Introduction to Ethics and Fraud

IMPOSSIBLE TO SEPARATE

ROBERT E. DIXON—OKLAHOMA STATE UNIVERSITY
But because fraud is man’s peculiar vice, More it displeases........and therefore, the Fraudulent are lower, suffering more.

Dante (Inferno)
So, what is ethics?

What is morality?

Who makes the rules?

Is higher Ed Unique?

Who does it hurt?

What’s the Difference?

Is it ok sometimes?

Research issues

What is the greater good?

Athletics

What is the greater good?

Financial

Right or Wrong?

Is there a right Choice?

Honor, integrity, character, code

Where can fraud happen?
Ethics Defined

As defined by Webster
- Is the *study of standards of conduct and moral judgements*; Moral reasoning: The system or code of morals of a particular person, religion, *group*, or *profession*.
- The Scientific Study of Morality
- In basic terms....making the right decision even when there is no one to answer to but ourselves.

“Educating the mind without educating the heart is no education at all.”

--------Aristotle
Definition of Fraud

From an institutional perspective, fraud includes any intentioned or deliberate act to deprive the institution of property or money by guile, deception or other unfair means.

Fraud, every conscience stung, a man may practice upon him who trusts, and him who shows no ability to discern.....

_Dante_
“Part of establishing the standards is that it is NOT seen as something separate and apart/ That it really becomes part of the very structure of the business world. And what comes of that, of course are higher standards, more ethical behavior, and to the benefit of everyone.”

Paul Sarbanes..... Interview with Neil Amato (July 30, 2012) Journal of Accountancy
Uncontrolled and/or Unethical Behaviors may be indicators of fraud or potential fraud

- Ignoring Regulatory Requirements
- Lying and falsification of records
- Ineffective Service
- Harassment
- Discrimination
- Drug, alcohol, and gambling abuses/addictions
- Wrongful termination or fear of wrongful termination
Ethics 101 (John C. Maxwell)

- 43% of employees (surveyed) committed an unethical act.
- 75% observed unethical acts and did nothing.
- Reasons:
  - Participation Attitude—They are also part of the 43%,
  - Apathetic—The employee who notices really doesn’t care,
  - Afraid—The employees don’t feel safe reporting the incident, and/or
  - Surrender Attitude—Why bother? Nothing will be done anyway.
What can be done?

- Diversity in the workplace
- Frequent and robust communications with employees
- Frequent assessment of the culture of the organization/division/department/staff
- Wider questions/broader topics in assessment—including misconduct reporting.
- Strong(er) policies against retaliation—protecting
- Greater visibility of compliance/deterrence functions
- More resources for managers and staff relating to compliance/ethics

Janet Hawkins (Journal of Accountancy June 2014)
think
Traditions, Deeply Rooted and Sometimes Practical

ETHICS IN THE UNIVERSITY CULTURE
References

Gordon Marino – St Olaf College
Kathleen McAuliffe “Disgust Made us Human”

Amitai Etzioni – The Brookings Institute
ACFE “Ethical Lapses by CFE’s”

Christopher Newfield

James Counelis

Dennis Collins

Frank J Navran

William Readings

Nina Rosenstand—San Diego Mesa College

Thorstein Veblen

Lawrence Kohlberg

NSF “On Being A Scientist”

The Atlantic Monthly

Harvard Business Review

The New Yorker
Most assume “...improving moral lives (ethical behavior) is a matter of developing conceptual understanding and analytical acumen. If we just know a little more about ethics...”

Study and train all you want, but in those moments when it all counts.........

“A quiet conscience makes One strong.”
-----Anne Frank

While most of us have the moral/ethical training to handle most situations, this training and understanding clashes with our own immediate self-interest or preservation.

So........... Why Study Ethics?

• It’ fascinating stuff?

CPE?

For a life well-lived?

To get excited over boring things?
Theory of Moral Reasoning

Lawrence Kohlberg

- People at various stages of development answer questions pertaining to certain dilemmas with varying degrees of reasoning.
- Example--Should a civil defense worker leave his post to help his own family members, who may have been injured in a disaster, or should he stay where he is and help others.---The Heinz Dilemma
Ethical Challenges/Problems/Dilemmas

A unresolved dilemma challenging or threatening a person’s moral duties and values. The dilemma is most often caused because there is no clear choice because there are conflicting but arguably valid sides in the situation.

How do we solve them?
The Primary Base of Intuitive Ethical Decision-Making

• Physiological/Neurological
• Cultural/Subcultural
• Lived Experience
• Societal Expectations

“I hold that a strongly marked personality can influence Descendants for generations.”
------Beatrix Potter
Body and Mind
Culture
Images, Sounds, Language, Smells, Feelings, Experiences

Create/Foster/Reinforce/Extinguish/

- Archetypes
- Stereotypes
- Symbols
- Preferences
- Bias
- Prejudices
- Gag Factors
## The Obvious vs. the Obscure

<table>
<thead>
<tr>
<th>Love</th>
<th>Life</th>
<th>Bad</th>
</tr>
</thead>
<tbody>
<tr>
<td>Truth</td>
<td>Liberty</td>
<td>Hot</td>
</tr>
<tr>
<td>Beauty</td>
<td>Morality/Ethics</td>
<td>Cold</td>
</tr>
<tr>
<td>American Way</td>
<td>Pain</td>
<td>Normal</td>
</tr>
<tr>
<td>Honor</td>
<td>Sadness</td>
<td>Justice/Fairness</td>
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<tr>
<td>Happiness</td>
<td>Celebrity</td>
<td>Value/Worth</td>
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<tr>
<td>Patriotism</td>
<td>Good</td>
<td>Style</td>
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</tbody>
</table>
What Makes You?

• We all have some simple story that defines us.
  – Some Aha Moment, Some break we received, some opportunity we have experienced.

• Recognize the things that make us who we are.
  – Biology, Influences, and indoctrinations.

• Certain issues touch us differently.
  – Sensitivity buttons.
  – Things disgust us to different degrees
What’s Your Story?

“I’ve read dozens of books
About heroes and crooks,
And I’ve learned much
From both of their styles”
-------Jimmy Buffett
From Our Base
We Build and Accept A Social Contract

Your expectations of others
◦ People (in personal and business/public relationships).
◦ Organizations

Their expectations of you.
◦ In your personal dealing, and/or
◦ Your representation and support of your organization (within and without)

Disruption.
◦ An ethical lapse occurs when a person fails to meet standards of the social contract to which they are a party thus causing their actions to be judged according to that contract.
Codes of Conduct formed by the Contract

Universal/Jurisdictional Defined Laws and Rules
  ◦ Origins in Natural and/or Common Law

Sect—Culturally/Religiously Defined Laws Rules
  ◦ Imago Dei, Natural Law

Institutional/Organizational—Rules established by a group.

Family—established rules

Social Group—established rules
With the Goals to Live and Work and Prosper and form Decisions

Within a society
  ◦ With laws,
  ◦ With rules,
  ◦ With reasonable expectations of goodwill,
  ◦ With reasonable expectations of decency,
  ◦ With changing norms.
To Accept the Consequences of Breaking the Rules of the Social Contract

<table>
<thead>
<tr>
<th>Jail Time</th>
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</thead>
<tbody>
<tr>
<td>Civil Fines/Penalties</td>
</tr>
<tr>
<td>Excommunicated, Shunned, Dropped from the Church Roles</td>
</tr>
<tr>
<td>Terminated, Reprimanded, Removed from the profession</td>
</tr>
<tr>
<td>Disinherited, Kicked-out, Divorce</td>
</tr>
<tr>
<td>Excluded from the play group or club, loss of certain privileges</td>
</tr>
</tbody>
</table>
A Social Contract in Academia?

A Convergence----

Universities are unique entities where multiple influences, agendas, disciplines, cultures, and sub-cultures converge into one.

- Professional and academic organizations represented in higher education have standards unique to the profession. AICPA, ABA, AMA, APA, IIA, ACFE, et AL.

Other Standards

- Accrediting Boards, HLC, AAUP, NCAA, Research Compliance Groups
The University

Universitas—“...into one body”
- The University of Bologna; The University of Paris; Oxford University
- Historically---for the past 900 years or so...........
  - Given special, collective legal rights, charters, self-regulating
The Higher Learning In America: A Memorandum On the Conduct of Universities By Business Men, 1918

- The purpose of a university’s administration is to see that the faculty has what they need at the time that they need it.....
Nine Principles of an Ethical Institution (Plus 1)

James S. Counelis

- **Academic Freedom**
  - The freedom to teach
  - The freedom to learn
  - The moral imperative of truth

- **Organization and Control**
  - Autonomy of the Institution
  - Collegiality of Faculty Decision-Making
  - Civility in discourse

- **Fairness**
  - Tolerance for differing opinions
  - Equity in access
  - Equity in evaluation

- **PLUS 1: Financial Integrity**
  - Stewardship
Academic Freedom

It is the founding principle of the University

The Moral Imperative of Truth
The Freedom to Teach
The Freedom to Learn
Governance

Autonomy
Collegiality of Faculty Decision-Making
Civility in discourse
Fairness

Tolerance for differing opinions
Equity in access
Equity in evaluation
Financial Integrity

We are the fiduciary
Monitored Policy Directives
Drive Policy Performance

Top-down Expectation creates Bottom-up Performance
Organization/Management

Individual
Establishing an Ethical Tone

Personal, Departmental, Divisional, Institutional

- We broadcast our expectations/non-expectations across a wide spectrum.
Here’s a Problem in Policy Development and Enforcement

There is a disconnect on a very basic level between management and staff.

- Staff may assume the ethics of the leadership of the organization are flawed, but this is a failure. Individuals must recognize their personal ability and obligation to influence/create the ethical behavior of the organization.
  - Create a micro-ethical climate for a macro-ethical behavior.
- Management must never forget/neglect/postpone their obligation to behave as individuals within the whole.
  - Create a macro-ethical climate for micro-ethical behavior.
  - Failure of one does not create an excuse for another

When my fist clinches, Crack it Open
Before I use and lose my cool.
-------The Who
More to the Point....

Every individual affects the total organization and the organization’s effectiveness on the expanded community----
And the reputation of the organization affects the expanded community’s view of the individual.
When ethics fail

- The Breakdown of the Organization and relationships.
  - Consider the intra-connectivity of the organization.
  - Consider the symbiotic relationship the organization and the members of the organization have with the greater community.
Organization’s Eco-System

Everyone needs Self-awareness and Inter-reliance upon Others

- Each manager is an individual within the organization.
- Every individual is a manager of some area within the organization.
- Every individual influences the operation of the organization as well as influences how others (within and without) perceive the organization. THUS:
The Zen of the Organization

We fail to recognize the “Not two” and create a segmented/disjointed organization.

◦ It is difficult to separate the individual from the organization. It is difficult to separate the organization from the individual. Yet, we really try to do so.

When a person believes they are truly part of the organization, that the organization needs them, and the person accepts their responsibility in maintaining a healthy organization, a segmented organization cannot exist.
Five Components of Ethical Decision Making

1. Identifying the Issue
2. Gather the Information for an informed Decision
3. Consider the Outcomes
4. Make the Decision
5. Live with the Decision
   a) Participate in establishing an environment where ethical behavior is expected and encouraged.
   b) Question the intent of an action as well as the action itself.
   c) Hire ethical people.
On Hiring—Be Deliberate

Job Announcement
Resumes/Applications
Reference Checks
Background Checks
Personality Surveys*
Interviews
Was a background check run on the perpetrator prior to hiring?

- Yes: 52%
- No: 48%

Did the check reveal existing red flags?

- Yes: 10%
- No: 90%
What types of background checks were run on the perpetrator prior to hiring?

- Employment history: 78%
- Criminal checks: 75%
- Reference checks: 55%
- Education verification: 50%
- Credit checks: 36%
- Other: 4%
We all have different world views, but there is a basic social contract.

Most of us purposefully strive to do the right thing—Ethics is within each of us.

There is an internal struggle within each of us between righteousness and our self interests.

Higher education is unique

The organization stands as a collective of the individuals and represents the individuals.

Each has a role in directing the organization’s ethical practices.

Pay attention during the hiring process.

May your hands always be busy
May your feet always be swift
May you have a strong foundation
When the winds of change shift

-------Bob Dylan
As a lead in to our next session............................................................

WHY DO PEOPLE—Good People—BREAK BAD?

In between the moon and you,
Angels get a better view
Of the crumbling difference
In wrong and right.

Adam Duritz
The Counting Crows
“Round Here”
FRAUD in the University Culture—entering the Eighth Circle
(with my apologies to Dante)

ROBERT DIXON
OKLAHOMA STATE UNIVERSITY
Acknowledgements

Resources

- Association of Certified Fraud Examiners
- American Institute of CPAs
- Dr. David C. Bosserman
- Mr. Kevin Robinson
- Ms. Kathy K. Elliott
- Ms. Brenna T. Dixon
- Dante
- Fraud
  - What constitutes fraud
  - Various types of fraud
- Major factors that can lead to fraud
- How fraud is most often detected
- Fraud deterrence and prevention
What Constitutes Fraud

What are the General Types of Fraud
THE FRAUD TREE

OCCUPATIONAL FRAUD AND ABUSE CLASSIFICATION SYSTEM

Corruption

Conflicts of Interest
- Purchasing Schemes
- Sales Schemes

Bribery
- Impeccable Kickbacks
- Bid Rigging

Illegal Gratuities
- Economic Extortion

Asset Misappropriation

Not Worth/Not Income Overstatements
- Timing Differences
- Fictitious Revenues
- Concealed Liabilities and Expenses
- Improper Asset Valuations
- Improper Disclosures

Not Worth/Not Income Understatements
- Timing Differences
- Understated Revenues
- Overstated Liabilities and Expenses
- Improper Asset Valuations
- Improper Disclosures

Financial Statement Fraud

Cash

Thrift of Cash on Hand
- Shimming
- Cash Larceny

Thrift of Cash Receipts
- Receivables
- Refunds and Other

Fraudulent Disbursements
- Payroll Schemes
- Expense Reimbursement Schemes
- Check Tampering
- Surrogate Disbursements

Inventory and All Other Assets

Larceny
- Asset Registrations and Transfers
- Fraud Sales and Shipping
- Purchasing and Receiving
- Unconcealed Larceny

Sales
- Uncollected
- W/D Off Schemes
- Understated
- Lapping Schemes
- Uncollected

Unconcealed
- Waived
- Refunded
- Authorized
- Forged
- Misstated
- Fictitious
Occupational Fraud

"the use of one's occupation for personal enrichment through the deliberate misuse or misapplication of the employing organization's resources or assets"
Fraudulent Statements
Concealed Liabilities
Fictitious Revenues
Improper Asset Valuations
Improper Disclosures
Timing Differences
Non-financial

Corruption
Conflict of Interest
Bribery
Illegal Gratuities
Economic Extortion

Asset Misappropriation
83.5%  89%
2016 Report  2018 Report
Asset Misappropriation

Cash:
- Larceny
- Skimming
- Fraudulent Disbursements

Inventory & All Other Assets:
- Misuse
- Larceny
What asset misappropriation schemes present the greatest risk?

- Check and payment tampering: $150,000 (12%)
- Billing: $100,000 (20%)
- Noncash: $98,000 (21%)
- Payroll: $63,000 (7%)
- Cash larceny: $75,000 (11%)
- Skimming: $50,000 (11%)
- Expense reimbursements: $31,000 (14%)
- Cash on hand: $20,000 (15%)
Fraudulent Disbursements

- Billing Schemes
- Payroll Schemes
- Expense Reimbursement Schemes
- Check Tampering Schemes
- Register Disbursement Schemes
Payroll Schemes

Payroll schemes
- Any scheme in which an employee causes his or her employer to issue a payment by making false claims for compensation
  - Employee claims overtime for hours not worked
  - Employee adds ghost employees to the payroll
  - Median loss $90,000
Payroll Red Flags

Multiple/Unrelated employees sharing bank accounts

Multiple/unrelated employees sharing common address

Multiple family members (or unusually close relationships) in same department with “sign-off” authority granted.

High variances from one period to another without reasonable/verifiable explanations

A person unfamiliar to the payroll system check/verify records

Unreconciled Payroll/Benefit accounts

Slow payments to taxing agencies, fringe benefit providers, court systems

Anomalies in payroll records—improper changes in salary levels

Falsified time sheets
Skimming Schemes

Skimming schemes

◦ Any scheme in which cash is stolen from an organization before it is recorded on the organizations books or records
  ◦ Employee accepts payment from a customer but does not record the sale
  ◦ Understated sales and receivables
  ◦ Theft of check through the mail
  ◦ Median Loss $53,000

2016 ACFE Report to the Nations
Skimming Red Flags

Rising Variances in “costs of goods sold”

Unexplained Write-downs on Inventory records.

Write-offs (discounts) for currently enrolled students or Active Grants

Rising accounts receivables

Variances in daily sales, collections, or deposits
Billing Schemes

Billing schemes
- Any scheme in which a person causes his or her employer to issue a payment by submitting invoices for fictitious goods or services inflated invoices or invoices for personal purchases
  - Employee creates a shell company and bills employer for nonexistent services
  - Employee purchases personal items, submits invoice for payment
  - Median loss $100,000
Billing Red Flags

INCOMING BILLS

Sudden appearance of Unfamiliar vendors or sudden increase in use of a Vendor.

Vendor Complaints

Variances in use of commodities

Conflict of Interest

Appearance of a vendor not necessarily appropriate for work activities

OUTGOING BILLS

Write-offs—variances, types of students, Grant Accounts, customers

Unreconciled accounts

Customer Complaints on missing payments to accounts or delays in processing checks/misapplied checks

Tuition vs Enrollment
Cash Larceny

Cash larceny schemes
- Any scheme in which cash is stolen from an organization after it has been recorded on the organization’s books and records
  - Employee steals cash and checks from daily receipts before they can be deposited in the bank
  - Petty cash, change funds, vault cash
- Median loss $80,000
Cash Larceny Red Flags

High $$ student refund checks or refunds to granting agencies
Checks returned to department for disbursement
Inadequate receipts
Increased use of Pcard by individual (relatively speaking)
Write-offs
Unusual activities in drop/withdrawal refund activities
Customer/Student complaints
Missing inventory or equipment
Expense Reimbursement Schemes

Expense reimbursement schemes

- Any scheme in which an employee makes a claim for reimbursement of fictitious or inflated business expenses
  - Employee files fraudulent expense report, claims personal travel, nonexistent meals, “drinks a taxi fare,” etc.
  - Median loss $26,000

2016 ACFE Report to the Nations
Expense Reimbursement Red Flags

Unfolded or pristine invoices/receipts

Lack of invoices/receipts or numerous claims for reimbursement below the receipt-required threshold.

Unreasonable costs assigned to a particular event (Taxi Fare, Lunch)

Failure to itemize receipts or misappropriate expenses
Check Tampering Schemes

Check tampering schemes

- Any scheme in which a person steals his or her employer’s funds by forging or altering a check on one of the organization’s bank accounts, or steals a check the organization has legitimately issued to another payee
  - Employee steals blank company checks, makes them out to himself or an accomplice
  - Forged maker, forged endorsement, altered payee, authorized maker schemes
- Median loss $158,000

2016 ACFE Report to the Nations
Check Tampering Red Flags

Someone brags on their ability to sign the “bosses” name

Customer/Student complaints on not receiving check.

One person writes, records, and reconciles bank account (think about a petty cash fund)

“Confidential human subjects”

Someone has the ability to manipulate a dataset without oversight/sign-off

Non-inventoried check stock.

Excess number of manual checks instead of “system” checks

Department insists on picking up check.

“Send-to” address is out of character to vendor address or varies from invoice address.
Non-Cash Schemes

Any scheme in which an employee steals or misuses non-cash assets of the victim organization

- Employee steals inventory from a warehouse or storeroom
- Employee steals or misuses confidential customer financial information
- Median loss $70,000
Non-Cash Red Flags

Motor pool vehicles are routinely gone on the weekend/holiday period.
Inconsistent checks on inventory of equipment
Incomplete log records. (Mileage and/or check out)
Continuous loss and replacement of small tools, equipment, etc.
Inconsistency in application of store/recharge rates.
Non-Cash Red Flags

Motor pool vehicles are routinely gone on the weekend/holiday period.

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Incomplete log records. (Mileage and/or check out)

Continuous loss and replacement of small tools, equipment, etc.

Inconsistency in application of store/recharge rates.
Occupational Fraud in Education

Median Loss--------

$68,000
How does the perpetrator’s level of authority relate to occupational fraud?

- Employee: $50,000 - 44%
- Manager: $150,000 - 34%
- Owner/executive: $850,000 - 19%
- Other: $189,000 - 3%

Median Loss | Percent of Cases
How does the perpetrator’s tenure relate to occupational fraud?

- 9% Less than 1 year: $40,000
- 44% 1–5 years: $100,000
- 23% 6–10 years: $173,000
- 24% More than 10 years: $241,000
How does the perpetrator’s tenure relate to median loss at different levels of authority?

- **Employee**
  - 6 years or more: $100,000
  - 5 years or less: $35,000

- **Manager**
  - 6 years or more: $200,000
  - 5 years or less: $125,000

- **Owner/executive**
  - 6 years or more: $1,000,000
  - 5 years or less: $672,000
How does the perpetrator’s age relate to occupational fraud?

<table>
<thead>
<tr>
<th>Age Range</th>
<th>Percent of Cases</th>
<th>Median Loss</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt;26</td>
<td>5%</td>
<td>$23,000</td>
</tr>
<tr>
<td>26-30</td>
<td>10%</td>
<td>$40,000</td>
</tr>
<tr>
<td>31-35</td>
<td>15%</td>
<td>$100,000</td>
</tr>
<tr>
<td>36-40</td>
<td>19%</td>
<td>$100,000</td>
</tr>
<tr>
<td>41-45</td>
<td>19%</td>
<td>$200,000</td>
</tr>
<tr>
<td>46-50</td>
<td>14%</td>
<td>$250,000</td>
</tr>
<tr>
<td>51-55</td>
<td>9%</td>
<td>$237,000</td>
</tr>
<tr>
<td>56-60</td>
<td>6%</td>
<td>$480,000</td>
</tr>
<tr>
<td>&gt;60</td>
<td>3%</td>
<td>$355,000</td>
</tr>
</tbody>
</table>
How does the perpetrator’s gender relate to occupational fraud?

<table>
<thead>
<tr>
<th>Gender</th>
<th>Median Loss</th>
<th>Percent of Cases</th>
</tr>
</thead>
<tbody>
<tr>
<td>Male</td>
<td>$156,000</td>
<td>69%</td>
</tr>
<tr>
<td>Female</td>
<td>$89,000</td>
<td>31%</td>
</tr>
</tbody>
</table>
How does gender distribution and median loss vary based on the perpetrator’s level of authority?

- **Employee**
  - $50,000: Male 58%, Female 42%
  - $165,000: Male 73%
  - $128,000: Male 27%
  - $295,000: Male 14%

- **Owner/executive**
  - $1,000,000: Male 86%
How does the perpetrator’s education level relate to occupational fraud?

- High school graduate or less: 24%
- Some university: 15%
- University degree: 47%
- Postgraduate degree: 14%

MEDIAN LOSS

PERCENT OF CASES
How does the number of perpetrators in a scheme relate to occupational fraud?

- **One Perpetrator**: 52% of cases, $74,000 Median loss
- **Two Perpetrators**: 19% of cases, $150,000 Median loss
- **Three or More Perpetrators**: 30% of cases, $339,000 Median loss
How does detection method relate to fraud duration and loss?

- **Active detection method**
- Potentially active or passive detection method
- **Passive detection method**

**Median months to detection**

- **30**
- **25**
- **20**
- **15**
- **10**
- **5**
- **0**

- **IT controls**
- **Surveillance/monitoring**
- **Account reconciliation**
- **Internal audit**
- **Management review**
- **Document examination**
- **Tip**
- **External audit**
- **By accident**
- **Confession**
- **Notified by police**

**Fraud loss**

- **$39,000**
  - 5 months
- **$50,000**
  - 6 months
- **$52,000**
  - 11 months
- **$108,000**
  - 14 months
- **$110,000**
  - 18 months
- **$250,000**
  - 23 months
- **$150,000**
  - 24 months
- **$186,000**
  - 24 months
- **$935,000**
  - 24 months

Report to the Nations ACFE 2018
Fraud Triangle

Developed by Dr. Donald R. Cressey
The Accidental Fraudster
The Predator
Pressure
Rationalization
Criminal Mindset
Incentive
Perceived Opportunity
Arrogance
Personal Integrity
<table>
<thead>
<tr>
<th></th>
<th>ACFE – 2018 Report to the Nations</th>
<th>KPMG – Global Profiles of the Fraudster</th>
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</thead>
<tbody>
<tr>
<td>Gender</td>
<td>69.0% Male 31.0% Female</td>
<td>79% Male 17% Female 4% Unknown</td>
</tr>
<tr>
<td>Age</td>
<td>5% Under 26 10% 26-30 15% 31-35 19% 36-40 19% 41-45 14% 46-50 9% 51-55 6% 56-60 3% Over 60</td>
<td>1% 18-25 14% 26-35 37% 36-45 31% 46-55 8% Over 55</td>
</tr>
<tr>
<td>Tenure</td>
<td>9% Less than 1 year 44% 1 – 5 years 23% 6 – 10 years 24% More than 10 years</td>
<td>2% Less than 1 year 19% 1 – 4 years 14% 4 – 6 years 38% More than 6 years</td>
</tr>
<tr>
<td>Position</td>
<td>44% Employee 34% Manager 19% Owner/Executive 3% Other</td>
<td>32% Management 26% Executive – Director 20% Staff Member 5% Executive – Corp Officer 3% Non-Executive Director 3% Other 2% Owner / Shareholder</td>
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## Primary Internal Control Weaknesses Observed

<table>
<thead>
<tr>
<th>ACFE – Report to the Nations</th>
<th>2016</th>
<th>2018</th>
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<tbody>
<tr>
<td>Lack of Internal Controls</td>
<td>29.3%</td>
<td>30%</td>
</tr>
<tr>
<td>Override of Existing Internal Controls</td>
<td>20.3%</td>
<td>19%</td>
</tr>
<tr>
<td>Lack of Management Review</td>
<td>19.4%</td>
<td>18%</td>
</tr>
<tr>
<td>Poor Tone at the Top</td>
<td>10.4%</td>
<td>10%</td>
</tr>
<tr>
<td>Lack of Competent Personnel in Oversight Roles</td>
<td>6.4%</td>
<td>8%</td>
</tr>
<tr>
<td>Other</td>
<td>5.9%</td>
<td>6%</td>
</tr>
<tr>
<td>Lack of Independent Checks/Audits</td>
<td>4.2%</td>
<td>4%</td>
</tr>
<tr>
<td>Lack of Employee Fraud Education</td>
<td>2.0%</td>
<td>2%</td>
</tr>
<tr>
<td>Lack of Clear Lines of Authority</td>
<td>1.6%</td>
<td>1%</td>
</tr>
<tr>
<td>Lack of Reporting Mechanism</td>
<td>0.5%</td>
<td>&lt;1%</td>
</tr>
</tbody>
</table>

<p>| KPMG – Global Profiles of the Fraudster | | |
|----------------------------------------|------|
| Weak Internal Controls                 | 61%  |
| Reckless Dishonesty Regardless of Controls | 21%  |
| Collusion Circumventing Good Controls  | 11%  |
| Other                                  | 5%   |</p>
<table>
<thead>
<tr>
<th>Fraud Scheme</th>
<th>Duration</th>
</tr>
</thead>
<tbody>
<tr>
<td>Payroll</td>
<td>30 months</td>
</tr>
<tr>
<td>Check and payment tampering</td>
<td>24 months</td>
</tr>
<tr>
<td>Financial statement fraud</td>
<td>24 months</td>
</tr>
<tr>
<td>Expense reimbursements</td>
<td>24 months</td>
</tr>
<tr>
<td>Billing</td>
<td>24 months</td>
</tr>
<tr>
<td>Cash larceny</td>
<td>24 months</td>
</tr>
<tr>
<td>Corruption</td>
<td>22 months</td>
</tr>
<tr>
<td>Skimming</td>
<td>18 months</td>
</tr>
<tr>
<td>Noncash</td>
<td>18 months</td>
</tr>
<tr>
<td>Cash on hand</td>
<td>12 months</td>
</tr>
<tr>
<td>Register disbursements</td>
<td>12 months</td>
</tr>
</tbody>
</table>
### Initial Detection of Occupational Fraud

<table>
<thead>
<tr>
<th>Method</th>
<th>2016</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tip</td>
<td>39.1%</td>
<td>40%</td>
</tr>
<tr>
<td>Internal Audit</td>
<td>16.5%</td>
<td>15%</td>
</tr>
<tr>
<td>Management Review</td>
<td>13.4%</td>
<td>13%</td>
</tr>
<tr>
<td>By Accident</td>
<td>5.6%</td>
<td>7%</td>
</tr>
<tr>
<td>Account Reconciliation</td>
<td>5.5%</td>
<td>5%</td>
</tr>
<tr>
<td>Other</td>
<td>5.5%</td>
<td>6%</td>
</tr>
<tr>
<td>Document Examination</td>
<td>3.8%</td>
<td>4%</td>
</tr>
<tr>
<td>External Audit</td>
<td>3.8%</td>
<td>4%</td>
</tr>
<tr>
<td>Notified by Police</td>
<td>2.4%</td>
<td>2%</td>
</tr>
<tr>
<td>Surveillance/Monitoring</td>
<td>1.9%</td>
<td>3%</td>
</tr>
<tr>
<td>IT Controls</td>
<td>1.3%</td>
<td>1%</td>
</tr>
<tr>
<td>Confession</td>
<td>1.3%</td>
<td>1%</td>
</tr>
</tbody>
</table>
What is Fraud Deterrence?

Protecting the Organization

- Internal Controls
- Risk Assessments
- Tone at the Top (and Tone at the Middle) and PERSONAL RESPONSIBILITY
- Effective Reporting Policy/Procedures
- Heighten Awareness
- Move from being reactive to being proactive
- Pay attention to what’s going on in the lives of others
- Monitor, Monitor, Monitor, Monitor, Monitor...
Behavioral Red Flags

- Living beyond means
- Financial difficulties
- Unusually close association with vendor / customer
- Wheeler-dealer attitude
- Control issues, unwilling to share duties
- Divorce / Family problems
- Irritability, suspiciousness, or defensiveness
- Addiction problems
- Complained about inadequate pay

- No behavioral red flags
- Refusal to take vacations
- Excessive pressure from within organization
- Past employment-related problems
- Social Isolation
- Past legal problems
- Excessive family / peer pressure for success
- Complained about lack of authority
- Instability in life circumstances
<table>
<thead>
<tr>
<th>Control</th>
<th>Percent of cases</th>
<th>Control in place</th>
<th>Control not in place</th>
<th>Percent reduction</th>
</tr>
</thead>
<tbody>
<tr>
<td>Code of conduct</td>
<td>80%</td>
<td>$110,000</td>
<td>$250,000</td>
<td>56%</td>
</tr>
<tr>
<td>Proactive data monitoring/analysis</td>
<td>37%</td>
<td>$80,000</td>
<td>$165,000</td>
<td>52%</td>
</tr>
<tr>
<td>Surprise audits</td>
<td>37%</td>
<td>$75,000</td>
<td>$152,000</td>
<td>51%</td>
</tr>
<tr>
<td>External audit of internal controls over financial reporting</td>
<td>67%</td>
<td>$100,000</td>
<td>$200,000</td>
<td>50%</td>
</tr>
<tr>
<td>Management review</td>
<td>66%</td>
<td>$100,000</td>
<td>$200,000</td>
<td>50%</td>
</tr>
<tr>
<td>Hotline</td>
<td>63%</td>
<td>$100,000</td>
<td>$200,000</td>
<td>50%</td>
</tr>
<tr>
<td>Anti-fraud policy</td>
<td>54%</td>
<td>$100,000</td>
<td>$190,000</td>
<td>47%</td>
</tr>
<tr>
<td>Internal audit department</td>
<td>73%</td>
<td>$108,000</td>
<td>$200,000</td>
<td>46%</td>
</tr>
<tr>
<td>Management certification of financial statements</td>
<td>72%</td>
<td>$109,000</td>
<td>$192,000</td>
<td>43%</td>
</tr>
<tr>
<td>Fraud training for employees</td>
<td>53%</td>
<td>$100,000</td>
<td>$169,000</td>
<td>41%</td>
</tr>
<tr>
<td>Formal fraud risk assessments</td>
<td>41%</td>
<td>$100,000</td>
<td>$162,000</td>
<td>38%</td>
</tr>
<tr>
<td>Employee support programs</td>
<td>54%</td>
<td>$100,000</td>
<td>$160,000</td>
<td>38%</td>
</tr>
<tr>
<td>Fraud training for managers/executives</td>
<td>52%</td>
<td>$100,000</td>
<td>$153,000</td>
<td>35%</td>
</tr>
<tr>
<td>Dedicated fraud department, function, or team</td>
<td>41%</td>
<td>$100,000</td>
<td>$150,000</td>
<td>33%</td>
</tr>
<tr>
<td>External audit of financial statements</td>
<td>80%</td>
<td>$120,000</td>
<td>$170,000</td>
<td>29%</td>
</tr>
<tr>
<td>Job rotation/mandatory vacation</td>
<td>19%</td>
<td>$100,000</td>
<td>$130,000</td>
<td>23%</td>
</tr>
<tr>
<td>Independent audit committee</td>
<td>61%</td>
<td>$120,000</td>
<td>$150,000</td>
<td>20%</td>
</tr>
<tr>
<td>Rewards for whistleblowers</td>
<td>12%</td>
<td>$110,000</td>
<td>$125,000</td>
<td>12%</td>
</tr>
</tbody>
</table>
What is Fraud Prevention?

Fraud prevention requires a system of rules, which in their aggregate, *minimize the likelihood of fraud occurring while maximizing the possibility of detecting any fraudulent activity that may transpire.*
The biggest deterrence to fraud is... the perception of detection.
Things to Think About

Most experts agree that it is much easier to prevent fraud than detect fraud.

“That could never happen here, we have a policy against it.”

The people who can hurt you the most are the people you trust the most.
The Perpetrator

Before
- Oh, what a tangled web we weave when first we practice to deceive
- ......But once we’ve practiced for awhile, Oh my, how we’ve improved our style!

After
- I remember sitting in your office ashamed, hopeless, afraid, and grieving over the pain my selfish decisions had caused to my coworkers, my employer, my family, and myself.

*All hope abandon, ye who enter in.............*

*Dante*
Be Inquisitive

During a review of the Bursar’s daily deposits you note that a significant number of the deposits from one staff member have very little cash included. The other deposits have large cash amounts. All deposits balance to the cashiers’ daily reconciliations. Would this be of concern to you?
WHAT CAN WE DO

Be Inquisitive

Management Review of Internal Controls

Surprise Audits

Fraud Training

Anti-Fraud Policy

Fraud Examiner Department
“TRUE CHARACTER IS DEFINED BY WHAT YOU DO WHEN NO ONE IS LOOKING.”

ANON