



Fraud Prevention and Deterrence

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Meet the Presenters



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Agenda

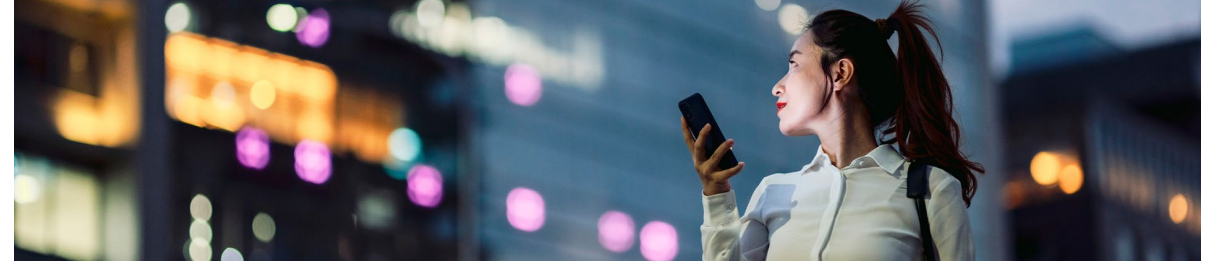
1. Introductions
2. Key Takeaways
3. What is Fraud?
4. Fraud Deterrence & Prevention
5. Perpetrators of Fraud
6. Most common types of fraud in Public Sector
7. Q & A



Key Takeaways



- How Entity Level and Transaction Level Controls helps in your organization
- Outside factors contribute to someone committing fraud
- An organization cannot control pressure/outside incentives & rationalization but can limit opportunity for fraud
- Focus on perceived opportunities
- Take the person out of the picture – TRUST IS NOT A CONTROL
- Assess the ENVIRONMENT, not the person



- Fraud is most frequently detected by tips & proactive measures
- Controls protect the organization & employees
- Good people commit fraud
- Become aware of factors that can indicate fraud in the public sector

What is Fraud?



What Is Fraud?

- Fraud is a deliberate act (or failure to act) with the intention of obtaining an unauthorized benefit, either for oneself or for the institution, by using deception or false suggestions or suppression of truth or other unethical means, which are believed & relied upon by others.

Fraud Deterrence & Prevention



Fraud Prevention Check-Up

▪ Oversight

- Board, Audit Committee, or other governance roles

▪ Ownership

- Responsible parties identified to manage fraud risks
- Communication to business units



Fraud Prevention Check-Up (cont.)

- **Assessment**

- Ongoing process to identify fraud risks in functional areas

- **Tolerance & Management**

- What risk is acceptable? Has it been approved?
- Avoidance, Acceptance, Sharing, Reduction

- **Process-Level Controls & Re-engineering**

- Basic controls (authorization, custody, recording)
- Controls can be costly, consider new processes

Fraud Prevention Check-Up (cont.)

- **Environmental-Level Controls**
 - Top-down ethical culture
 - Code of conduct
 - Training
 - Communication & reporting concerns
 - Formal investigative process by cross-functional team
- **Proactive Fraud Detection Methods**
 - Proactive & Preventive > Reactive & Detective
 - Leverage systems & exception reporting

Fraud Risk Assessment

• Overview/Benefits

- Identify potential inherent fraud risks
- Assess significance & likelihood of occurrence
- Evaluates areas most susceptible to fraud
- Maps existing controls to fraud risks
- Determines if controls are operating properly
- Identify ineffective or non-existent controls
- Respond to residual fraud risks



Fraud Risk Assessment (Cont.)

• **Employee Assessment**

- Does the organization have written policies & procedures for accounting & purchasing?
- Does senior management exhibit & encourage ethical behavior?
- Does the organization provide an anonymous way to report suspected violations of fraud, waste, & abuse?
- Are pre-employment background checks performed?
- Are the duties related to authorization, custody of assets, & recording or reporting of transactions segregated?
- Do employees feel they are treated & compensated fairly?

Fraud Risk Assessment (Cont.)

• **Employee Assessment**

- Do any employees appear to be spending far more than they are earning?
- Do any employees resent their superiors?
- Do any employees have outside business interests that might conflict with their duties at the company?
- Is the organization experiencing high employee turnover?
- Are employees required to take annual vacations?
- Does the organization have unrealistic productivity measurements & expectations?
- Does the organization educate employees about the importance of ethics & anti-fraud programs?

Fraud Risk Assessment (Cont.)

- **Management Assessment**

- Is the board of directors composed of mainly officers of the company or related individuals?
- Is the organization under pressure to report favorable earnings?
- Do any key employees have friends or relatives reporting directly to them?
- Do any key employees have outside business interests that might conflict with their duties at the organization?
- Has the organization recently experienced large operating or investment losses?

Fraud Risk Assessment (Cont.)

- **Management Assessment**

- Does the organization delay or avoid supplying auditors with the information necessary to complete the audits?
- Does the organization have poor accounting records?
- Does the accounting department appear to be inadequately staffed?
- Does the organization lack an internal control system, or does it fail to enforce the existing internal controls?



Best Practice – Complete Entity-Wide Risk Assessment Using SWOT

- Assess entity-wide risks using questionnaires &/or meetings
- Use SWOT analysis; leverage management surveys/meetings to develop common themes
- Do not treat as a task; take action to better your organization



How Does a Control Environment Manage Risk?

An effective system of internal control

Provides accountability for achieving strategic objectives

Promotes operational efficiency & effectiveness

Improves the reliability of financial reporting to stakeholders

Strengthens compliance with applicable laws & regulations

Safeguards assets

Source: The Institute of Internal Auditors

COSO Components

<h1 style="font-size: 2em; margin: 0;">COSO</h1>		<p>▶ The COSO framework consists of 17 principles that support five components</p>		
Control Environment	Risk Assessment	Control Activities	Information & Communication	Monitoring
<ul style="list-style-type: none"> ▶ Demonstrates commitment to integrity & ethical values ▶ Exercises oversight responsibility ▶ Establishes structure, authority, & responsibility ▶ Demonstrates commitment to competent talent ▶ Enforces accountability 	<ul style="list-style-type: none"> ▶ Specifies clear objectives ▶ Identifies & analyzes risk ▶ Assesses fraud risk ▶ Identifies & assesses significant changes 	<ul style="list-style-type: none"> ▶ Selects & develops control activities ▶ Selects & develops general controls over technology ▶ Deploys control activities through policies & procedures 	<ul style="list-style-type: none"> ▶ Uses quality information ▶ Communicates internally ▶ Communicates externally 	<ul style="list-style-type: none"> ▶ Conducts ongoing &/or separate evaluations ▶ Evaluates & communicates deficiencies timely

Source: COSO



What Are Examples of Control Activities?

- **Control activities occur at all levels & functions, in all organizations, & may include**
 - Segregation of duties
 - Authorization
 - Reconciliation
 - Review & approval
 - Education & training
 - Performance planning & evaluation



Examples of Entity-Level Controls

- Board of Directors meets quarterly; minutes are documented
- Employees sign off on The Code of Ethics during new-hire orientation & annually thereafter
- Employees undergo background checks before hiring into “sensitive” positions
- Management annually reviews policies & procedures to ensure they represent current business practices

Examples of Entity-Level Controls (cont.)

- The Continuity of Operations Plan (COOP) is tested annually
- Annual user access reviews are performed by management to confirm that the principle of least privilege & segregation of duties controls are maintained
- Security awareness training is taken by all employees annually

Examples of Transaction-Level Controls

- The Accountant prepares the deposit for the armored car pickup the evening before deposit date; deposit is locked in a safe & only appropriate personnel have access
- Travel & expense vouchers are approved by employees' supervisors before being processed for payment
- Procurements over \$X are approved by the Purchasing Director, Finance Director, & the Division Director requesting the purchase
- Expenditures are approved based on delegated authority with specific thresholds.
- Fixed assets are controlled and inventoried on a regular basis

Examples of Transaction-Level Controls (cont.)

- Separate those responsible for vendor master file & staff responsible for approving invoices or signing checks
- Prohibit payment of invoices to companies not on the approved vendor list
- Separate those receiving goods or authorizing services to those processing invoices & payments to those that receive & reconcile bank statements
- Ensure no control breakdowns like stamps for signatures when access to the stamp is easy



Internal Controls & The Human Element

- Internal controls should provide an environment for
 - Order & efficiency
 - Accuracy & completeness
 - Prevention of fraud, waste, & abuse
- Internal controls do not ensure these objectives
 - People within an organization following & enforcing internal controls do
- Trust
 - Trust is not an internal control

Benefits of Implementing a Strong Internal Control Program

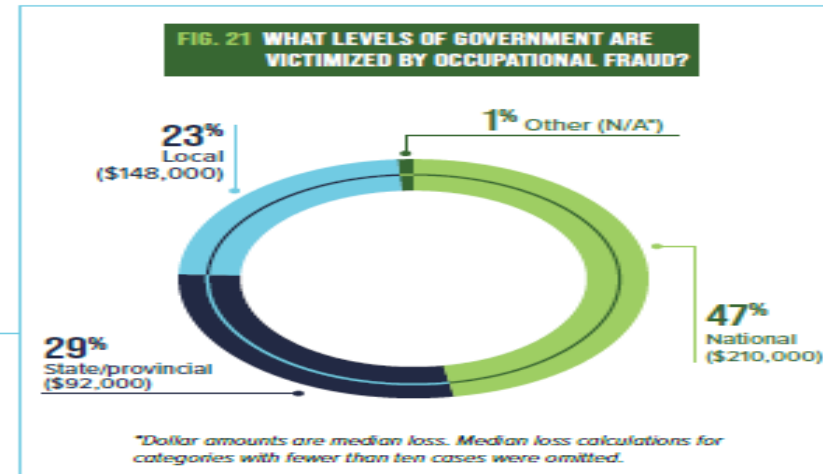
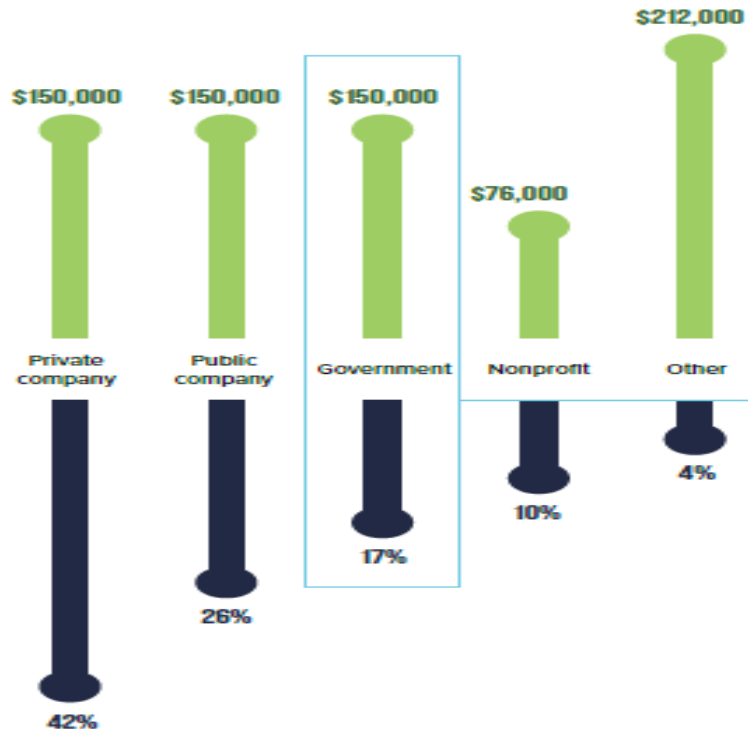
Weak Internal Controls	Strong Internal Control Program
<ul style="list-style-type: none"> ▪ Insufficient documentation to support a complete entity-level evaluation ▪ An entity-wide risk assessment is not performed ▪ Insufficient documentation of risk assessments for each significant fiscal process ▪ Insufficient documentation of testing controls for each significant fiscal process 	<ul style="list-style-type: none"> ▪ Implemented <ul style="list-style-type: none"> • Entity-wide risk assessment ▪ Identified, documented, & tested <ul style="list-style-type: none"> • Entity-level controls • Transaction-level controls • IT controls ▪ Benefits <ul style="list-style-type: none"> • Effective/efficient operations • Reliable financial reporting • Compliant with laws/regulations • Safeguard assets

Perpetrators of Fraud



Types Of Organizations Victimized By Occupational Fraud

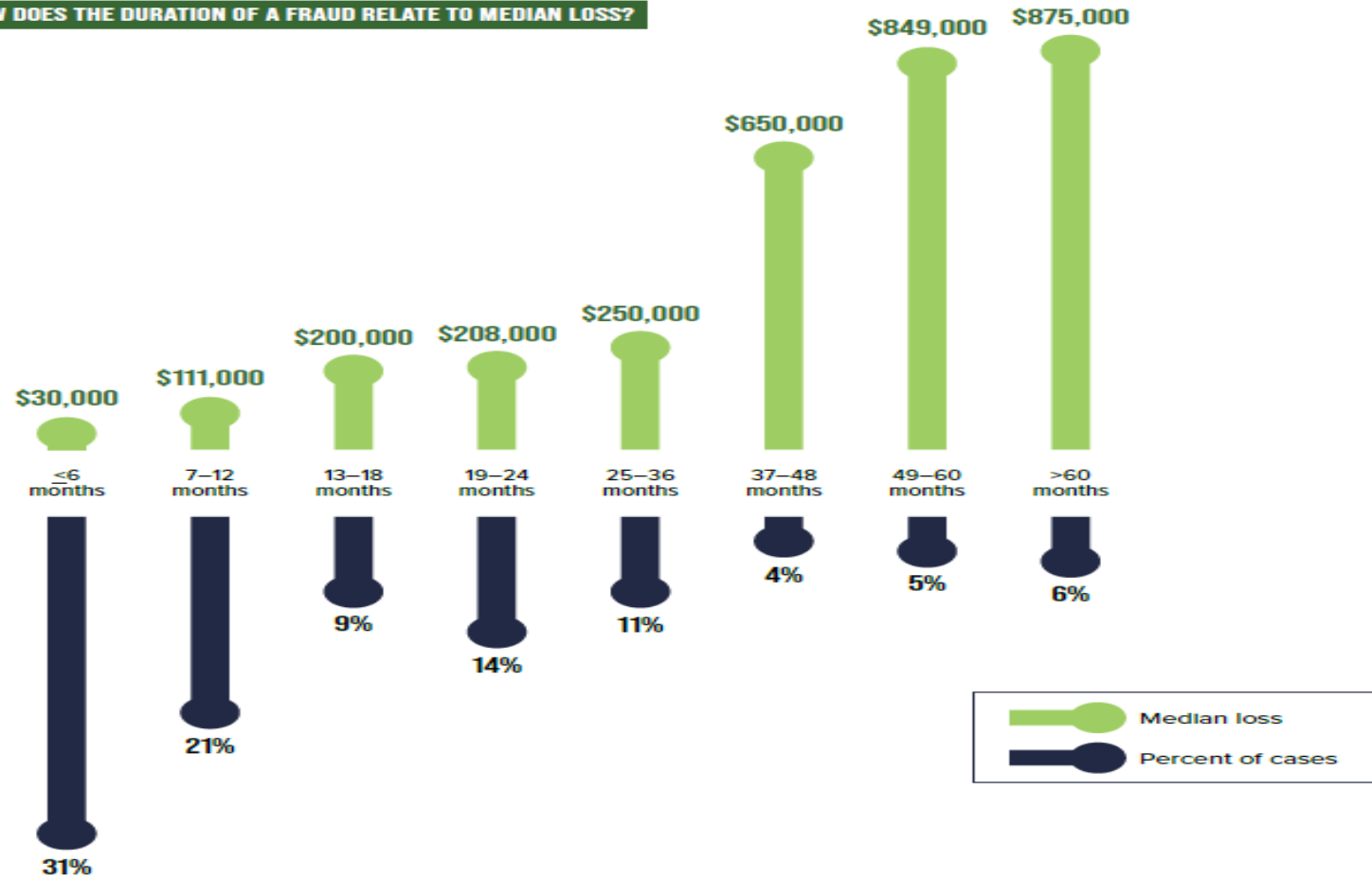
FIG. 20 WHAT TYPES OF ORGANIZATIONS ARE VICTIMIZED BY OCCUPATIONAL FRAUD?



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Duration

FIG. 7 HOW DOES THE DURATION OF A FRAUD RELATE TO MEDIAN LOSS?



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Tenure

FIG. 42 HOW DOES THE PERPETRATOR'S TENURE RELATE TO OCCUPATIONAL FRAUD?



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Tenure

FIG. 42 HOW DOES THE PERPETRATOR'S TENURE RELATE TO OCCUPATIONAL FRAUD?



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Greatest Fraud Risk By Department

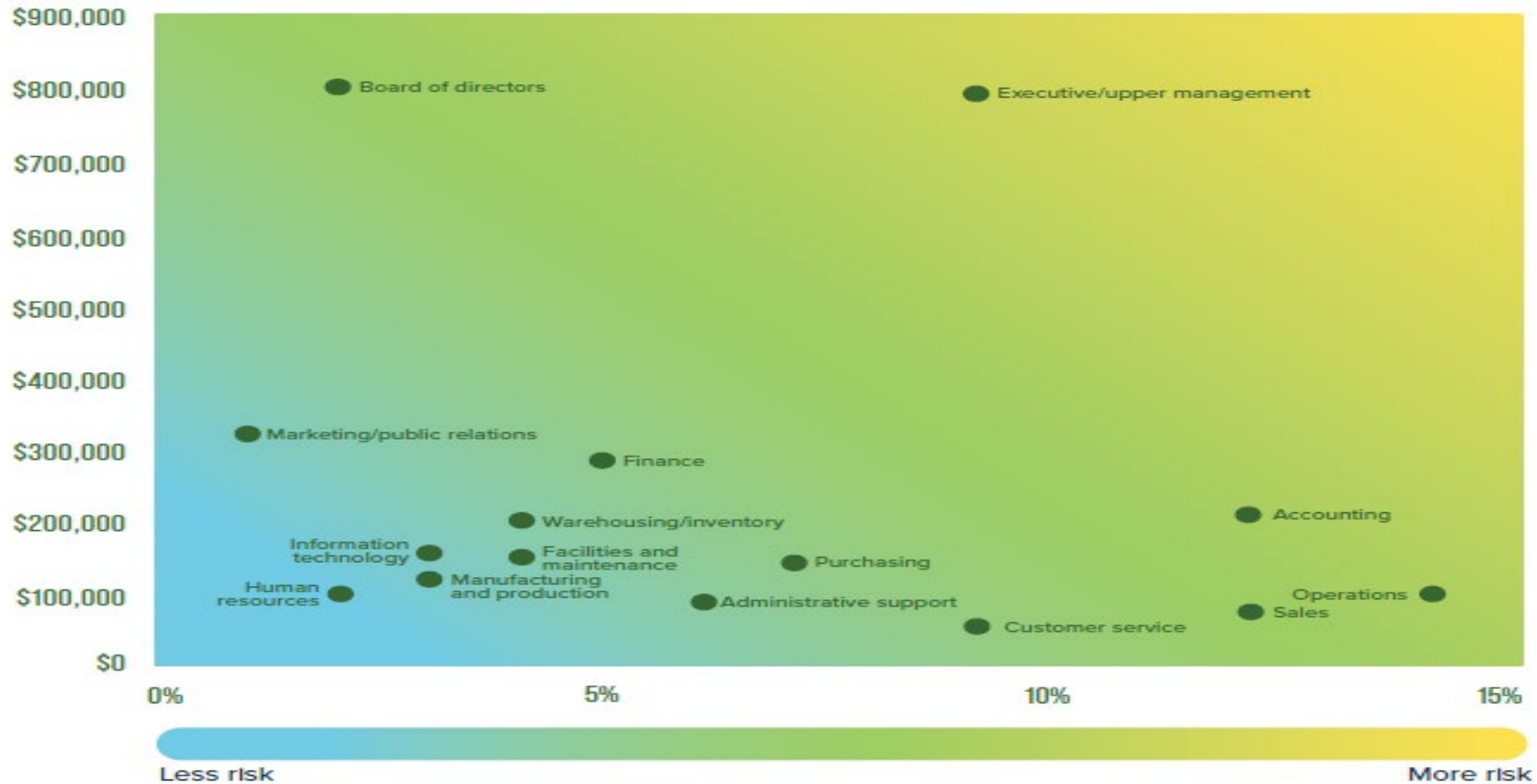
Department*	Number of cases	Percent of cases	Median loss
Operations	227	14%	\$100,000
Accounting	202	12%	\$208,000
Sales	202	12%	\$75,000
Customer service	154	9%	\$55,000
Executive/upper management	146	9%	\$793,000
Purchasing	109	7%	\$143,000
Administrative support	98	6%	\$88,000
Finance	82	5%	\$285,000
Warehousing/inventory	64	4%	\$200,000
Facilities and maintenance	59	4%	\$150,000
Information technology	52	3%	\$156,000
Manufacturing and production	43	3%	\$120,000
Board of directors	37	2%	\$800,000
Human resources	29	2%	\$100,000
Marketing/public relations	23	1%	\$321,000
Research and development	9	1%	*
Legal	9	1%	*
Internal audit	4	<1%	*

*Departments with fewer than ten cases were omitted.

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Greatest Fraud Risk By Department

FIG. 43 WHAT DEPARTMENTS POSE THE GREATEST RISK FOR OCCUPATIONAL FRAUD?



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Fraud Types By Department

FIG. 44 WHAT ARE THE MOST COMMON OCCUPATIONAL FRAUD SCHEMES IN HIGH-RISK DEPARTMENTS?

Department	Cases	Billing	Cash larceny	Cash on hand	Check and payment tampering	Corruption	Expense reimbursements	Financial statement fraud	Noncash	Payroll	Register disbursements	Skimming
Operations	227	22%	7%	10%	8%	44%	13%	2%	20%	12%	2%	8%
Accounting	202	33%	19%	17%	32%	36%	21%	9%	16%	15%	6%	21%
Sales	202	13%	9%	7%	4%	49%	7%	4%	20%	4%	2%	12%
Customer service	154	10%	11%	15%	12%	40%	6%	2%	25%	3%	3%	10%
Executive/upper management	147	33%	11%	10%	14%	65%	24%	11%	18%	16%	4%	8%
Purchasing	109	33%	8%	6%	4%	79%	6%	4%	21%	4%	3%	5%
Administrative support	98	31%	15%	19%	15%	46%	17%	4%	18%	10%	4%	20%
Finance	82	20%	23%	24%	22%	45%	17%	11%	11%	11%	4%	13%



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Initial Detection of Occupational Frauds

FIG. 13 HOW IS OCCUPATIONAL FRAUD INITIALLY DETECTED?

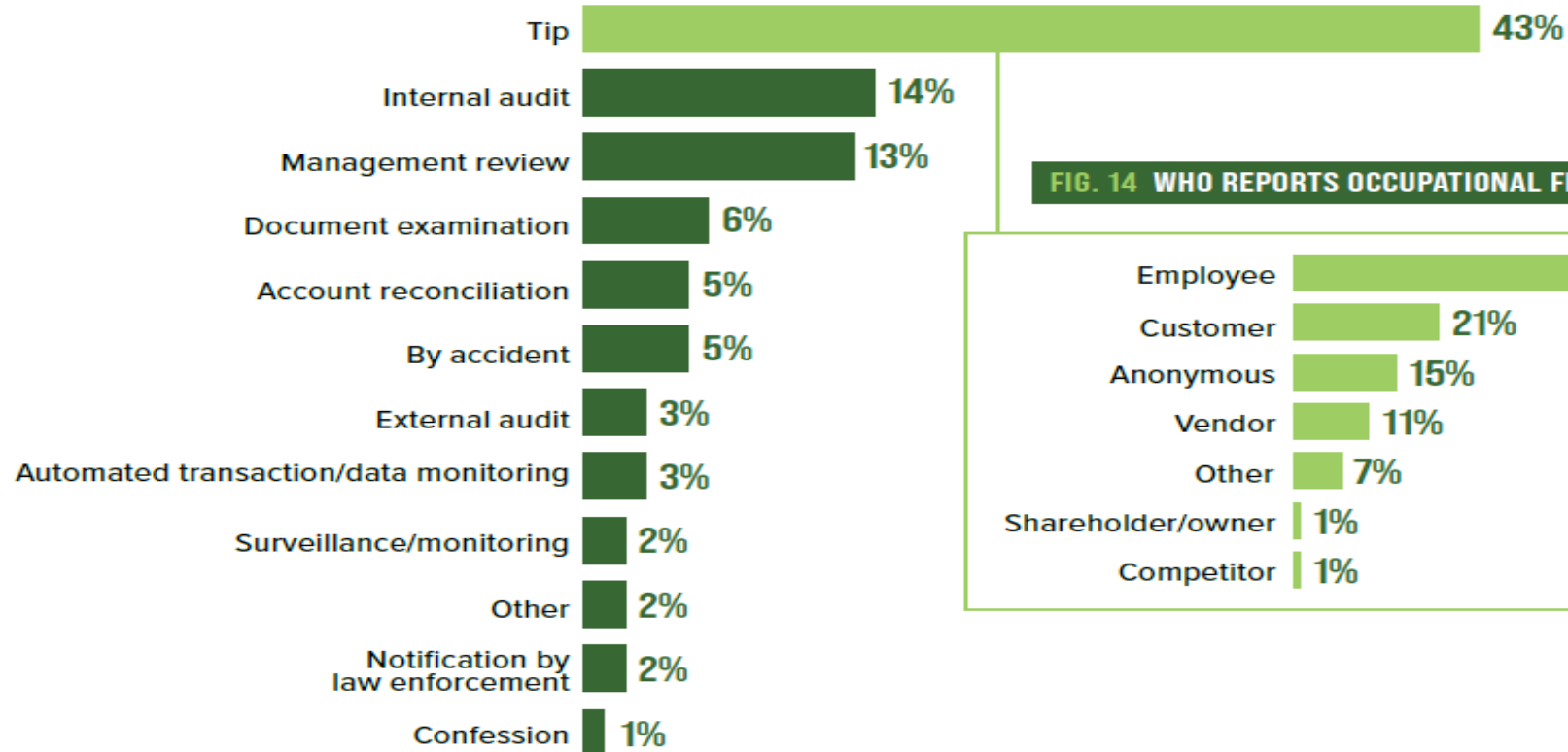
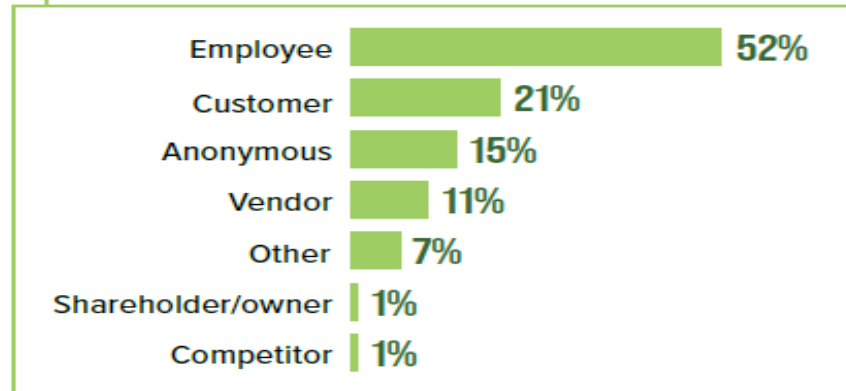


FIG. 14 WHO REPORTS OCCUPATIONAL FRAUD?



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Length of Fraud Schemes Before Detection

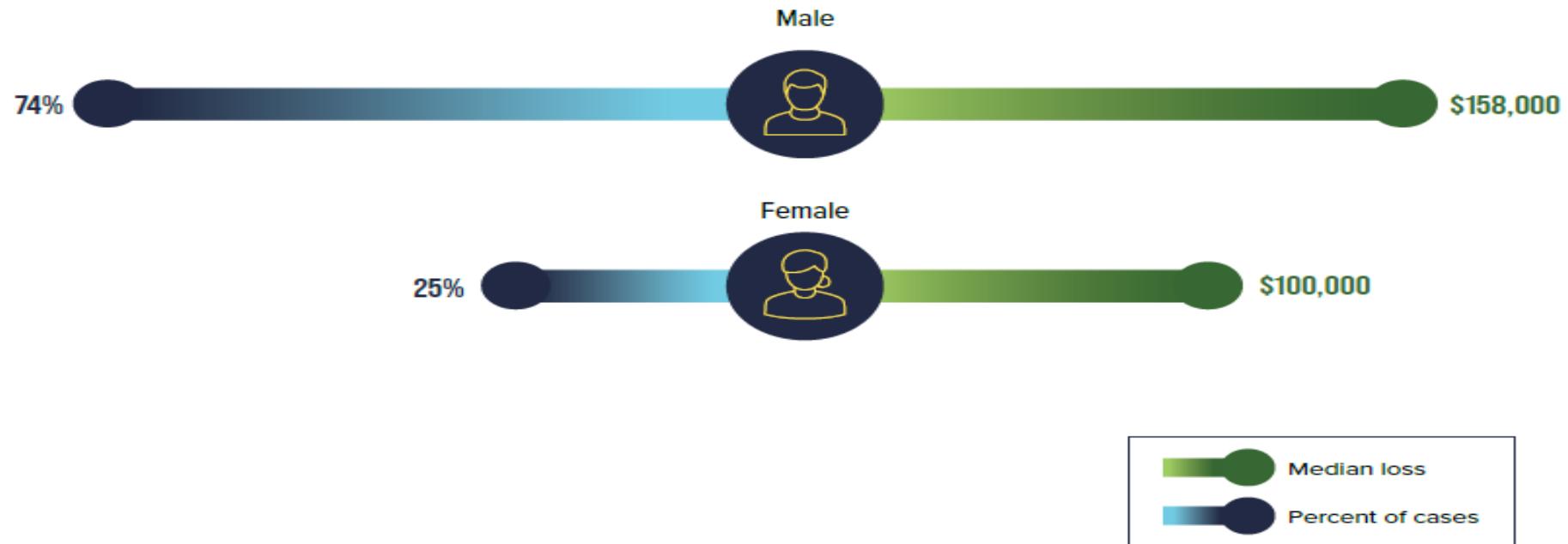
FIG. 8 HOW LONG DO DIFFERENT OCCUPATIONAL FRAUD SCHEMES LAST?



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Fraud By Gender

FIG. 45 HOW DOES THE PERPETRATOR'S GENDER RELATE TO OCCUPATIONAL FRAUD?



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Fraud By Age

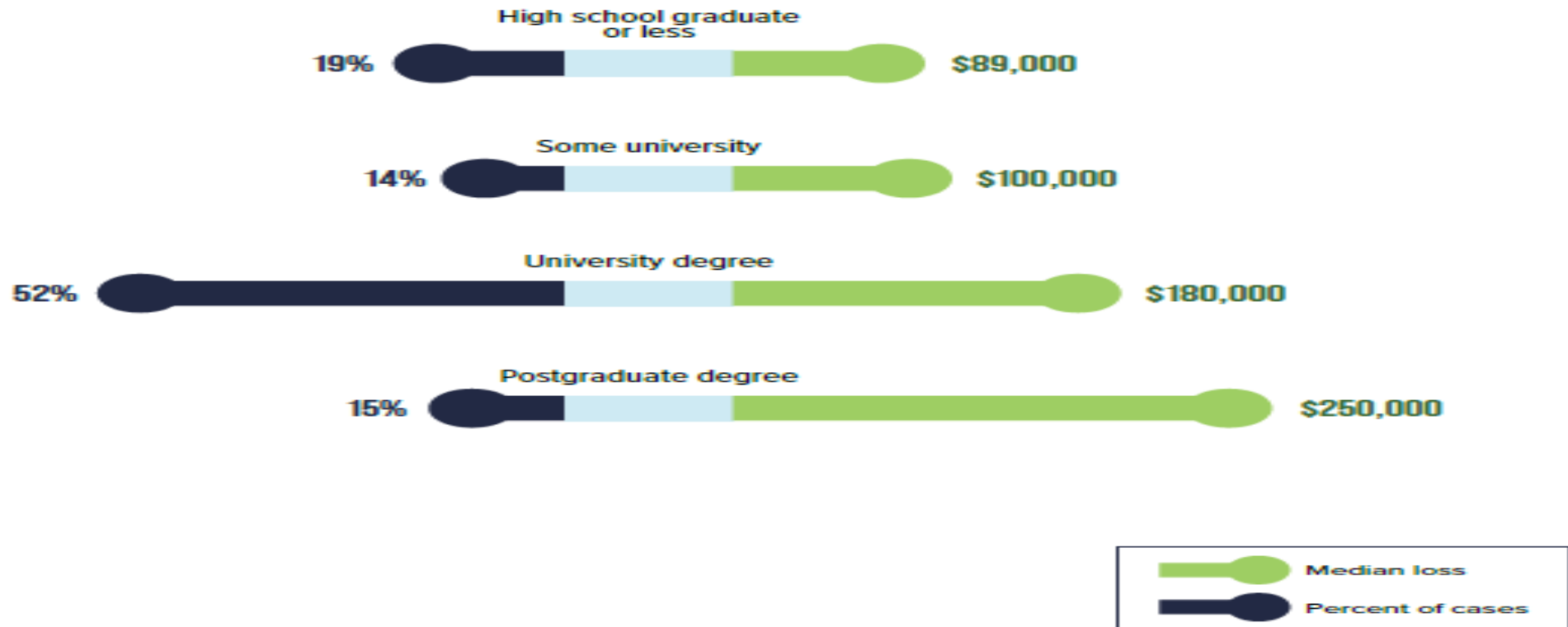
FIG. 48 HOW DOES THE PERPETRATOR'S AGE RELATE TO OCCUPATIONAL FRAUD?



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Fraud By Educational Level

FIG. 49 HOW DOES THE PERPETRATOR'S EDUCATION LEVEL RELATE TO OCCUPATIONAL FRAUD?



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Criminal & Employment Backgrounds

FIG. 51 DO PERPETRATORS TEND TO HAVE PRIOR FRAUD CONVICTIONS?

Amos, Jamie (Jamie.Amos@forvis.com) is signed in

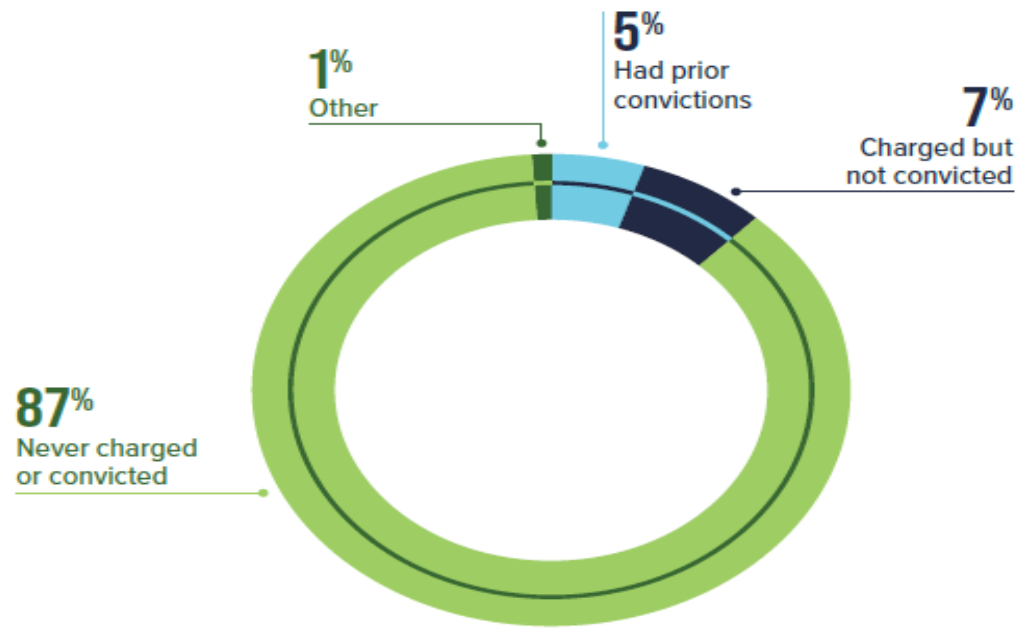


FIG. 52 DO PERPETRATORS TEND TO HAVE PRIOR EMPLOYMENT-RELATED DISCIPLINARY ACTIONS FOR FRAUD?

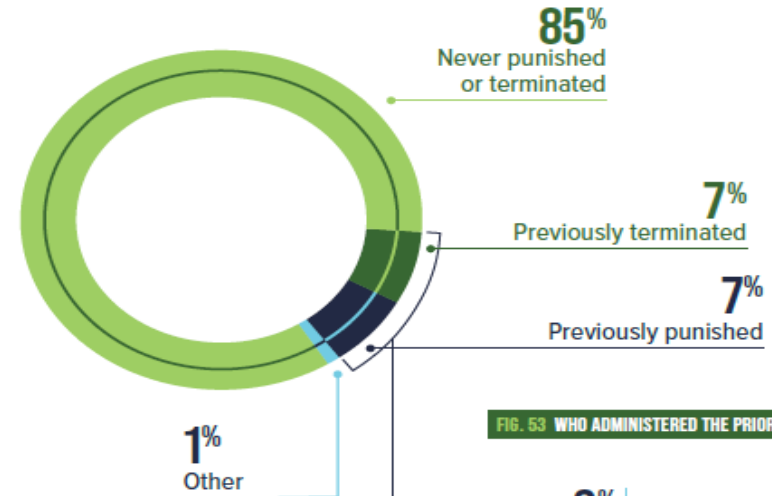
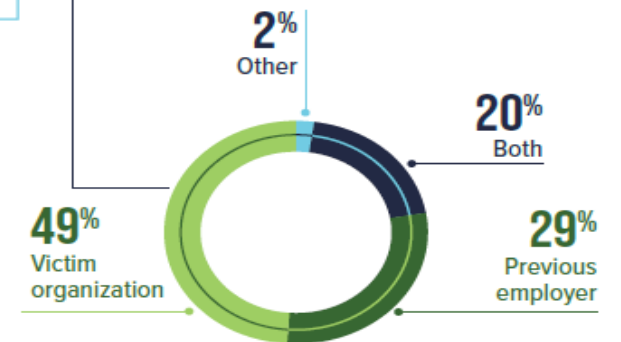


FIG. 53 WHO ADMINISTERED THE PRIOR DISCIPLINE?



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Story Time...

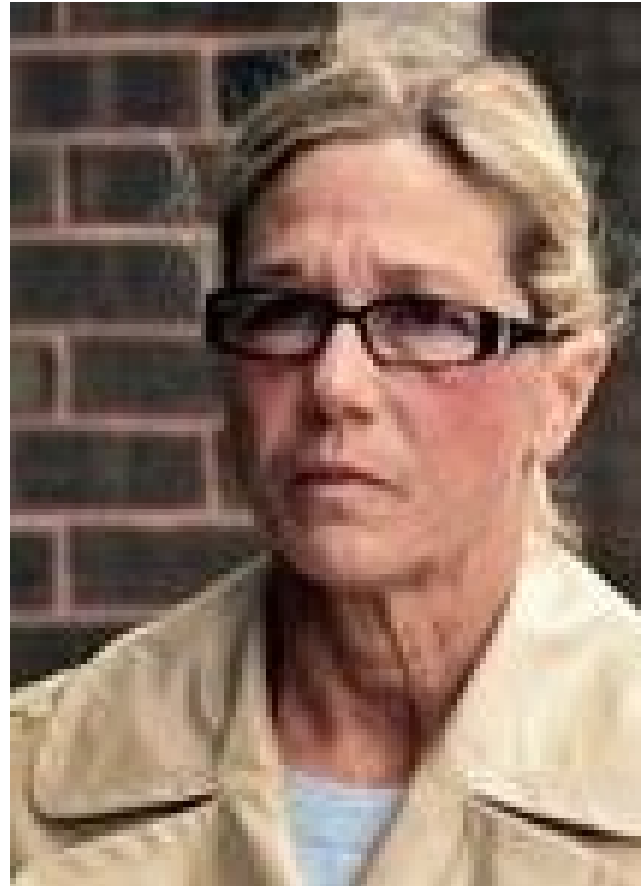
- **Meet Rita Crundwell:**

Worked for Dixon, IL for almost 30 years

Owned 400 horses with a salary of \$80K

Described as:

- Sweet as pie
- Couldn't find a nicer person on the face of the planet
- Nicest person to work for
- If you needed something she'd give it to you



Lavish Lifestyle

- State of the art horse facilities
- \$2.1M home
- \$259K horse trailer
- Second home in Florida
- Expensive jewelry
- Fur coats
- Etc.

The Embezzlement

- \$53M over 22 years
- Started small & grew over the years
- Transferred funds to a fake bank account in the City's name
- Checks made payable to "Treasurer"
- Fake invoices for capital projects shown to auditors
- No segregation of duties
- When asked by the Commission about budget shortfalls, she said the state was late disbursing funds
- Caught by City Clerk while on extended vacation

Most Common Types of Fraud in Public Sector



Occupational Fraud

- Top occupational frauds in public sector
- Corruption (52%)
- Billing (24%)
- Payroll (18%)
- Noncash, Cash Larceny & Expense Reimbursement (each 15%)

FIG. 26 WHAT ARE THE MOST COMMON OCCUPATIONAL FRAUD SCHEMES IN VARIOUS INDUSTRIES?

Industry	Cases	Billing	Cash larceny	Cash on hand	Check and payment tampering	Corruption	Expense reimbursements	Financial statement fraud	Noncash	Payroll	Register disbursements	Skimming
Banking and financial services	305	12%	12%	18%	14%	44%	6%	5%	16%	4%	4%	8%
Manufacturing	175	27%	6%	4%	7%	55%	17%	6%	29%	10%	1%	9%
Government and public administration	170	24%	15%	8%	14%	52%	15%	4%	15%	18%	4%	11%
Health care	117	38%	9%	8%	12%	47%	21%	1%	22%	16%	2%	9%
Energy	78	19%	8%	9%	8%	60%	13%	4%	29%	10%	3%	6%
Retail	78	17%	10%	13%	5%	40%	6%	0%	32%	3%	9%	14%
Construction	73	38%	12%	7%	19%	52%	25%	10%	25%	23%	4%	23%
Education	70	36%	9%	13%	10%	43%	17%	0%	16%	7%	6%	19%
Insurance	69	19%	6%	6%	20%	49%	12%	9%	16%	10%	6%	9%
Technology	65	28%	9%	2%	9%	65%	11%	3%	32%	14%	0%	5%
Transportation and warehousing	60	18%	10%	18%	7%	52%	12%	2%	33%	10%	3%	7%
Religious, charitable, or social services	58	36%	17%	24%	17%	45%	29%	3%	10%	7%	2%	16%
Information	52	15%	10%	10%	0%	62%	10%	2%	27%	6%	0%	10%

Source: ACFE 2024 Report to the Nations

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Corruption

Dishonest conduct by those in power



Categories of Corruption

- Bribery
- Kickbacks
- Illegal gratuities
- Economic extortion
- Undisclosed conflict of interest

Red Flags for Corruption

- Off-book fraud, so can be difficult to detect
- Payments often do not go through the organization's accounting records
- Payments can be anything of value, not just cash
- Look for behavioral red flags in employees & vendors
- Look for internal control deficiencies in the procurement process
- Look for lack of transparency & documentation in the procurement process

Behavioral Red Flags

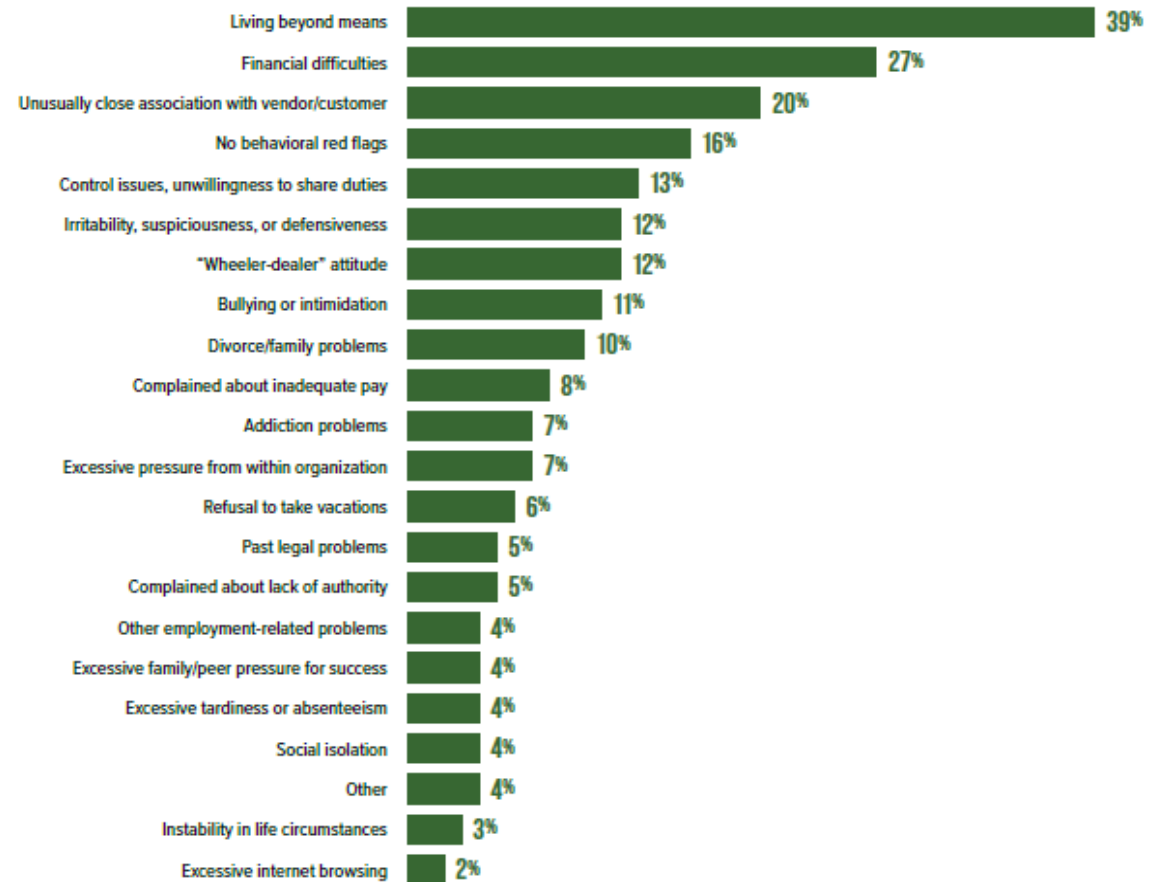
My experience

- Living beyond means
- Too close association with vendors/customers
- Control issues, unwillingness to share duties
- Wheeler-dealer attitude

Digital forensics

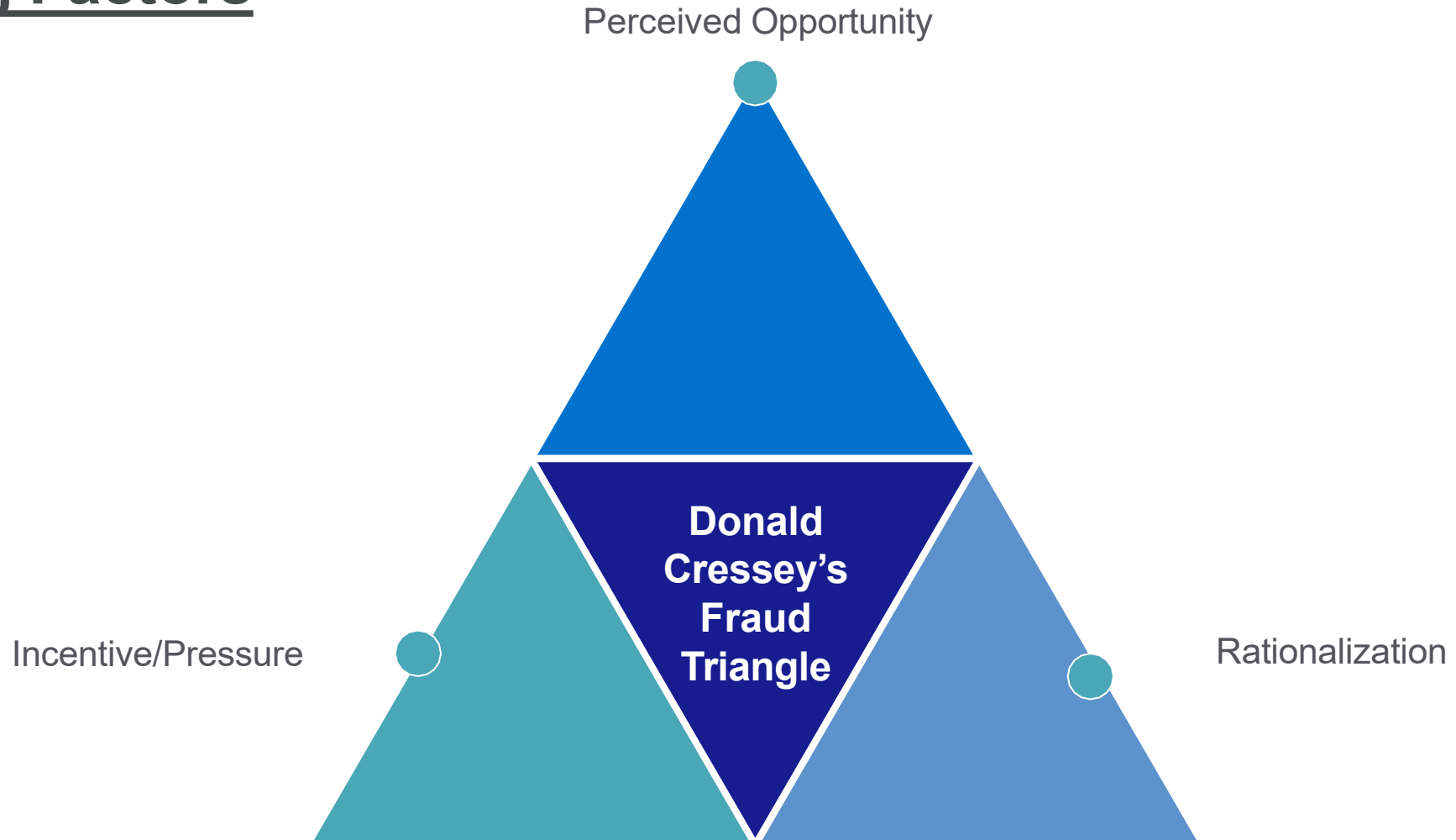
- Always check the browsing history on their work computer for evidence of online gaming or checking on casino loyalty/reward points

FIG. 54 HOW OFTEN DO PERPETRATORS EXHIBIT BEHAVIORAL RED FLAGS?

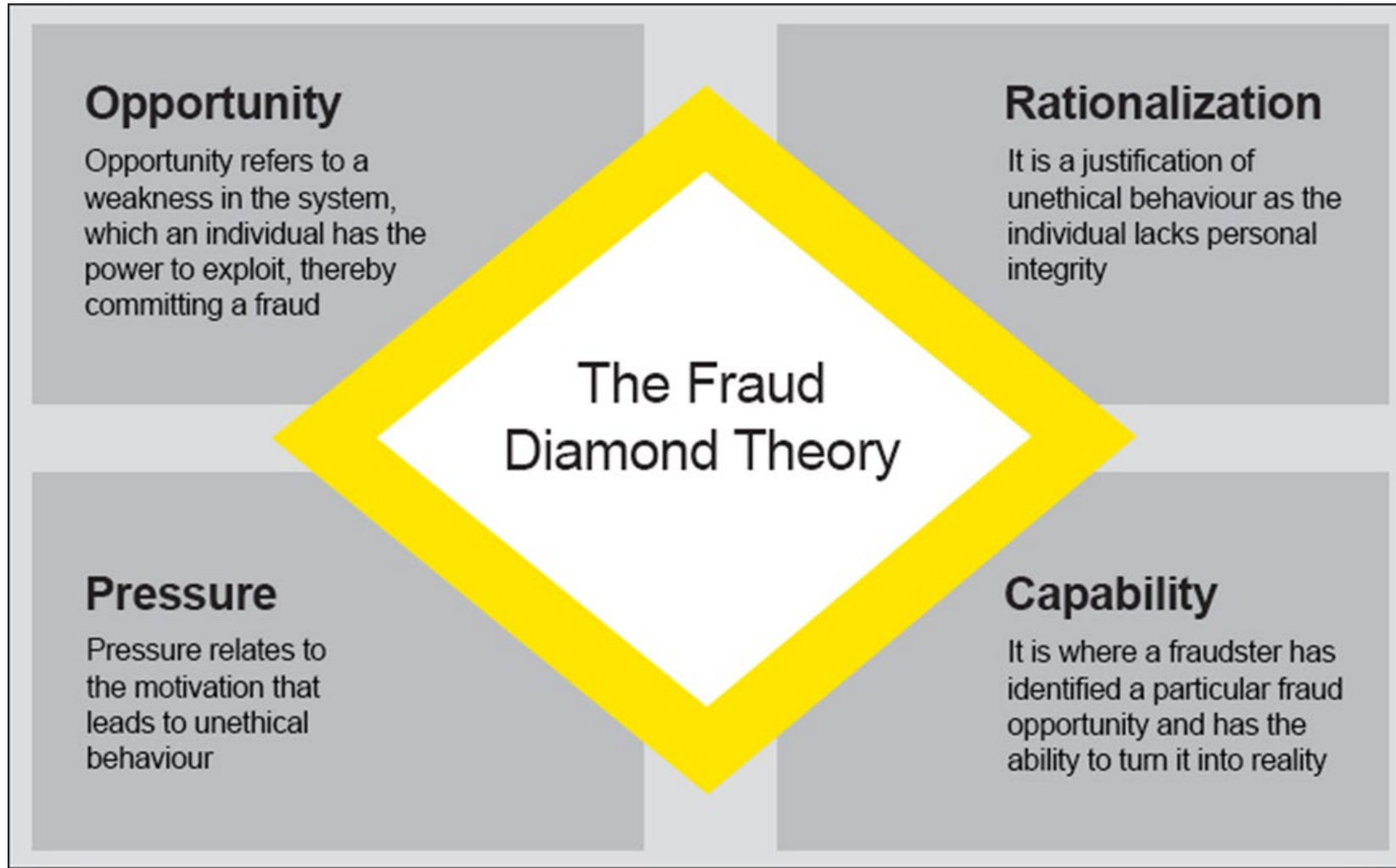


Source: ACFE 2024 Report to the Nations

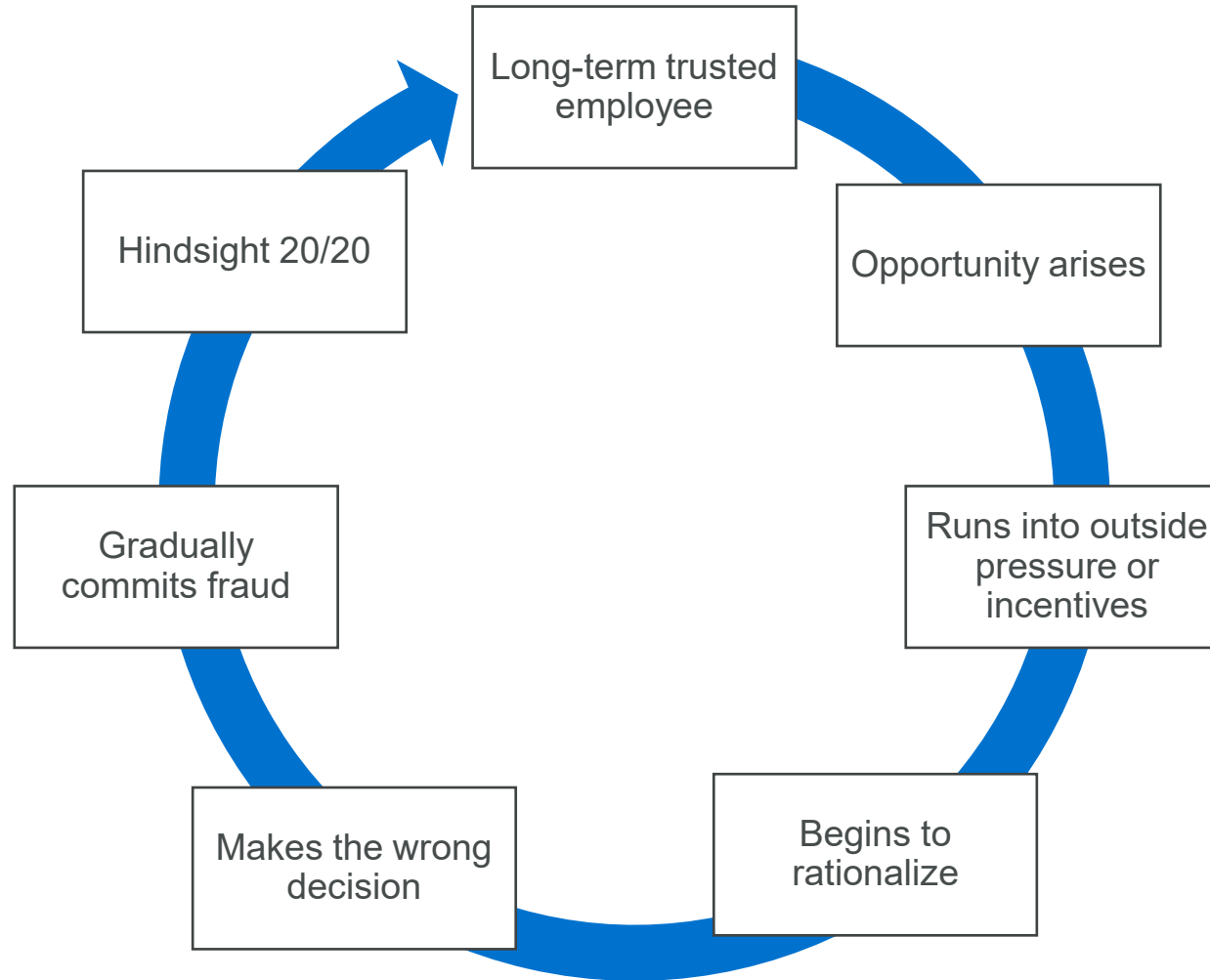
Enabling Factors



Fraud Diamond



The Fraud Cycle



Data Analytics for Corruption

- Compare order quantity to optimal reorder quantity
- Compare purchase volumes/prices from like vendors
- Compare quantities ordered & received
- Check for inferior goods (# of returns by vendor)
- Text analytics (analyze the suspected fraudster's email ...)

Prevention & Detection Guidance

- Clearly written policies & procedures, particularly in the procurement area, that provide for appropriate competition
- Monitoring of compliance with policies & procedures
- Transparency
- Protest function
- Fraud or ethics hotline

Billing Fraud



Billing Schemes

- Fraudster creates false support for a fraudulent purchase, causing the organization to pay for goods or services that are nonexistent, overpriced, or unnecessary
- Invoicing via shell company (fictitious vendor)
- Invoicing via an existing vendor
 - False invoicing for non-accomplice vendors
 - Pay-&-return schemes
- Personal purchases with organization's funds

Red Flags for Billing Fraud

- Vendors that seem unusual or are unapproved
- Increases in payments to a vendor without corresponding increase in goods/services
- Very large payments to one vendor
- Vendor prices that seem unusually low or high
- Repeated purchases from a vendor with a record of poor-quality goods/services
- Sequential invoices
- Invoices that look unprofessional or photocopied
- Invoices missing key information such as address or phone number

Prevention & Detection Guidance

- Segregation of duties
- Implement policies for providing appropriate verification of any changes to existing invoices, bank deposit information, & contact information
- Use purchase orders or require separate approvals of invoices
- Separate bank reconciliation from bill payment
- Keep the vendor master file current

Payroll Fraud



Payroll Schemes

- Falsified wages – employees claim hours they did not work or falsify their timesheets in some form or fashion
- Unauthorized bonuses – payment of bonuses not authorized by management
- Mid-month draws – mid-month payment not deducted from the normal salary, giving employee compensation not earned
- Ghost employees – payments to former employees or employees who do not exist
- Benefit schemes – receiving benefits or extra compensation not earned, such as excessive leave

Red Flags in Payroll

- Although payroll is usually an automated function, it is a vulnerable area, especially if collusion is involved
 - Inconsistent overtime hours for a cost center
 - Overtime charged during a slack period
 - Overtime charged for employees who normally would not have overtime wages
 - Budget variations for payroll by cost center
 - Same employee assigned to multiple departments
 - Employee in payroll but not on phone list or active employee files

Data Analytics for Payroll Fraud

- Employees with duplicate SSN, names, addresses, phone numbers, or bank account numbers
- Employees with no sick/vacation/time off
- Employees with few or no payroll deductions
- Employees with no bank account information for electronic payments
- Payments before hire or subsequent to termination

Prevention & Detection Guidance

- Segregation of duties
- Ensure payroll employees take vacations
- Periodically review payroll reports for anomalies
- Review employee addresses & bank account numbers to determine if multiple payments are going to the same address or bank account
- Periodically review benefit reports for anomalies, such as an employee who has selected no benefits

Prevention & Detection Guidance

- Departments should review payroll distribution lists for reasonableness
- Monitor overtime payments for reasonableness, support, & approval
- Review leave accruals for reasonableness

Noncash Fraud



Noncash Schemes

- Noncash fraud occurs when employees steal their employer's noncash assets such as information, inventory, equipment, fixed assets, or supplies
 - Stealing government property from databases, warehouses, or storage areas
- It also occurs when employees use their employer's information, inventory, equipment, fixed assets, or supplies without authorization for personal purposes
 - Government proprietary information sold to an unauthorized third party
 - Government intellectual property stolen for unauthorized use or sale
 - Government vehicle used to move a relative's household
 - Government equipment/machinery used to complete private work of an employee
 - Government computer & time used by employee to write a book

Red Flags for Noncash Schemes

- Increase in purchased inventory, but no increase in sales
- Abnormal inventory shrinkage
- Abnormal after-hours access to inventory storage area or databases
- Lack of physical security over assets/inventory
- Lack of appropriate controls over data

Prevention & Detection Guidance

- Segregation of duties
- Appropriate internal property handling policies with documentation
- Physical safeguards
- Periodic property inventories
- Periodic review of database user access including dates & times accessed

Expense Reimbursement & Purchasing Card Fraud



Expense Reimbursement/P-Card Schemes

- Any scheme in which an employee makes a claim for reimbursement for fictitious or inflated business purchases or expenses
- Employee files fraudulent expense report, claiming personal travel, nonexistent meals, etc., as incurred business expenses
- Employee purchases personal goods/services & charges to or requests reimbursement from the employer

Red Flags for Expense Reimbursement/P-Card Schemes

- Employee becomes defensive when asked to provide supporting documentation
- Unusual or excessive reimbursements to one employee
- Expenses claimed on days employee did not work
- Purchases that do not appear to be business related
- Photocopies of receipts are provided instead of originals
- Parts of dates or amounts on receipts appear to be altered or missing
- Insufficient or nonexistent supporting documentation
- Submitted receipts are consecutively numbered
- Expenses in round dollar amounts
- Expenses just below receipt submission threshold

Data Analytics for Expense Reimbursement/P-Card Schemes

- Identify transactions on weekends, holidays, or while employee is on vacation
- Identify split transactions in which a large purchase is split into smaller transactions just under approval threshold
- Identify unusually high or frequent expense reimbursement/p-card usage
- Identify expenses in round dollar amounts
- If utilizing “bankcard” electronic data, ask for Level 3 data

Prevention & Detection Guidance

- Get supporting documentation for purchases
 - Itemized receipts – not just credit card statement
- Address possible weaknesses in review process
 - No review/weak review
 - Wrong person doing the review
- Question any potentially inappropriate purchases
- Strengthen expense-/purchase-related policies
- Do not allow personal purchases on corporate credit cards/p-cards as a standard practice

Questions?

