NACM-Canada’s 14th Annual Credit Conference & Expo

How to Protect Yourself from Business Fraud

October 26, 2012
Agenda

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2. What is Fraud
3. Impact of Fraud
4. PwC 2011 Global Economic Crime Survey
5. Occurrence of Fraud
6. Fraud Prevention & Detection
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   b. Employee Expense Fraud
   c. Procurement Fraud
   d. Corruption of Foreign Public Officials Act (“CFPOA”) Overview
   e. Common Compliance Sensitive Areas for Bribery and Corruption
   f. The Anti-Fraud Regime Framework
7. Conclusion
Objectives of this Session

✓ Improve awareness of fraud.
✓ Improve ability to detect fraud.
✓ Reduce risk of occurrence of fraud.
✓ Improve ability to deal with fraud.

*Overall Goal: To increase awareness, detection and prevention of fraud.*
What is Fraud?

**General Definition**

- Generally, fraud represents *non-violent financial crime* perpetrated against *business, government* or *individuals*.
- Involves personal gain at the expense of the organization.
- The primary factor that distinguishes fraud from error is whether the underlying action is *intentional* or *unintentional*. 
Impact of Fraud

Cost of Economic Fraud

 Fallout from fraud is not simply the direct costs. Can also impact:

- Staff morale/motivation.
- Reputation/brand image.
- Business relationships with customers, suppliers, stakeholders, etc.
- Negative impact on resources.
- Reallocation of staff time.
- Negative impact on salary increases and bonuses.
Fraud – A Significant and Growing Threat

• Survey of nearly 4,000 organizations in 78 countries.

• Globally 34% of respondents were victims of economic crime in the previous 12 months – an increase from 30% reported in 2009.

• 32% of Canadian organizations surveyed reported being victims of economic crime in the previous 12 months.
No Industry is Immune

But some report more fraud than others...

- Insurance: 48%
- Communication: 48%
- Government/state-owned enterprises: 46%
- Hospitality and leisure: 45%
- Financial services: 44%
- Retail and consumer: 42%
- Entertainment and media: 34%
- Transportation and logistics: 32%
- Engineering and construction: 31%
- Aerospace and defence: 29%
- Energy, utilities and mining: 29%
- Automotive: 25%
- Other industries/business: 23%
- Pharmaceuticals and life sciences: 23%
- Manufacturing: 23%
- Chemicals: 22%
Types and Detection of Economic Fraud

Types of Economic Fraud Globally

• Asset misappropriation (72%)
• Accounting fraud (24%)
• Bribery and corruption (24%)
• Cybercrime (23%)

Detection of Economic Fraud Globally

• Chance or internal/external tip off (41%)
• Suspicious transaction reporting (18%)
• Internal audit (14%)
• Preventative fraud risk management activities (10%)
The Typical Fraudster Profile

• 40% of organizations that were victims of economic crime in the previous 12 months said external fraudsters perpetrated the fraud:
  – Customers, agents/intermediaries

• 56% of companies surveyed reported that the perpetrators of fraud were from their own employees, mainly junior and middle management.
  – However, senior management fraud was more sophisticated and in larger in dollar amounts

• The typical profile of a perpetrator:
  – Male (77%)
  – Age 31-40 (43%)
  – First degree graduate (37%)
  – With the company between three and five years (30%)
General Types of White Collar Crime / Fraud

• Misappropriation of assets
  – Theft of cash (skimming / lapping)
  – Theft of inventory
  – Theft of intellectual property
  – Vendor fraud
  – Payroll fraud

• Fraudulent financial reporting
  – Usually perpetrated by top management
  – Intent is to make company’s financial performance/position look better than it really is

• Corruption
  – Bribes and kickbacks
  – Conflicts of interest
Rule of Thumb

May Commit Fraud
Opportunity & Motivation
60%

Honest
20%

Dishonest
20%
The Perfect Storm

Three conditions commonly found when a fraud occurs:

- Incentive/pressure
- Opportunity
- Attitude/Rationalization

Fraud Risk
Occurrence of Fraud

**Typical Environment in Which Fraud Occurs**

- Poor tone from the top.
- Trust is placed in employees.
- Employees have detailed knowledge of the accounting systems and its weaknesses.
- Management domination subverts normal internal controls.
- Expected moral behaviour is not communicated to employees.
- Unduly liberal accounting practices.
- Ineffective or nonexistent internal auditing staff.
- Lack of or ineffective internal controls combined with liquid assets.
- Poor accounting records.
- Incomplete and out of date procedural documentation.
Theft of Cash / Other Assets

- Asset misappropriation is the most common type of fraud reported by companies.
- Probably since it is the most attainable.
- This could include theft of cash or any other company assets.
- Theft of inventory (e.g., supplies).
- Theft of confidential information (e.g., employee).
- Theft of cheque stock or cheque tampering to obtain money.
**Employee Expense Fraud**

- There is a significant amount of abuse in this area.
- Some red flags:
  - falsified receipts and invoices.
  - expenses without supporting receipts.
  - re-use of receipts.
  - lack of approval or inappropriate level of approval on expenses being claimed.
Procurement Fraud

- Be alert for purchases that violate procurement policies.
- Remember these questions and considerations:
  - Were proper procurement processes followed?
  - Competitive tendering when appropriate.
  - Were proper approvals obtained?
  - Do invoices have appropriate signatures before being paid?
  - Remember value-for-money / quality of goods and services.
  - Disclosure of conflicts of interest.
  - Be alert for fictitious vendors and/or invoices.
**Corruption of Foreign Public Officials Act (“CFPOA”) Overview**

- Corruption of Foreign Public Officials Act enacted in 1999.
- Increased enforcement in recent years.
- Prohibits the promise, payment or giving of money (or anything of value) to a foreign public official for improper advantage in obtaining or retaining business.
- Applies to Canadian and foreign nationals and corporations.
- Must be a real and established link to Canada.
- Includes employees, contractors, agents, sub-contractors and other parties representing or seen to be representing your organization.
Common Compliance Sensitive Areas for Bribery and Corruption

- All points of contact with public or government officials.
- Payments, gifts, gratuities.
- Contractors and their sub-contractors, agents.
- Inadequate or no record-keeping relating to payments, benefits, gratuities.
- Inadequate policies and processes to define payments, gifts, gratuities, facilitation payments.
- Inadequate or no processes for approval (pre and post) for payments, benefits, gifts, gratuities.
- Inadequate or no reporting and monitoring by appropriate levels of management and the Board.
The Anti-Fraud Regime Framework

Eight Components of an Anti-Fraud Regime

• Governance – Oversight by the Audit Committee and the Board
• Fraud Risk Assessment
• Code of Business Conduct and Ethics
• Incident Reporting Mechanisms – internal and external
• Investigative Protocol
• Remediation Protocol
• Hiring and Promotion Policies and Procedures
• Management Evaluation and Testing
Key Points to Remember

- Fraud is prevalent in Canada.
- Increasing requirements and public pressure on all organizations.
- Deterrence, detection and prevention of fraud is an ongoing process.
- The key to success is transparency and consultation.
**Key Points to Remember (continued)**

- Impact of economic crime on **reputation** and **staff morale** can be more important than the direct financial loss.

- It is not a matter of **IF** an organization will be the victim of an act of fraud, but **WHEN**.

- **Be alert for red flags and communicate your concerns.**
Thank you

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