

Is There Still Fraud?



**Based on the Association of Certified Fraud Examiners (ACFE)
2008 Report to the Nation on Occupational Fraud & Abuse**

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As I recently looked back over my rather eclectic 30 plus year career which includes roles in a wide variety of industries it was surprising to recall the number of cases of fraud I encountered, uncovered or investigated. These were not scandalous events of the scope and scale that we have recently seen that lead to SOX. But they were events that none the less negatively impacted the organizations where they occurred and the people within that organization ... never for the short term better ... but often for the long term good. So my experience leads me to encourage you to be alert to the fact that fraud does occur and will continue to occur. It is going on all around us, from simple pilferage to personal use of company assets to more complex schemes involving collusion and diversion of company assets. It is up to each organization to be vigilant and diligent in preventing fraud. Just when you think it won't happen to you ... it could.

Every two years the Association of Certified Fraud Examiners (ACFE) conducts a survey among its members on occupational fraud that he or she had investigated during the preceding two-year period. The most recent survey covered the period from January 2006 to February 2008. It shows that fraud occurs in all types of organizations (e.g., approximately 40% occurred in private companies, 28% in public companies, 18% in government and 14% in not-for-profit). Here are some facts from this most recent study, which contained over 950 cases.

1. **The median estimate is that a typical U.S. organization loses 7% of its annual revenue to fraud.** This means that an organization with revenue of \$500 million will lose \$35 million to fraud each year. Fraud losses come directly off the bottom-line so you need to think about how much in additional sales your company would need to get back that 7%.
2. **In the ACFE study, over 25% of the frauds investigated by its members involved losses of \$1 million or more.** More than 63% involved a loss of at least \$100,000. These are only the frauds that were identified and investigated – what else was going on in these organizations that was not detected?
3. **Asset misappropriation (theft or misuse of an organization's assets) is the most common type of occupational fraud and abuse representing approximately 90% of the study's reported cases.**
4. **Corruption, where an individual uses his/her influence in a business transaction to obtain a benefit for themselves contrary to that person's duty to his/her employer, represented just over 27%, and fraudulent financial statements represented 10%.**
5. **Within a given occupational fraud scheme, the perpetrator(s) will often engage in several different forms of illegal conduct.** In fact, over 25% of all the frauds in the study involved some form of corruption that involved asset misappropriation. Keep this in mind when investigating a known fraud – look for additional schemes that may also be underway. A typical example is an employee who accepts kickbacks or other bribes from a vendor in order to process invoices for fictitious goods and services.

6. **In this study, the banking and financial services industry has the highest number of cases at 132 (15%) and a median loss of \$250,000.** While the telecommunications industry had only 16 cases (2%) the median loss (\$800,000) was higher.
7. **The single biggest method of fraud detection in a company is through tips, or complaints, accounting for over 45% of the frauds detected;** 42% of million-dollar frauds were uncovered through a tip. Of the cases in the study where fraud was detected by a tip, 31% were received via a hotline or other formal reporting mechanism. It is important to note that tip “hotlines” should be open to non-employees including customers and vendors, and the existence of the hotline can be communicated to them via purchase orders, invoices, requests for proposals, etc.
8. **For all companies with an anonymous fraud hotline in place, median loss was reduced by 60%.** An anonymous tip line is required by the Sarbanes-Oxley Act and must be monitored by the Audit Committee of the Board of Directors. Naturally, this monitoring needs to be robust to be effective.
9. **Internal audits plus internal controls accounted for over 55% of frauds detected.** Surprise audits and job rotations/mandatory vacations were the least commonly used anti-fraud control among those employed.
10. **Owners and executives were the least likely perpetrators of occupational fraud, but when they were the principal perpetrators the median loss was \$834,000.** This is over five times greater than the losses caused by managers and more than eleven times higher than the median loss caused by employees. Perpetrators with long tenure at an organization, as well as older perpetrators also increased the size of the loss. Education level had the same effect – employees with a postgraduate degree generated the highest median loss, more than double the loss of perpetrators with only a bachelor degree.
11. **Fraud schemes by perpetrators employed in the legal department resulted in the greatest median loss of \$1,100,000;** fraud schemes by executives and upper level-management employees were second with a median loss of \$853,000.; and third, the purchasing department had median losses at \$600,000.
12. **Nearly two-thirds of fraud schemes covered in the study, where done by perpetrators acting alone, where the median loss was \$115,000.** However, in schemes that involved at least two or more, the resulting median loss was \$500,000.
13. **More than half of the victim organizations conducted a background check on employment history and 40% ran a criminal background check on the employee prior to hiring. Yet this practice has little impact on the overall incidence of fraud as fully 87% of perpetrators in this study had never been charged or convicted of a crime.** To be sure, background checks may weed out the employee candidate with the goal of defrauding the employer, but they will not catch the typical occasional fraudster who has no prior criminal record. Many employers are reluctant to share negative information about past employees for fear of potential legal liability.



For additional information, or to download the *2008 Report to the Nation on Occupational Fraud & Abuse from ACFE*, use this link: <http://www.acfe.com/documents/2008-rttn.pdf>