

# Fraud in the Workplace

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## Overview of RSM McGladrey

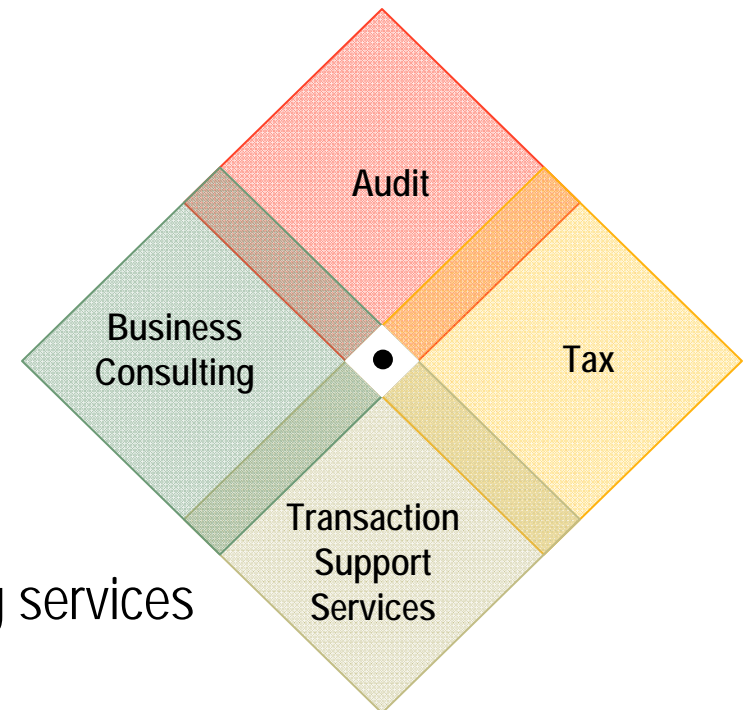
- 5<sup>th</sup> largest accounting, tax and business consulting firm in the U.S.
- 7<sup>th</sup> largest worldwide association of consulting and CPA firms
- Together, with McGladrey & Pullen
  - 2nd largest\* accounting firm in the Phoenix metro area
  - 100 offices
  - 8,000 employees
  - 63 markets nationwide

\* Based on number of cpa's

RSM McGladrey Inc. and McGladrey & Pullen, LLP have an alternative practice structure. Though separate and independent legal entities, the two firms work together to serve clients' business needs. RSM McGladrey, Inc. and McGladrey & Pullen, LLP are member firms of RSM International – an affiliation of separate and independent legal entities.

## Service Offerings

- Audit
- Tax
- Business Consulting
  - Restructuring
  - Litigation support
  - Internal audit/Sarbanes-Oxley consulting services
  - IT
  - Staff Augmentation
  - Financial Systems implementations
- Transaction Support Services



# Restructuring and Litigation Expertise

## SITUATION

- Litigation consulting
- Expert witness
- Due diligence & fraud investigations
- Court appointed examiner
- Workouts and restructuring
- Financial consulting
- SEC and state regulation
- Union wage claims
- Employee pension/insurance
- Contract compliance
- Business Valuations
- Asset valuations/liquidations

## REPRESENTATIVE ISSUES

- Fraudulent conveyance
- Fraud/theft/misappropriation
- Insolvency matters
- Civil/criminal RICO
- Piercing corporate veil
- Damage assessment
- Directors & officers liability
- Contract dispute
- Labor law
- M&A Transactions
- Operations / management
- Business / asset valuation

## **Lois A. Folk, CPA, CFE**

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- Forensic Accounting Practice
  - Fraud Investigations
  - Forensic Accounting
- Complex Litigation Services
  - Litigation Consulting
  - Expert Witness Services
- Bankruptcy / Receivership
  - Asset Liquidation & Trustee Services
- Commercial Litigation
- Directors & Officers Liability

## 2006 ACFE Report to the Nation on Occupational Fraud & Abuse

- Study based upon 1,134 cases of occupational fraud
- Investigated between Jan. 2004 and Jan. 2006

## Occupational Fraud and Abuse Impose Enormous Costs on Organizations

- Median loss = \$159,000
- 25% of fraud cases were greater than \$1.0 Million in losses
- Nine cases caused over \$1.0 Billion in losses

# How Much do U.S. Organizations Lose to Fraud Each Year?

Guess

## U.S. Organizations Lose 5% of Their Annual Revenues to Fraud

When applied to the 2006 U.S. Gross Domestic Product, this 5% would translate to approximately:

**\$652 Billion in fraud losses/year**

What are the Characteristics of the Organizations that are Hardest Hit by Fraud?

Guess

# Which Industries Have the Highest Fraud Losses?

Guess

## Industries with the Highest Median Losses per Fraud Scheme

Government and Retail were among those with the lowest losses

Wholesale Trade	(\$1,000,000)
Construction	(\$500,000)
Manufacturing	(\$413,000)
Government	(\$82,000)
Retail	(\$80,000)

## Small Businesses Continue to Suffer Disproportionate Fraud Losses

- Median loss suffered by organizations with less than 100 employees was \$190,000 per scheme
- This was higher than the median loss in even the largest organizations

## Most Common Frauds For Small Businesses

- Employee writing company checks
- Employee skimming revenue
- Employee processing fraudulent invoices

# Why do Small Businesses Suffer Such High Fraud Losses?

- Poor job at detecting fraud
  - Did not have Hotlines
  - Less than 20% had internal audit departments conducting surprise audits
  - Did not have employees training to detect fraud

## How do Most Small Companies Detect Fraud?

- By Accident – more than any other means

## Who Commits Fraud?

Department	% of Cases
Accounting	30%
Executive	20%
Sales	14%
Customer Service	11%
Finance	4%

## Who Commits Fraud?

- Owners/Executives made up less than 20% of the perpetrators, but accounted for the largest fraud losses

Position	Median Loss
Owner/Executive	\$1,000,000
Manager	\$218,000
Employee	\$78,000

## Perpetrator's Annual Income

As incomes rose, so did fraud losses.

Incomes	Median Loss
Employees in the lowest classification	\$75,000
Employees in the highest classification	\$8,000,000

## Fraudster's Position Within the Organization Influences Extent of Loss

Highest level of authority  
+  
Highest level of income  
=  
Highest total loss

## The Perpetrator — Effect of Tenure

More tenure

=

More trust

=

More opportunity

=

More success committing fraud

## The Perpetrator — Effect of Gender

Gender	Median Loss
Male ( 61% of the cases)	\$250,000
Female (39% of the cases)	\$100,000

Median loss by males committing fraud were more than twice as high as the median loss in fraud committed by women.

## The Perpetrator — Effect of Age

The greater the age, the higher the median loss.

## The Perpetrator — Effect of Education

As education levels rose so did losses from their frauds.

Higher education

=

Higher authority

=

Higher \$ losses

## How is Fraud Committed?

All Occupational Fraud Falls into Three Major Categories

- Asset Misappropriation
- Corruption
- Fraudulent Statements

## Asset Misappropriations

- Scheme involving the theft or misuse of company's assets
  - Fraudulent invoices
  - Payroll fraud
  - Skimming revenues
- 91.5% of all cases in this study
- Median loss of \$150,000

## Corruption

- Scheme where person uses their influence in a business transaction to obtain an unauthorized benefit contrary to their employer
- Examples
  - Accepting or paying a bribe
  - Engaging in a business transaction where there is an undisclosed conflict of interest
- 30.8% of the cases in the study
- Median loss of \$538,000

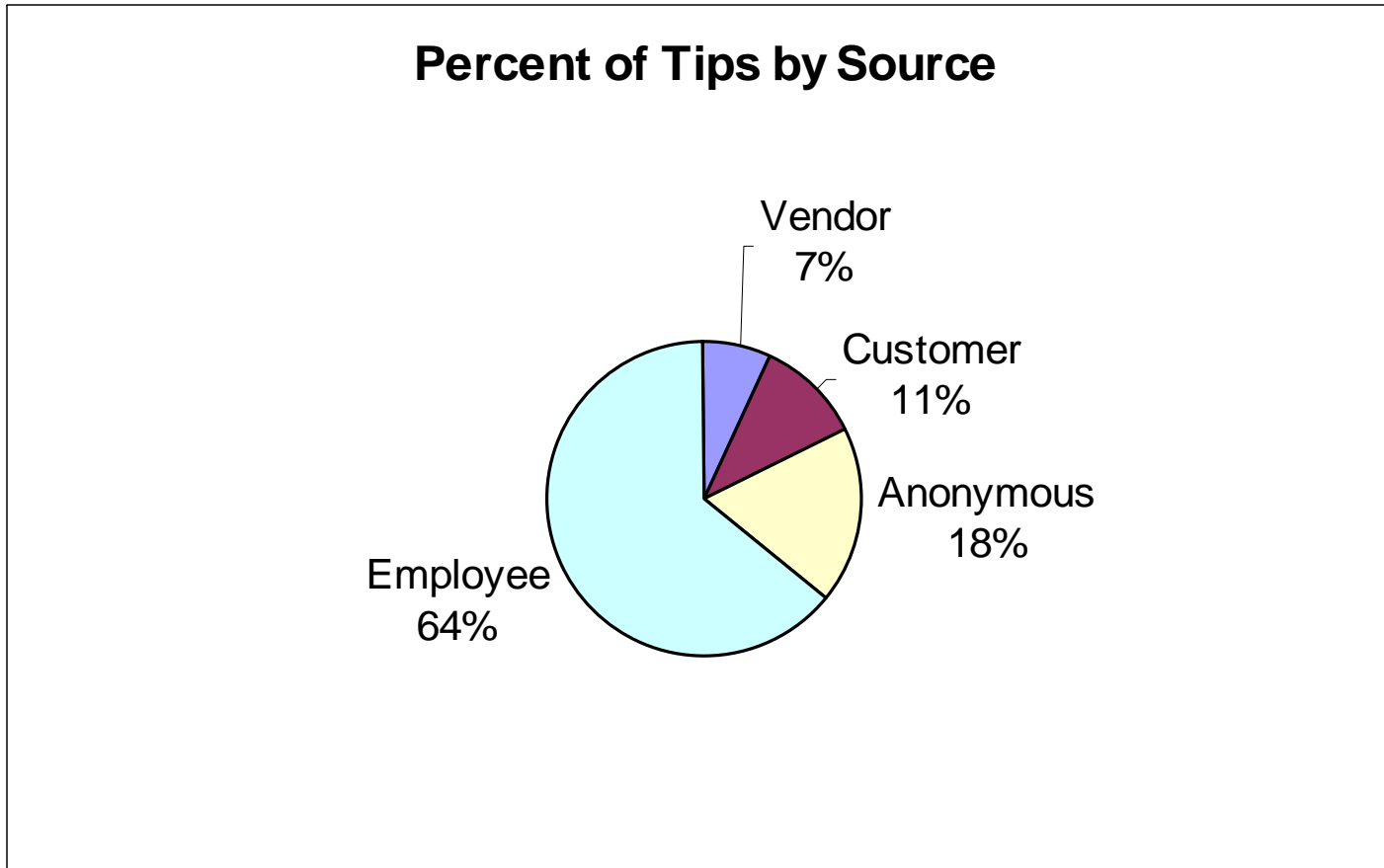
## Fraudulent Statements

- Making an organization appear more or less profitable
- Examples
  - Booking fictitious sales
  - Recording expenses in the wrong period
- 10.6% of the cases in this study
- Median loss of \$2,000,000

## How is Fraud Detected?

Detection Method	% of Cases
Tip	34.2%
Accident	25.4%
Internal Audit	20.2%
Internal Controls	19.2%
External Audit	12.0%
Notified by Police	3.8%

# Who is Responsible for Tips on Fraud?



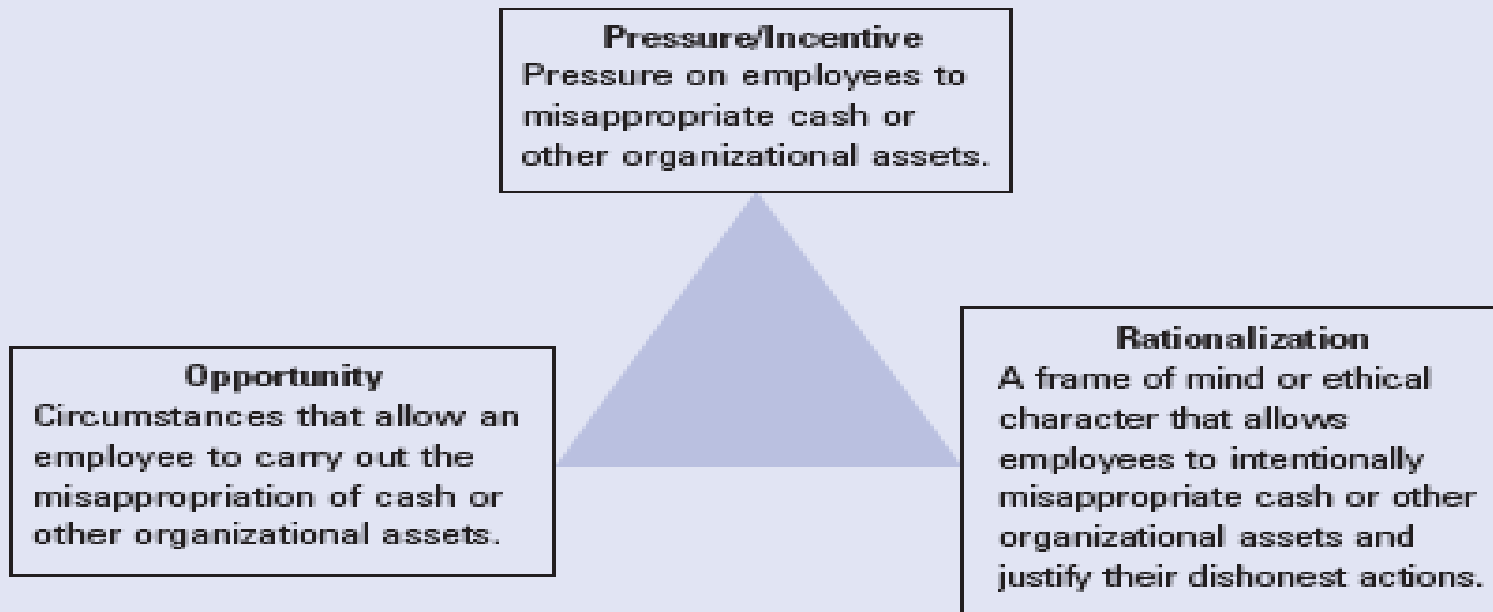
## How to Limit Your Fraud Losses

- Hotlines for Hot Tips
- Internal Audit Departments
  - With surprise audits
  - By conducting anti-fraud training for employees and managers

## Frequency of Anti-Fraud Measures used by Companies

Measure	% of Cases
External Audit	75.4%
Internal Audit	59.0%
Fraud Training	45.9%
Hotline for tips	45.2%
Surprise Audits	29.2%

### The Fraud Triangle



Sources: *Occupational Fraud Abuse*, by Joseph T. Wells, CPA, CFE (Obsidian Publishing Co., 1997);  
*Fraud Examination*, by W. Steve Albrecht (Thomson South-Western Publishing, 2003).

## 2006 ACFE Report to the Nation on Occupational Fraud & Abuse

Free download of the report can be found at  
[www.acfe.com](http://www.acfe.com)