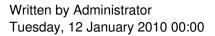
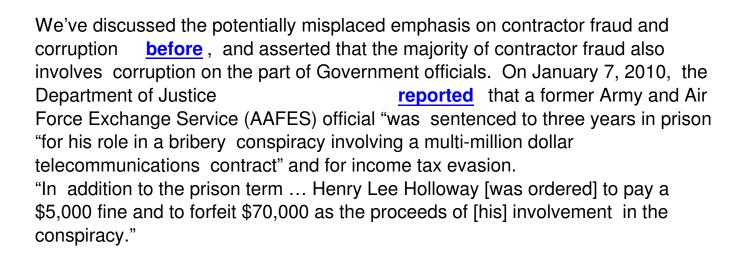
Fraud is Everywhere





The DOJ press release notes that the AAFES provides billions of dollars of goods and services each year to service men and women by operating base and post exchanges. Holloway was a general store manager at the Central Exchange in the Republic of Korea (

RoK)
from 2003 through 2007. During his tenure, he accepted "at least \$70,000 worth of stock, entertainment, travel expenses, cash and other things of value" from the

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Written by Administrator Tuesday, 12 January 2010 00:00

CEO of Samsung Rental Company (SSRT) in return for maintaining "SSRT's \$206 million contract with AAFES to provide telecommunications services to U.S. Armed Forces installations" in the RoK

, "despite Holloway's knowledge and belief that SSRT was underperforming and violating the terms of its contract with AAFES." (The SSRT CEO was sentenced to five years in prison and a \$50,000 fine.)

But fraud and corruption are not confined to the aerospace/defense industry. On December 24, 2009 reports emerged that Koss Corporation fired its long-time VP of Finance and Corporate Secretary, for allegedly embezzling millions from the company. The individual in question (Ms. Sujata "Sue" Sachdeva), was "suspended" on December 21

"for financial improprieties," and was fired on December 24

for embezzling as much as \$31 million over the past 18 years. Two members of the Koss accounting staff who reported to Ms. Sachdeva

were also put on unpaid administrat

ive leave. A

ccording to the

Wall Street Journal

"The government alleges she embezzled company funds to pay off her personal American Express credit-card charges for the purchases of furs, jewelry, apparel and home decor.'

Importantly, Ms. Sachdeva, as VP of Finance, was responsible for many "management representations" provided to its external auditors, Grant Thornton. Because those representations can no longer be relied upon, Koss' financial statements must be reaudited, and will likely need

to be restated. Koss is a publicly traded company, so the

SEC and

PCAOB

will also be involved in the resolution. But Grant Thornton won't be involved in that resolution, because that audit entity was dismissed

after the fraud was uncovered.

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It's not clear why Grant Thornton was dismissed (and replaced by a smaller audit firm). News reports indicate that the dismissal was based on a "recommendation" from Koss' audit committee. One might think that Grant Thornton was being blamed for failing to uncover the multi-million dollar embezzlement scheme during its audits. (One article notes that it was American Express who brought the

fraud to the company's attention--and not the external auditors, nor the internal auditors.) However, Grant Thornton states that "The fraud was apparently conducted by a longtime, trusted senior financial executive who was hired and supervised by senior management. The company (Koss) did not engage Grant Thornton LLP to conduct an audit or evaluation of internal controls over financial reporting. Establishing and maintaining effective internal control is management's and the board's responsibility."

Those in Government contracting hear a lot about internal control systems and contractor "business systems". As far as we can tell, current DCAA audit guidance tells auditors to expect perfection from DOD contractors, with the slightest mistake potentially imperiling the adequacy determination of an entire i nternal control system. Based on DCAA testimony before the Commission on Wartime Contracting, more than two-thirds of the largest contractors have at least one inadequate control system. But as this story shows, very few systems of internal controls can prevent 100% of fraud and corruption, especially when it is a trusted member of the senior leadership team who is engaging in it.