



world compliance

Fraud Prevention



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Defining fraud

Fraud is defined as the use of one's position within an organization to misuse said position for personal enrichment. The main forms of fraud are:

- Illegal use of a fiduciary duty
- Bribes
- Hiding material information
- Stealing of cash or property
- Stealing intellectual property
- Any other statutory offense

In 2004, The Association of Certified Fraud Examiners reviewed over 500 fraud cases to determine the business cost of fraud, the methods used to commit fraud, fraud detection as well as legal ramifications.

To illustrate the report, the association developed a Uniform Occupational Fraud Classification System which they referred to as the Fraud Tree <http://www.mass.gov/ig/publ/fraudadv.pdf>. The Fraud Tree classifies fraud into three main categories:

- **Corruption schemes:** This includes bribery, conflict of interest, economic extortion and illegal gratuities. This category represented 30% of all fraud cases examined.
- **Asset misappropriation:** Includes stealing both cash and property, this category represents by far (93%) the largest percent of fraud committed
- **Fraudulent statements:** Includes both financial and non financial information, this category represented only 8% of all fraud

Please note that these numbers exceed 100%, this is due to the fact that multiple cases involved a combination of fraud categories.



Impact to businesses

The 2004 report went on to indicate that the average business losses 6% of their annual revenues to fraud. This is particularly true for smaller organizations (less than 100 employees). The percent of losses grows to 21% when evaluating slightly larger organizations with 100 to 999 employees. The report also indicated that organizations in the private sector were more vulnerable than comparatively government offices.

Profiling those who commit fraud

The majority of persons who commit fraud are usually first time offenders, only 12% of those who committed fraud had been previously convicted of a fraud related case. Also, fraud is usually committed by someone holding an executive position, has been in the company for a long time and is highly respected.

Fraud detection

Fraud is usually detected either through an audit or an informant's tip. The first line of defense, especially when hiring someone to occupy a sensitive position, should be to perform a thorough background check. In addition though, an organization should implement the following strategies to combat fraud:

- Develop a set of internal controls
- Implement a continuous program of anti fraud education
- Conduct regularly scheduled fraud audits
- Implement an anti fraud policy



Fraud policy recommendations

Ensure that the fraud policy is written into the organizations code of ethics and mission statement. The following are guidelines towards developing a fraud policy:

- Ensure that all fraud policies are in writing
- The policy should clearly delineate the rules governing consultants in regards to conflicts of interest
- The policy should clearly delineate the use of the organizations assets such as company vehicles
- The policy should clearly delineate the organizations policy towards timekeeping, travel, reimbursements and other related items
- All new employees should be handed a copy of the fraud policy statement and made to sign indicating that they have received it and that they understand the content
- The organization should ensure that employees review the company's fraud policy annually as part of the ongoing education program
- The fraud policy should cover all applicable laws and regulations with an explanation detailing what is a conflict of interest as well as clearly delineating steps to take when being offered a gift from a third party
- The fraud policy should clearly delineate the expected employees conduct while at work, including the consequences of drug or alcohol use
- The fraud policy should also cover the ethical standards that are expected from both employees as well as political contributors



Fraud prevention programs

First and foremost, the organization needs to conduct a fraud risk assessment to identify the company's vulnerabilities within each of the three categories of fraud that were earlier mentioned (Corruption schemes, fraudulent statements and asset misappropriation). It is recommended to hire either an external Certified Fraud Examiner consultant or Certified Public Accountant firm to conduct the assessment. Once completed and the vulnerabilities have been identified, the organization can set to the task of designing a fraud prevention program: The following guidelines are meant to serve as the core requirements for a comprehensive program:

Oversight

- Create an audit committee empowered to evaluate and review senior management concerning financial reporting
- Implement anti fraud processes and controls to be regularly monitored by management
- Create an internal audit team that is well versed in the company's workings to identify those indicators that would suggest fraud is occurring
- Hire independent auditors who can provide a non-biased (outsiders) perspective as well as unearth previously missed risks
- Hire a Certified Fraud Examiner to provide special expertise that otherwise may not be available within the organization

Internal audit controls

An audit committee designed to work with the organizations accounting department to ensure that adequate processes are in place, including sound accounting principles and regularly scheduled audits

Division of responsibilities

Contract management and individual financial transactions should be divided and handled by multiple persons to avoid concentration in any particular area



Employee hot line

Provide employees with a communication channel to anonymously report suspicious activity and or ethical misconduct

Education program

Conduct an anti fraud education program at least annually and ensure that all new hires be given the same

Reporting

Ensure that everyone in the organization knows who the appropriate department is to be contacted for reporting suspicious and or fraudulent behavior



A World in Compliance

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