

UNMASKING DECEPTION: School District Fraud Protection



Session Leaders

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Chief Financial Officer

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Shelby County Public Schools, Kentucky

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- Approximately 7000 students
- About 1000 contracted employees
- 12 schools



Session Leaders

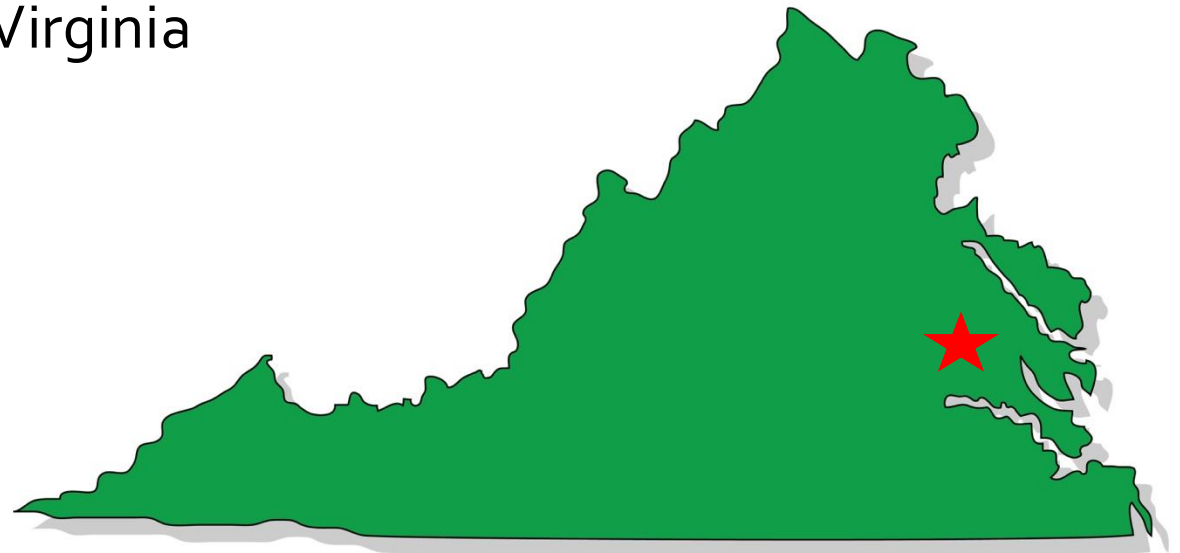
Staci M. Longest, CFE, SBA

Director of Budget & Finance

King William County Public Schools, Virginia

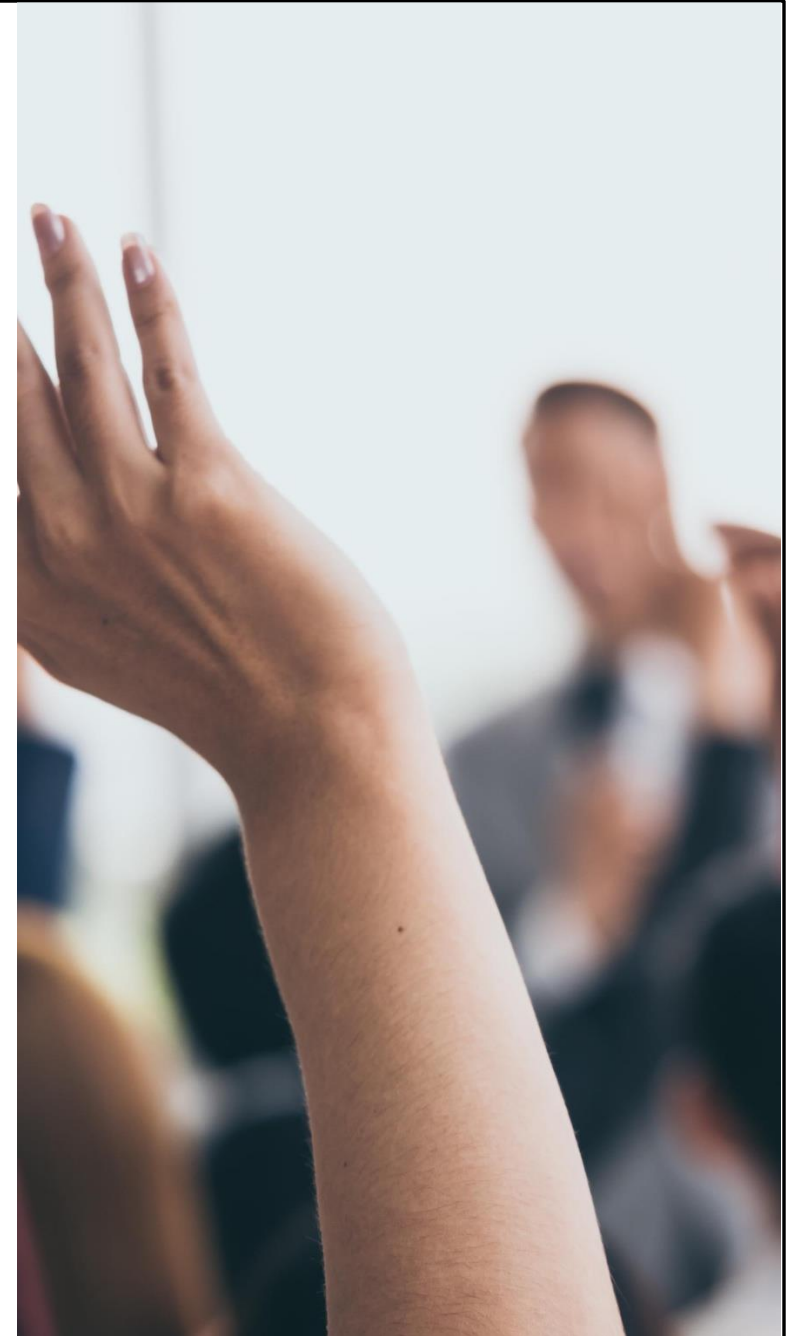
slongest@kwcps.k12.va.us

- Approximately 2000 students
- About 415 contracted employees
- 4 schools & 2 Alternative School



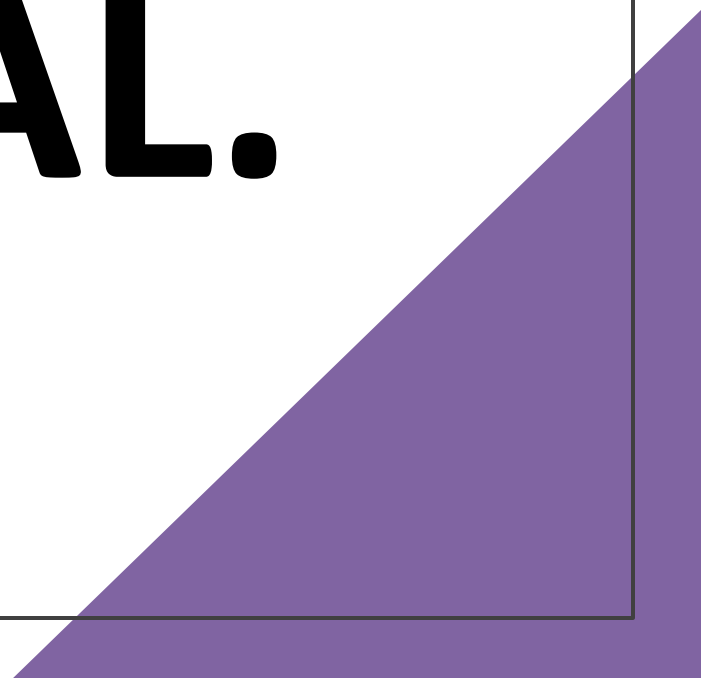
Stand Up, Sit Down

- Stand Up IF:
 - You require an approved purchase order before committing funds
 - You use positive pay
 - You have a warning banner on external emails
 - You use digital tickets instead of cash at the door
 - You solicit tips relating to potential fraud
 - You have strong controls for credit card usage
 - The bank contact is NOT your payroll staff
 - Your district requires annual training on finance procedures



EVERYONE MIGHT STEAL.

*Good people make bad decisions in tough
circumstances.*

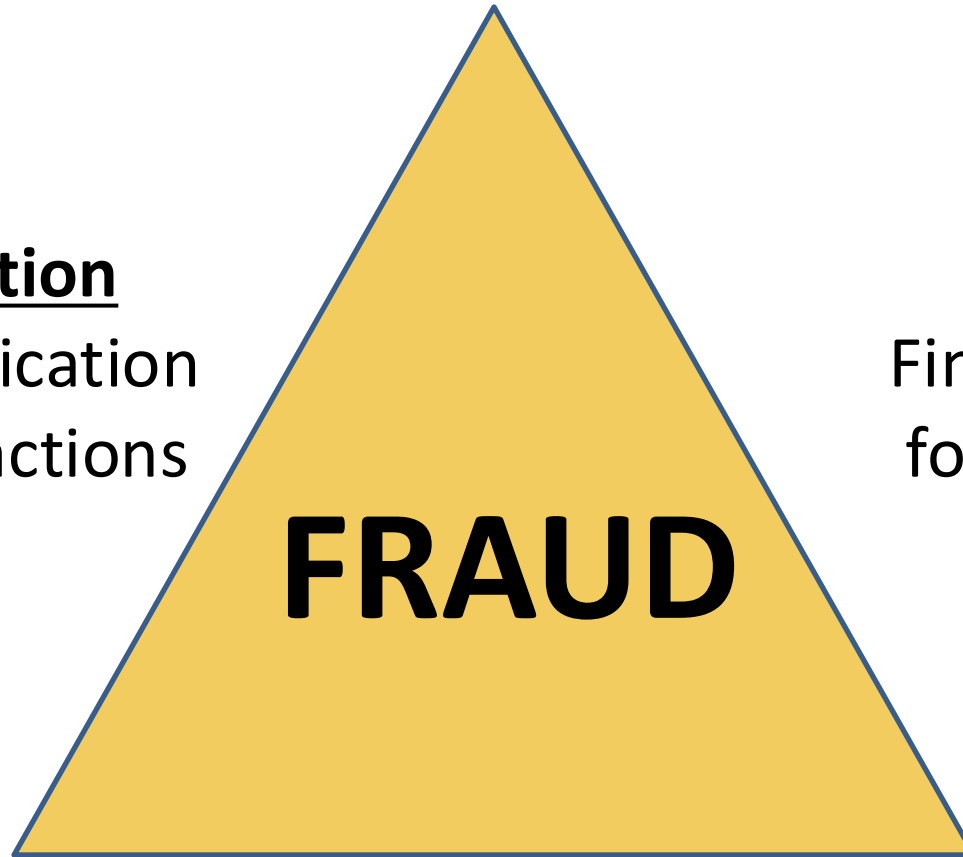


Rationalization

Personal justification
of dishonest actions

Incentive

Financial or emotional
force pushing toward
fraud

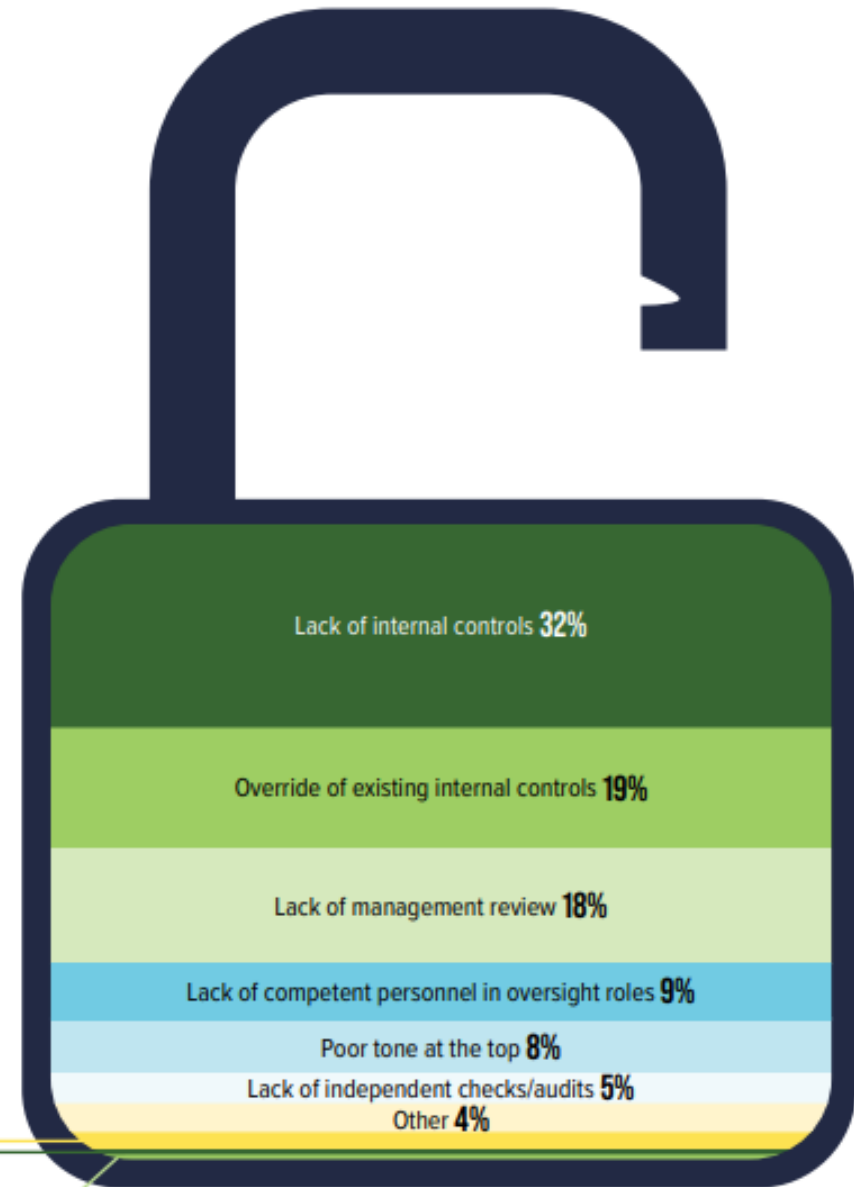


Opportunity

Ability to execute plan without
expectation of being caught

**WE CONTROL THE
OPPORTUNITIES THROUGH
INTERNAL CONTROLS**

Internal Control Weaknesses Contribute to Fraud



Lack of employee fraud education 3%

Lack of clear lines of authority 1%

Lack of reporting mechanism 1%

Internal Control Defined

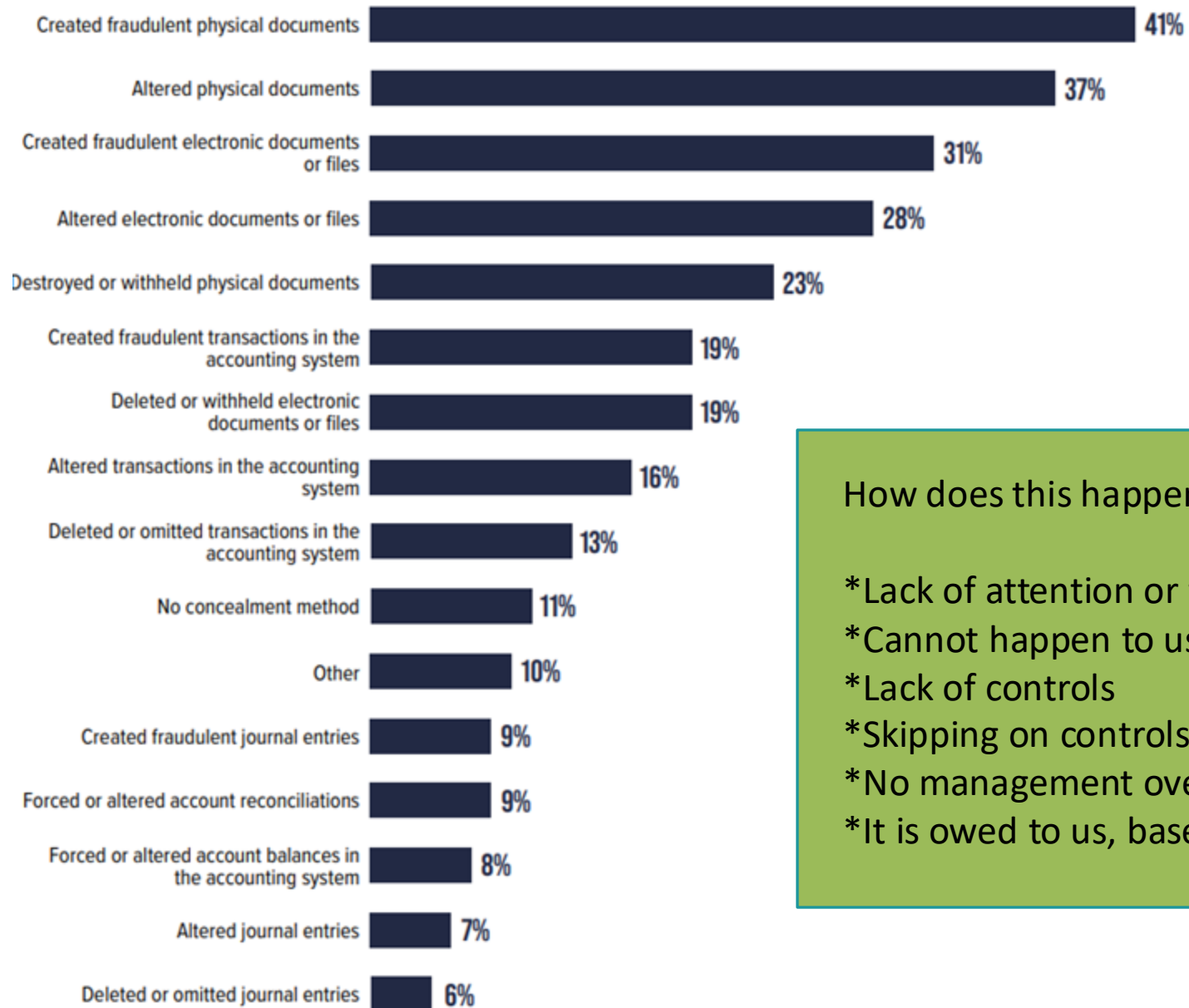
Internal control is a manual or automated process designed to provide reasonable assurance regarding the achievement of objectives relating to operations, reporting, and compliance

- Preventive controls – stop something bad from happening before it occurs
- Detective Controls – identify something bad after it has occurred

**TRUST IS NOT AN
INTERNAL CONTROL**



FIG. 10 HOW DO OCCUPATIONAL FRAUDSTERS CONCEAL THEIR SCHEMES?



How does this happen?

- *Lack of attention or focus
- *Cannot happen to us type attitude
- *Lack of controls
- *Skipping on controls
- *No management oversight
- *It is owed to us, based on pay or hours worked

Accounts Payable Controls:

- Adding vendors, making changes to vendors, adding ACH accounts- should be done by a different person than the one entering in the accounts payable. (sometimes hard for small districts- have a review process in place)
- Ensuring you have controls in place for review of your accounts payable batch, looking for duplicate payments, reviewing invoice numbers, looking for the wrong accounts being charged.
- Always keep your eyes out for duplicate invoices. We are seeing an increase in email invoices and mailing invoices. We are seeing duplicates sent into finance from time to time even with invoice numbers that vary.



WHEN PAYING BY PAPER CHECKS

You need to ensure your paper check stock is locked at all times. Best practices: Have someone other than the AP clerk manage check stock. That is a good control

If you have blank check stock, still keep it locked up but it isn't numbered and not useful unless printed through the accounting system.

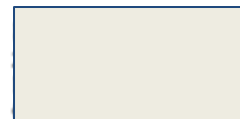
In Virginia, we are seeing an increase in check tampering and check fraud. Therefore, this has been a pretty hot topic in our area.



CHECK FRAUD

WARNING: THIS DOCUMENT HAS SECURITY FEATURES IN THE PAPER

KING WILLIAM COUNTY PUBLIC SCHOOLS
KWPCS
18548 King William Road
King William, VA 23086



NO. 33775

VOID AFTER 180 DAYS

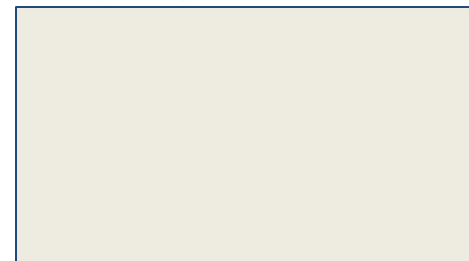
DATE ISSUED
02/02/24

CHECK NO.
33775

CHECK AMOUNT
\$*****38,889.28

Thirty Eight Thousand Eight Hundred Eighty Nine AND 28/100 Dollars

TO THE ORDER OF:
Angelique Velasquez
437 Manor Rd Apt 10
Newport News, VA 23608-3635



Check cut to Dominion
Power, Electric Services

It was washed and
submitted thru Mobile
Deposit



After a check fraud back in
May 2023, we put positive
pay in place.

- Has occurred to at least 9 other school districts in VA since the Fall 2023.
- King William never lost funds; without processes in place this could have had a different outcome.

CONSIDER POSITIVE PAY:



- We worked with our Treasurer's office to get Positive pay set up with our bank. It will verify Vendor name, amount, check number, and date.
- If you have positive pay set up already, please verify with your bank that they have it set up to compare Vendor name, Amount, check number, and date.
- If you don't have positive pay set up already, ensure you look into getting this set up as soon as possible.
- You will get variances from those reports that then need to be verified by staff.

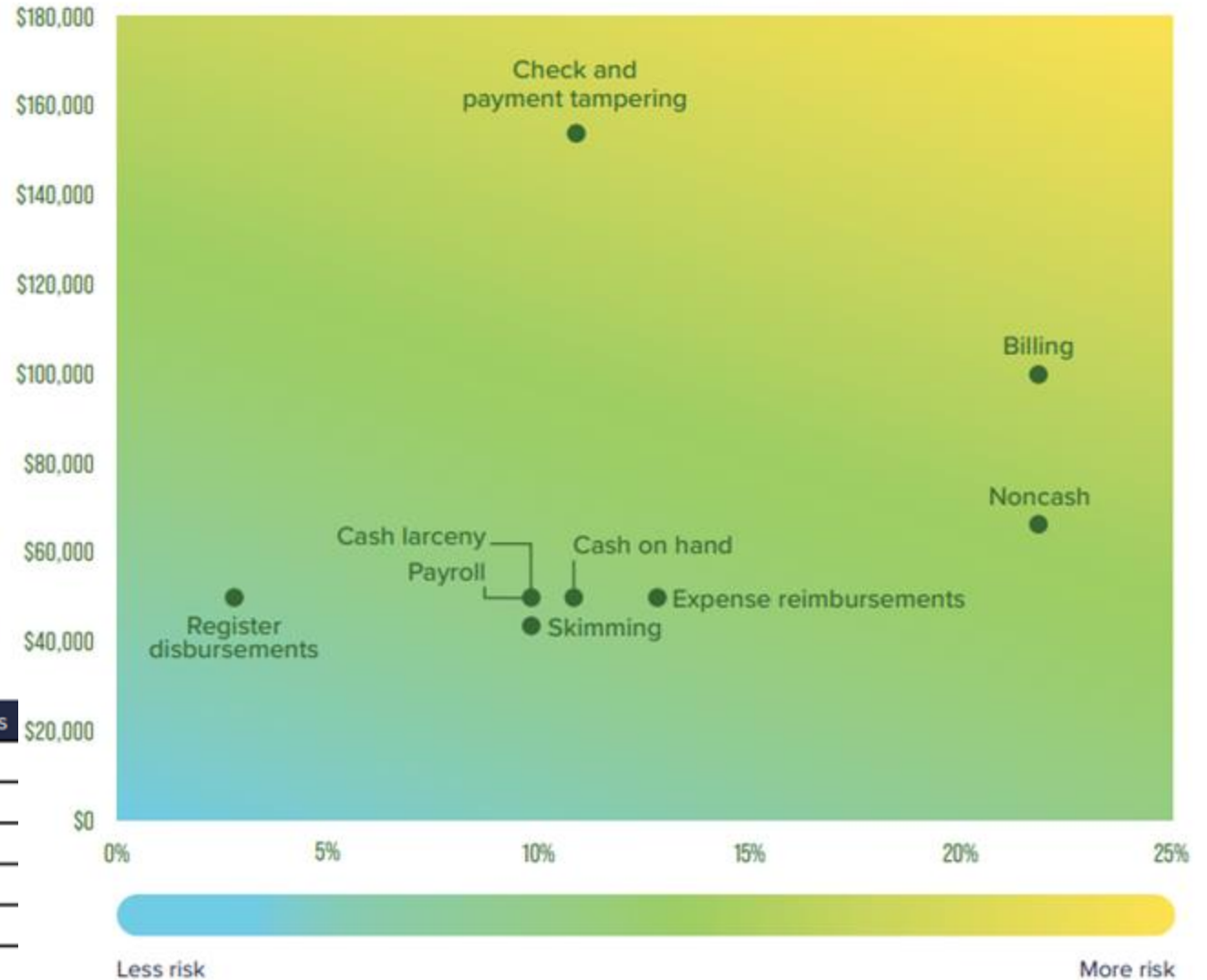
Check & Payment Tampering: Medium risk but highest \$\$ loss

These sub-schemes pose the
greatest risk



Category	Number of cases	Percent of all cases	Median loss
Noncash	426	22%	\$66,000
Billing	424	22%	\$100,000
Expense reimbursements	248	13%	\$50,000
Check and payment tampering	217	11%	\$155,000
Cash on hand	205	11%	\$50,000
Skimming	200	10%	\$43,000
Cash larceny	192	10%	\$50,000
Payroll	190	10%	\$50,000
Register disbursements	52	3%	\$50,000

FIG. 5 WHICH ASSET MISAPPROPRIATION SUB-SCHEMES PRESENT THE GREATEST RISK?



Paying by ACH:



Advantages:

- Financial savings from cutting checks
- Financial savings from mailing checks
- Vendor receives payments faster
- Checks don't get lost in the mail (less check tampering)

Disadvantages:

- Teaching vendors how it works
- Separate internal controls needed including the ACH file upload process
- **Brings additional cyber fraud risks- must find process to review changes**



Chief Financial Officer-
\$6.7 Million in 20 months

- Nine years in prison for money Laundering & mail fraud
- January 2022- October 2023
- Chief Financial Officer, age 38

59 Wire Transfers, including:

- Several vehicles, including eight luxury golf carts for over \$160,000 and a 2023 Chevrolet Suburban
- Spending over \$100,000 on gambling, including at Rivers Casino in Portsmouth, Colonial Downs Racetrack in New Kent and the Virginia Lottery
- Paying at least \$29,000 to an “intimate partner” and tens of thousands of dollars to a bank account in the name of Raines’ wife
- Spending over \$9,000 on private limousine services, including to chauffeur Raines and his guests in a Mercedes limousine from Raines’ house to Virginia vineyards
- Several purchases of cryptocurrency, including Bitcoin and Dogecoin, and transferred funds to his brokerage accounts
- Paying tens of thousands of dollars towards his student loan debt, his mortgage and other loans
- Paying over \$125,000 for private jet travel for Raines’ friends and family, including paying over \$34,000 to travel with his wife and his friends to Nashville, TN, for three days in a private jet
- Spending over \$19,000 to purchase eight separate 2022 1-oz American Gold Eagle Bullion coins and a 100-oz silver bar, which are pictured



External Fraud

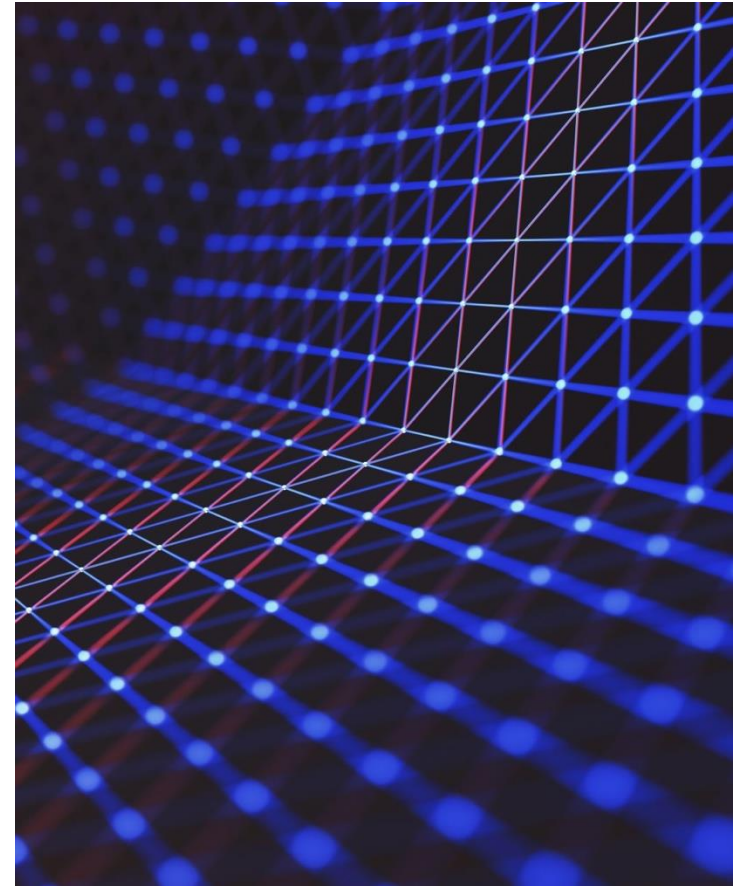
TN school district loses \$3.4 million to a fake vendor

Finance director received an email from someone posing as a rep from Pearson

Used pearson.quest instead of pearson.com email address

Finance director initiated 2 wire transfers

2 weeks later the bank alerted them of potential fraud activity



External Fraud



- Business Email Compromise (BEC) scam
- According to the FBI, BEC scams resulted in \$2.9 billion in losses in 2023
- New Haven school district lost \$6 million when hackers gained access to the school district COO's email account and monitored emails to vendors

EXTERNAL FRAUD

How do we prevent this sort of thing from happening?

- District personnel verify any changes with the vendor contact
- Use the contact in your financial system; not the name on the questionable invoice/form
- Review all the documents very carefully
 - Looking for spelling mistakes
 - Names changed just slightly
 - Different emails; sometimes one letter missing
- External email warning banners
- Require a PO and invoice for all payments, including wire transfers



P-CARD/ CREDIT CARD PROGRAM

Do you have internal controls in place for this?

Easier way to process payments and rebates for using the p-card program

Ensure every staff is responsible for uploading their own receipts into the system, ensure your finance area has oversight and they have processes in place to reconcile at payment time.

If you are looking to do a P-card process, you will need:

- P-card policy & Procedures Manual
- Purchasing card employee agreement
- P-card training (PowerPoint or in person) – we send it out twice a year



P-CARD FRAUDS:

- Employees using p-cards to purchase personal items
- Employees using p-card to purchase lunches without adequate documentation.
- Employees using p-card and having items shipped to alternate address than school
- Amazon- will set up accounts in which can be approved before order is placed at a central level.
- True credit card number compromise, seems to happen more around holidays than other times of the year for us
- We are watching the transactions daily; three people within finance have access to transactions and we are pulling transactions for surprise audit and addressing on a case by case basis. Most times end users aren't uploading requested documentation as set for in procedures.

Embezzlement

Former Finance Director

City of Homewood, Alabama

Embezzled \$950,000

From May 2023- March 2024

Tip regarding questionable Credit card transactions sparked a State Audit

Moved money from the City's bank account to a commercial bank account then to his own account by altering bank statements and falsifying journal entries

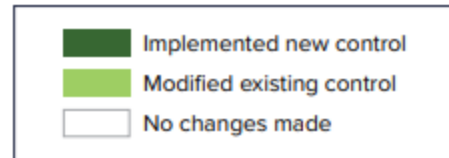
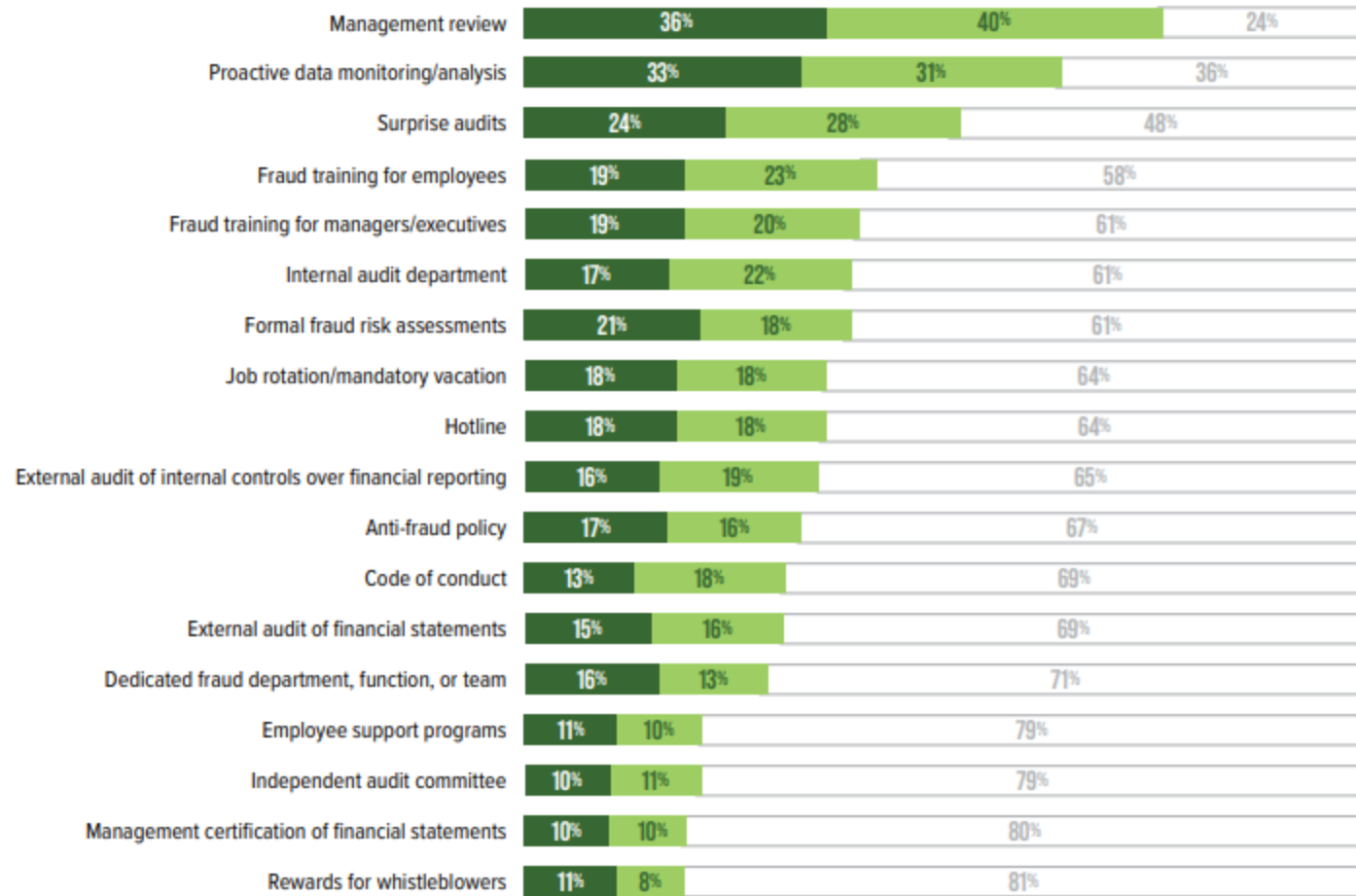


Embezzlement



- High School Athletic Booster Club President arrested on several charges including felony credit card fraud. (Hanover County, VA)
- President of the New Kent Girls Softball League arrested on one Count of Embezzlement-Misappropriation of funds.(New Kent County, VA)

FIG. 32 WHAT ANTI-FRAUD CONTROLS DID THE VICTIM ORGANIZATION MODIFY IN RESPONSE TO THE FRAUD?



RECAP: CHECK AND PAYMENT TAMPERING



The accounts payable clerk cannot also create/edit vendor records; segregation of duties



Require W-9, phone number, google some



Never pre-sign checks or use signature stamps



Control the check stock



Void check procedure

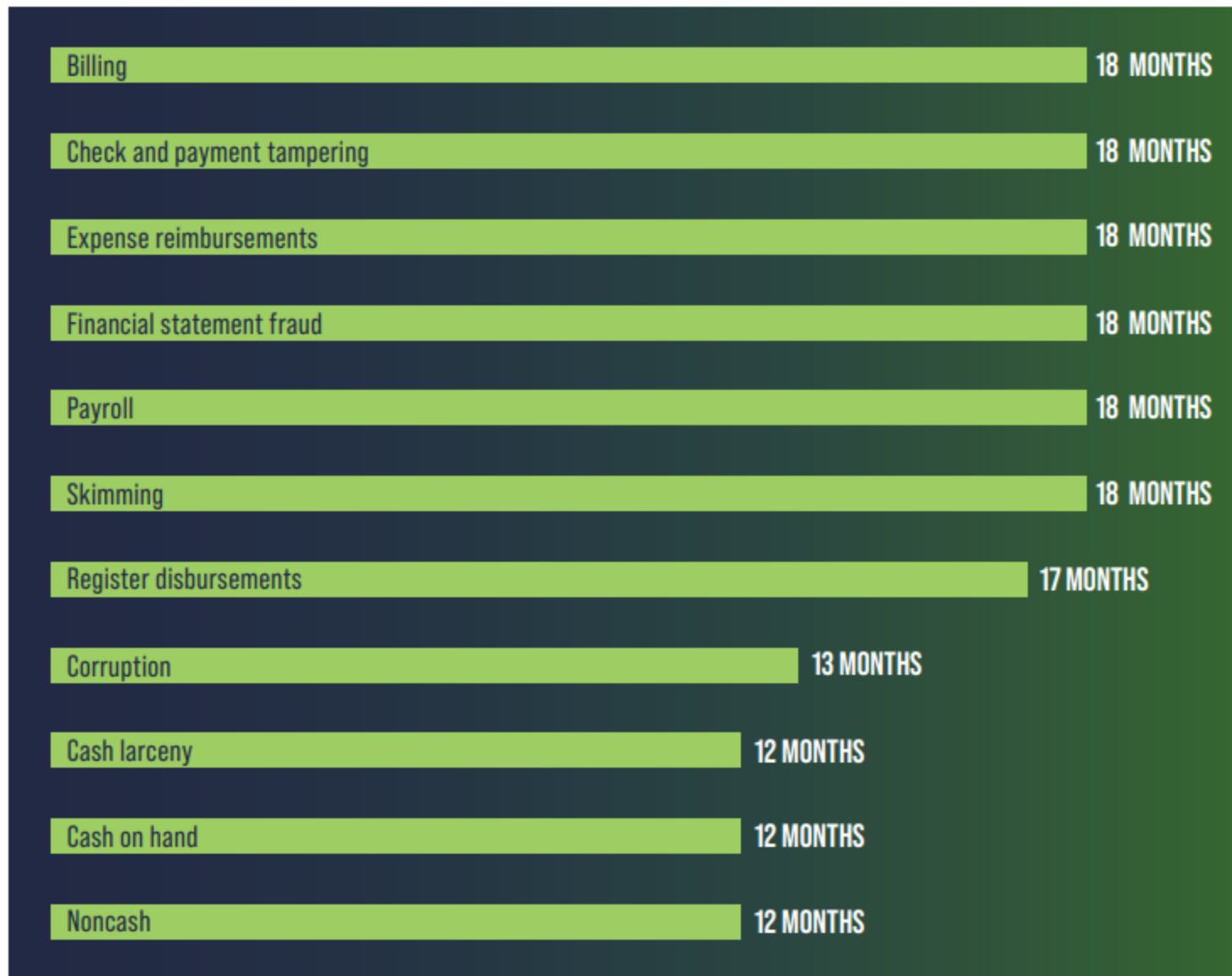


Rounded invoice amounts; amounts just below thresholds; acronym payees



Remit address/account changes; including ACH and ACI

FIG. 8 HOW LONG DO DIFFERENT OCCUPATIONAL FRAUD SCHEMES LAST?





Embezzlement

- Phoenix school district victimized by 2 budget specialists
- They deposited unauthorized checks into their personal accounts
- Falsified memo lines, forged signatures
- Falsified district accounting software to conceal the crime
- More than \$30,000

Embezzlement

- Orange County school district loses \$16 million
- Senior Director of Financial Services managed the district's fiscal operations; had access to school district bank accounts as well as student body bank account
- He wrote checks in small dollar amounts to "M S D" with extra spacing
- After getting proper signatures, he changed the amounts and payee names and deposited into his own account
- Falsified bank statements and records to conceal the theft

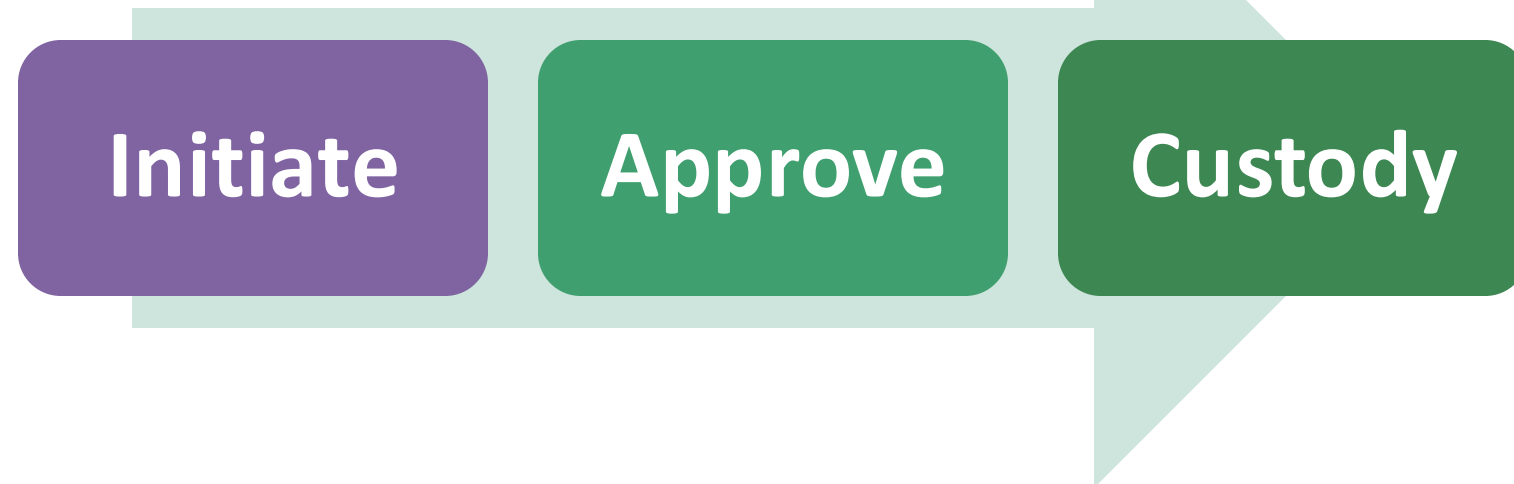


SEGREGATION OF DUTIES - DEFINED

No single individual should have control over two or more phases of a transaction or operation

No one individual employee can complete a significant business transaction in its entirety

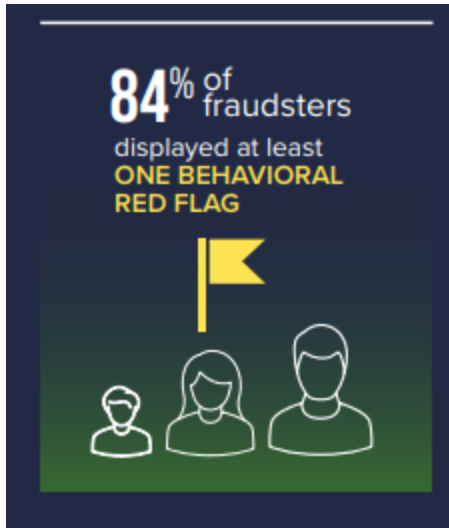
No one employee should be in a position to commit fraud and then conceal it





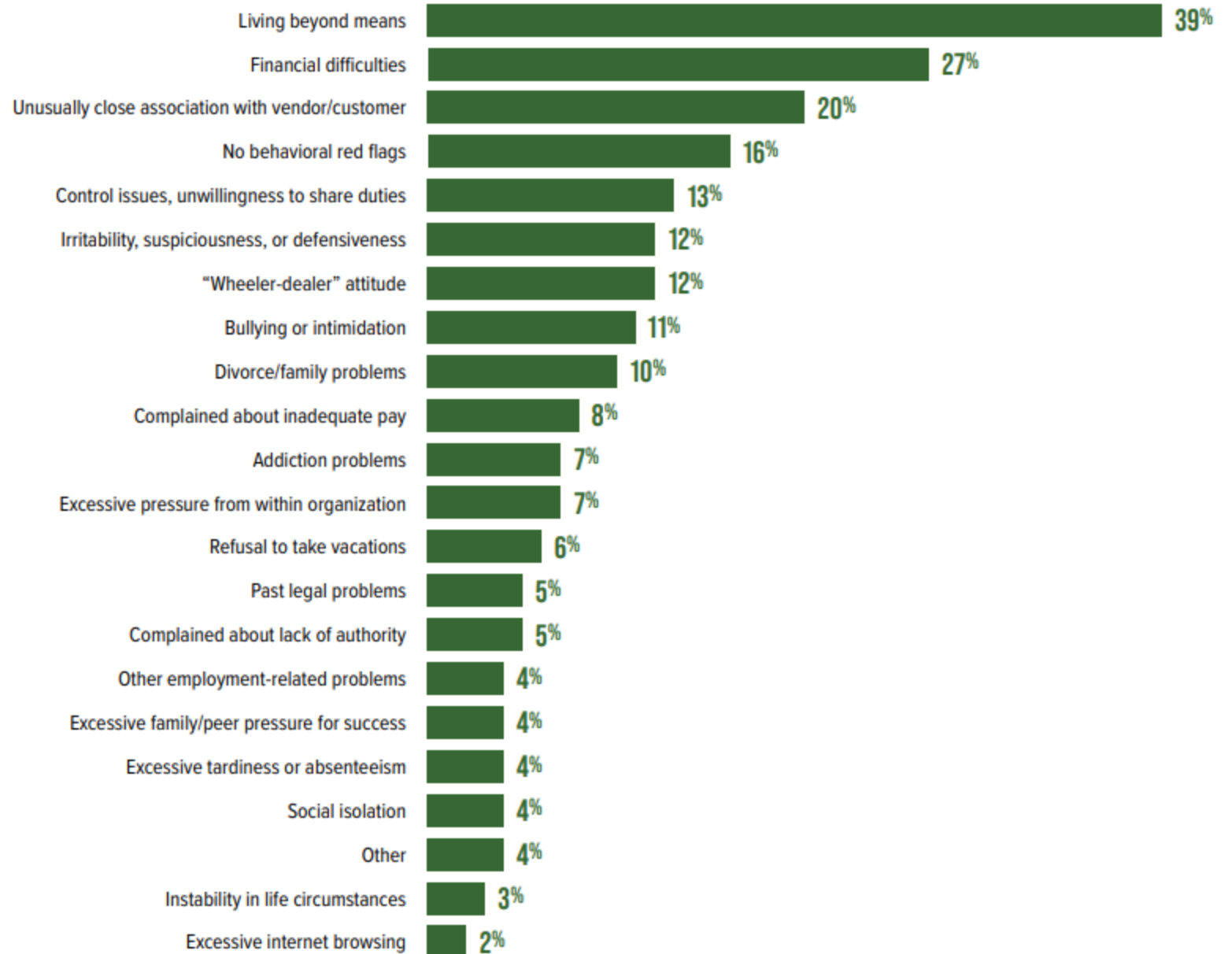
Payroll Fraud Prevention

- Person preparing the payroll should not also have access to add/activate employees; segregation of duties
- Analytical review of payroll
- Watch for bank account changes
- Procedure for changing pay rate
- Approval process for extra pay



OCCUPATIONAL FRAUD 2024:
A REPORT TO THE NATIONS®

FIG. 54 HOW OFTEN DO PERPETRATORS EXHIBIT BEHAVIORAL RED FLAGS?



RED FLAGS

How can we use this knowledge to design better internal controls?

Require cross training

Require mandatory vacations for key positions

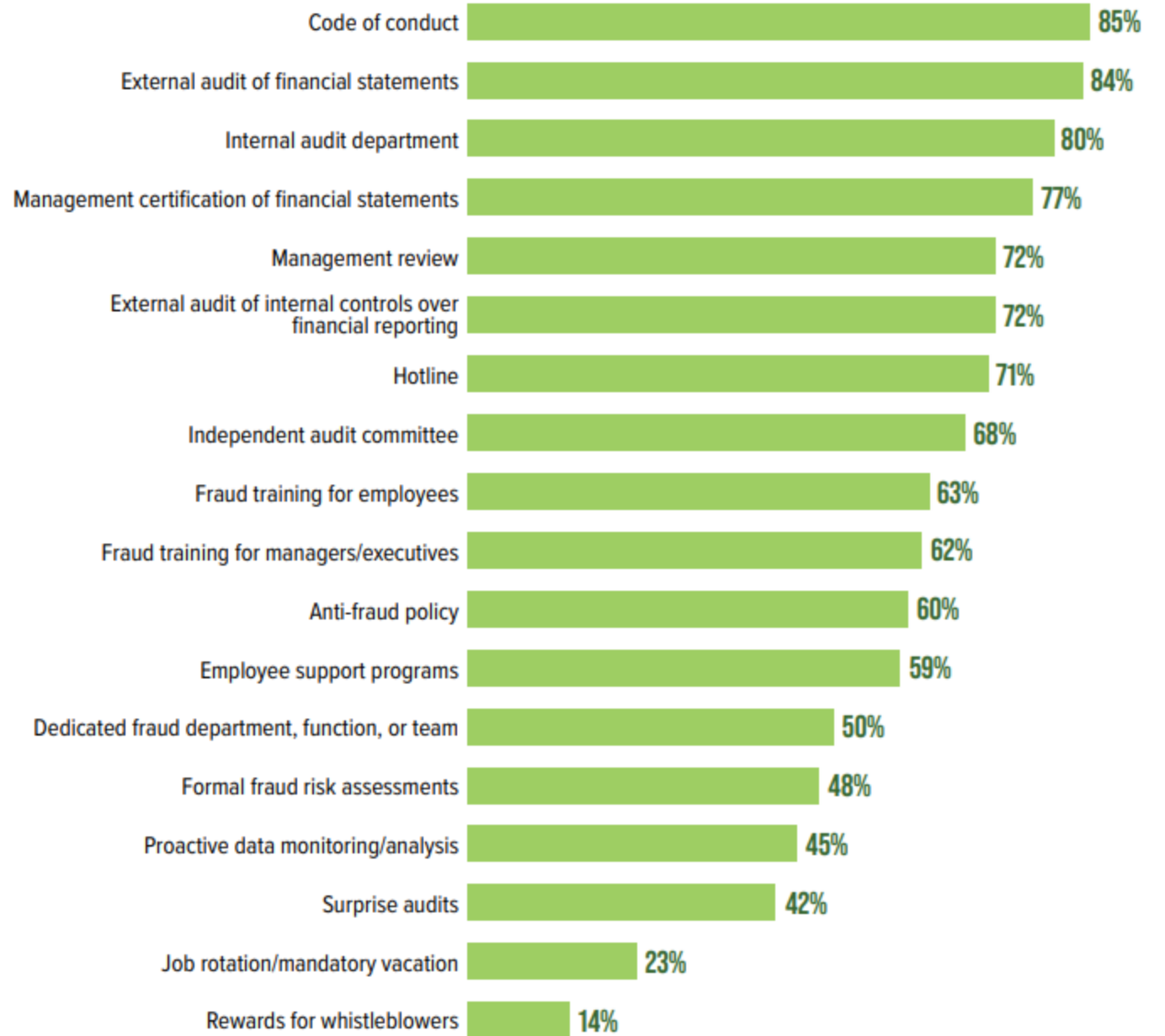
Bond key positions; background checks

PO approvals ahead of transactions

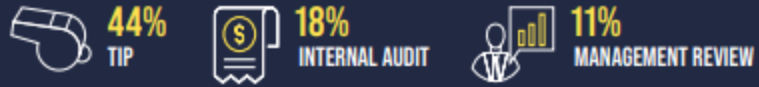
Observation, awareness

Run a ACH bank account file against your payroll bank account file and look for same account numbers.

FIG. 27 WHAT ANTI-FRAUD CONTROLS ARE MOST COMMON?



TOP 3 WAYS FRAUD IS DETECTED in government organizations:



Government organizations are **MUCH MORE LIKELY TO REFER CASES TO LAW ENFORCEMENT** for criminal prosecution than other organization types.

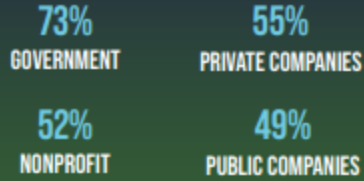


FIG. 13 HOW IS OCCUPATIONAL FRAUD INITIALLY DETECTED?

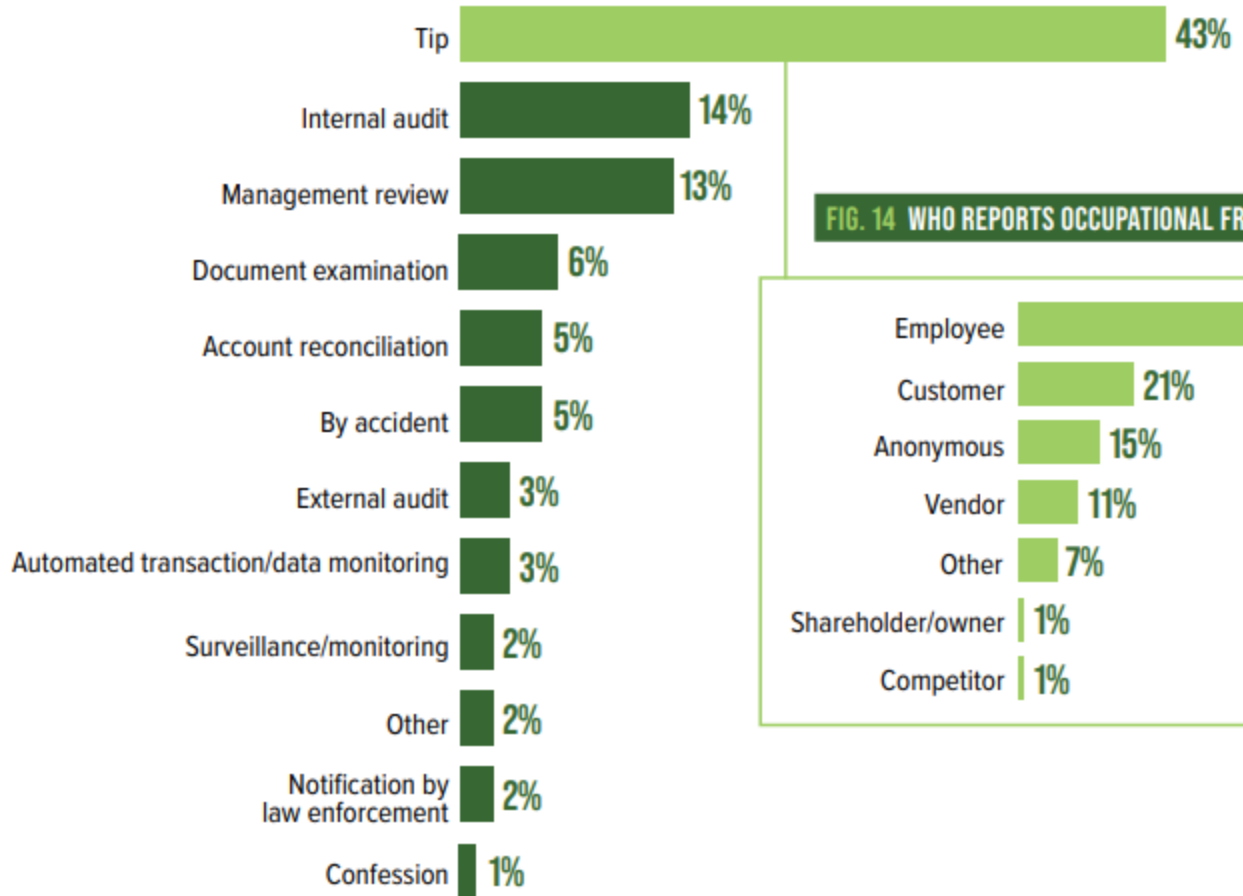
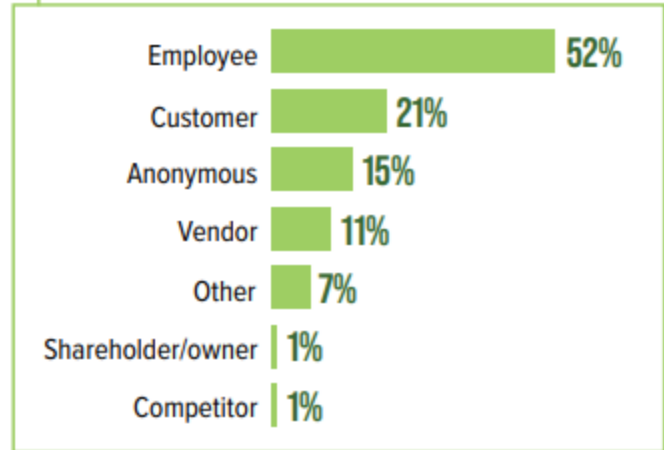


FIG. 14 WHO REPORTS OCCUPATIONAL FRAUD?



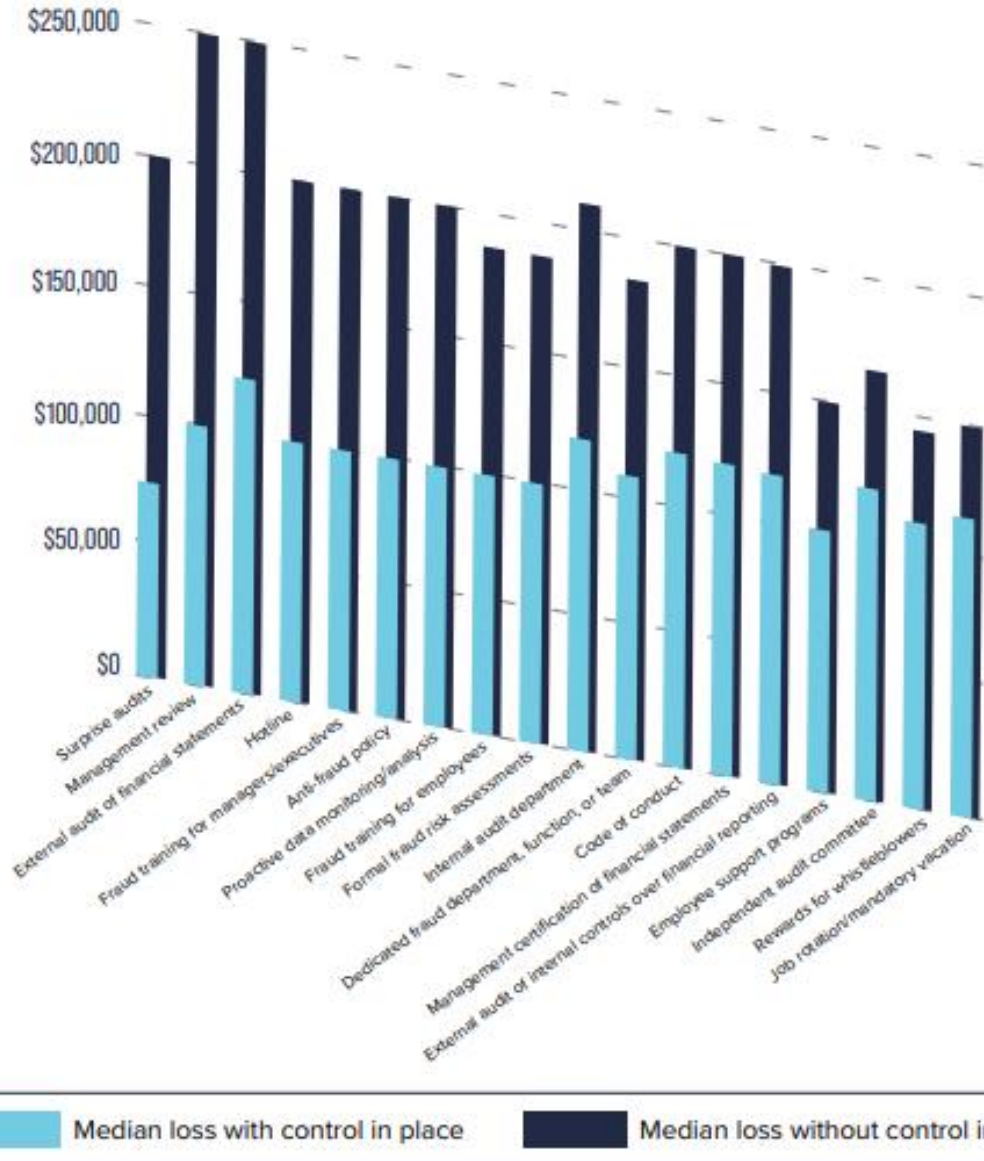
**The annual audit is not intended to
uncover fraud**



FIG. 28 HOW DOES THE PRESENCE OF ANTI-FRAUD CONTROLS RELATE TO MEDIAN LOSS?

Most effective controls:

- Management review
- Code of conduct
- Job rotation/mandatory vacation
- Hotline
- Surprise audits
- Proactive monitoring/analysis



Identifying Risk Areas

CASH

Are there incentives or pressures to steal?

Are management overrides allowed or possible?

Are there any red flags?

Where do opportunities exist?

Long-term, experienced staff

VERIFICATION STRATEGIES

Approvals



Supporting documentation

Purchases

Reimbursements

Refunds

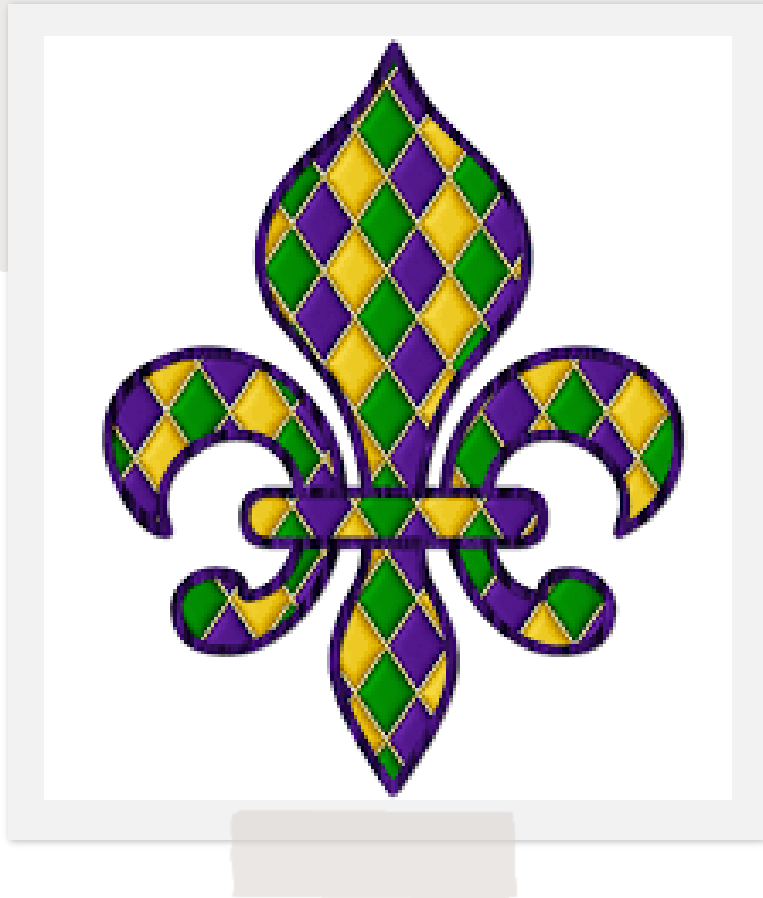


Employ professional skepticism

Does it make sense?

Does it look right?

Key Takeaways



- Recognize fraud can happen in your schools/district
- **Segregation of duties**
- Pre-approval of purchasing through purchase orders
- Cross training
- No management overrides; Tone at the Top
- Don't throw away protocol because of friendships or trust