

FORVIS

Mitigating Big Risks for Small Businesses

Outsourced Accounting Services

Presenters

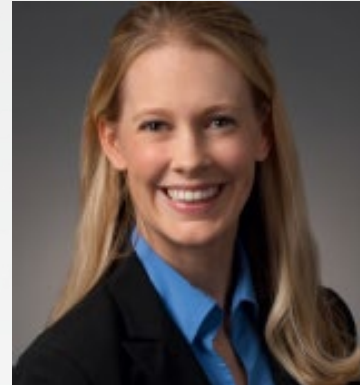


Neely Duncan

Partner – DFW

neely.duncan@forvis.com

972.361.3744



Brinn Serbanic

Partner – DFW

brinn.serbanic@forvis.com

254.756.8610

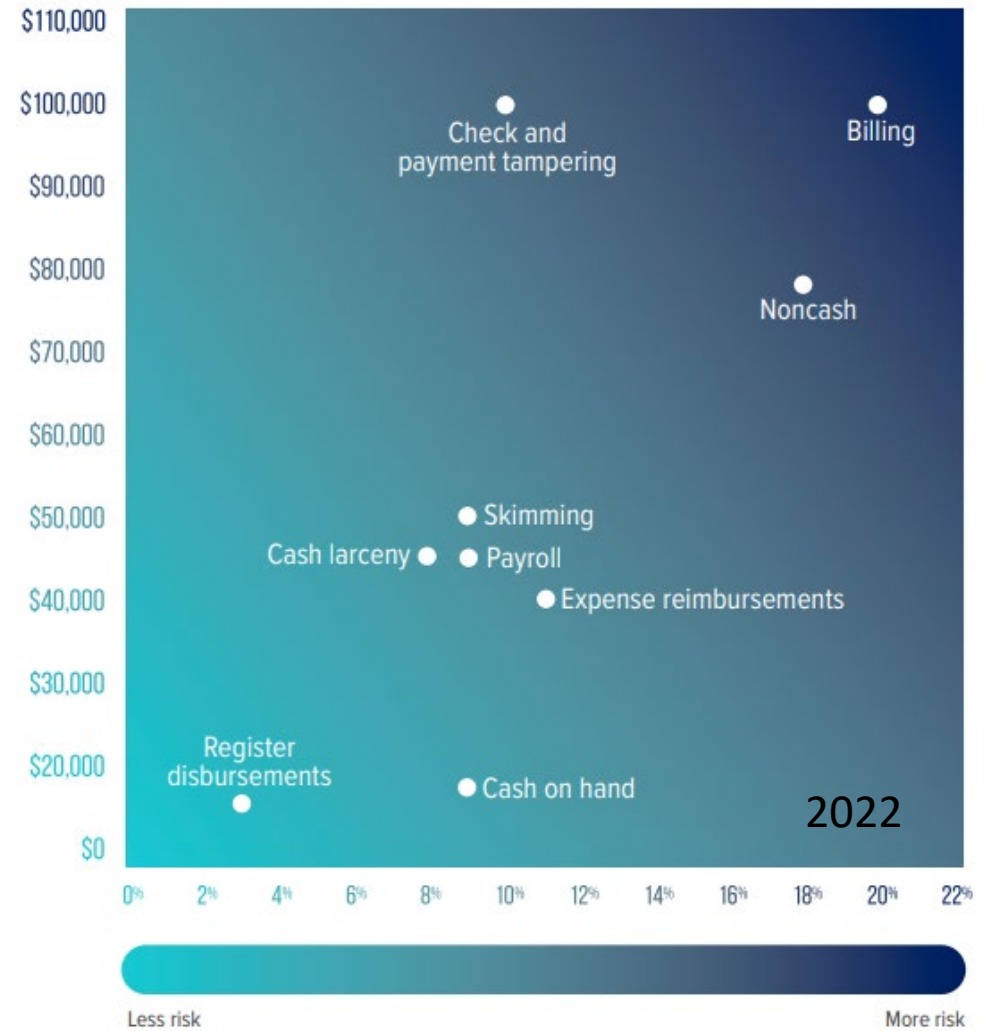
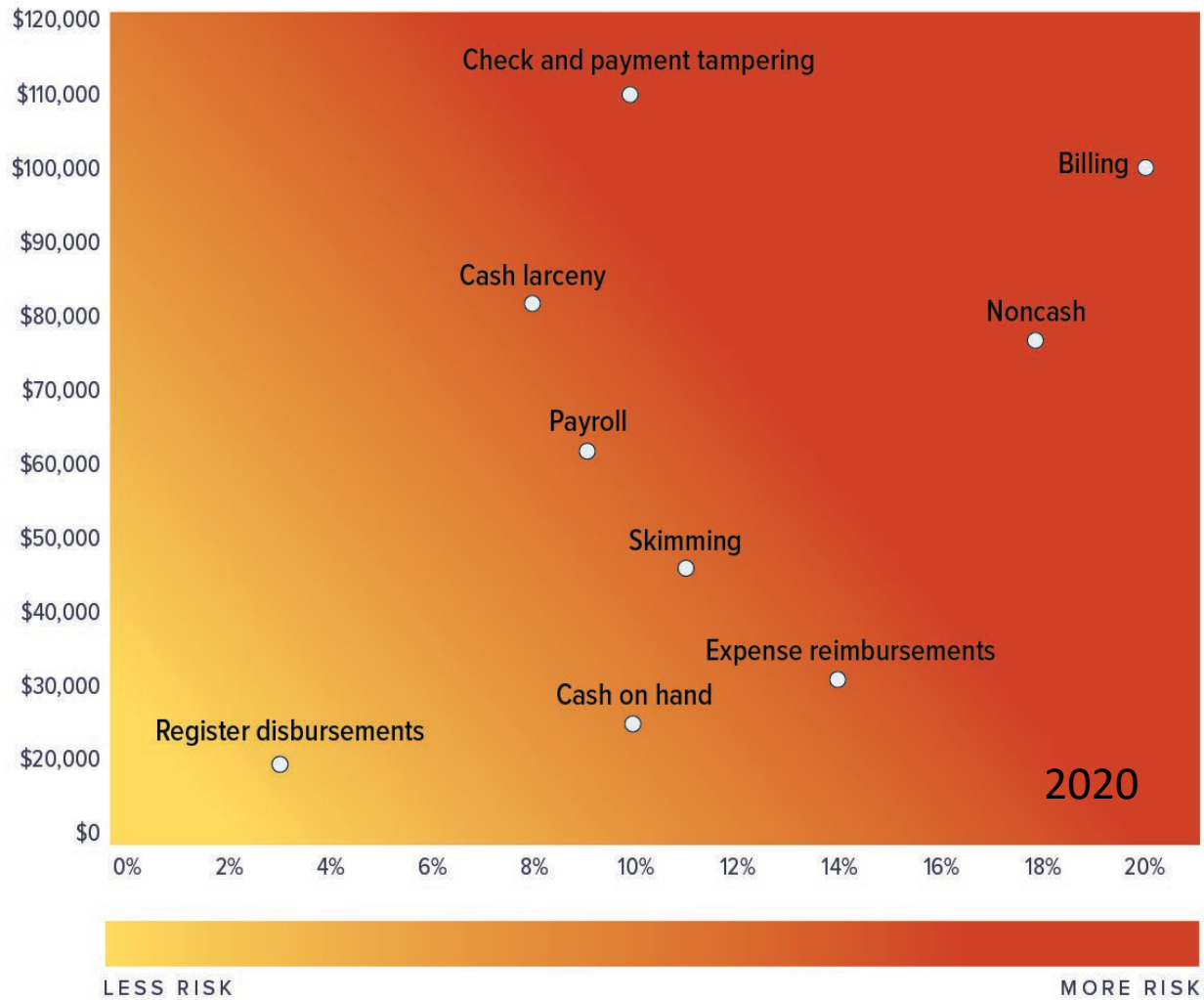
Facts About Fraud

- Estimated that typical organization loses 5% of its annual revenue
- **\$3.6 billion** was the total loss caused by the cases in the study
- The median loss per case was \$117,000
- 21% of these cases caused losses of at least \$1 million
- 8% of fraud cases involved the use of cryptocurrency



Facts About Fraud

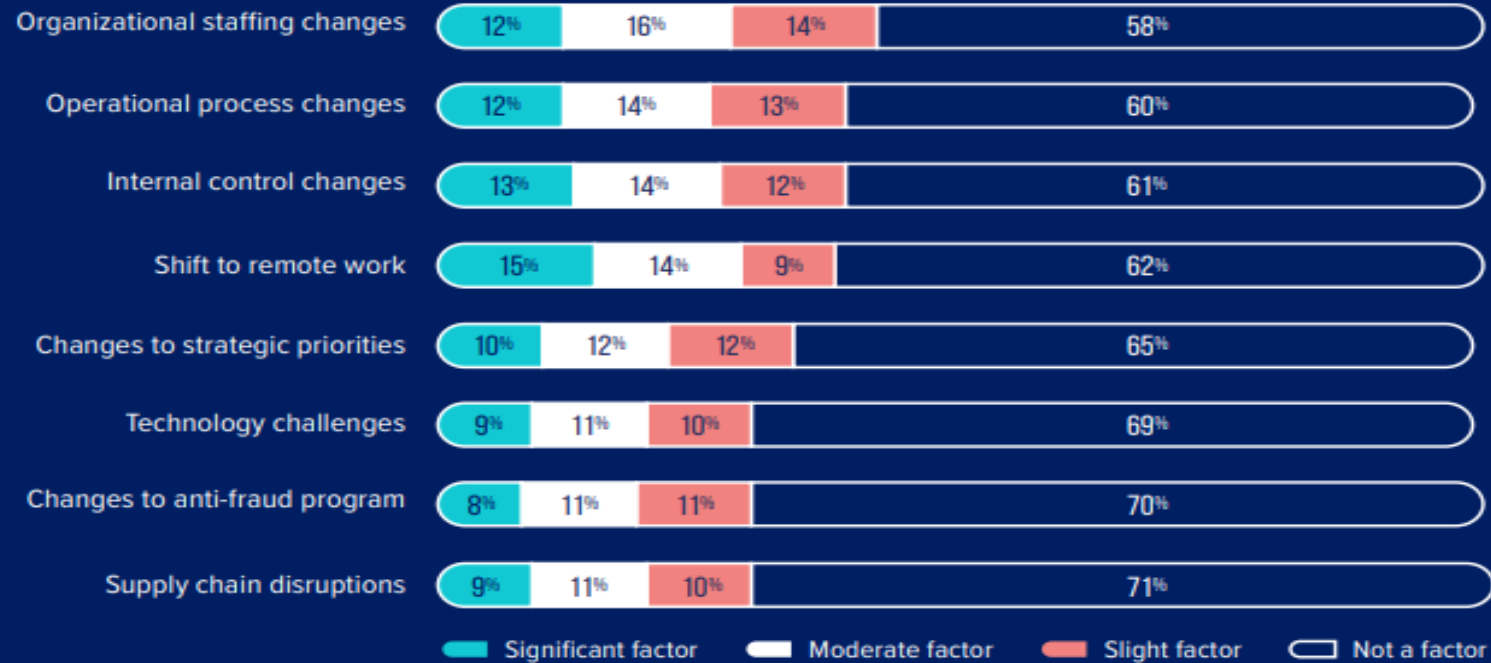
What asset misappropriation schemes present the greatest risk?



FORVIS

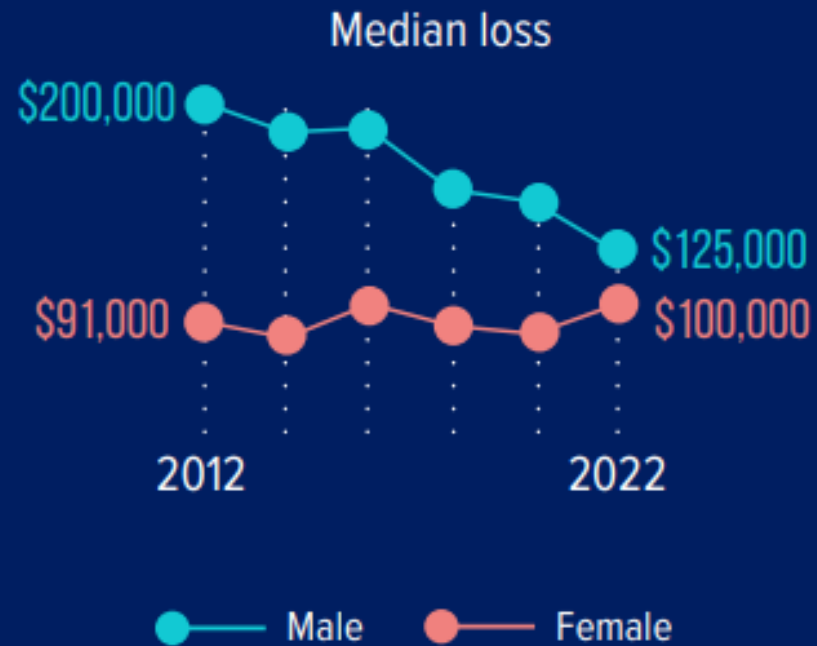
Facts About Fraud – COVID

TO WHAT EXTENT DID PANDEMIC-RELATED FACTORS CONTRIBUTE TO OCCUPATIONAL FRAUDS?



Facts About Fraud

MEN are perpetrating an **INCREASING** percentage of **FRAUDS**, but the gap in **LOSSES** has **NARROWED**.



MALE

65%
2012  73%
2022



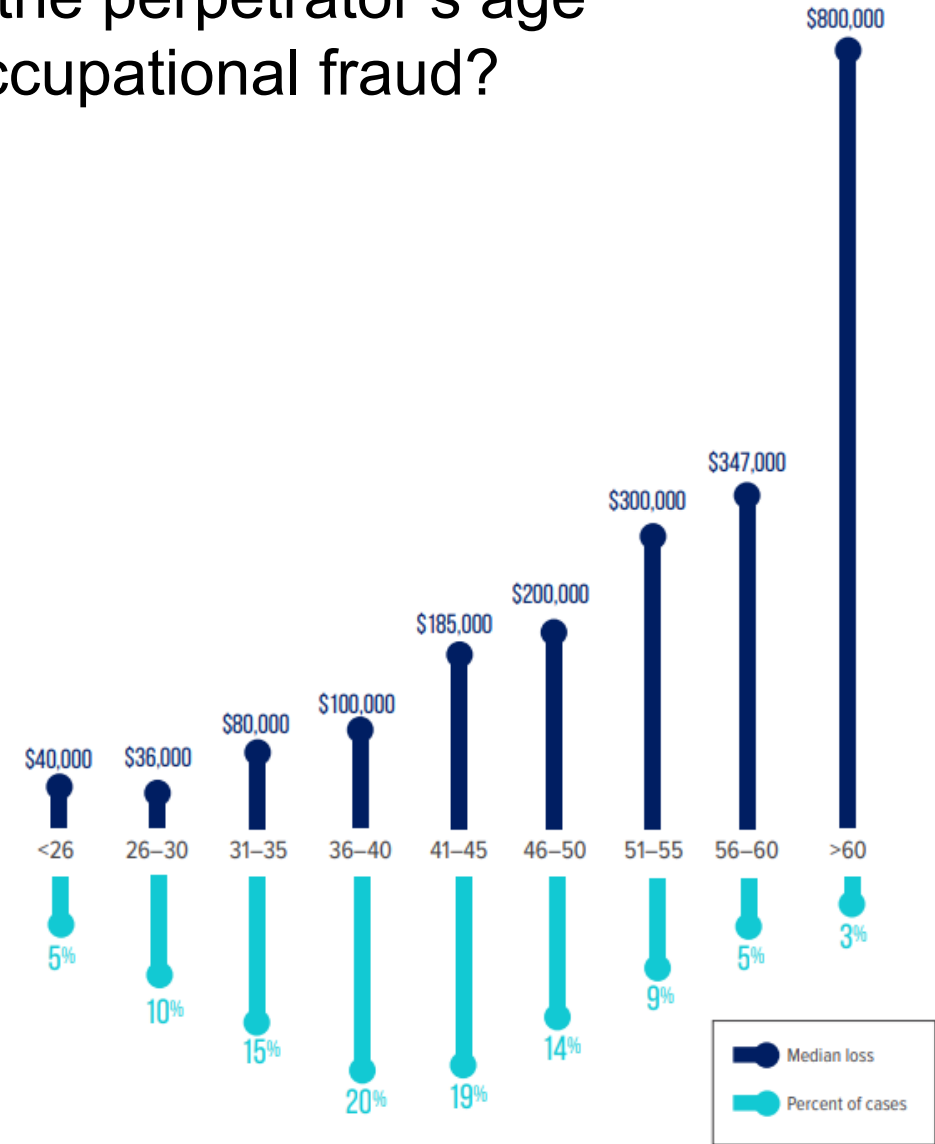
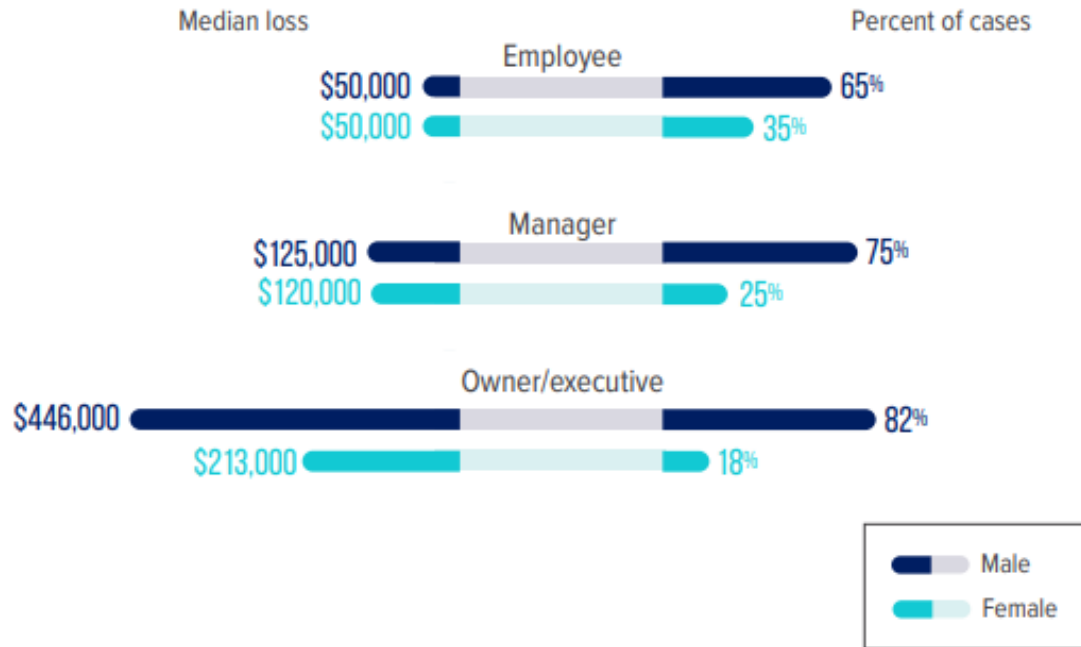
FEMALE

35%
2012  27%
2022

Facts About Fraud

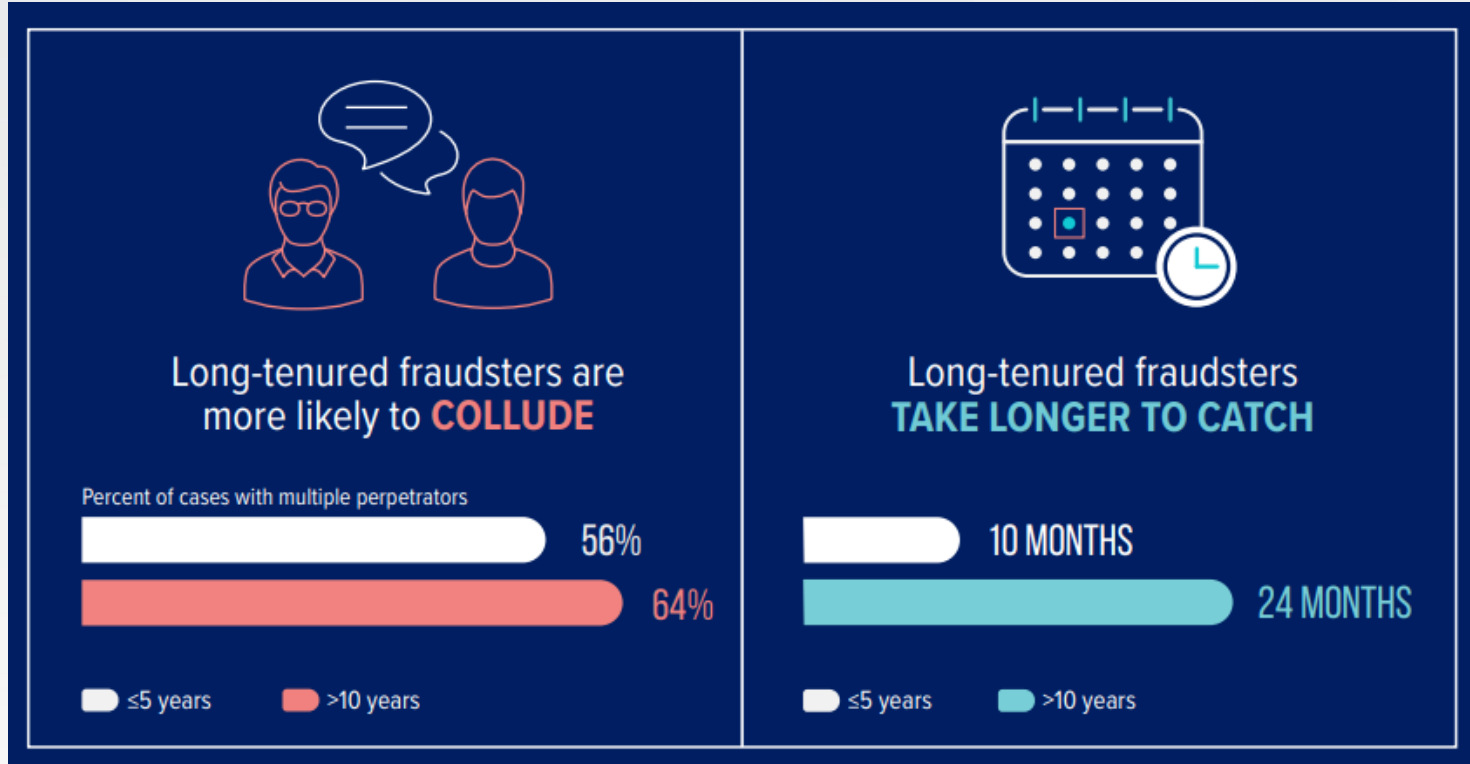
How does the perpetrator's age relate to occupational fraud?

How do gender distribution & median loss vary based on the perpetrator's level of authority?

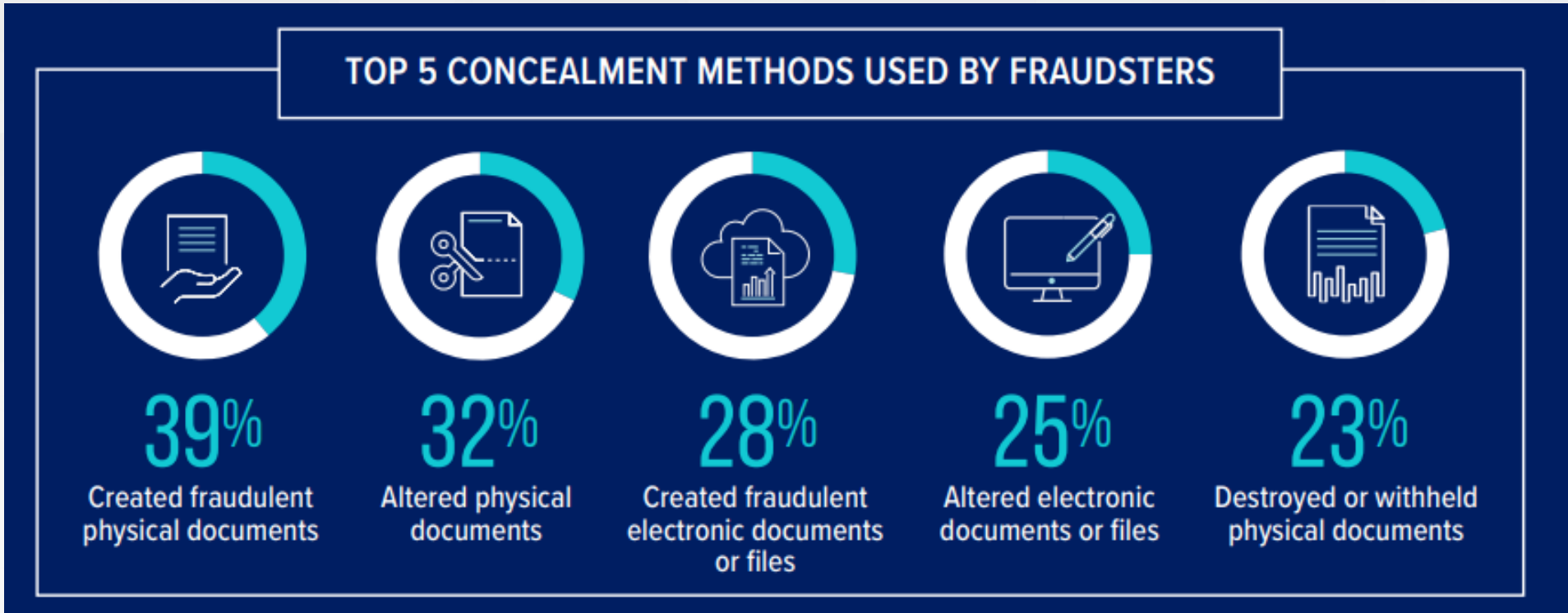


Facts About Fraud

How does the perpetrator's tenure relate to occupational fraud?

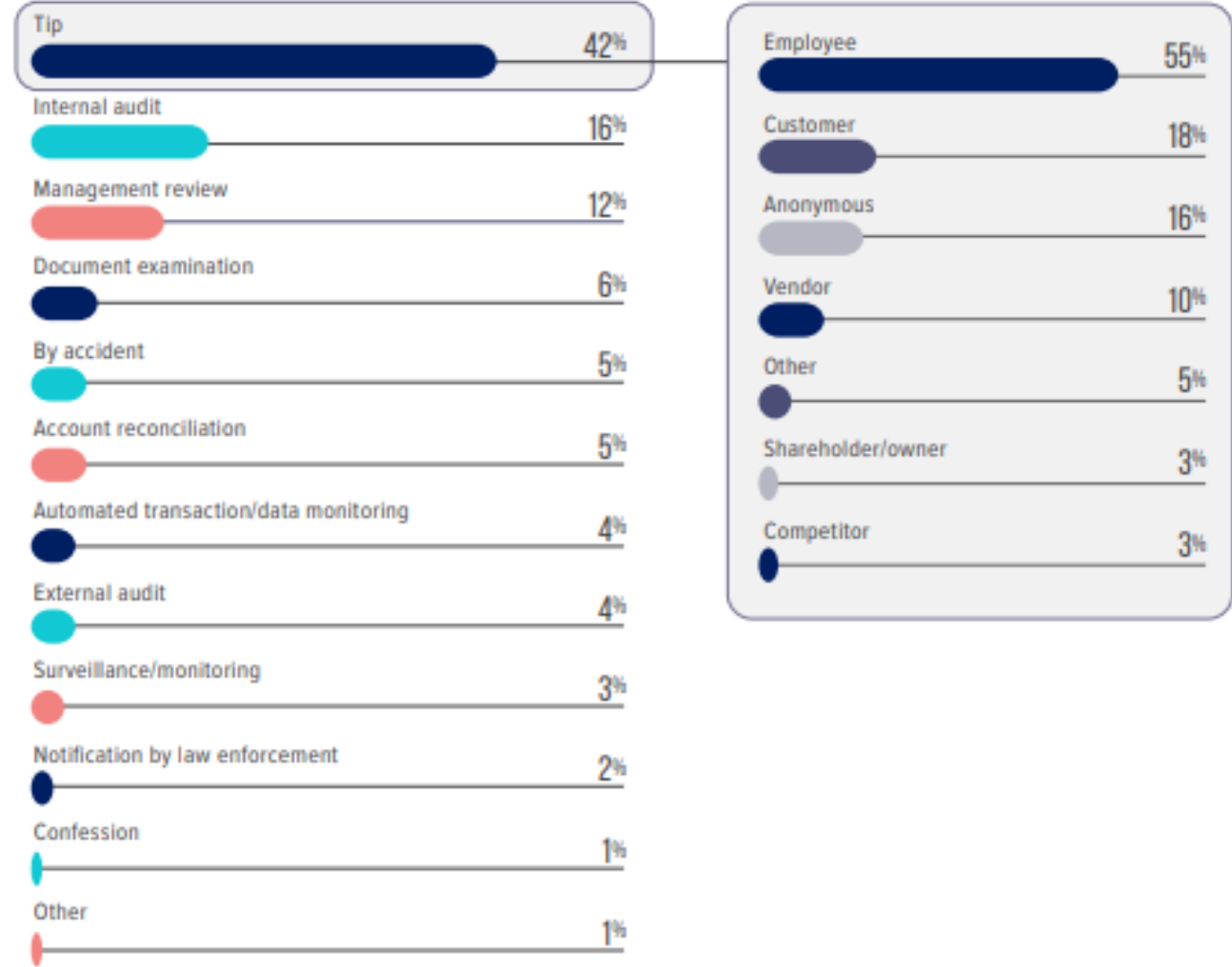


Facts About Fraud



Facts About Fraud

How is fraud usually detected & by whom?



Facts About Fraud – Hotlines

EFFECT OF EMPLOYEE AND MANAGER FRAUD AWARENESS TRAINING ON HOTLINES AND REPORTING

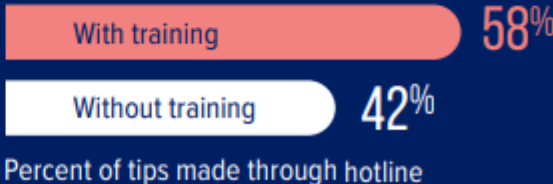
TRAINING INCREASES the likelihood of detection by tip

45% of cases detected by tip with training

37% of cases detected by tip without training



Reports of fraud are **MORE LIKELY TO BE SUBMITTED** through hotlines with training



70% of **VICTIM ORGANIZATIONS** had hotlines

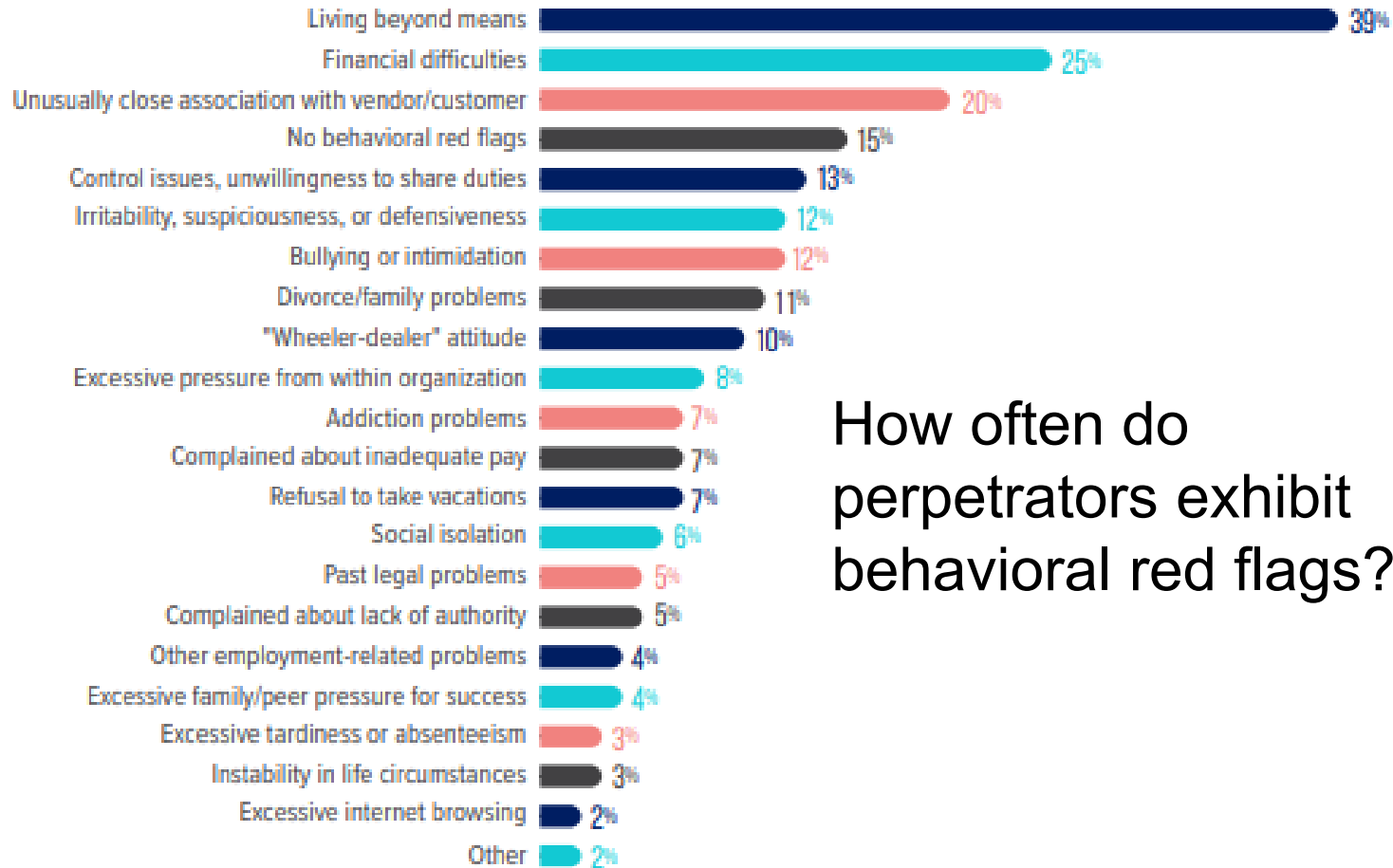
Fraud losses were **2X HIGHER** at organizations without hotlines



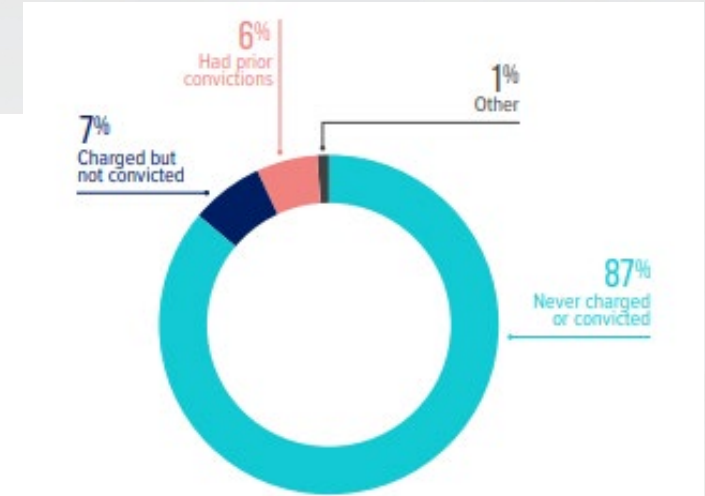
With hotlines **\$100,000**

Without hotlines **\$200,000**

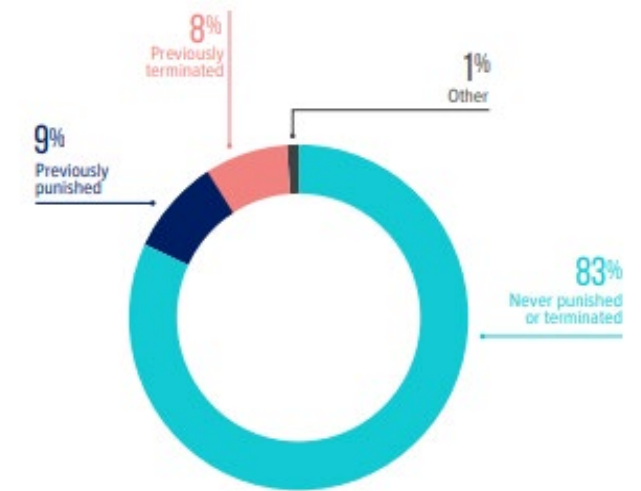
Facts About Fraud



How often do perpetrators exhibit behavioral red flags?



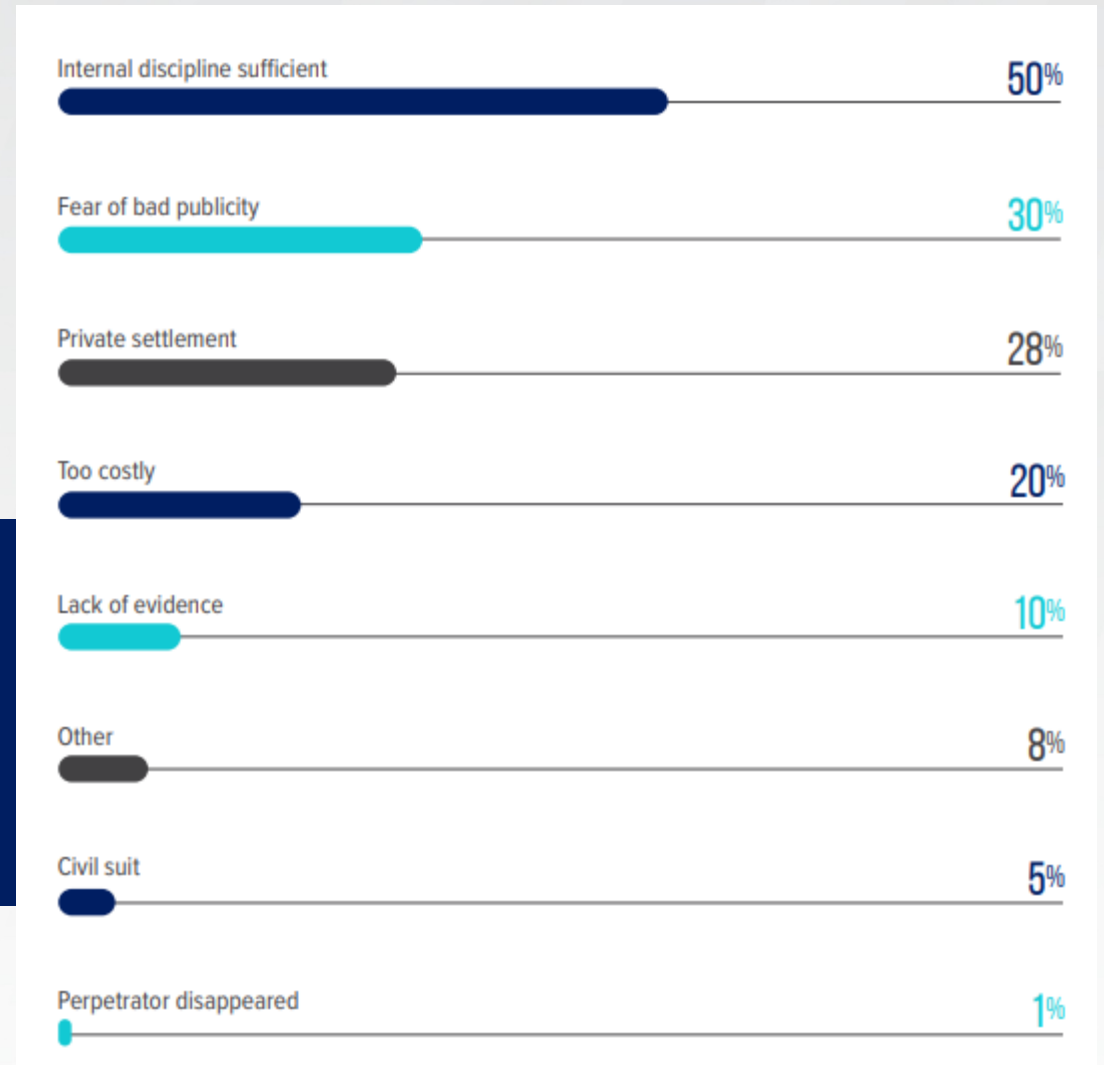
Perpetrators with prior fraud convictions



Prior employment-related disciplinary actions for fraud

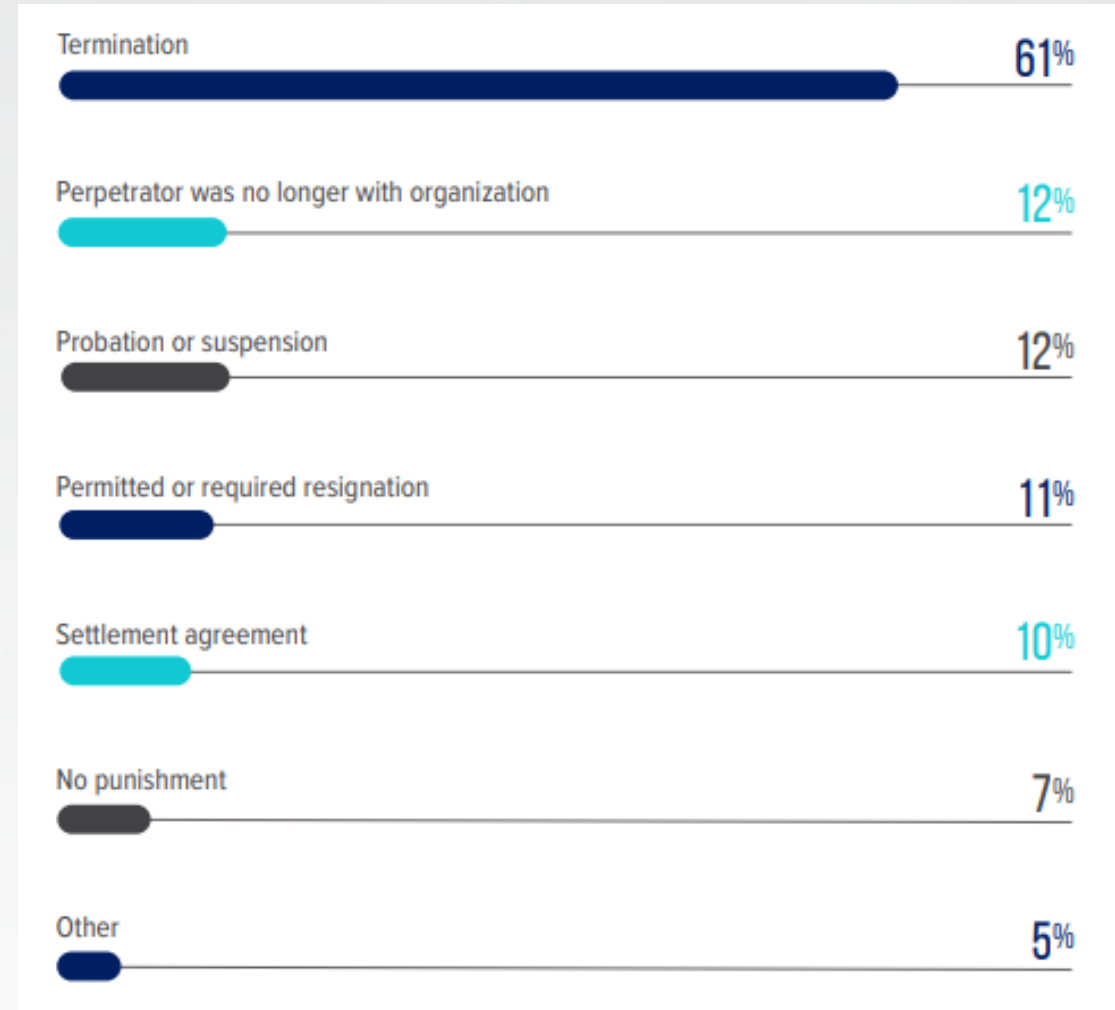
Facts About Fraud

Why do organizations decline to refer cases to law enforcement?

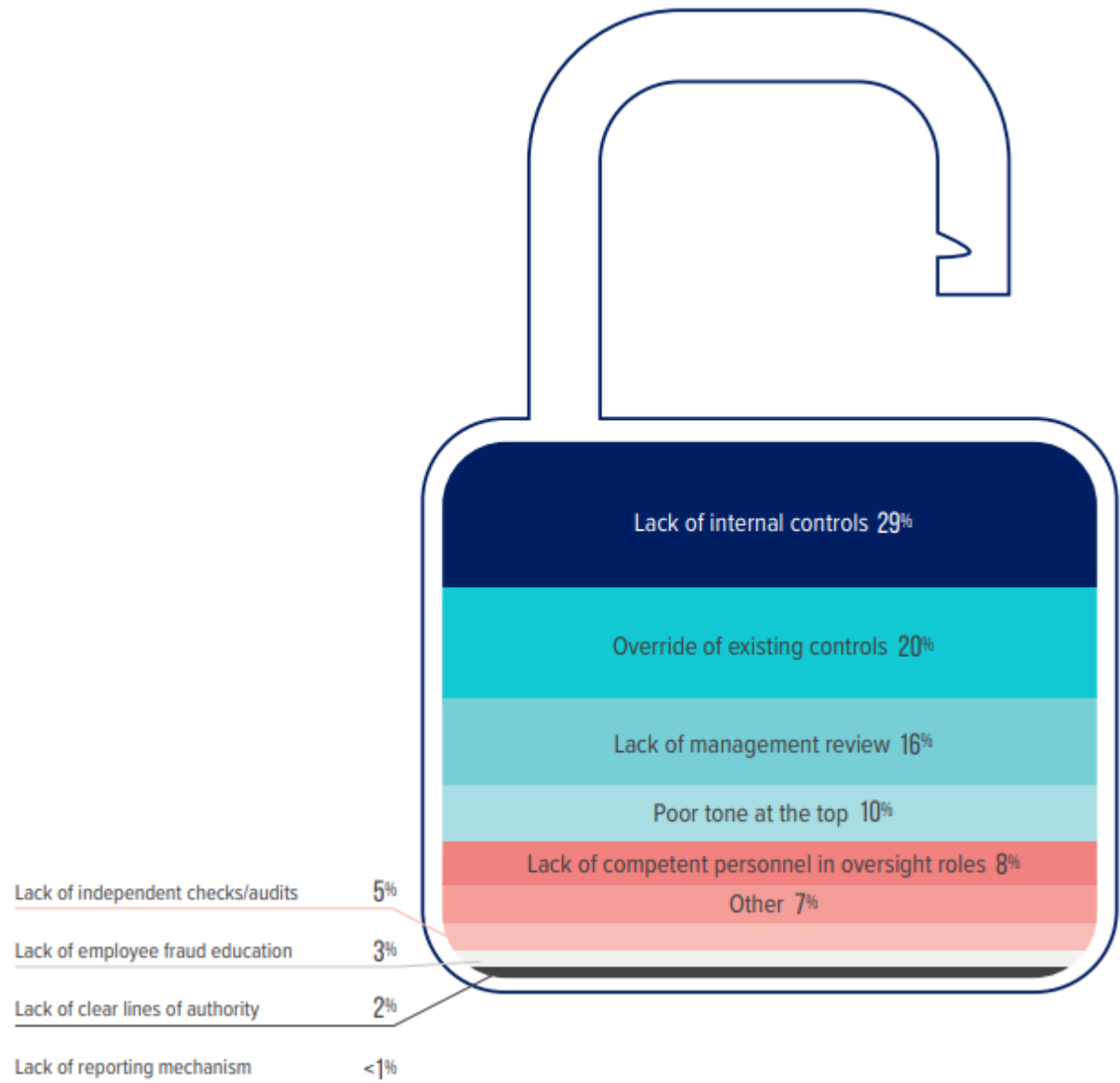


Facts About Fraud

How do victim organizations punish fraud perpetrators?



Facts About Fraud & Internal Controls



Facts About Fraud & Internal Controls

What controls are most common?



Process vs. Control

Process	Control
Captures data, changes data, & potentially introduces possible errors	Does not change; prevents or detects & corrects errors introduced through processes
Process: post, payment, compile, prepare, etc. Control: agree, match, approve, review, double check, safeguard, authorize	

Three-Step Process to Understand Controls

- What process is used to complete a transaction?
- What could go wrong?
- What controls are in place to prevent errors?



Strong Control Environment

- Management oversight & involvement throughout process
- Preventive controls
- Detective controls



Control Analysis

- What controls are in place?
- Are there any gaps that need to be addressed?
- Do the controls in place provide an effective & efficient organization/operation?



Example Analysis

Cash Receipts		
Process	What Could Go Wrong	Control
Set Up New Vendor	Fictitious vendor	Review of new vendors
Set Up Receivable Balance	Wrong amount, wrong aging, wrong restriction, wrong period	Supervisor review & approval
Revenue/Rec. JE Created	Input/processing error, data lost, access issues	Supervisor review & approval of entry
Cash Received	Cash stolen, record wrong amount	Reconciliation & review
Create Cash Receipts Listing	Cash stolen, record wrong amount	Reconciliation & review
Cash JE Created	Wrong account, period, amount	Review & approval
JE Posted to GL	Input error – account, period, amount	Review
Financial Statements Created	Wrong line item	Management review & budget comparison

The Control Environment

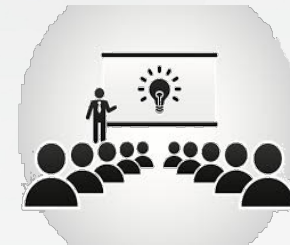
- Tone at the top – **YES, YOU MAKE THE BIGGEST DIFFERENCE TO PROTECTING YOUR ORGANIZATION**
- Typical management exceptions
- COSO
 - Integrity & ethical values
 - Commitment to competence
 - Board of directors & audit committee
 - Management's philosophy & operating style
 - Organizational structure
 - Assignment of authority & responsibility
 - Human resource policies & procedures



Recommendations – Education

■ Educate

- Technology is no substitute for employee education
- Educate & re-educate the entire organization, not just IT
- Include the board, executives, & vendors
- Knowledge is power
- Do not discourage false-positive reporting
- Document your security policies in a knowledge database so everyone understands exactly what is going on & why
- Develop & rehearse a robust incident response program



Segregation of Duties

- No single individual is responsible for receiving, recording, & depositing funds or writing & signing checks
- No single individual is permitted to request, authorize, verify, & record expenditures
- Flowchart the process
- In small businesses where fewer people are on staff, consider the power of automation!
 - Accounts payable platforms such as Bill

Categories of Duties

- Custody of assets (access)
- Record transactions (recording)
- Authorization & reconciliation (monitoring)
- Key: Analyze if **access & recording** or **access & monitoring**
- Analyze conflicts & look for potential errors & complementary controls

Example #1

Director of Finance is the only accounting & finance staff

- Access duties – custody of deposits
- Recording duties – all journal entries to record any revenue activity in the accounting system
- Monitoring Duties – all reconciliations (bank, accounts receivable) as well as responsibility for monitoring the classification of revenue

What could go wrong?

What Could Go Wrong?

Director of Finance could remove & keep cash from the deposits & conceal through writing off A/R & adjusting all reconciliations

How to Lower Chance of Error/Fraud

- Since there is no other staff on the accounting/finance team, there are no further segregation of duties
- Complementary controls – All items to be deposited are logged by a staff prior to handing off to the Director of Finance for deposit. Or use a lock box that would funnel deposits through the bank directly
- Compensating controls – Operations team ties deposit slip back to A/R log after funds are deposited, CEO reviews all reconciliations

Example #2

CEO

- Access duties – receive payments
- Recording duties – initiate &/or approve write-off of an uncollectible account
- Monitoring duties – review bank reconciliations prepared by accounting/finance team

What Could Go Wrong?

CEO could receive & keep a payment, then initiate & approve the account write-off.

CEO could also take a payment & not give it to the operations team to include on the A/R log.

How to Lower Chance of Error/Fraud

- Segregate duties to remove the CEO's ability to either accept payments or to initiate/approve account write-offs
- Complementary controls – Write-offs require another signature before processing, the CEO has no access to record write-offs in either the CRM database nor the accounting system. Use a lock box that would funnel deposits through the bank directly
- Compensating controls – Report of all write-offs that occurred in the CRM database in a month are reviewed by the CEO as well as the operations team

Segregation of Duties

- Receipts process
- Payroll process
- Bank reconciliation process
- Outsourcing accounting services
- Use technology & automation
 - For example, vendor analysis tools

Segregation of Duties – Governance

- Officer receive online view-only access
- Examine each check for an unrecognized payee, unusual endorsement, or other indications of irregularities
- Review wire transfers & the bank accounts to which the transfers were made & ask questions
- Debit blocks for ACH with your banker
- Positive pay services

Segregation of Duties – Governance

- Verify payroll names
- Do not allow controller/bookkeeper to sign checks
- Do not sign checks which have not been completely filled in
- Fidelity insurance
- Review supporting documentation closely looking at names, dates, address, EIN, etc.
- Vendor checks
- Vacations, cross-train
- Variance analysis

Controls Over Bank Reconciliations

- Time frame to be completed
- System access
- Reconciliation to the general ledger
- Who does the reconciliation?
- Approval procedures
- Bank statements
- Wire transfer procedures
- Mail handling; random checks
- Who opens the mail?
- Monitoring processes

Controls Over Payroll & Hiring Process

- Time sheet approval
- Encourage/require a direct deposit requirement for payroll
- Separate bank account for payroll – zero balancing account
- Use third-party administrator/staffing services
- Background & credit checks
- Exit interviews
- Reference checks – beware of internal referrals
- Past work experience checks

Controls Over Inventory

- **Inventory**
 - What do you want to protect?
 - Who do you want to protect it from?
 - How likely is it that you will need to protect it?
 - How bad are the consequences if you fail?
 - How much trouble are you willing to go through in order to try to prevent those?
 - Classification of inventory



Controls Over Disbursements/Contracts

- Set up approved-vendor list
- Invoice approval procedures – delegation of authority
- Petty cash
- Check processing & **don't forget wires**
- Limit employee advances & reimbursements
- Periodic review by an objective person of the list of all vendors receiving fees/checks from the business (a common scheme involves creating a fictitious vendor)

Case Examples

- From a [Washington Post](#) article, a former employee of the Association of American Medical Colleges was able to create fake invoices in the names of legitimate groups that she then approved for payment. When the checks were ready, she had them returned to her, not sent to the vendors. Under that system, a spelling change of just four letters allegedly netted \$3.7 million for her when she purportedly created nearly 200 false invoices in the name of the well-known Brookings Institution policy center, but deposited the checks into accounts she opened for her own “Brookings Institute.” She was later sentenced to 46 months in prison
- A bookkeeper was [sentenced to two years in prison](#) in 2016 for stealing \$800,000 from National Veterans Service Fund in Connecticut from 2009 to 2014, writing checks to herself & then altering the ledgers to make it appear the money went to veterans

Red Flags for Expense Reimbursement & Credit Card Schemes

- Purchases that do not appear to be business related
- Missing original documents supporting expenses
- Altered receipts
- Many receipts from the same vendor
- Submitted receipts are consecutively numbered
- Expenses in round dollar amounts
- Expenses just below receipt submission threshold
- Segmenting expenses across periods to remain below receipt submission threshold
- Cash payment for expenses typically paid with credit card



Improving Expense Reimbursement Processes

Review & update reimbursement policies

Formalize expense reimbursement process

Review work/vacation schedules

Institute use of mileage tracking apps

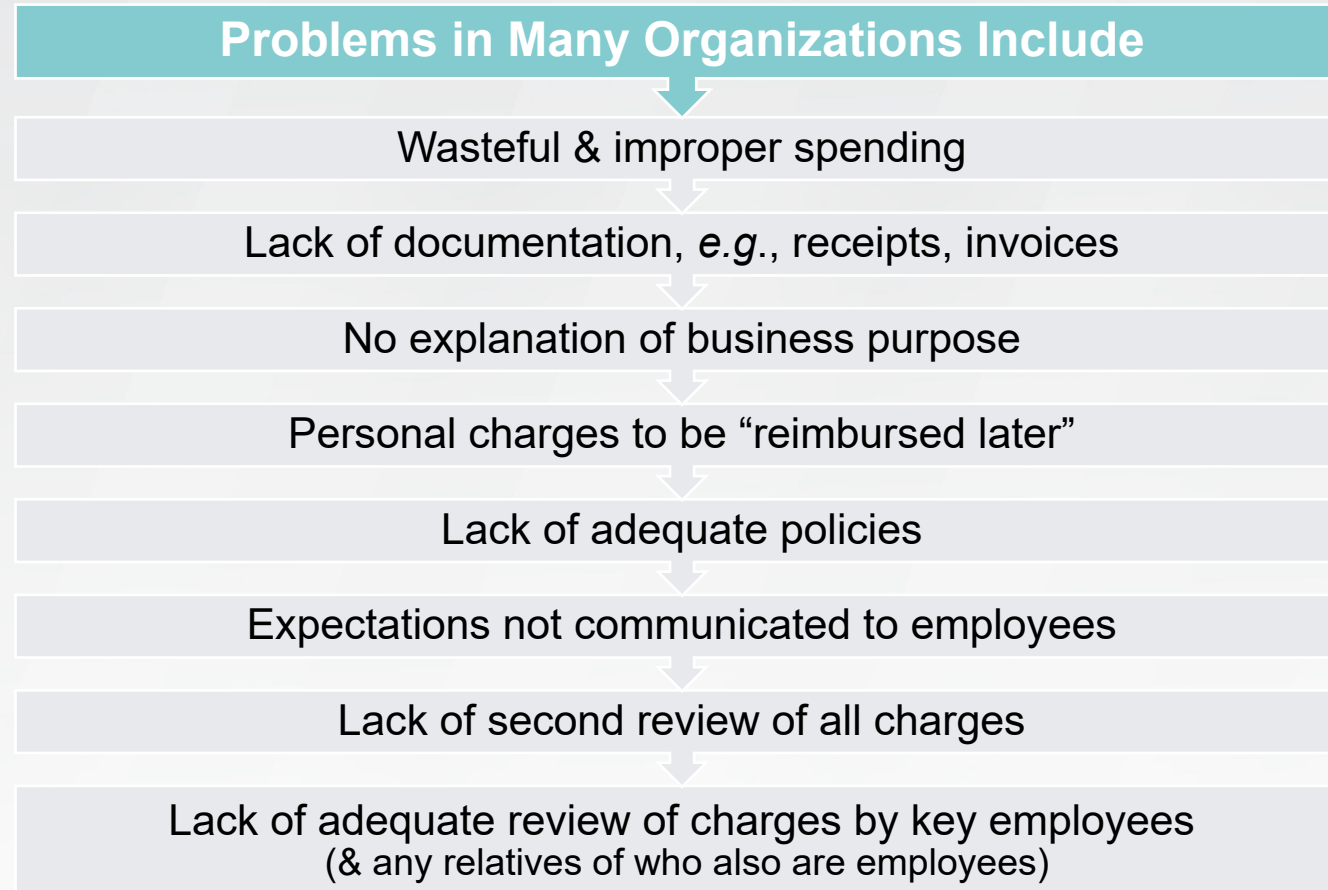


Expense Reimbursement, Credit Cards, P-Card Schemes

- Any scheme in which an employee makes a claim for reimbursement of fictitious or inflated business expenses
 - Employee files fraudulent expense report, claiming personal travel, nonexistent meals, etc., as incurred business expenses
 - Employee purchases personal items & requests reimbursement from the employer



Corporate Credit Cards



Controls Over Credit Card Purchases

- Policies & procedures
 - Employee signature
 - Documented business purpose
 - Number of users
 - Limits
 - Authorization
 - Monitoring
- Review (the right people at the right level)
 - Get supporting documentation for purchases
 - Address possible weakness in the review process
 - Question any potentially inappropriate purchase

Improving Credit Card Processes

Monitor Credit Card Holders & Implement a Two-Step Approval Process

Limit the Use of Personal Credit Cards

Do Not Allow Personal Purchases on Corporate Credit Cards/P-Cards as a Standard Practice

Set Reasonable/Lower Credit Limits

Merchant Code Blocking (P-Cards)

Electronic Analysis of Charges



Example

- An elementary school bookkeeper was accused of cashing \$55,239 worth of checks from the PTA between 2011 & 2015
- The bookkeeper was in charge of purchasing items for the PTA on a district-issued credit card; PTA would then cut checks to reimburse the school account
- The bookkeeper would cash the checks personally & pocket the money

Controls Over Receipts

- Use a lockbox
- Involve a second person in cash receipts processing
- Verify cash logs
- Make bank deposits daily
- Receiving credit card payments/receipts (PayPal)
- Physical movement of cash (wires)

Controls Over Physical Safeguards

- Limiting access (locking cabinets, doors, etc.)
- **Don't forget controls over collections & inventory**
- Fireproof safes
- Reconcile physical inventory of furniture & equipment
- Physical inventory
- Cameras

Example

- A machine shop manager at a General Hospital was sentenced to a year in prison in 2014 for stealing more than \$640,000 in parts, by ordering tools & equipment for his own use as well as by selling leftover brass discs to scrap dealers after they were used in radiation treatments

Cyberthreats

- Malware
 - Phishing
 - Increased remote workforce
 - Mobile Threats
-
- There continues to be targeted ransomware campaigns focused on specific industries like healthcare & government, among others

Best Practices



Review & update policies & procedures annually



Perform walk-through of controls either annually or on a rotating basis to determine reliability



Annual review of user access rights

Questions?

FORV/S

FORVIS is a trademark of FORVIS, LLP, registered with the U.S. Patent and Trademark Office.

Resources



- [Frequently Asked Questions: Internal Controls for Fraud Prevention | FORVIS](#)
- [Fighting Internal Fraud in Accounts Payable & Payroll | FORVIS](#)
- [FORVIS Outsourced Accounting Services](#)
- [FORVIS Nonprofit](#)

FORVIS

Thank you!

forvis.com

The information set forth in this presentation contains the analysis and conclusions of the author(s) based upon his/her/their research and analysis of industry information and legal authorities. Such analysis and conclusions should not be deemed opinions or conclusions by FORVIS or the author(s) as to any individual situation as situations are fact specific. The reader should perform its own analysis and form its own conclusions regarding any specific situation. Further, the author(s) conclusions may be revised without notice with or without changes in industry information and legal authorities. FORVIS has been registered in the U.S. Patent and Trademark Office, which registration is pending.

FORVIS

Assurance / Tax / Consulting