

The BakerTilly logo, featuring a stylized 'G' icon, is followed by the text 'bakertilly'. To its right is a small 'x' symbol, followed by the Henry+Horne logo, which consists of a grid of squares, and the text 'Henry+Horne'.

bakertilly × Henry+Horne

Government Fraud

**Case Studies with
Situational Ethics**





WHO WE ARE

About Us

EFFECTIVE DECEMBER 1, 2022

We are a leading advisory CPA firm, and we forge the way with a coast-to-coast and global advantage

Our 6,500+ professionals and 500+ partners help us drive businesses forward

Today's Topic

- Fraud Update
 - Report to the Nations 2022
 - Key findings
 - Detection
 - Tips for fraud prevention
- Case Studies
- Ways to prevent fraud



Report to the Nations

- The information gathered for this presentation can be found at www.acfe.com.
- You can also obtain a copy of the Association of Certified Fraud Examiners 2022 Report to the Nations at this website.



Report to the Nations

- **12** Edition of the largest global study on Fraud
- **2,110** real cases cited
- **23** Major industries, including government

What is Occupational Fraud

- Occupational fraud is a form of fraud where an employee, manager, or executive uses their position to carry out fraudulent activities within an organization.
- Local governments are not immune to occupational fraud, and in fact, they are more vulnerable to it due to:
 - Their decentralized nature,
 - High degree of autonomy, and
 - Limited resources for fraud prevention.

Report to the Nations

- The main purpose
 - **Methods** by which fraud is committed
 - **Means** by which it's detected
 - **Characteristics of organizations** that are victimized
 - **Characteristics of people** committing fraud
 - **Results** of these cases

Key Findings - 2022

2,110 cases
of
occupational
fraud
(2020 was
2,504)

\$3.6 billion
in total
losses
(2020 was
\$3.6B)

12 Months to
Detect on
average
(2020 was
16 months)

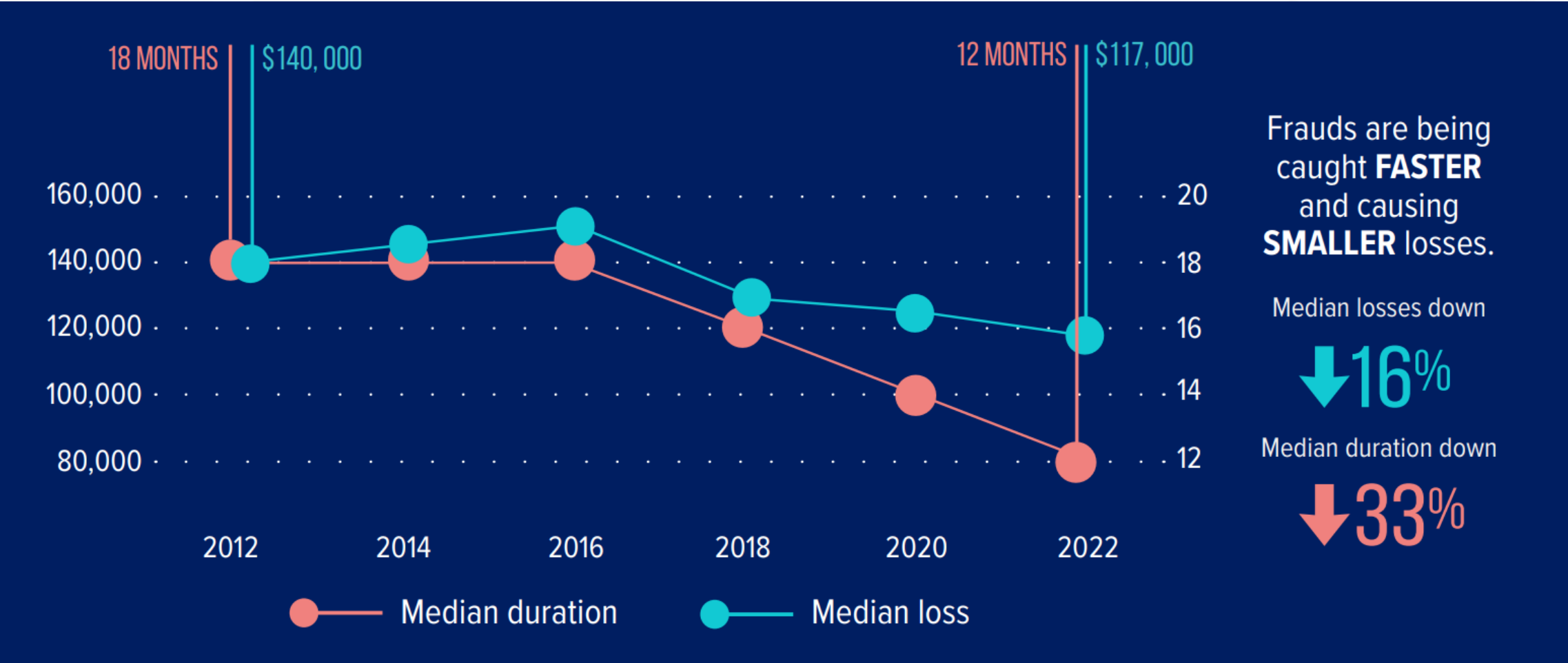
Across 133
countries

Corruption
was
common
across all
regions

Key Findings

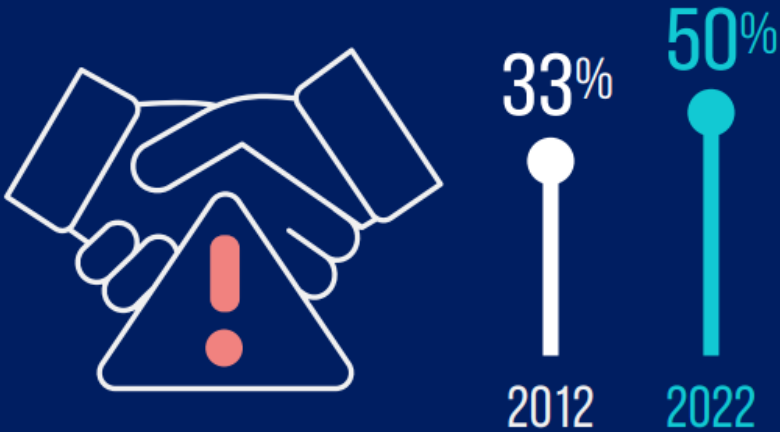
- Estimate of 5% of revenue lost each year
 - Median loss per case is \$117,000 (2020 was \$125k)
 - Average loss per case is \$1,783,000 (2020 was \$1,509,000)
- Corruption was the most common scheme
 - 86% of cases with median loss of \$100,000
- Financial statement fraud is the least common but the most costly
 - 9% of cases with median loss of \$593,000

10 Year Fraud Trends Globally

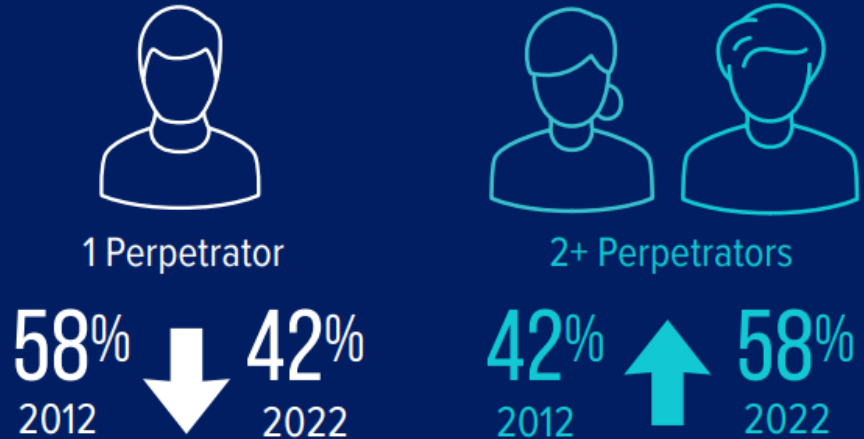


10 Year Fraud Trends Globally

The percentage of cases involving **CORRUPTION** is on the **RISE**



FRAUDSTERS are **COLLABORATING MORE**








10 Year Fraud Trends Globally

Implementation rates for 17 of the 18 analyzed anti-fraud controls have **INCREASED OVER THE LAST DECADE**



These five have **INCREASED** the most:

	2012	2022	Increase
 Hotline	54%	70%	16%
 Fraud training for employees	47%	61%	14%
 Anti-fraud policy	47%	60%	13%
 Fraud training for managers/ executives	47%	59%	12%
 Formal fraud risk assessments	36%	46%	11%



Popular ways to Conceal Fraud



12% of cases did not involve any attempts to conceal the fraud

EVIDENCE



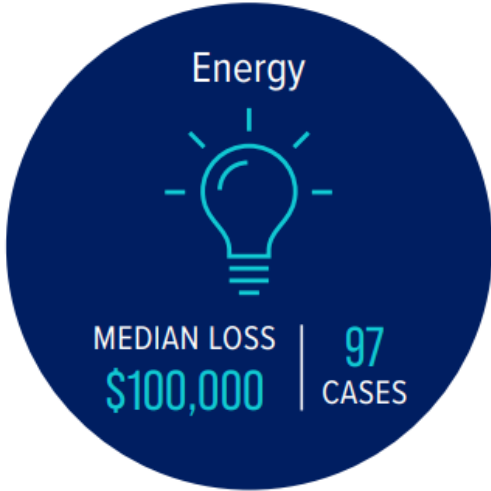
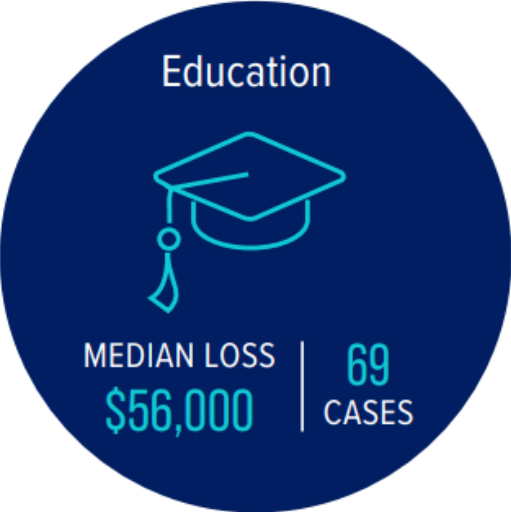
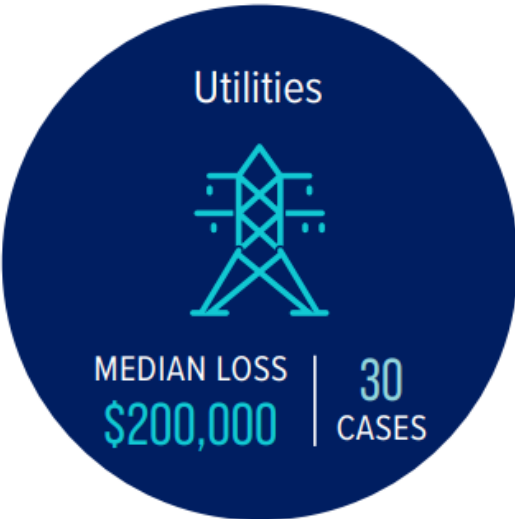
57% OF CASES involved the creation of fraudulent evidence



38% OF CASES involved concealment methods affecting BOTH physical and electronic evidence.



What about Government?



What about Government?

TOP 5 MEDIAN LOSSES BY INDUSTRY



ORGANIZATIONS WITH THE **FEWEST EMPLOYEES** HAD THE HIGHEST MEDIAN LOSS (\$150,000)

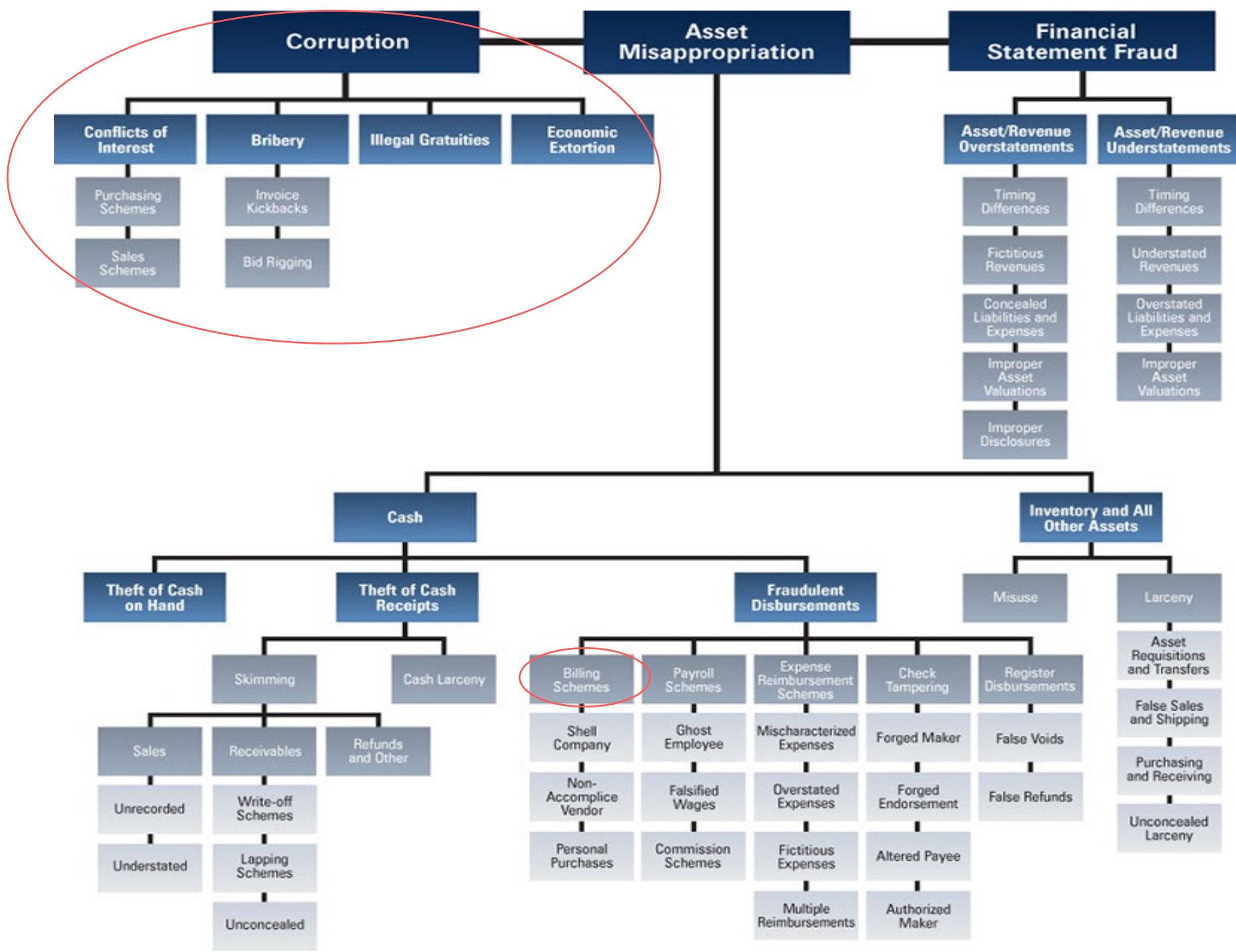


What about Government?

INDUSTRY	Cases	Billing	Cash larceny	Cash on hand	Check and payment tampering	Corruption	Expense reimbursements	Financial statement fraud	Noncash	Payroll	Register disbursements	Skimming
Banking and financial services	351	10%	11%	14%	14%	46%	8%	11%	11%	4%	2%	10%
Government and public administration	198	21%	8%	7%	9%	57%	12%	8%	16%	16%	3%	8%
Manufacturing	194	26%	5%	9%	7%	59%	10%	12%	23%	10%	4%	8%
Health care	130	20%	6%	8%	8%	50%	11%	9%	18%	12%	2%	9%
Energy	97	24%	9%	6%	8%	64%	16%	8%	13%	6%	3%	2%
Retail	91	19%	10%	9%	9%	43%	7%	4%	24%	5%	7%	14%
Insurance	88	15%	9%	8%	10%	40%	9%	5%	8%	10%	2%	11%
Technology	84	21%	6%	10%	6%	54%	14%	8%	30%	5%	1%	1%
Transportation and warehousing	82	20%	9%	15%	4%	59%	11%	7%	22%	9%	4%	11%
Construction	78	24%	8%	10%	14%	56%	17%	18%	24%	24%	3%	9%
Education	69	26%	9%	12%	12%	49%	12%	12%	19%	14%	4%	12%
Information	60	15%	5%	5%	8%	58%	12%	12%	33%	7%	2%	7%
Food service and hospitality	52	19%	10%	21%	17%	54%	13%	13%	29%	19%	10%	17%

- Billing Schemes
- Corruption





Example of Billing Scheme

- Fayette County Water Fund
 - <https://www.fox5atlanta.com/video/1152300>



Example of Corruption Scheme

- City of Atlanta Water Department Scheme
 - <https://www.fox5atlanta.com/video/1185842>



Starbucks Gift Card Question

What are the three
cornerstones of Fraud

Pressure

Opportunity

Rationalization



The Seven Signs of Ethical Collapse

- ASU Professor Marianne Jennings, J.D.
 1. Pressure to maintain the numbers
 2. Fear and silence
 3. Bigger-than-life CEO or Director
 4. Weak Board of Directors (City Council)
 5. Conflict (Stock options, related parties, etc.)
 6. Innovation like no other
 7. Goodness in some areas atones for evil in other areas

The Seven Signs of Ethical Collapse

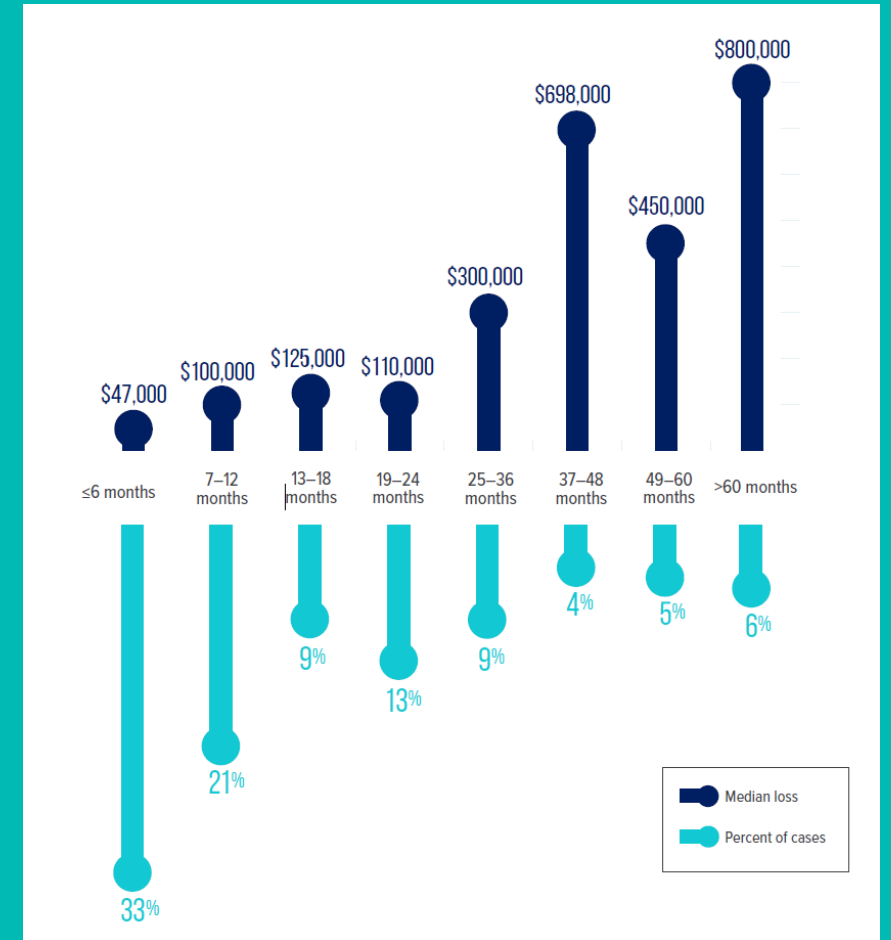
Understanding What Causes Moral
Meltdowns in Organizations



Marianne Jennings, J.D.

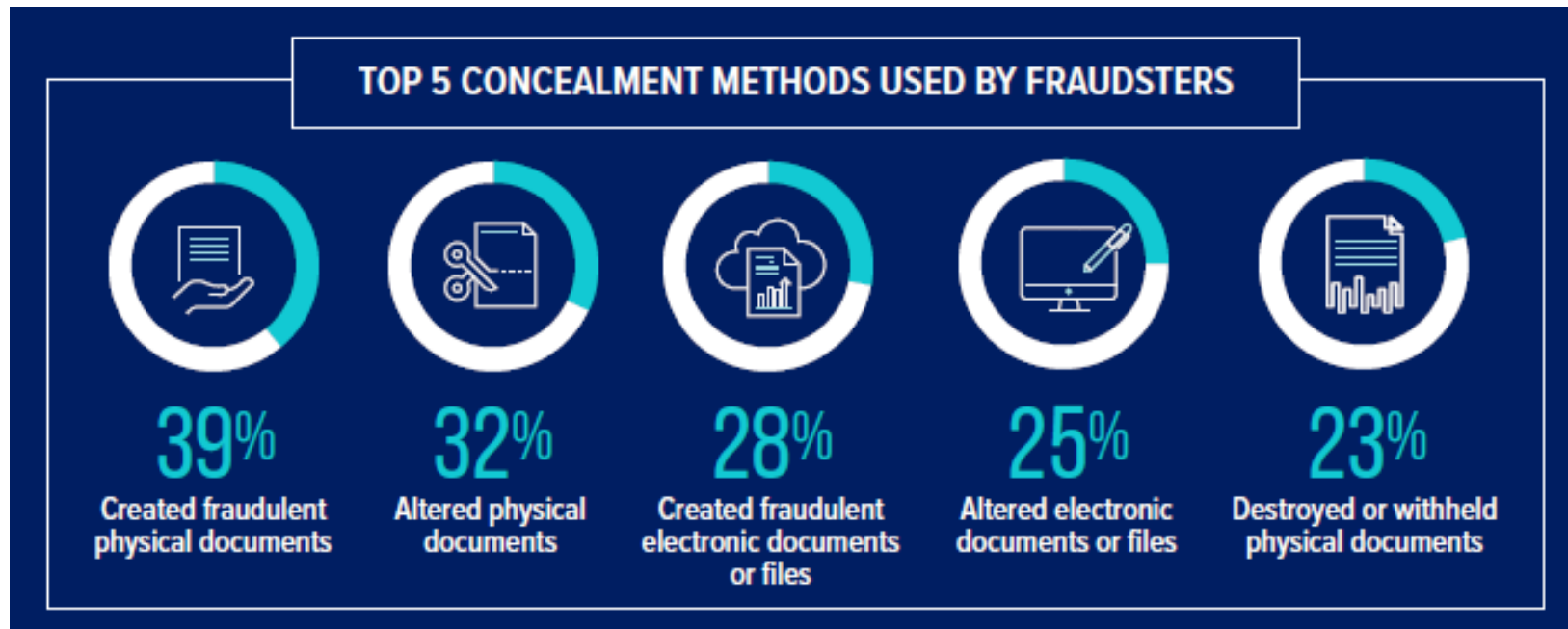
How long do frauds last?

- How does the duration of a fraud relate to median loss?
- If they collude, the loss is higher in a shorter period of time.



Key Findings

How are frauds concealed?



Key Findings

- Who has access to receiving invoices?
 - Can they alter the PDF?
 - Do they have access to creating new vendors?
- If Executives have the most control, who is above them?
 - Does the board or council monitor the high-level transactions?



How?

- Fraudulent Documents
 - Fake PDF, fake checks
- Altered documents
 - Changed the PDF, changed the check
- Altered electronic document
 - PDF edit, accessible electronic signature
- Created fraudulent files
 - Fictitious vendor, invoice, purchase order



Case Study #1

- Metro Waste Authority Theft
 - [Video](#)



Case Study #1



- Metro Waste Authority - Shell Company
- Agency Director of Operations for the Metro Waste Authority, Des Moines, IA - **Stole \$1,800,000**
 - Authority Director created a shell company as the sole owner, blamed it on his wife.
 - Much of what the shell company charged to the Authority were services that the Authority's Director was providing to the Authority as apart of their job description. (Essentially, they were being paid twice for the same job.)



Case Study #1

- Metro Waste Authority - Shell Company
- Purchasing Controls
 - The Authority never sought bids on the “work” being claimed as expenses by the shell company
 - No segregation of duties, small government dilemma
 - No vendor checks
 - Checks were picked up at the office instead of mailed
 - No conflict-of-interest forms signed



Case Study #1

- Metro Waste Authority - Shell Company
- Discovered by the Executive Director
- Investigated by the State auditor
- Cause – Segregation of Duties, Lack of Procurement and Vendor Checks
 - Arizona Corporation Commission
 - <https://www.azcc.gov/>
 - County Assessor
 - <https://mcassessor.maricopa.gov/>



Case Study #1



- Metro Waste Authority
 - Shell Company
 - Charged on 10 counts of mail fraud
 - Pleaded down to 1 count
 - Faced up to 20 years in prison
 - Was actually sentenced to 57 Months or 4.75 years

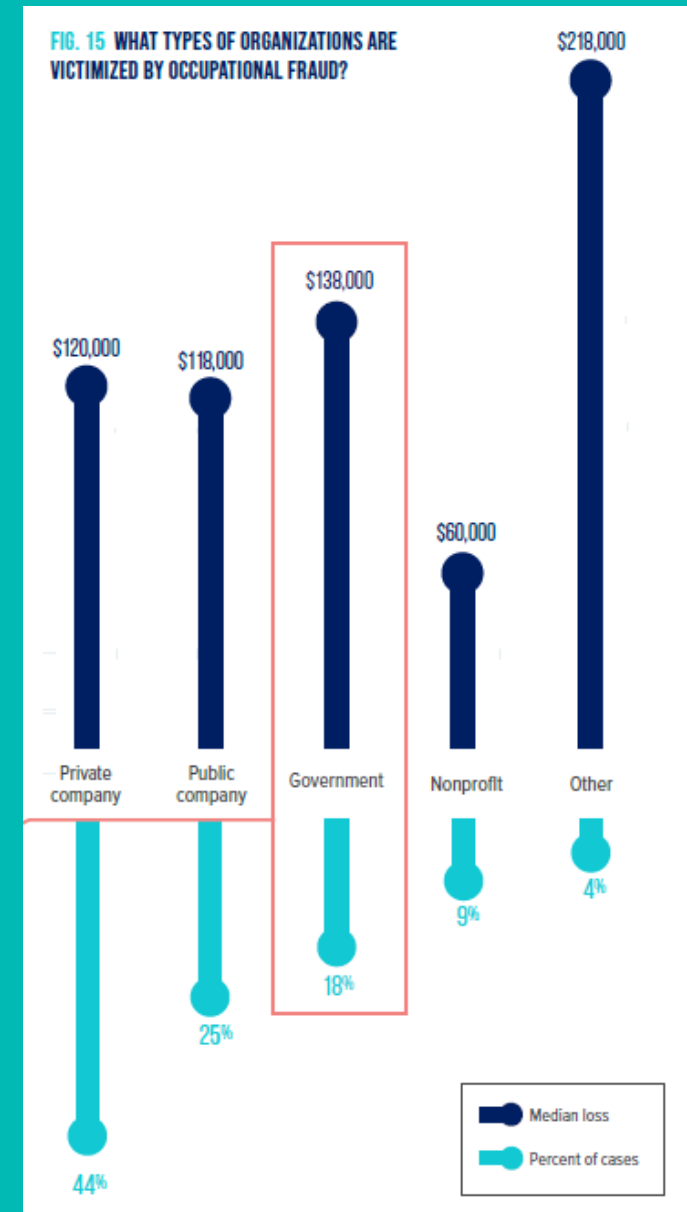
Candy Question

How could procurement have help Metro Waste Authority?

- a) Help determine market prices for boxes
- b) Aid in paying a fair price
- c) Reduce the possibility of shell companies
- d) All of the above

Which organizations are being targeted?

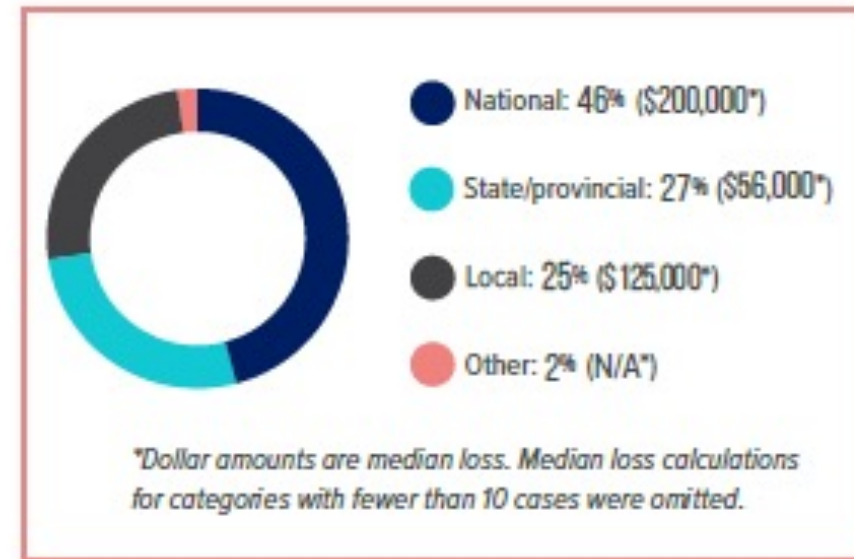
- Private companies
- Governments have one of the highest median losses



Which organizations are being targeted?

- State Governments at 27%
- National level have more staff, higher budgets
- Local have less staff and resources

FIG. 16 WHAT LEVELS OF GOVERNMENT ARE VICTIMIZED BY OCCUPATIONAL FRAUD?



Candy Question

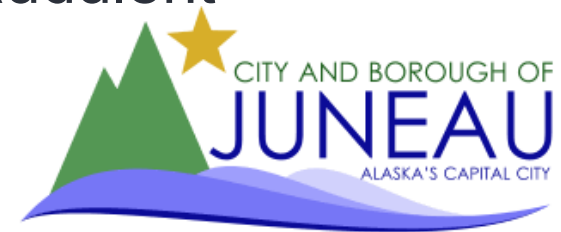
Government is one of the highest at which of the following?

- a) Highest median losses to fraud
- b) Highest number of cases
- c) Highest percent of skimming schemes
- d) Highest percent of asset misappropriation schemes



Case Study #2

- An outside scammer (not a governmental employee) Frauded the City of Juneau, AK via email – **Stole \$329,630**
 - Insurance recovered \$250,000, policy limit on fraud, the City is out the remaining \$80,000
 - Scammer posed as an employee of a legitimate construction vendor and had the City procurement personnel update their direct deposit information
 - Legitimate vendor billed the City, the direct deposit hit the fraudulent account
 - Perpetrators not yet found



Case Study #2

- Discovered –
 - The real vendor called to notify the City that no payments were being received after the City disbursed funds to the fraudulent account.
- Cause –
 - Increased phishing scams, lack of knowledgeable personnel
- Phishing Scams
 - [Video](#)



Starbucks Gift Card Question

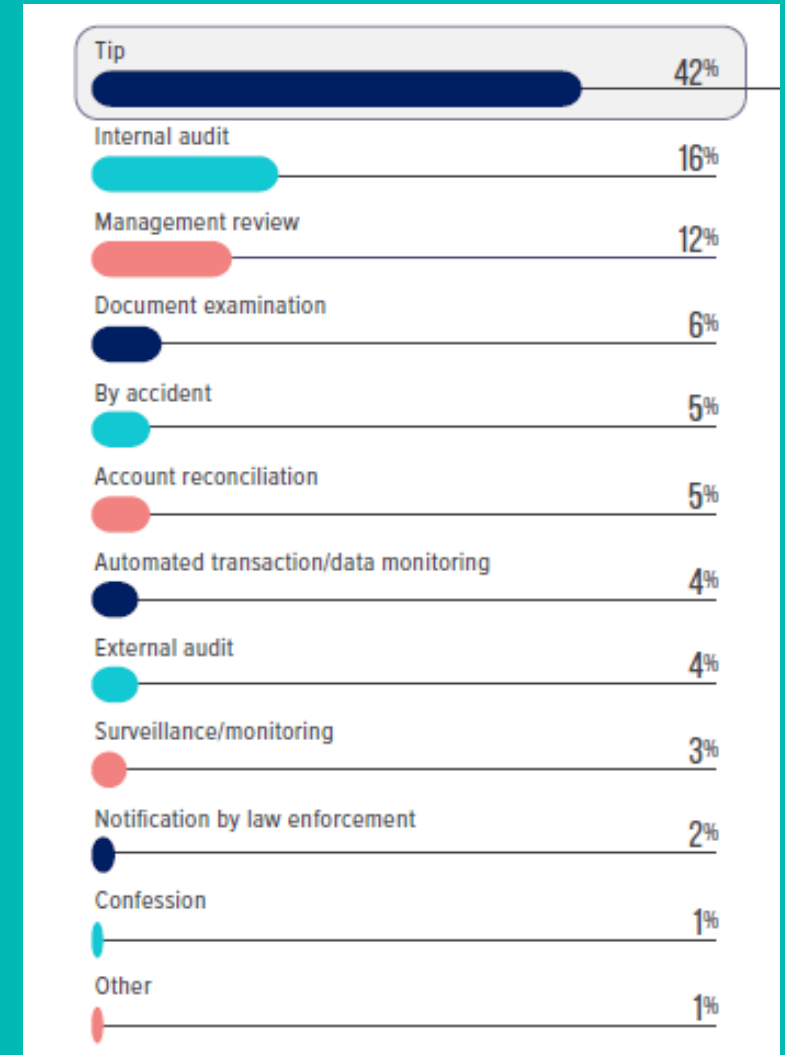
In this situation, what is the best ethical way to combat phishing scams?

- a) Reply to the email asking a specific question only that vendor should know.
- b) Mail a letter to the vendor's address detailing the account changes.
- c) Make a separate phone call to the vendor's phone number on record to verify the changes.
- d) Both b and c



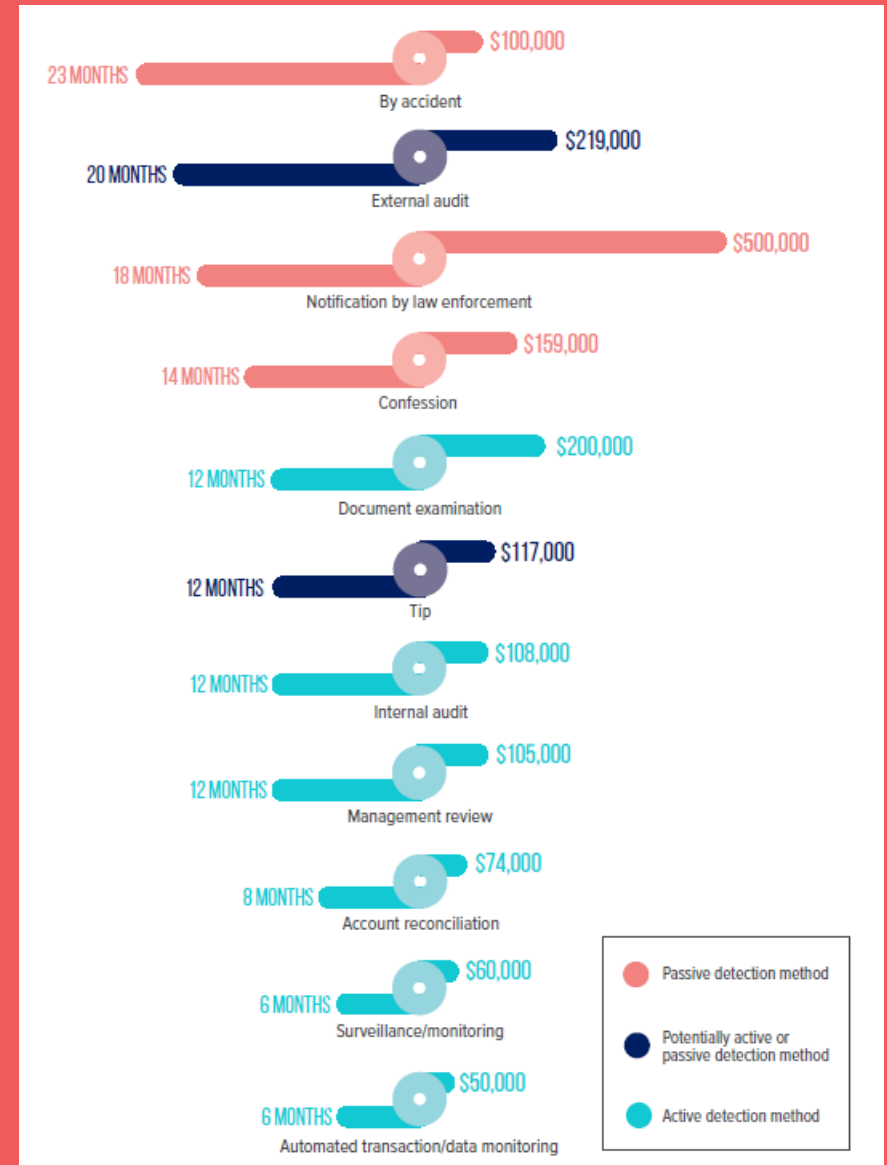
Detection

- Tips are highest form of detection for the last 10 years
- Systems to use
 - Hotline, email, supervisor
 - Training
 - Communication: where can your staff turn?



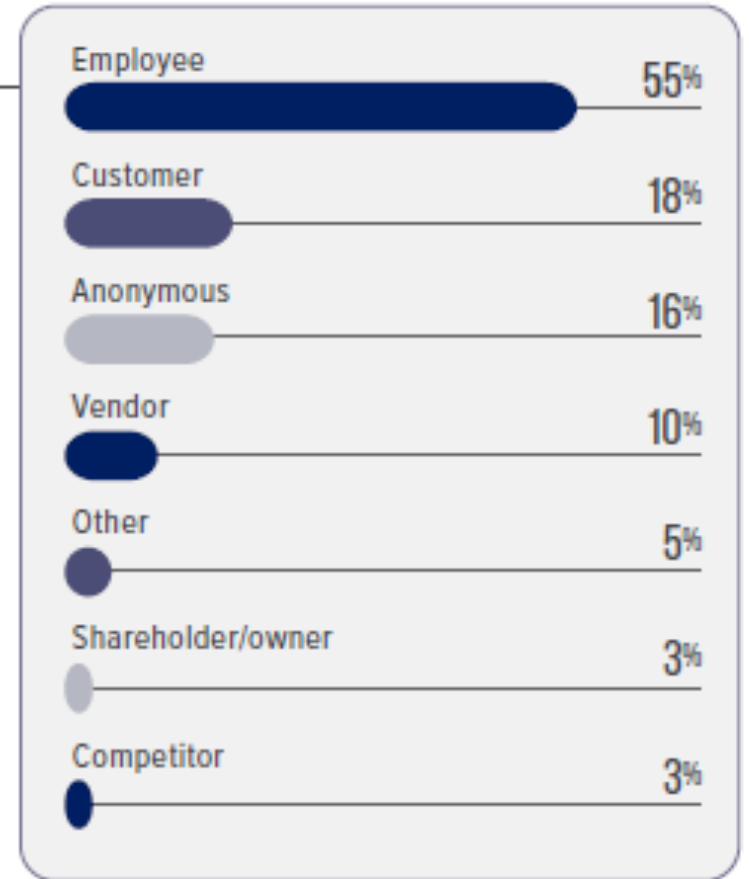
Detection

- Active detection methods
 - Least duration
- Passive detection method
 - Longest duration



Detection

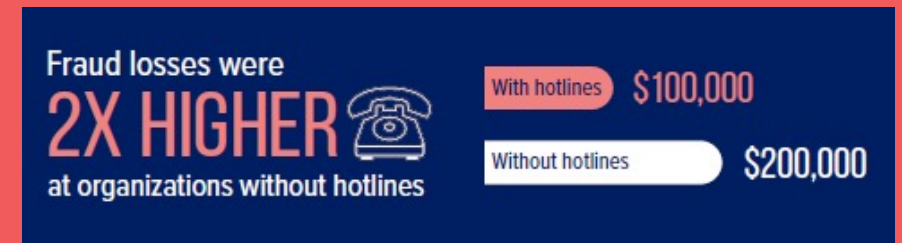
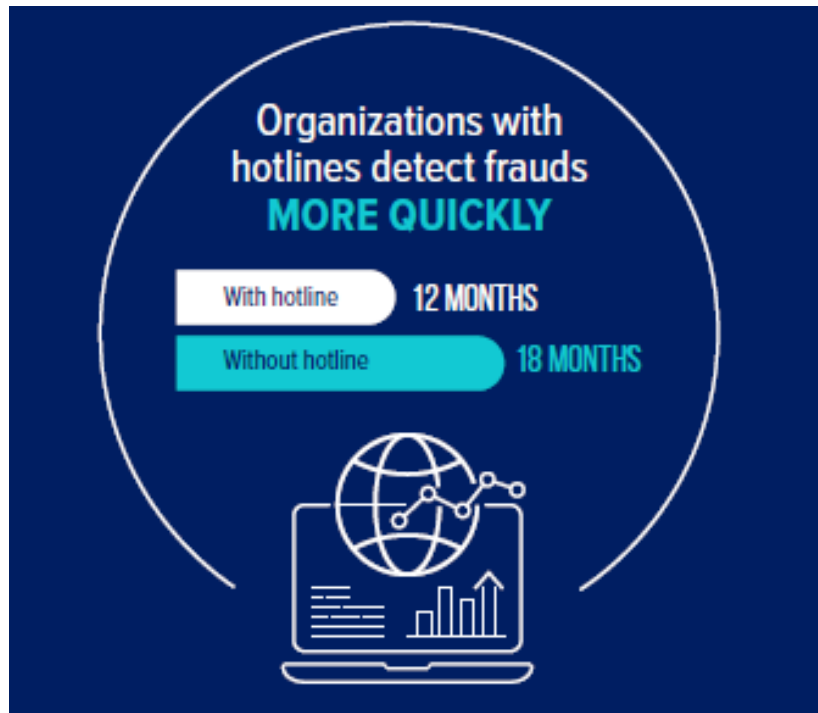
- Employees are your biggest asset
- 2020 Data
 - Employee 50%
 - Customer 22%
 - Anonymous 15%
 - Vendor 11%
 - Other 6%



Detection

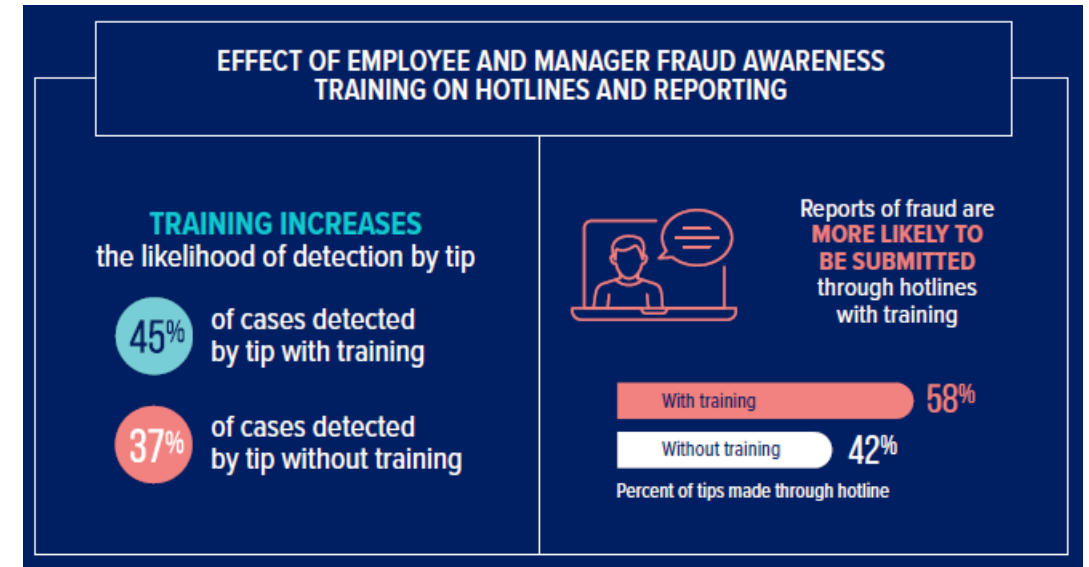
- Hotlines

- Tips are detected faster
- Reduce the amount stolen
- Keeps it anonymous



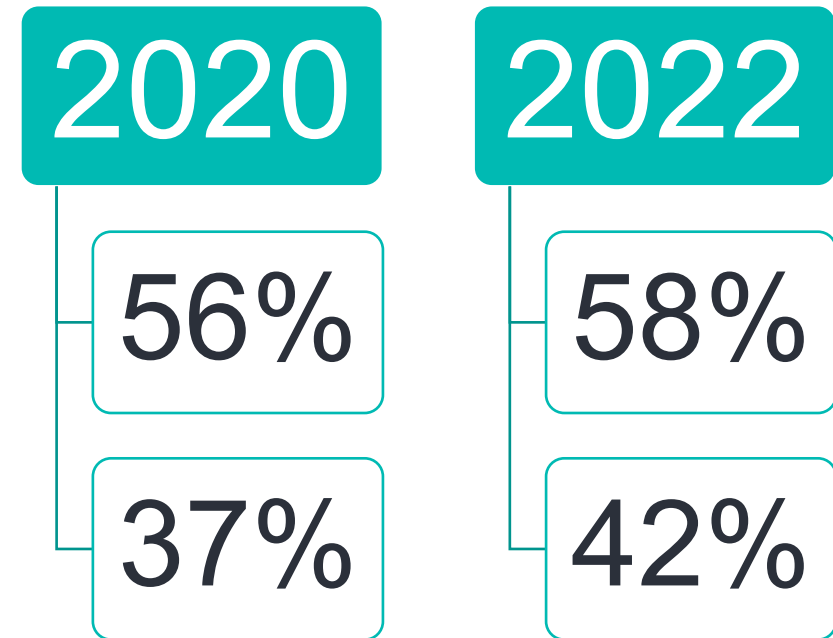
Detection

- Training to identify fraud is a large part of catching the perpetrators
- Maintaining a reporting mechanism increases the chances for earlier detection



Detection

- Reports of fraud are more likely to be submitted through hotlines
 - With Training
 - Without Training



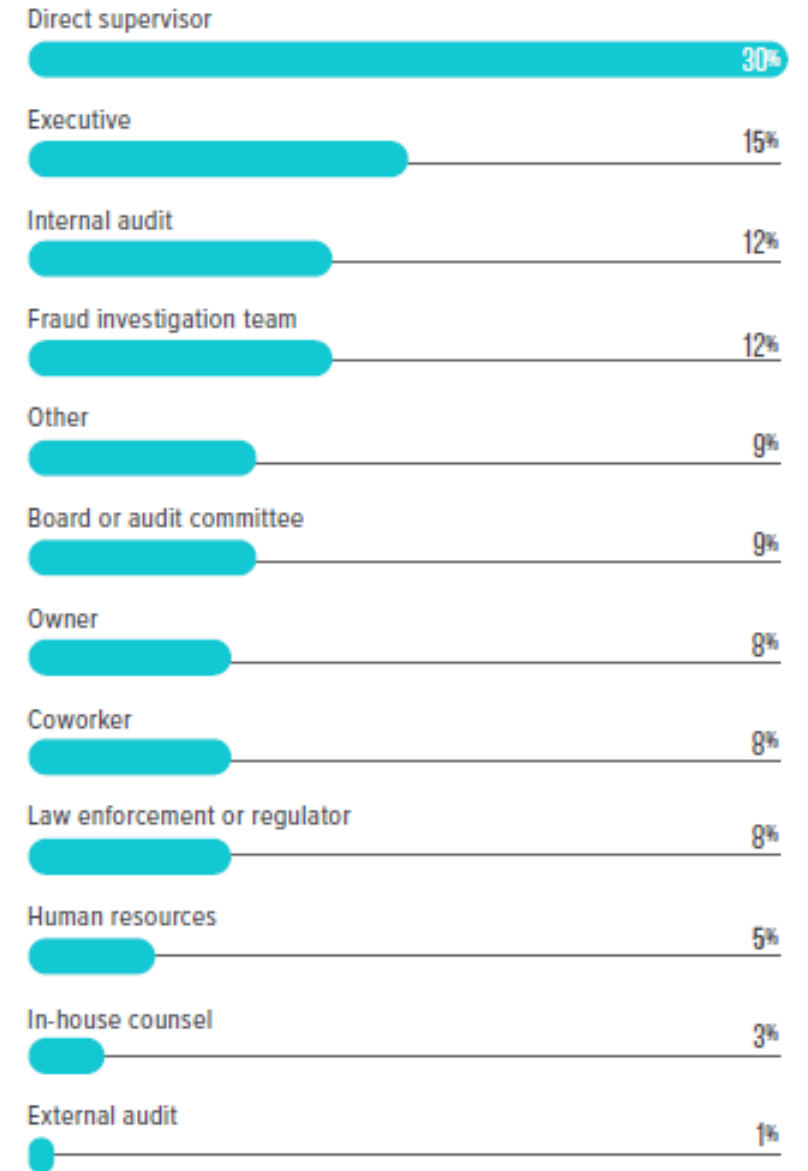
How is it reported?

- Email has surpassed all forms of reporting at 40%
- 2020 there was a close tie with three different forms of reporting



How is it reported?

- If there is no hotline – these are the channels used
- Supervisors should create the channel for communication
- Reports can be made informally



Candy Question

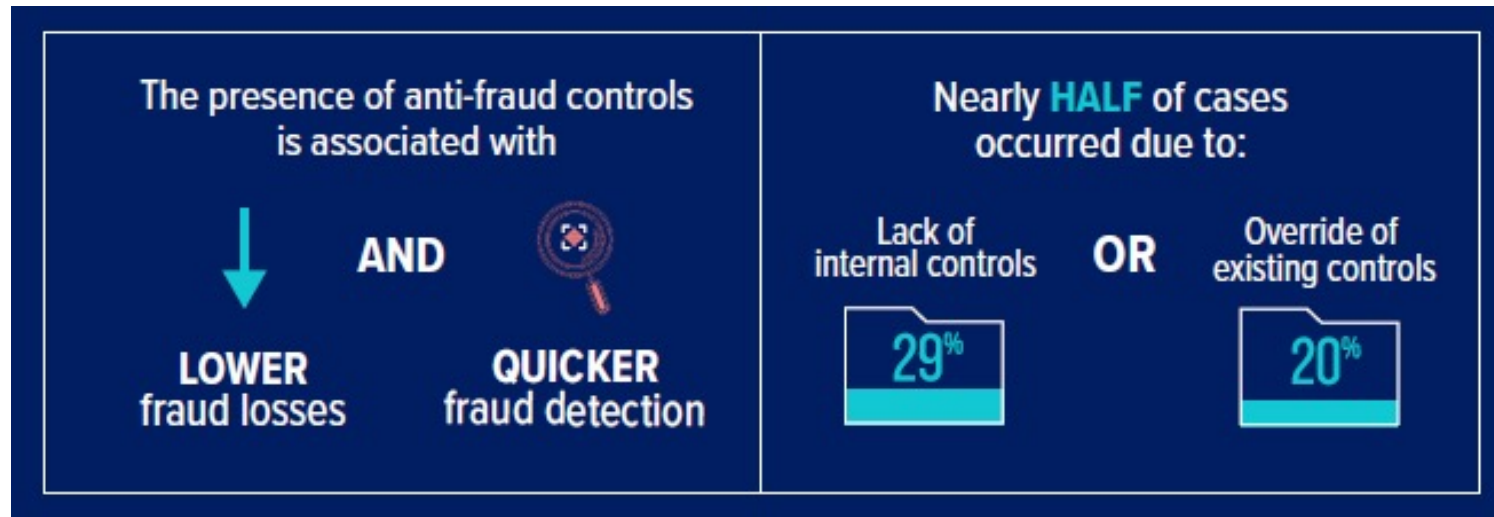
What's the most prevalent way fraud is detected?

- a) Management review
- b) External audit
- c) Tips
- d) Internal audit



Controls

Lack of controls or override of existing controls can result in higher losses and longer duration

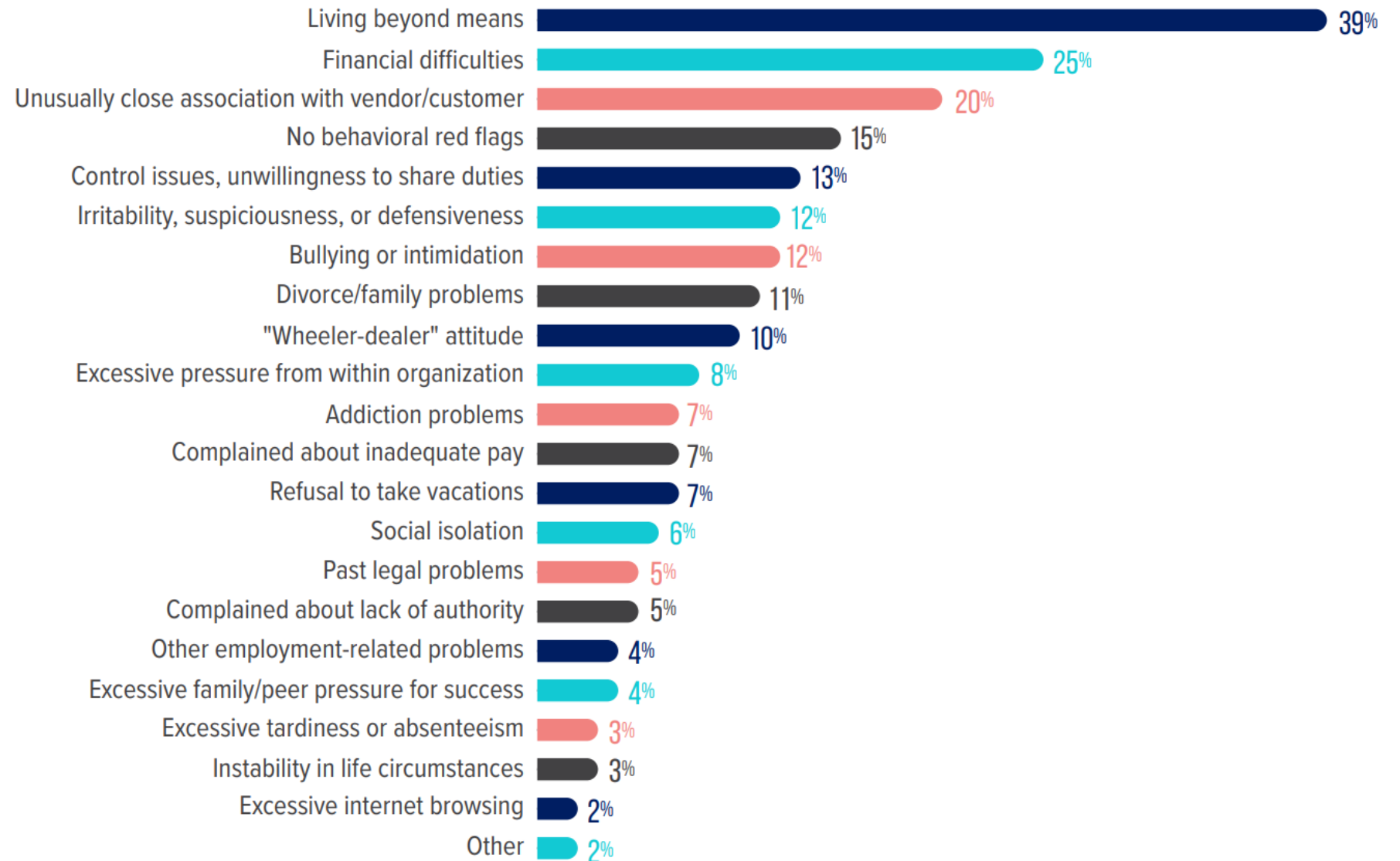


Controls

- Controls implemented that reduced fraud by 50%
 - Job rotation/mandatory vacations
 - Hotline
 - Surprise audits
- Others that were used to reduce fraud by 40%
 - Proactive data monitoring and analysis
 - Anti fraud policy
 - Fraud training for employees
 - Formal fraud risk assessments
 - Code of conduct

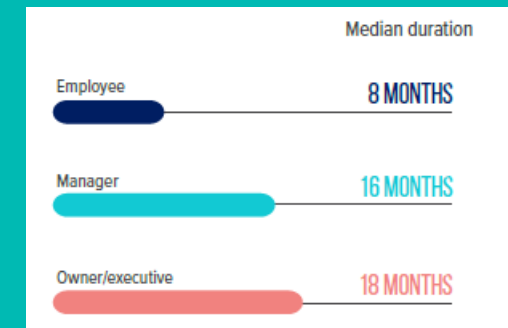
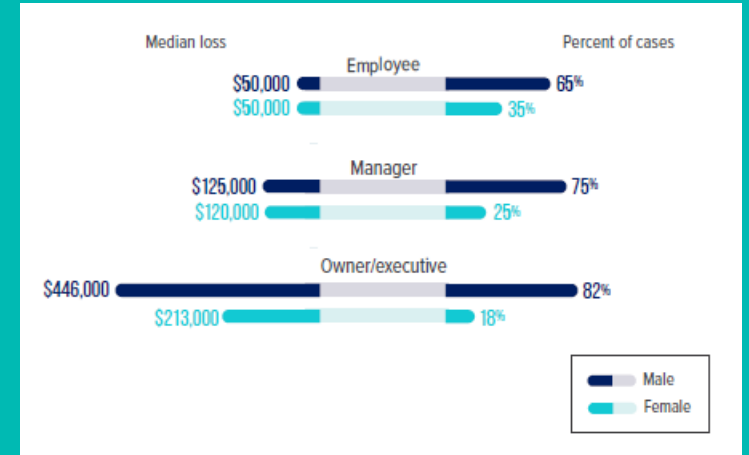


Red Flags!



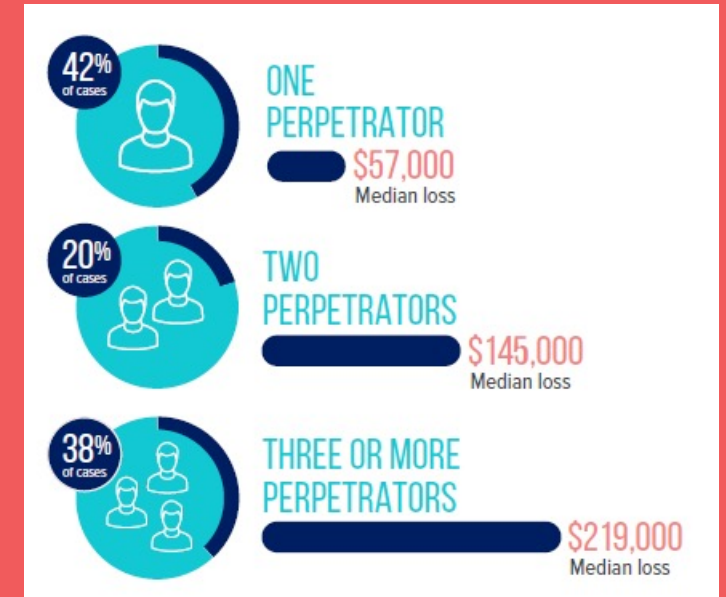
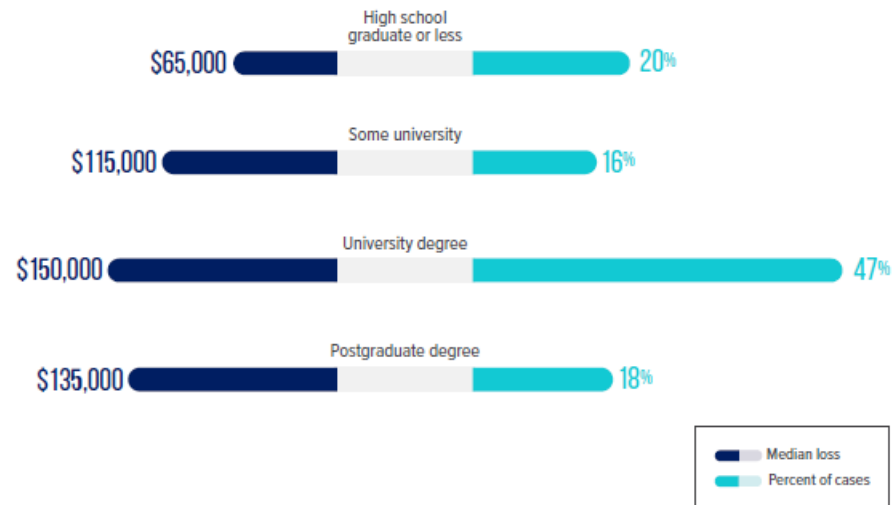
Profile of a Fraudster

- Employee's longevity with the entity increased the amount stolen
- 73% of cases were male
- The higher the position, the more that was stolen
- 20% were between 36-40 years
 - Next highest is 41-45
 - Over 60 yr had a median loss of \$800k



Profile of a Fraudster

- Colluding – 58% used more than one person
 - Still caught in 12 months
- Education level



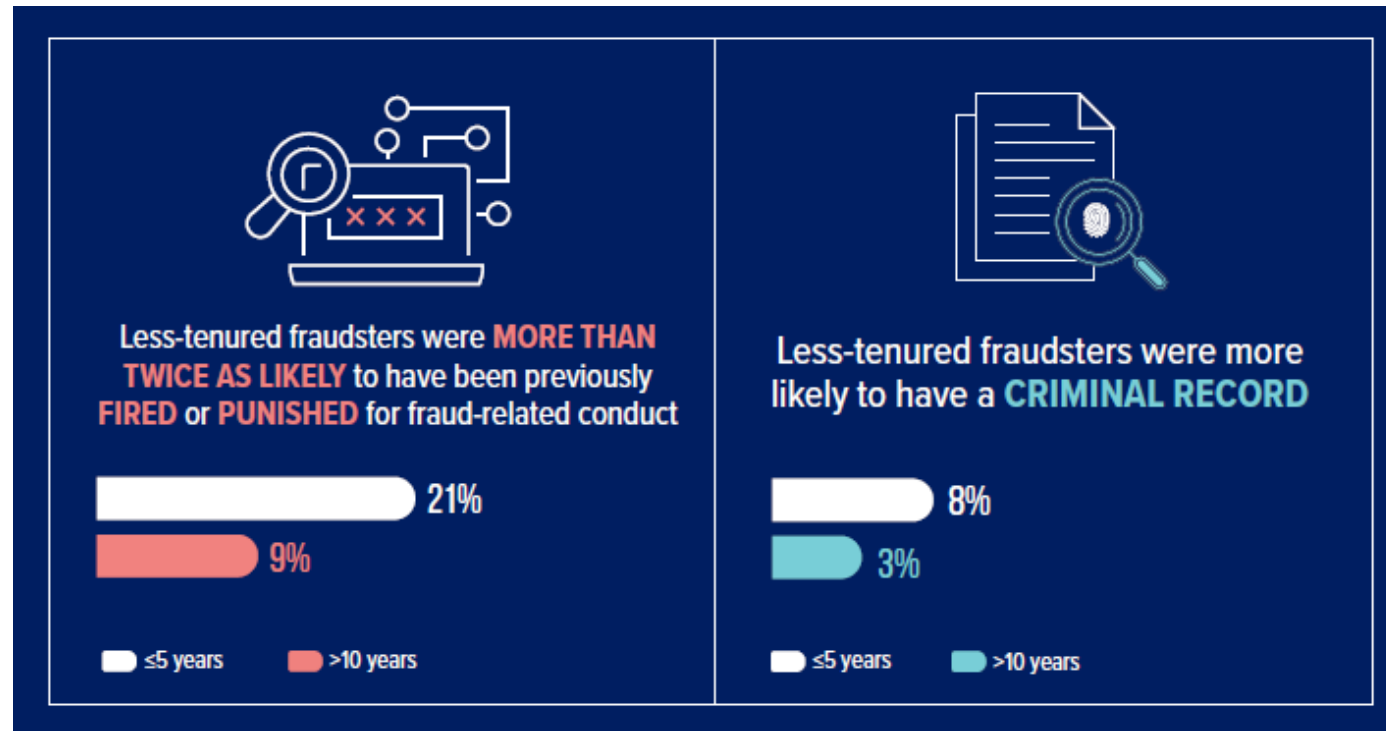
Profile of a Fraudster



- Years of tenure dictating the amount stolen
- They have more knowledge of the systems
- Promoted up the line and now have more control
- More likely to collude and takes longer to catch
- Gained more trust

Profile of a Fraudster

- Less tenured employees
 - How are you checking for previous activity?



Candy Question

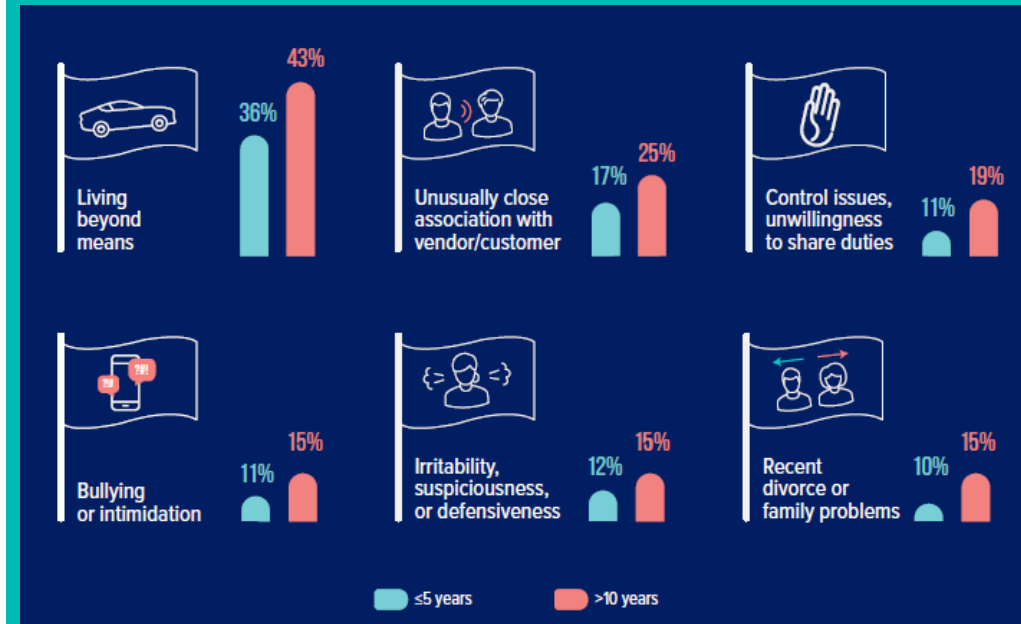
What is the biggest red flag for fraudsters

- a) Excessive internet browsing
- b) Social isolation
- c) Complained about inadequate pay
- d) Living beyond means



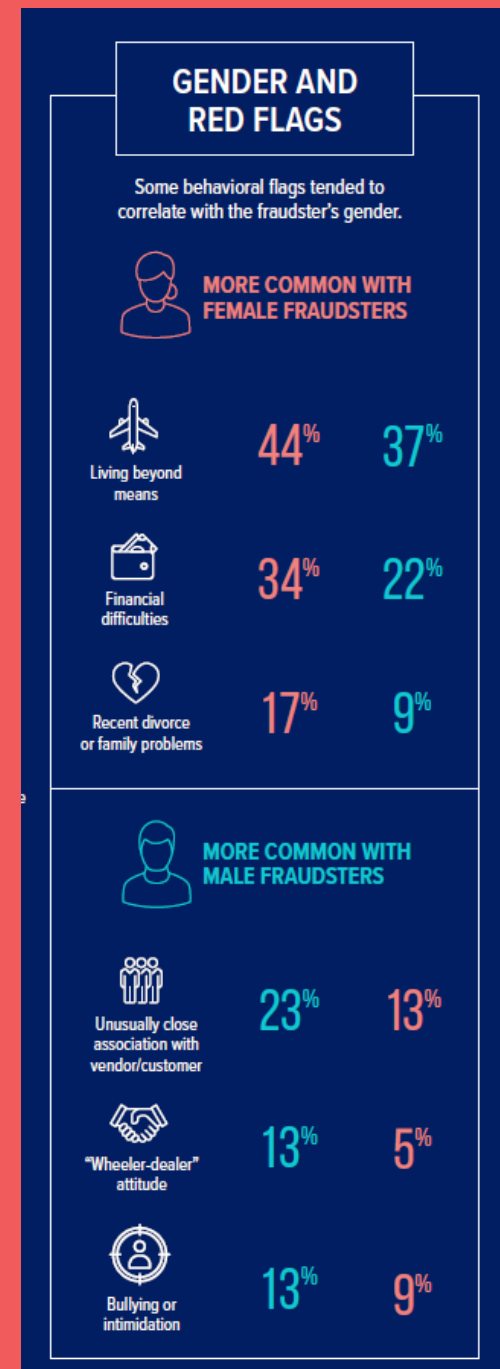
Profile of a Fraudster

- 85% of fraudsters displayed at least one behavioral red flag
 - These were more common among them
 - Living beyond means has been the most common since the study has been around in 2008

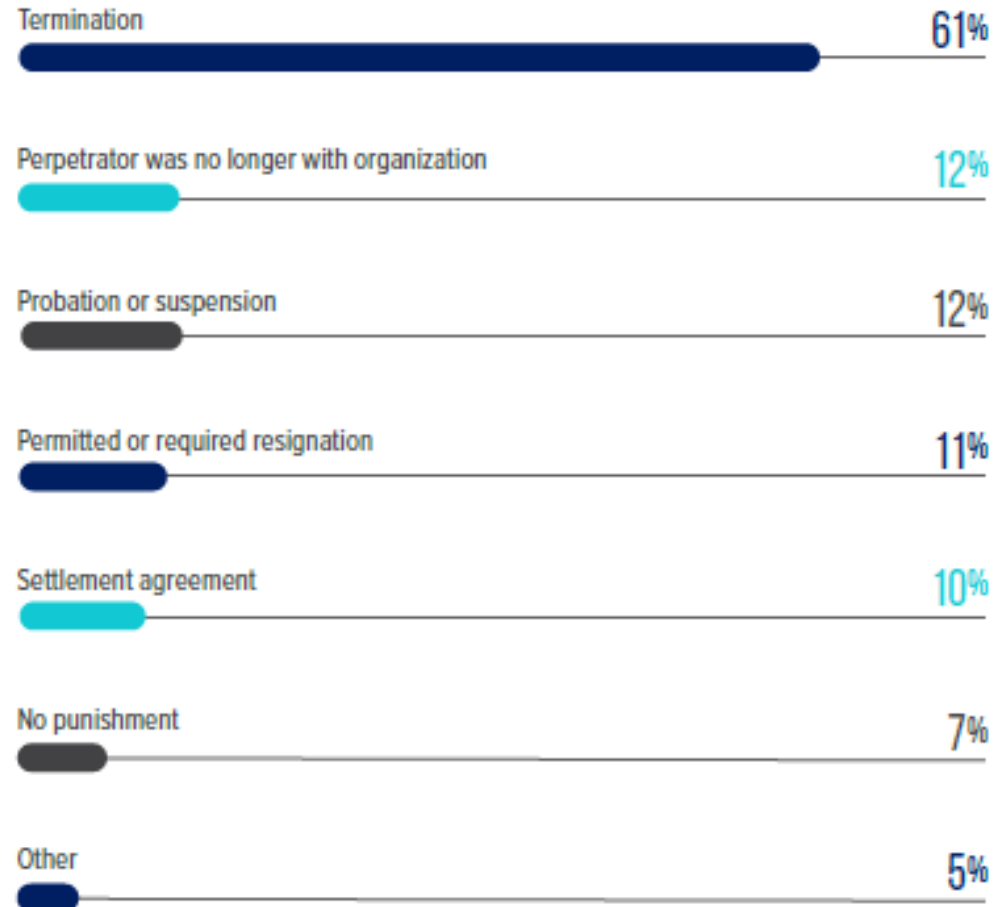


Profile of a Fraudster

- Comparison of female to male for red flags
 - How do we act differently?
- Females
 - Study says live beyond ones means
- Males
 - Study says unusually close with vendors or customers (golf anyone?)

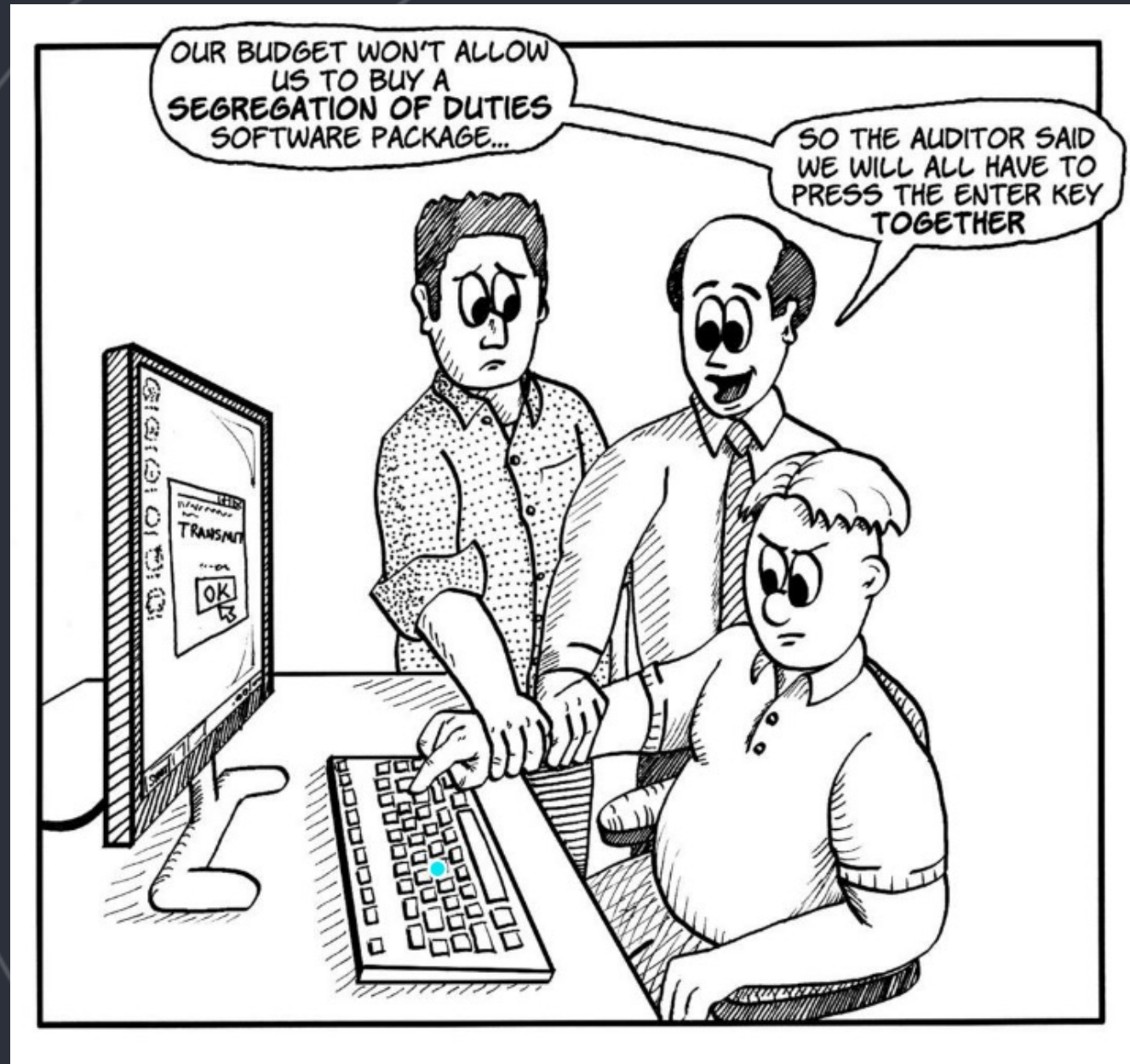


Action Taken



- 50% of entities that didn't refer to law enforcement cited internal discipline as the reason
- 52% of entities didn't recover any fraud losses

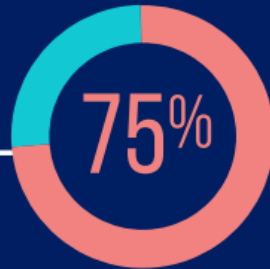
What do you do?



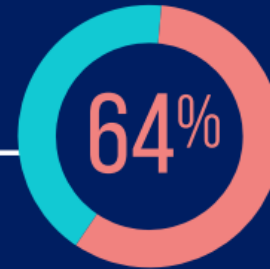
What did organizations do?



81% of victim organizations **MODIFIED** their anti-fraud controls following the fraud.



Increased management review procedures



Increased use of proactive data monitoring/analysis

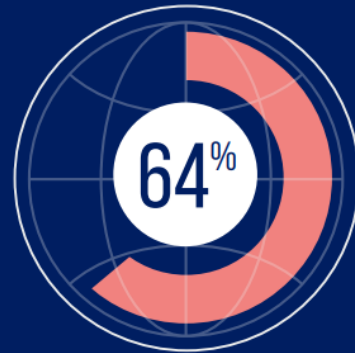
What did organizations do? (Continued)

MOST COMMON CHANGES MADE TO ANTI-FRAUD CONTROLS

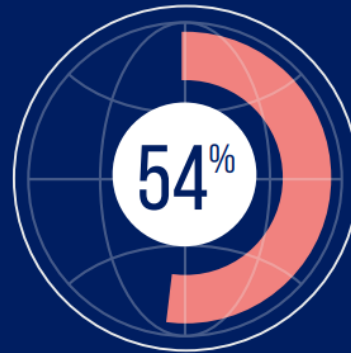
Of changes made to anti-fraud controls, the most common involved implementing or modifying:



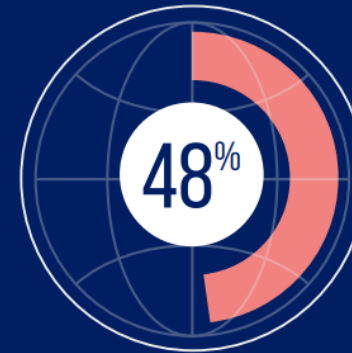
Management
review



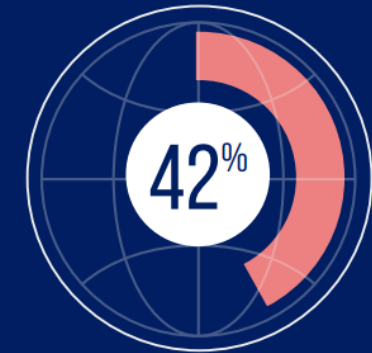
Proactive data
monitoring



Surprise audits



Internal audit
department



Anti-fraud training

What did organizations do? (Continued)



WHICH TYPES OF ORGANIZATIONS WERE MOST LIKELY TO MODIFY THEIR ANTI-FRAUD CONTROLS?



10 Steps to Stop Fraud

1. Ongoing anti-fraud training provided
 - Provide a definition of fraud
 - Teach employees how to communicate
2. Effective fraud reporting system (Hotline)
 - Give employees a place to provide tips without reprimand
3. Proactive measures taken and publicized to employees
 - Surprise audits (Announced to everyone)
4. Management/Tone at the top honest
 - Use realistic performance goals with management

10 Steps to Stop Fraud (Continued)

5. Fraud risk assessments performed
 - Identify organization's vulnerabilities
 - Sample templates online (cost vs benefit)
6. Strong controls in place
 - Segregation of duties
 - Test controls for effectiveness
7. Hiring policy include necessary items
 - Criminal and civil background checks

10 Steps to Stop Fraud (Continued)

8. Support programs in place for employees struggling with addiction
 - Counseling
9. Open-door policy with Upper Management and Governance
 - Allow for times with informal two-way communication
10. Regular anonymous surveys
 - Ethics survey at least once a year or more.

Amazon Gift Card Question

What's the greatest pressure to commit fraud during the pandemic?

- a) Cut in benefits
- b) Having to wear a mask
- c) Forced vaccinations
- d) Fear of job loss



Why do anything?

- By taking proactive steps to prevent occupational fraud, local governments can:
 - Protect their assets,
 - Maintain public trust, and
 - Avoid costly legal and reputational damage.

Questions?



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