Definition of Fraud

• An intentional perversion of truth
• for the purpose of inducing another in reliance upon it
• to part with some valuable thing or surrender a legal right
Motivation to Commit Fraud

Three factors are present when a person commits fraud

1. Perceived Pressure
2. Perceived Opportunity
3. Rationalization

Source: Donald Cressey – The Fraud Triangle. Other People’s Money: A Study in the Social Psychology of Embezzlement
Making The Connection

Ethics
• Standards of Behavior
• Ideals
• Moral action, conduct or character

Fraud
• Dishonesty
• Deception
• Bad Faith
The Underlying Issue of Fraud

The element of **deception allows fraud to hide in plain sight** among all the transactions posted.

If you knew the transaction was fraudulent, you would not have processed it.

**How do you identify anomalous transactions** among all the transactions in the data set?
The Underlying Issue of Fraud

• Deception or falsehood is an act or statement which misleads, hides the truth, or promotes a belief, concept, or idea that is not true.
• Craft your questions carefully
• Listen to the response – Words have meaning
  • Misperception
  • Omission of critical details
• Professional skepticism

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The Fraud Tree

Fraud, Waste & Abuse

Corruption
- Conflict of Interest
- Bribery / Kickbacks / Bid Rigging
- Illegal Gratuities
- Economic Extortion

Asset Misappropriation
- Cash
- Fraudulent Disbursements
- Inventory and all other assets

Financial Statement Fraud
- Account revenue overstatement
- Asset revenue understatement
Define the Scope of the Issue

On average, businesses lose about five per cent of their revenue to fraud every year. Corruption, financial statement fraud, healthcare fraud, asset misappropriation and other forms of fraud are real risks for today’s businesses.

Source: ACFE Report to the Nation on the Risk of Occupational Fraud
Scope of the Issue Continued

Source: ACFE Report to the Nation on the Risk of Occupational Fraud
How is Fraud Detected?

Organizations with **FRAUD AWARENESS TRAINING** for employees were more likely to gather tips through **FORMAL REPORTING MECHANISMS**.

- 56% of tips with training
- 37% of tips without training

43% of schemes were detected by tip, and half of those tips came from employees.

Telephone hotline and email were each used by whistleblowers in 33% of cases.

Source: ACFE Report to the Nation on the Risk of Occupational Fraud
How is Fraud Detected?

**USE OF TARGETED ANTI-FRAUD CONTROLS HAS INCREASED OVER LAST DECADE**

- **HOTLINE**: 13%
- **ANTI-FRAUD POLICY**: 13%
- **FRAUD TRAINING FOR EMPLOYEES**: 11%
- **FRAUD TRAINING FOR MANAGERS/EXECUTIVES**: 9%

**A lack of internal controls contributed to nearly 1/3 OF FRAUDS**

**THE PRESENCE OF ANTI-FRAUD CONTROLS IS ASSOCIATED WITH LOWER FRAUD LOSSES AND QUICKER DETECTION**

**CERTAIN FRAUD RISKS WERE MORE LIKELY IN SMALL BUSINESSES THAN IN LARGE ORGANIZATIONS:**

- Billing fraud: 2X HIGHER
- Payroll: 2X HIGHER
- Check and payment tampering: 4X HIGHER

Source: ACFE Report to the Nation on the Risk of Occupational Fraud
How is Fraud Detected?

80% of fraudsters faced some form of internal discipline from the victim organization, 46% of victim organizations declined to refer cases to law enforcement because internal discipline was sufficient. 42% of occupational fraudsters were living beyond their means. 26% of occupational fraudsters were experiencing financial difficulties.

Source: ACFE Report to the Nation on the Risk of Occupational Fraud
Small Town Big Fraud – Trusted Employee

Rita Crundwell
• Former Comptroller, Dixon Illinois, $83,000 annual salary
• Sentenced to 19.5 years in federal prison
• Stole $54 million in city funds
• 169 unauthorized fund transfers over 12 years
• World class quarter horse breeder farm business
  RC Quarter Horses LLC, Dixon Illinois
• Winner of 52 world championships

Dixon, Illinois,
• Population 15,000 - 150 miles west of Chicago
• Largest municipal embezzlement in U.S. history
• Annual budget $9 million
• City in financial crisis – hiring freeze – layoffs – multi year pay freeze - infrastructure improvements deferred – public safety improvements denied
• Crundwell opened a checking account that appeared to be a city account; RSCDA c/o Rite Crundwell
• Diversion of funds from City of Dixon State of Illinois municipal money market fund to RSCDA
Ponzi Schemer Bernie Madoff – Trusted Advisor

- Largest fraud in Wall Street history
- Largest Ponzi scheme in history
- New investor funding used to pay returns to older investors
- Provides the illusion of profitable investment

- Madoff was an investment advisor
- Helped launch NASDAQ and advised the SEC on the system
- Over several decades Madoff enjoyed the image of a self-made financial guru
- Statements claimed investor accounts totaled $65 billion with double digit returns on investment
- No securities were ever bought or sold
- All the transactions on the statements were fake
- More than 15,400 claims against Madoff were filed
- Estimates indicate the scheme ran 20 years
- Victims ranged from Florida retirees to Hollywood elite
- Sentenced to 150 years in prison
- Madoff died April 14 in federal prison (82 years old)
Fraud Risk Thrives in Uncertainty

- Historically, fraud fills the void when GDP declines
- Fraud thrives in times of uncertainty and anonymity
- Pandemic curtailed in person transactions in favor of e-commerce
Anti-Fraud Framework

Corporation Governance

Control Environment
- Risk Assessment
- Resource Management
- Training & Education
- Technology

Incident Response
- Integrated Fraud Management Platform
  - Loss Recovery
  - Fraud Investigation
- Reporting, Public Relations

Detection
- Data Management and Analysis
- Client Record and Transaction Platforms

Fraud Prevention
- Client Record and Transaction Management

Channel Management
- Internet
- Mobile
- Office
- POS
- Call Center

Policies and Procedures Development

Program Management

Monitoring / Self-Testing
# Anti-Fraud Framework

## Enterprise Foundation
- Formal fraud strategy
- Fraud Prevention Policy

## Control Environment
- Risk Assessment
- Resource Management
- Training
- Socialize risk of fraud and red flags

## Fraud Prevention
- Channel Management
- Account Management

## Fraud Detection
- Ongoing monitoring
- Anomaly detection
- Data Management
- Data Quality
- Data Security
- Data Lineage
- Metadata Repository

## Incident Response
- Enterprise-Wide Corporate Authority
- Investigation Management
- Loss Recovery
- Financial Management Reporting
Fraud Risk Mitigation – Culture – Code of Conduct and Code of Ethics

• Tone from the top
• Value Statement
• Good and lawful corporate citizen
• Do the right thing - Integrity
• Fair and respectful treatment
• Communicate expectations
• An affirmative duty to report
• Safe Harbor free from retaliation
• Employee Hotline
Enhancing the Anti-Fraud Risk Management Program

- Fraud strategy in alignment with enterprise risk
- Fraud policy align to strategy
- Procedures reflect strategy
- Fraud risk assessment
- Communication of the fraud risk management program
- Effective preventative and detective controls including transaction monitoring and testing
- Establish a communication plan to receive information
- Establish incident response plan
- Establish and Report on Fraud Typologies
- Monitor, evaluate and report on the enterprise fraud risk management program
Questions?
Closing thoughts

Thomas Paar, CFE, CAMS
Crowe LLP
thomas.paar@crowe.com
(630) 575-4324