Inside job
Prevent and detect employee fraud

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PREVENTING EMPLOYEE FRAUD – the use of a position of employment for personal gain through the deliberate misuse or theft of government assets or resources – is a concern both to government management and elected officials. The purchasing department, with its control over expenditures and the risk of padded orders, paying for goods and services not received, theft of goods purchased, and corrupt contract award practices, is of special concern.

Figures found in the Association for Certified Fraud Examiners' (ACEF) 2002 *Report on Occupational Fraud and Abuse*, suggest that governments of every size and kind are exposed to the risk of criminal wrong doing.

Fortunately, help is often readily at hand. The local police fraud squad can be a useful resource and insurance companies – especially those offering employee bonding – also stand willing to provide advice. However, common sense goes a long way. Deterring crime involves three essential thrusts: first, take reasonable steps to prevent wrongs from being committed; second, ensure that mechanisms are in place to identify wrongs that do occur; and third, ensure that appropriate punishment is meted out.

Punishment acts as a deterrent. Governments are prone to let transgressors off the hook, because of the potential adverse fall-out of a scandal. However, a failure to prosecute is almost always unwise; it will be perceived as a cover-up when the tale of wrong doing eventually leaks – and most cases do. Also, a failure to prosecute undermines the best methods of prevention and detection.

Fear of detection is a powerful deterrent. Telling new employees during their orientation and training that fraud is not tolerated and informing them what to do if they suspect fraud can deter crime. Employees should be encouraged to report unusual activity, including unexplained changes in the lifestyle of their co-workers.

Prevention begins when employees know that management is watchful. One of the most common symptoms of possible wrong doing is an overly keen employee who refuses to delegate, works extraordinary long hours, or never takes a vacation or sick leave. Perpetuating a scam requires constant attention. Generally, a narrow range of factors motivates employee crime:

- personal financial problems, particularly where coupled with gambling, drugs or alcohol;
- striving to meet unrealistic performance goals;
- earning bonuses or rewards; and
- revenge (e.g. to compensate for perceived low pay or a missed promotion, lack of recognition).

Many effective tools are close at hand. Ensure that managers are trained to use a computer's security and auditing features, which can assist them in preventing and detecting employee fraud, e.g., requiring a password before gaining access to functions that deviate from standard procedure can be sufficient. Requiring a regular change in user passwords is also effective. Some software can be programmed to generate a report of unusual transactions, or an atypical pattern of transactions.

Often, the viability of a scam depends upon the predictability of the employer's practices. According to the ACEF, 59 percent of all fraud is discovered when changes are made to internal policies and procedures.

The consent of a prospective employee is required to do a thorough background check (e.g., past employment, criminal convictions and checking references), but this helps screen out repeat offenders, who commit a surprisingly large number of the crimes. Few people with a troubled past will provide references to an employer with a reputation for such investigations. Never hire or promote on faith and gut feelings. Few scams work without a too trusting victim.

Employee crimes are often crimes of opportunity. Strong internal controls over contracting – incorporating checks and balances not only regarding decision making, but also in each area of public administration – serve three primary objectives: to promote operational efficiency; to ensure accurate and timely reporting; and to encourage compliance with organizational policies, procedures, laws, and regulations. No single employee should control a transaction from beginning to end, and no financial or similar data should be susceptible to deletion without an audit trail. In the private sector, a system of dual approval (e.g., a supervisor and an independent representative of the accounting department) is considered an optimal approach. Even the best prevention measures may fail; detection must also be employed.

Management must consistently and persistently monitor expenditures and confirm that the proper approvals are in place. Unfortunately, staff reductions resulting from budget cutbacks hamper their ability to do this. One area of special concern is increases in the upset limit for a contract. When an increase is requested, determine why. Sole sourcing is another common problem area. Who will verify that a competitive bid process is not possible?

Petty cash and P-card transactions are other areas. P-cards are often used to circumvent standing order arrangements, and to avoid an open, competitive bid process. And, outright pilfering from the till is not unknown.

Surprise audits are effective. Caught by surprise, employees have no chance to change the records to hide a fraud. Missing records are often a tip-off. A change in pattern, such as a sudden increase in business with a particular supplier, may indicate double billing.

Another tool may be a hotline or other formal method of whistle blowing. Most employees are honest and want to do something when they see a crime. This may encourage them to come forward.

Employees who know that management is watching over things carefully understand that their crime is more likely to be detected, and are less likely to do wrong. Widespread fraud is an unintended response of poor leadership. Showing little support for ethical behavior and encouraging sharp practice sends the wrong signal to employees. No employer can allow employees to believe that stealing is possible or excusable.

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