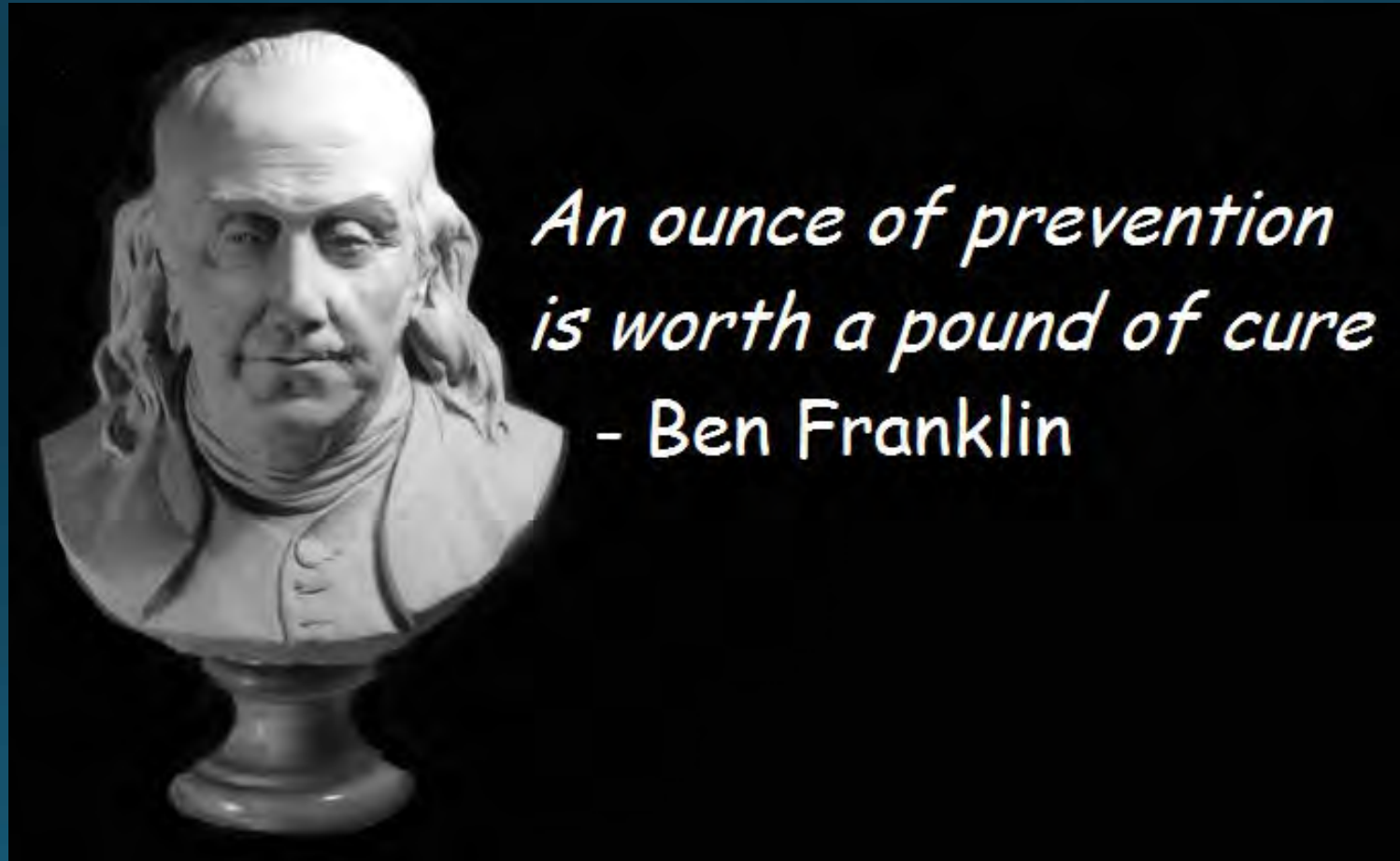


# Fraud Prevention



# Fraud Defined

Fraud is deliberate deception to secure unfair or unlawful gain from another person or their employer. Elements of fraud include:

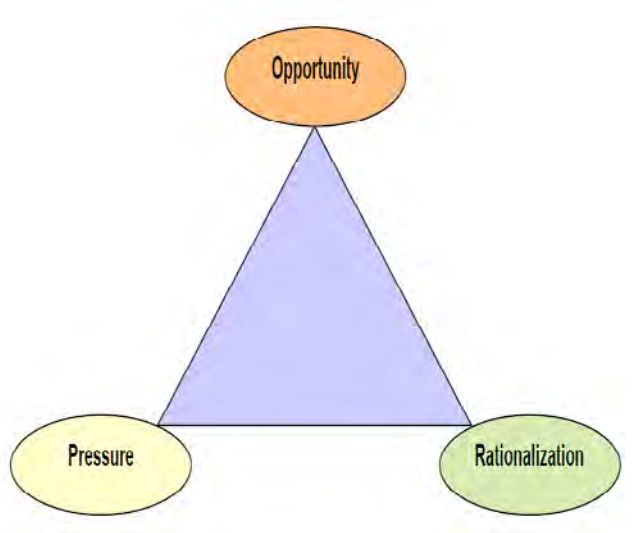
- A false representation, or concealment of a material fact;
- Made with the knowledge of falsity/intent to deceive;
- Inducing another person or the employer to act upon the representation, to his/her or the employer's detriment and;
- A gain or benefit to the perpetrator



# The Fraud Triangle

Model developed by  
Dr. Donald Cressey

Explains the factors that cause someone to commit occupational fraud, and consists of the following three components which, together, lead to fraudulent behavior:



- Perceived opportunity to misappropriate cash/assets
- Perceived Pressure: Motivation or incentive to commit acts.
- Rationalization: Justifications for dishonest acts

# Occupational Fraud



Internal fraud, also called *occupational fraud*, can be defined as:

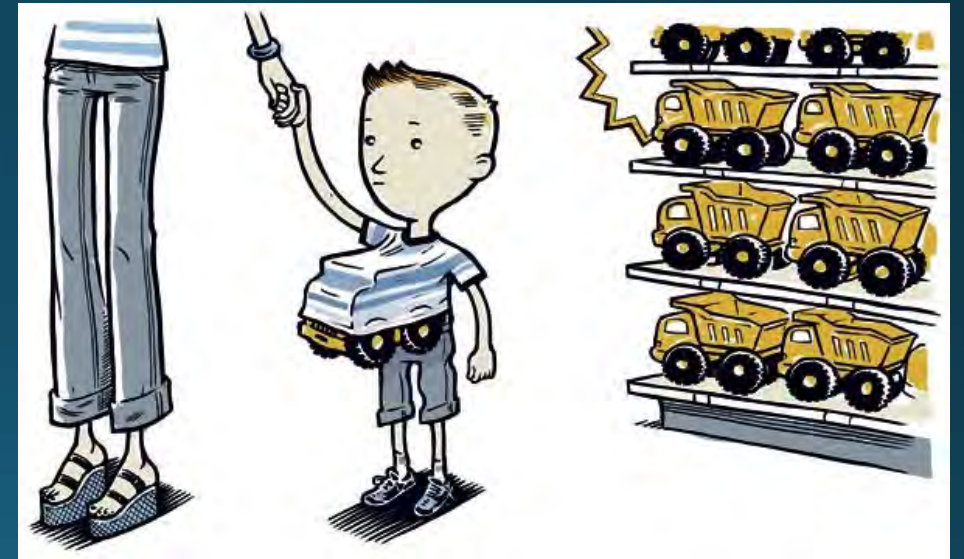
“The use of one’s occupation for personal enrichment through the deliberate misuse or misapplication of the organization’s resources or assets.” Simply stated, this type of fraud occurs when an employee, manager, or executive commits fraud against his or her employer.

# Examples of Occupational Fraud

## Asset Misappropriation:

The most common type of occupational fraud, which includes both theft and misuse of employer resources:

- Theft of cash on hand
- Theft of cash receipts
- Fraudulent disbursements
- Theft of inventory
- Misuse of assets



# Examples of Occupational Fraud

## Corruption:

- Conflicts of Interest
- Bribery
- Illegal Gratuities



## Financial Statement Fraud:

- Asset/Revenue Overstatements
- Asset/Revenue Understatements



# Extent of Occupational Fraud



- Asset Misappropriation

Occurs in > 83% of cases reported to ACFE

Median loss \$125,000

- Financial Statement Fraud

Occurs in < 10% of cases reported to the ACFE

Median Loss \$ 97,000

- Corruption

Occurs in >35% of cases

Median loss \$200,000

Source: The ACFE 2016 Report to the Nations on Occupational Fraud

# Opportunity, Pressure, and Rationalization



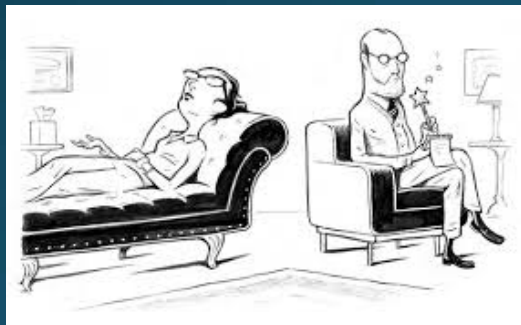
## Examples of Opportunity include:

- Inadequate or no supervision or review
- Inadequate separation of duties
- Lack of management approval for transactions
- Weak internal control systems



## Examples of Pressure include:

- Unrealistic deadlines
- Gambling /drug addiction/recent divorce
- Living beyond means
- Other financial/personal problems



## Examples of Rationalization (justification of actions) include:

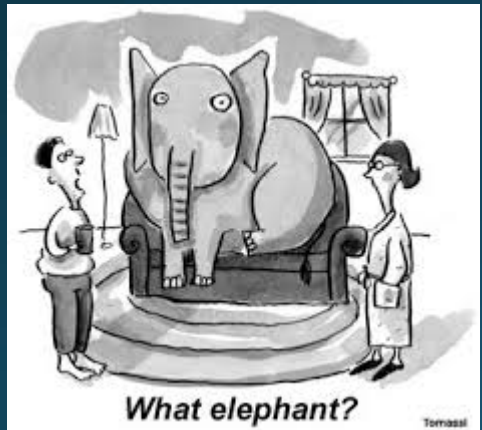
- "I deserve this. No one will find out anyway."
- "I can't afford to lose my home, my car, etc."
- "I really need the money and will put it back."
- "I'm underpaid."

# Behavioral Red Flags of Fraud



A red flag is a set of circumstances that is unusual in nature.

It is a signal that something may be out of the ordinary, and may need to be investigated further.



Red flags do not indicate guilt or innocence, but merely provide possible warning signs of fraud.

# Examples of Red Flags

## Employee Red Flags

- Lifestyle changes
- Significant personal debt
- Refusal to take vacation
- Behavioral changes

## Management Red Flags

- Reluctance to provide information to auditors
- Weak internal controls
- High employee turnover
- Excessive # year end transactions
- Override controls

## Cash or Accounts Receivable

- Excessive voids/discounts/returns
- Bank accounts not reconciled timely
- Out of sequence/missing cash receipt numbers
- Vendors complaints - receiving notices of non-payment

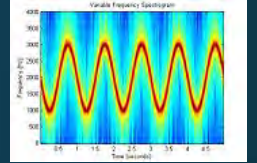
## Payroll

- Inconsistent overtime
- Employees with no/few deductions
- Duplicate SSN & addresses
- Overtime during slow periods

## Purchasing / Inventory

- Purchases that bypass normal controls
- Vendors without physical addresses
- Vendor addresses matching employee addresses
- Lack of physical security over assets or inventory
- Abnormal inventory shrinkage

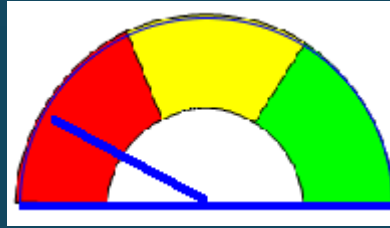
# Red Flags Exhibited - Occupational Fraud



<u>Red Flags</u>	<u>Asset</u>		
	<u>Misappropriation</u>	<u>Corruption</u>	<u>F/S Fraud</u>
Living Beyond Means	49%	49%	49%
Financial Difficulty	32%	24%	24%
Association with Vendor	18%	38%	14%
Wheeler-Dealer Attitude	15%	21%	24%
Control Issues	16%	16%	18%
Divorce	14%	11%	11%
Irritability	13%	14%	18%
Addiction	11%	7%	13%
Inadequate Pay	10%	10%	6%

Source: The ACFE 2016 Report to the Nations on Occupational Fraud

# Initial Detection of Occupational Frauds



- Tips
- Internal Audit
- Management Reviews
- By Accident
- External Audit
- Document Exam
- All other methods combined

39.00%

17.00%

13.00%

6.00%

4.00%

4.00%

17.00%

Total

100.00%

The best protection  
is early **detection**

Source: The ACFE 2016 Report to the Nations on Occupational Fraud

# Fraud Prevention Methods



- Authorization/approval authority in place for contracts/transactions
- Communicate that a fraud prevention program exists – helps serve as a deterrence to fraud
- Conduct continuous auditing – Sample transactions or metrics exceeding established thresholds
- Conduct audits – external and internal
- Conduct fraud/risk assessments
- Conduct periodic physical inventories – fixed assets, sensitive assets, and bench stocks
- Conduct surprise cash counts
- Eliminate the opportunity for fraud – strengthen/evaluate internal controls for key functions and activities
- Implement a fraud prevention/anti-fraud policy
- Implement a whistle blower hotline
- Organizational units monitor budgets – Budget vs. Actual (Revenue and Expense)
- Organizational units conduct variance analysis of their key metrics, including revenues and expenses
- Provide clear ethical policies/procedures that communicate expectations to employees, including penalties or expected outcomes for violating.

# What Should I Do if Fraud is Suspected?



## Options

- Report to your supervisor or manager, or through chain of command
- Report through the District's anonymous hotline – available online [4cd.edu](http://4cd.edu), or by phone - EthicsPoint Inc. at **855-433-9922** (toll-free)
- Contact Internal Audit Services (IAS) immediately, for an investigation, when there is suspicion of improprieties, violations to codes of conduct, or financial irregularities.
- Confirmed Impropriety - Report confirmed improprieties to IAS immediately upon receiving a confession. Do not attempt to negotiate/resolve with the employee/perpetrator.