
FRAUD: It can't happen to us . . . CAN IT?

Michael T. Lewis, CFA, Partner
Christina Solomon, CPA, CFE, Manager

February 15, 2008

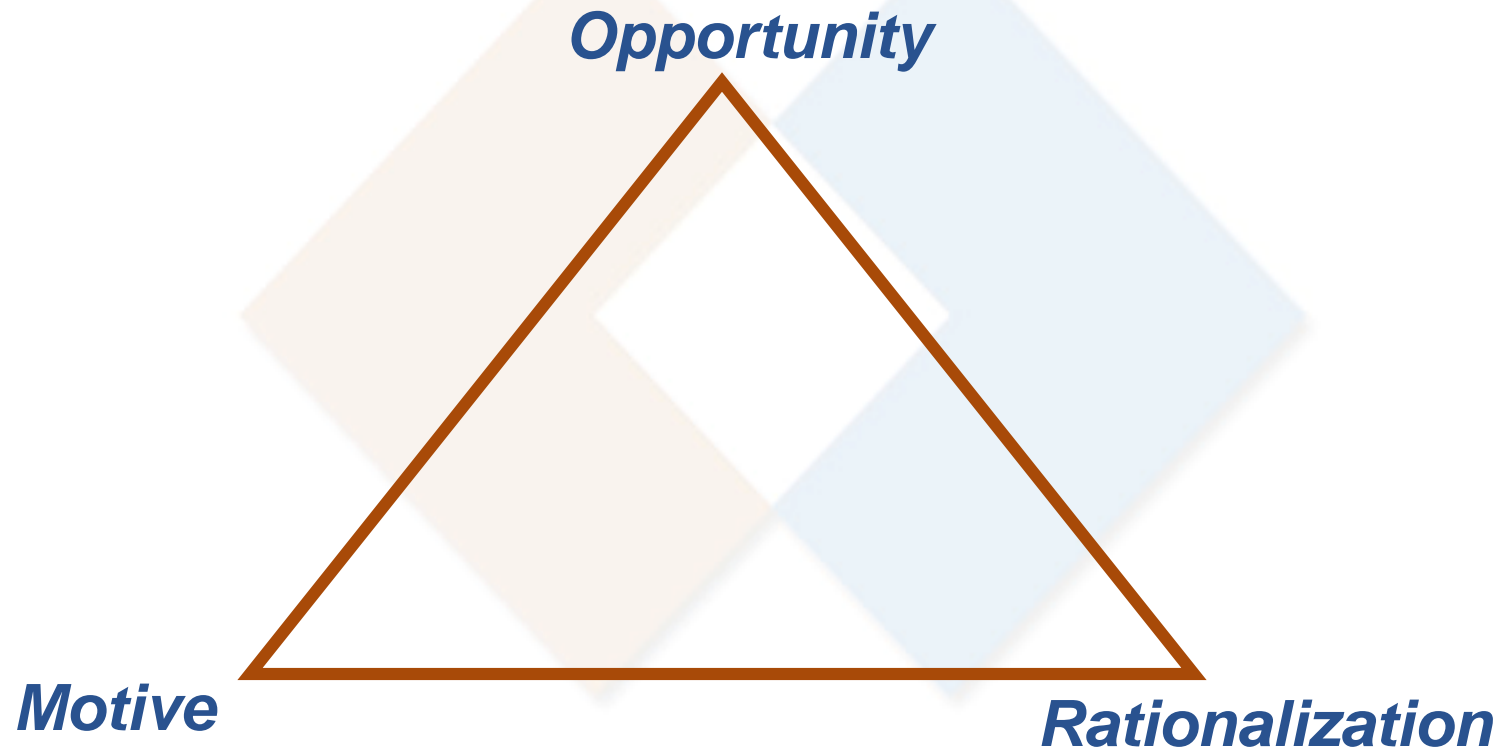
Objectives

- ❖ Prevalence of fraud
- ❖ Identify fraud schemes and risk factors
- ❖ Value of internal controls

Common Myths

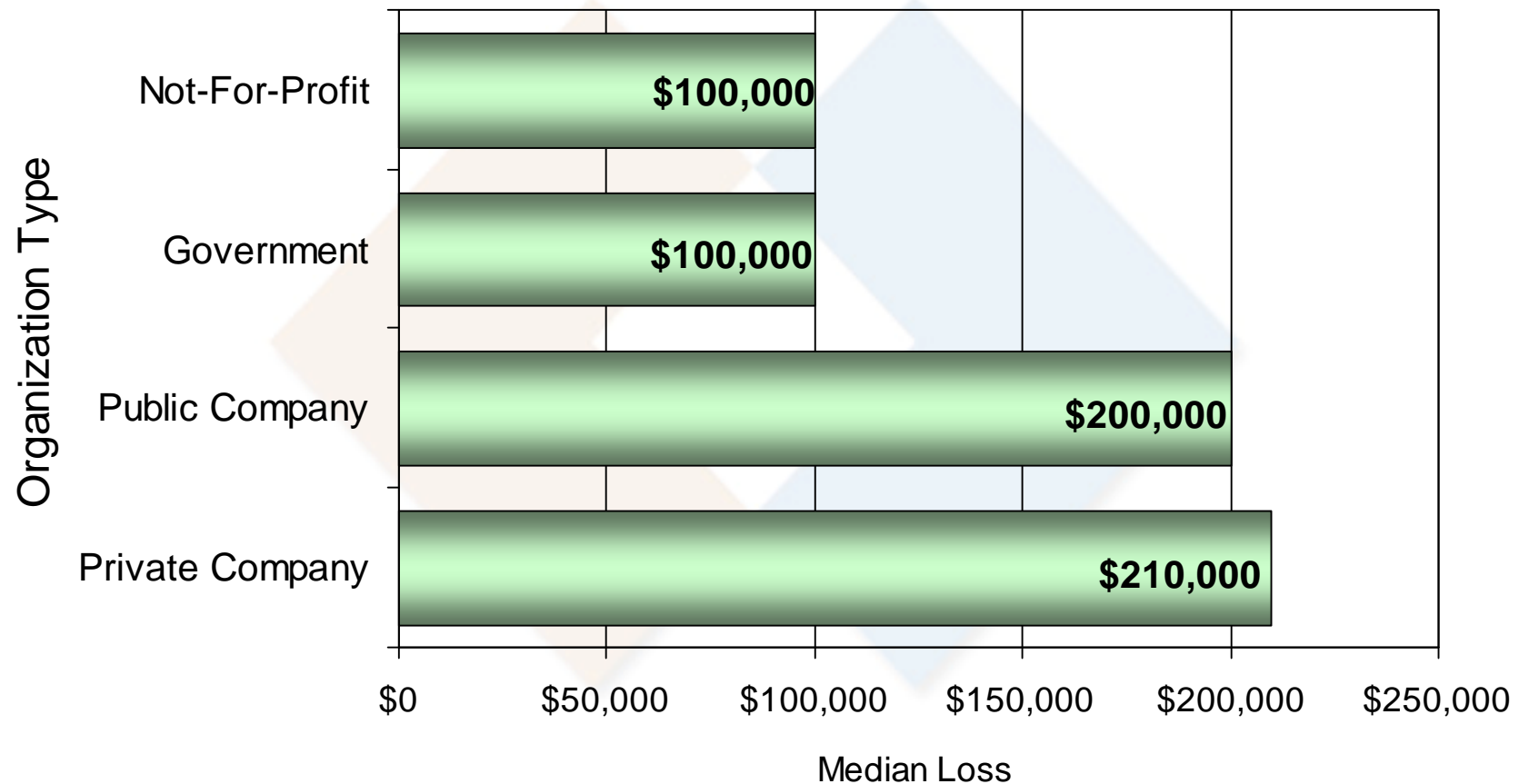
- ❖ Our people won't commit fraud
- ❖ Fraud is immaterial
- ❖ Fraud is complex and undetectable
- ❖ Prosecuting deters others

The Fraud Triangle



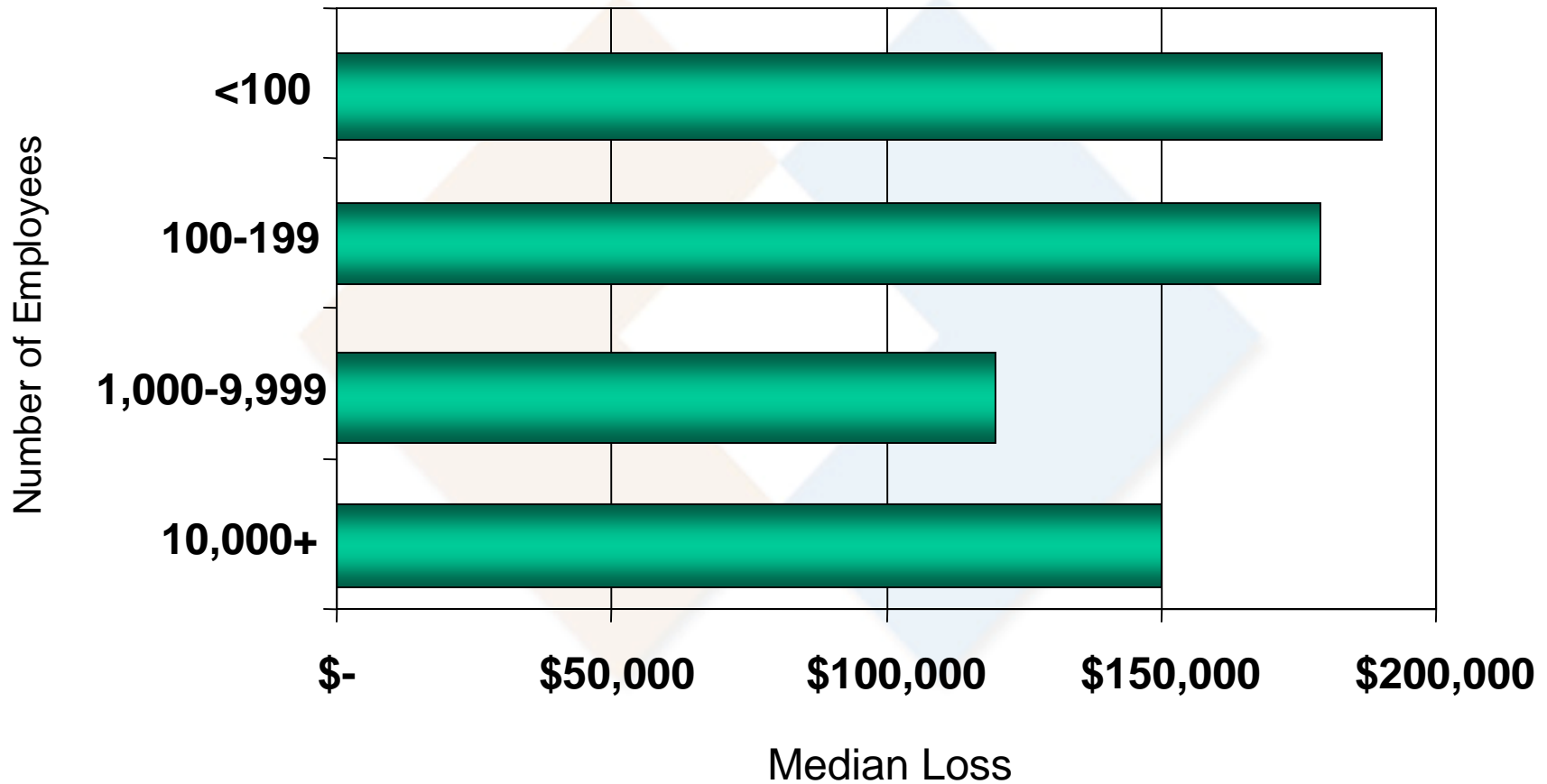
Source: "Why Employees Commit Fraud" by Joseph T. Wells, www.ACFE.com

Impact on Victim Organization



Source: 2006 ACFE Report to the Nation on Occupational Fraud & Abuse

Impact on a Victim Organization



Source: 2006 ACFE Report to the Nation on Occupational Fraud & Abuse

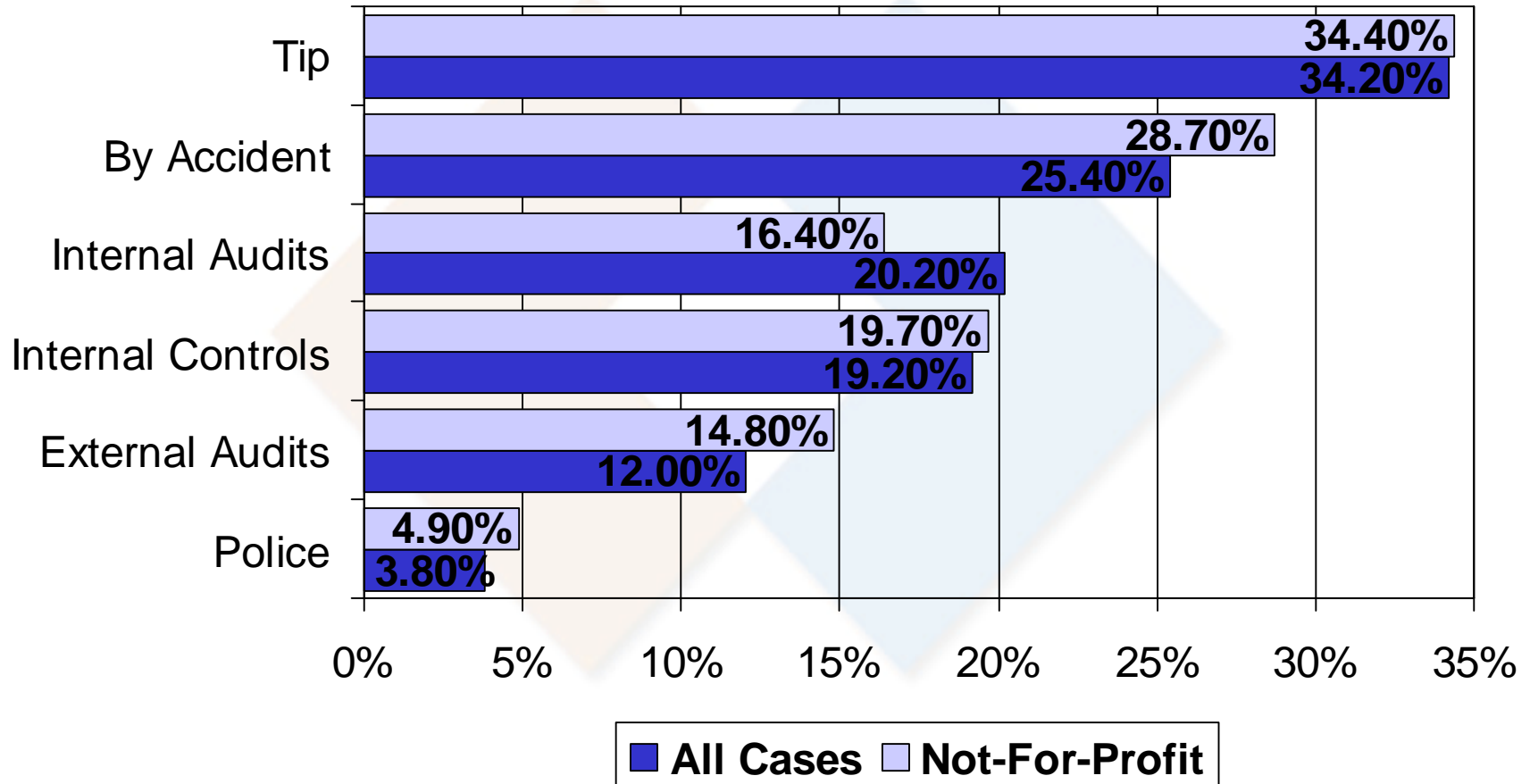
Fraud Schemes

Not-For-Profit Organizations (147 Cases)

Scheme	Cases	%
Corruption	43	29.3%
Billing	42	28.6%
Expense Reimbursements	42	28.6%
Check Tampering	36	24.5%
Skimming	33	22.4%
Cash Larceny	26	17.7%
Non-Cash	21	14.3%
Payroll	19	12.9%
Fraud Stmt	8	5.4%
Wire Transfers	8	5.4%
Register Disbursements	1	0.7%

Source: 2006 ACFE Report to the Nation on
Occupational Fraud & Abuse

Detecting Fraud



Source: 2006 ACFE Report to the Nation on Occupational Fraud & Abuse

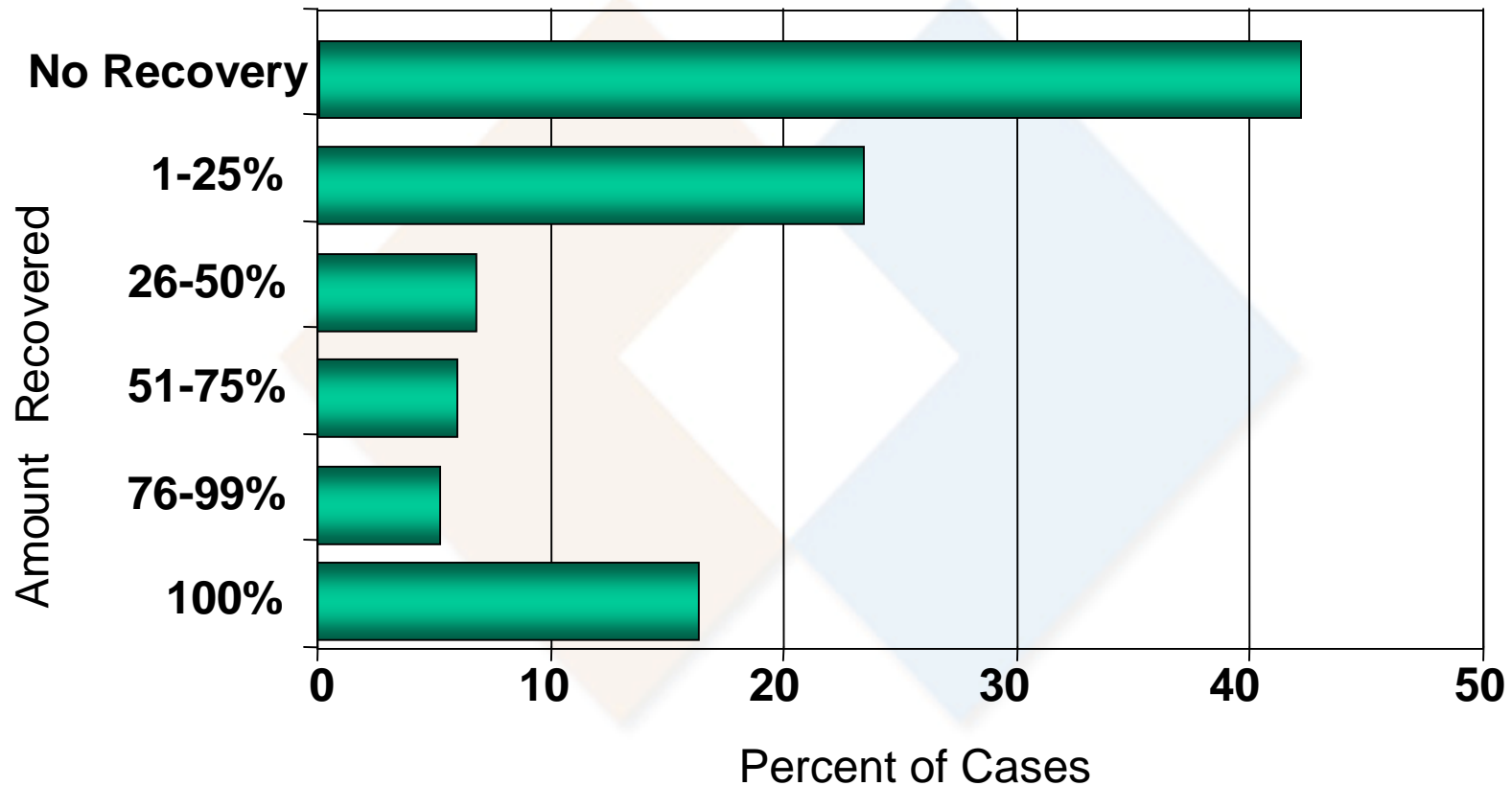
Anti-Fraud Measures

Not-For-Profit Organizations (147 Cases)

Control	Cases	%
External Audit	104	70.7%
Internal Audit	67	45.6%
Fraud Training	50	34.0%
Surprise Audits	47	32.0%
Hotline	33	22.4%

Source: 2006 ACFE Report to the Nation on
Occupational Fraud & Abuse

Recovery of Losses



Source: 2006 ACFE Report to the Nation on Occupational Fraud & Abuse

Fraud: Common Threads

- ❖ Weak internal controls
- ❖ Too much trust
- ❖ Poor management oversight
- ❖ Lack of financial audit
- ❖ No background checks
- ❖ Lack of independent checks on bank credit card statements
- ❖ Failure to use a bank's fraud prevention tools

Billing Schemes

- ❖ Types of billing schemes:
 - ▶ Shell companies
 - ▶ Pass-through schemes
 - ▶ Pay and return schemes
 - ▶ Personal purchases

Red Flags: Shell Companies

- ❖ Invoices for unspecified consulting or other services
- ❖ Unfamiliar vendors
- ❖ Vendors with PO Box address
- ❖ Vendor name consisting of only initials
- ❖ Rapid increase in purchases
- ❖ Multiple monthly billings
- ❖ Address match
- ❖ Large billings broken up

Check Tampering

- ❖ Forged maker
 - ▶ forged signature
- ❖ Intercepted check
 - ▶ altered payee or forged endorsement
- ❖ Concealed check
 - ▶ Failure to review checks before signing
- ❖ Authorized maker
 - ▶ Signer prepares fraudulent disbursement

Red Flags: Check Tampering

- ❖ Voided checks
- ❖ Missing checks
- ❖ Checks payable to employees
- ❖ Altered or dual endorsements
- ❖ Customer complaints regarding payments

Expense Schemes

- ❖ Mischaracterized Expenses
- ❖ Overstated Expense Reports
- ❖ Fictitious Expenses
- ❖ Multiple Reimbursements

Non-Cash

- ❖ Access to confidential information
- ❖ Theft of intellectual property
- ❖ Inappropriate usage of organization assets (i.e. computers or software)

Types of Corruption

- ❖ Conflicts of Interest
- ❖ Bribery
- ❖ Illegal Gratuities
- ❖ Extortion

Internal Controls: Managing Risk



Internal Control Maturity Level



Controls: Cash Receipts

- ❖ Proper segregation of duties is key:
 - ▶ Receiving and recording payments
 - ▶ Use of lockbox
 - ▶ Daily deposits
 - ▶ “For deposit only” accounts
 - ▶ Bonded employees
 - ▶ Compare deposits to cash receipts journal

Controls: Cash Disbursements

- ❖ Check writing and Signing Considerations
- ❖ Check requisitions and other support
- ❖ Vendor Master Files

Controls: The Bank Statement

- ❖ Reconciliation should be independent from cash receipts and cash disbursements functions
- ❖ Review of bank statement
- ❖ Review of cancelled checks
- ❖ Review of reconciliation

Controls: Staffing Considerations

- ❖ Mandatory vacations
- ❖ Conflicts of interests
- ❖ Background checks
- ❖ Hotlines

Controls: Other Considerations

- ❖ Analytical review
- ❖ Reporting requirements
- ❖ Document policies and procedures
- ❖ Officer and Board responsibilities

If You Suspect Fraud

- ❖ Get the facts
- ❖ Contact employment law attorney
- ❖ Contact your CPA
- ❖ Read your fidelity bond
- ❖ Consider filing police report
- ❖ Consider prosecuting the fraudster

Objectives Revisited

- ❖ Statistics show prevalence of fraud
- ❖ Detailed some schemes and red flags
 - ▶ Be on the lookout!
- ❖ Need for internal controls

Questions?
