

### The Origins, Players, and Consequences of White-Collar Crime

“I need a miracle.” This was the last Facebook status update sent to date by Kweku Adoboli to his 400 friends on September 13, 2011. The following night at 3:30 a.m. the handcuffs clicked shut around his wrists. The photo of the star banker with his boyish good looks in a lavender-colored pullover, which was handed over to the police in London by UBS, was seen around the world. The 31-year-old investment banker would be responsible at the final reckoning for losses of around US\$2 billion at the major Swiss bank.

Yet it all started on a relatively small scale—at least by the standards of an investment bank. Adoboli, who had always dreamed of pursuing a successful investment banking career in the most glamorous financial centers of the world, suffered a US\$400,000 trading loss in October 2008. He decided not to register the loss so as not to endanger his meteoric rise at UBS. Instead, he extended the settlement dates for his failed trading activities and thus managed to manipulate his own accounting department and internal controls—in order to buy himself time to cover the loss through other business transactions. His employers were under the impression that Adoboli was bringing in millions of dollars of profit, yet in reality he continued to incur heavy losses. His business transactions became increasingly reckless and more costly, while the illusion he created to try to conceal his manipulation became ever more complex and adventurous. That is until everything fell apart with a bang! It was all uncovered by an unrelenting accountant in the back office, as Adoboli got himself embroiled deeper and deeper in a series of contradictions. The miracle Adoboli so yearned for never materialized and he was found guilty of fraud and sentenced to 7 years in prison in November 2012.

The Adoboli case reveals—in a very vivid and topical manner—a great deal about the nature of white-collar crime, its players, and its consequences, all of which will be presented and reflected upon in this chapter. It is not uncommon for major scandals to start off with small offenses, in whose genesis the personality profile of the perpetrator and his/her motives play a decisive role. Understanding this role and being able to apply the knowledge to the investigation of fraud cases,

as well as to all preventative measures, is a fundamental skill required by all those dealing with white-collar crime.

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## 2.1 White-Collar Crime: A Practical Definition

What do we mean precisely when we talk of white-collar crime? The specialist literature and those practically involved in this area are very divided on the matter. The definitions and key features of this term become blurred depending on the relevant academic discipline or the jurisdiction of the relevant authority. Therefore, there is no generally accepted definition upon which all those involved in social science, political science, criminology, and law enforcement can agree (see Heissner 2001, p. 236 ff.). Does white-collar crime mean crime committed in the economy, crime committed by the economy, or crime committed against the economy? And does white-collar crime only deal with actions that can be penalized according to the statute book, or also with other socially damaging behavior?

The sheer complexity of this phenomenon (see Göppinger 1997, p. 541) and the broad range of possible offenses make it difficult to generalize on this subject. Because even if the term white-collar crime itself were clearly defined, there is still no clear differentiation between this term and equally relevant phenomena, such as corruption and antitrust crimes, that—at least in a judicial sense—form their own individual categories.

For the sake of clarity and practical application, this book will refrain from providing an overly theoretical derivation of the term at this point.<sup>1</sup> Instead, a practical working definition will be derived and explained, which will cover everything that managers in the world of business and, by implication, a forensic audit and crime enforcement authorities come across in their work. This method will help to develop a holistic overview of the subject.

### 2.1.1 Different Aspects for a Comprehensive Understanding of White-Collar Crime

The term white-collar crime can be highly misleading. This is simply because it is so complex and is not uniformly applied as previously mentioned above. The term is eagerly used to describe all manner of different things, from one context to the next, all of which could be encapsulated by the phrase “actions damaging to business.” To be sufficiently prepared to tackle liability issues and the debate surrounding them, it makes good sense to delve a little deeper into the material in order to gain an overview of which “actions damaging to business” are designated as legal offenses by lawyers, auditors, district attorneys, and the police, and what is actually meant when it comes to white-collar crime or corruption.

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<sup>1</sup> Subject covered by, among others, Heissner (2001, p. 25–31) and Hlavica et al. (2011, p. 84 ff).

It is difficult to develop a comprehensive understanding of the phenomenon of white-collar crime due to the existence of such an enormous range of different offenses—all with countless gradations and variations. Depending on the definition, this can start with interns stealing pens and printer paper out of the office supplies cupboard and definitively ends with complex manipulation of balance sheets and unauthorized market speculation as in the cases of Adoboli and Kerviel. It already becomes clear at this point that some offenses are committed at a superficial level for the company—meaning they initially benefit the company—for example, in some cases of corruption. On the other hand, there are also white-collar crimes that are clearly directed against the company, such as breaches of trust or embezzlement. Because there is no legal definition for the term white-collar crime in Germany, the Federal Criminal Police Office (Bundeskriminalamt—BKA) refers to the purely criminal definition of white-collar crime found in Article 74c of the German Code on Court Constitution (Gerichtsverfassungsgesetz—GVG).<sup>2</sup> This stipulates which court is responsible for handling which offenses and defines practically everything that crime enforcement authorities understand to be white-collar crime in concrete terms. This includes criminal offenses:

1. According to the Patent Act (Patentgesetz), the Industrial Design Act (Gebrauchsmustergesetz), the Semiconductor Protection Act (Halbleiterschutzgesetz), the Plant Variety Protection Law (Sortenschutzgesetz), the Trade Mark law (Markengesetz—MarkenG), the Design Act (Geschmacksmustergesetz), the Copyright Act (Urheberrechtsgesetz—UrhG), the Law Against Unfair Competition (Gesetz gegen den unlauteren Wettbewerb—UWG), the Stock Corporation Law (Aktiengesetz—AktG), the Company Disclosure Law (Gesetz über die Rechnungslegung von bestimmten Unternehmen und Konzernen), Limited Liability Companies Act (Gesetz, betreffend die Gesellschaften mit beschränkter Haftung), the German Commercial Code (Handelsgesetzbuch—HGB), the Law for the Implementation of the EEC Regulation on the European Economic Interest Grouping (Gesetz zur Ausführung der EWG-Verordnung über die Europäische wirtschaftliche Interessenvereinigung), the German Cooperatives Act (Genossenschaftsgesetz), and the Reorganization of Companies Act (Umwandlungsgesetz).
2. According to the laws dealing with the banking, securities, stock market, and credit systems, as well as those according to the Insurance Supervision Act (Versicherungsaufsichtsgesetz) and the German Securities Trading Act (Wertpapierhandelsgesetz—WpHG).
3. According to the Economic Offenses Act (Wirtschaftsstrafgesetz) 1954, the Foreign Trade Act (Außenwirtschaftsgesetz), the Foreign Exchange Control Laws (Devisenbewirtschaftungsgesetzen) and fiscal monopoly, tax, and customs law, even insofar as such penal provisions according to other laws are applicable; this is not true if the same action represents a criminal offense according to

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<sup>2</sup> Web link: [http://www.gesetze-im-internet.de/gvg/\\_74c.html](http://www.gesetze-im-internet.de/gvg/_74c.html). Accessed: June 26, 2013.

the Narcotics Act (Betäubungsmittelgesetz), nor a tax offense related to motor vehicle tax.

4. According to the German Wine Act (Weingesetz) and food law.
5. Classified as computer fraud, subsidy fraud, investment fraud, credit fraud, bankruptcy offenses, fraudulent preference and fraudulent preference of a debtor, and anticompetitive agreements for invitations to tender, as well as corruption and bribery in business transactions.
6. Classified as fraud, a breach of trust, profiteering, the granting of an undue advantage, and bribery, insofar as special knowledge of economic life is required to assess the case (Article 74c GVG, see Heissner 2001, p. 28 ff.).

Statistics on offenses and responsibilities of each court as defined in Article 74c of GVG are published, for example, in the Police Crime Statistics (Polizeilichen Kriminalstatistik—PKS) and yearly in the Situation Report on White-Collar Crime (“Bundeslagebild Wirtschaftskriminalität”) by the BKA. The fact that the descriptions of these offenses, as well as the case numbers, should be treated with caution from a practical point of view will be dealt with briefly when we come to examine the actual damage caused by white-collar crime later.

A critical examination soon reveals that the term white-collar crime as it is formally used in Germany is not all-encompassing. Anybody who only counts those offenses that are listed from a legal standpoint under the heading of “white-collar crime” will then be likely to overlook the manipulation of balance sheets, corruption of officials, industrial espionage, or money laundering.

To form a practical overview of all relevant offenses, it is necessary to broaden our view. Therefore, this chapter will initially define in detail what corporate leaders, management boards, managers, and supervisory boards should understand under the term white-collar crime when it is discussed in this book. This means that the following sections will examine offenses that cause damage in companies and destroy assets—and for which company executives are responsible, or even liable, for detecting, solving, and preventing.

This will then be supplemented by offenses in the areas of competition and antitrust law, which are being more strictly regulated on an international and supranational scale, plus the whole area of corruption: from illegally accepting an advantage through bribery payments to the manipulation of invitations to tender and price fixing. Although these are also included, to some extent, in Article 74c of GVG, they almost form their own type of offense due to the large number of legal aspects included in international regulations. This is also valid, to a similar extent, for the areas of IT security, data protection, industrial espionage, and so-called “cybercrime.”

The term white-collar crime takes on another dimension when we examine what is today called “noncompliance”—even if this area already implicitly includes special offenses related to corruption.

A really clear distinction between white-collar crime in its strictest sense and noncompliance is, however, essential to be able to form a comprehensive understanding. White-collar crimes such as fraud or manipulation are, in general, directly

committed against the company. A bookkeeper who sets up imaginary employees in order to transfer salaries to a private bank account is directly costing the company money because capital is being drained away.

In contrast, many cases of noncompliance appear at first glance to be beneficial to the company. For example, if a company gains a competitive advantage by bribing officials or decision-makers in relation to invitations to tender, then it is certainly not detrimental to the company's short-term success—quite the opposite. In fact, it is possible to trace the success stories of whole companies back to a corruption or antitrust offense. Even the types of offenses that do not directly cause damage within the company need to be taken into account to prevent value destruction in the long term.

The Siemens case is likely to mark a significant turning point when it comes to international law enforcement in the area of corruption. The times of openly practiced and silently tolerated corruption are now truly a thing of the past. These types of antitrust offenses are now consistently and professionally investigated and represent a threat to the very existence of even larger companies if the criminal investigations are carried out in a correspondingly committed manner. For example, if profits are disgorged or the offenses result in sanctions such as companies being blacklisted.

### **2.1.2 Alternative Term: “Deviant Behavior”**

Experience working both as a police detective and in forensic auditing has shown that it is, however, necessary to critically evaluate the use of the umbrella term white-collar crime to describe all of the listed offenses. This is because it is not always appropriate nor does it properly reflect reality. The term white-collar crime is also simply too harsh in many cases at a purely human level. Those who seek to understand this phenomenon and its manifestations must be capable of recognizing the people behind the phenomenon and understanding their motives. It is certainly understandable that people need to tell it like it is in order to discourage this type of behavior and to develop awareness of the problem. These crimes are not trivial offenses but in many cases criminal acts—even if the perpetrators aren't wearing balaclavas.

Yet there is also a danger here of overgeneralizing. Again and again we see cases where employees wind up in difficult situations due to personal pressures, the criminal involvement of third parties, or simply due to ignorance—only to then be punished as criminals. Even in the Adoboli case described earlier, it would be a mistake to view the perpetrator as a lone operator driven simply by greed. From a criminalistics point of view, perpetrators are more often products of their environment than we or our own prejudices would like to admit.

An alternative, which could certainly be used as a synonym in this book, is offered by the term “deviant behavior”—a more encompassing description of white-collar crime, corruption, fraud, and all other imaginable cases of infringements against the existing regulations in the sense of noncompliance. The

phrase “deviant behavior” originally stems from the field of sociology and has gradually found its way into the area of criminology (see Dollinger and Raithel 2006, as well as Göppinger and von Bock 2008). In principle, the term describes everything that is not considered adequate or desirable from a business or social standpoint. This does not necessarily mean, however, that they are criminal offenses.

In summary, the term “deviant behavior” is used in this book to describe everything that causes damage from a company perspective—behavior that a forensic audit is designed to detect and prevent. In many cases, this is connected to the liability of supervisory persons in terms of their obligation to protect against and detect this behavior in accordance with German and international legislation, as already explained in Chap. 1.

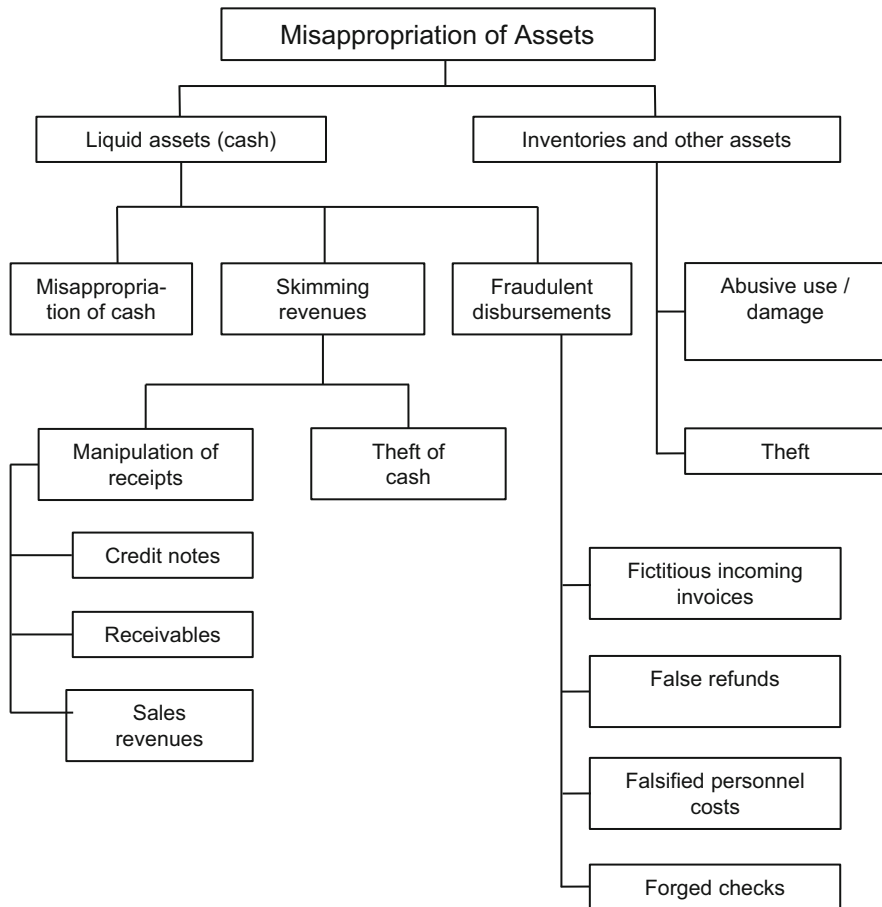
### **2.1.3 Overview of the Relevant Offenses Included Under “Deviant Behavior”**

Any attempt to systemize “deviant behavior” is thus difficult due to the many different forms in which it manifests itself. Nevertheless, a number of different approaches can be found in relevant literature that are dedicated to precisely this task. This book will initially focus on a commonly used approach found in the Anglo-American world for the classification of white-collar crime: the so-called “Fraud Tree” (see ACFE online, for example <http://www.acfe.com/fraud-tree.aspx>) from the Association of Certified Fraud Examiners (ACFE 2013). It divides “deviant behavior” into three main categories from an economic perspective, representing them and their relationship to one another in the form of a family tree. The main categories in the Fraud Tree are Misappropriation of Assets, Financial Statement Fraud, and Corruption. This approach already deviates from the strictly judicial definition of white-collar crime to view the subject much more from an economic perspective.

#### **2.1.3.1 Elements of the Fraud Tree: Misappropriation of Assets**

The assets of a company can generally be damaged in two different ways. One way is as a result of theft or misuse of material goods: such as a warehouse manager who falsifies stocktaking sheets in order to sell goods to criminals on the black market. However, it could also be a manager using the company car to drive to Portugal for a family holiday. What is true for “physical” assets is naturally also true for liquid assets.

In its simplest form, this involves the theft of cash. However, money can also be skimmed off through the manipulation of sales revenues, receivables, or credit notes. In addition, the misappropriation of assets through liquid means can also be achieved in the form of fabricated expenditure. For example, this could be the payment of a fictitious employee, or alternatively, fake incoming invoices, false refunds, or forged checks (Fig. 2.1).



**Fig. 2.1** The ACFE fraud tree: misappropriation of assets

### 2.1.3.2 Elements of the Fraud Tree: Financial Statement Fraud

Financial statement fraud is a special form of the misappropriation of assets and covers six different types of crime. These include misleading statements such as invoicing excessive amounts, crimes in the area of company valuations such as the overstatement of assets or the understatement of liabilities, incorrect reporting period accrual such as booking profits before they are realized, the concealment of expenses and liabilities, and the booking of fictitious revenues, for example, from fake customers or bogus companies (see Hofmann 2008, p. 79 ff.).

From the perspective of criminal law, most of the crimes involved in the misappropriation of assets and financial statement fraud are simply classified as fraud. Fraud in accordance with the definition in Article 263 of the German Criminal Code (Strafgesetzbuch—StGB) always includes deception or fraudulent representation—completely characteristic elements of white-collar crime. This is

also the reason why fraud makes up the largest proportion of cases dealing with white-collar crime (see Bundeskriminalamt, Situation Report on White-Collar Crime 2010).

While the perpetrator who plays the active role in these types of manipulation is generally charged with fraud, the responsible supervisory persons such as management boards or supervisory boards must answer the charge of a “breach of trust.” In accordance with Article 266 of StGB, a breach of trust is classified as a so-called “special crime” that only affects those people that have a “fiduciary duty to protect third-party financial interests” at the time of the crime (see BGHSt 24, 387 in Hlavica et al. 2011, p. 303). Put simply, if a manager, management board, or supervisory board at an incorporated company permits the share capital to be diverted, endangered, wiped out, or used for criminal activities then they are committing a criminal act. A prison sentence of up to 10 years can be handed out in particularly serious cases (Fig. 2.2).

#### **Specialist Information: Special Elements of Fraud<sup>3</sup>**

- Subsidy fraud according to Article 264 of StGB
- Capital investment fraud according to Article 264a of StGB
- Computer fraud according to Article 263a of StGB
- Credit fraud according to Article 265 of StGB<sup>4</sup>

#### **2.1.3.3 Elements of the Fraud Tree: Corruption**

Corruption is divided into two branches in the Fraud Tree: bribery/corruptibility and conflicts of interest. Bribery can take the form of bid rigging or kickbacks—so-called “hidden provisions”—meaning the payment or receipt of bribes. Following the conclusion of a business transaction, this involves a proportion of the amount paid being refunded to one of the parties involved in the transaction.

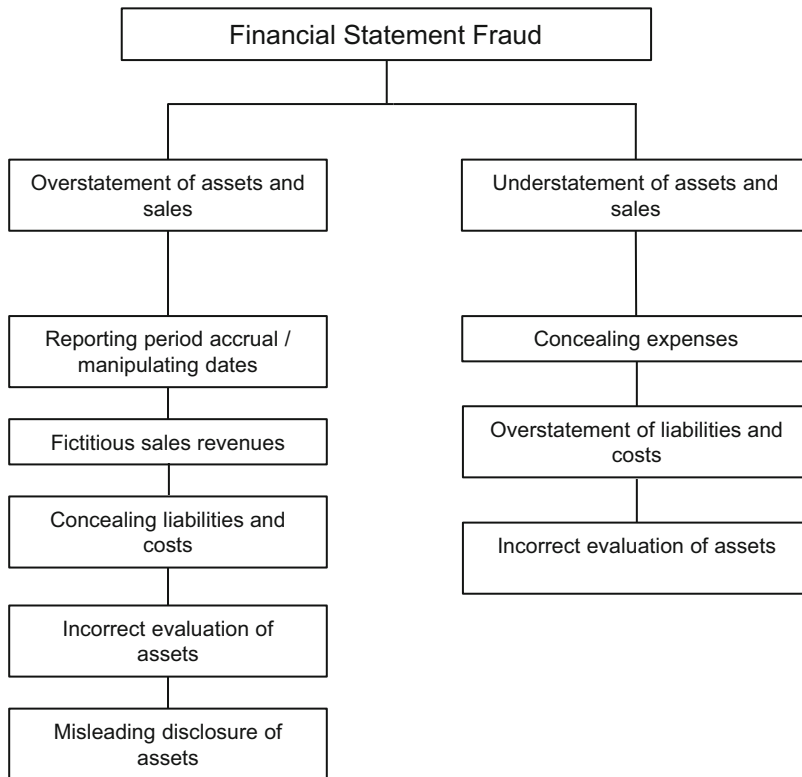
A conflict of interests can develop quicker than one would initially think. If the purchaser at one company, for example, has a good acquaintance in the sales department at another company and they confide in their acquaintance that they depend on the conclusion of the transaction for personal financial reasons, the purchaser already has a conflict of interest, which could possibly lead to the purchase of raw materials or other products at overinflated prices. In this way, a conflict of interest can thus develop in both purchasing and sales.

Just as with the term white-collar crime, there is also no legal definition for the term “corruption” in German criminal law. Depending on who is bribing whom or

<sup>3</sup> The German Criminal Code (Strafgesetzbuch) defines a lot of other special elements in the area of fraud, which go above and beyond the basic definition of the offense according to Article 263 of StGB, in order to close any loopholes in the criminal legislation.

<sup>4</sup> For detailed descriptions see Hlavica et al. (2011, p. 301 ff).



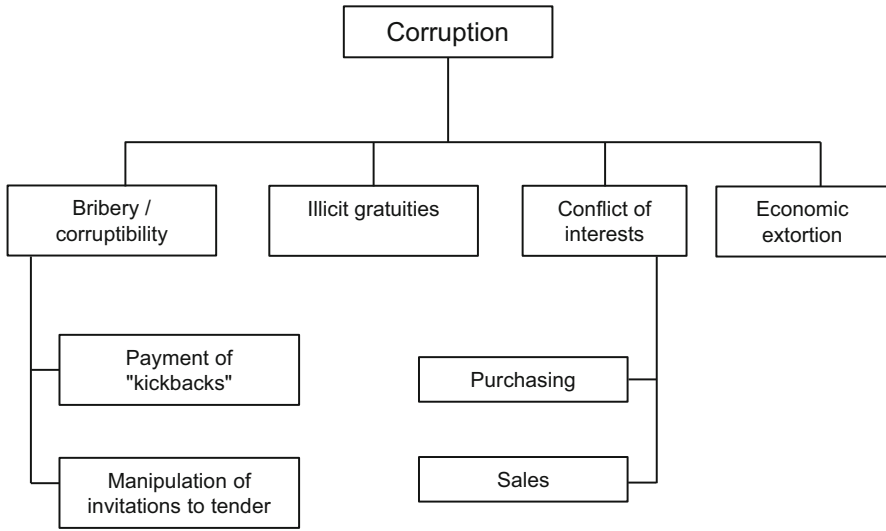


**Fig. 2.2** The ACFE fraud tree: financial statement fraud

who is providing whom with what advantage, different paragraphs of criminal law are valid (Fig. 2.3).

#### **Specialist Information: Elements of Corruption**

- Bribery of voters or members of parliament according to Articles 108b and 108e of StGB
- Commercial bribery according to Articles 299 to 302 of StGB
- Bribery of public officials according to Articles 331 to 335 of StGB
- Other relevant legislation includes the Law on Combating International Corruption (Gesetz zur Bekämpfung der internationalen Bestechung—IntBestG), the EU Bribery Act (EUBestG), and, depending on the nature of the business, the UK Bribery Act and the Foreign Corruption Practices Act (USA).



**Fig. 2.3** The ACFE fraud tree: corruption

This may at first appear to be a comprehensive framework of legislation. Nevertheless, it is not least the businesses themselves who continuously complain that German corruption legislation is patchy and fear that it lacks international credibility. This is emphasized by the fact that Germany has not ratified the UN Convention against corruption to this day.

The bone of contention in the past was the repeated bribery of public officials, which in practice is only punishable in advance of parliamentary elections. Many other forms of corruption are thus not covered: for example, exerting influence on the issuing of public contracts and corresponding “remuneration” in the form of favors or gifts; or one classic form of corruption: the offer of a free vacation on a Spanish finca.

The three main categories of the Fraud Tree from the ACFE are concentrated on corruption and fraud in the area of assets and financial statements. Alongside these crimes there are, however, other special forms of white-collar crime that management boards and supervisory boards need to take into account. Due to their topical nature and liability-related relevance, the following sections will take a particularly detailed look at money laundering and tax and balance sheet fraud—before the list of crimes is complete.

### 2.1.3.4 Money Laundering

Money laundering is a term that should be familiar to everyone from Mafia films. In general, gangsters have the problem of channeling their illegally acquired money into the general economic cycle while attracting as little attention as possible. Any other solution would be too suspicious and merely provide authorities with needless

opportunities for criminal investigations. Therefore, money laundering describes nothing more than the process of integrating illegally acquired money into the legal financial system under some sort of pretense.

This might sound a little far-fetched at first, but banks in particular can experience massive problems with money laundering as a result of their extremely complicated and convoluted financial transaction systems. These mean it is not always clear at first glance which money is illegal and must be laundered. However, the consequences of overly lax controls can prove disastrous: In December 2012, the major British bank HSBC paid a US\$1.9 billion fine because they had been found guilty of facilitating money laundering through dubious transactions.

Naturally, there are not many bankers whose intention at the very beginning is to break arms embargos, launder drug money, or finance terrorism through their transactions. Yet the banker and his superiors must nevertheless fulfill comprehensive international monitoring and reporting obligations using so-called “legitimization and identification checks.”

In Germany, money laundering is a crime according to Article 261 of StGB, while it is regulated on an international stage by a diverse range of laws, regulations, and directives from the EU, UN, OECD, and OSCE.

### **2.1.3.5 Tax and Balance Sheet Fraud**

Tax offenses and corresponding balance sheet fraud are extremely typical examples of white-collar crime that remain hidden for a long time yet cause huge damage over the years.

However, as soon as they are discovered, they quickly attract massive public attention and result in draconian punishments. One reason for this is that both tax fraud investigators and criminal investigators are becoming ever-more specialized and now relentlessly pursue these types of crime.

One recent example saw the business premises of the Deutsche Bank turned upside down by 500 (!) police officers, officials from the tax fraud investigation office, and the BKA during a raid that resulted in the arrest of five employees in the middle of December 2012. Their suspicion was sales tax fraud, tax evasion, money laundering, and obstruction of justice relating to the trade of CO<sub>2</sub> emission certificates. The bank was accused of utilizing the so-called sales tax merry-go-round method in which tax was refunded by the state in advance to bogus companies but never paid back.

In a legal sense, German balance sheet and tax law is probably the most complex in the world. Related crimes are listed according to Articles 369 to 384 of the General Fiscal Code (Abgabenordnung—AO) between tax offenses and tax infringements.

**Specialist Information: Elements of Balance Sheet and Tax Law (Excerpt)**

- Tax evasion according to Article 370 of AO
- Infringement of the tariff laws (professional, violent, and gang-based smuggling) according to Article 372 of AO
- Illegal import or export of objects subject to duty according to Article 373 of AO
- Handling the profits of tax evasion according to Article 374 of AO
- Counterfeiting of money or tokens according to Articles 148 to 149 of StGB

Incorrect or incomplete statements according to Article 370 of AO can relate to tax declarations for income tax and sales tax, but also to notifications and corrections according to Article 153 of AO, or tax benefits such as deferments according to Article 222 of AO (see Harz et al. 2013, p. 83).

Tax infringements usually result in fines in accordance with Article 377 of AO.

These infringements include frivolous tax evasion (Article 378 of AO), minor tax fraud (Article 379 of AO), and illegally obtaining entitlements to tax refunds or tax rebates (Article 383 of AO).

Balance sheet crimes are covered by Article 331 No. 1 of HGB, which sanctions false statements in interim reports, annual reports, statements of affairs, or opening balance sheets with fines and terms of imprisonment of up to 3 years—all members of the corporate bodies authorized to represent the company who were aware of the incorrect statements or approved them are held criminally responsible.

### **2.1.3.6 Other Relevant Offenses and How They Are Dealt with Under Criminal Law**

Even if the already described offenses of fraud, corruption, and manipulation make up the majority of white-collar crimes in Germany, it is important not to forget other relevant offenses and how they are dealt with under criminal law. Depending on the industry sector or the focus of the company, these offenses should be included in the risk analysis to a greater or lesser extent.

This includes, for example, offenses dealing with insolvency. The hectic and emotional nature of an insolvency process provides fertile ground for practically every form of white-collar crime. This ranges from straightforward fraudulent actions in accordance with Article 262 of StGB through to serious crime.

**Specialist Information: Elements of Insolvency Offenses (Excerpt)**

- Withholding social security payments according to Article 267 of StGB
- Forging documents according to Article 266a of StGB
- Delaying insolvency proceedings according to Article 15a of the German Insolvency Act (Insolvenzordnung—InsO)
- Bankruptcy according to Article 283 of StGB

Naturally, it is not necessarily illegal per se for a company to “go bust” as a result of commercial factors. However, bankruptcy becomes a crime if the company’s inability to pay is brought about either through negligence or intentional actions.

A comparatively new discipline in the area of white-collar crime is Internet and computer crime, which the BKA futuristically names “cybercrime” in its overview of the subject. This includes, for example, forming fraudulent networks or “phishing” sites on the Internet, and manipulating or sabotaging computers, which is still covered under the crime of willful damage to property (Article 303 of StGB). As a reaction to the increasing danger posed by computer crime, the legislators have supplemented the legal regulations with Article 303a of StGB “Data manipulation” and Article 303b of StGB “Computer sabotage” (see Schönke et al. 2010, StGB, Article 303a in Harz et al. 2013, p. 168).

The situation becomes even more fascinating when it comes to product piracy and the infringement of intellectual property (Articles 106, 107, and 108 of UrhG, as well as the threat of punishment in accordance with Article 143 of MarkenG) in the unauthorized disclosure and interception of data.

Today, the digital nature of companies and their data has inevitably heralded a new chapter in the history of economic and industrial espionage, the defense against which falls increasingly under the responsibility of top managers—regulated in Germany in antitrust law according to Articles 17 ff. of UWG and supplemented since 1997 in Articles 298 ff. of StGB.

As a result of the major loss of assets in the cases surrounding Jerome Kerviel, Nick Leeson, or Kweku Adoboli, attention has now been focused even more on unauthorized trading and insider trading. While insider trading is defined in Germany according to various articles of WpHG and is punishable with a prison sentence of up to 5 years, the area of market speculation is stuck in a grey zone with respect to criminal law. American legislators and judicature handle insider trading, in particular, much more rigidly: in October 2011, an American federal court sentenced Raj Rajaratnam, head of the unfailingly and mysteriously well-performing hedge fund Galleon, to an 11 year jail sentence and a fine of over US\$60 million for insider trading and conspiracy. It turned out that the stock market guru was extremely well connected among the high circles of the American economy—even receiving exclusive information seconds after the conclusion of important supervisory board or management board meetings. In a subsequent civil process, the SEC issued Rajaratnam with a claim for damages amounting to US\$93 million.<sup>5</sup>

In the area of unauthorized speculation, it is less the criminal dimension and more the liability issues that face management boards and supervisory boards, together with the very high damages awarded on average in these cases, which has created the sense of urgency for preventing unauthorized speculations in

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<sup>5</sup> This sentence is the severest ever issued to date for insider dealing—despite the fact that the social engagement of the perpetrator was already taken into account as a mitigating circumstance.

advance. The technical and forensic capabilities for preventing this behavior will be specifically examined in Chap. 4.

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## 2.2 The Development of White-Collar Crime

A holistic examination of white-collar crime needs to focus of course on more than just the offenses themselves and their liability implications. Therefore, this section will look in more depth at how and why criminality as a whole and white-collar crime in particular develops. What theoretical models exist that can help us to understand this phenomenon? These models already encompass basic features of criminology that need to be taken into account in the design of compliance management systems, even though the development of white-collar crime or “deviant behavior” is too complex and too dependent on individual factors to be represented using a general formula.

### 2.2.1 White-Collar Crime: A Necessary Evil of the Market Economy?

Humans are thoroughly rational animals. Yet the things that make them tick are relatively simple according to the findings of an economic analysis of human actions (see Heissner 2001, p. 282 ff.)—which found they basically strive for self-improvement and optimization. It is thus no coincidence that humans have developed a framework in the form of the market economy that promotes the credo of self-improvement as its highest guiding principle.

If we study cases of white-collar crime long enough, it becomes clear that self-interest—the driving force for social prosperity—also acts as an incentive to step outside the boundaries of what is allowed. The positive energy that our economic system draws from the human drive for improvement is, to a greater or lesser extent, in natural conflict with standards such as laws. After all, not everybody is simply allowed take what they want, even if the basic mechanisms of the market economy ensure that in reality this remains the golden rule.

Therefore, it is safe to say that white-collar crime is a necessary evil of the market economy and will never really disappear from it. As long as people seek their own personal advantage in a competitive setting, they will also defraud and deceive others. An important element contributing to the very existence of white-collar crime is an intrinsic level of uncertainty when it comes to the quality of goods. This basically describes nothing more than a permanent lack of information. If everybody always knew everything about everything, then fraud would be impossible; it would prove futile to offer goods and services at excessive prices, falsify balance sheets, or break promises. The same applies to scarcity: If there were always sufficient contracts for all of the construction companies then nobody would need to seek an advantage through the payment of bribes.

As a result of its inherent characteristics, the market economy thus promotes this type of criminality to a large extent. But anybody who thinks that less competitively

driven economic systems, such as communism, escape white-collar crime and corruption is of course equally mistaken. It was not even possible to ask for directions in Russia in the 1980s without having money or cartons of cigarettes at the ready to offer as bribes. Therefore, the fact that white-collar crime occurs cannot only be due to the systems and their rules. A major role must also be played by humans themselves, who are, in reality, not always the completely rational animals they are portrayed to be, nor are they only driven by self-interest.

At the end of the day, white-collar crime is not a purely economic issue. It is actually reassuring that white-collar crime is just as foreseeable and “normal” inside the factory gates as it is outside of them. Because, when viewed in light of the concept of “deviant behavior,” fraud and corruption are and shall remain nothing more than cultural, sociological phenomena that occur in every situation where people have to manage scarce resources. When white-collar crime can be understood with these points in mind, it becomes a great deal more predictable. This makes it easier to prevent in a systematic way than, for example, capital crimes. Murder and manslaughter are much more frequently governed by emotion than white-collar crime, which is much more carefully planned on the whole.

### **2.2.2 Sociological Aspects in the Development of White-Collar Crime**

What is “deviant behavior”? And what is criminal behavior? In response to these fundamentally philosophical questions, the “traditional” criminologist proposes the following theory: In all its various facets, criminality has always been the result of standardization processes (see Heissner 2001, p. 171). It is irrelevant whether we are dealing with Neanderthals, South Sea pirates, or managers, every society develops its own standards and ground rules over time, irrespective of whether these “social factors” (see Merton 1968) are later introduced into legislation and become subject to social control or not. Therefore, anything outside of the norm can be classified as “criminal.” In simple terms, there is good, and there is evil.

According to the “Labelling Approach” (see Heissner 1996, Sect. 4.2.2), this social control is, however, not only a consequence of criminality but also contributes to criminality at the same time. “The young delinquent becomes bad, because he is defined as bad” (see Tannenbaum 1938, p. 17) is a particularly meaningful quote in this context. It ultimately calls for us to rethink the way in which criminality is explained—to focus not just on the concepts of “outside the norm” or “inside the norm,” but to incorporate much more powerful sociological aspects into any explanation of (white-collar) crime.

Those who look deeper will find that social factors influencing the development of white-collar crime in particular are just as complex and multifaceted as those found in the area of capital crime—and despite common assumptions, they are not always based around money.

This is also the reason why controls and documentation are only the first step in protecting oneself against white-collar crime. At the very heart of every deviant act

lies the person—the person themselves, and the environment in which they live and with which they interact. The following considerations will focus on precisely this point and use the practical knowledge acquired while fighting white-collar crime to help understand, recognize, and, in the next step, prevent “deviant behavior.”

### 2.2.3 The Fraud Triangle: A Standard Instrument for Explaining White-Collar Crime

It is useful to firstly make an important observation. Economists and management consultants constantly try to outdo themselves by producing ever-more wondrous geometric structures to explain white-collar crime in its proper context—using triangles, squares, sparkling diamonds, or rotating cylinders. However, the process of meaningfully simplifying complex phenomena and illustrating them with some geometric form is not easy and often ends in failure.

Nevertheless, it is useful to briefly introduce the so-called “Fraud Triangle” as a standard instrument for the explanation of white-collar crime. This is because it illustrates some important patterns that can act as stimuli for white-collar crime and corruption, which should be considered during the development of a compliance management system. The triangle can be traced back to the 1940s, when it was developed by Donald R. Cressey<sup>6</sup> as part of his dissertation (see Hofmann 2008, p. 204).

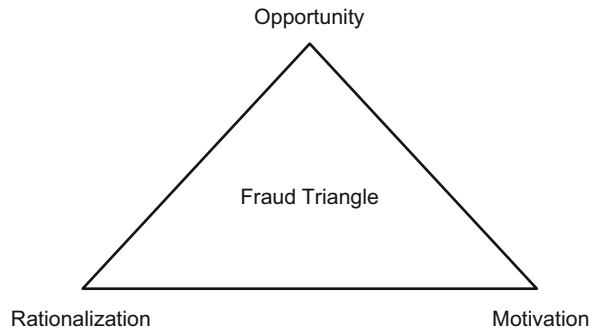
The three corners of the triangle symbolize the conditions required for the development of white-collar crime, namely “Motivation,” “Opportunity,” and “Rationalization.” According to the Fraud Triangle, offenders must experience some form of motivation to deceive, find themselves in an organizational structure that provides the opportunity to commit the crime, and also be able to rationalize the consequences of their actions within their own sense of wrongdoing. Only then will employees become perpetrators—this is the fundamental theory behind the triangle. The Fraud Triangle has long been the source of some dispute among criminologists. The reason is that it encourages us to simplify the extremely complex personal, sociological, or cultural factors that influence a person before and during every action. In addition, this triangle could in turn be used to explain almost every form of crime. The fact is that every single crime creates its own small Fraud Triangle.

Nevertheless, anybody who is keen to understand and fight white-collar crime in their company over the long term can use the different corners of the triangle as points of orientation. In the interests of completing the picture, the three corners of the triangle should be briefly described. This is done from a managerial viewpoint and with the some key points depending on the crime (Fig. 2.4).

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<sup>6</sup>Incidentally, Cressey was a student of the notable criminologist Edwin H. Sutherland, who introduced the term “white-collar crime” to the field of criminalistics and put an end to the perception of criminality as a “phenomenon of the underclasses.”



**Fig. 2.4** The fraud triangle

### 2.2.3.1 Opportunity

The corner of the Fraud Triangle named “Opportunity” is certainly the easiest to control from a management perspective. This is because every opportunity to commit fraud or corruption is synonymous with a weakness in the internal control system. It is necessary for this system to fail before criminal actions become possible at all, and are then allowed to mature in secret. The perfect anti-fraud or compliance management system would remove all opportunity for fraud and thus eliminate white-collar crime at its very roots.

This means that every company, depending on its organization and management, creates the opportunities for its employees to commit fraud itself. Overly complex processes and systems provide perpetrators with an open invitation to conceal and disguise these sorts of crimes.

### 2.2.3.2 Rationalization

There is hardly any other criminal discipline outside of white-collar crime where future perpetrators are inclined to view themselves as the victim to such an extent. Justifications such as “but everybody does it” are often heard, while this attitude is often combined in many cases with a sudden and clear desire for fair treatment. However, it is also possible to manage these reactions in advance. People do not ultimately feel misused or unfairly handled and simply take the idea of “fairness” into their own hands without reason.

### 2.2.3.3 Motivation

The third corner of the triangle is “Motivation.” According to Cressey, this is usually a financial problem that cannot be shared or transferred to somebody else (see Cressey 1973, p. 30 ff.). Particularly when examining white-collar crime, “motive” as a key criminalistics term deserves closer examination, and will thus be discussed in greater detail in the next section of this chapter. Especially because, in contrast to Cressey, practical experience has shown that the various motives that influence the behavior of individual people are considerably more multifaceted than just those that fall into the financial category.

## 2.3 Motives for White-Collar Crime

In principle, the motives behind white-collar crime differ hugely from person to person and from culture to culture. The difference between Western industrial nations and the economic systems in Southeast Asia is particularly notable. What are the reasons behind this different mentality when it comes to the development and rationalization of white-collar crime?

In the last few decades, the Western world has evolved to become much more individualistic and anonymous. In Germany, this can be seen especially in the demographic disintegration of multi-generational households. Wherever these types of social communities along with their inherent value systems are missing, the concept of individualism gains in importance. And wherever “everybody is looking out for number one,” the motives for (white-collar) crime almost inevitably develop—and are expressed—in a wide variety of forms. The decisive question here is: What needs to happen in a person’s head for them to decide to break with their own norms, take unusual risks, and permanently create an illusory world around themselves that needs to be maintained? In general, we are dealing ultimately with people who have received a sound base of values and norms on their journey through life—not with those who have grown up in an environment of complete lawlessness. Every future perpetrator (“deviant”) experiences a shorter or longer period of metamorphosis and ultimately leaves their familiar value system behind. This can be due to a number of reasons.

In the following section, the most common motives encountered by fraud and corruption investigators will be briefly mentioned and explained. This section does not claim to be complete from an academic point of view, but rather it serves to offer a practical understanding of the subject matter.

### 2.3.1 Motive: Pursuit of Social Status

Everybody wants to be successful. Everybody wants to maintain or improve their quality of life and conform to the ideal image of the dynamic, successful social climber promoted by the world of advertising and the media. Therefore, this means that rationalization in America and Europe is primarily about one thing: myself. This is then combined with the pursuit of social status and recognition.

It is especially true that in those sectors of the economy where remuneration is given in the form of bonuses, such as the banking and insurance sectors, employees often find themselves in a situation where they can obtain business transactions through manipulation. Nevertheless, experience has shown that it is not simply “greedy” individuals who are behind fraud cases in reality.

In particular, the intention to achieve “personal gain” is a motive that is heavily dependent on the social environment of the individual. Therefore, the much-quoted concept of “greed” is only a subcomponent of people’s pursuit of social status. And, every now and then, it is possible to identify cases where this clearly plays no role at all.

### **2.3.2 Motive: Feeling of Obligation and Emergency Situations**

In Southeast Asia, motives are often completely different, for example. In the much more hierarchical state and economic systems in countries such as China, Japan, or Korea, it is often the case that families or superiors enjoy unreserved loyalty from an individual that will often supersede their own moral conscience. For example, if a manager in China puts money aside to support his or her family, he or she in many cases will not consider it to be unjust—and will certainly not consider it a crime. Instead, it is a service for the benefit of his or her family and thus an obligation.

Outside of Asia, it is also of course possible that personal and family crises become a motive for white-collar crime. These motives can range from a family dog who needs an operation right through to the provision of expensive medication for parents, grandparents, a spouse, or children when this treatment is not covered by their health insurance—if there actually is such a thing as a health system in that country.

### **2.3.3 Motive: Obedience to Authority**

Obedience to authority can also be a motive for acting in a deviant manner. If all instructions issued by superiors are carried out unconditionally—as is the culture in many corporations—the risk of corruption and fraud also increases. This is because anonymously informing and reporting fraudulent actions, via a whistle-blowing system for example, is not viewed as acting honestly but rather as betrayal. In general, the international fight against crime has shown that this phenomenon is particularly widespread in Asia because Europeans and Americans historically have a different approach to this subject.

### **2.3.4 Motive: Pragmatism**

Economic pragmatism can also become a motive for white-collar crime. For example, take a sales representative in the plant construction sector who has been employed by their company for 30 years or more. In these 30 years, the employee has inevitably developed a certain routine and a “hustling” approach, which has included learning a trick or two. “In some countries it’s impossible to do anything without paying a few bribes” or “everybody does it that way” are typical quotes from these types of employee.

It certainly doesn’t have to be this exotic though. There have certainly been a few very pragmatic bookkeepers who have ensured that their companies have de facto falsified their balance sheets due to incorrect accounting procedures, advance billing, or prepayments—even if they only wanted to help out their colleagues because “it simply wasn’t possible any other way.”

### **2.3.5 Motive: Ignorance**

Although ignorance offers no protection against punishment, it is nevertheless necessary to take into account whether a crime was committed intentionally or through negligence when passing judgment on and sanctioning white-collar crime. Anybody who fails to raise the awareness of their employees and inform them about corruption issues increasingly exposes themselves to the danger that offenses will simply be committed due to ignorance. Employees that genuinely do not know that bank transfers to offshore accounts on the Cayman Islands should, at the very least, be critically scrutinized will subsequently become accessories to the act or even criminals themselves.

Legislation in the area of balance sheet and tax law does occasionally change. A company must ensure that its employees understand and can properly apply these changes. Yet they are often quite simply not aware of the reasons for these changes to the legislation. This situation probably occurred when the practice of offsetting tax for so-called “necessary expenditure” was disallowed. There were inevitably one or two employees that were under the impression that these types of payment just had to be accounted for in a different way. Spreadsheets with the standard field “N. E.” (necessary expenditure) simply continued to be used.

### **2.3.6 Motive: Career Ambitions**

In America and Europe—but also to an increasing extent in emerging countries—an individual’s own career ambitions can clearly become a motive for white-collar crime. Anybody who wants to climb the career ladder at any price will almost inevitably find themselves in a situation where they end up manipulating balance sheets or project results, or intentionally concealing risks in order to look good on their references, work assessments, and CVs.

### **2.3.7 Motive: Boredom**

It may sound banal, but boredom can also be a motive for fraudulent actions. The appeal of testing and pushing the boundaries is deeply anchored in the human psyche and should not be underestimated. Why shouldn’t somebody spice up their gray daily routine in the finance department of a medium-sized company by taking their lead from the pages of a John Grisham novel?

It may even sound a little far-fetched, but boredom is a much more common motive for white-collar crime than one would at first imagine.

### **2.3.8 Motive: Pressure to Perform**

A traditional factor in the development of corruption is the pressure that is placed on employees to perform. In many cases, management personnel underestimate the level of pressure experienced by their employees. If targets are too ambitious or simply impossible to achieve, manipulation and falsification are often the only way forward.

### **2.3.9 Motive: Revenge**

Admittedly, revenge is a much more frequent motive for committing capital crimes than it is for economic crimes. Nevertheless, employees are increasingly placed in situations where they feel humiliated or personally attacked. The credo “I’ll show them” is almost inevitably a factor in crimes such as “pimping” your own balance sheets, through to internal smear campaigns against other employees. The disquiet resulting from these actions can damage the company and ruin whole careers in one fell swoop.

Another dimension of revenge is defiance: “Others are constantly filling their pockets and I’m being left by the wayside? Not a chance!” is a typical excuse for white-collar crime when factors such as defiance and resignation come into play. This motive can occur particularly frequently if an organization has already experienced a certain “level of corruption” and this fact is also known—at least to a latent extent—throughout the company.

### **2.3.10 Motive: Social Recognition**

As mentioned earlier, those who want to properly understand white-collar crime must wave goodbye to the concept that it develops exclusively from monetary motives. Employees in sales and marketing departments are often just yearning for recognition and a pat on the back, or even just to hear two little sentences such as: “Good news that you closed the deal. Well done.” Occasional praise and true appreciation, as well as managers actively listening to their employees, could be enough to prevent some crimes in advance. Praise could also be given in another form: “Good that you didn’t act on their demand for a bribe. It isn’t worth it. We’ll just pull out of the business transaction!”

### **2.3.11 Motive: Peer Pressure**

“Either you are with us or against us.” “This is how it works here.” These are sentences that you are particularly likely to hear in isolated company departments like purchasing or among field staff. The fact that white-collar crime also occurs everywhere where intense group dynamics come into play is due to two human

mindsets: fear of being outcast from the group and the misapprehension that decisions are better when they are made by a group—the so-called “Bay of Pigs Phenomenon” (see Dobelli 2011, p. 17 ff., “Social Proof”).

**Conclusion About Motives: White-Collar Crime Is a Personal Management Issue that Develops on Three Levels** The sheer spectrum of possible motives for “deviant behavior” already demonstrates that the phenomenon of white-collar crime is unbelievably multifaceted, while motivation comes from a much broader background than simply a desire for personal enrichment. Social factors also play an important role. The consequence is that rigid controls do not offer any impenetrable protection against damage because the dynamics behind “deviant behavior” almost always transcend mechanical control systems. There is no question that internal control systems (ICS) are a good idea and important. However, if we take into account the serious sociological and psychological factors at play in the heads of each individual perpetrator then we can come to only one conclusion. The development and prevention of white-collar crime is ultimately a personal management issue involving “soft skills.”

As long as the fight against corruption and fraud remains stuck at the middle management levels of an organization, the corresponding measures will remain reactionary and limited to mechanical controls that do not do justice to the complex sociological phenomenon that is white-collar crime. Practical experience gained from working around the world for one of the big four auditing firms shows that many crimes—or deviant actions—that later result in tangible public scandals could have been prevented if “deviant behavior” had been taken seriously as an element of personal management. This sometimes includes unbelievably banal aspects such as praise for frustrated employees, a firm commitment made to the sales team on clean business practices, or merely having a sympathetic ear for employees and understanding their moods. Indispensable in these situations are the manager’s own belief in what he or she is saying and being able to communicate this clearly.

Personal impressions gained from discussions with colleagues and employees are—with a bit of previous knowledge about criminal psychology and a little practice—probably the most effective method for developing a feeling for the current risks with relation to fraud and corruption. If the company management are disinterested, too proud, or simply not around to talk openly and honestly with their employees every now and then, it is still possible to develop sophisticated control systems. Yet the danger of offenses being committed remains, however, many times greater than if relevant awareness raising and training measures are implemented.

If damaging cases have already occurred or need to be resolved in the company, the process of anchoring awareness for the issue within the personnel management is the decisive factor for success. If the situation involved fraud or corruption, and in the next step compliance, it is fatal if superiors are not really aware of what has happened—meaning how the manipulation was being carried out and how the offense can be prevented in future. It is also dangerous if attentive employees or

whistleblowers are not taken seriously because management boards or managing directors ignore the matter.

Fraud and corruption cases over the last few years have clearly demonstrated that the following is true. Every time there is a lack of commitment to compliance and clean business practices, it is an unspoken invitation for people to carry out criminal acts. This starts at the level of the management board and impacts on all management levels across the whole organization. It may initially sound extremely drastic but all companies are, to a large extent, responsible themselves for the level of awareness they generate on “deviant behavior” via corporate policy and corporate management. In summary, it is possible, when examining how white-collar crime arises in companies and organizations, to define three levels where conditions can be decisive for enabling white-collar crime to develop, thrive, or be prevented.

1. **Awareness of the problem among the management of the company** How does the management of the company deal with the issue of white-collar crime? What do management boards and top-level managers say about the subject? What incentives have really been introduced? The importance of developing an overarching level of awareness for the problem of “deviant behavior” in a commercial enterprise cannot be overstated.

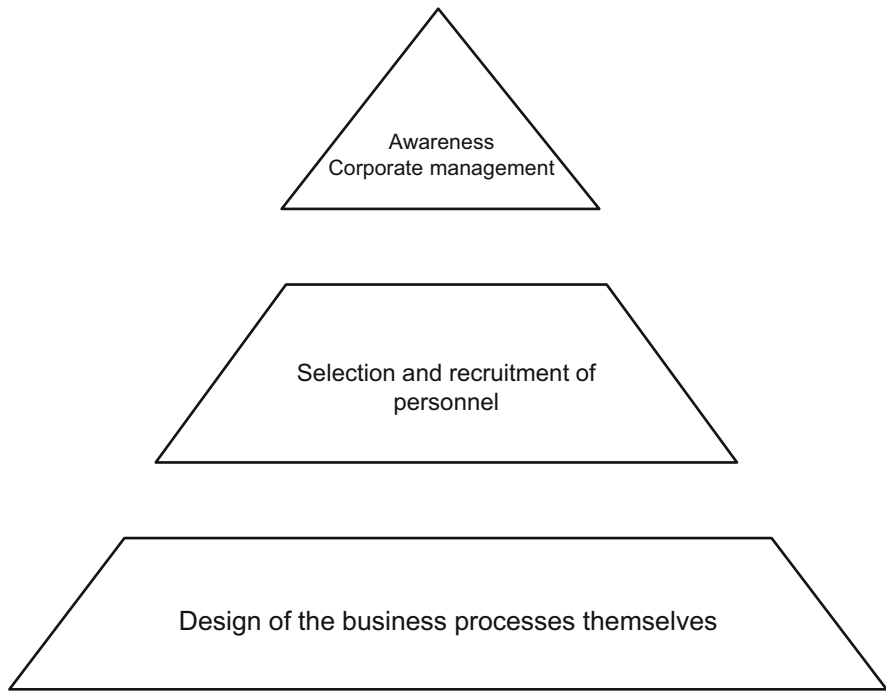
Companies with management teams that either do not take the subject seriously enough or even deliberately look the other way—i.e., create no awareness within the corporate culture—are condemned to somehow come to terms with the loss of assets due to white-collar crime and the threat of damaging penalties and profit disgorgement settlements, as well as personal liability risks. Corrupt leaders will never control a clean company.

2. **Selection and recruitment of personnel** The selection of staff and the recruitment of management personnel has a direct influence on the management culture and the level of compliance. The company once again finds itself at a critical junction that will decisively define how the issue of white-collar crime is confronted in the future. The situation is relatively clear: if I fill my sales team with extrovert, high achievers and issue directives from a management level such as “closing the business transaction is the absolute priority,” no one should be surprised if employees start to pay bribes. Or if I recruit “gamblers” into my investment banking division then I have to accept that risks will be taken. Anybody who thinks that seasoned managers can be taught to act differently is deluding themselves.

The selection of personnel is already a pivotal factor in deciding whether there will be compliance or noncompliance in the company.

3. **Design of the business processes themselves** Ultimately, it is also the business processes that prevent, enable, or even promote white-collar crime because every lack of transparency and every form of complexity facilitates manipulation.

Companies all too often sign up to the “four-eye principle.” Yet once business processes and the basis for making decisions becomes so complicated that the company management are practically no longer able to take decisions, it is only a



**Fig. 2.5** Three levels for the development of white-collar crime

question of time until somebody exploits this complexity to intentionally conceal risks, or to deliberately mislead supervisory bodies. The supervisory boards hold a position of responsibility in this area. It is all too rare for them to actively demand clearly understandable and transparent decision-making criteria—or for them to actually read them.

Something that is complicated can never be completely free of risk (Fig. 2.5).

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## **2.4 Perpetrator Typologies in the Area of White-Collar Crime**

If you are not careful when attempting to explain white-collar crime and identify “typical perpetrators,” you will quickly end up with the same old stereotypes and clichés. The fascinating attraction of this subject, fortified by memorable images of these sorts of crimes on film and television, encourages people to overdramatize the situation. Incidentally, journalists are particularly prone to repeatedly fall into this trap.

Attention is thus quickly focused on ambitious employees striving to climb the career ladder: university graduates in their mid-thirties, with an above-average



income, and a penchant for expensive suits, fast cars, and beautiful women. A description of suave, sophisticated types in the 007 mold. Next down the line of course will always be the quiet, introverted financial accountant who secretly sneaks into the office at the weekend to devote himself to his secret passion: crime. And finally, there is the diligent workaholic, always the last to leave the office and then later, during the court proceedings, everyone will say of him: “It came as no surprise. He was a ticking time bomb.”

And these characters are all naturally linked by their seemingly insatiable lust for money.

Anybody who focuses on these types of fantasies is clearly on the wrong track. In the previous section discussing the motives driving people to commit these types of offenses, it was already possible to demonstrate that white-collar crime is a highly adaptable phenomenon that cannot be adequately described using generalizations. The situation is exactly the same when it comes to perpetrators and their typologies. After two decades working in the fields of criminal investigation and forensic auditing, it has naturally been possible to identify reoccurring criminal profiles. Nevertheless, it would be foolish to claim that there could ever be a universally valid categorization of white-collar criminals—there is quite simply no typical white-collar criminal, just as there will never be typical murderers, drug dealers, or traffic violators. No fraud or corruption investigator or their respective employer should make the mistake at the very onset of focusing on a specific criminal profile, whether this is identifying a “perpetrator of choice” at a certain hierarchical level, or associating the crimes with a particular social class. The world of crime—as has often been shown through experience—is always good for a surprise or two.

### **2.4.1 An Overview of the Perpetrator Typologies**

What turns an employee into a perpetrator? On the one hand, it is of course the right motivation. However, if the colorful assortment of offenses classified as white-collar crime are examined for long enough, patterns start to emerge in which certain types of personality appear particularly frequently. Nevertheless, there are exceptions to this rule.

The following typologies are based on experience gained from fighting corruption and fraud. It does not claim to be universally or seamlessly applicable. However, it is designed to facilitate a better understanding of the origins of white-collar crime—and to help discover corresponding approaches for detecting and protecting against it. By taking a broader view on the subject, a model can be developed that combines the criminological perspective of crime together with the more sociological view of perpetrators. In the fight against fraud and corruption, this then forms a basis from which employees can start to understand risk in their company, or to retrace the development of offenses—thus providing the basic knowledge required for the following chapter on “forensics.”

### **2.4.1.1 The Crooks: Criminals Through and Through**

In already existing criminal typologies, it is amazing that one type of person is almost consistently missing: the crooks. These are people who have simply done nothing else their whole lives except lie, cheat, and manipulate. Not only are they to be found out on the street but also in the office. It is both surprising and alarming at the same time to realize how many people in top management positions at successful companies are quite simply criminals through and through.

This category of perpetrator routinely commits offenses as a matter of course. And with each success they become more self-confident and their inhibitions are lowered. Criminals become really dangerous for an organization when their supposed success in business creates an appearance of genius—and any critical investigation would be viewed almost as heresy. This success usually continues until their self-confidence turns into carelessness and these crooks commit offenses that cannot be overlooked even by loyal subordinates or supervisory boards, or their web of lies simply collapses in on itself.

### **2.4.1.2 The Gamblers: Untouchable**

People who commit white-collar crime are naturally not all bad by definition, nor criminal. A tendency for risk taking combined with corresponding pressure to perform is often sufficient. A good example are gamblers: extrovert, success-orientated, and confident of victory at all times. Americans would call these types of people “overconfident.”

The gambler remains untouchable and unaware of any wrongdoing right up until they are convicted—and in some cases even afterwards. They believe that they are the only ones who understand the world and nobody else has any idea how “business actually works.” The fact that gamblers are employed almost by nature in exposed areas of the company like fieldwork, sales, or distribution should not come as much of a surprise to anybody.

### **2.4.1.3 Free Riders: Particularly Clever**

Free riders are less self-confident than gamblers or outright crooks. They appear everywhere where the actual perpetrators are not able to keep their crimes hidden—or the real perpetrator requires somebody else to cover up their actions. For example, an accountant or controller who covers up kickbacks—or the payment of bribes.

In these cases, “particularly clever” free riders decide not to report this irregularity. Instead, they decide to make a little something for themselves on the side—after all, if everybody else is a criminal why should they forgo their own share? They believe that “it’s going to happen anyway so why not.” It sounds quite practical: Earn a little more on the side without getting your own hands dirty.

Free riders tend to accumulate more frequently in those organizations in which corruption and white-collar crime become almost a natural part of everyday business. As part of the discussion about setting up compliance management systems in Chap. 4, we will once again see how important it is to create the right whistle-blowing system to turn potential mutual beneficiaries into important informants.

#### **2.4.1.4 The Neglected: Being the Hero Just Once**

Another type of perpetrator that is also frequently overlooked are those neglected personalities in the company. In the case of the neglected, their offenses are almost never committed for the purpose of earning more money—at least not in the first instance. These people are much more interested in being the hero for once or receiving some recognition within the company.

Therefore, when the neglected decide to manipulate an invitation to tender for their own benefit, conceal costs, or acquire projects by bribing decision-makers, they are only really interested in one moment: the moment they turn up at the office the next day, somebody pats them on the shoulder and says: “Super, well done.” It sounds trivial but a large proportion of the crimes committed by this group of perpetrators could be prevented in advance by fairer employee management or the actual presence of management personnel.

If management personnel are drowning in their daily flood of e-mails and rushing from appointment to appointment while losing any chance of personal contact with their employees, the chances increase that the neglected will try to obtain attention and recognition in their own way.

#### **2.4.1.5 The Unsuspecting: Good Employees**

White-collar crime does not necessarily have to be combined with criminal energy or particularly devious intentions—at least not at the level it is actually performed. The class of perpetrators described under the banner of the “unsuspecting” demonstrate that it is often ignorance that leads to substantial offenses.

The unsuspecting are actually “good employees” who follow instructions and refrain from questioning the situation. Let us look at the example of a sales manager who wants to generate illegal earnings and asks one of his employees to accept an invoice for consultancy services that never in fact took place—the fee for which should be paid into a dummy account.

If the required awareness about white-collar crime is lacking, the good employee does as they are told and accept what is going on without enquiring any further. They fail to check the services stated on the invoice, and do not seek any reassurances from other parties that they were ever provided. As already mentioned, they are simply doing their job—and making themselves guilty of (or complicit in) serious manipulation.

This situation can also arise when laws change and business practices that were previously permitted are now forbidden. A lack of awareness and training almost inevitably leads to offenses being committed. District attorneys and corruption investigators are not particularly interested whether crimes are committed out of ignorance. A crime remains a crime.

This makes handling convicted “perpetrators” who have in reality “only done their job” even more difficult. In many cases, the unsuspecting simply do not accept that they have done anything wrong. Their justification is ultimately that “we have always done it that way.” In practice, these employees are quickly dropped like hot potatoes without the employer following up the case with the person involved and

examining the background to the crime. Investigating these types of cases often reveals fatal errors in the system.

#### **2.4.1.6 The Lost: Feeling Wretched**

A final class of perpetrators—also often forgotten from the perspective of theoretical sociology—are the lost. This comprises those people who have already become drawn into white-collar crime and corruption and who over time probably cause the greatest damage to companies if management personnel do not identify the situation and offer them a possible exit strategy.

While not meaning to trivialize their actions in any way, a significant number of white-collar criminals find themselves simply “drifting” into crime through peer pressure, the pressure to perform, or for personal motives—and feel wretched about the situation every single day.

The lost generally can’t find a way out of the situation themselves. This is because confessing to their actions would expose them, brand them perhaps forever as fraudsters, lead to the loss of their jobs, and possibly ruin their painstakingly constructed social lives. A feeling of solidarity with, or even fear of, their accomplices can also play an important role. It is not uncommon for those who wish to abandon white-collar crime to fear the consequences of their decision. The results can range from social condemnation and dismissal through to threats and violence.

In this context, there is an increasing demand within organizations for management personnel to develop a feeling of intuition for distinguishing in each case between real manipulators or remorseful perpetrators who are really searching for a way out of a bad situation.

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## **2.5 The Consequences of White-Collar Crime**

There are two approaches for examining the consequences of white-collar crime. One is more focused and direct, and takes the viewpoint of the company. The other provides an overarching, global view from the perspective of the economy in general. For the sake of simplicity, this chapter will only describe the direct consequences for companies and organizations of both major and minor white-collar crimes. The consequences of white-collar crime and corruption as viewed from the perspective of the economy and society as a whole will be subsequently examined in the final chapter of this book.

It is necessary to initially attempt at this point to quantify the actual level of damage caused to the German economy by white-collar crime. However, it soon becomes clear by examining the Situation Report on White-Collar Crime from the BKA that it is almost impossible to reliably assess this damage, which makes any attempts to quantify the actual consequences of white-collar crime extremely difficult.

It is certainly the case that the damage caused by white-collar crime is greater than is often thought, or reports issued by the press or the authorities would lead us

to believe. For example, the BKA estimated in its Bundeskriminalamt, Situation Report on White-Collar Crime (2010)<sup>7</sup> that the damage caused by white-collar crime amounted to 4.7 billion euros. The fact that this at first seemingly gigantic sum only represents a tiny proportion of the damage actually inflicted by white-collar crime, or rather “deviant behavior,” is not clear at all to most.

It is interesting to focus on the statistics issued by the BKA for a moment in order to consider what really lies behind these figures. The Situation Report on White-Collar Crime only actually contains those cases reported to and investigated by the police authorities. Offenses and any associated damage that are detected by internal auditing departments, law firms, or auditing firms, and whose consequences are dealt with internally within the company, are not included in the statistics. The same is also true for cases of corruption, espionage, and other offenses causing damage. All cases of damage resulting from noncompliance that may prove expensive for the company but where the perpetrator is not punishable under criminal law are also missing from the BKA statistics. After all, the police were not required to detect and investigate, and so the crime was not reported.

But that’s not all. Even damage caused by criminal acts that are immediately detected by the public prosecutor’s offices or the financial authorities without the involvement of the police authorities are also missing from the statistics—for example in the event of subsidy fraud, illegal labor, or tax evasion.

The virtual damage caused by white-collar crime—in comparison to the figures taken from the BKA Situation Report—is now sure to have grown considerably.

There are only two other things that we need to add to properly understand the actual situation. If we take all of the crimes that are actually detected and investigated with police involvement, only those cases that resulted in a conviction before the courts would, by definition, make it into the statistics. Should it emerge in a fraud case that the accused was in reality a victim of an evil plot and is acquitted, the court costs, legal fees, and expenditure for solving the case are not entered into the statistics as damage caused by white-collar crime—even when they originated *de facto* within the company.

And last but not least, white-collar crime continues to be a phenomenon in which an above-average number of crimes fail to be reported and thus never appear in any criminal statistics around the world. Therefore, the damage caused by these crimes remains hidden in the rows of files stored at law firms or in the company archives. What is the reason for this? It is certainly dependent on the individual case and the person involved in the crime. However, it is rarer than one thinks that the failure to report these crimes is due to the completely corrupt nature of the organization, the clandestine celebration of criminality in dark conference rooms, or a lack of awareness for wrongdoing. From a purely practical perspective, supervisory boards, management boards, or managing directors often refrain from reporting these crimes in many cases in order to limit damage, or to protect the company from

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<sup>7</sup> These were the most current reports (Bundeslagebilder) available up to February 2013.

the sorts of damage that can prove even worse. Some of these types of damage will now be presented here.

Therefore, we hold to the premise that quantifying the damage caused by white-collar crime is almost impossible for the simple reason that many cases remain undetected, unsolved, uninvestigated, or not even reported. Official criminal statistics such as those provided in the Situation Report on White-Collar Crime from the BKA, and their assessments of the damage caused, thus need to be treated with caution. They only deal with a very small proportion of the total scale of destruction to company assets caused by fraud and corruption<sup>8</sup>—which goes far beyond a purely material perspective.

This almost inevitably brings us to the following question: Which areas of companies and organizations are most damaged by white-collar crime, and to what extent?

### **2.5.1 Extent of the Damage Caused by White-Collar Crime**

White-collar crime never solely results in just material damage alone. In order to fully appreciate the immense difference that can be made today by protecting against fraud and corruption, no one can avoid taking a holistic view of all of the possible types of damage. It is a good idea in this process to move away from merely focusing on figures and to look into the deeper consequences and damage that could be caused by white-collar crime in your own company. Just because it is impossible to express some types of damage in numbers does not mean that they should not be taken seriously. The recent history of fraud and corruption scandals has demonstrated that directly observable financial losses are generally the most harmless type of damage that a company sustains due to white-collar crime. Nevertheless, we will examine this type of damage first, which is purely material in nature and directly affects company assets.

#### **2.5.1.1 Damage to Company Assets**

When white-collar crime is experienced in a company, somebody is certain to ask at the end of the day: “What did it all cost us?” In this context, all of the cash-value assets that were directly lost due to the fraudulent or criminal actions must be calculated. As soon as the first suspicions of fraud or corruption arise, it is important to keep account of the damage and costs involved in clearing up the crimes. This is because the company may have insurance against this sort of damage, or the damages may be legally recoverable from those people involved in the crime in the form of compensation.

This includes all company assets that disappear from the company without the provision of anything in return. Irrespective of whether it is through theft, forgery,

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<sup>8</sup> It is likely that this accounts for a figure in the tens of billions per year; it is not really possible to carry out a valid assessment of this figure for the reasons stated.

or fraud—which occur to varying extents depending on the individual case. The company is thus directly damaged. This can occur in an “explosive” way and be immediately visible or develop slowly over a long period of time in a more concealed manner.

### **A Blessing in Disguise: Promptly Identified Damage**

The first example should be familiar to everybody: money is embezzled or misappropriated and assets are stolen or destroyed. This mostly involves a “one-time perpetrator” who just wanted to land a “major coup”—and failed. The larger the fraud and the greater the damage that has to be concealed, the more conspicuous it is likely to be and the easier it is for a trained investigator to uncover it. Companies that are hit by these types of immediate damage can actually view it as a blessing in disguise. Although the company has to pay for the damage until compensation can be claimed from the perpetrators, or the insurance pays out, the losses are more or less immediately known and have, for example, been quantified and traced by an independent auditing firm. In addition, they do not represent a major threat to the existence of most companies.

### **Every Minute Is Critical: A Creeping Exponential Loss of Value**

The situation becomes more serious when these crimes remain hidden over a long period of time and control mechanisms have either failed, were not available, or have been undermined. If the damage is not directly noticed and the fraudulent activities are too ingenious or complex for the existing prevention systems, the result will be the creeping destruction of company assets.

Even if this “only” results in material damage in the end, the longer the period of time in which a crime remains undetected, the more fundamental the damage will be. This damage can very quickly reach critical dimensions for companies of all sizes. The UBS case surrounding Kweku Adoboli demonstrates this clearly. If you were to plot a curve to illustrate the typical damage caused in these cases, you would find time and time again from a certain point on that the resulting damage no longer increases in a linear fashion but instead shoots exponentially upwards. Why is this the case? Fraud, trafficking, and manipulation are always based on the pretense of reality—thus the more complex a fraudulent act becomes, the greater the investment that has to be made by the fraudster to keep this pretense of reality alive. Money has to be relocated, an increasing number of documents falsified, and an ever-greater number of people bribed to avoid exposure. This is the point at which the truly major damage occurs—when this spiral effect has been set in motion and the internal control systems fail.

#### **2.5.1.2 Damage Due to Fines and Sanctions**

Technically speaking, fines and sanctions could also be classified as material damage, but they need to be viewed much more critically than basic “damage to assets” and thus represent another type of damage caused by white-collar crime. This is especially true in cases of corruption and antitrust crimes. We are primarily talking here about penalties issued in response to manipulation, or fraud crimes

according to StGB, or fines issued in accordance with OWiG for violations of the duty of supervision. These fines can be issued and enforced by courts or crime enforcement authorities. In Germany, the maximum fine that can be issued to managers for violating their duty of supervision according to Article 130 of OWiG is limited to 1 million euros—which does not really represent a deterrent if you compare it to the average wage earned by top managers. Politicians are currently discussing whether to increase this figure from 1 to 10 million euros in order to—in the truest sense of the word—take account of the potential riches to be made from white-collar crime and the bulging wallets of managers.

If we go one step further, we encounter a much more significant type of damage for companies in the area of fines and sanctions—namely internationally enforceable fines, profit disgorgement settlements, and market restrictions that are imposed, for example, under EU law. This naturally deals in the first instance with crimes of corruption such as cartelization, price fixing, and the abuse or granting of privileges in invitations to tender. The international antitrust authorities in the EU and the American Federal Trade Commission have, in particular, not been squeamish when it comes to issuing fines for antitrust crimes. For example, the energy company e.on was ordered to pay 38 million euros for damaging a seal on a room in which EU competition investigators had secured files. e.on already had first-hand experience of the extent of the damage that can arise due to antitrust fines from back in 2009. As a result of price fixing on the gas market, e.on and the French gas importer Gaz de France Suez were each fined 553 million euros. The record EU fine was issued at the end of 2012 to the so-called “TV and computer screen cartel.” The total amount came to 1.47 billion euros.

Although they do not result in quite so spectacular sums of money, international sanctions such as exclusion from certain markets can have even more drastic consequences. Something that may only “hurt” a global player could quickly mean the end of a medium-sized company. In contrast to profit disgorgement settlements for antitrust crimes, it is simply sufficient in these cases to have reasonable suspicion or evidence of a single incident in order for licenses to be revoked and for companies to be excluded from certain markets for long periods. The FCPA represents the legal basis in this area, for example, in the USA. After all, the regulatory authorities in each country decide themselves with whom they want or don’t want to do business.

### **2.5.1.3 Damage to Innovation and Competitiveness**

Corruption in the form of antitrust crime can result in sustainable damage that stretches far beyond the level of any fines issued to companies, affiliated groups, and even whole economic sectors. We are now dealing with truly self-inflicted damage that—once established—can only be put right through a great deal of effort or radical intervention. We are talking here about operating “outside the competition,” when companies simply purchase their sales success through bribery, cartelization, price fixing, or the manipulation of invitations to tender. And then use these methods, at least for a period of time, to simply bypass the competition.



Why is this dangerous and why does it damage companies? The answer is that it prevents the sustainable development of the company because at some point corruption becomes routine. And freeing yourself from this routine is difficult because, on paper at least, the company is performing really well so why should it change anything? But there will never be any real innovation in the company's products and services because their money is invested in bribes instead of in corporate or product development. This is a system that is doomed to failure, particularly in the fast-moving cycles of a global economy. Because the poorer the products become in comparison to the ever-evolving competition, the more bribes need to be paid in order to generate turnover. When it is finally discovered that a huge problem exists in the area of innovation, competitiveness, and product quality, the impact is usually unbearably harsh and extremely damaging.

#### **2.5.1.4 Damage to Public Reputation**

In the wake of, and in reality also often simultaneously to, the fines and the corruption investigations, companies do not only face business-related damage due to white-collar crime. Damage to reputation pushes the effects of white-collar crime into larger and almost impossible to quantify dimensions. This is because the stakeholder relationships with suppliers, investors, customers, politicians, and business partners become strained, or are directly destroyed by publicized cases of white-collar crime.

Trust that has been painstakingly built up, a carefully managed market image, or credibility developed over years can all be blown away in seconds. The consequences can be extremely varied in nature and go far beyond the idea that “now people think badly of us,” to include falling sales, customer and supplier boycotts, impeded access to the capital markets, loss or exclusion from public contracts, and an exodus of employees. These are all short-term or long-term consequences of white-collar crime and corruption. There are then also those companies or NGOs whose public reputation is decisive for their very success or failure. This was the situation at UNICEF (see Leyendecker 2010), where it was revealed in 2008 that money had been systematically embezzled at the organization—the consequence was a massive fall in donations and, for a brief moment, it looked like UNICEF had completely lost its right to exist.

#### **2.5.1.5 Damage to Employees and the Corporate Culture**

At least as serious as the external effects of fraud and corruption scandals on a company are the direct consequences on internal life at a company. These consequences are felt at a number of different levels: heads generally roll when white-collar crimes are suspected, investigated and punished. This naturally involves the perpetrators themselves but also subsequently includes uninvolved persons with supervisory responsibility and, in the final reckoning, the management boards. A company needs really good reasons not to dismiss a manager or management board implicated in the scandal once it has become public. The public pressure is quite often simply so great that a company—then represented in the form of the supervisory board—will also remove high-ranking and otherwise

irreproachable managers from their offices to enable a clean start, or simply to signal that the company is taking the fight against fraud and corruption seriously.

Therefore, companies are almost inevitably forced into the situation where they have to dismiss employees—the type of perpetrator involved or the motives behind the action are relatively academic. In this chapter, we have already seen that we are not only dealing with hardened criminals. The loss of employees results in really serious damage if competition-related expertise leaves the company or strategically important company departments need to be newly staffed.

Something that is also hardly taken into account in Europe when calculating the level of damage is management attention. This means the time required by the highest management levels in the company to deal with these events. It is only logical that while the CEO and supervisory board are busy with white-collar crime and its consequences, they lack the time to devote to their real task—managing the company.

But what happens if there are no personnel-related consequences and top performers are retained at all cost? And what if the company fails to express a clear commitment to transparency, the resolution of the problem, and the implementation of future provisions to the public and the workforce? Experience has shown that everything will then only become much worse because there is nothing that is more damaging to a company's corporate culture in the long term than the feeling that fraud and corruption has not been fairly dealt with. Any company that acts in line with the motto "punish the little guy but let the big guns walk away" is at risk of sustainably undermining their corporate culture. What are the results in these cases? Mistrust, defiance, frustration, rage—practically everything that stands in the way of smooth cooperation and thus healthy value creation in the company—while at the same time laying the foundations and motivation for further white-collar crime.

**Major Damage Develops in Secret** This examination of the different types of damage has shown that the really major damage caused by white-collar crime and corruption in a company develops under the surface. Namely, when misconduct or criminal actions are not immediately identified and dealt with. There are an increasing number of cases in which the original cause of massive damage in a company were trifling matters that gradually grew in scope until they became serious issues.

Purely financial damage is still the least important evil from the perspective of the company management. Those companies who have already suffered significant damage to their public reputation, general competitiveness, or corporate culture are hit much harder.

This makes providing executives and managers with a holistic awareness of this subject even more important because the earlier misconduct is detected, the lower the chance that the damage quietly accumulates under the surface until it finally erupts.

## 2.6 Conclusion: Management Bears the Responsibility

It can thus be observed from an examination of the perpetrators and offenses related to “deviant behavior” that this subject is much more multifaceted and a great deal more abstruse than one would at first think. Anybody who wants to effectively fight white-collar crime and corruption needs to delve deep into the corporate culture and the personal motivations driving their employees.

In the sense in which it has been defined here, “deviant behavior” is primarily a sociological phenomenon that, although there remains an element of surprise, it is possible to anticipate with the appropriate preparation.

Those who understand how white-collar crime and corruption develop in this context cannot fail to be aware of the position of responsibility held by management when it comes to preventing misconduct before it occurs. In many cases, this is possible simply by ensuring clear communication and having a sympathetic ear for employees.

After this examination of the criminalistics and socioeconomic foundations, the next chapter will focus on the concrete steps that need to be followed when it comes to investigating suspected cases of fraud and corruption. What problematic situations are caused by perpetrators and offenses? What are the typical measures used to conceal crime in critical company departments? And what technical and criminalistics methods can be used today within a company in the field of forensics?

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Corruption

Heissner, S.

2015, XV, 184 p. 11 illus., Hardcover

ISBN: 978-3-319-12720-0