Government Fraud, Waste & Abuse

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Agenda

- Fraud and Other Basics
- ACFE 2024 Report to the Nations
- Procurement Fraud and Red Flags
- Various Government Engagements, Expectations and Professional Standards

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Revisit the Basics

Fraud Basics

Tried and True Fraud Triangle - Pressure, Opportunity and Rationalization

Fraud Motivation – Motivation is not same for everyone! (Money, Ego, Entitlement, Ideology, Coercion)

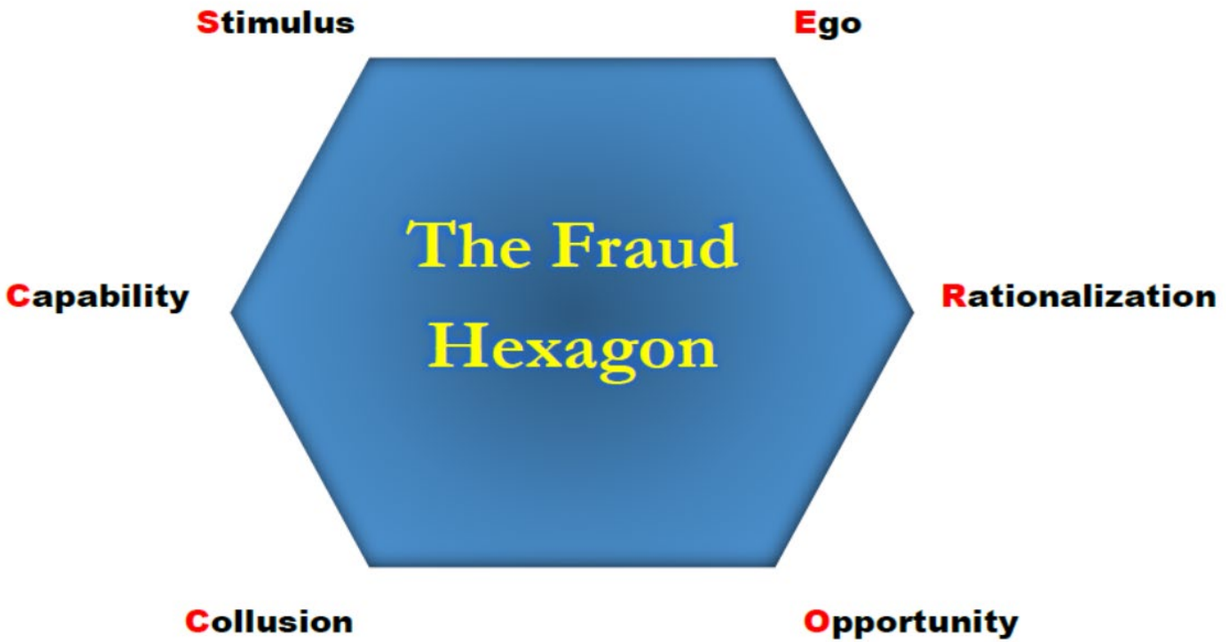
Accidental and Predator Fraudsters - More than one type

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Fraud Basics

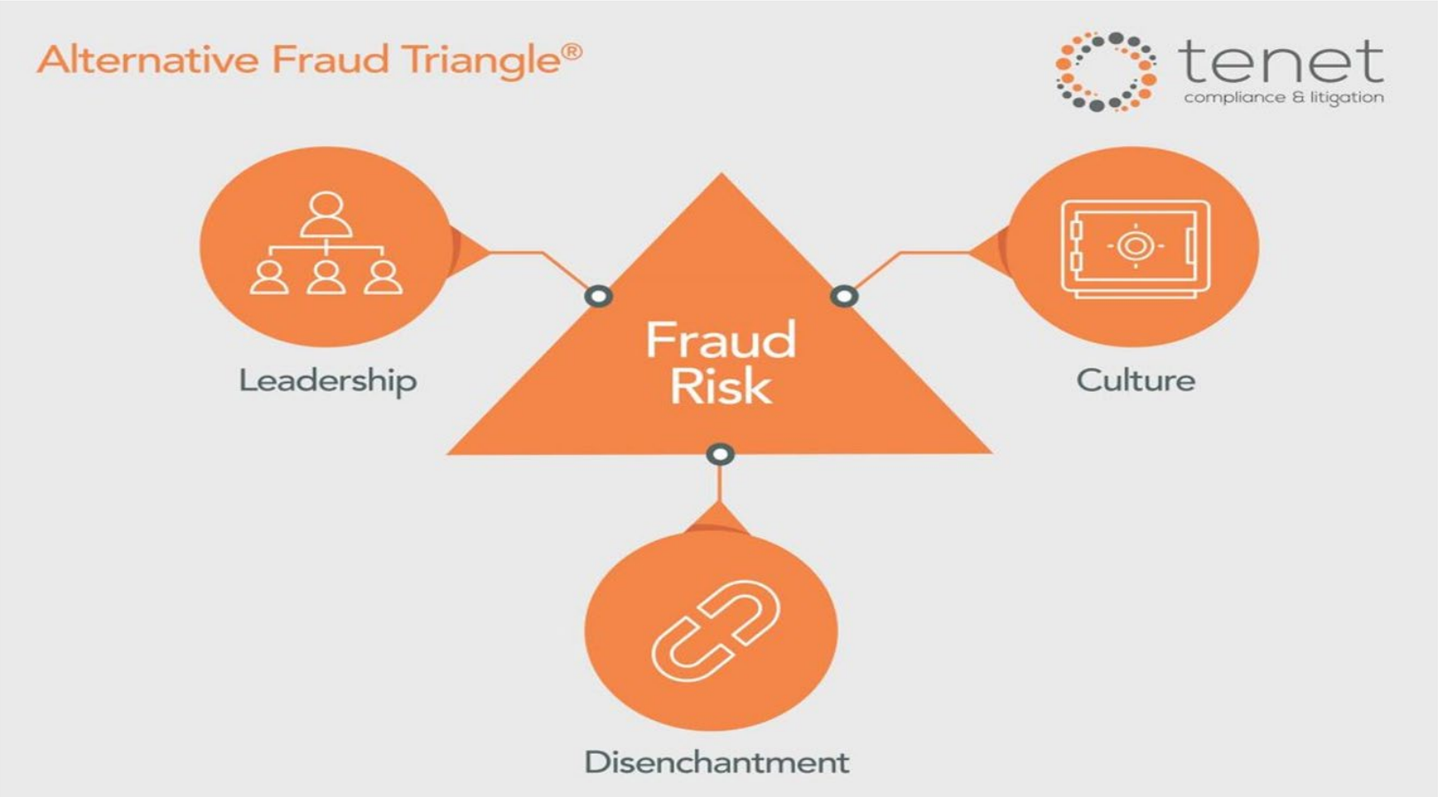
Figure 8: The Fraud Hexagon



Source - **Elaborating on the theory of fraud. New theoretical extensions by *Georgios L. Vousinas1***

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Fraud Basics



Source - **Beyond the 'red flags' – The Alternative Fraud Triangle by Arun Chauhan**

The Alternative Fraud Triangle by Arun Chauhan

Leadership – Essentially the point of this component to the alternative risk triangle relates to the theory of organization rot which occurs from the top down. The environment created by leadership either improves or reduces the risk of fraud.

Disenchantment – Stress and pressure in a working environment can lead employees to feel demotivated and undervalued. More disenchantment results in a higher the risk of fraud.

Culture – A small clique of disenchanted team members can demotivate entire teams and inculcate a toxic working culture thereby promoting a high risk of fraud. It's important to ensure your business' culture is working for your team so they remain engaged, motivated and are not inclined to carry out dishonest actions such as fraud.

Florida on Fraud, Waste and Abuse

F.S. 11.45 Defines

Fraud - means obtaining something of value through willful misrepresentation, including, but not limited to, intentional misstatements or intentional omissions of amounts or disclosures in financial statements to deceive users of financial statements, theft of an entity's assets, bribery, or the use of one's position for personal enrichment through the deliberate misuse or misapplication of an organization's resources.

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Florida on Fraud, Waste and Abuse

F.S. 11.45 Defines

Waste - means the act of using or expending resources unreasonably, carelessly, extravagantly, or for no useful purpose.

Abuse - means behavior that is deficient or improper when compared with behavior that a prudent person would consider a reasonable and necessary operational practice given the facts and circumstances. The term includes the misuse of authority or position for personal gain.

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Examples of Waste and Abuse

- North Miami Beach officials (including City Manager and 3 commissioners) racked up $1.4 million in unauthorized charges
  - 300K unexplained charges from 67 employees
  - One employee had 50K in food charges in only 19 months
- Misuse of position
- Use of state-run databases for personal use

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Public Purpose Concept

Public Purpose – A governmental action or direction that purports to benefit the populace as a whole. https://www.yourdictionary.com/public-purpose

Discussion examples of Public Purpose in Florida addressed by Florida's Attorney General's Office:

AGO 2002-18 – Bradford County BOCC submitted two questions; can public funds be used to assist a volunteer fire department in making payments for the purchase of a fire truck and donated to a NFP to help maintain a former school building that will be used by various community organizations, private parties and governmental entities

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Public Purpose Concept

Discussion examples of Public Purpose in Florida addressed by Florida's Attorney General's Office (continued):

AGO 78-101 – Jackson County PA attorney asked if a PA could expend $500 in public funds for the development and distribution of informational material explaining the operations of the PA office.

AGO 2006-12 – Town of Kenneth City requested an opinion regarding two issues; allowing homeowners associations and others the use municipal property at not cost for social functions and use public funds to pay for insurance coverage for the town and for organizations and others using municipal property.

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Public Purpose Concept

AGO 2002-18 Response – In both cases the fire truck funding and the donation were deemed to be for a valid purpose. Specifically, it was indicated that the donation be supported by the county commission determination that the county purpose was served, and safeguards implemented to assure the accomplishment of that purpose.

AGO 78-101 Response – "In considering a question involving the expenditure of public funds by a public officer, it is necessary to determine whether the officer in question has been expressly authorized by statute to expend funds for the purpose under consideration or must be considered to have been given such authority by necessary implication in order to carry out some duty or function expressly imposed or authorized by statute." Ultimate opinion was it was not an appropriate use of public funds.

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Public Purpose Concept

AGO 2006-12 Response – Use of public property would require the legislative body of the municipality to take official action in order to validate the use of municipal property by homeowners' association or others at no cost. Because based upon information submitted to AG the insurance purchased covers the City for liability as well as the event sponsors it would appear to serve a public purpose.

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ACFE 2024 Report to the Nations

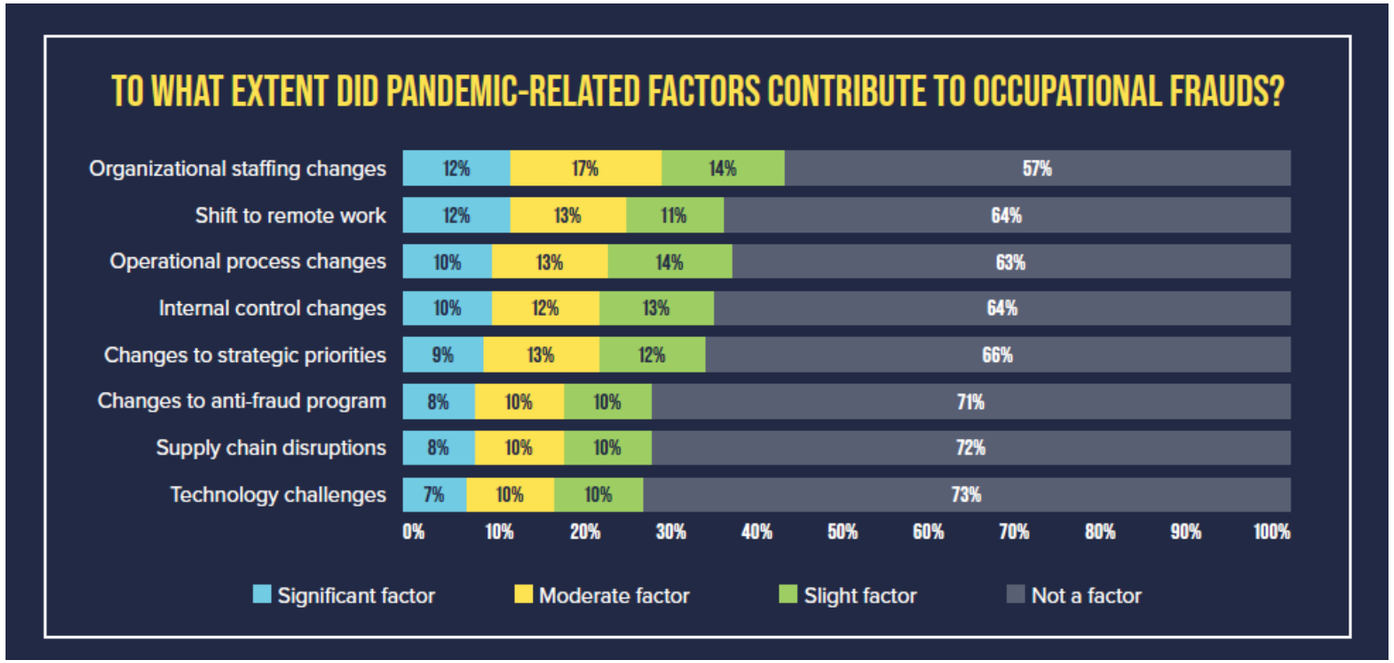
2024 ACFE Report to the Nations

- Study covered 1,921 (623 in US) cases from 138 countries and total losses in excess of $3.1 Billion
- Typical length of time for a case is 12 months at an average loss rate of $9,900 per month
- Median loss was $145,000 average loss per case was $1.7 million
- **43% of frauds were detected by a tip more than half of tips from employees! 3X more than other methods of detection**
- Reporting: web-based 40%, e-mail 37%, phone 30%

2024 ACFE Report to the Nations

Impact of COVID:

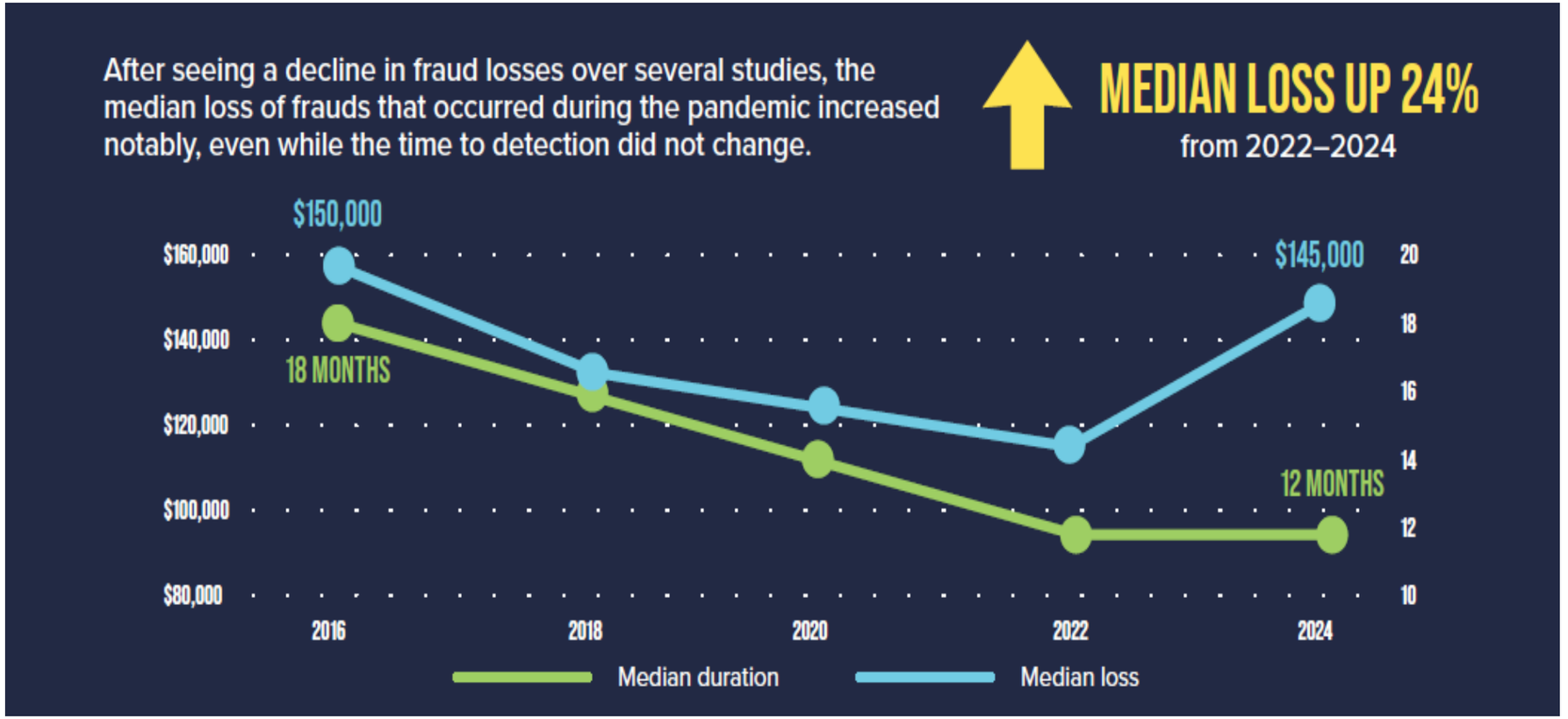
53% of cases had at least one pandemic-related factor contribute to the occurrence of fraud.



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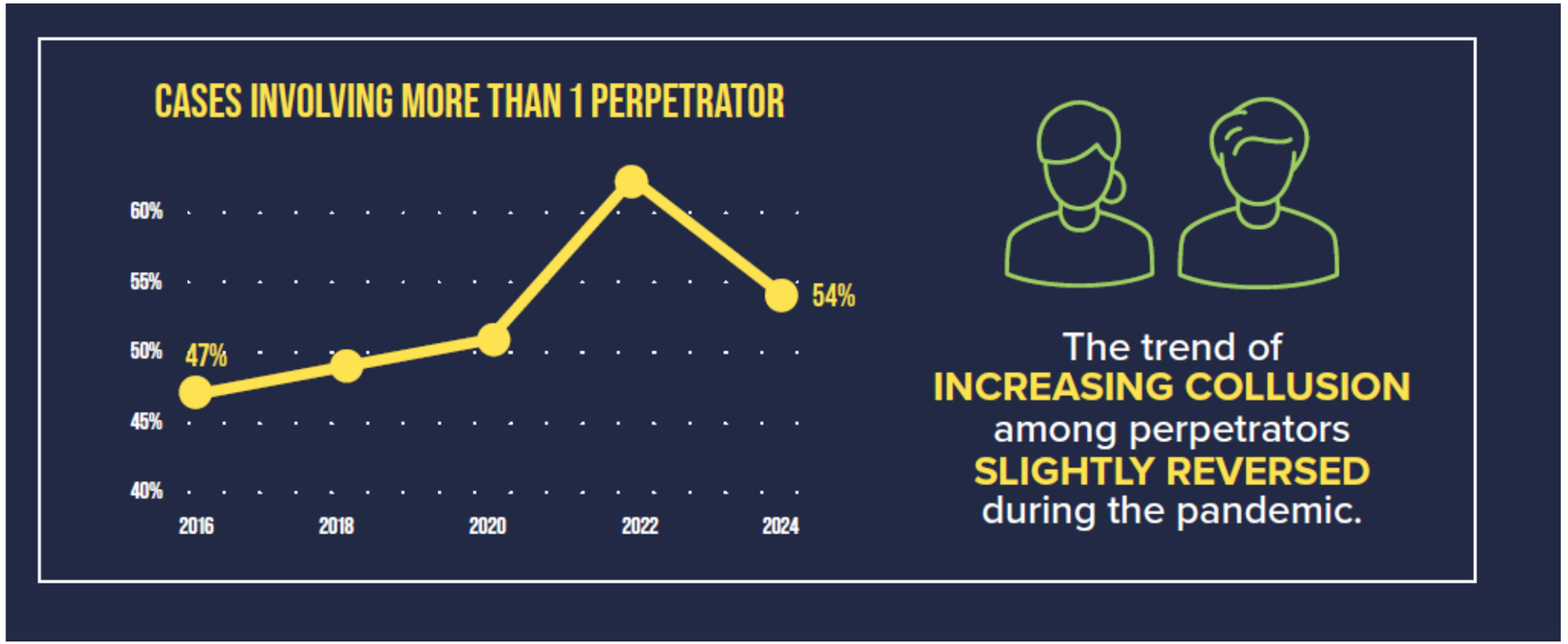
Impact of COVID:



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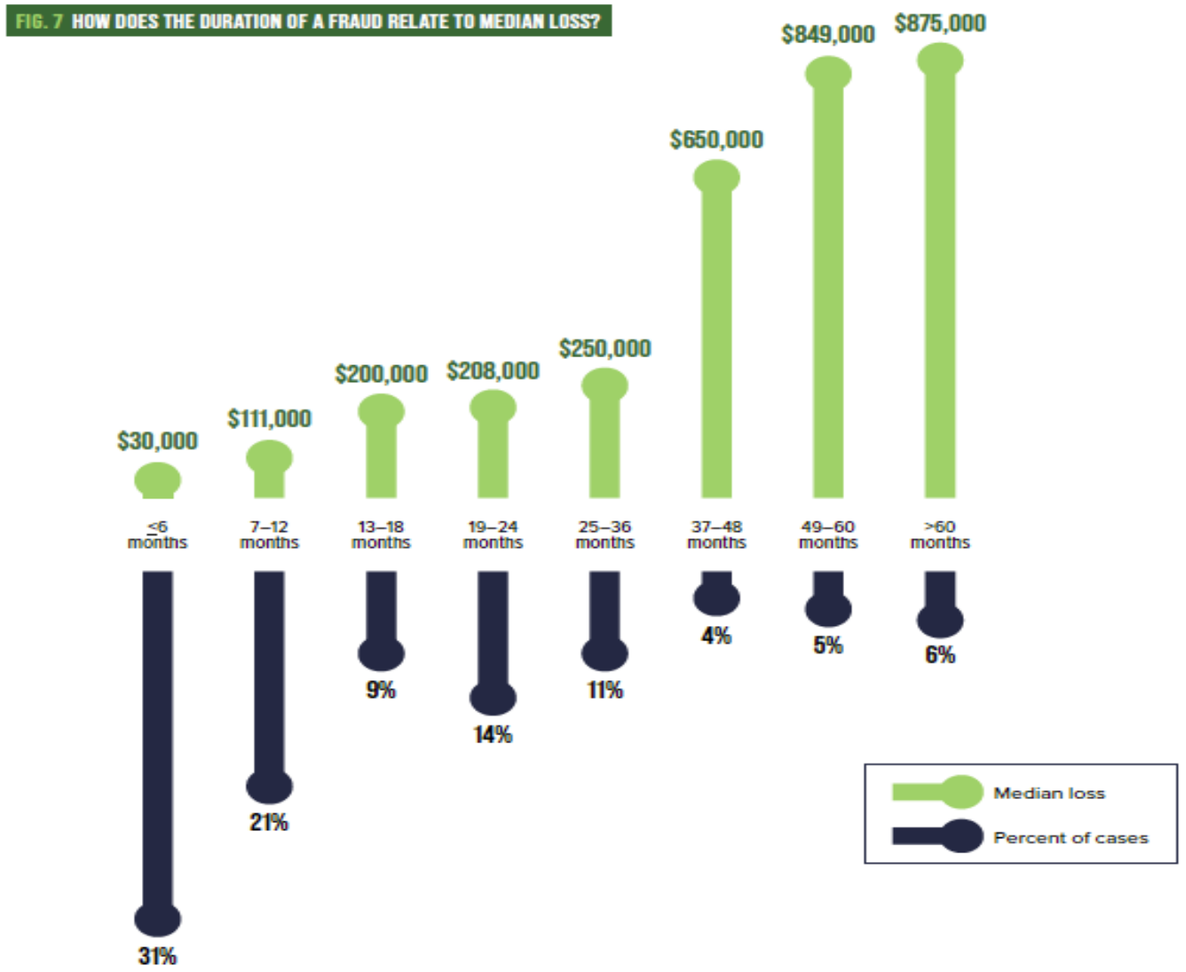
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Impact of COVID:



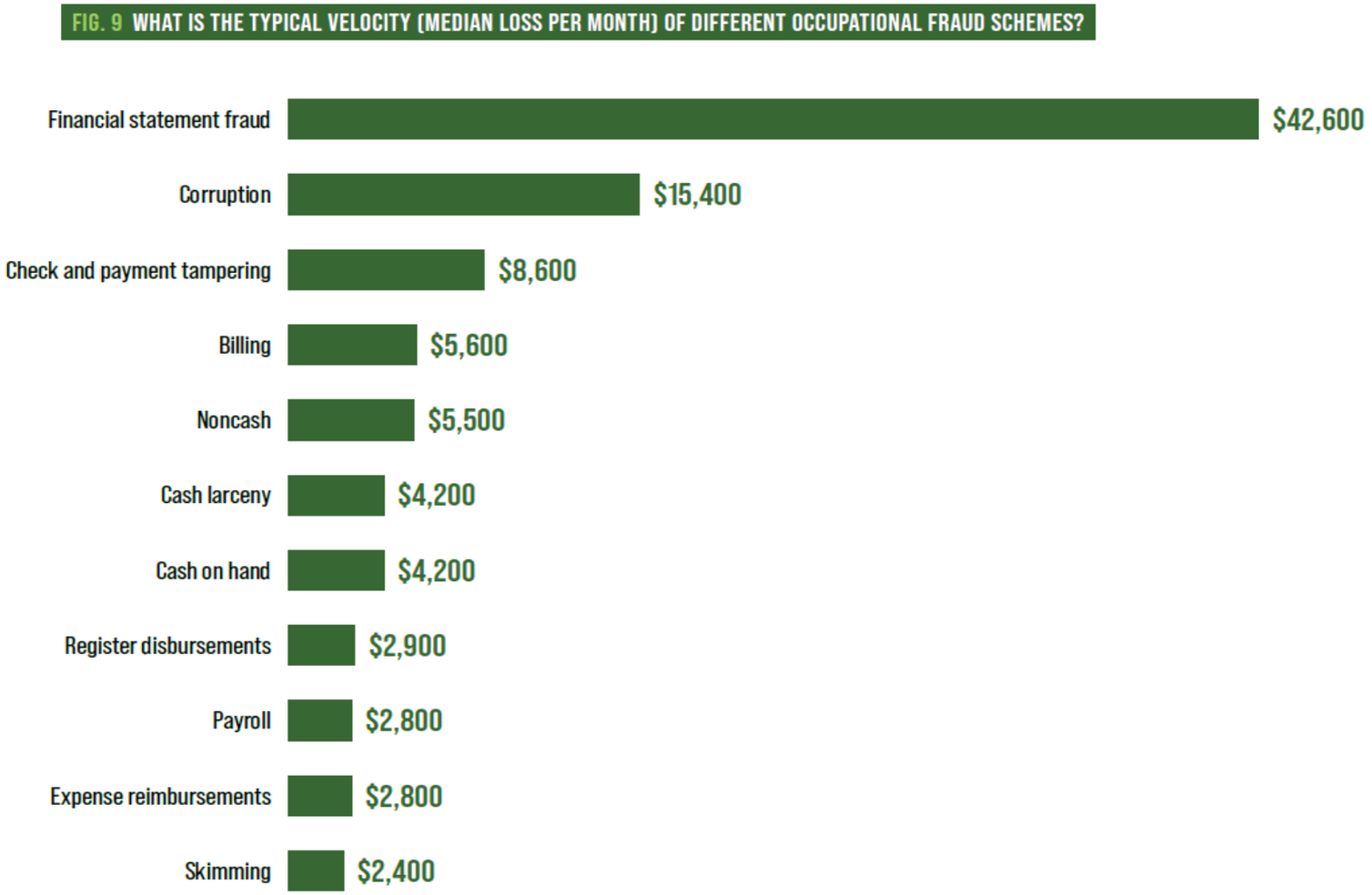
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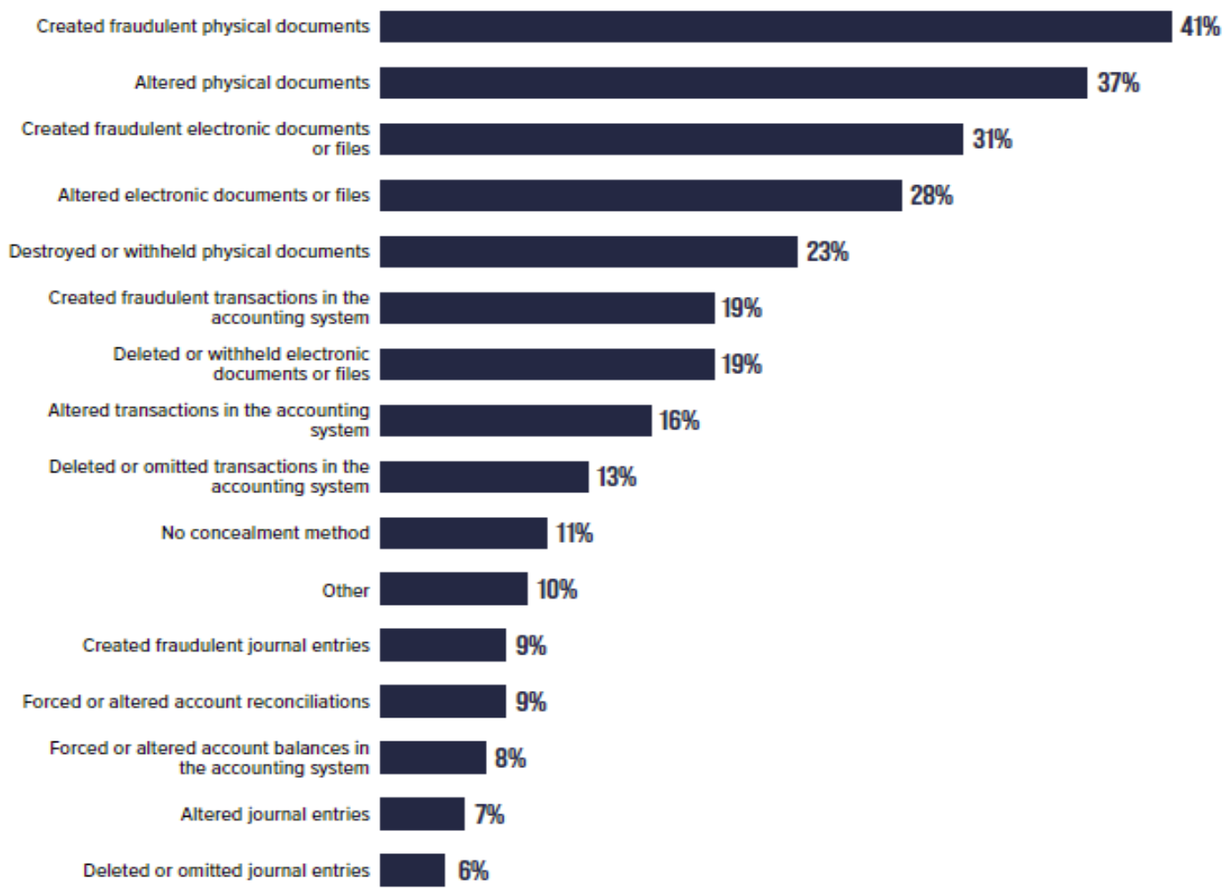
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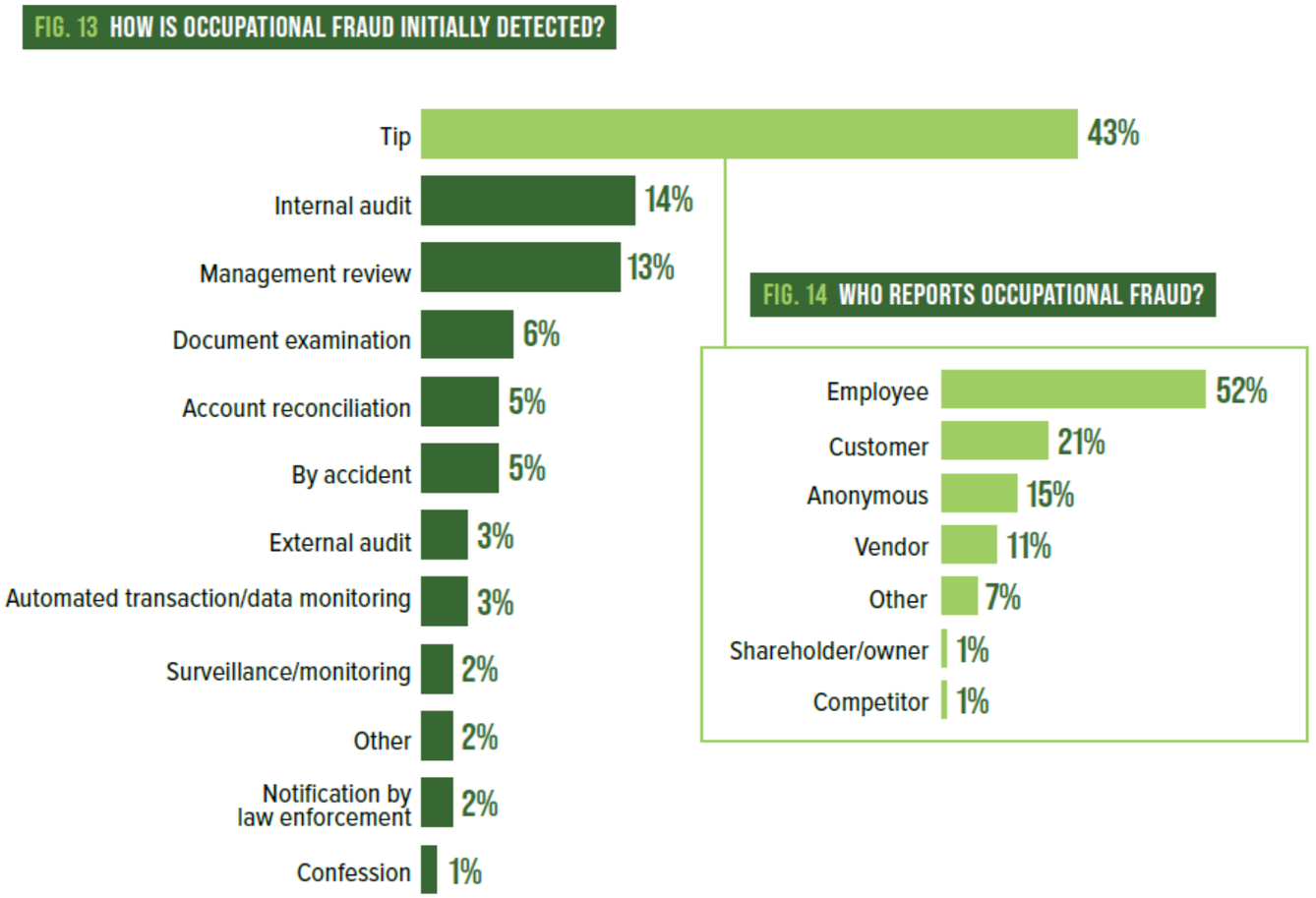
FIG. 10 HOW DO OCCUPATIONAL FRAUDSTERS CONCEAL THEIR SCHEMES?



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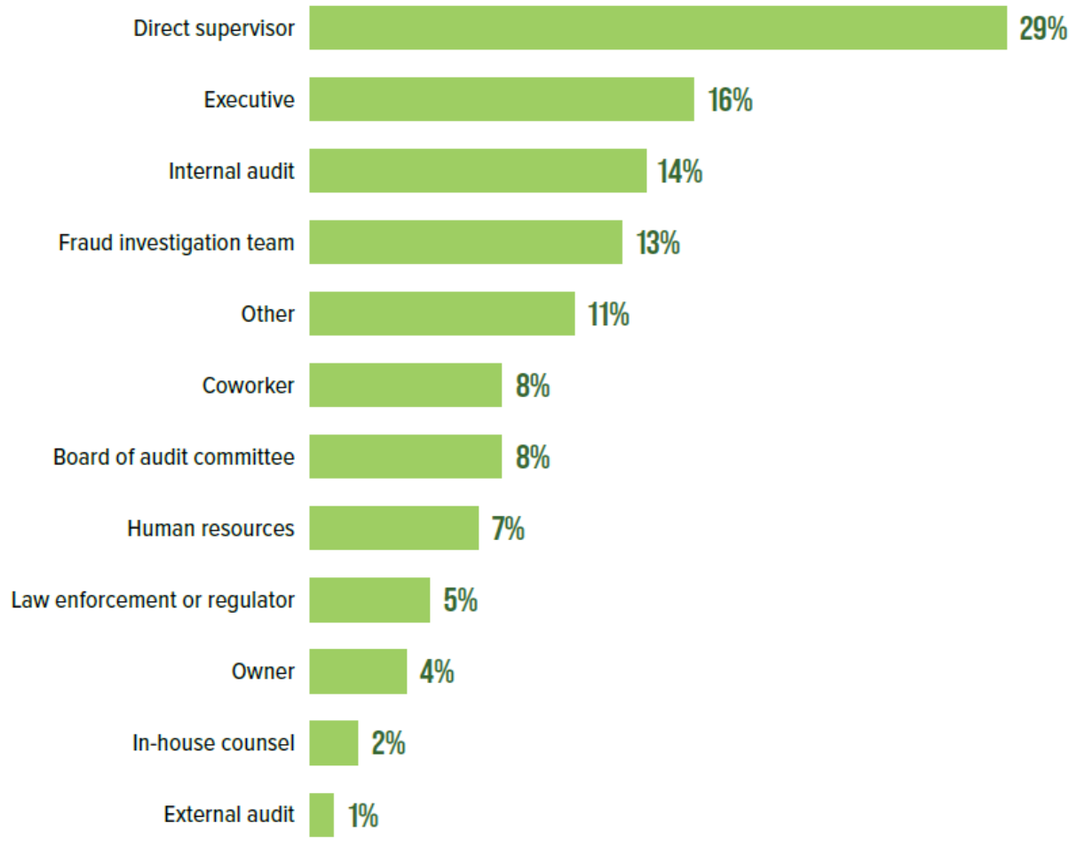
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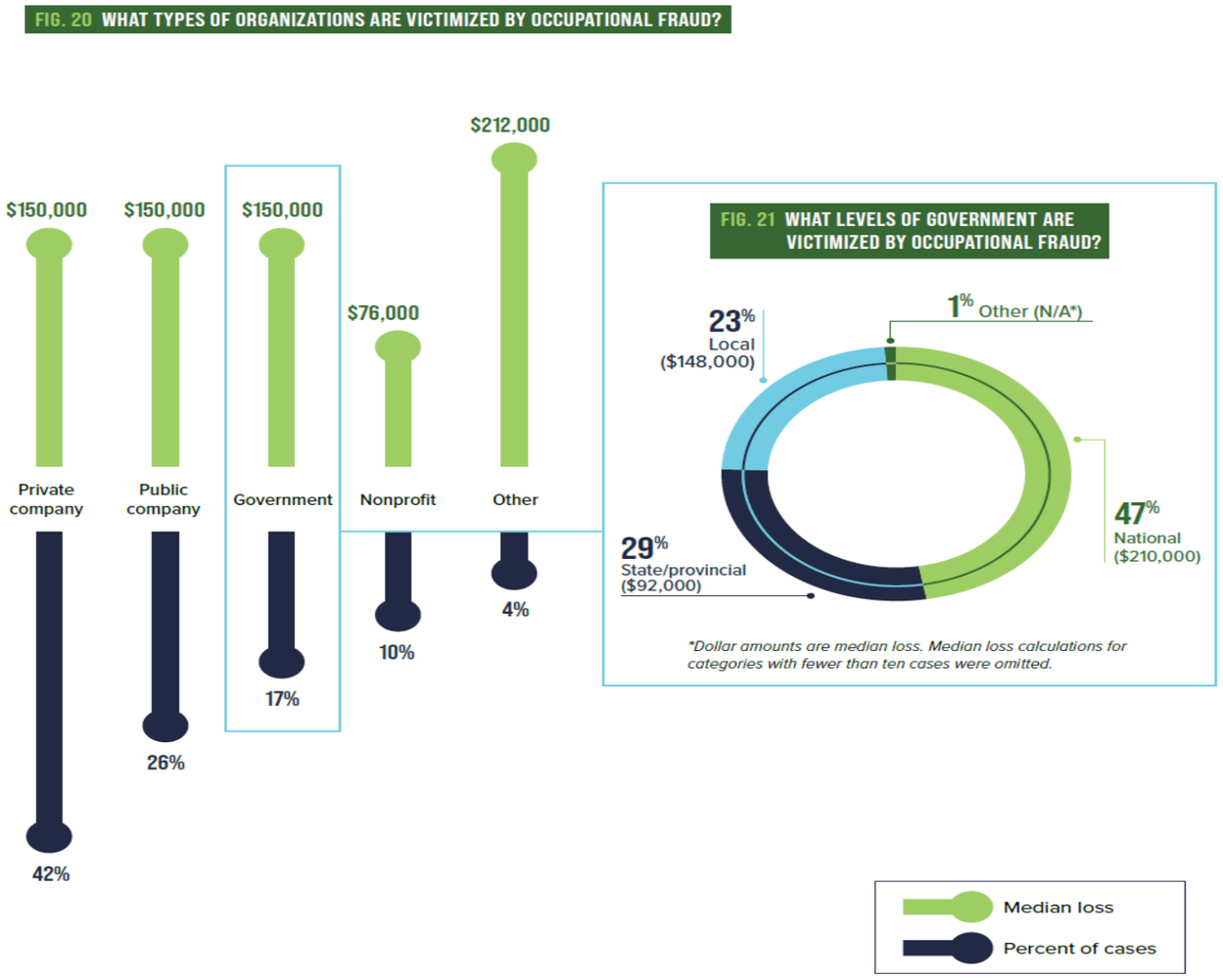
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FIG. 17 TO WHOM DID WHISTLEBLOWERS INITIALLY REPORT?



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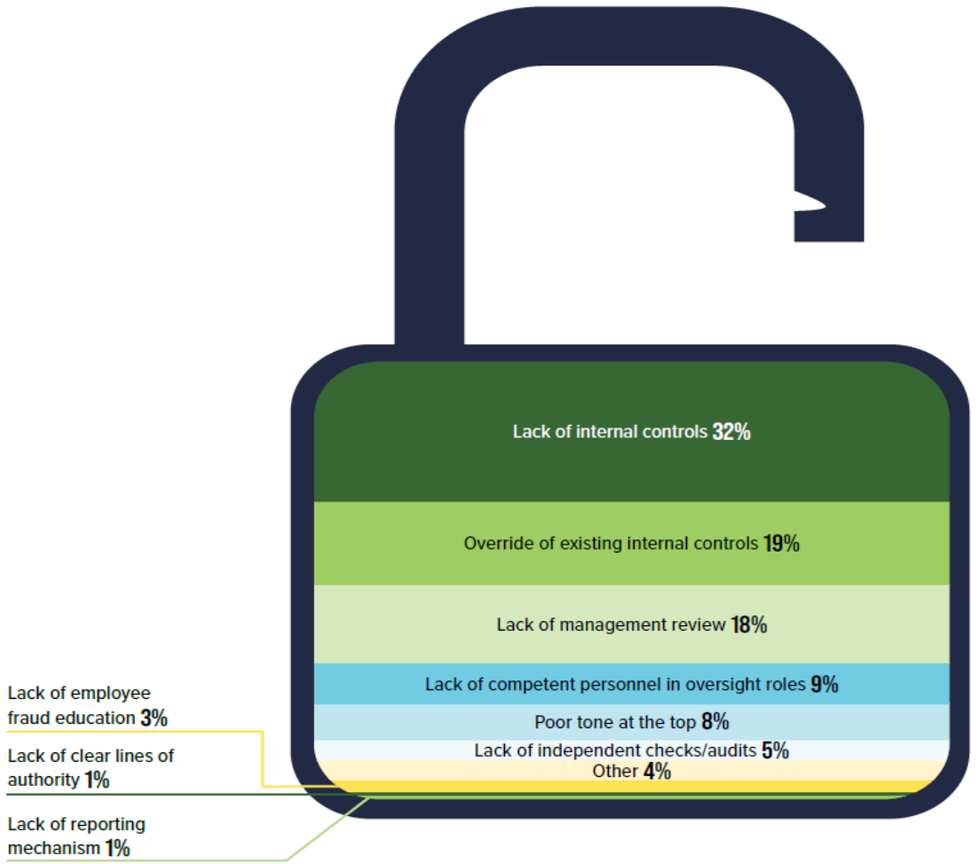
FIG. 22 HOW DOES AN ORGANIZATION'S SIZE RELATE TO ITS OCCUPATIONAL FRAUD RISK?



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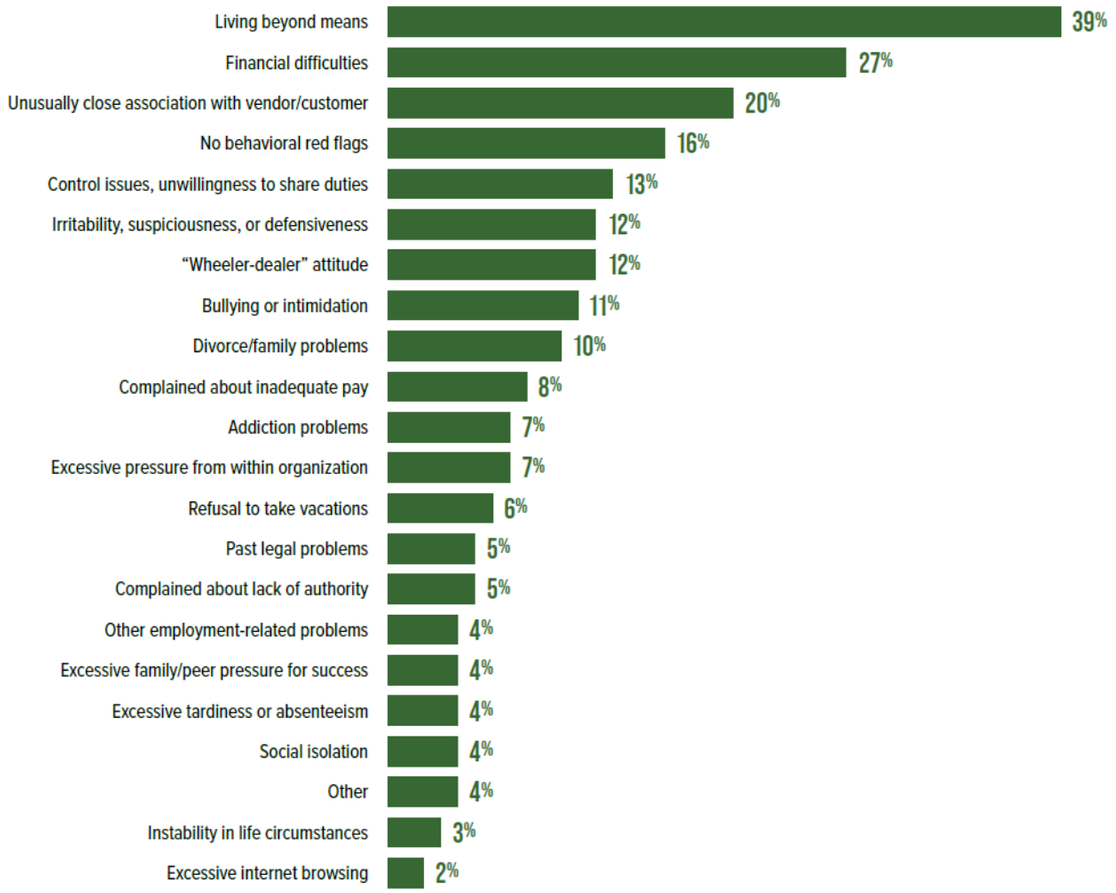
FIG. 37 WHAT ARE THE PRIMARY INTERNAL CONTROL WEAKNESSES THAT CONTRIBUTE TO OCCUPATIONAL FRAUD?



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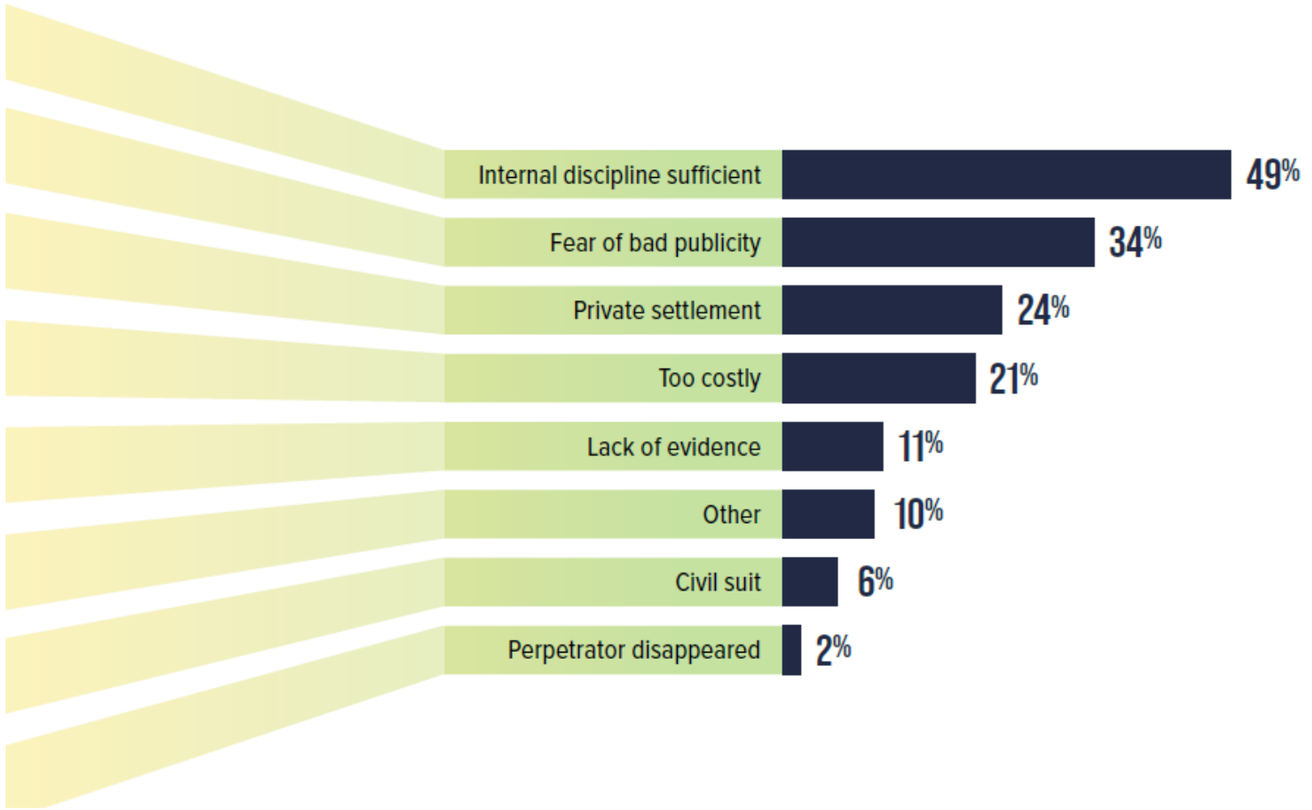
FIG. 54 HOW OFTEN DO PERPETRATORS EXHIBIT BEHAVIORAL RED FLAGS?



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FIG. 59 WHY DO ORGANIZATIONS DECLINE TO REFER CASES TO LAW ENFORCEMENT?



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Procurement Fraud and Related Red Flags

Procurement Frauds and Red Flags

Fictitious Vendor: an employee with procurement responsibilities, or in accounts payable, or an outsider, submit bills from a non-existent vendor. Normally, fictitious vendors claim to provide services or consumables, rather than goods or works that can be verified. Dishonest bidders also can submit “bids” from fictitious bidders as part of bid-rigging schemes.

Fictitious Vendor Red Flags:

- Paid vendors are not on the approved vendor list or listed in business or telephone directories
- Invoiced goods or services cannot be located or verified
- Inadequate vendor identification information
- Incorrect or non-existent address or phone number
- Vendor address or phone number is the same as an employee’s

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Procurement Frauds and Red Flags

Fictitious Vendor Red Flags (Continued):

- Small initial purchase from vendor, followed by much larger purchases
- Payment provided without an invoice
- Copied or unusual supporting documents, such as purchase order or receiving document submitted with invoice
- Multiple companies that have the same address/telephone numbers

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Procurement Frauds and Red Flags

Vendor Management

- Require approval for vendor changes, i.e., banking information
- Verification of change with vendor contact
- Consider issuing check after changing banking information
- Annual review of vendor list

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Procurement Frauds and Red Flags

Credit Card Fraud: Employees use an organization's credit card to make unauthorized purchases. Credit cards are sometimes used to circumvent procurement policies.

Credit Card Fraud Red Flags:

- Unreasonable or unexplained high volume of purchases from a particular vendor
- Split purchases without purchase order to avoid upper-level review or to circumvent the purchasing policy
- Receipts or invoices supporting purchases are missing or photocopied, which may indicate they were altered
- Receipts or invoices are not sufficiently detailed to document actual purchases

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Procurement Frauds and Red Flags

Credit Card Fraud Red Flags (Continued):

- Lack of proper approvals and/or separation of functions, such as requiring manager approval prior to purchase, cardholder makes the purchase, and an independent person receives the purchase
- Vendor used excessively by only one cardholder
- Purchases made during weekends or holidays which are outside of cardholder's or organization's work schedule period

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Procurement Frauds and Red Flags

Split Purchases: Single procurement split into two or more purchase orders or contracts, each below upper-level review or competitive bidding thresholds, to avoid review or competitive selection. Repetition of this scheme, favoring the same parties, can be a strong indicator of corruption.

Split Purchases Fraud Red Flags:

- Two or more similar procurements from the same supplier in amounts just under competitive bidding or upper-level review limits
- Unjustified separation of purchases, e.g., separate contracts for labor and materials, each of which is below competitive bidding limits, but when combined is over such limits
- Sequential purchase orders or invoices under upper-level review or competitive bidding limits
- Contracts under the competitive bid limit followed by change orders that increase amount of the contract

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Procurement Frauds and Red Flags

Conflict of Interest: Conflicts of interest can arise if procurement personnel have undisclosed interests in a supplier or contractor, accept inappropriate gifts, favors or kickbacks from vendors, or engage in unapproved employment discussions with current or prospective contractors or suppliers. Kickbacks can be prosecuted as a conflict of interest, as well as bribery.

Conflict of Interest Fraud Red Flags:

- Unexplained or unusual favoritism of a particular contractor or vendor
- Contracting or purchasing employee lives beyond means
- Close socialization, acceptance of inappropriate gifts, travel or entertainment from a vendor
- Procurement employee appears to conduct side business

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Procurement Frauds and Red Flags

Change Order Abuse: Contractor acting alone or in collusion with contract personnel, can submit unjustified or inflated change order requests to increase profits, or, as a result of corruption, use the change order process to extend a contract that should be re-bid

Change Order Abuse Red Flags:

- Weak internal controls and procedures regarding review or need for change orders
- Numerous, unusual or unexplained change orders for a specific contractor approved by the same employee
- Pattern of low-bid award followed by change orders that increase the price or scope of the contract, or extend the contract period
- Vague contract specifications followed by change orders

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Procurement Frauds and Red Flags

Change Order Abuse Red Flags (Continued):

- Poorly documented change orders, or change order requests in round number amounts, if that is unusual for the job
- Pattern of change orders just below upper-level approval limit
- High-level personnel involved in change order decisions, especially for specific contractors
- Purchase orders of contracts extended by change order, rather then re-bidding of contract

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Procurement Frauds and Red Flags

Co-Mingling of Contracts: Dishonest contractors submit multiple bills on different contracts or work orders for work performed or expense incurred only once. A contracting official can facilitate the scheme and share in the profits by writing similar work orders under different contracts and accepting the multiple billings.

Co-Mingling of Contracts:

- Contractor submit several billings for the same or similar expenses or work under different contracts
- Contractor submits the same or similar documentation support billings on different contracts
- Multiple awards for similar work are given to the same contractor
- Similar work orders are issued to the same contractor under more than one contract

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School Supply Scam

Detroit Public Schools (DPS) Supply Scam

- Involved 12 principals, assistant superintendent and vendor
- Scheme began in 2002 and continued until January 2015
- DPS principals had the primary authority for selecting vendors from a list approved by DPS and for certifying that invoiced goods were received
- Vendor received approximately $2.7 million from DPS based on payment for fraudulent invoices
- Principals accepted bribes and kickbacks totaling approximately $909,000

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Laurens School District Waste & Abuse

A Laurens County school district spent nearly $1 million more than it should have on expenses like food, travel and gift cards over the past four years, according to a report from the state Office of Inspector General:

- Unnecessary expenses, often originating from questionable record-keeping and policy loopholes
- Stanley stainless steel tumblers, steak dinners and electronic picture frames were among expenses charged to an account intended for student meals
- Laurens County staff used $12,600 to pay for birthday meals and end-of-year dinners at sit-down restaurants
- Staff members spent $8,500 on gift cards and giveaways

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Laurens School District Waste & Abuse

- The district reimbursed employees for over $36,000 worth of expenses that did not follow district policy, such as trips taken without the proper approvals
- “With rare exception, anything received by the Finance Department was reimbursed to the employee without question or ensuring compliance” with the district’s policies
- Overspending on hotels and lodging
- Investigators also found “a general culture and expectation of providing food at meetings,” adding up to more than $201,700 over four years for staff meals.

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Various Government Engagements, Expectations and Professional Standards

Introduction – Why Discuss Engagements?

- Central Florida City advertises for Forensic Audit
- New Commission in Texas Forensic Audit - “Is everything on the up and up?”
- Derby CT. - Vote to conduct a Forensic Audit
- Marion OH. - City Council approves extra $20,300 for forensic audit services.

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Engagements

Attestation Engagement - CPA is engaged to issue or does issue an; examination, review, agreed-upon procedures, on subject matter, or an assertion about the subject matter, that is the responsibility of another party. AICPA Attestation Standards (SSAE)

Audit – covered by AICPA Audit Standards (SAS)

Accounting and Review Services – covered by AICPA standards on accounting and review services (SSARSs)

Consulting – covered by AICPA standards for consulting services (SSCS)

Engagements *(Cont.)*

Government engagements - undertaking an engagement for the benefit of a government comes with additional responsibilities such as Statutes, rules, and regulations, etc. CPAs are obliged to follow the applicable governmental requirements as well as the applicable AICPA attestation standards. Examples of such requirements include:

FL BOA 61H1
FL Single Audit Act
Rules of FL Auditor General – Local Govt. 10.550, 10.650 and 10.800
Uniform Guidance
Yellow Book

Engagements *(Cont.)*

Standards and Expectations of Government Engagements (No matter the type)

- Planning
- Documentation
- Competency
- Independence/Integrity of mind when performing the engagement
- Wrap up and reporting

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Engagements *(Cont.)*

Are engagements optional or required?

- Financial Statement Audits?
- Single Audit – Federal and/or State?
- Attestation Engagements?
- Performance audits?
- Internal Audits?
- Other?

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Factors Impacting the Need and Type of Engagement

Factors Impacting the Need and Type of Engagement

Legal/Compliance

Public Perception

Change over in key personnel, management or governance

Need to evaluate operations, policies or procedures

Identification of fraud, waste or abuse

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Factors Impacting the Need and Type of Engagement *(Cont.)*

What type of engagement does a government need?

- Mandated (legal or compliance)
- Will the engagement restore trust
- Will the engagement address the need
- Cost

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What my friends think I do



What my date's parents think I do



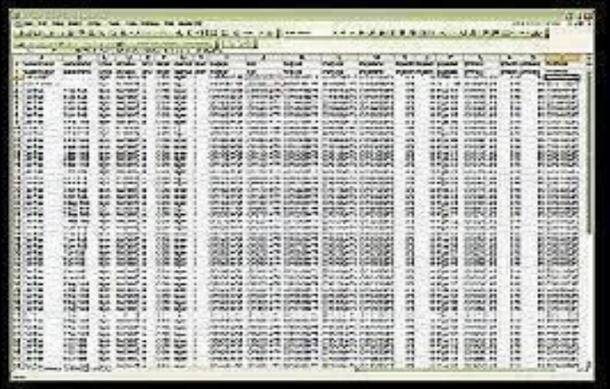
What society thinks I do



What my parents think I do



What I think I do



What I actually do



Forensic Engagements

Forensic Engagement

ACFE - Fraud Examination and Forensic Accounting

Forensic Accounting is the use of professional accounting skills in matters involving potential or actual civil or criminal litigation. Therefore, forensic accounting is litigation support involving accounting.

Accordingly, many fraud examinations can be considered forensic accounting, but not all forensic accounting is fraud examination.

Although accountants and non-accountants can conduct fraud examinations, only accountants can perform forensic accounting work.

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Forensic Engagement *(Cont.)*

AICPA – Standards of Forensic Services (SSFS)

The term forensic is defined as “used in, or suitable to, courts of law or public debate.” Forensic accounting services generally involve the application of specialized knowledge and investigative skills to collect, analyze, and evaluate certain evidential matter and to interpret and communicate findings.

Forensic services consist of either litigation or investigation engagements. When and engagement meets the definition above SSFS standards apply.

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Forensic Engagement *(Cont.)*

Considerations of a fraud or forensic accounting engagement

- What is assumed purpose of the engagement
- What level of knowledge does the investigation or audit team need
- Consider that the engagement can start out as one thing and become another
- Know how and for whom the report will be written

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Forensic Engagement *(Cont.)*

ACFE – Fraud Examination Methodology

- ✓ Assume litigation will follow
- ✓ Act on predication
- ✓ Approach investigations from two perspectives
- ✓ Begin with general before moving to specific
- ✓ Use the fraud theory approach

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Forensic Engagement *(Cont.)*

ACFE – Fraud Examination Methodology *(Cont.)*

Assume litigation – this is to ensure the fraud examiner maintains compliance with the rules of evidence and remains within the guidelines of established legal system.

Act on predication – totality of circumstances would lead a reasonable, professionally trained, and prudent individual to believe that a fraud has occurred, is occurring or will occur. If an examiner cannot articulate a factual basis or good reason for an investigative step then they should not do it. This is a continual process throughout the investigation and its purpose is to minimize the potential of liability to themselves or their client.

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Forensic Engagement *(Cont.)*

ACFE – Fraud Examination Methodology *(Cont.)*

Approach investigation from 2 perspectives – 1.) Seek to prove that fraud has occurred and 2.) Seek to prove that fraud has not occurred

Begin with general and move to specific – examinations should begin with general information that is known and then transition to details. Ex. Doing interviews of people suspected of being less(not) involved (but with knowledge) to witnesses who appear to be more involved.

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Forensic Engagement *(Cont.)*

ACFE – Fraud Examination Methodology *(Cont.)*

Use the fraud theory approach – This approach involves the following steps:

- Analyzing available data
- Creating a hypothesis
- Testing the hypothesis
- Refining and amending the hypothesis

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QUESTIONS?????