

Fraud Prevention Techniques for Higher Education

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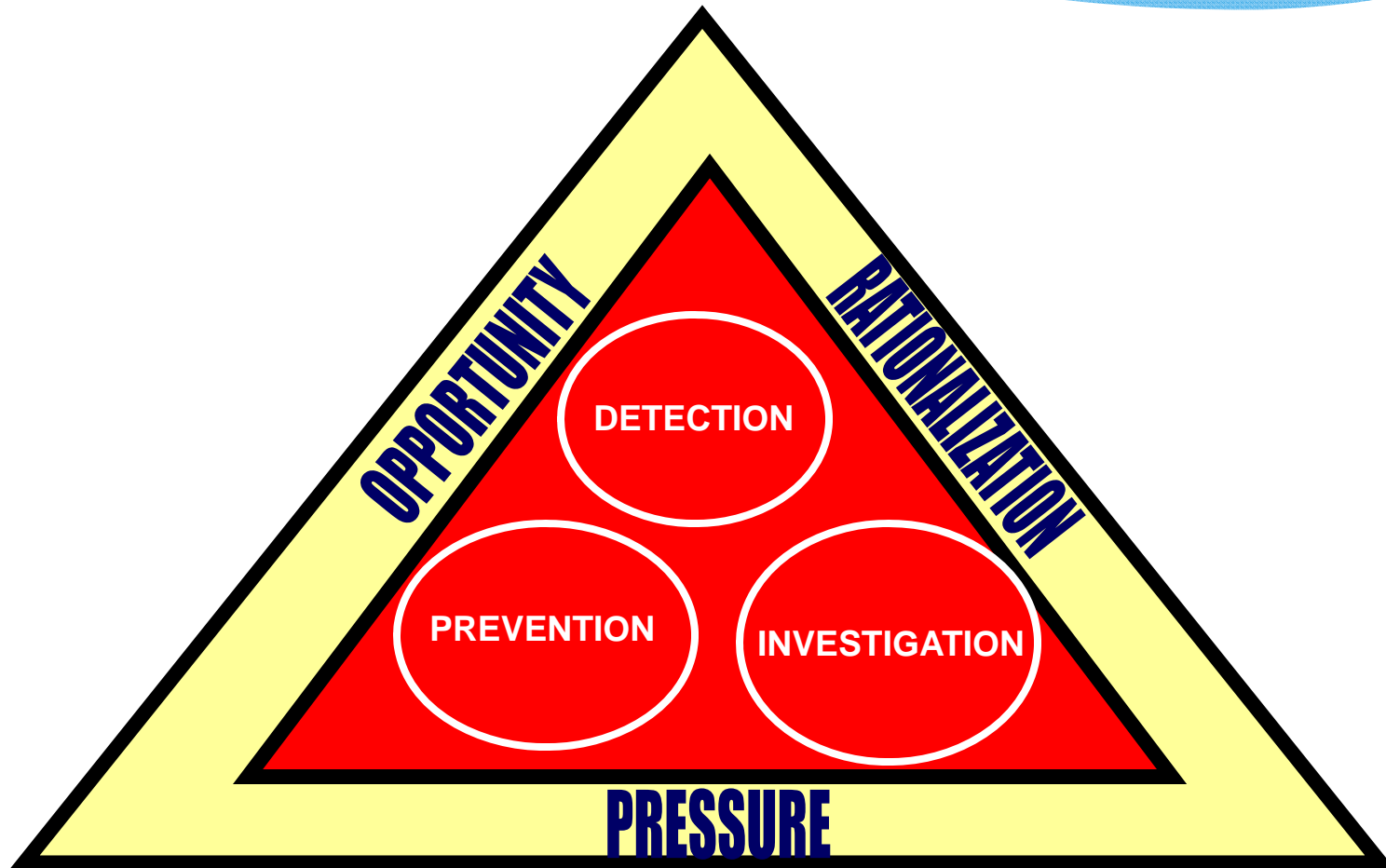
Session Goals

- Identify the different forms of fraud.
- Recognize areas where institutions of higher education are particularly vulnerable to fraud.
- Understand the role of management and those charged with governance in prevention and detection of fraud.
- Learn how to develop and maintain a fraud risk assessment program.

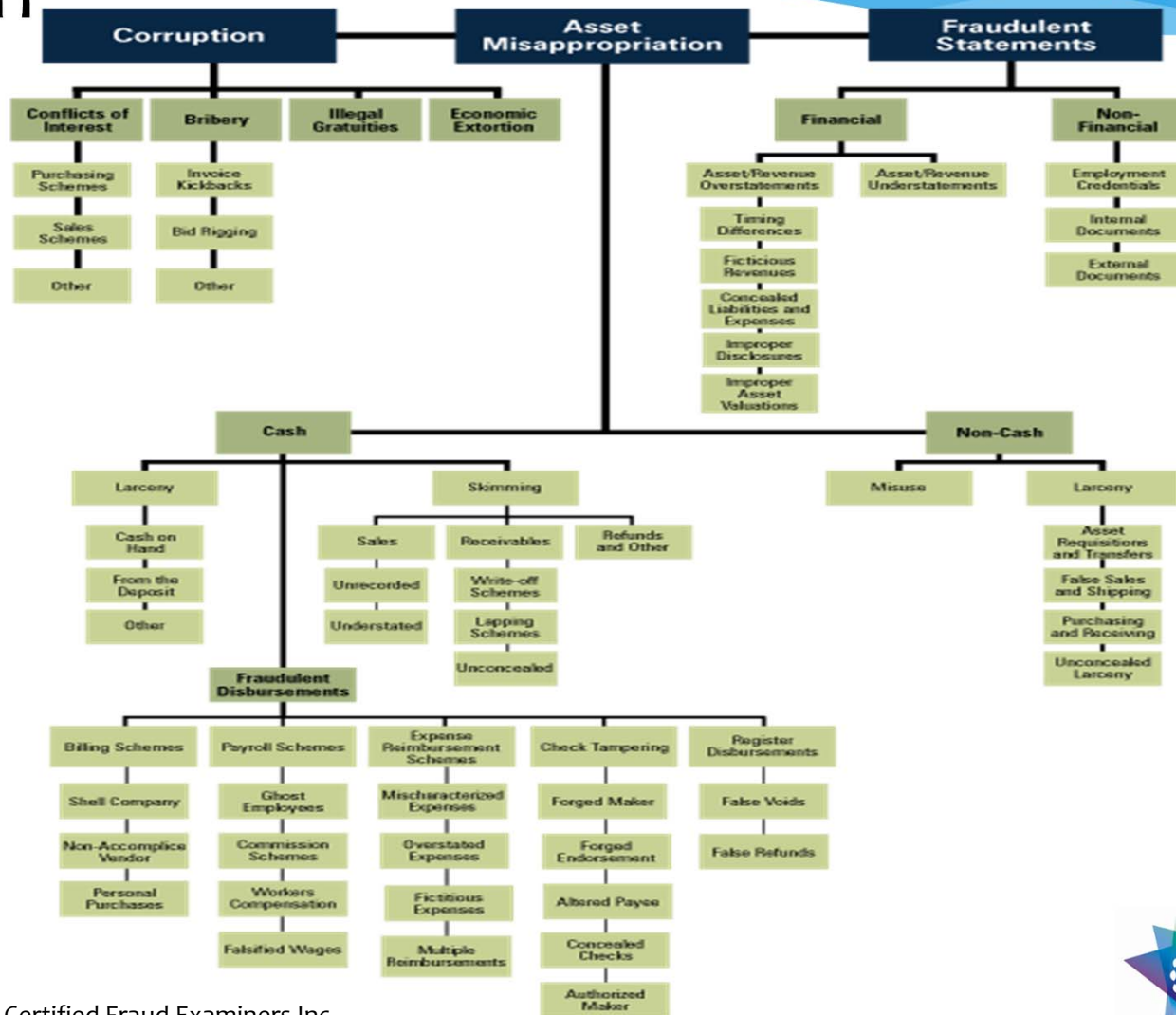
Introduction to Fraud

- Webster's Dictionary: “**Deceit**, trickery; cheating, **intentional** deception to cause a person to **give up property** or some lawful right.”
- AICPA EDP Fraud Review Task Force: “Any **intentional** act, or series of acts, that is designed to **deceive** or mislead others and that has an impact or potential **impact on an organization's financial statements.**”
- The Accountant's Handbook of Fraud & Commercial Crime: “Fraud is criminal **deception** **intended** to **financially benefit the deceiver.**”

Fraud Triangle



Occupational Fraud & Abuse Classification System



Embezzlement

- High Risk Areas for Higher Education
 - Check mailed to the organization
 - Printing expense
 - Postage expense
 - Personnel-related expenses

Examples

➤ A. University Contributions Coordinator

1. University credit card
2. Schedule vs. expenses
3. Billing statement control
4. Discovered after person left the organization

➤ B. Controller in control

1. Copy, Fax, Locked Office, No Secretary
2. Finance Committee
3. Shell Company – acronyms, vendor management, verification
4. Building Improvements – 2 buildings
5. Did not consider year over year total costs
6. Discovered by new Auditor

Actual Cases

➤ A. Bookstore cashier

1. Fraudulent refunds to personal credit card
2. Short time-frame; 2-3 months long
3. Discovered by merchant processor
4. Importance of tracking register control

➤ B. External IT Penetration

1. External “hacker” accessed ACH system, created false payroll file
2. File date was not on normal pay date
3. Controller identified it as abnormal, did not initiate payment
4. Importance of IT security and separate approval of “on-us” transfers

Actual Cases (cont.)

➤ A. External ACH

1. Third party used check to create fraudulent ACH
2. This payment avoids Positive Pay verification
3. Discovered during routine bank reconciliation
4. Instituted debit blocker, where only pre-approved merchants may receive and ACH from college bank account

➤ B. Internal construction fraud

1. Employee created false vendors, created contracts and POs to them for work done by other vendors
2. Fraud was complex, with multiple signatories, fictitious contracts and releases
3. Discovered during request for warranty repair
4. Over \$2.0 million over 3 years

Role of Management and Those Charged with Governance

➤ Role of Management

- Tone at the top
 - Promote awareness of fraud risk management program
- Identification of risks
 - Assess operating and reporting risks periodically
 - Identify and consider the likelihood and significance of such risks
- Prevention and detection of fraud
 - Promote that effective detective controls are in place
 - Take appropriate action for risks identified
 - Establish policies and procedures to mitigate risks
 - Monitor internal controls
 - Develop a process to investigate fraud and take corrective action

Role of Management and Those Charged with Governance (continued)

- Role of Those Charged with Governance
 - Define the role of the Board or Audit Committee as it relates to fraud
 - Set the appropriate tone at the top
 - Maintain oversight of the fraud risk assessment
 - Understand fraud risks at the organization
 - Monitor management's activities related to internal controls and financial reporting
 - Obtain regular reports from management
 - Interact with external auditors, and outside experts as necessary

Fraud Risk Management: *where to begin*

- Fraud risk assessment
- Who is responsible?
- What is involved?
 - Written policies and procedures
 - Summary of procedures and activities already in place to aid in assessment
- Can come in many different formats
 - Single comprehensive document addressing all aspects of fraud risk management
 - Brief outline emphasizing the main characteristics of the fraud risk program
 - Outline within a control framework, referencing separate policies/procedures

Fraud Risk Management: *where to begin* (continued)

- Update on a routinely scheduled basis
 - Needs to evolve with the organization
- Involve appropriate personnel
- Consider relevant fraud schemes and situations
- Link the fraud risks to appropriate controls to prevent/detect

Fraud Risk Assessment: *three step process*

- 1. Identify inherent fraud risks
 - Incentives, pressures, and opportunities
 - Include account-level, financial reporting, and IT specific risks

- 2. Assess likelihood and significance of each fraud risk
 - Historical information
 - Known fraud schemes from other organizations
 - Interviews with staff

- 3. Respond to likely and significant fraud risk
 - Cost-benefit analysis

- **Note: Results of this brainstorming should be documented in some routine format to help assess the information**

Fraud Risk Assessment: documentation

- Example brainstorming documentation matrix included in handouts: “*Fraud Risk Assessment Matrix*”

ABC Organization
Fraud Risk Assessment
Date

Identified Fraud Risk	Likelihood ¹	Significance ²	Actions to Manage Risk/ Control Activities ³	Responsible Parties/Department	Control Effectiveness Assessment ⁴	Remaining Risks?	Fraud Risk Response
Example 1: Inappropriate manual journal entries may be made. There is no independent review of entries made by the Controller.	High	High	Entries made by all personnel except the Controller must be reviewed and entered by another person who would be knowledgeable enough to question the entry were it in appropriate. The CFO reviews the monthly internal financial statements and inquires about unusual fluctuations (detective control).	Finance/Controller/CFO	Not sufficient	Numerous small entries may be made that could go unnoticed from a financial statement level review. Also, entries may be made to make trends look normal and go unnoticed in a financial statement trend analysis.	The CFO will begin reviewing manual entries made by the Controller on a monthly basis.
Example 2: Employee expense reimbursements may be for nonbusiness purposes.	High	Moderate	Employees enter their expenses in their timesheets and are reimbursed on the following payroll. Employees must submit receipts for all expenses \$25 or greater. If an employee does not submit receipts within one month after the expense being entered, the reimbursement will be reversed on his/her next paycheck.	Finance Department / Employees	Sufficient	n/a	n/a
Example 3: Bookstore merchandise may be stolen by personnel.	Moderate	Low	Security cameras are in place in the store and storage room. Inventory is counted periodically and all variances reconciled. There are always at least two people present at the bookstore. Background checks are completed before employees are hired.	Bookstore management/ Human Resources	Sufficient	n/a	n/a

Fraud Risk Assessment: *considering potential fraud*

- Consider the fraud that could occur
 - Who, internal and external, could be involved
 - If the potential fraud is collusive, consider the detective control that would identify the fraud
 - How may the perpetrator exploit a weakness in internal controls?
 - How could a perpetrator circumvent or override controls?
 - How could a perpetrator conceal a fraud?
- Matrix handout includes several examples to help aid in brainstorming

Fraud Risk Management Program

- Documentation of fraud risk governance
 - Who is responsible
 - Organization's commitment and approach
 - Identify organization-wide anti-fraud controls
 - Identify process-level anti-fraud controls or refer to separate policies
- Approval by Board of Directors
- Communication to employees, donors, customers, etc.
- Continuous updates/monitoring
- Reporting Procedures and Whistleblower Protection
 - Documentation should note the process to follow if fraud is detected
 - Consider promoting fraud reporting procedures on intranet or other means

Fraud Risk Prevention: *avoiding future frauds*

- Set the tone at the top
 - Create a culture where fraud is discouraged and reporting encouraged
 - When fraud is discovered, deal decisively with employees involved

- Spend time to think of risk points and how a fraud could be perpetrated
 - With limited resources, what is material?
 - Plan how could a fraud occur, and then devise strategies to militate
 - Similar to emergency planning
 - Ex: Rather than an entire false payroll file (easy to spot) what if hacker inserts a fake employee into EVERY payroll file?

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