When It's One of Your Own

A First-Person Account of Fraud Inside a Bank

by Dave London

Most financial institutions have encountered people who, in debt over their heads, commit an illegal act to get out of their situations. But it's a whole new ball game when the criminal is CEO of the institution. The narrator of this story was a highly respected CEO of a bank that was considered to be among the safest in the U.S. But his risk of choice did not involve syndicated loans, hedge funds, or subprime lending. He went outside the bank. In succumbing to an addiction for gambling, he self-destructed out of home and family and went to prison for committing fraud. He can no longer afford even to pay health and auto insurance. Here is his story.

I am the former CEO of a $300 million bank in Pittsburgh, Pennsylvania. My story's purpose is to give financial institutions one very painful example of how fraud can crop up anywhere inside the institution, the far-reaching effects it can have, and what banks need to do to mitigate the potential for internal fraud activities. And it's not just newer employees that are most likely to commit fraud, nor is it any particular level of employee that is most likely to commit fraud. I was with my bank for 25 years, and I am the one that committed fraud. It all began with a quest for some excitement and luxury.

My first trip to Atlantic City was in the 1970s, and I was hooked immediately by what I saw as the high life. A friend who drove me there, a local businessman, was a high roller, and the casinos loved him. He received comps for food, for drinks, and for lodging. It looked good to me and I wanted it.

The problem with being a high roller was that I found myself gambling longer, more frequently, and for higher amounts than I could afford to lose. The losses started to accumulate and I found it more and more difficult to meet these debts. By the early 1990s it became impossible. I was

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already using 17 credit cards from various institutions to pay off debts. But I didn't commit fraud. Not yet.

To pay back some of the losses, I started sports betting, which I felt would be a sure thing because I had an extensive background in sports. In fact, I didn't lose a bet…during the first year. So my bets grew successively higher, even when I began to lose heavily, to the point of losing $400,000 on one football game.

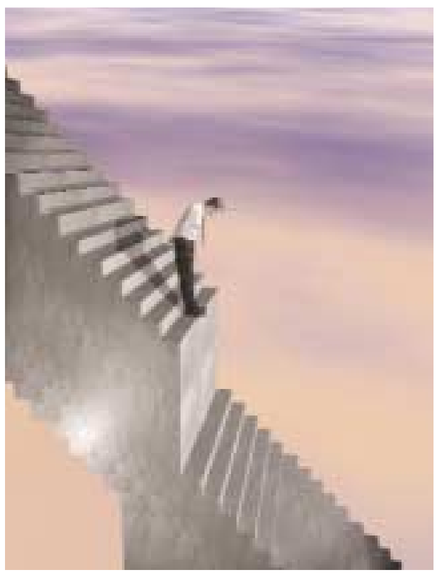
So now I was making sports bets, placed from multiple phone booths so they would not be traced back to the bank, and continuing the trips to Atlantic City, looking for the big win that would put things right. It didn't happen, and my losses grew to more than three-quarters of a million dollars.

Meantime, I managed to function well as CEO of my bank. No one, other than my bookies, knew about my gambling addiction and losses. The secrecy made it even more imperative to find a quick solution. Besides, telling my wife would have meant instantly curtailing the activities to which I was now fully addicted.

And So It Began

My bank's house limit for loans to the CEO was $50,000 in addition to my mortgage. Loans to officers of the bank were required to have the board of directors' approval; these requests were considered at their monthly meetings. I had already tapped out my personal line of credit, so, of course, I had to find a way to obtain money from the bank without my directors knowing that I was directly benefiting from the loans. I found a way.

As CEO of my bank, I could do almost whatever I wanted. So in 1991, I began approving loans myself. From 1991 to 1995, I asked friends to take out personal loans in multiples of $10,000. The proceeds from the loans granted to my friends were issued to them as a cashier's check. They then turned the checks over to me. I cashed the checks at different branches of my bank; I would take only $10,000 and ask for a cashier's check for the balance.



This, of course, was done to keep from being detected through currency transaction reports as required by federal law. I never deposited any of the money into my personal account.

Naturally, I couldn't pay off gambling debts, keep gambling, and make the payments on these loans, so I had to roll them over into other loans. Ten individuals eventually were caught up in my scam.

I repaid the bookies by sending large sums of cash in hundred-dollar bills hidden in magazines or newspapers and delivered by overnight mail. This was, I sincerely felt, the only way out. I also rationalized that there was nothing really wrong in what I was doing.

During this time, I also developed loan schemes involving other local banks. Since I had been with my bank for 25 years, I was personally known and respected by these banks' CEOs. I would go to a CEO and ask for $20,000 to $50,000, telling him that the money was for investments. This was not a total lie, as I was developing a product with a podiatrist friend, and I believed this venture would eventually pay off all the loans. However, the information I had presented to the CEOs was distorted, especially on the debt side; I did not list the individual loans at my bank that were not in my name, and nothing in writing connected me with those loans. In all, I borrowed $300,000 from CEOs of these banks. So now, in addition to 10 friends, seven banks were caught up in my scam.

Paying the Piper

In some ways, I didn't feel my gambling activities and method of paying the debt were much different from those of customers or even some of our board members. Several board members gambled fairly heavily and also borrowed from the bank. A loan was a loan, I felt—proceeds could be used any way the customer so desires. These borrowers were all creditworthy and the loans were not at preferred rates. Most of the board members knew I gambled on occasion; in fact, a couple accompanied me on various trips and others knew of the occasional heavy debt and places I visited.

A woman who was a member of the board eventually caught on to what I was doing in order to pay off my debts. She had learned that a mutual friend had been taking out loans for me. This board member cornered me…several times. She, the mutual friend, and I discussed the situation, and she told me to inform my wife of the problem, get help, and quit gambling. I did, but meantime, our bank's own policies led to the wider revelation of my activities.

An employee in our loan department refused to sign a code of ethics statement about any activity by a director or officer of the bank that was illegal or unethical. This employee had processed some of my loans and suspected that this practice was not appropriate. She went to the bank CFO, who referred her to the board. She sought legal counsel and then went before the board.

The board began an investigation of possible fraud and hired a legal firm to assist in the investigation. Following an audit of the loans, I was suspended from the bank and was asked to leave the building immediately. The board next notified the FDIC, the state's Department of Banking, the FBI, and the U.S. Attorneys office.

I was terminated, as was the COO, who lost her job because the board determined that, as second in command and a friend of mine, she was aware of my conduct and had done nothing. In point of fact, other factors, including jealousy, were at play in employee allegations concerning her behavior. According to reliable sources, she sued the bank and was awarded a million-dollar settlement. Office politics and another disgruntled employee entered into other facets of the case.

Impact and Mitigation

TV, radio, and newspapers all were focused on me and on the bank. Because of the large amount of money involved from my activities and the COO's lawsuit, rumors began that the bank was in financial difficulty and collapsing. Although the bank had previously been in negotiations to merge with another bank, rumors flew again when the bank was sold, and the name of the bank was quickly changed to the acquiring bank's name.

The investigation into my lending practices delayed the merger for more than a year. Massive expenses were created, ranging from employees being paid overtime for reviewing microfilm in tracing back transactions to extra accounting and auditors' expenses. Legal expenses were quite high in my investigation; in addition to my own case, the bank suffered huge expenses over nearly two years in defending the legal action the COO brought against the bank.

Another major impact on the bank was the mass confusion my sudden departure caused among the customers of the bank as well as the employees. The newspapers stated my reason for departure was my questionable management procedures. The employees were told they were not allowed to communicate with me at all; if they did, they would be fired. The acquiring bank also had to place in reserve for loan losses the large amount that I still owed. In addition, the bank set up a contingency fund for the potential of additional legal action against the bank. An employee initiative to set up an ESOP to acquire control of the bank was ruled out as a possibility, mostly because of the situation I had caused.

To mitigate the risks of fraud arising from gambling as well as other causes, banks are well advised to send the board notification whenever their officers or employees have taken out a loan. The notification should go to a review committee comprised of board members.

Also, in my case, a teller who suspected something was wrong was reluctant to report someone of my level. Employees should be able, even encouraged, to communicate directly with the banks' directors, review committee, and the auditing firm if they suspect fraud. Our bank also had weak procedures for reporting currency transactions. Blame could be placed on several possible individuals. However, when it is the CEO of the bank, people tend to back off to avoid repercussions.

How could a man of moderate intelligence have let this happen? It's a question I ask daily. Gambling is one of the fastest-growing addictions in our society. As in alcohol or drug addiction, people don't recognize their problem or admit to having one. My own board is indicative of the extent of the problem. Employees suspected of this addiction—no matter what their level—need to seek professional treatment and enter treatment centers as needed. ❒