

Proactive Fraud Prevention

Don't wait.

Understand what can go wrong.

Assess risks.

Strengthen controls.

Introductions

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AGENDA

- Fraud Stats
- School District vulnerability to fraud
- What does your District have in place to mitigate fraud risk?
- What can go wrong?
- ACFE's Fraud Triangle
- Internal control framework (COSO / ACFE)
- Effective controls
- Incident response

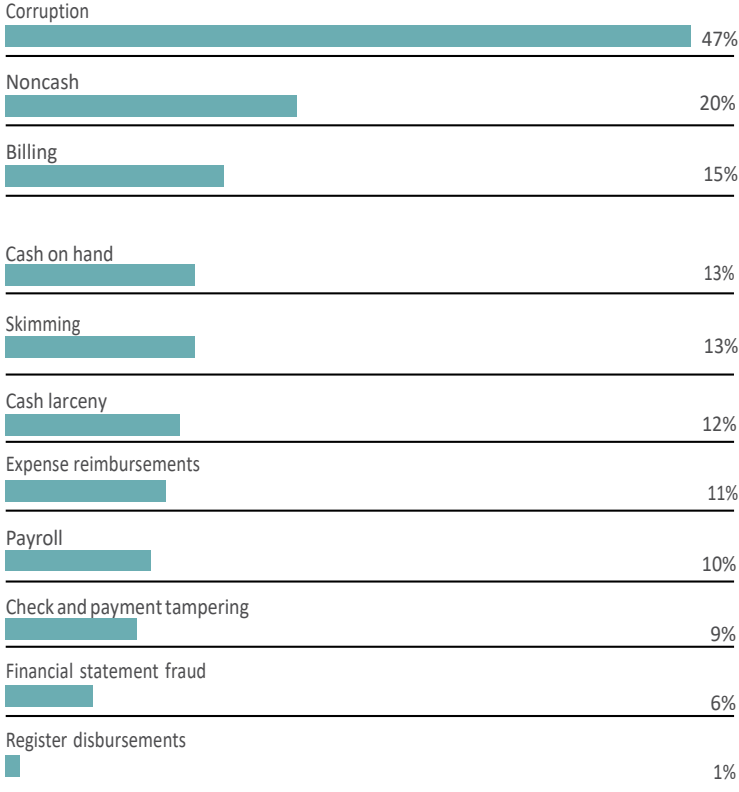
Stats*

- Median loss = \$118,000
- Median duration of fraud scheme = 18 months
- Levels of Gov't victimized by Occupational Fraud / Median loss
 - National = 38% / \$200,000
 - State/Provincial = 26% / \$110,000
 - Local = 31% / \$84,000
 - Other = 5% / \$58,000

*ACFE 2018 Report to the Nations Government Edition

Stats

FIG. 2 What are the most common occupational fraud schemes in government agencies?



School District Vulnerability to Fraud

- Small offices / Small budgets - Lack of segregation of duties
- Trust
- Concentrating on educating children
- Not designed to make a profit
- Inexperience/Naivete' makes District ripe for vendor fraud
- Conflicts of Interest
- Political Activity
- Covid – business processes altered

What does your District have in place to mitigate fraud risk?

- Internal Audit? Internal Audit Plan?
- Risk Assessment?
- Board review of transactions / Audit Committee?
- Transparency?
- Independent oversight?
- Fraud hotline / Whistleblower system?
- Comprehensive Policies and Administrative Procedures?
- Detailed Code of Conduct?

But My Auditor Gave a Clean Opinion!

- An unqualified audit opinion does NOT mean that there is no employee dishonesty or fraud occurring in the organization.
- Employee dishonesty and other acts of fraud can be significant and the books can still balance; often exists even when bank accounts are reconciled.
- Does management letter address internal controls?
- Materiality

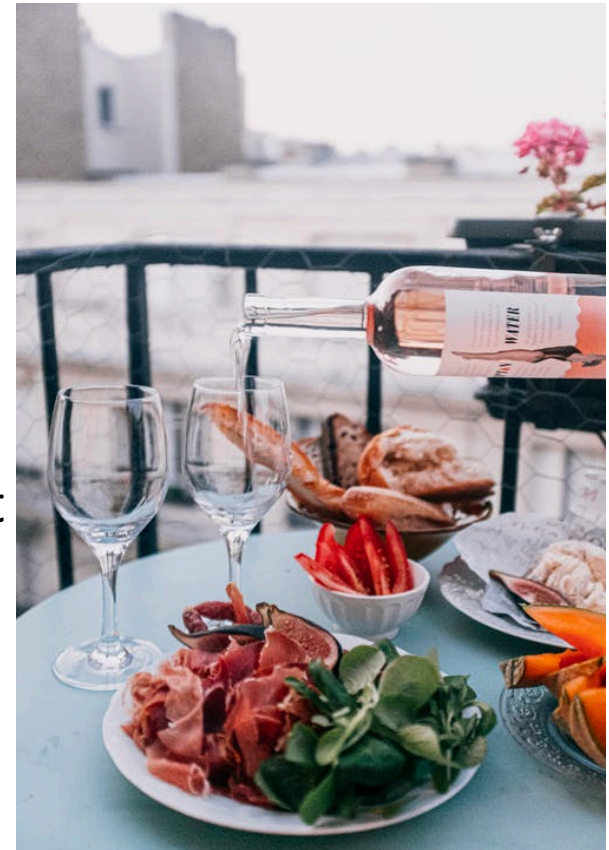


What can go wrong?

- Payroll Fraud – cheating time, fraudulent time edits
- Ghost payrollers
- Fraudulent reimbursements
- Excessive overtime
- P-Card
 - Unauthorized expenditures
 - Circumventing procurement / spending rules
- Stringing
- Tax exempt purchases

What can go wrong?

- Criminal background
 - Update periodically
- Fraudulent leaves of absence
- Worker's comp fraud
- Unauthorized use of District assets
- Ethics violations
 - Direct and indirect economic interest
 - Gifts / “Wining and dining”
- Bribery and kickbacks
- Collusion with vendors
 - Stringing
 - Over billing
- Lack of knowledge of procurement and spending rules



What can go wrong?

- Bidding / specs - Collusion schemes
 - Bid rigging, rotating, suppression
- Sole source
- Emergency
- Change orders
- Ghost vendors
- Ghost invoices
- Billing
 - Overbilling
 - Mischarging
- Product substitution

Fraud triangle (ACFE)



When People Commit Fraud

- **Pressure /Motivation**
 - Personal financial problems
 - Power
 - Overlook controls to get the job done or impress the boss
- **Opportunity** – the person must see some way he can use his position of trust to solve his financial problem with a low risk of getting caught
- **Rationalization** – fraud is acceptable or justifiable act
 - Borrowing
 - Underpaid
 - Provide for family
 - Employer is dishonest, deserved to be fleeced
 - Nobody will miss the money

When People Commit Fraud

- Trusted employees
- Lack of oversight creating a “perceived” opportunity
- Management and others focusing on the core mission of the agency
- Rationalization

Internal Control Framework

- It is management's job to ensure that proper controls are in place to prevent fraud, as well as detect it. (ACFE)
- Internal control is a process, effected by an entity's board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives relating to operations, reporting, and compliance. (COSO)

COSO Internal Control Framework

- Control Environment
- Risk Assessment
- Control Activities
- Information and Communication
- Monitoring

Control Environment

- Control Environment provides the foundation for the internal control system throughout the entire organization. The control environment is established by the **directors and senior management** and sets the moral and ethical tone of an organization.
- Principles
 - Personnel at all levels demonstrate a commitment to integrity and ethical values.
 - Board oversees the development and performance of internal control.
 - With Board oversight, management establishes the structures, reporting lines, and appropriate authorities and responsibilities.
 - Organization demonstrates a commitment to attract, develop, and retain competent individuals in alignment with objectives.

(ACFE)

Risk Assessment

- Risk Assessment involves the identification and assessment of the risks the entity faces in achieving its organizational objectives. This process is dynamic and iterative, and it forms the basis for determining how risks will be managed.
- Principles
 - Clear objectives to enable the identification and assessment of risk.
 - Identify risk to the achievement of objectives.
 - Consider the potential for fraud.
 - Identify and assess changes that could significantly impact the system of control.

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Control Activities



- Control Activities are the policies and procedures that enforce management's directives intended to mitigate risk.
- Principles
 - Control activities selected to mitigate risks.
 - General control activities over technology to support the achievement of objectives.
 - Control activities deployed through policies that establish what is expected and procedures that put policies into action.

(ACFE)

Information and Communication

- Information and Communication relates to the exchange of information in a way that allows employees to carry out their internal control responsibilities.
- Principles
 - Obtain or generate and use relevant, quality information to support the functioning of internal control.
 - Internally communicate information, including objectives and responsibilities for internal control.
 - Communicate with external parties regarding matters affecting the functioning of internal control.

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Monitoring

- Monitoring is the process that assesses the effectiveness of a control system over time. Includes both ongoing, automated evaluations and periodic, separate evaluations.
- Principles
 - Select, develop and perform ongoing and/or separate evaluations to ascertain whether the components of internal control are present and functioning.
 - Evaluate and communicate internal control deficiencies in a timely manner to those parties responsible for taking corrective action, including senior management and the Board.

(ACFE)

Proactively reduce fraud risk

- Transparency
- Audit Committee / Board review of transactions
- Internal Audit
- Audit Plan / Risk Assessment
- Independent oversight
- Fraud hotline / Whistleblower system
- Comprehensive Policies and Administrative Procedures
 - Roles in control environment defined
 - Clearly define acceptable / prohibited PCard transactions

Proactively reduce fraud risk

- Due Diligence in Hiring
- Segregation of duties
- Cross train
- Rotate staff
- Updated IT systems
 - Audit trail
- Positive Pay
- Due diligence in hiring vendors
- Payroll change report

Fraud Incident Management Protocol

- Establish a Response Team
 - Receive and evaluate tip
 - Puts process into place
 - Avoids conflicts
 - Confidentiality and Privileged
- Decide who will investigate and how investigation will be conducted (Law enforcement is not always the answer)
- Preserve evidence
- Is immediate action warranted? (Administrative Leave)
- Who will interview witnesses and subjects?
- Evaluate evidence
- Present to Board
- Media response

Questions and Answers

We thank you for your time!

Presenters:

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