regarding their complicity in the matter." Swainler's survived the loss but was later purchased by a prominent Canadian investment group and now operates under that umbrella.

Doug Andrews, who lectures and writes articles on insurance fraud in addition to conducting investigations, finds that people resist seeing cases like Swainler's as a real crime.

"There's a belief that perpetrating fraud against an insurer is a victimless crime." Reports from the KPMG accounting firm and the Canadian Coalition Against Insurance Fraud place the insurance losses in Canada between \$1 billion and \$2.6 billion a year. But Andrews believes that "[you can] take the middle figure of \$2 billion and double it." Though a significant portion of those losses is related to occupational crimes, an accurate account is not yet available. That's because some of the major acts that occur in business felonies—like supplier and kickback fraud—aren't included in the insurance industry figures. Nevertheless, these crimes are serious and proliferating. "They are frequent," Andrews says, "and often systematic and well organized. Especially since insurance companies don't advertise as aggressively in Canada as they do in the United States, people see insurance as a kind of faceless bureaucracy." With the tremendous amounts of money changing hands in this industry every day, "there's a mindset that labels these companies fair game. . . . But people see the difference in the end, when they pay their premiums."