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The Truth About Fraud... It Can Be Prevented

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YOU CAN'T FOOL
ALL THE PEOPLE
ALL THE TIME...
BUT, YOU CAN
COME PRETTY
CLOSE.



... What is Fraud?

- Intentional material, false statement or willful omission of material fact, either orally or in writing.
- Knowledge by the perpetrator that the statements or omissions are false and misleading.
- Intent for the misrepresentation to be acted upon.
- Reliance by the victim on the statements made.
- Damage to the victim who relied upon the statements.

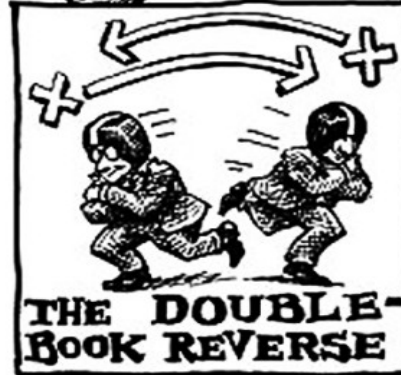




... Occupational Fraud

- **Occupational frauds** are those in which an employee, manager, officer or owner of an organization commits fraud to the detriment of that organization. The three major types of occupational fraud are: *Corruption, Asset Misappropriation* and *Fraudulent Statements*.
- The complete classification of occupational fraud, frequently referred to as the Fraud Tree (next slide);
- Committed for the purpose of the direct or indirect financial benefit to the perpetrator;
- Costs the employee's organization assets, revenues or reserves

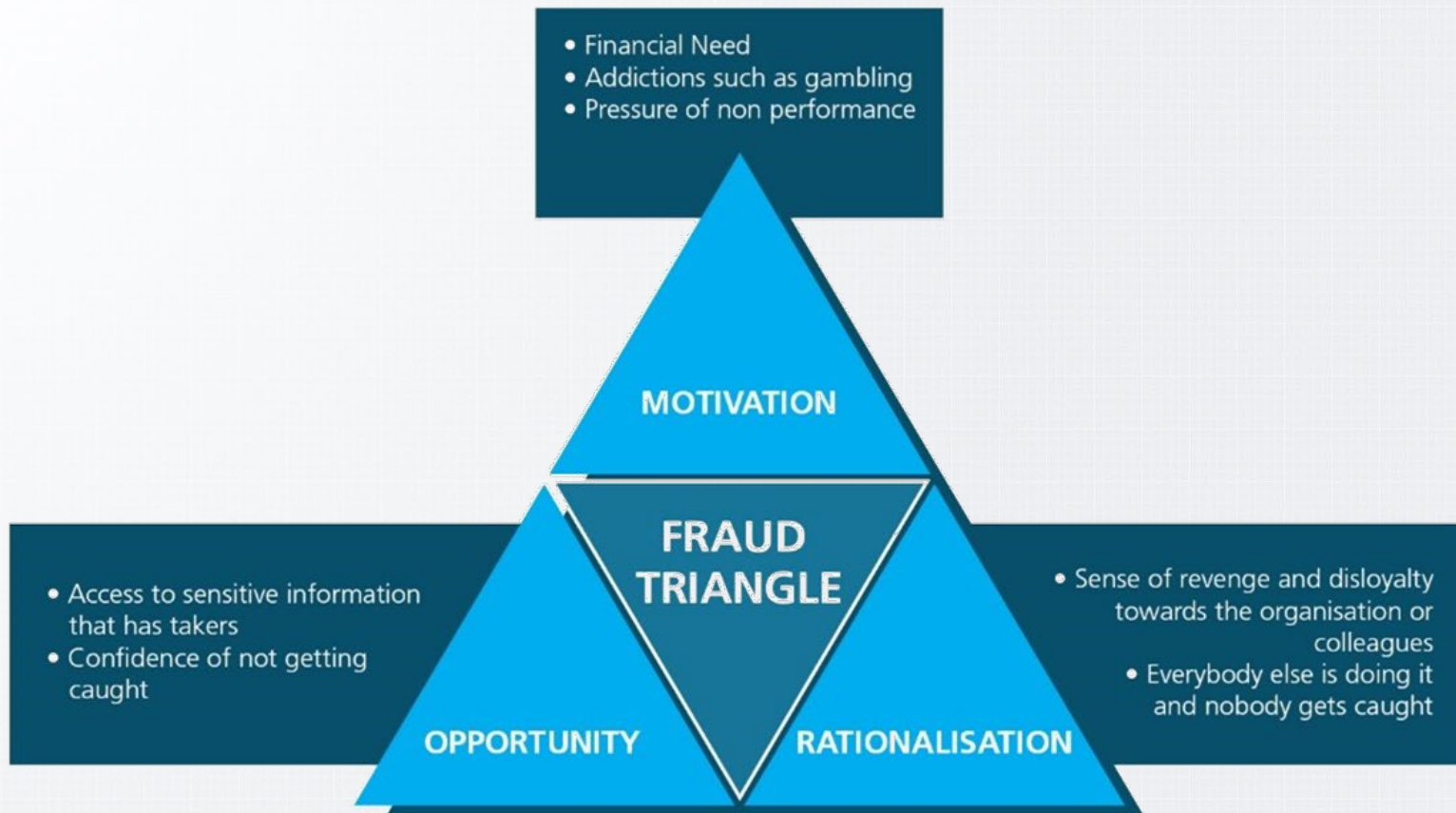
CORPORATE ACCOUNTING PLAYBOOK



M. WUERKER

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Fraud Triangle



... 2018 ACFE Report to the Nations

2,690

real cases of
occupational fraud

from

125 countries

in

23 industry
categories

\$7 BILLION+

IN TOTAL LOSSES

\$130,000

MEDIAN LOSS PER CASE

22%

OF CASES CAUSED
LOSSES OF

\$1 MILLION+



Median duration
of a fraud scheme



MONTHS

CONCEALING FRAUD

An act of fraud typically involves not only the commission of the scheme itself, but also efforts to conceal the misdeeds. Understanding the methods fraudsters use to cover their crimes can help organizations better design prevention mechanisms and detect the warning signs of fraud.

TOP 8 CONCEALMENT METHODS USED BY FRAUDSTERS



Created fraudulent physical documents



Altered physical documents



Created fraudulent transactions in the accounting system



Altered transactions in the accounting system



Altered electronic documents or files



Destroyed physical documents

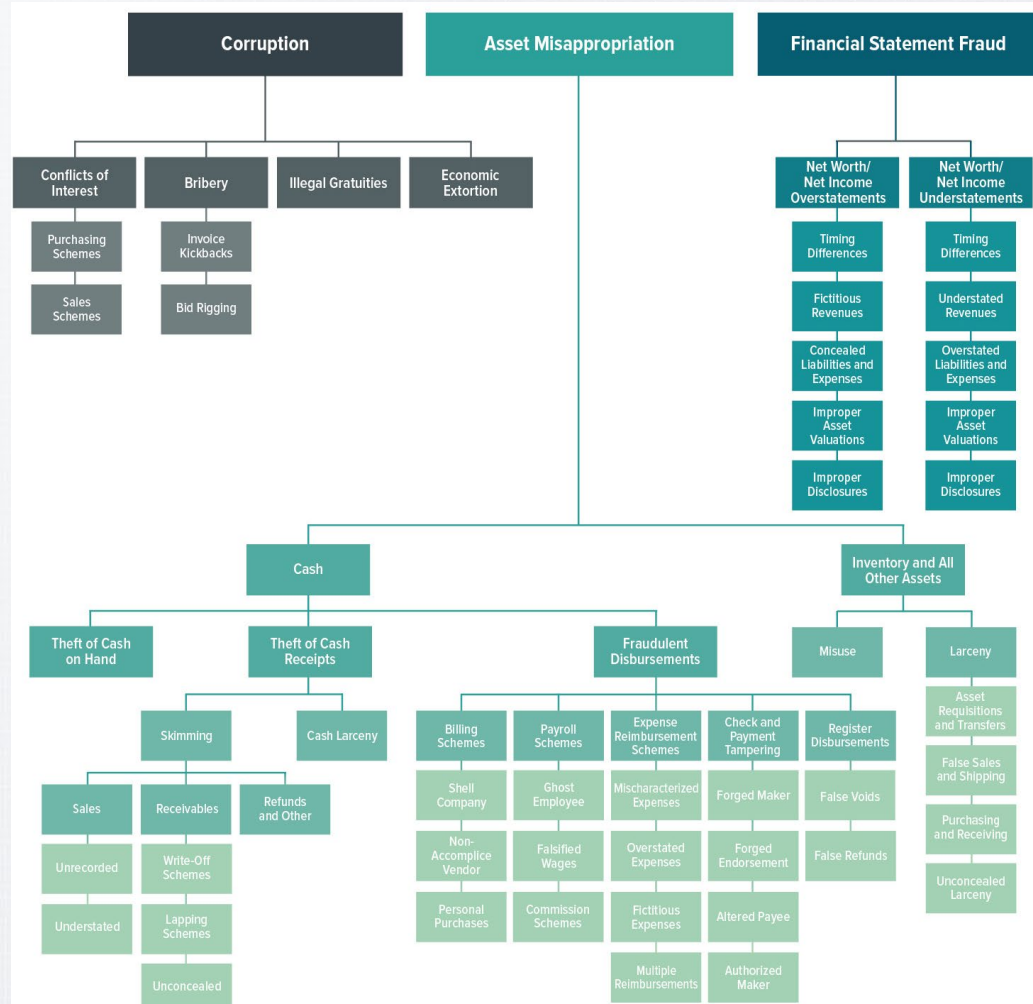


Created fraudulent electronic documents or files

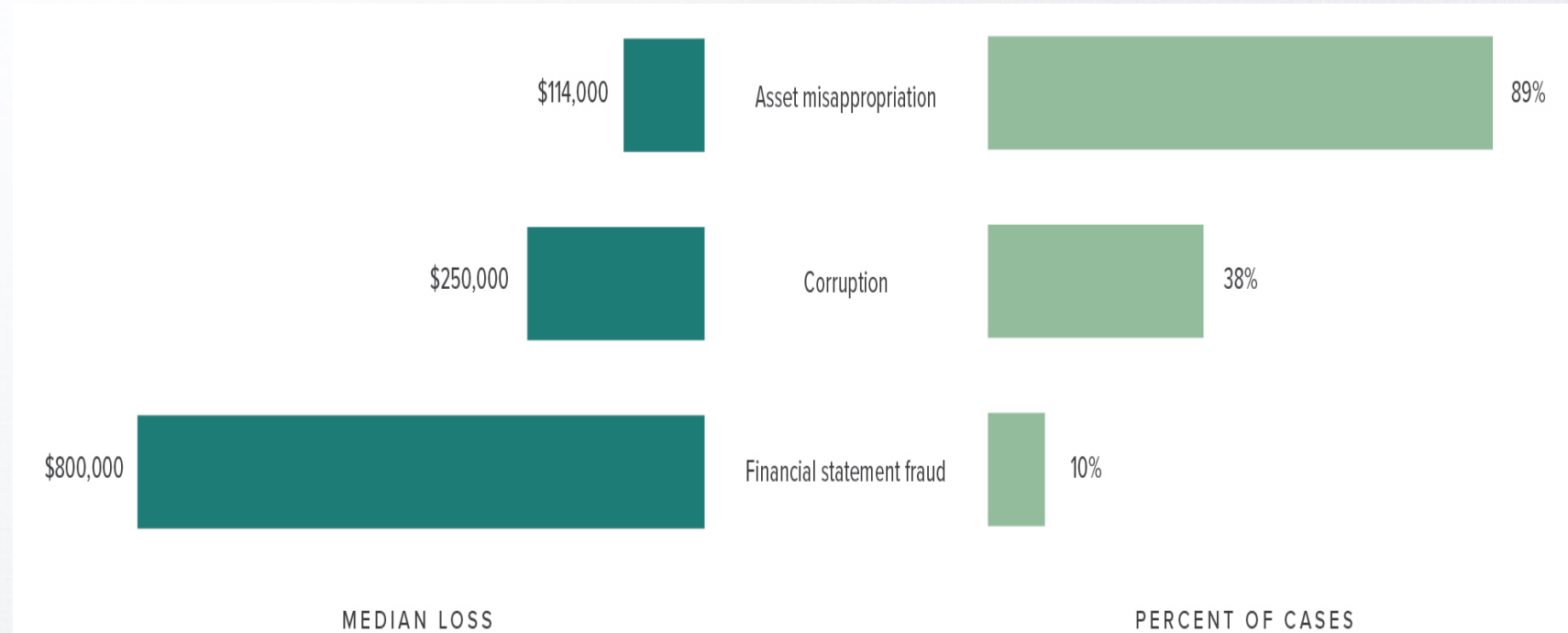


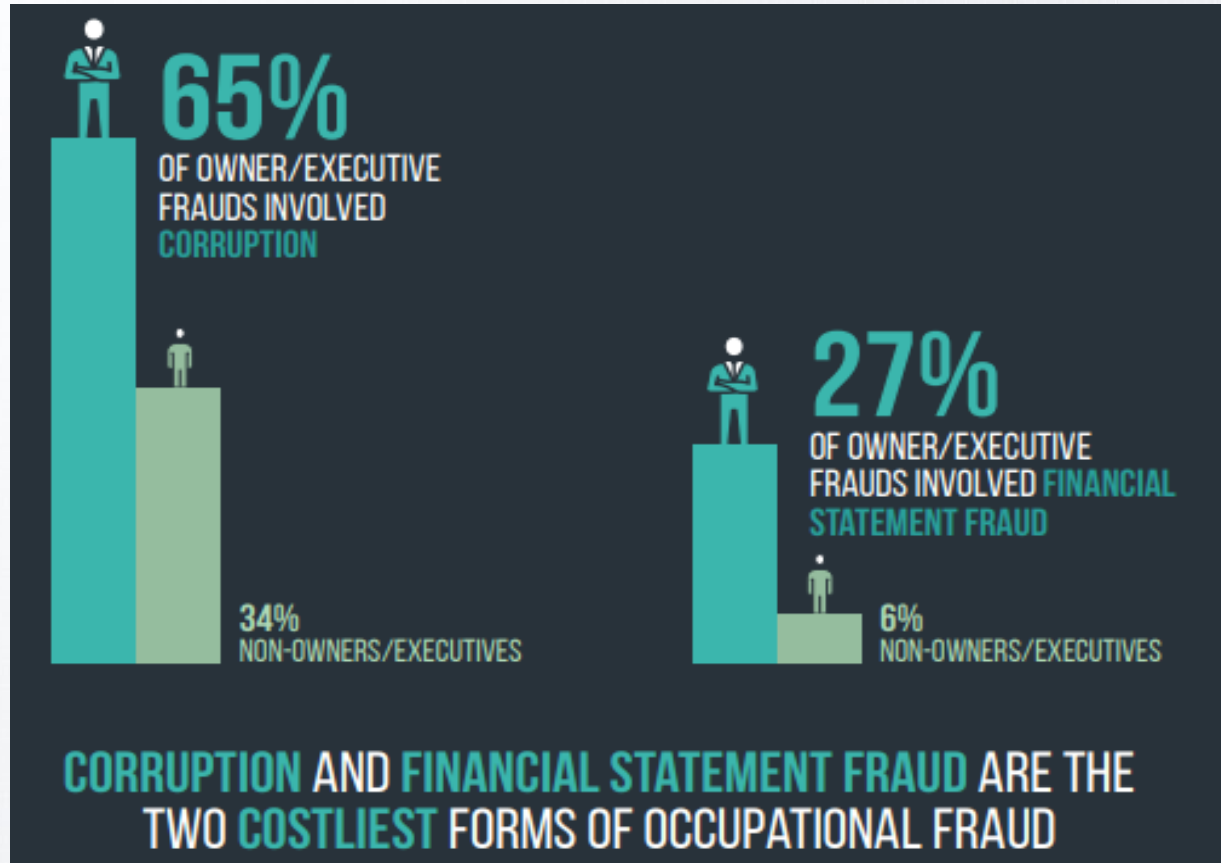
Created fraudulent journal entries

Occupational Fraud and Abuse Classification System (the Fraud Tree)



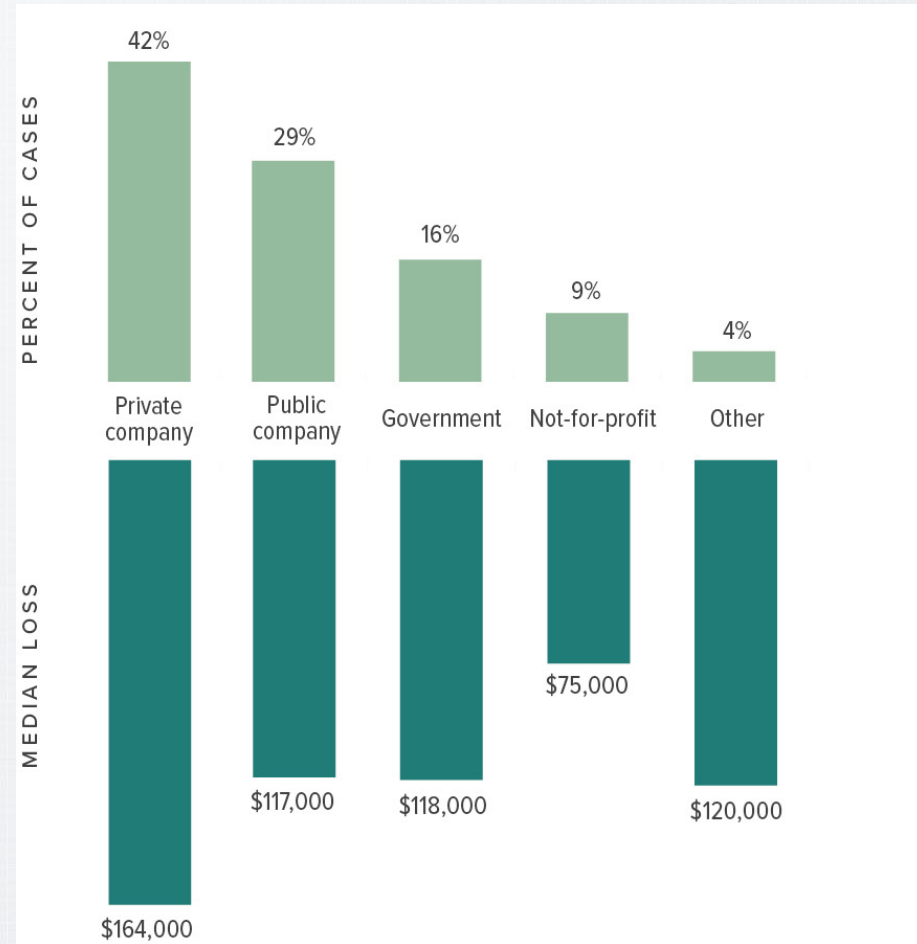
... How is Occupational Fraud Committed?





....

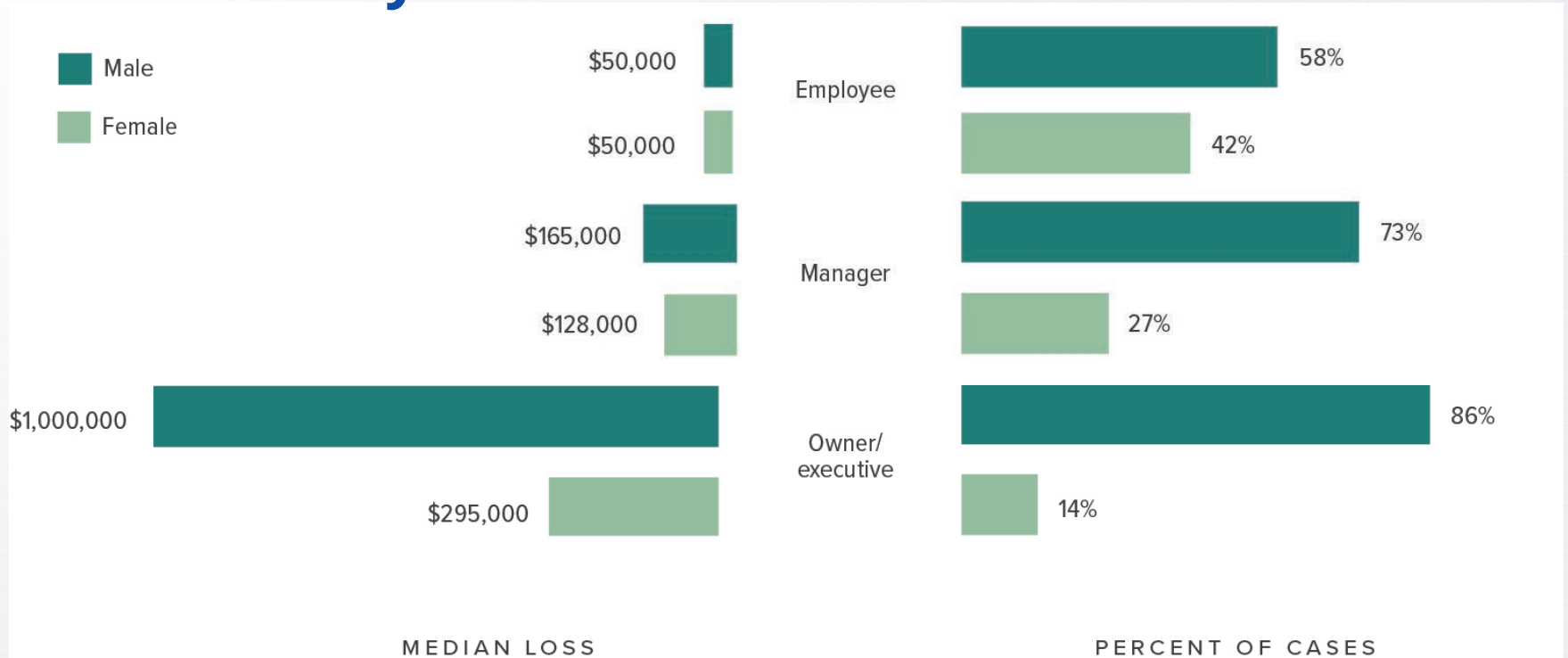
What Types of Organizations Are Victimized by Occupational Fraud?



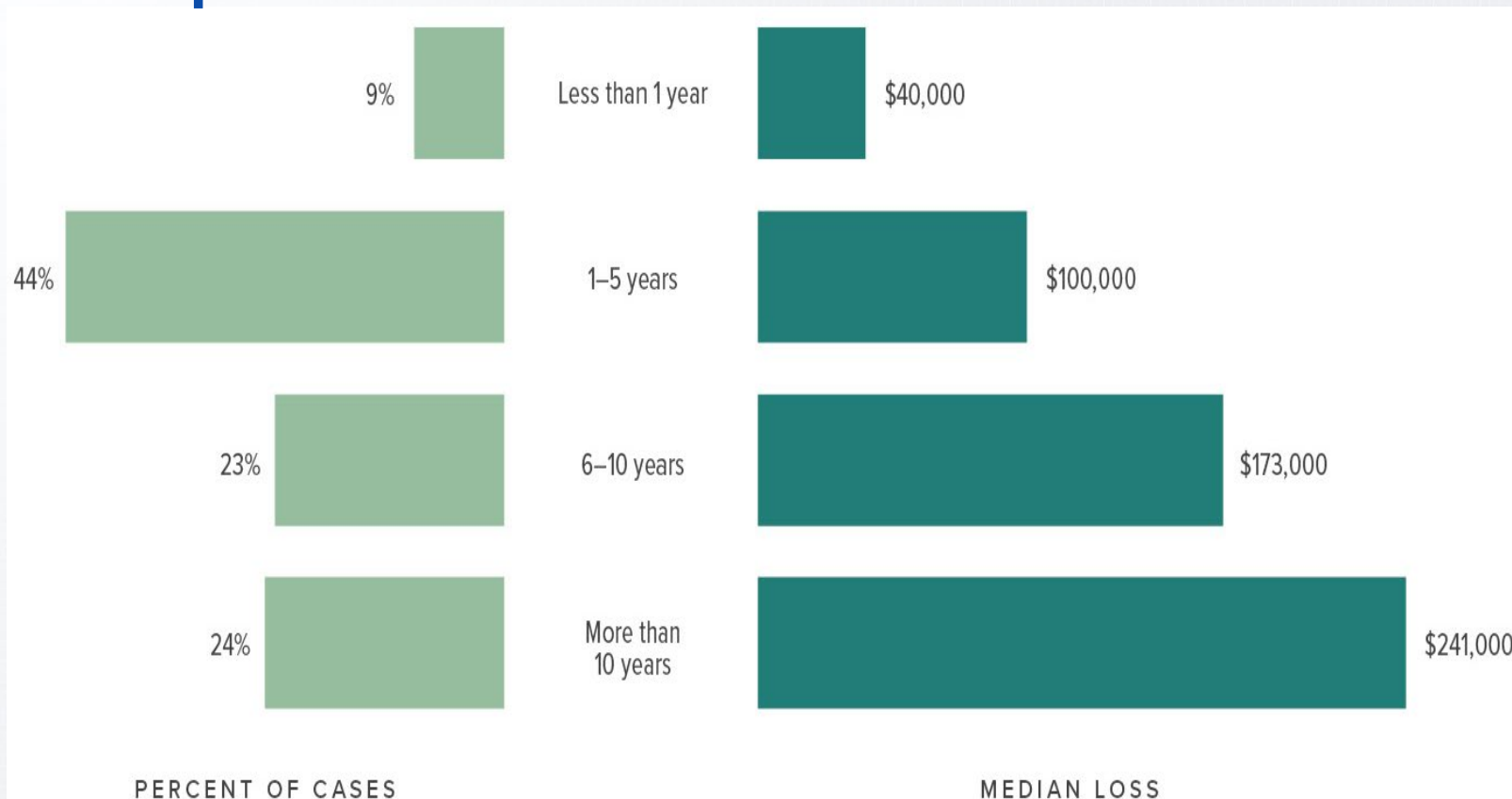
... How Does an Organization's Size Relate to Its Occupational Fraud Risk?



How Does Gender Distribution and Median Loss Vary Based on the Perpetrator's Level of Authority?

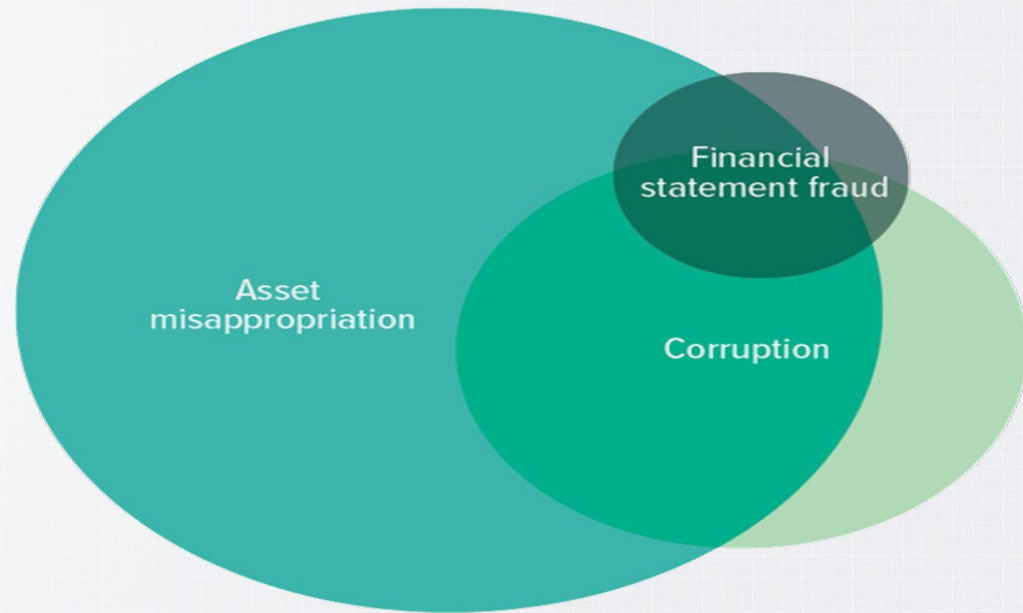


... How Does the Perpetrator's Tenure Relate to Occupational Fraud?



....

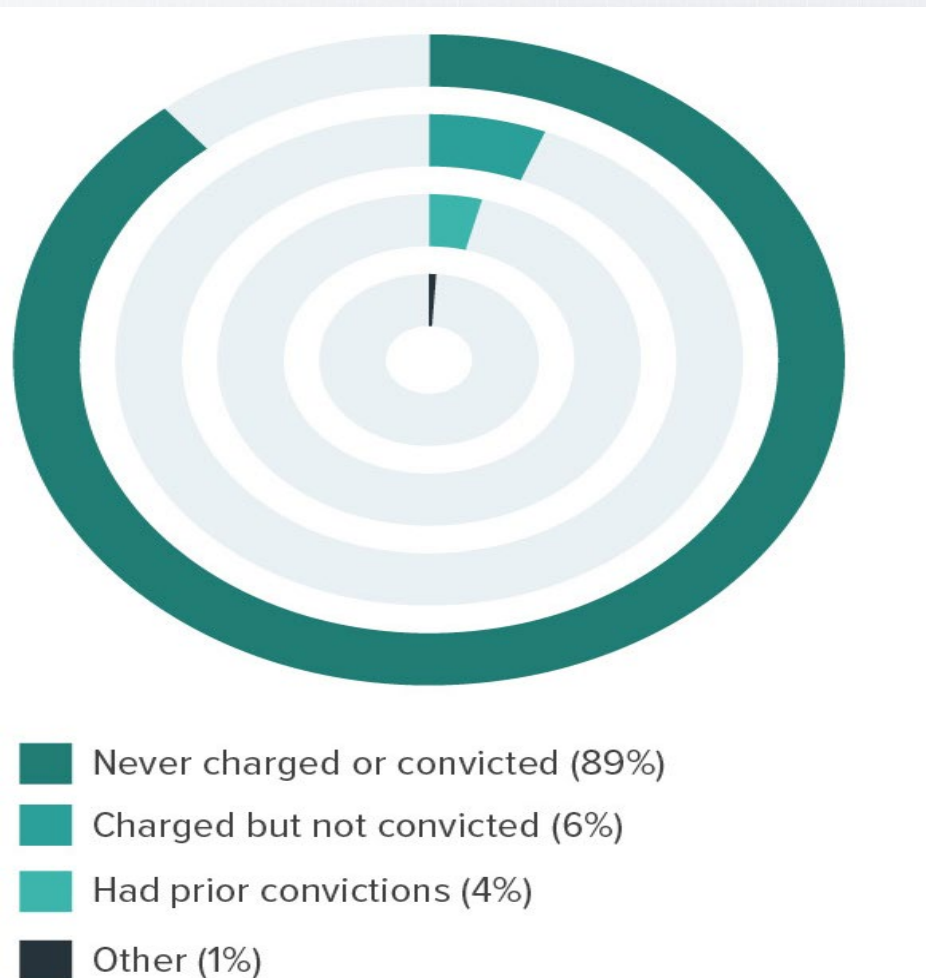
How Often Do Fraudsters Commit More Than One Type of Occupational Fraud?



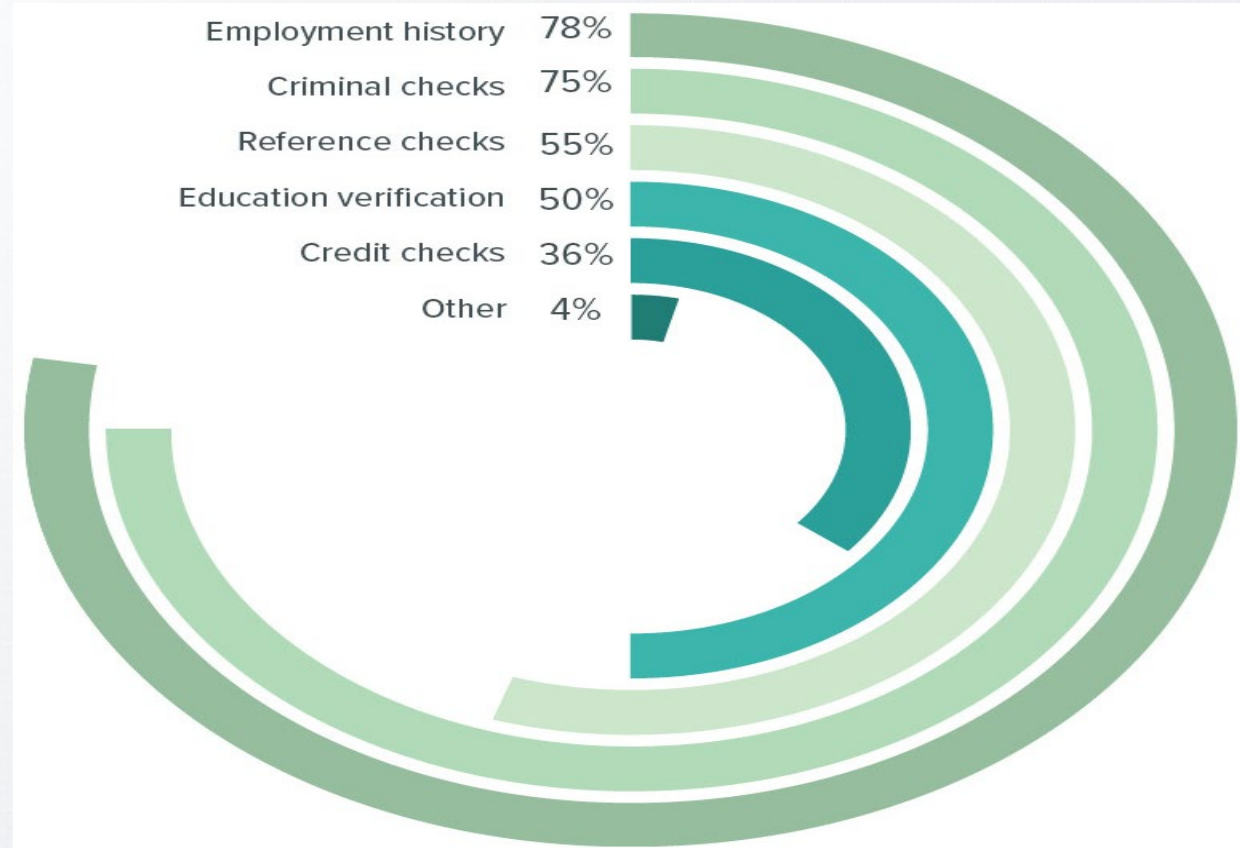
Asset misappropriation only	57%
Asset misappropriation and corruption	23%
Corruption only	9%
Corruption, asset misappropriation, and financial statement fraud	4%
Asset misappropriation and financial statement fraud	3%
Financial statement fraud only	1%
Corruption and financial statement fraud	1%

....

Do Perpetrators Tend to Have Prior Convictions?



... What Types of Background Checks Were Run on the Perpetrator Prior to Hiring?



... Red Flags of Fraud



We can increase our awareness of fraud by the red flags that may indicate that a fraud scheme is taking place!

The Fraud Triangle

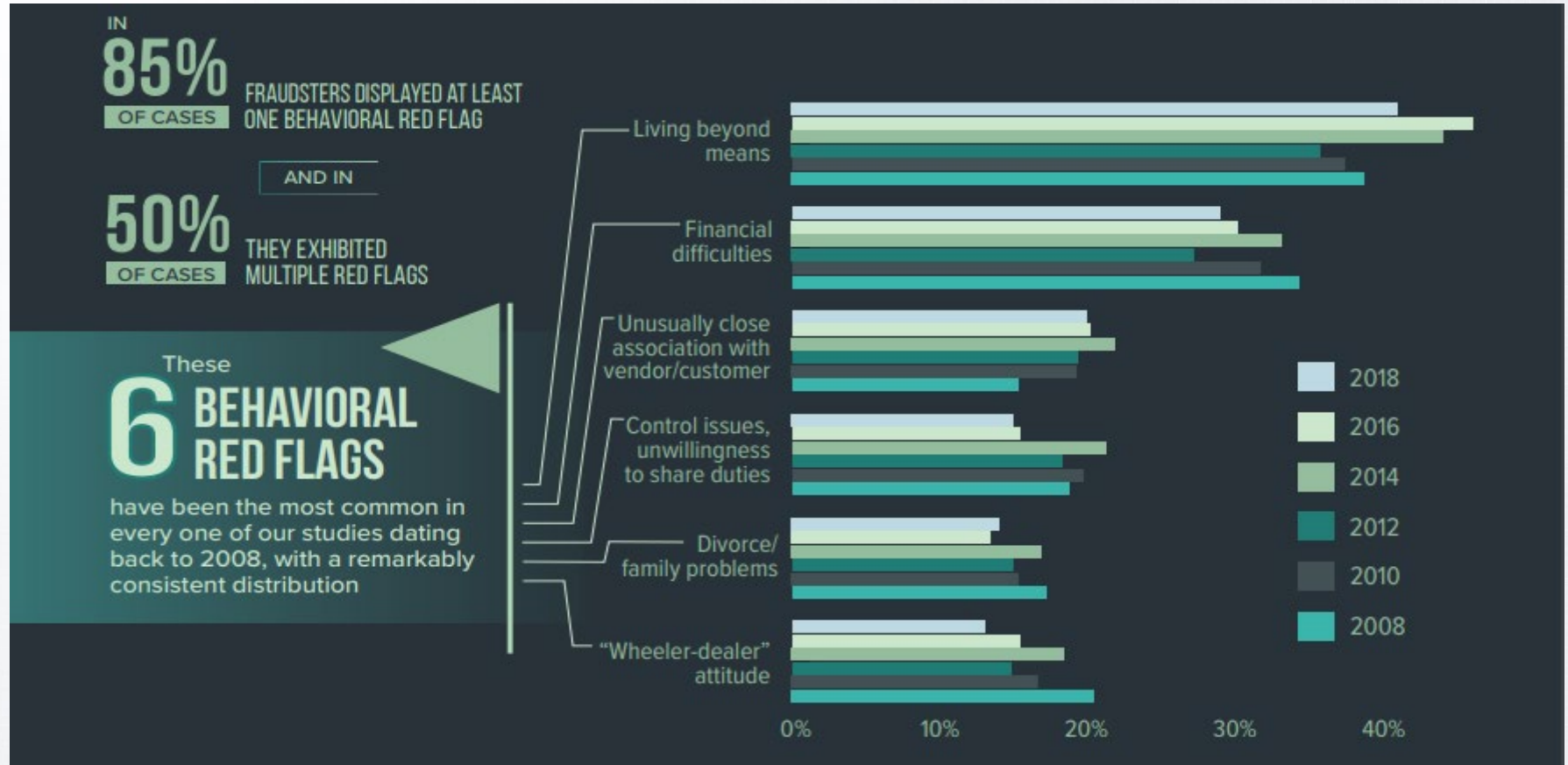


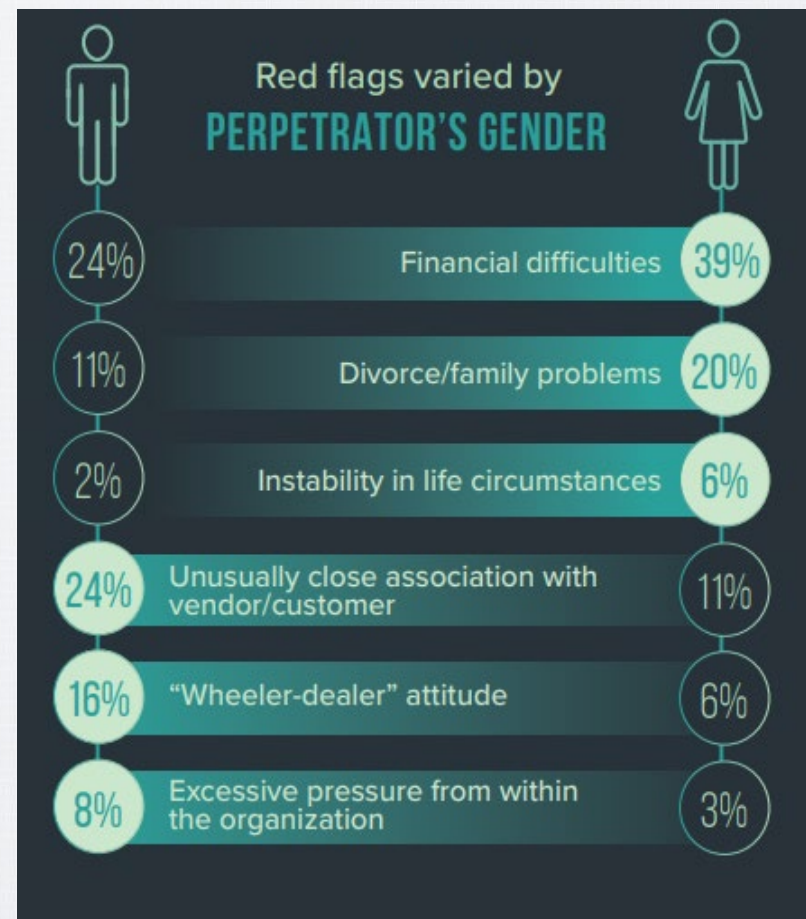
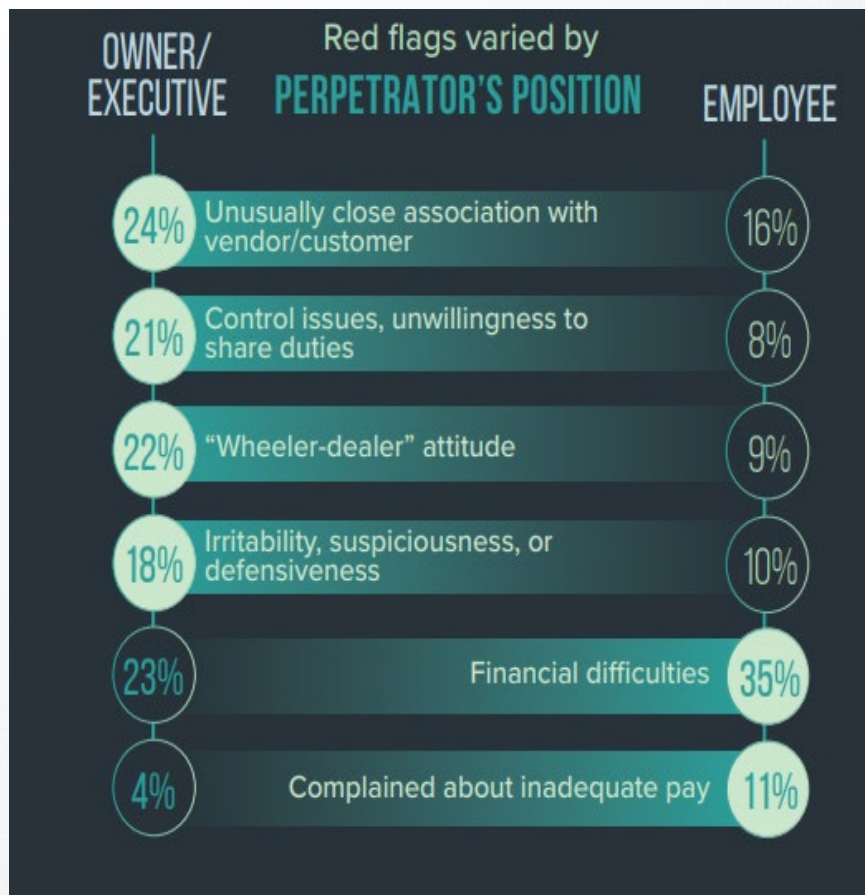
... The 6 Behavioral Red Flags

1. Living Beyond Means
2. Financial Difficulties
3. Unusually Close Association with Vendor/Customer
4. Control Issues, Unwillingness to Share Duties
5. Divorce/Family Problems
6. “Wheeler-Dealer” Attitude



... The 6 Behavioral Red Flags





... Red Flags of Fraud

Pressures

- Living above their means
- Substance Abuse
- Gambling Issues
- Emotional Instability
- Medical or Family issues



... Red Flags of Fraud

Opportunity

- Weak to non-existent internal controls, including lack of segregation of duties
- Absentee ownership
- No/limited outside review of financial records
- Nature of the business
 - Heavy reliance on cash payments
 - Portable inventory
 - Significant number of vendors

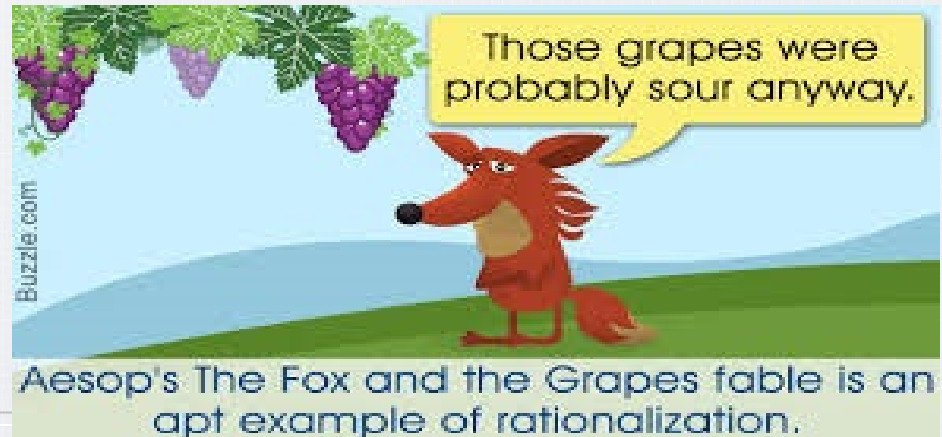




Red Flags of Fraud

Rationalization

- Tone at the top – I am only doing what ownership or other management personnel do
- This is my way of getting what is due to me
- I am only borrowing the money, once I get past this issue, I will pay it back and no one will know.



... Other Red Flags

- Operating results that don't mirror the industry or competitors – good or bad
- Business that consistently has cash flow issues despite profitability.
- “Hoarding” of information and access to records
- Answers to questions that don't make sense or which require significant time to answer
- Complex relationships with vendors and financing sources that do not make sense or are not easily explained

... Online Transaction Fraud

- Deleting all current authorized users from the Company's PayPal account at once
- Reviewing which users require access to this system and reissue new individualized credentials to each. We strongly recommend limiting this access to one or two individuals at the most, as beyond this level, the ability to fraudulently interact with the account significantly increases
- Ensuring terminated employees, who have been assigned such credentials, have had their credentials immediately cancelled, and at that, simultaneously, the Company changes the password access to the system
- Assigning specific responsibilities for oversight of the overall PayPal account



... Not-For-Profit Fraud

- Proper Segregation of duties when it comes to programs that take in cash for program fees
- The person in control of the general ledger and accounts receivable should not be the one collecting the cash
- Proper reconciliations of program services vs program revenue
- Personnel that has everyone of the fraud triangle signs:
 - Strong personality that won't let anyone else collect cash
 - Doesn't take vacations
 - Family health issues
 - Can't ever seem to get their work done/Very busy
- When accounts receivable does not make sense or is long and outstanding

... Church Fraud

- Minister had complete control of bank accounts and investment accounts
- No board oversight
- Fraud started small and no one noticed
- ATM withdrawal at Pointe Place, Yellow Brick Road and Turning Stone
- Nearly liquidated church's entire investment portfolio

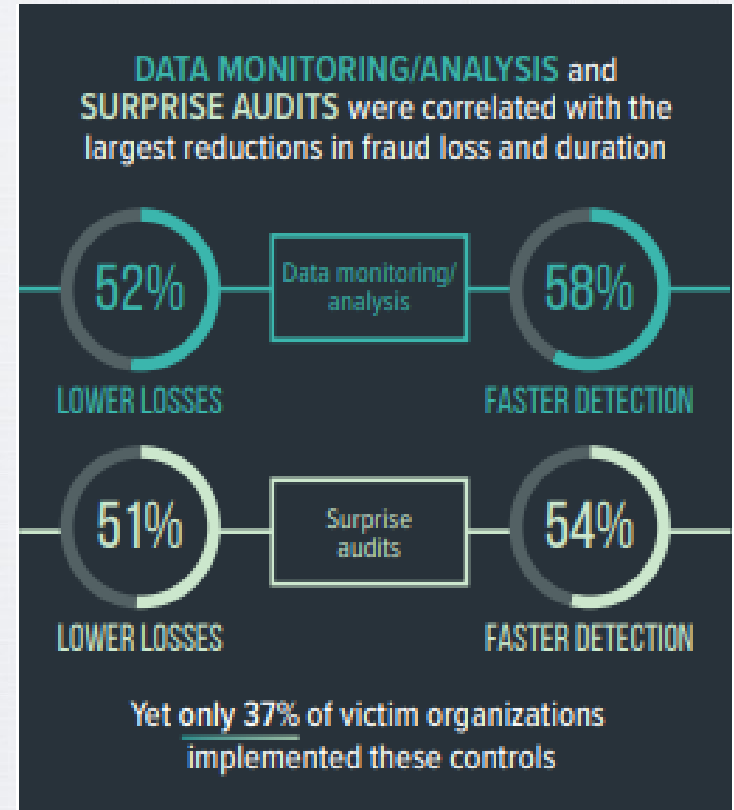




... Most Effective Internal Controls

Although you can never eliminate fraud, you can implement controls that help prevent and detect fraud when it occurs.

1. Data Monitoring/Analysis
2. Surprise Audits
3. External Audit of Internal Controls over Financial Reporting
4. Job Rotation/ Mandatory Vacation
5. Management Review
6. Hot Line



... Anti-Fraud Controls In Place While Fraud Still Occurs

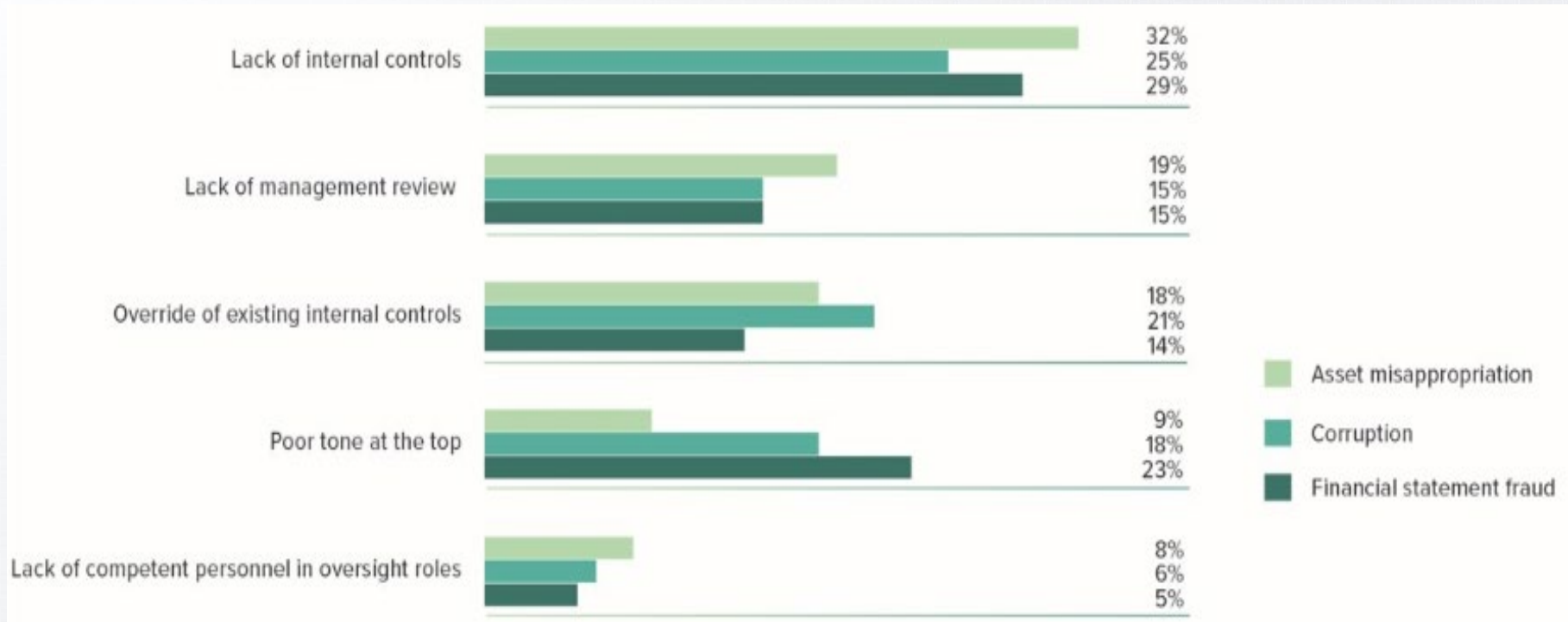
Control	Percent of cases	Control in place	Control not in place	Percent reduction
Code of conduct	80%	\$ 110,000	\$250,000	56%
Proactive data monitoring/analysis	37%	\$ 80,000	\$165,000	52%
Surprise audits	37%	\$ 75,000	\$152,000	51%
External audit of internal controls over financial reporting	67%	\$100,000	\$200,000	50%
Management review	66%	\$100,000	\$200,000	50%
Hotline	63%	\$100,000	\$200,000	50%

... Primary Internal Control Weakness that Contribute to Fraud

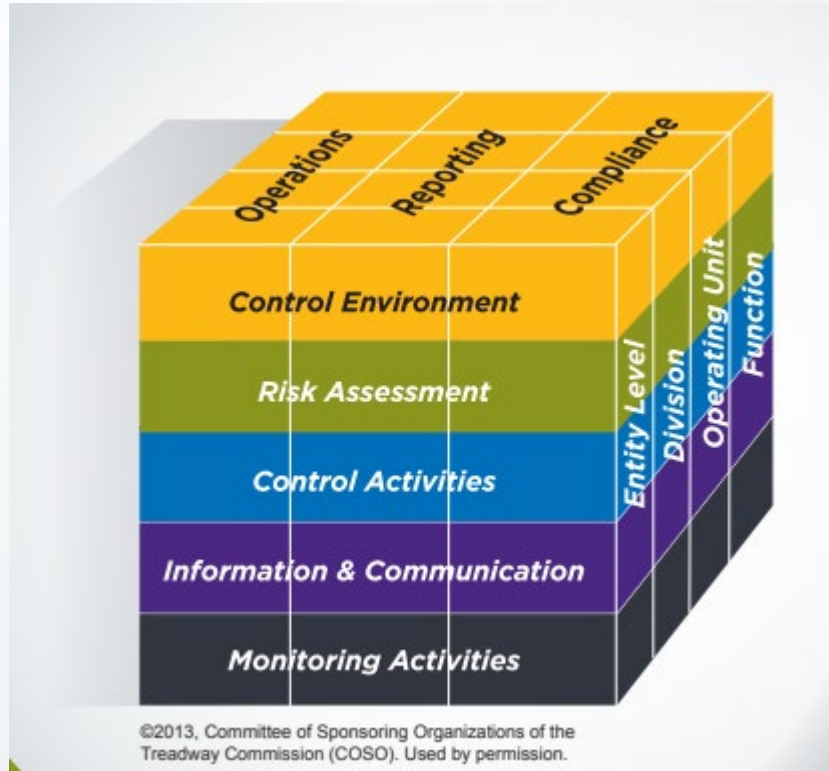
- Lack of Internal Controls – 30%
- Overriding Existing Controls – 19%
- Lack of Management Review -18%
- Poor Tone at the Top – 10%
- Lack of Competent Personnel in Oversight Roles - 8%



How Do Internal Control Weaknesses Vary by Scheme Type?



... COSO Internal Control – Integrated Framework Principles

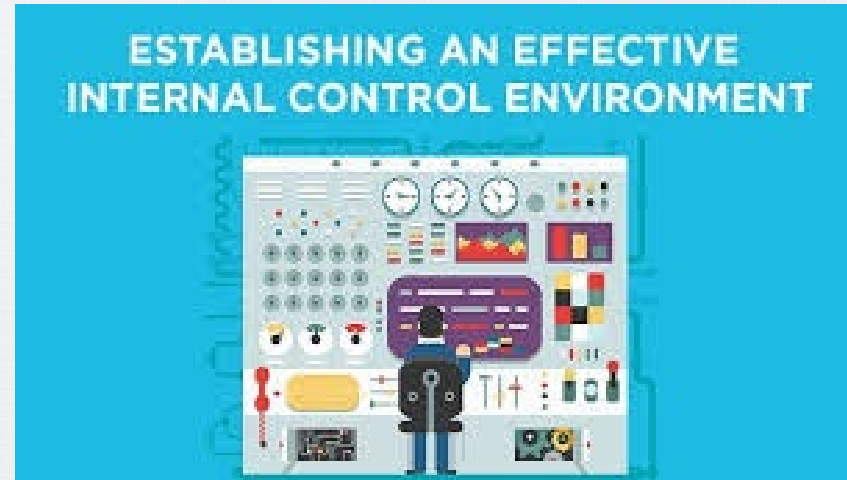


INTERNAL CONTROL WEAKNESSES
WERE RESPONSIBLE FOR NEARLY
HALF OF FRAUDS



... Control Environment – Tone at the Top

- Demonstrates commitment to integrity and ethical value
- Exercises oversight responsibilities
- Establish structure, authority and responsibilities
- Demonstrates commitment to competence
- Enforces Accountability



... Risk Assessment

- Specifies suitable objectives
- Identifies and analyzes risk
- Assess fraud risk
- Identifies and analyzes significant change



... Control Activities

- Selects and develops control activities
 - Segregation of Duties
 - Physical Controls
 - Authorization
 - Performance Review
 - Information Processing
- Selects and develops general controls over technology
- Deploys through policies and procedures

... Information and Communication

- Uses relevant quality information
- Communicates internally
- Communicates externally



... Monitoring Activities

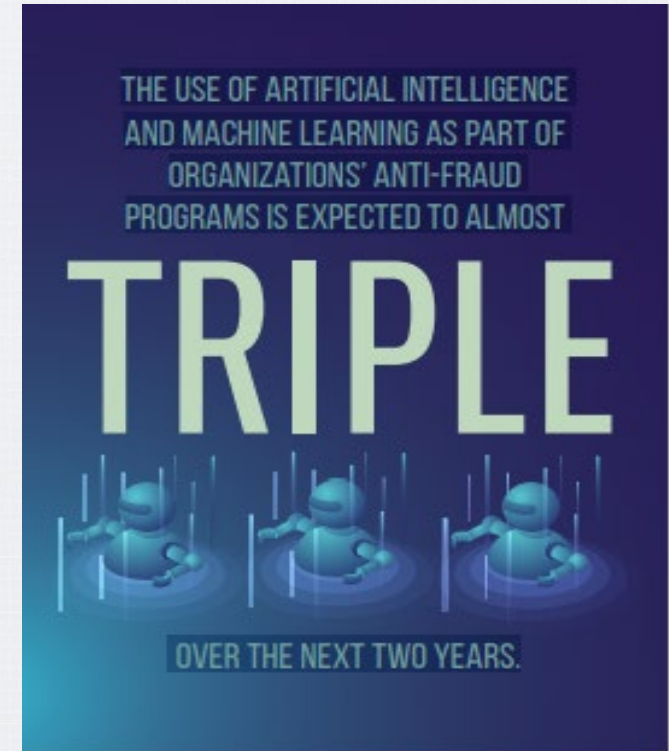
- Conducts ongoing and/or separate evaluations
- Evaluates and communicates deficiencies



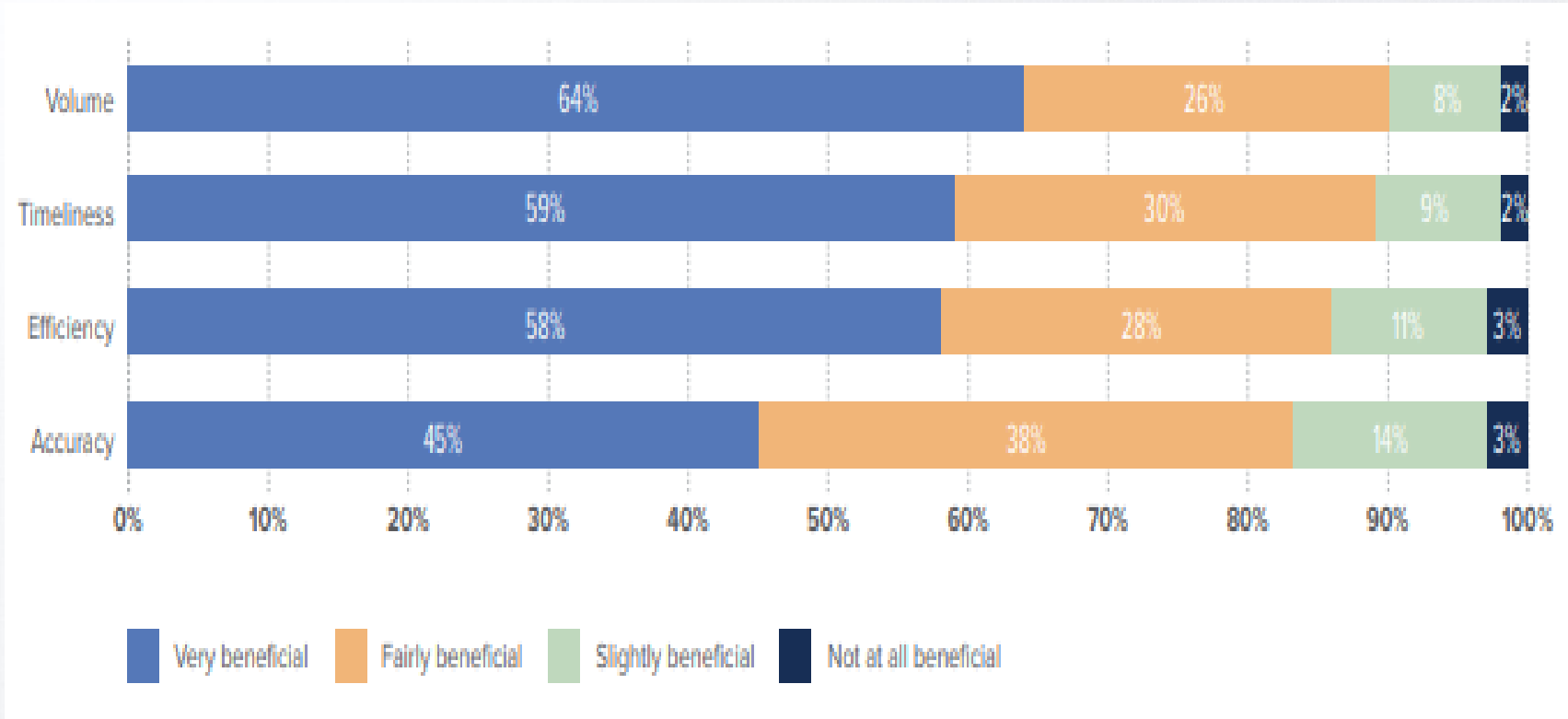


... The Use of Data Analytics

- Data analytics typically refers to the use of analytics software to identify trends, patterns, anomalies, and exceptions in data.
- In recent years, organizations have increasingly adopted data analytics techniques and approaches to assist with marketing, customer service, brand protection, financial management, and numerous other areas, including fraud prevention and detection.



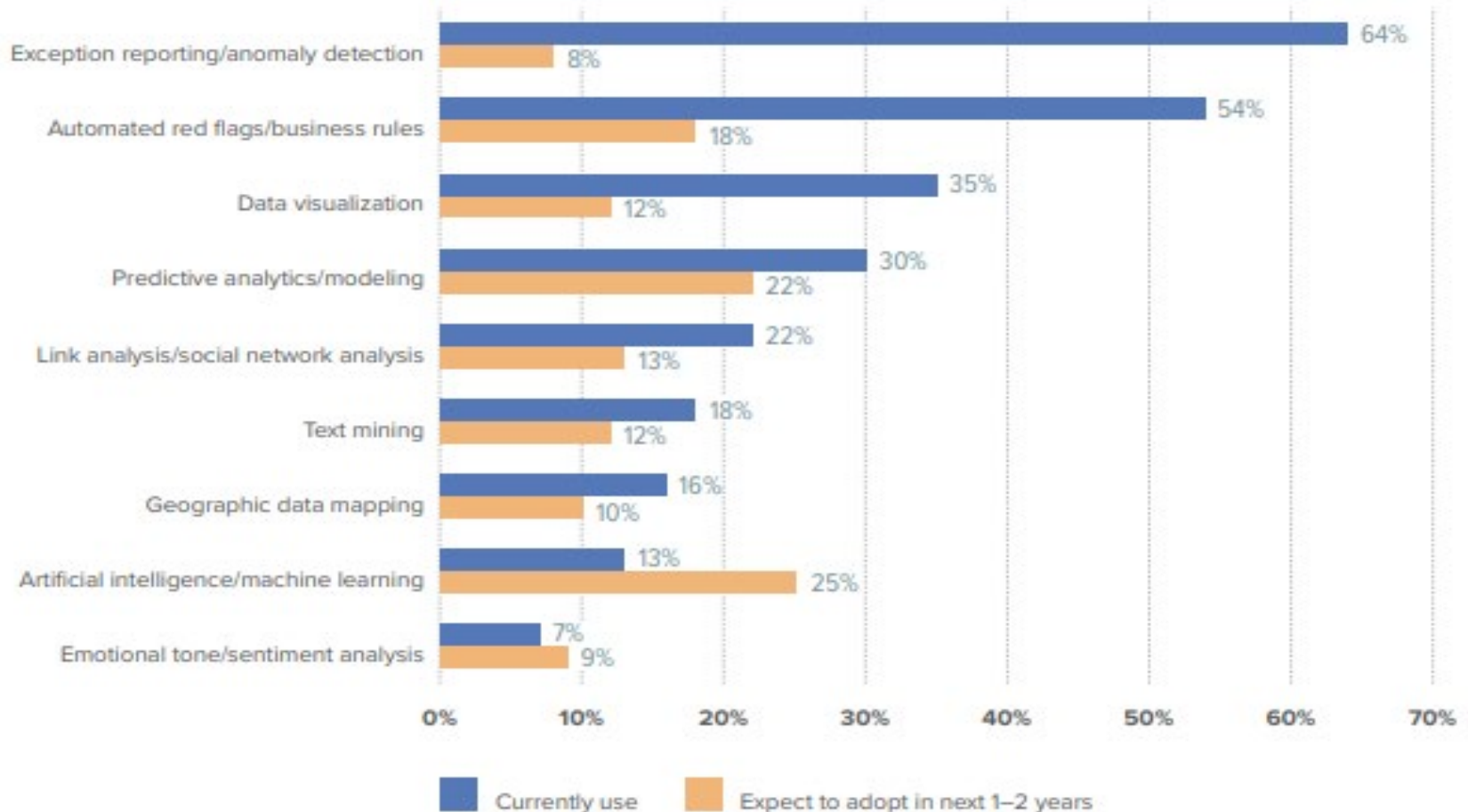
... How Beneficial is Data Analytics to Different Areas of Organizations' Anti-Fraud Initiatives?



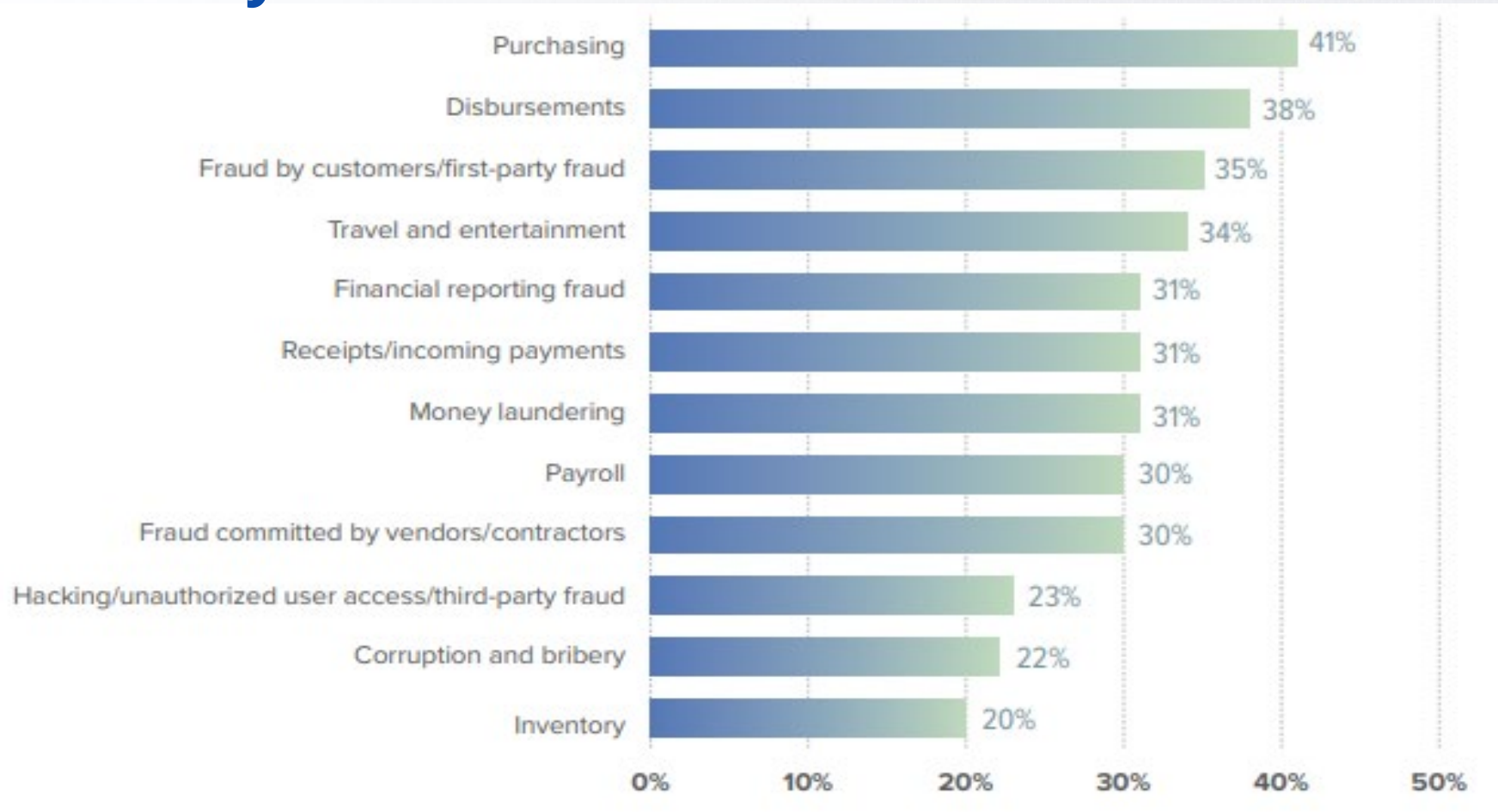
... **Benefits of Data Analytics**

- Identify fraud more efficiently and effectively before it becomes material
- Focus detection efforts on suspicious transactions
- Reduce sampling errors
- Gain insight into how well internal controls are operation
- Ability to effectively monitor trends
- Compare data from diverse sources to identify instances of fraud or noncompliance

... What Data Analysis Techniques Do Organizations Use to Fight Fraud?



... In What Risk Areas Do Organizations Use Data Analytics to Monitor for Fraud?



... What Other Technologies Are Organizations Using to Fight Fraud?

- Case management software programs developed in-house
- Digital forensic and e-discovery software
- Online evidence capturing software
- Biometrics
- Blockchain/distributed technology
- Robotic
- Virtual/augmented reality



... Biggest Obstacle Implementing Data Analytics

- While technological advancements can bring many benefits, adopting new technology often comes with challenges and potential barriers to success. Anti-fraud technology is no different.
- Moving forward, data analytics will be an integral tool to preventing and detecting fraud.

BUDGET AND
FINANCIAL CONCERNS
ARE THE
BIGGEST OBSTACLE
FOR MANY ORGANIZATIONS.



... What to Take Away

- Never going to eradicate fraud
- What we can do, though, is build the defenses against fraud:
 - Awareness of the red flags and behavior red flags
 - Build the best Internal Controls system allowed by:
 - Financial resources
 - Personnel resources



Questions





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