What Were They Thinking? Detecting and Combating Fraud

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forv/s mazars

Meet the Presenter

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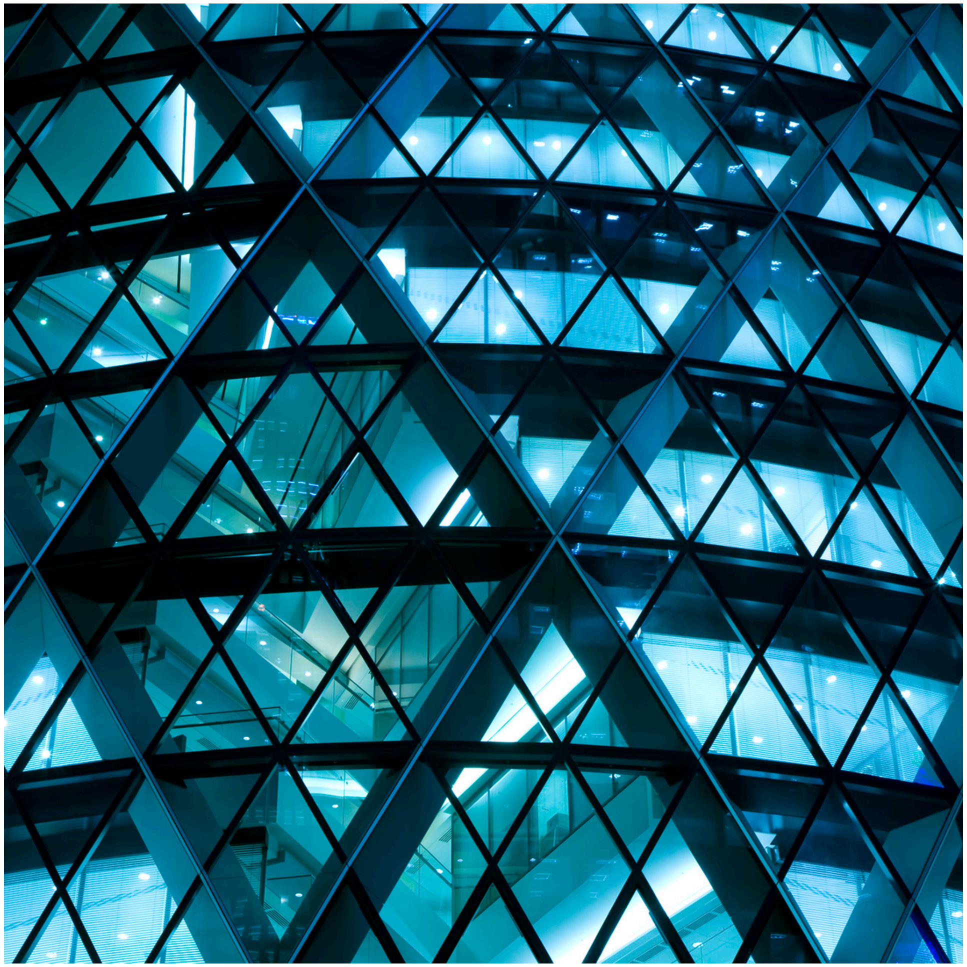
Meet the Presenter

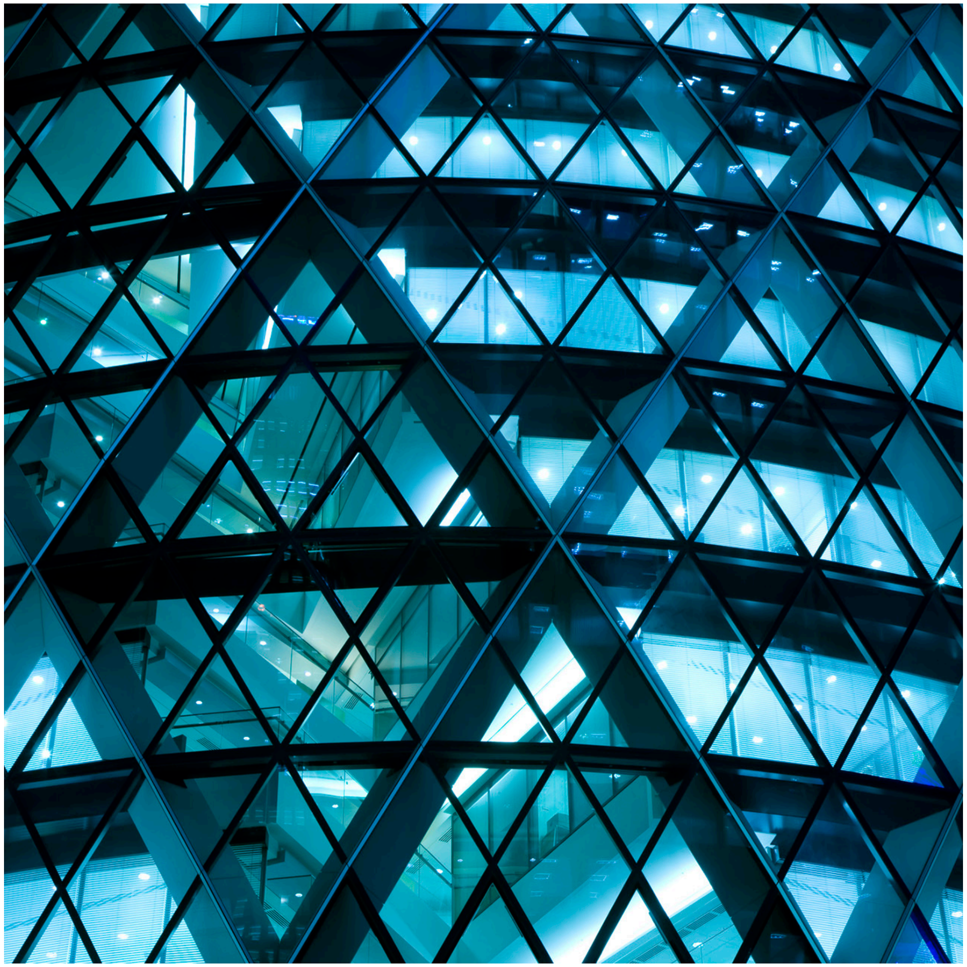
Agenda

1. Introduction
2. What is Fraud?
3. Why Do People Commit Fraud?
4. Most Common Types of Fraud
5. Fraud Deterrence and Prevention
6. Perpetrators of Fraud
7. Fraud Risk Assessment for Employees and Management
8. Fraud Risks in Remote Work Environments
9. AI – The Future of Fraud Detection
10. Tools and Tech of Fraud
11. Interesting Facts About Fraud



Key Takeaways

1. Outside factors contribute to someone committing fraud
2. Good people commit fraud
3. Focus on perceived opportunities
    - Take the person out of the picture – TRUST IS NOT A CONTROL
    - Assess the ENVIRONMENT, not the person
4. Perpetrators of fraud come in all sizes and shapes
5. Remote work can be a benefit to some and not to others.
6. How AI will affect fraud now and, in the future
7. Technology Tools can help with fraud detection and prevention



What is Fraud

What is Fraud

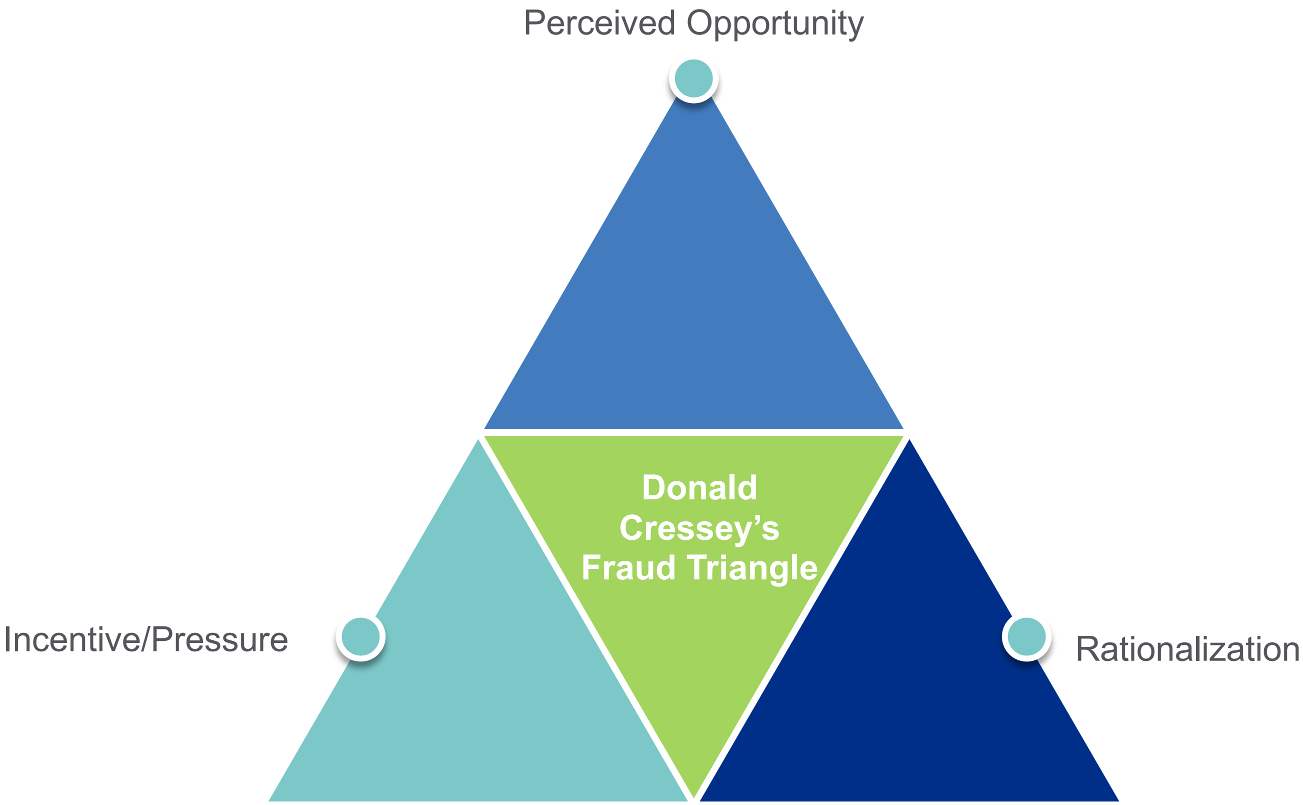
- Fraud is a deliberate act (**or failure to act**) with the intention of obtaining an unauthorized benefit, either for oneself or for the institution, by using deception or false suggestions or suppression of truth or other unethical means, which are believed & relied upon by others

What Is Fraud-Waste-Abuse?

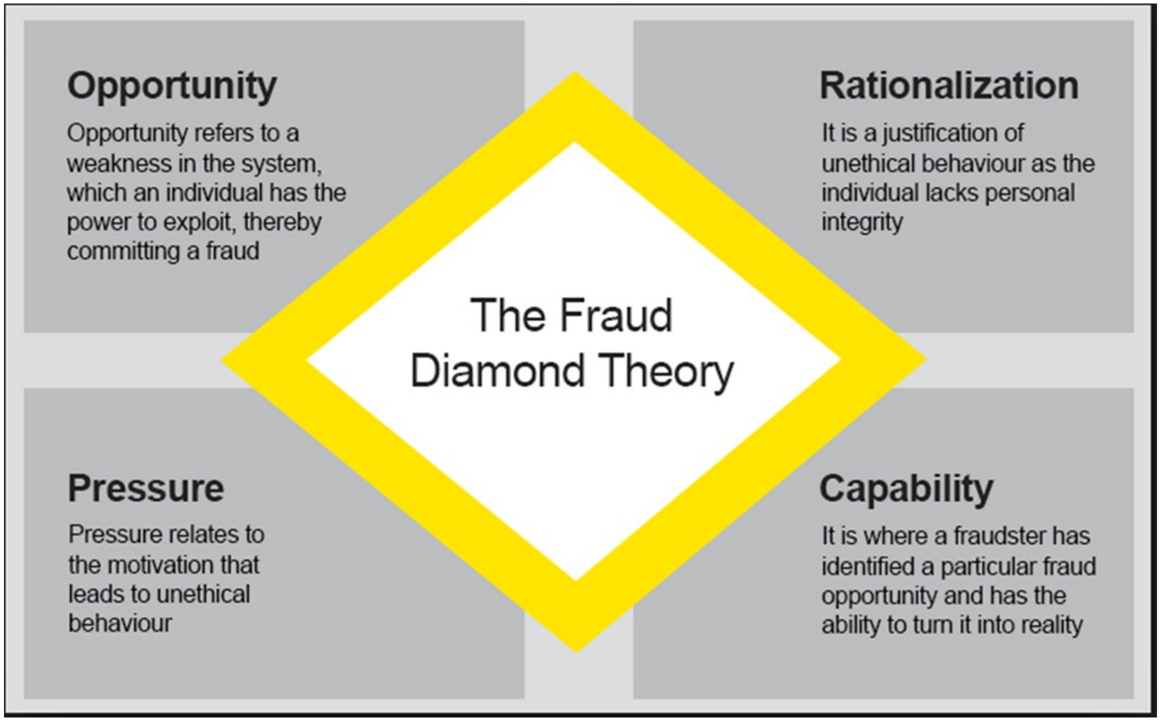
- Fraud—an attempt to obtain something valuable through intentional misinterpretation
- Waste—misuse of funds or resources through excessive or nonessential expenditures
- Abuse—occurs when there is an intentional & unacceptable use of grant funds or misuse of one's position

Why Do People Commit Fraud?

Enabling Factors



Fraud Diamond



The Fraud Diamond Theory

Opportunity

Opportunity refers to a weakness in the system, which an individual has the power to exploit, thereby committing a fraud

Rationalization

It is a justification of unethical behaviour as the individual lacks personal integrity

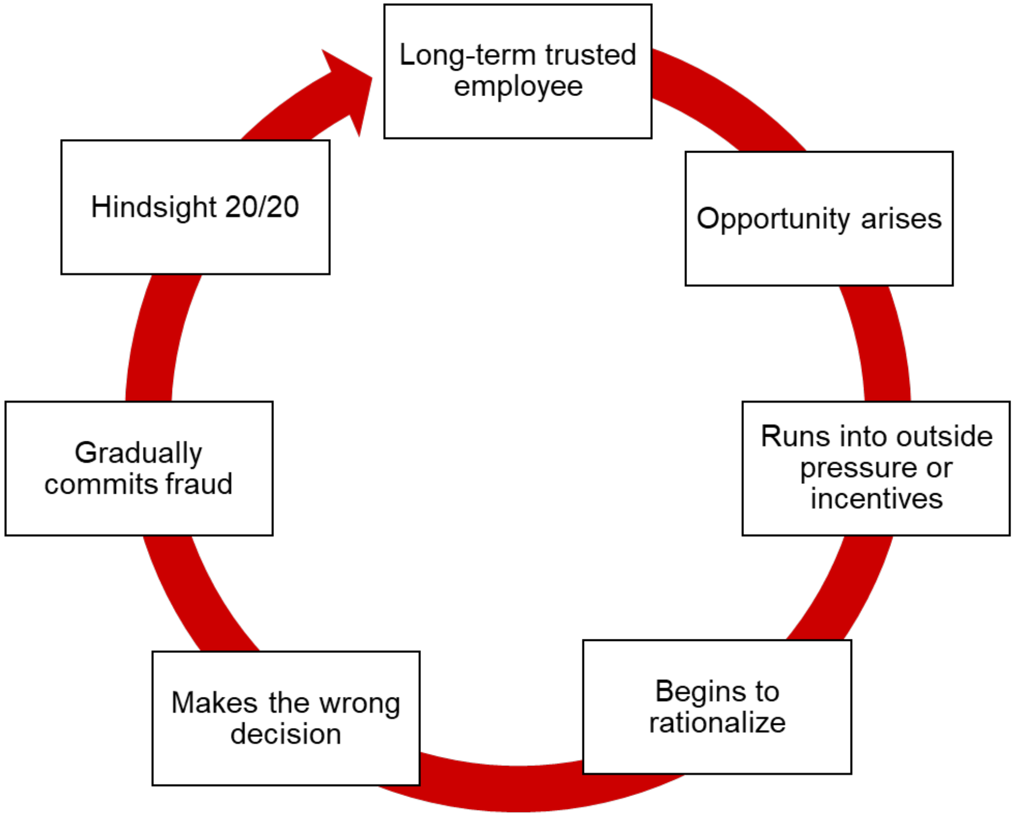
Pressure

Pressure relates to the motivation that leads to unethical behaviour

Capability

It is where a fraudster has identified a particular fraud opportunity and has the ability to turn it into reality

The Fraud Cycle



Long-term trusted employee

Opportunity arises

Runs into outside pressure or incentives

Begins to rationalize

Makes the wrong decision

Gradually commits fraud

Hindsight 20/20

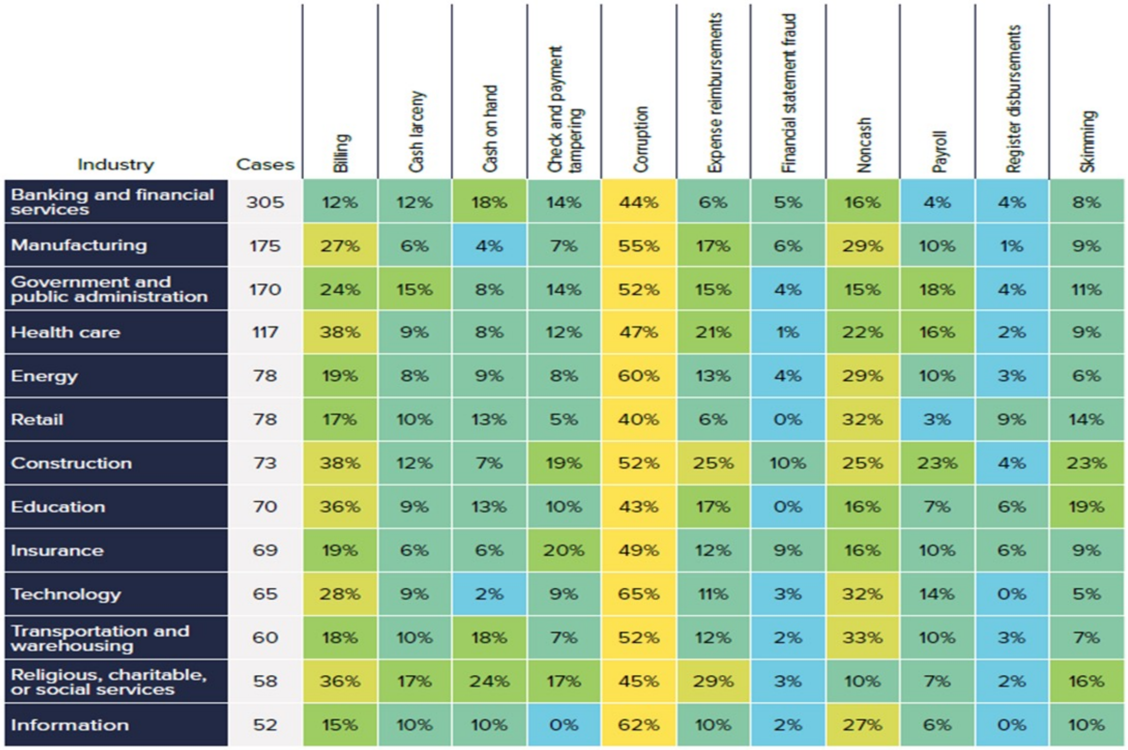
Most Common Types of Occupational Fraud

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%

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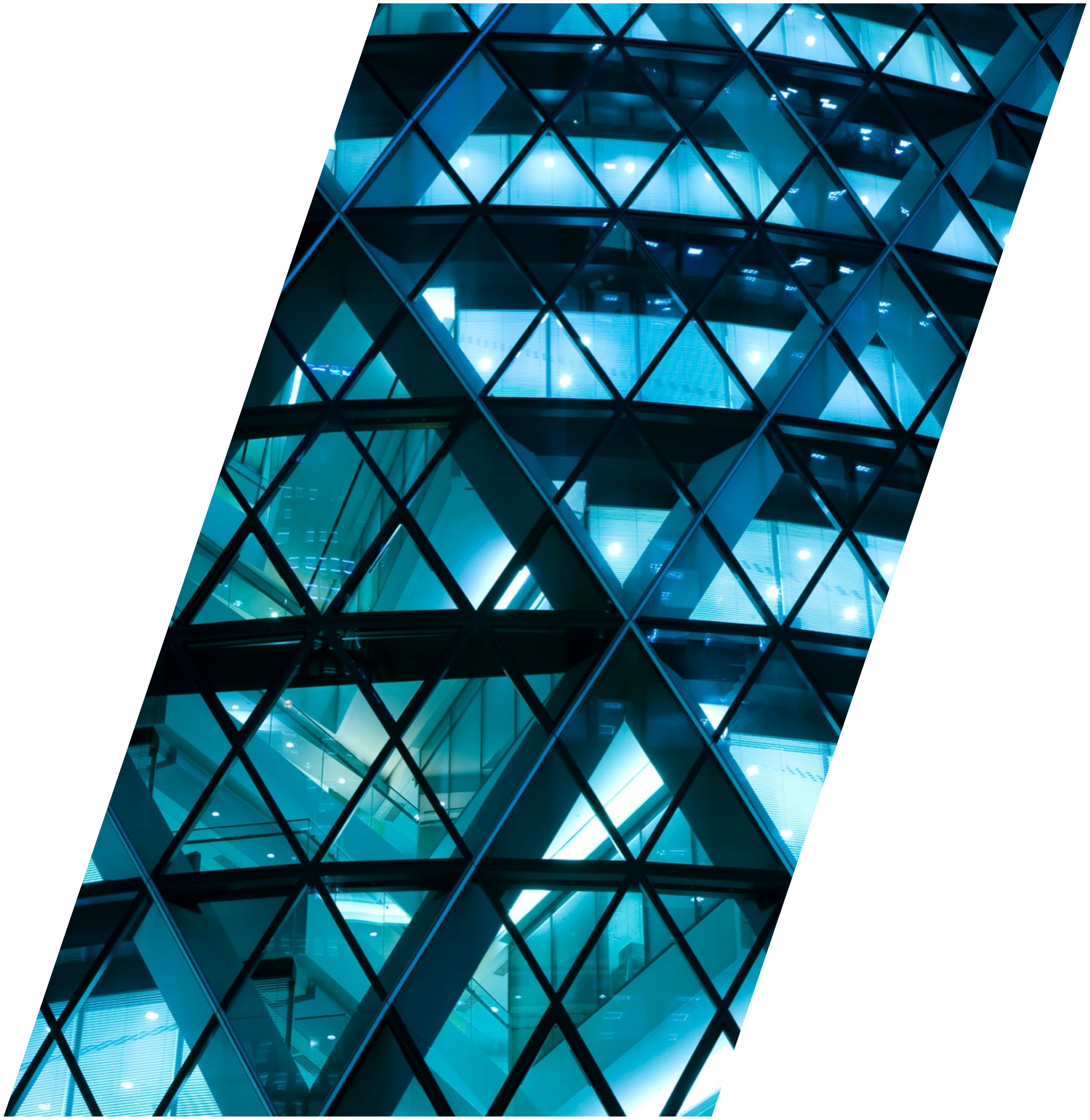
Corruption

Corruption is dishonest conduct by those in power.



City of Atlanta – Public Corruption

Corruption and Categories

Corruption is an off-book fraud, so it can be difficult to detect

Categories of Corruption

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

Red Flags for Corruption

- 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 Flags for Corruption

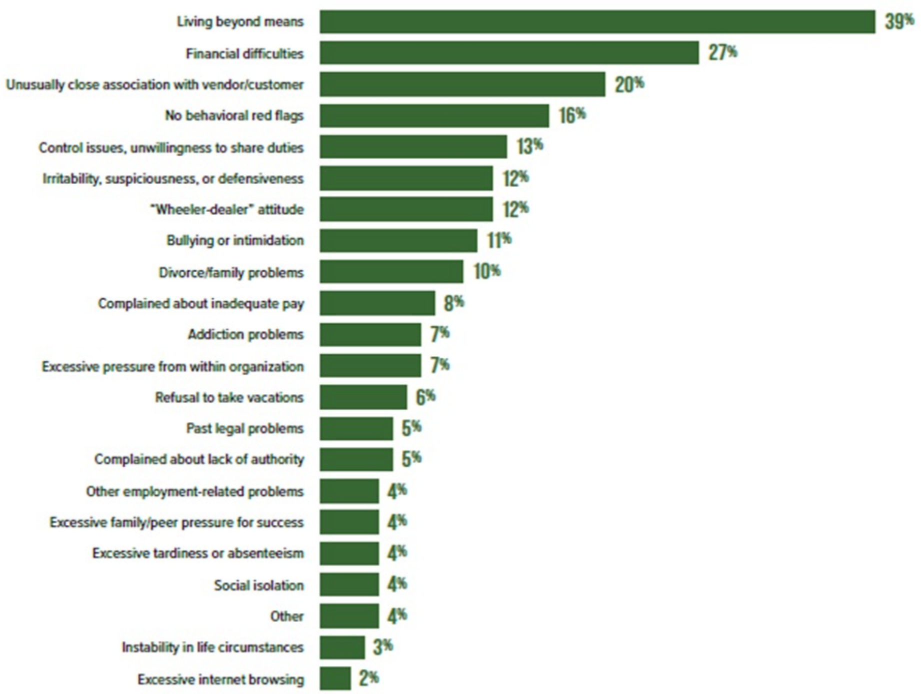
My experience

- 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?



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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

Fraud Deterrence & Prevention

Initial Detection of Occupational Frauds

FIG. 13 HOW IS OCCUPATIONAL FRAUD INITIALLY DETECTED?

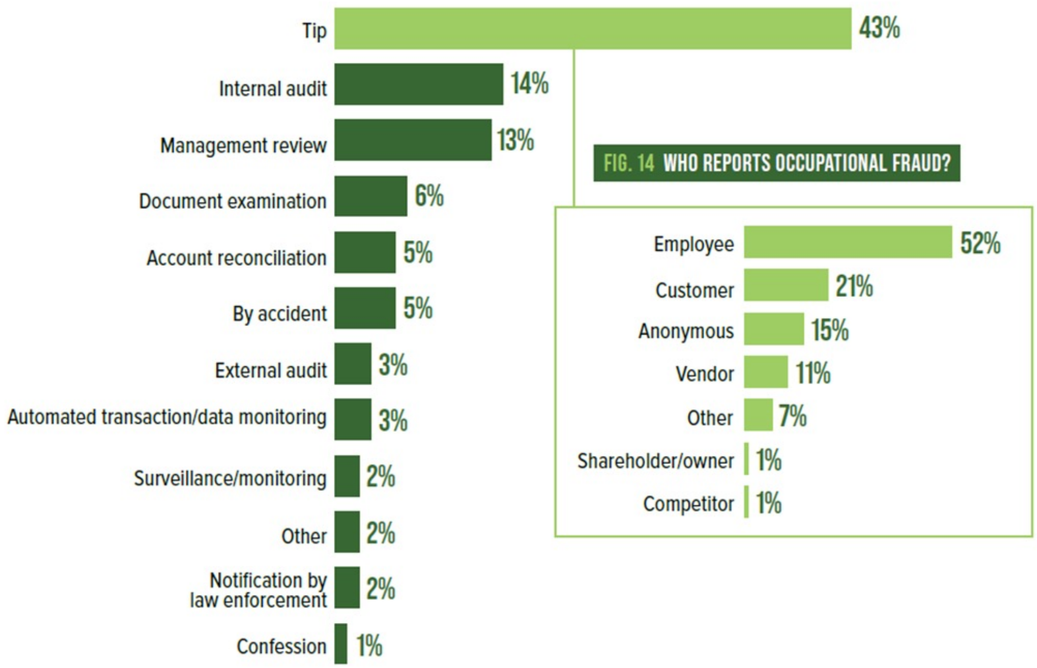

FIG. 14 WHO REPORTS OCCUPATIONAL FRAUD?

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Fraud Prevention Check-Up

- **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 Prevention Check-Up

- **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

Let’s Talk About “TRUST”

- **Trust**
  - ➢ Trust is not an internal control
  - ➢ Trust, at its core, is a firm belief in the reliability, honesty, and integrity of someone or something. It involves a willingness to be vulnerable, expecting that the person or thing you trust will act in a way that benefits you.
- **Trust Exercise**
  - ➢ Think of someone you trust.
  - ➢ What qualities do they possess?
  - ➢ What would you trust them with?
  - ➢ WHAT IF?

Fraud Prevention Check-Up

- **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

The Perpetrators of Fraud

Fraud Risk Assessment Employee & Management

Fraud Risk Assessment

Employee Assessment

- Are pre-employment background checks performed?
- Do employees feel they are treated & compensated fairly?
- 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?

Fraud Risk Assessment

Management Assessment

- Is the board of directors composed mainly of related individuals?
- Is the organization under pressure to report favorable earnings?
- 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?

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

Fraud Risks in Remote Work Environments

Challenges Associated with Remote Work

Occupational Fraud

- Time theft
- Locality cost of living
- Overemployment
- Steal corporate data and sensitive information

Low Productivity

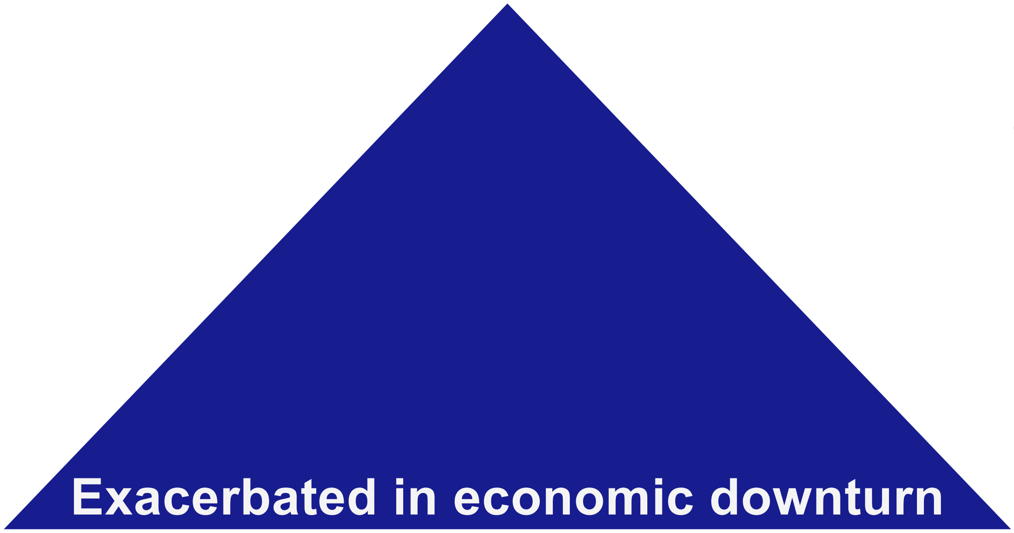
- Running errands
- Other leisure activities

External Data Theft and Cyber Threats

- Lowered sense of awareness of cybersecurity threats

Remote Work Can Increase Risk of Fraud

The biggest threat is from unsupervised employees



Exacerbated in economic downturn

Perceived Pressure

- Salaries that don’t keep abreast of inflation
- Financial situations

Opportunity

- Physical access and less strict IT controls
- Less managerial oversight

Rationalization

- Emotional disconnect with employer or team
- Many employers still striving to do more with less

Time Theft

Red Flags ⚐

- Not responding to emails, chats, or calls during business hours
- Not attending or joining late for phone or video call meetings
- Completing work assignments late
- Taking long or frequent breaks that are unaccounted for
- Logging a full day on timesheets despite starting late or ending early
- Logging a full day despite doing personal and/or non-work activities while on the clock, including outside employment
- Asking for overtime that a manager has not authorized
- Asking a colleague to clock-in and out for them (“buddy punching”)

Strategies for Combatting Time Theft

- Change KPI from time-based to achievement-based targets
- Schedule routine check-ins with employees to assess productivity
- Ask employees to work from the office a few days a week
- Use of technology platforms that indicate activity, or monitoring of computer or network activity logs and phone or video call logs
- Employer Code of Conduct, including penalties for violations, annually read and signed by employees

Overemployment/Moonlighting

Red Flags

- Candidate asks to be hired as a contractor
- Candidate’s CV has periods of overlapping employment
- Employee is slow to answer/return emails, chats, and calls
- Employee does not want to be on camera during video calls
- Technology platform/activity tracking indicates employee routinely works outside of normal work hours
- Employees work is often last minute, seems rushed, and often does not meet expectations

Strategies for Combatting Overemployment

- Discuss stance on moonlighting/overemployment in interview
- Employment contract prohibits moonlighting/overemployment
- Ad hoc check-ins with employees to assess productivity
- Ask employees to work from the office a few days a week
- Use of technology platforms that indicate activity, or monitoring of computer or network activity logs and phone or video call logs

Low Productivity

Red Flags

- Declining work quality
  - Frequent mistakes
  - Missed deadlines
- Decreased employee engagement
- Inability to reach reasonable goals
- Exhibiting stress in communications and interactions

Strategies for Combatting Low Productivity

- Emphasize performance rather than hours worked
- Provide the right technology
- Set reasonable goals
- Assist your remote employees in creating a dedicated WFH space
- Eliminate low-quality meetings where an email will suffice
- Practice inclusive communication
- Invest in professional development

Cybercrime

Risks for Remote Worker IT Security

- Weak passwords and lack of multifactor authentication
- Unsecured Wi-Fi networks
- Phishing attacks
- Unsecure home network devices
- Lack of security updates
- Data backup and recovery

Managing Remote Workers to Mitigate Fraud

- Culture of accountability
- Policies regarding remote work
- Cybersecurity training and requirements
- Time-tracking software
- Flexible work schedules
- Office-issued equipment and devices

AI – The Future of Fraud Detection

AI Uses in Fraud Detection

Automated Anomaly Detection

- Unusual transaction amounts
- Multiple transactions from the same device
- Purchases made from different locations in a short period of time

Behavioral Analysis

- Purchases outside of normal spending habits

Natural Language Processing

- Analyze individual communications (email or chats) to identify indications of fraud

Continuous Learning

- AI can be continually trained with new data to improve accuracy and effectiveness over time

Benefit of AI Fraud Detection

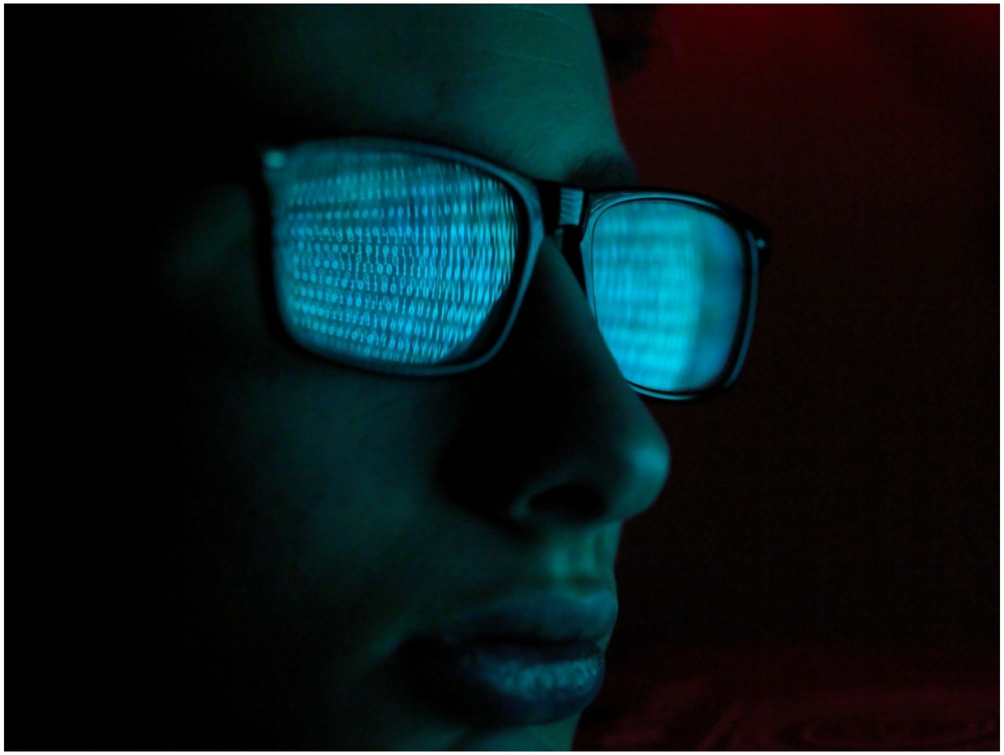
- Real-time detection and prevention
- Scalability
- Cost reduction
- Increased accuracy
- Stakeholder trust and satisfaction

Challenges of AI Fraud Detection

- Data quality and availability
- Integration with existing systems
- False positives and stakeholder friction
- Keeping up with evolving threats
- Regulatory compliance and ethical considerations

Building an AI Fraud Detection Strategy

- Establish a cross-functional fraud management team
- Monitor and update continuously
- Develop a comprehensive fraud detection strategy
- Invest in the right tools
- Practice ethical data usage
- Simulate attacks to test robustness
- Foster a culture of security

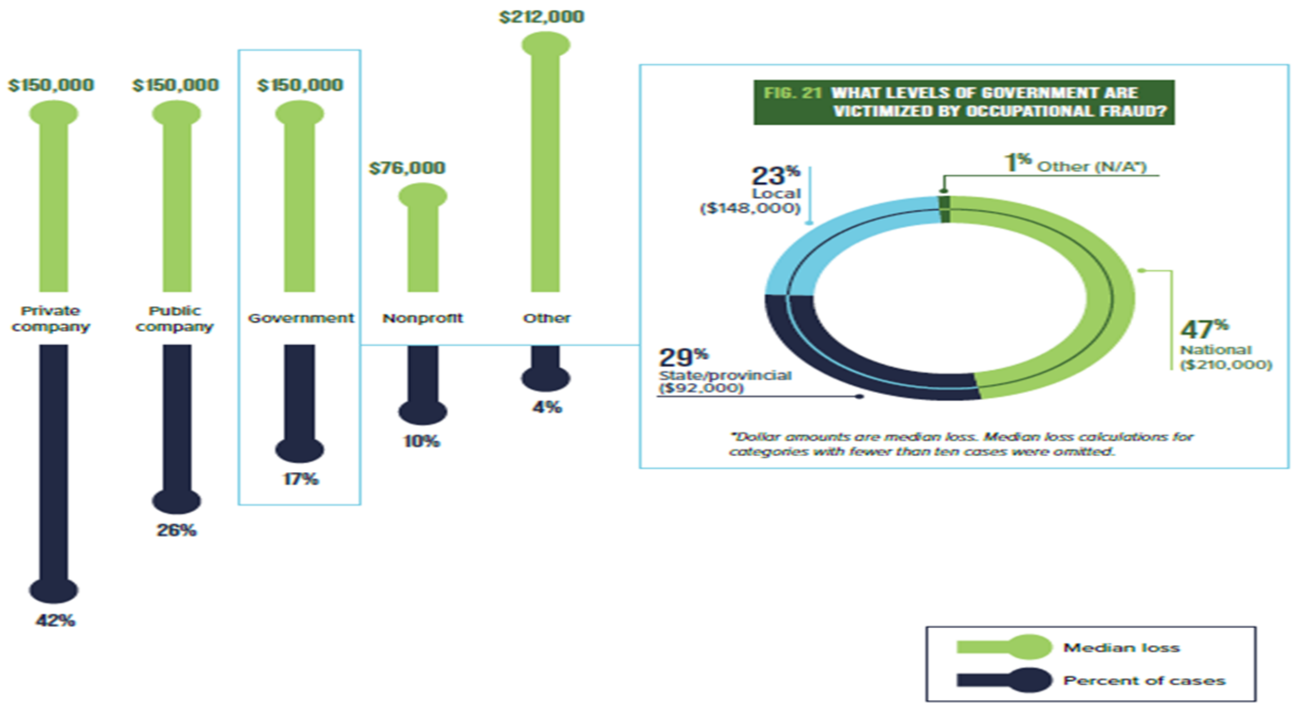


Interesting Facts About Fraud

Types Of Organizations Victimized By Occupational Fraud

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

FIG. 21 WHAT LEVELS OF GOVERNMENT ARE VICTIMIZED BY OCCUPATIONAL FRAUD?



*Dollar amounts are median loss. Median loss calculations for categories with fewer than ten cases were omitted.

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Duration

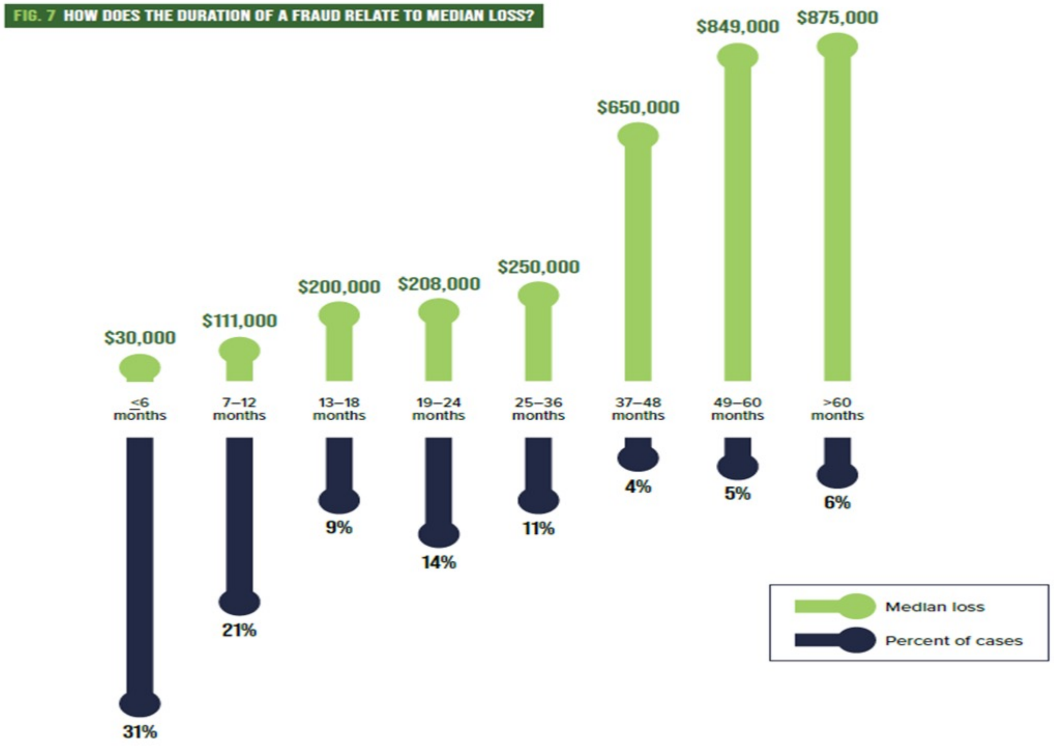

FIG. 7 HOW DOES THE DURATION OF A FRAUD RELATE TO MEDIAN LOSS?

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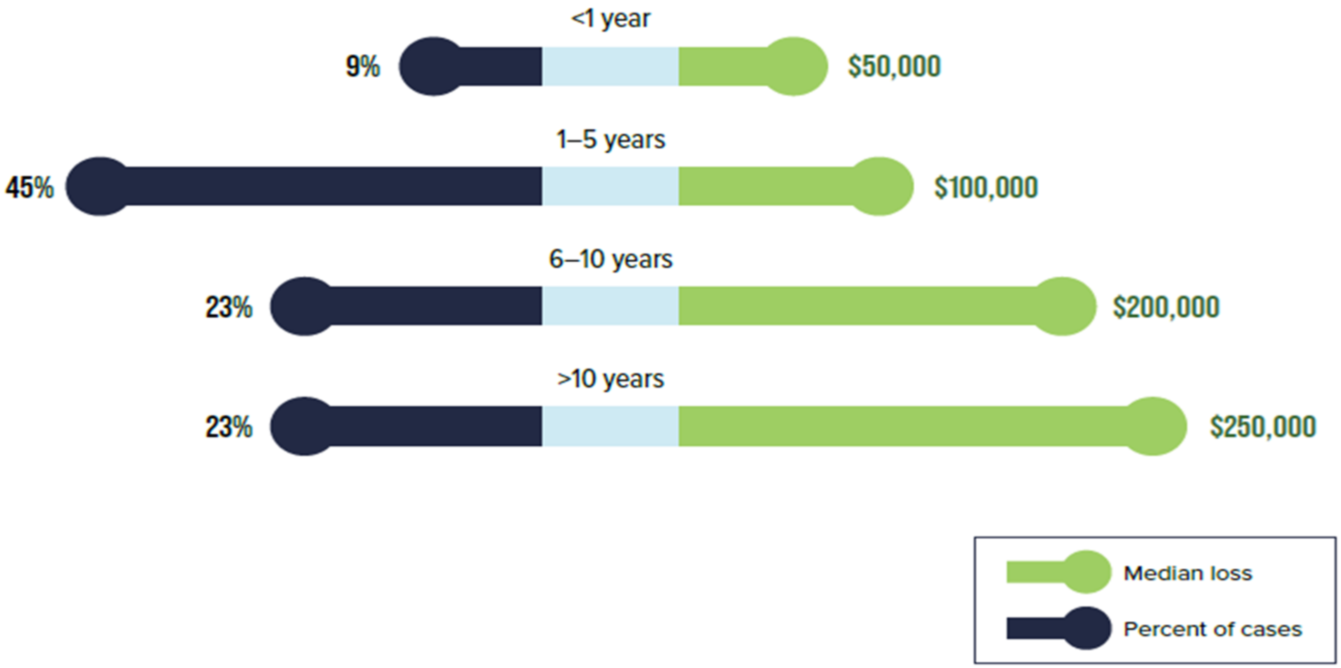
Tenure

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



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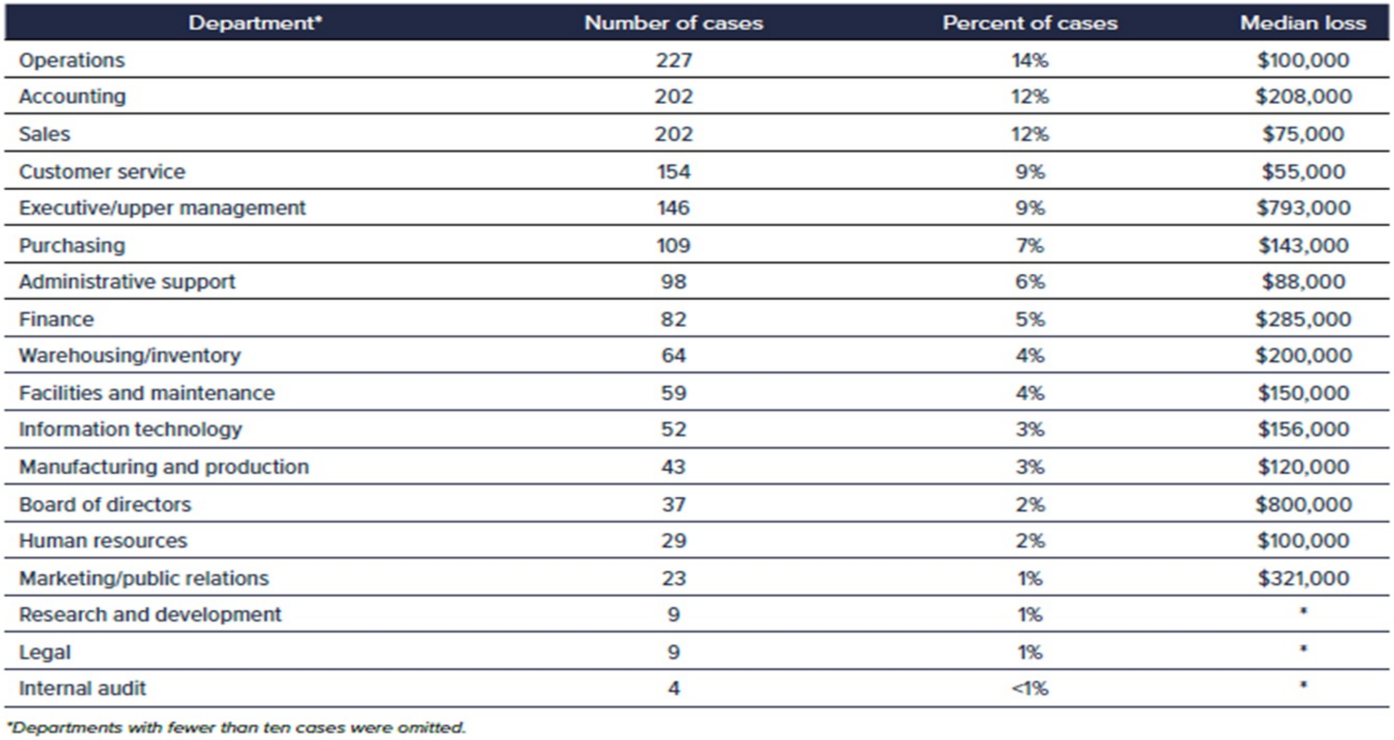
Greatest Fraud Risk By Department



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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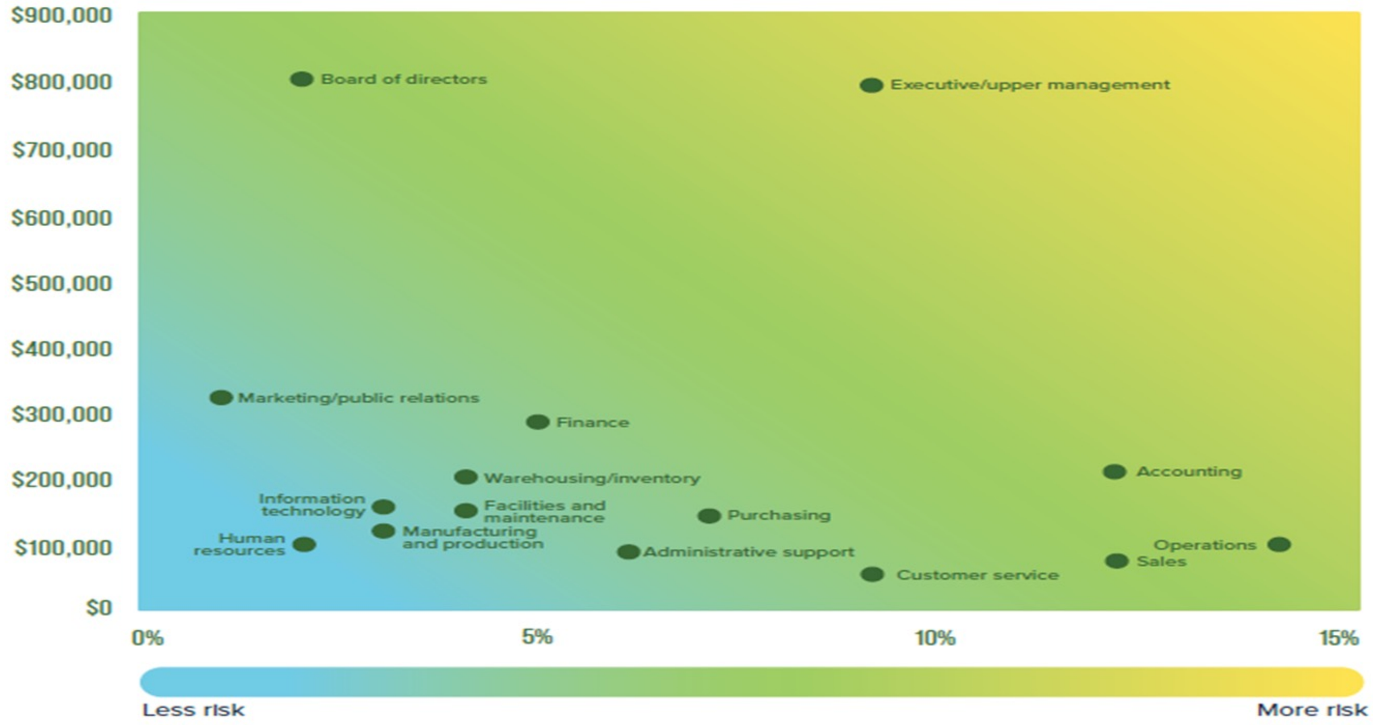
Greatest Fraud Risk By Department

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



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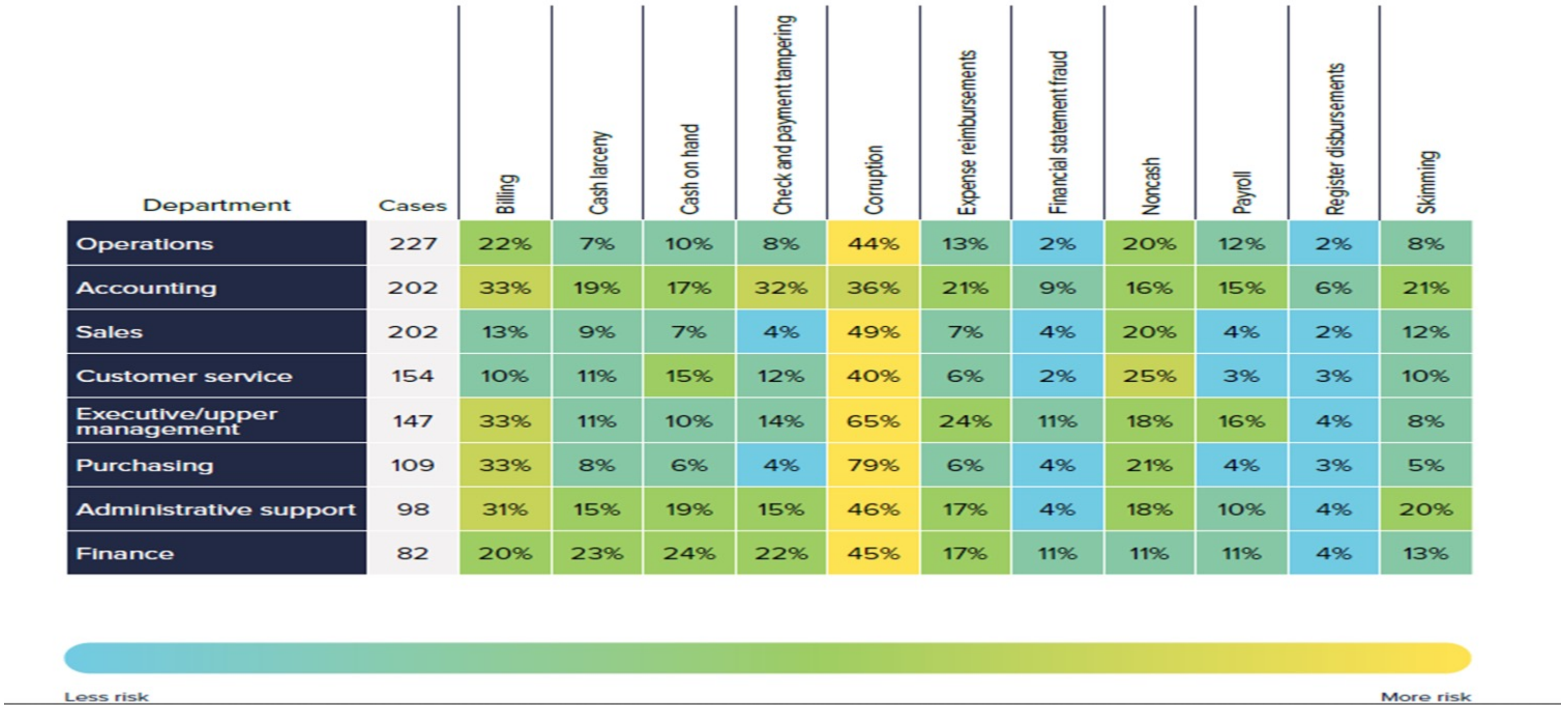
Fraud Types By Department

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%

Less risk

More risk

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Initial Detection of Occupational Frauds

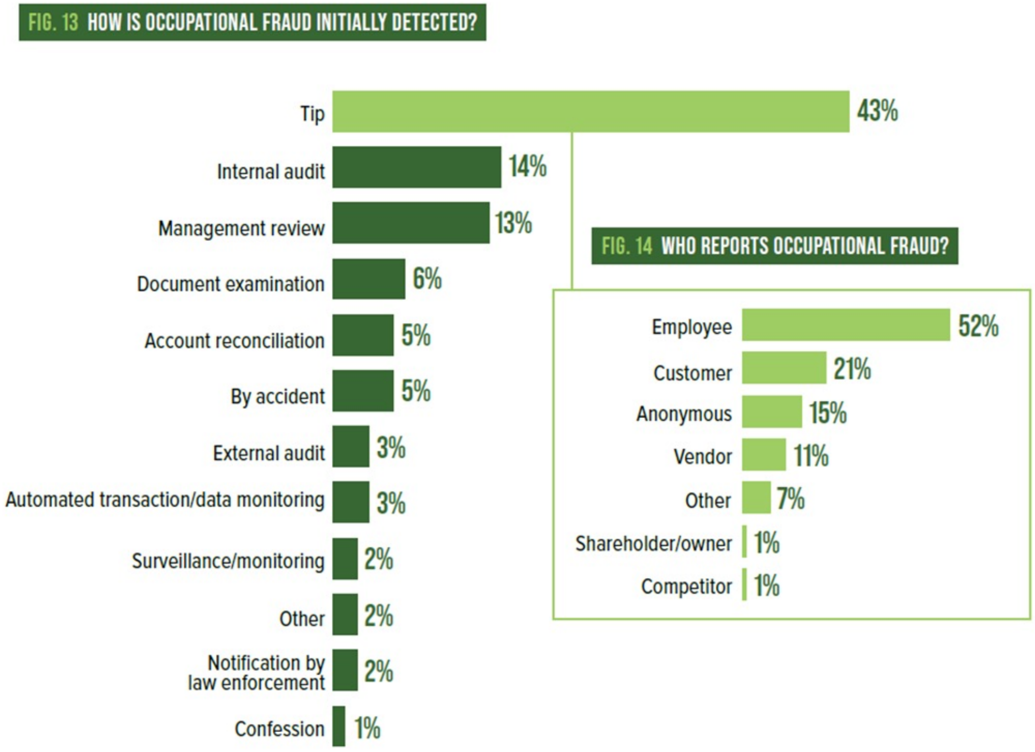

FIG. 13 HOW IS OCCUPATIONAL FRAUD INITIALLY DETECTED?

FIG. 14 WHO REPORTS OCCUPATIONAL FRAUD?

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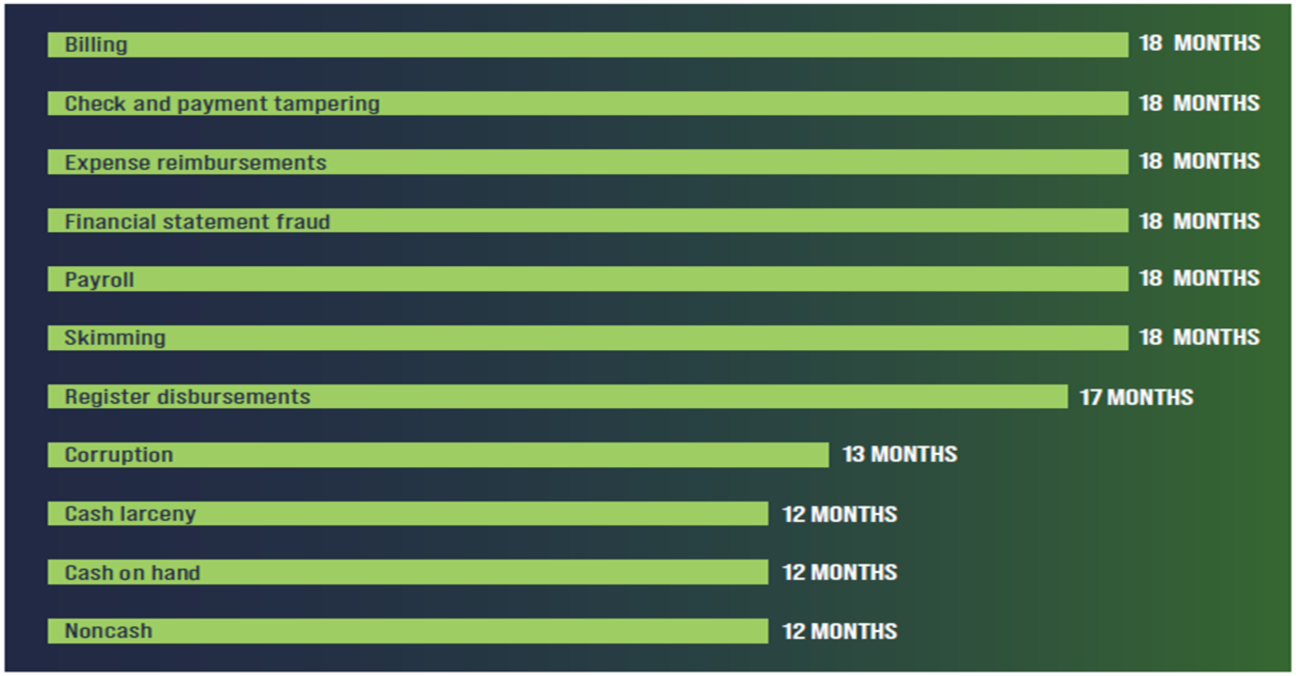
Length of Fraud Schemes Before Detection

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



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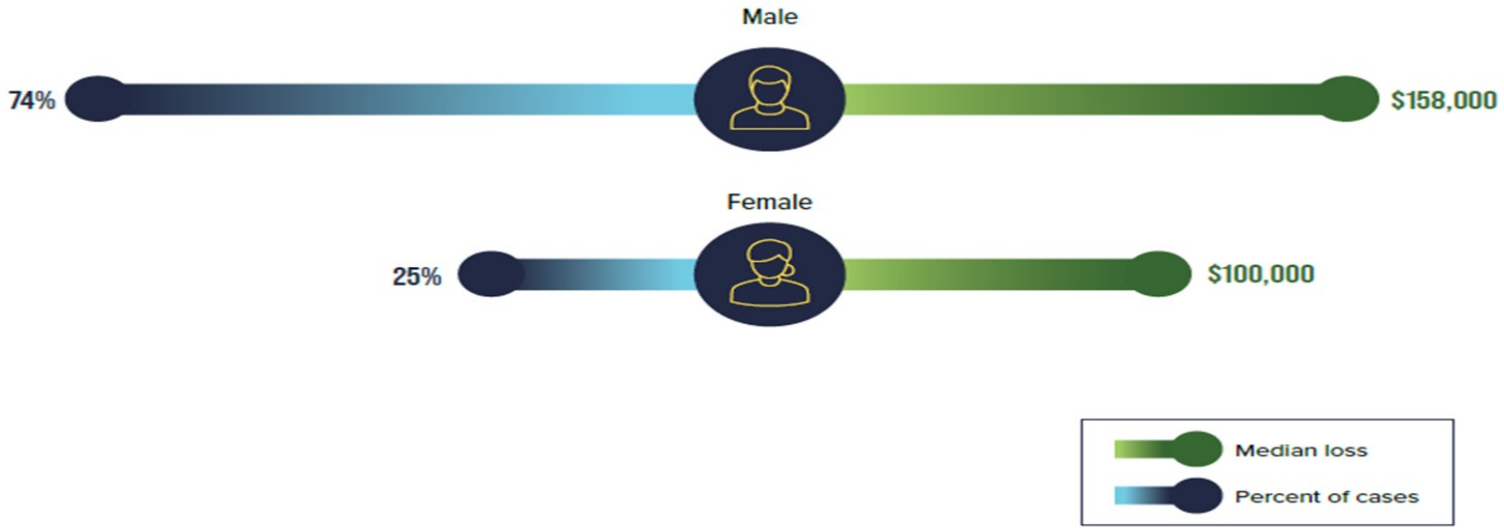
Fraud By Gender

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



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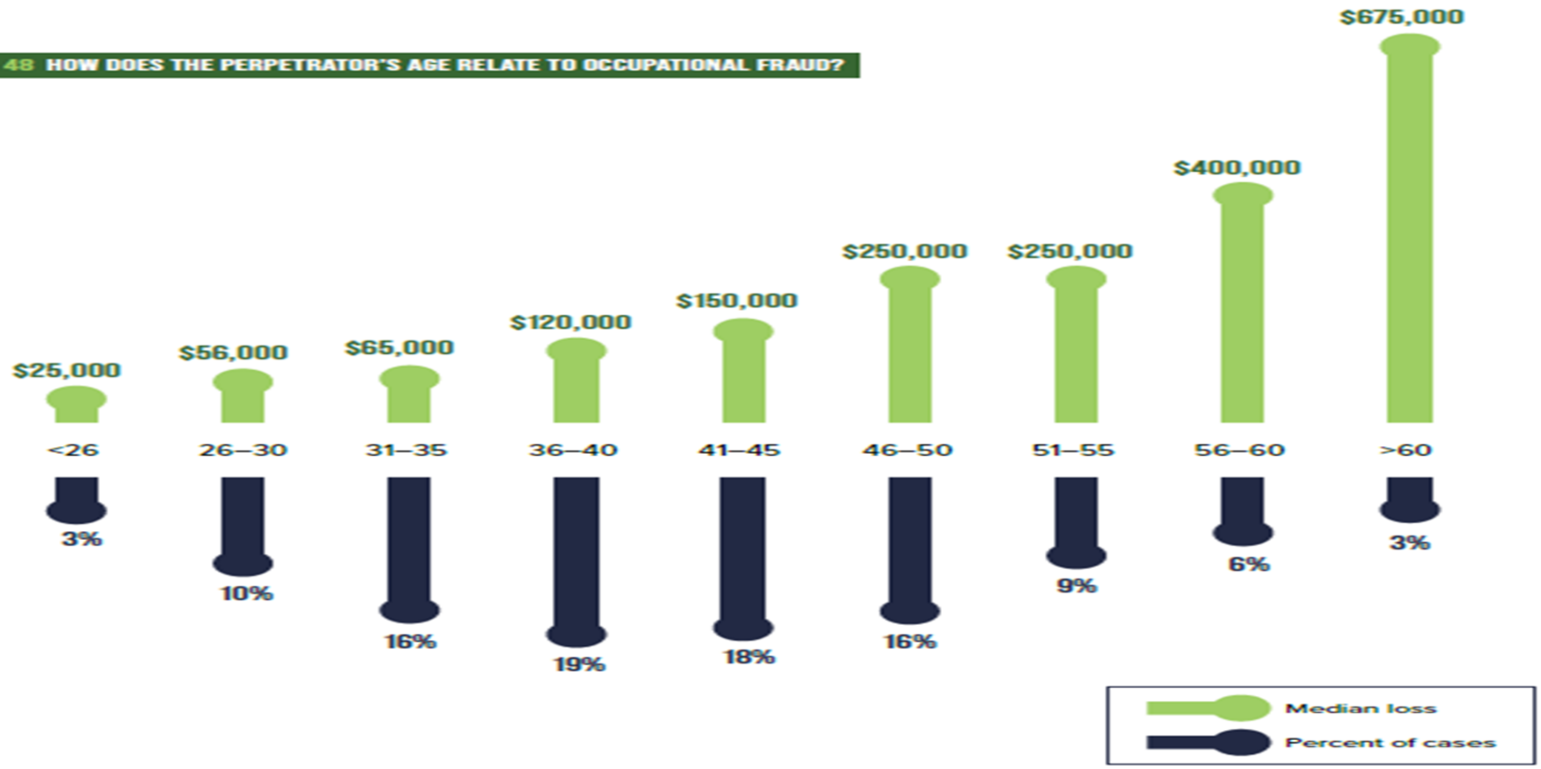
Fraud By Age

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



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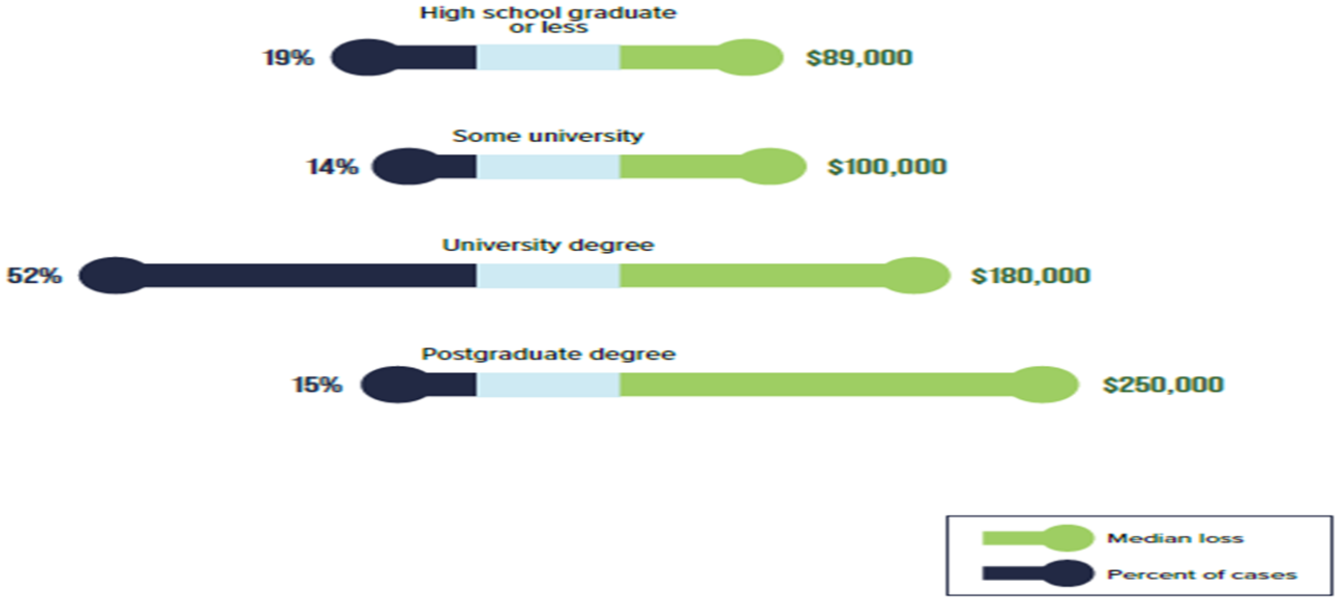
Fraud By Educational Level

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?

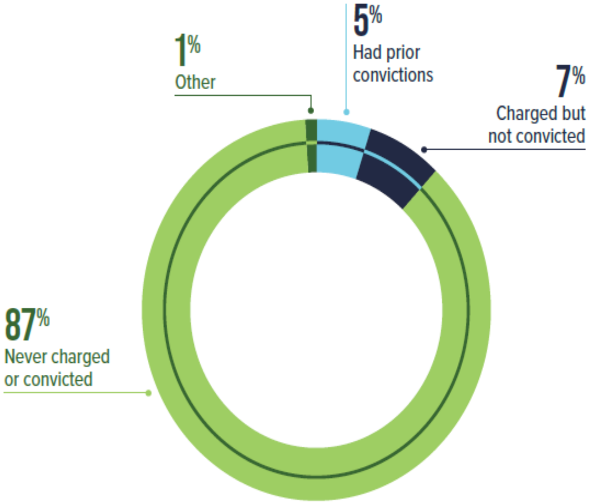
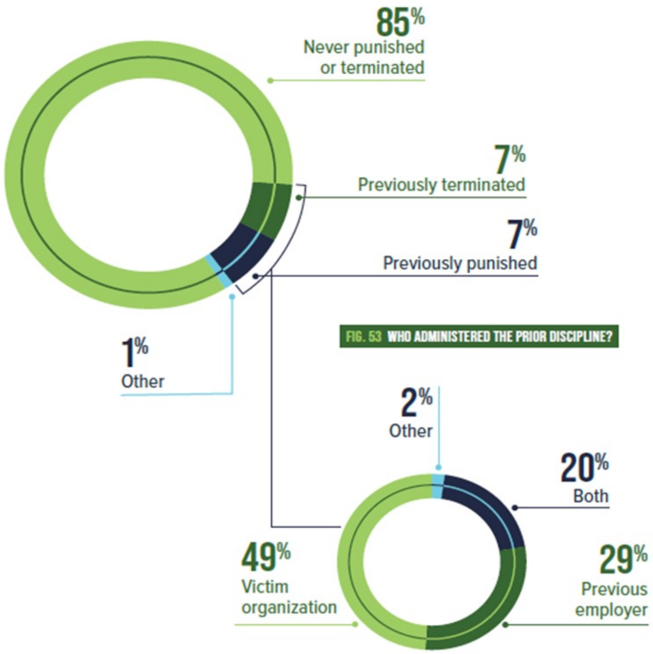


FIG. 52 DO PERPETRATORS TEND TO HAVE PRIOR EMPLOYMENT-RELATED DISCIPLINARY ACTIONS FOR FRAUD?

FIG. 53 WHO ADMINISTERED THE PRIOR DISCIPLINE?



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