

Fox Rothschild Podcast

The Presumption of Innocence Podcast Series: Episode 14

Follow the Money

Featuring Matthew Lee of Fox Rothschild LLP and Michael Shanahan of Alvarez & Marsal

Lee: Welcome everyone to the next episode of "The Presumption of Innocence" podcast. My name is [Matthew Lee](#). I am a co-host of the podcast along with my colleague, [Matt Adams](#). Matt and I are Co-Heads of the [White-Collar Criminal Defense and Regulatory Compliance Practice](#) at Fox Rothschild. We are thrilled to be back with another episode of our podcast.

Today, we are pleased to welcome to the podcast [Michael Shanahan](#), who is with Alvarez & Marsal. Mike is a Senior Director with Alvarez & Marsal's Dispute and Investigations Practice. He's based in Philadelphia, which is where I am. His practice specializes in assisting legal counsel and senior management during financial and fraud investigations, as well as the economic and accounting aspects of litigation.

Mike is a graduate of Villanova University and he holds a number of credentials, including the CPA license. He's a Certified Fraud Examiner and he is also certified in financial forensics. Mike, welcome to the podcast.

Shanahan: Thank you for having me. I appreciate the opportunity to join the podcast and talk a little bit about what I do.

Lee: We're thrilled to have you. Let's get started. Why don't you tell the audience a little bit about your practice and what kind of work you do at your firm?

Shanahan: As you mentioned, I have an accounting background. I'm a CPA and Certified Fraud Examiner. I'm often retained by corporations, either by management, board or their audit committees. They typically need outside counsel to investigate accounting irregularities, bribery, corruption matters or other employee misconduct and theft.

Now, I also get involved in litigation matters, serve as an expert witness dealing with economic damages or accounting issues. One area of particular focus for me is working on behalf of fiduciaries. That's a topic we're going to talk more about today.

Lee: The audience for our podcast, Mike, is white-collar criminal defense practitioners, forensic accountants, and the like, so, sounds like the work you do is going to be of great interest to our listeners.

Let's talk a little bit about the work you do for fiduciary services. Tell us what exactly that entails.

Shanahan: Over the years, I've done a lot of work on behalf of fiduciaries. Think of a trustee or a receiver that's appointed in a matter. Those matters may arise out of a bankruptcy. An example of a matter that arises out of a bankruptcy could be a trust that's created to enhance value for a group of

unsecured creditors. Another example, and I think this is an example that would be a particular interest to your listeners, would be an example of when the receiver is appointed to wind down a fraudulent scheme, such as a Ponzi scheme.

Lee: What exactly is a receiver or a receivership? Can you just give us a little basic background on that concept?

Shanahan: A receiver would be an individual that's appointed to take control of an entity, perhaps following, let's say, the SEC files an action to stop a fraudulent scheme, a Ponzi scheme. One of the remedies that they may move for is the appointment of a receiver to come in and take control of the entities and possession of the assets.

Lee: One of the fraudulent schemes that we read a lot about, and a lot of our listeners often get involved in, are Ponzi schemes. That seems to be a pretty common fraud scheme, where you might see a receiver that's appointed. Can you talk a little bit about your work in that area and perhaps give us some examples of some cases where you've been involved in that situation?

Shanahan: In my experience, when we're talking about a Ponzi scheme, as I mentioned before, that the SEC will file a complaint and one of the remedies that they would seek is the appointment of a receiver. The receiver will be appointed by the court. It's possible that in conjunction with the appointment of the receiver, the SEC may also move to appoint a financial advisor, or they may give discretion to the receiver to retain that position and that's typically the role that I would serve in, would be the financial advisor to the receiver.

Lee: So the primary goal of the receiver, or the primary mission of the receiver, is to figure out where the assets went and try to recover them for the benefit of the victims in the case of a Ponzi scheme. Is that right?

Shanahan: Yeah, that's exactly right. Hit the nail right on the head.

Lee: Can you talk to us about some matters that you've been involved in and what your specific work entails?

Shanahan: The one matter that comes to mind is a hedge fund or an investment scheme that raised about a hundred million dollars of assets or capital to be managed. The investors in that scheme thought that they were investing into a fund that would then, in turn, invest into traded equities. In reality, what was occurring is their money was just being used to finance the extravagant lifestyle of an individual.

So, how the scheme unwound is, and as you can imagine -- a Ponzi scheme for those that are not familiar is a scheme where the existing investors, in order for an existing investor to be paid off to redeem their investment, new investors have to contribute capital. If you think about that, it's really impossible for that scheme to continue in perpetuity.

At some point they're going to run out of money. In this one instance, that's exactly what happened. There were investors that were interested in redeeming their investments and at some point the fraudster was unable to keep up with those redemption requests. And they were left with a group of investors who were demanding their repayment and were unable to get that.

That caused them to go to the SEC and file complaints to initiate an investigation.

Lee: Are you assisting the SEC in that matter or working with federal prosecutors? How do you fit in the overall investigation?

Shanahan: Good question. In that particular instance, the SEC moves to appoint the receiver and the receiver retained me as the financial advisor with a goal of a couple of steps. First and foremost, understanding factually what occurred. I usually simplify it and say, where did all the money come from and where did all the money go to? You have to perform an investigation to develop sufficient information and facts in order for you to bring affirmative causes of action, in order to recover money for the defrauded investors.

Lee: What does that look like? Or what does that entail or what are the types of actions that you can pursue?

Shanahan: In a Ponzi scheme, you often hear the terms "net winner" and "net loser." The investors themselves, they either got more money out of the fund than they put in when it stopped, or they were left with a loss.

A net winner is someone who received more principal or received more than they invested, whereas a net loser didn't get all their money back.

If they received more than they contributed to the fraud, what they thought when they made the redemption is that redemption was actually a receipt of profits. Because as the fraud's going on over the years, you may put some money in and you receive statements that say, "I made 10%, I made 20% each year." And you believe your investment grew by some amount. Then you redeem your investment. You take all that money with you.

In reality, given that the funds weren't invested as they were supposed to be and they were funding an extravagant lifestyle of an individual, what you received was not actual profits, but you received someone else's money.

The court allows to bring a cause of action or claim to recover the amount of your net winnings, assuming you redeemed that amount in good faith. That's one of the first steps that we take to understand is, who are the investors? How much money did they contribute and how much money did they receive? Who are the net winners and who are the net losers? That's one of the first steps I would say that we take in the investigation, because then we can begin bringing litigation if we need to. Or, we can make payment demands of the net winners. If they're not willing to return the money, then we can pursue litigation against them to recover those funds.

The other area that we look at would be third-parties. So, are there accounting firms or financial institutions that perhaps were negligent in their duties and have some potential liability to the investors that we could potentially pursue?

Lee: Mike, I assume in some of these more complex fraud investigations tracing the money could be pretty difficult, particularly if you've got sophisticated fraudsters that are using techniques to hide money. How do you go about finding the money, and how difficult is it?

Shanahan: Cash is king, right, Matt?

Lee: Indeed.

Shanahan: It really is about, as you said, it's following the money. First and foremost, we need to identify all of the financial institutions and financial accounts that were utilized in the fraud. Then, it's gathering that information and ensuring they have a comprehensive set of the books and records. Whether that be records directly from the financial institutions, coupled with books and records that were maintained by the defendant entities and reconstructing from that information the actual cash flows, the cash inflows and cash outflows that occurred.

Lee: What if you uncover in the course of one of your investigations that money has been moved offshore. It's no longer in the U.S. financial system. How hard is it for you to trace money and recover money that's been placed outside the jurisdiction of the United States?

Shanahan: It certainly adds a level of complexity to an investigation when funds are moved offshore, but it doesn't mean that those funds are beyond the reach of, in this instance, a receiver.

Now, you may need to retain local counsel in whatever jurisdiction the funds were moved to in order to attain documentation or bring a cause of action against the party that ultimately receives the funds. But you still have a path to recover those monies, assuming they were paid to a party without any reasonably equivalent value exchanged back to the distributing entity.

Lee: Oftentimes, Mike, I assume that in the course of your investigation of, say, a Ponzi scheme, there is a parallel criminal investigation and/or prosecution underway of the fraudsters. Can you talk a little bit about how your investigations interact with a parallel criminal investigation? If they do at all.

Shanahan: Oftentimes our investigation is starting on the back end of the criminal investigation. By the time the SEC files their action and moves to a point of receiver, usually the Department of Justice is already well into the criminal investigation. It's not that uncommon for the individual that was perpetrating the fraud to be arrested on the same day that the SEC files their action. Criminal charges are brought simultaneously.

Lee: Do you find that prosecutors and/or federal agents are willing to share information from their own investigations with you to help you in your work on behalf of the receiver?

Shanahan: They are. I think it depends on the circumstances. I've had instances where the federal government has been very willing to share. It really was the view towards ensuring our investigation is conducted as efficiently and cost effectively as possible. But I've had other experiences where perhaps there are other parallel investigations ongoing, and because of that, the government is a bit more guarded in the information that they will share with us.

So, it really depends on the circumstances of the case and if there are other investigations ongoing around the Ponzi scheme or individuals that were involved.

Lee: I assume it's part of your investigation: One of the things you're interested in doing is talking to as many people as you can to get information about where money may have been stashed or moved. How difficult is it to get people to talk to you? Because I assume that if there is a swirling criminal investigation, you may have some individuals who are unwilling to talk, asserting the Fifth, or worried about incriminating themselves if they talk to anyone, whether it's government or someone working for a receiver like you. Do you run into those difficulties in trying to get information from witnesses?

Shanahan: You can at times. I would say, sometimes, as you know from your time as a prosecutor, it may be in the best interest of the individual that's charged with perpetrating the crime to cooperate, as that could be a reduction to their sentence, or at least a reduction and the points for their sentence.

When it comes to other individuals, I think you've kind of hit the nail on the head. Other individuals that feel they may have some exposure will be more guarded and unlikely to cooperate with our investigation.

Lee: Mike, have you ever had the opportunity to testify in court in one of these receiver cases?

Shanahan: I have. So, I've had the opportunity in cases where the government has used me in the criminal prosecution of the individual that was perpetrating the crime.

Lee: In these cases when you have been called to testify in court, are you testifying as an expert witness or as a fact witness or perhaps both?

Shanahan: I've had the opportunity to testify as both. I've had instances where I've been put forward as a fact witness to speak to and testify to the fraud and how it occurred. Then I've also been put forward as an expert to speak to the damages or losses that were suffered by the investors.

Lee: Mike, as you know, one of the areas that I practice in is tax. So, I can't let this episode go by without asking you about taxes. Tell us a little bit about how you deal with tax issues that might come up in the course of an investigation. For example, what, if you, in the course of your investigation, determine or discover that there's some unfiled tax returns.

Or, I guess worse, some tax returns that have been filed, but aren't accurate. How do you deal with those tax issues as they arise?

Shanahan: I'd be interested in your take, cause I think you just described the two scenarios that we encounter when taxes are not filed or when the taxes are filed based on fraudulent financial statements.

In an instance where taxes are not filed, one objective of the receiver is to wind the entities down. In order to wind the entities down, we need to resolve any tax liabilities. So, I'm actually interested in your perspective and your take on, how do you address winding an entity down when that entity never filed tax returns?

Lee: I assume the IRS would insist on the receiver filing at least some of the returns for which the statute of limitations is open and ensuring that whatever taxes are due, probably with interest, perhaps even penalties, are paid in order to properly wind down the entity. I assume that's the position the IRS typically takes when these situations come up in your investigations. Is that right?

Shanahan: That is correct. That's a position. I would say often to the extent there's a reasonable basis or defensible position to not file historical tax returns prior to the appointment of the receiver. When you're talking just about a scheme that was purely fraudulent, there's no legitimate business, it's just purely a fraud, it's in the best interest of the investors to not have to incur the cost of preparing historical tax returns. The IRS may not always agree with that, but from a cost effective perspective for the investors, that's the best approach.



When we have instances where the receivership entities file tax returns based on fraudulent tax returns, that usually means it has generated some sort of tax liability. That the perpetrator of the fraud was filing tax returns and reporting income in order just to perpetrate the fraud or continue to perpetrate the fraud.

In those instances, what we would evaluate is whether or not we have the ability to file amended returns and recover the taxes that were paid to the IRS or to any tax in the fraud.

Lee: That concludes this episode of "The Presumption of Innocence" podcast. Again, I am Matthew Lee, Co-Chair of the White-Collar and Criminal Defense Practice at Fox Rothschild. I'm based in Philadelphia.

I want to say a big thank you to our special guest today, Michael Shanahan. Thank you very much for coming on to the podcast. Really appreciate you sharing your insights and talking about your practice. Mike is a Senior Director at Alvarez & Marsal based in Philadelphia. We really appreciate your time today, Mike. So thanks for joining us.

Shanahan: Thanks for having me, I really appreciate you having me on.

Lee: Stay tuned for an upcoming episode of "The Presumption of Innocence" podcast.

Thank you for joining us today.