Organizational Fraud
Increased Risks in a Downturn Economy

Ron Schwartz, Deloitte Financial Advisory Services LLP
March 24, 2023
Agenda

1. Organizational Fraud Basics
2. Financial Statement Fraud
3. Asset Misappropriation
4. Controls
Organizational Fraud Basics
How Organizational Fraud is Committed

2022 Frequency of Organizational Frauds by Fraud Type

- **Asset Misappropriation**: 86%
- **Corruption**: 50%
- **Financial Statement Fraud**: 9%

Source: Association of Certified Fraud Examiners Report to the Nations 2022
Financial Statement Fraud
Fraud Examples

**Balance Sheet**

1. **Improper Valuation of Assets**
   - Inventory manipulation
   - Accounts receivable schemes
   - Improper capitalization of expenses

2. **Manipulation of Liabilities**
   - Failure to accrue for known liabilities
   - Reserve manipulation

**Income Statement**

1. **Improper Revenue Recognition**

2. **Improper Capitalization of Expenses**

3. **Reserve Manipulation**

4. **Improper Classification of Expenses from Cost of Sales to below Gross Margin**
Case Example:
Financial Statement Fraud (Round Trip Transaction)
## Financial Statement Fraud

### Split Purchase Orders

<table>
<thead>
<tr>
<th>Supplier Name</th>
<th>PO Creation Date</th>
<th>PO Amount $</th>
<th>PO Number</th>
<th>PO Item Description</th>
<th>Requisition Number</th>
<th>Req Approver</th>
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<tbody>
<tr>
<td>TechCo</td>
<td>01-Jun-2016</td>
<td>$18,500</td>
<td>5099002267</td>
<td>Outsourced services</td>
<td>7884</td>
<td>A.G.</td>
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<td>TechCo</td>
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<td>$16,000</td>
<td>5099002268</td>
<td>Z bank Legal reporting</td>
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<td>A.G.</td>
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</tbody>
</table>
Polling Question

01

What employee pressures, that may lead to fraud, are you most concerned about?

A. Pressure to meet budget/forecast
B. Employee living beyond means/financial pressure
C. Employee not feeling appreciated or fairly compensated
D. Other
Asset Misappropriation
Asset Misappropriation

**Asset misappropriation** fraud involves third parties or employees who abuse their position to steal from an organization through fraudulent activity such as:

- Theft of cash
- Diverting checks or wire advices
- Procurement fraud
- T&E fraud
- Payroll/overtime fraud
- Theft of inventory or other assets
Case Example: Asset Misappropriation (Purchase Card Abuse)
Asset Misappropriation: Purchase Cards

Using corporate p-cards for personal gain:

❖ One of the more commonly occurring employee frauds

Fraud tests can help identify the following:

- Goods and services acquired from suspect vendor codes
- Cards being used on weekends or while the employee is on vacation
- Fuel purchases in large quantities
- Employees with similar job functions having widely varying expenses
Asset Misappropriation

Altering of Receipts
Asset Misappropriation

Altering of Receipts

<table>
<thead>
<tr>
<th>Date</th>
<th>Order_ID</th>
<th>DeptNo</th>
<th>ClassName</th>
<th>SkuDesc</th>
<th>Account Amount</th>
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</thead>
<tbody>
<tr>
<td>8/18/2015</td>
<td>2015343217807230000000</td>
<td>76</td>
<td>PPD GIFT CARDS</td>
<td>Gift Card, Visa, Scroll, $200</td>
<td>$ 827.80</td>
</tr>
</tbody>
</table>

ITEM DESCRIPTION: Item #: 295223 - HP 53A, Black Original Toner Cartridge (Q7553A), 2PK

Your Price: $206.95 / each

QTY: 4

SUBTOTAL: $827.80
TAX: 0.00
TOTAL: $827.80
Case Example:
Asset Misappropriation (Vendor Payments)
## Asset Misappropriation

Master Vendor File Fraudulently Altered

<table>
<thead>
<tr>
<th>[VENDOR]</th>
<th>[TRANS_DATE]</th>
<th>[VENDOR_SNAME]</th>
<th>CHANGED FIELD</th>
<th>[BEFORE_IMAGE]</th>
<th>[AFTER_IMAGE]</th>
</tr>
</thead>
<tbody>
<tr>
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<td>7/28/2014</td>
<td>REALTY LLC</td>
<td>Vendor Name</td>
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</tr>
<tr>
<td>37858</td>
<td>7/28/2014</td>
<td>REALTY LLC</td>
<td>Bank Account Number</td>
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<tr>
<td>37858</td>
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<td>REALTY LLC</td>
<td></td>
<td><a href="mailto:XXX@realtycompany.net">XXX@realtycompany.net</a></td>
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<td><a href="mailto:ap.XXXrealty@gmail.com">ap.XXXrealty@gmail.com</a></td>
<td></td>
<td><a href="mailto:XXX@realtycompany.net">XXX@realtycompany.net</a></td>
</tr>
</tbody>
</table>
Polling Question

02

What type of asset misappropriation scheme(s) are you most concerned about?

<table>
<thead>
<tr>
<th>Option</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>A. Theft of cash</td>
<td></td>
</tr>
<tr>
<td>B. Procurement fraud</td>
<td></td>
</tr>
<tr>
<td>C. T&amp;E or P-card fraud</td>
<td></td>
</tr>
<tr>
<td>D. Payroll/overtime fraud</td>
<td></td>
</tr>
<tr>
<td>E. Theft of inventory/other assets</td>
<td></td>
</tr>
<tr>
<td>F. Other</td>
<td></td>
</tr>
</tbody>
</table>
Controls
Common Anti-fraud Controls

2022 Anti-Fraud Controls

- External audit of F/S: 82%
- Code of conduct: 82%
- Internal audit department: 77%
- Management certification of F/S: 74%
- External audit of ICOFR: 71%
- Hotline: 70%
- Management review: 69%
- Independent audit committee: 67%
- Fraud training for employees: 61%
- Anti-fraud policy: 60%
- Fraud training for managers/executives: 59%
- Employee support programs: 56%
- Dedicated fraud department, function, or team: 48%
- Formal fraud risk assessments: 46%
- Proactive data monitoring/analysis: 45%
- Surprise audits: 42%
- Job rotation/mandatory vacation: 25%
- Rewards for whistleblowers: 15%
- Percent of cases

Source: Association of Certified Fraud Examiners Report to the Nations 2022
### Initial Detection of Organizational Frauds

#### 2022 Initial Detection of Organizational Frauds

- **Tip**: 42%
- **Internal Audit**: 16%
- **Management Review**: 12%
- **Document Examination**: 6%
- **Account Reconciliation**: 5%
- **By Accident**: 5%
- **Automated Transaction/Data Monitoring**: 4%
- **External Audit**: 4%
- **Surveillance/Monitoring**: 3%
- **Notified by Law Enforcement**: 2%
- **Confession**: 1%
- **Other**: 1%

**Source:** Association of Certified Fraud Examiners Report to the Nations 2022
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