Hospitality Fraud and Corruption

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Fraud and corruption continue to be a major issue for hospitality companies – particularly given continued focus on corruption risks in emerging markets and an uptick in fraud occurring in loyalty programs. This presentation will highlight the various areas where fraud and corruption have permeated the hospitality industry, and examine some legal tools used to combat this kind of fraud and corruption including actions by the Securities & Exchange Commission (SEC), the broad applications of the Foreign Corrupt Practices Act (FCPA), and best practices for hospitality compliance programs. Additionally, the seminar will offer valuable insight and analytics that can help hospitality businesses deal with this increasingly problematic area.

Background

The SEC and FCPA

The SEC has implemented a number of special tools in its efforts to enforce fraud in hospitality and other industries. First, the SEC created a Financial Reporting and Audit Task Force that look at trends and patterns of conduct that are risk triggers for financial fraud, including areas relating to revenue recognition, asset valuations, and management estimates. Financial statements are also reviewed for red flags. Crowdfunding and Jump-Start Our Business Start-Ups Act ("JOBS") are two mechanisms by which fraud and corruption occurs; in response, the SEC has made rules, particularly to the JOBS Act, that limit the monetary amount that can be raised in a 12-month period to $1million.

Given the increasingly globalized economy, the FCPA has become a popular way for the U.S. government to combat fraud and corruption practices. The FCPA applies broadly to hospitality businesses that (a) maintain some formal tie to the U.S., and (b) commits an act in the U.S. that constitutes a violation. Traditionally, industries including oil/gas and engineering were the primary targets of the regulators, but the industries have expanded to include telecom, entertainment, financial services, and hospitality.

Compliance Programs

It is important that hotels implement compliance programs (and be sure their vendors are as well). Programs should have sufficient staffing and resources after considering a hotel's size, structure and risk profile. Senior executives should be responsible for oversight, and corporate leaders should be diligent about creating a "culture of compliance" that is reinforced at all levels. Policies should be clear, concise and accessible to all employees, and updated periodically to reflect changes the hotel experiences (i.e. an acquisition or merger). Training and continuing advice are necessary—and should be comprised of covering company policies, instruction on applicable laws, case studies and practical advice to address real life potential scenarios.

Hotels need to conduct due diligence, and undertake ongoing monitoring steps, including audits, employee surveys, periodic training exercises, and third-party compliance certifications. Disciplinary

measures should be appropriate and clear, and hotels may want to implement compliance incentive programs including internal recognition.

Loyalty Programs

Loyalty program fraud continues to be on the rise, particularly in the airline and hospitality industries. Loyalty program fraud can be grouped into three main categories: fraud by employees, fraud by business partners, and fraud by criminal organizations. The first two categories of fraud have plagued loyalty programs for many years, with mixed responses in terms of security efforts. In 2011, a former sales manager of a Marriott Renaissance hotel gave herself enough Marriott rewards loyalty points to purchase $103,000 worth of goods from a SkyMall airline catalog, with the goods later sold for cash. The third area regarding criminal organizations has recently become a major problem for hospitality and other credit card points-related business.

In order to limit liability and overall risk, hospitality businesses must safeguard their reward programs. That includes program guidelines, controls and a monitoring process. Here are some examples.

- Red flags for potential loyalty program infringement/fraud

    o A surge in employee access and time spent on the customer loyalty database

    o A variance in redemption activities

    o Repeated unsuccessful login attempts to the rewards website

    o New shipping addresses or other uncommon updates to customer profiles

This session will additionally focus on the need, as well as the opportunity, to leverage data across a hospitality entity's individual business units to enhance decision quality, combat fraud and corruption, nudge behavior and increase a hospitality owner/manager's ability to highlight what was previously difficult to ascertain. Particular focus will be paid to technology and visualization tools, enhancing data quality with third-party or external sources and advanced analytic methodologies.