

# Preventing Financial Waste, Fraud, & Abuse

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# Federal Regulations: Designed to Prevent

- **Fraud**
- **Waste**
- **Abuse**

# And Yet....Fraud Happens...

- **In Head Start**
- **In Community Action**
- **In Human Services**
- **In government**
- **In every type of business entity**

# 3 Types of Fraud Risks

- **Misappropriation**
- **Misstatement**
- **Corruption**

# Misappropriation

- **Stealing funds, equipment, or other assets**
- **Misusing assets**

# **3 Common Misappropriation Frauds**

- 1. Ghost employees**
- 2. Improper travel & entertainment expenses**
- 3. Employment tax manipulation**

# Misstatement Fraud

**Issuing financial statements or other reports that misrepresent the organization's financial condition, program performance, or compliance with law & regulation**

# Common Misstatement Frauds

- Reporting **unsubstantiated** or **unallowable costs** in grant financial reports
- **Noncompliance** with restrictions
- Misrepresentation of **program activities**

# Corruption

- **Making decisions which are not in the best interest of the corporation for personal gain**
- **Conflict of interest**
- **Gifts & incentives to influence decisions**
- **Excess benefits transactions**

# Common Corruption Fraud

- **Excessive employee compensation**
- **Kickbacks**
- **Bid rigging**
- **Vendor billing fraud**

# Fraud in Your State???

- **Misappropriation?**
- **Misstatement?**
- **Corruption?**

# Fraud Realities

- **No fool-proof systems** to prevent or detect fraud
- **Perfect controls = unreasonable cost**
- **Prevention** is the most **cost effective** way to deal with fraud

# State Monitors & Fraud???

- What do the **feds expect your State** to do to prevent/detect fraud?
- What **role** does your State expect **monitors** to play in preventing & detecting **fraud**?

# Monitor Roles in Fraud Prevention?

- **Recognize environmental warning signs**
- **Discuss fraud issues with CEO**
- **Encourage effective Board oversight**

# More Monitor Roles in Fraud Prevention. . .

- **Communicate concerns about controls & fraud risks to Board**
- **Encourage investment in adequate infrastructure**

# Organizational Risk Factors for Fraud

- **Inactive/inattentive Board**
- **Inadequate operating funding**
- **Cash flow problems**
- **Overstressed management**
- **Underinvestment in infrastructure**

# Pro-Fraud Environment

- **Ineffective or no review of top management**
- **Inattentive Executive Director**
- **Inadequate internal monitoring**
- **Financial stress & cash flow problems**
- **Overstressed staff**

# Anti-Fraud Environment

- **Effective Board oversight**
- **Integrity at the top**
- **High value on controls & compliance**
- **Random internal monitoring**
- **Third party fraud hotline**

# Culture of Integrity

- **Employee confidence in management integrity**
- **External review of top exec expenses, comp, & performance**
- **Perceived fairness**

# Monitors & Fraud Detection

- **Is fraud detection a goal of monitoring visits?**
- **Testing transactions: Your role vs. independent auditor role?**
- **Your preparation to deal with fraud evidence if found?**

**Fraud is much more likely to be detected by tips than by any other means... including monitors or auditors!**

# Sources of Tips

**Employees - 64 %**

**Anonymous - 18%**

**Customer - 11%**

# Hotlines Most Effective Anti - Fraud Strategy

- **Cut median loss in half**
- **Reduced time before detection significantly**

# Are You Prepared?

Do you have **clear procedures** to follow:

- **If you suspect fraud?**
- **If you find evidence of fraud?**

# What Would You Do If...

- **You found evidence that employees were added to the payroll without proper authorization?**
- **You found expense reimbursements that were issued to the Executive Director without submission of documentation?**

# **Basic steps to deal with evidence that may indicate fraud..**

- **Make photo copies of evidence**
- **Discuss problem with higher management or Board if CEO involved**
- **Encourage manager/Board Member to retain control of evidence**

## *Spotting Common Frauds*

# **Excessive Compensation**

- **Review Board minutes for evidence of proper comp setting practices**
- **Review 990 reporting for comp from related entities**
- **Review treatment of executive expense reimbursements**

## *Spotting Common Frauds*

# **Ghost Employees**

- **Review controls for adding & removing employees from payroll**
- **Review paycheck distribution controls**
- **Ask top management to explain how controls work to prevent & detect ghost employees**

## *Spotting Common Frauds*

# **Travel & Entertainment**

- **Review control procedures**
- **Determine how top management reimbursements are processed**
- **Review Board policy regarding CEO expense allowances & reimbursements**

## *Spotting Common Frauds*

# **Billing Fraud, Kickbacks, & Bid Rigging**

- **Review procurement procedures & test multiple purchases**
- **Review procedures for adding & deleting vendors**
- **Review process for authorizing routine purchases & payments**

## *Spotting Common Frauds*

# **Employment Taxes**

- **Look closely at procedures for review of accuracy of paychecks**
- **Review procedures for verifying that deposits are made timely**
- **Beware “over-depositing” of payroll taxes**

## *Spotting Common Frauds*

# **Grants Administration**

- **Tie grant reports to General Ledger**
- **Review implementation of cost allocation plan**
- **Review systems for internal compliance monitoring**

# Your Next Steps?

- **Review monitoring checklist to be strengthen “fraud environment” assessment?**
- **Clarify monitor expectations?**
- **Clarify procedures when fraud is suspected?**