

# FROM “PREY” TO “PROTECTOR”

## Avoiding Common Fraud Pitfalls

By Jenell West

It sounds like the setup for a primetime crime drama: trusted employees embezzling tens of thousands of dollars from their employers.

This isn't fiction, though. It's real life and it's happening right now.

According to the most recent Report to the Nations on Occupational Fraud and Abuse from the Association of Certified Fraud Examiners' (ACFE), the annual median loss experienced by organizations in the government and public administration sector is \$64,000. In fact, more than 10 percent of fraud cases affect this industry—second only to banking and financial services.

But there's good news: there are steps you can take today to help prevent your municipality from falling prey to such misfortune. The following are some common schemes you need to be aware of, along with tips to avoid falling victim to them.

### Cash Receipt Fraud

Cash receipt fraud is typically committed by those responsible for collecting or remitting cash. Think ancillary revenue sources such as dog licenses, fees at community centers and school activities—not main sources of funds like tax payments.

To prevent cash receipt fraud:

- Consider replacing pen-and-paper procedures with computerized systems when possible. If you can't replace your pen-and-paper system, use pre-numbered receipts and verify that the number of receipts issued corresponds with your accounting records.
- Leverage audit trails/reconciliation features within computerized systems as appropriate.

- Require the employee remitting funds to sign his or her name on transmittal forms and deposit tickets so that you have clear evidence of who was remitting the funds.
- Require employees to place cash and checks in a sealed, tamper-evident bag prior to remittance to their colleagues/bank.
- Develop and implement a document retention policy. Documents should be stored by an employee who is not responsible for collecting, recording or reconciling cash receipts.
- Perform spot checks of cash deposits.

### Credit Card Fraud

Credit card fraud is one of the most frequently occurring types of fraud—lax documentation guidelines allow fraudsters to add non-work-related charges to your credit cards.

To mitigate credit card fraud:

- Design an acceptable use policy for your credit cards and require employees to acknowledge it in writing. This policy should clearly state the consequences of credit card misuse and missing receipts.
- Review employees who have been issued credit cards and verify that their spending limits are appropriate.
- Cancel credit cards when employees are terminated.
- Require that copies of original, detailed receipts be submitted with credit cards and expense reports.



## Expense Report Fraud

Expense report fraud is committed at all levels of an organization. Employees are emboldened by poor review procedures, which can lead to lavish meals with friends and gifts purchased under the guise of business dinners and other seemingly innocuous activities.

Prevention tips mirror those of credit card fraud. In addition:

- Designate a qualified staff member to review and approve documentation related to expense reports. Expense reports belonging to upper-level staff should be reviewed by your city council, board of commissioners, etc.
- Approach a review logically. When and where was the item purchased? Does the location make sense? If a vendor lunch took place 20 miles away from their office and yours, why? If a gift was recorded as being given to someone, call and ask what they thought of it.
- Detect outliers like consistently high totals and unusual growth in total expenses.
- Compare projected expenses to actual expenses for business trips and other items that may be included on numerous expense reports.

## YOUR FRAUD PREVENTION TOOLKIT

Once you understand what to look out for, it's also good to make sure you have the proper tools for preventing fraud at your disposal. Everyone loves a red flag—they help highlight situations that require prompt attention. Red flags can include an employee living beyond his or her means, a refusal to take vacations, unusually close associations with vendors and an unwillingness to share job responsibilities. Financial difficulties and domestic problems frequently afflict perpetrators of fraud.

Your strongest assets in the fight against fraud? Your employees and vendors. Just under half of all internal cases are reported by those who work for and with the victimized organization. Minimize losses by implementing a user-friendly reporting system such as a 24/7 hotline and encourage your staff to utilize it.

Management review and internal audit are also key contributors to uncovering suspicious activity.

In-depth background investigations of new staff provide one of your strongest means of preventing internal fraud. Periodic re-investigations, especially for recently promoted individuals, are also essential.

Trust is not an internal control. Properly designed and customized internal controls help ensure that all money circulating in and out of the organization is accounted for and thoroughly documented. Enforcing this protocol provides the opportunity to identify fraud before it can inflict significant damage.



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## Misuse of Government-Owned Assets

Asset misuse can occur throughout your government. Using a government-owned vehicle for personal trips is one example.

To prevent misuse:

- Specify the terms of appropriate use and update as necessary in a contract or employee manual.

- Document the financial terms of any agreements in a contract or employee manual.
- Remind employees of these agreements and where they can find them.

## Collusion with Vendors

While rare, collusion with vendors can be costly. Investment in or ownership of a supplier or competitor, acceptance of inappropriate gifts and involvement in other business ventures with vendors are all instances of this type of fraud.

To prevent vendor collusion:

- Perform due diligence on any new vendors.
- Review disbursements to vendors to ensure that there is a valid contract governing the payments.
- Compare vendor addresses to employee addresses and promptly investigate any commonalities.

If you suspect fraud is taking place in your organization, be sure to secure legal counsel before taking any other steps. Become informed about your rights and the rights of the person or people perpetrating the fraud.

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