

Fraud

When I talk to a client or prospective client about fraud, it is usually after a fraud has occurred or is suspected. By the time a fraud has been committed, the company has already lost a lot of money on fraud. It just doesn't know how much the employee has stolen, and how much it is going to cost them to clean up the mess. In many cases, the thief is a trusted employee who has no financial means to repay the stolen money, and the likelihood of the company being made whole is remote.

Fraud, as it applies to an employment setting is: "the use of one's occupation for personal enrichment through the deliberate misuse or misapplication of the employing organization's resources or assets" (as defined by the Association of Certified Fraud Examiners (ACFE) in its 2008 Report to the Nation on Occupational Fraud and Abuse).

Does doing nothing to prevent fraud save money?

So the question is: "How expensive is failing to be proactive and preventing fraud?" For a company that is the victim of fraud, the answer will need to wait until it has hired a forensic accountant or similar specialist. This will likely cost the company thousands of dollars and could also cause weeks of business interruption. Some of the main misconceptions that result in companies failing to proactively manage fraud prevention are:

- Fraud only happens to the big companies;
- If fraud does occur, the loss would be minimal;
- The cost of prevention is prohibitive; and

- Prevention is ineffective.

The ACFE estimates that U.S. businesses lose approximately \$994 billion to occupational fraud very year. What is surprising to many, however, is that it is the small businesses (with fewer than 100 employees) that are likely to be the victim of fraud. According to statistics released by the ACFE in the 2008 Report to the Nation on Occupational Fraud and Abuse, 38.2 percent of all fraud victims are small businesses, and those businesses suffer an average loss of \$200,000.

Hire honest people

One of the first things a company can do to prevent fraud is to hire honest people. It is imperative to implement a thorough background check as a required step in all hiring situations. These background checks can be done internally or outsourced to agencies that do background checks professionally. The cost for this process is small compared to the costs of not detecting a potential threat.

In some fraud cases, the employee committing the theft is a good person who is pushed to the edge due to severe financial hardships caused by many things such as medical costs, gambling debts, etc. This employee is unlikely to have a criminal record and a background check won't address these cases. That is where internal processes come into play.

Segregation of duties

One of the most successful ways to prevent fraud that costs the company very little is segregation of duties. Good internal controls are an essential part of any effective fraud prevention program. While there are many sophisticated fraud schemes, it doesn't take sophistication or

complex accounting knowledge to steal from an employer. This is especially true if the employer gives a single employee access to the cash, signature authority, access to the accounting program and bank reconciliation responsibilities. Sound farfetched? Take a look at your own business practices:

- Who opens the mail?
- Who posts the check/cash payments?
- Who deposits the cash and checks?
- Who has authority to access and write off accounts receivable?
- Who can create accounts payable accounts?
- Who does the bank reconciliation?

In many small and large companies, the same person performs many if not all of these functions. One of the best ways to avoid theft in your company is to put these tasks in the hands of different people.

Almost every company has employees who seem to be permanent fixtures at the office. They have vacation that they refuse to take. In most cases, these employees are what they appear to be: good, honest and hardworking individuals without interests outside of their jobs. However, in some cases, this is not true.

Sometimes, your 15-year employee who never takes vacations and loves to work long hours may be robbing you blind. However, their method of thievery is not sophisticated, and if he or she ever left for an extended period of time, even for a week, their plot would be discovered. An effective way to disrupt a thief's scheme is to occasionally change their duties and responsibilities. An employee will have difficulty carrying on a long-term fraud if his or her duties and access to data and information are changed periodically.



prevention

anti-fraud measures
that cost little, but may
save a lot

By Timothy P. Muehler, CPA/ABV, CVA, J.D.

Making your employees anti-fraud advocates

As the owner or manager of the company, you set a tone of high ethics and loyalty. Employees need to be told that even small lapses in ethics will not be tolerated. Make honesty and integrity a condition of employment and an expectation of all employees.

Set up a fraud hotline with an outside provider that ensures complete anonymity. This gives your employees an outlet to report suspected activity anonymously, without risk of reprisal or animosity. Fellow employees have the best opportunity to observe the other employees and are most

likely to notice changes in behavior, etc.

Throw a surprise audit

Habits and routine are the friends of a thief. The more predictable a company's processes and behaviors are, the easier it is for fraud to be committed. One effective way to detect fraud and discourage potential theft is to perform a surprise audit. This isn't an audit in its truest sense. Rather, it is the organized, focused analysis of key areas that are the likely targets of fraud. At my firm, we assist our clients in setting up procedures and analysis that are usually integrated with sophisticated but affordable software. This software is capable of searching and analyzing millions of bits of data in a short period of time.

The search criteria may center on anomalies or outliers for certain accounts, such as checks written over or under a certain dollar amount. It might look for new accounts with regular, repetitive activ-

ity and for missing numbers or duplicate numbers in a sequence. These search criteria can be customized for the company's specific risk factors and once the protocol is established, running the search queues is quick and easy.

Benjamin Franklin once said, "An ounce of prevention is worth a pound of cure." This couldn't be truer when it comes to fraud. None of the suggested proactive steps to preventing fraud outlined in this article are high cost measures that are out of the reach of a small or midsize company. Implementing these suggestions may prevent fraud, and also may improve your company's business operations.



TIMOTHY P. MUEHLER, CPA/ABV, CVA, J.D. is a partner at Clifton Gunderson LLP in Milwaukee. He can be reached at 414-476-1880 or Timothy.Muehler@cliftoncpa.com.

PROFESSIONAL LIABILITY INSURANCE

Meeting the needs of your firm.

Den Boer & Associates specializes in providing professional liability insurance for CPA firms of all sizes. We do this by analyzing your current coverage and working with you to determine the exact protection needs of your firm, including any unique features of your practice. We then match those requirements with a professional liability insurance underwriter that will meet your specific needs. For more information please contact Rod Den Boer, Harry Stoll, or Jane Meekma at 262-522-4000.

www.dbains.com



den boer & associates
SPECIALTY INSURANCE PRODUCTS

N19 W24400 Riverwood Drive Suite 385
Waukesha, WI 53188