



Identifying and Dealing With Fraud and Abuse

September 9, 2003
3:00 – 6:40 pm

MIEM



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Agenda

Time	Topic	Presenters
3:00 – 3:05 pm	Introduction	Tom White, MSBO
3:05 – 3:45 pm	The Basics of Fraud & Abuse	David Wells, Plante & Moran, PLLC Sherry Buist, Standard Federal Bank
3:45 – 4:05 pm	Property/Employee Theft	Tom DeClercq, Michigan State Police
4:05 – 4:20 pm	Questions and Answers	Various Speakers
4:20 – 4:50 pm	Legal/Policy Issues	Roy Henley, Thrun, Maatsch & Nordberg P.C.
4:50 – 5:00 pm	Break	
5:00 – 5:30 pm	Public Relations in the Aftermath	Janet Roberts, Huron Valley Schools
5:30 – 6:40 pm	Roles, Responsibilities & Ethics	Mari McKenzie, Yeo & Yeo; Fred Haller, Plante & Moran, PLLC; Ric Peterson, MSBO

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David Wells Plante & Moran, PLLC

The Basics of Fraud and Abuse

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Vendor History Report

8/29/2001 10:02 AM
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Vendor 0855

Entity:

Vendor ID Vendor Name
Voucher# Invoice ID Inv Date Entity Due No: Discount taken Debit Credit Balance
Control # Check # Check Date

US DOLLAR	POWERWASH						
Beginning Balance:						0.00	
VCH09589	MT1000	3/1/2000	FF	Paid	899.15		899.15
VCH09589	MT1000	3/1/2000	FF	Paid	899.15		1,798.30
VCH10404	MT0020103	3/18/2000	FF	Paid		2,923.76	4,722.06
4218	45028	4/8/2000	FF		0.00	899.15	3,822.91
4218	45028	4/8/2000	FF		0.00	899.15	4,722.06
VCH11462	MT00200104	5/31/2000	FF	Paid		2,178.28	6,900.34
VCH12355	MT00200108	6/30/2000	FF	Paid		4,356.51	11,256.85
4973	45924	6/8/2000	FF		0.00	2,623.76	13,880.61
5814	46763	7/24/2000	FF		0.00	2,178.28	16,058.89
6153	47098	8/8/2000	FF		0.00	4,356.51	20,415.40
VCH15589	MT00200108	10/1/2000	FF	Paid		1,891.71	22,307.11
7724	48624	11/9/2000	FF		0.00	1,891.71	24,198.82
VCH17281	MT00200107	11/7/2000	FF	Paid		2,318.51	26,517.33
684	49354	12/15/2000	FF		0.00	2,318.51	28,835.84
VCH18707	MT00200110	1/19/2001	FF	Paid		2,951.71	31,787.55
1741	50442	2/15/2001	FF		0.00	2,951.71	34,739.26
VCH21530	MT00200110	4/4/2001	FF	Paid		3,280.20	38,019.46
VCH23275	MY00200111	4/7/2001	FF	Paid		2,520.73	40,540.19
5785	51628	4/22/2001	FF		0.00	2,520.73	43,060.92
3279	52074	5/2/2001	FF		0.00	3,280.20	46,341.12
VCH24373	MT00200112	6/22/2001	FF	Paid		1,171.27	47,512.39
4846	53521	7/17/2001	FF		0.00	2,520.73	50,033.12
4646	53521	7/17/2001	FF		0.00	2,171.27	52,204.39
VCH21519	MT0020010	2/23/2001	FF	Paid		2,357.64	54,562.03
Currency totals:					0.00	28,886.60	28,886.60

STATEMENT OF ACCOUNT

Statement Period: June 01, 2002 thru June 30, 2002

Account Number: _____

BUSINESS CHECKING ACCOUNT DETAIL (CONT.)

Check Number	Amount	Date Paid	Reference Number	Check Number	Amount	Date Paid	Reference Number
6299	1,402.98	06/03	0629906299	6300	30.00	06/12	0630006300
6300	820.00	06/04	0630006300	6301	107.00	06/12	0630106301
6301	84.00	06/05	0630106301	6302	800.00	06/20	0630206302
6302	93.00	06/05	0630206302	6303	1,000.00	06/27	0630306303
6303	80.00	06/05	0630306303	6304	91.00	06/18	0630406304
6304	40.00	06/07	0630406304	6305	70.00	06/17	0630506305
6305	60.00	06/07	0630506305	6306	92.00	06/19	0630606306
6306	12,210.00	06/08	0630606306	6307	59.01	06/19	0630706307
6307	1,218.00	06/10	0630706307	6308	88.00	06/19	0630806308
6308	35.00	06/10	0630806308	6309	347.00	06/20	0630906309
6309	45.00	06/10	0630906309	6310	60.00	06/20	0631006310
6310	181.00	06/13	0631006310	6311	100.00	06/19	0631106311
6311	2,177.00	06/14	0631106311	6312	62.00	06/27	0631206312
6312	15.00	06/14	0631206312	6313	158.01	06/25	0631306313
6313	99.00	06/17	0631306313	6314	180.00	06/25	0631406314
6314	99.00	06/27	0631406314	6315	30.00	06/21	0631506315
6315	120.00	06/27	0631506315	6316	70.00	06/26	0631606316
6316	120.00	06/27	0631606316	6317	18.00	06/27	0631706317
6317	2,061.00	06/07	0631706317	6318	230.00	06/27	0631806318
6318	3,061.00	06/07	0631806318	6319	2,200.00	06/27	0631906319
6319	10,000.00	06/12	0631906319	6320	2,000.00	06/27	0632006320
6320	19,000.00	06/12	0632006320	6321	1,131.35	06/28	0632106321
6321	96.00	06/19	0632106321	6322	1,995.00	06/25	0632206322

Number of Checks: 108 Total: 97,309.96

DAILY CHECK SUMMARY

Date Paid	Amount	Number of Checks	Date Paid	Amount	Number of Checks
06/03	1,402.98	10	06/11	209.00	30
06/04	820.00	3	06/12	3,517.38	40
06/05	8,170.00	2	06/17	20,714.70	38
06/10	1,128.00	5	06/19	2,314.91	4

7/2/02

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RECEIPTS & EXPENDITURE SUMMARY

ACCOUNTS	OPENING BALANCE	REVENUE	EXPENDITURES	TRANSFERS	ENDING BALANCE
	\$ -	\$ -	\$ -	\$ -	\$ -
	\$ -	\$ -	\$ -	\$ -	\$ -
	\$ -	\$ -	\$ -	\$ -	\$ -
	\$ -	\$ -	\$ -	\$ -	\$ -
	\$ -	\$ -	\$ -	\$ -	\$ -
TOTAL LEDGER BALANCES:	\$ 95,663.35	\$ 78,778.00	\$ 84,358.92	\$ -	\$ 87,102.43

BANK RECONCILIATION

ENDING BALANCE - CHECKING STATEMENT	\$ 47,210.00
ENDING BALANCE - Mem Fund - Sav	\$ 2,258.35
ENDING BALANCE - Mem Fund - Time Dep	\$ 825.35
ENDING BALANCE - Mem Fund - Time Dep	\$ 7,062.93
ENDING BALANCE - Time Dep	\$ 5,000.00
ENDING BALANCE - Time Dep	\$ 10,000.00
TOTAL DEPOSITS IN TRANSIT:	\$ 14,744.31
TOTAL OUTSTANDING CHECKS:	
ADJUSTED BANK BALANCE:	\$ 87,102.43
DIFFERENCE:	\$ -

NOTES:

ASSISTANT PRINCIPAL: [REDACTED] DATE: 7/2/02

PREPARED BY: [REDACTED] DATE: 7/3/02

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Fund shares are not deposits or obligations of, or guaranteed or endorsed by, any bank, and are not insured by the Federal Deposit Insurance Corporation, the Federal Reserve Board or any other agency. Fund shares involve certain investment risks, including the possibility of loss of principal. Share price, yield and total return may fluctuate and are not guaranteed.

FIDELITY FUND CASH MGR

ACCOUNT NUMBER: 800, 800, 100, 100, 00, 00
 DEALER NUMBER: 0000000000
 INVESTOR NAME: FINANCIAL SERVICES
 DEALER NAME: FINANCIAL SERVICES

SHAREHOLDER STATEMENT

TRADING DATE	TRANSACTION DESCRIPTION	DOLLAR AMOUNT	PRICE PER SHARE	SHARES THIS TRANSACTION	TOTAL SHARES OWNED
03-01	BALANCE FORWARD				352,662.570
03-13	PURCHASE	500,000.00	1.000	500,000.000	852,662.570
03-18	REDEMPTION	600,000.00	1.000	600,000.000	252,662.570
03-22	PURCHASE	1,900,000.00	1.000	1,900,000.000	2,152,662.570
03-25	REDEMPTION	250,000.00	1.000	250,000.000	1,902,662.570
03-26	PURCHASE CORRECTION 07-25-02	50,320.45	1.000	50,320.450	1,952,991.020
03-27	REDEMPTION	200,000.00	1.000	200,000.000	1,752,991.020
03-28	REDEMPTION	300,000.00	1.000	300,000.000	1,452,991.020
03-31	DIVIDEND REINVESTED	1,407.59	1.000	1,407.590	1,454,398.610

STATEMENT DATE	SHARES OWNED	CAPITAL GAIN	SHARES	TOTAL
03-31-02	5,466.83	0.00	1,404,070.160	1,404,070.160

SHAREHOLDER COPY
1 of 2

Fund shares are not deposits or obligations of, or guaranteed or endorsed by, any bank, and are not insured by the Federal Deposit Insurance Corporation, the Federal Reserve Board or any other agency. Fund shares involve certain investment risks, including the possibility of loss of principal. Share price, yield and total return may fluctuate and are not guaranteed.

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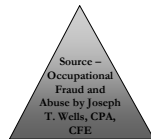
SHAREHOLDER COPY
2 of 2

The Fraud Triangle

PRESSURES/MOTIVES

- Greed
- Living beyond one's means
- High personal debt
- High medical bills
- Poor credit
- Personal financial loss
- Unexpected financial needs
- Addictions
- Extramarital affairs

Pressures/Motives

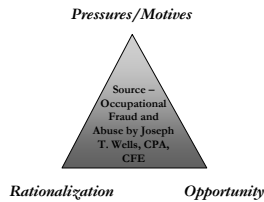


Rationalization Opportunity

The Fraud Triangle (Continued)

❶ OPPORTUNITY

- Lack or circumvention of internal controls
- Past failure to discipline embezzlers
- Management apathy
- Ignorance or incapacity to detect fraud
- Lack of an audit trail

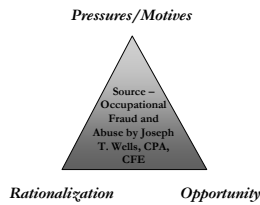


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The Fraud Triangle (Continued)

❷ RATIONALIZATION

- The Organization owes it to me
- I am only borrowing the money
- They can afford it
- I deserve more
- It's for a good purpose



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Definitions

- ❶ Fraud
- ❷ Internal Fraud vs. External Fraud
- ❸ Embezzlement vs. Larceny

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Profile of an Embezzler

- Tends to be a trusted employee
- Works long hours
- Dislikes mandatory vacation policy and cross training
- Likeable and generous (especially with new source of wealth)
- Personality may change, moodiness may set in, when stress of embezzlement catches up to them or when they feel they are about to be caught
- Deceptive and are usually quite good at lying

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Embezzlement Insights

- Embezzlement occurs when money is taken before or after it hits the bank.
- Taking money before it hits the bank is a little more risky because customers' accounts will have to be adjusted to conceal the embezzlement.
- Embezzlements start out small by "testing the waters" and grow over time. Thus, when discovered, it is usually at its highest level.

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Embezzlement Insights (Continued)

- Embezzlers don't quit embezzling when they think they have taken enough. They quit embezzling when they are either close to getting caught or there is no more money left.
- Embezzlers get bolder and sloppier over time.
- The signs are usually there.

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Vulnerabilities

• Symptoms of Organizations that are vulnerable to fraud:

- An Organization that has experienced a recent fraud and the perpetrator(s) did not receive sufficient discipline
- Accounting anomalies – the numbers just don't make sense
- Frequent overdrafts in Company bank accounts
- Bank reconciliations not prepared timely
- Extravagant lifestyles of employees that seem incongruent with their compensation

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Vulnerabilities (Continued)

- Unusual behavior of key employees
 - Depression
 - Addiction
 - Mood swings
- Rumors, tips and complaints from customers, suppliers and employees
- Management and/or employee circumvention of internal controls
- High employee turnover

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Vulnerabilities (Continued)

- Poor morale
- The Organization that is going through downsizing
- Frequent changes in management
- Reluctance of key employees to take vacations
- Something just doesn't feel right

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Common Schemes

- **Small organizations tend to be more vulnerable to embezzlement due to less stringent controls and lack of segregation of duties. The most common frauds are asset misappropriations involving an Organization's cash and checking accounts. Some of the most common embezzlement schemes include:**

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Common Schemes (Continued)

- **Lapping Schemes**
- **Checks written to the embezzler and cashed**
- **Checks written for embezzler's personal expenses, i.e. car payments, utility bills, credit cards)**
- **Checks written to fictitious vendors or businesses owned by the embezzler**
- **Wire transfers from the Organization to the embezzler's personal accounts**
- **Intercepting checks made out to the Organization and directing the bank to cash and convert them to cashier checks**

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Common Schemes (Continued)

- **Expense report fraud – duplicate submissions, over submissions**
- **Changing amounts on checks to vendors, initialing the new amounts, and splitting the difference with the vendor**
- **Overpayments to vendors and having the refunds mailed to the perpetrator**
- **Signing over ghost-employee checks**
- **Cashing checks made out to a business**
- **Forged checks**
- **Fraudulent endorsements**

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Fraud Indicators

ACCOUNTS RECEIVABLE/SALES

- Customer invoices billed out of sequence
- Gaps in invoice numbers
- Customer address on invoices different than the address listed in customer master file
- Multiple shipping addresses used for the same customer
- Manual, non-cash debit/credit adjustments made to customer files
- Customers with credit balances

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Fraud Indicators (Continued)

ACCOUNTS RECEIVABLE/SALES (continued)

- Customers whose addresses are the same as employee addresses
- Significant delinquent balances among newer customers
- Accounts written off shortly after being established, particularly ones on which no payments were recorded
- Unusual items or patterns
- Changes or anomalies in composition of sales
- Sale voids/refunds by location, employee, customer, etc.

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Fraud Indicators (Continued)

ACCOUNTS PAYABLE/PAYROLL

- No confirmation process for wire transfers
- Electronic checks
- Duplicate/over-payments to vendors
- Creation of fictitious vendor – how easy is it to set up a vendor?
- Monitoring of vendor maintenance files
- Checks issued out of sequence – review the beginning part of the bank statement

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Fraud Indicators (Continued)

ACCOUNTS PAYABLE/PAYROLL (continued)

- Vendors and employees whose addresses are post office boxes
- Vendors and employees who have the same address and/or phone number
- Vendors/employees whose address and/or phone number does not match with directories
- Vendors with no or disconnected phone numbers
- Vendors that have been recently added and old vendors that have been deleted

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Fraud Indicators (Continued)

ACCOUNTS PAYABLE/PAYROLL (continued)

- Checks issued to vendors not on an approved vendor list
- Checks issued to unfamiliar vendors whose names are similar to legitimate vendor names
- Checks issued to vendors that fall under the threshold that would normally require further management authorization
- Checks coded to unusual balance sheet or expense accounts
- Dual endorsees on the backside of the check
- Individual endorsing the backside of a check issued to a business

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Fraud Indicators (Continued)

ACCOUNTS PAYABLE/PAYROLL (continued)

- Checks with signature stamps
- Missing cancelled checks that are listed on the bank statements
- Checks issued to unfamiliar vendors whose names are similar to legitimate vendor names
- Checks issued to vendors that fall under the threshold that would normally require further management authorization
- Checks coded to unusual balance sheet or expense accounts
- Dual endorsees on the backside of the check

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Fraud Indicators (Continued)

⦿ ACCOUNTS PAYABLE/PAYROLL (continued)

- Individual endorsing the backside of a check issued to a business
- Checks with signature stamps
- Missing cancelled checks that are listed on the bank statements
- Check amounts recorded through journal entries rather than through check/disbursement registers or modules

Fraud Indicators (Continued)

⦿ ACCOUNTS PAYABLE/PAYROLL (continued)

- Payments for services that do not require delivery of goods or significant documentation to obtain payments. (For example payment of commissions or consulting fees.)
- Vendors in which client is sole customer, based on the vendor using consecutive invoice numbers over an extended period of time
- Manual, non-cash debit/credit adjustments made to vendor files

Fraud Indicators (Continued)

⦿ ACCOUNTS PAYABLE/PAYROLL (continued)

- Vendor master files that have been recently edited
- Vendors with debit balances
- Invoices with even dollar charges
- Vendors with non-matching "bill to" and "ship to" addresses
- Employees who have not executed tax withholding forms, health insurance benefits, or have not claimed health benefits in the current year

Fraud Indicators (Continued)

⊗ ACCOUNTS PAYABLE/PAYROLL (continued)

- Inactive employees who are receiving payroll checks
- Employees with inactive/bogus social security numbers
- Multiple employees with the same social security number

⊗ GENERAL LEDGER/REPORTS

- Journal entries with no description
- Journal entries using “misc”, “miscellaneous”, or “adjust”
- Journal entries to “Cash” accounts
- Bank reconciling items
- Fraudulent bank statements

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Key Documents

- ⊗ Bank statements
- ⊗ Checks
- ⊗ Bank reconciliations
- ⊗ General ledgers
- ⊗ Journal entries
- ⊗ Vendor master files
- ⊗ Payroll master files

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Fraud Prevention

⊗ Many frauds are discovered by accident or through anonymous tips. The following are preventive measures that Organizations can employ to reduce the possibility of embezzlement:

- Set the proper tone at the top of the Organization
- Mail monthly bank statements to the home of the Owner/CEO or to the office of a Board member
- Perform Specialized Internal Control Reviews

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Fraud Prevention (Continued)

- Have bank reconciliations performed in a timely manner by individuals who do not have access to accounting records and who do not process checks or deposits
- Implement Positive Pay
- Perform background checks
- Secure check stock and build check security features into checks
- Secure signature stamps

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Fraud Prevention (Continued)

- Implement a Hotline service
- Rotate job responsibilities without notice
- Enforce mandatory vacations
- Implement a good system of internal controls, including segregation of duties
- Create a positive and open work environment

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Sherry Buist Standard Federal Bank

Member ABN AMRO GROUP



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INTERNAL THEFT

Principal Categories of White Collar Crime

- Theft of Money or Property ←
- Theft of Trade Secrets
- Conflicts of Interest
- Breach of Fiduciary Duty
- Bribery
- Concealment of Material Facts
- Misrepresentation of Material Facts

INTERNAL THEFT

Embezzlement: To appropriate fraudulently to one's own use, money or property entrusted to one's care.

INTERNAL THEFT

Defalcation: Misappropriation of money held by an Official, Trustee, or Other Fiduciary.

INTERNAL THEFT

Larceny: The wrongful taking of money or property of another with the intent to convert or to deprive the owner of its possession and use.

INTERNAL THEFT

Elements of Embezzlement/Defalcation:

1. The suspect took or converted...
2. Without the knowledge or consent of the owner...
3. Money or Property of another...
4. That was entrusted to the suspect.

2002 Report to the Nation on Occupational Fraud & Abuse

- The Wells Report covers 633 occupational fraud cases that caused over \$7 billion in losses.
- More than half the thefts caused a loss of at least \$100,000.
- Typical perpetrator is a first time offender.

2002 Report to the Nation on Occupational Fraud & Abuse

- Cash is a target 90% of the time.
- Small businesses are the most vulnerable for fraud & abuse with average losses of \$127,000 as compared to larger business whose average loss was \$97,000.
- The average scheme lasted 18 months.

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2002 Report to the Nation on Occupational Fraud & Abuse

- Fraudulent statements are the most costly form of fraud with median losses of \$4.25 million per scheme.
- Corruption schemes accounts for 13% of reported frauds and cause more than \$500,000 in losses on average.

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2002 Report to the Nation on Occupational Fraud & Abuse

- Most common method of detection was by a tip from an employee, customer, vendor, or anonymous source. Second most common method of detection was "by accident".
- Organizations with fraud hotlines cut their losses by approximately 50% per scheme.

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2002 Report to the Nation on Occupational Fraud & Abuse

- Internal audits, external audits, and background checks also significantly reduce losses.
- The Wells Report estimated that 6% of revenues in 2002 would be lost to fraud & abuse.

2002 Report to the Nation on Occupational Fraud & Abuse

The Perpetrators:

1. Position: Schemes committed by Managers & Executives, on average cause a median loss of \$250,000.
2. Collusion: When collusion is involved median loss increased to \$450,000 per case.

2002 Report to the Nation on Occupational Fraud & Abuse

The Perpetrators: (cont.)

3. Gender: Number of cases reported with respect to gender showed that the number of incidents were very close; although the losses caused by males were more than three times higher as those committed by females.

2002 Report to the Nation on Occupational Fraud & Abuse

The Perpetrators: (cont.)

4. Individuals under the age of 26 committed 6% of frauds; Persons over the age of 35 committed 60% of the thefts; and persons between the ages of 36 – 50 committed nearly 50% of the thefts.

2002 Report to the Nation on Occupational Fraud & Abuse

The Perpetrators: (cont.)

5. Education: Losses caused by perpetrators with a college education was 3.5 times higher than those with high school diplomas.
6. Criminal History: Most perpetrators are first time offenders.

I am a victim of Fraud, now what?????

You discover that a trusted employee in your operation has been stealing money for a substantial amount of time.

Issues to Consider

- Employee status (e.g. terminate, suspend with or without pay, etc.).
- Interview/Interrogate employee depending on your firm's position on this issue.
- Obtain confession; "written" if possible.

Issues to Consider

- Secure work area/records.
- Contact either Investigations Dept. or Audit in order to perform a thorough investigation of theft.
- Contact Law Enforcement (e.g. local, county, state, federal).

Issues to Consider

- Examine existing policies and procedures that permitted the thief to perpetrate the scheme without detection.
- Change or modify policies/procedures to prevent reoccurrence of theft.

Recovery of Assets

1. Voluntary assignment of personal assets (e.g. 401K, IRA's, Bank accounts, etc.).
2. Court Order blocking transfer of assets (e.g. Bank accounts, property, etc.).

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Recovery of Assets

4. Criminal prosecution – Restitution.
5. Civil Suit.
6. Attempt to recover funds from other individuals that may have facilitated theft knowingly or unknowingly (e.g. accomplice).

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Recovery of Assets

I believe that my Bank facilitated this scheme (unknowingly); but had they exercised reasonable care this fraud would have been detected earlier.
I believe that my Bank owes me for the loss I incurred.

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What steps do I take?

- Contact your financial institution as soon as possible and inform an Officer of the Bank what has happened.
- Inform the Bank of the type and scope of the fraud (e.g. theft or corp. checks/ongoing 18 months).

What steps do I take?

- Request assistance from the Bank's Investigation Dept. or Audit Group.
- Retain legal counsel.
- Document loss and submit claim to Bank.

What actions will the Bank take?

- Bank will review claim & determine what if any liability rests with the Bank and what may be the result of negligence or culpability on the part of the company (e.g. employee has criminal background).

What actions will the Bank take? (cont'd)

- All supporting documents will be reviewed.
- Possibly customers & employees of the company may be interviewed.
- Affidavits of Forgery obtained.

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What actions will the Bank take? (cont'd)

- Has the matter been referred to Law Enforcement.
- The firm's outside auditing firm may be contacted for the results of any recently completed compliance audits.

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What actions will the Bank take? (cont'd)

- Workflow and paper trails and associated job responsibilities will be reviewed.
- Checks and balances (or lack of) will be reviewed.
- If possible the perpetrator will be interviewed.

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Bank Defenses
Uniform Commercial Code (UCC)
Article 3

- **Article 3-404**
Imposters; Fictitious Payees
- **Article 3-405**
Employer's Responsibility for Fraudulent Endorsement by Employee
- **Article 3-406**
Negligence Contributing to the Forged Signature or Alteration of Instrument⁶⁴

Bank Defenses

Uniform Commercial Code (UCC)
Article 4

- Article 4-406**
Customer's Duty to Discover and Report Unauthorized Signature or Alteration
- Article 4-111**
Statute of Limitations

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Summary

Must Have:

- **Firm/Entity needs to have adequate controls in place.**
- **Firm/Entity needs to have sound operational practices.**
- **Firm/Entity needs to have an effective Audit program.**

66

Summary

Suggestions:

- **Hotline to report suspected thefts/wrongdoing.**
- **Unannounced/surprised audits of funds/books.**
- **Expect the unexpected.**
- **Code of Conduct Policy.**

Summary

Suggestions: (cont'd)

- **Mandatory 1 week vacation/time off for sensitive areas.**
- **Criminal background/Credit checks on "new hires" & employees in key/sensitive positions.**
- **Insurance coverage.**

Tom DeClercq
Michigan State Police

Property/Employee Theft

Theft Prevention



• Thefts By Unknown Suspects (B&E)

- Good lighting/locks
- Limit access to building
- Single point of entrance & exit after hours.
 - Emergency exit is an exception with alarm
- Use of internal barriers

70

Theft Prevention

- Regular contact with police dept. for frequent property inspections (local/county/state)

• Thefts By Students/Teachers

- Establish zero tolerance scale
- Prevention & suspension/dismissal for theft

71

Theft Prevention

- Limit access to equipment/property when not in use
- Require accountability by teachers for monthly inventory on class property (set dollar amount)

72

Preventive Measures

- **Tag or label all school equipment**
 - Pre-established dollar amounts for equipment
 - Use of internal (hidden) tags for items such as computers
 - Tags should list owner of property and contact phone number

73

Preventive Measures

- **Inventory list established and maintained by office and classroom teacher**
 - Set inventory checks at regular intervals
 - Video surveillance

74

What To Do Once A Theft Has Occurred

- **Tip line established for anonymity**
- **Contact with police (detective)**
- **Establish what property had been stolen through inventory or audit**
- **Possible reward leading to recovery and/or arrest**

75

Embezzlement/Fraud



● Law Enforcement Perspective

- Must have system of checks & balances in place
- All levels of supervisors with fiduciary responsibilities must have oversight or be accountable

76

Investigation/Prosecution

● Law enforcement should be brought in immediately upon suspicion of fraud/embezzlement

- Law enforcement trained in interview/interrogation
- Law enforcement is unbiased (not a co-worker of parties involved)

77

Investigation/Prosecution

- Use of search warrants and/or investigative subpoenas to gain evidence that could be destroyed/alterd
- Resources available such as laboratory, Computer Crimes Unit, polygraph, surveillance

78

Investigation/Prosecution

● Civil arrangements should be avoided

- After suspect has defaulted on civil arrangement, victim has limited resources on receiving restitution when not established by court

79

Roy Henley
Thrun, Maatsch &
Nordberg, P.C.
Legal/Policy Issues

80

Spectrum of Legal Issues

- Authorized/Unauthorized Actions
- Actions with Civil Legal Implications
- Actions with Criminal Legal Implications

81

Authorized/Unauthorized Actions

☛ “The Well-Intentioned Mistake”

- Expenditures of Public Funds for Private Purposes
- vs-
- Use of Private Funds in a Segregated Account

82

Actions with Civil Legal Implications

☛ Employee Performance Issues

☛ “Crossing the Line”

- Employee Expenses
 - Statutory Authorization
- School Fund Management
- Use of School Property and Equipment

83

Actions with Criminal Legal Implications

☛ Embezzlement

- By Public Officer, Agent, or Servant

☛ Larceny

- From Specific Places
- By Conversion
- By False Personation

☛ Uttering and Publishing

84

Investigations

- ⊗ Witness Statements
 - Union Rights
 - Contractual Rights
 - Self-Incrimination Issues
- ⊗ Evidence Preservation
- ⊗ Documentation
- ⊗ FOIA Implications

85

Employment Actions

- ⊗ Contracts
 - Collective Bargaining Agreements
 - Individual Contracts
- ⊗ Due Process Issues

86

Civil Litigation

- ⊗ Burdens of Proof Against Employees
 - Recovery Actions
 - ⊗ Immunity
 - ⊗ Collection
 - Tenure Actions
- ⊗ Against Employers
 - Employment Actions
 - ⊗ Contract
 - ⊗ Due Process
 - ⊗ Civil Rights

87

Criminal Litigation

- Governmentally Controlled
- Sentencing
 - Restitution
- Effect Upon Civil Litigation

88

Policy Considerations

- Property Usage
 - Acceptable Use Policies
 - Computers
 - Other Property
 - Lack of Privacy Interests
 - Inventory Procedure

89

Policy Considerations

- Account Management
 - Board Authorization
 - Regular Account Reconciliation
 - Board Approval of All Employee Payments
 - Limited Access to Signature Places for Checks
 - Immediate Restrictive Endorsement of Checks

90

Cash Management

Establish Procedures for:

- Collection
- Deposit
- Recording

Separation of Duties

91

Fraud & Abuse

Break time

We will return promptly at
5:00 pm

Questions:
msbo@wkar.org

92

Janet Roberts
Huron Valley Schools

Public Relations in the Aftermath

93

Public Relations in the Aftermath

- Be Proactive
- Create a Communications Plan
- Spread Your Message

94

The Communications Plan

- What is the goal of the plan?
 - To proactively address the issue and counter any negative impact
- Under riding theme
 - Commitment to accountability—we take our role as stewards seriously

95

The Communications Plan

- Issues
 - How, what & when to communicate
 - To whom
 - How to show we have and will continue to do to safeguard our assets
 - How to demonstrate we will hire & retain quality employees
 - How to enhance our image

96

The Communications Plan

☛ Actions/Timing

■ General Actions

- ☛ Designate spokespersons
 - All media go through Communications Office
- ☛ Continue current/planned PR

The Communications Plan

☛ Actions/Timing (cont'd.)

■ Staff

- ☛ Use "7 Questions" document for COAT/Board
- ☛ Notify leadership team and supply talking points
- ☛ Remind leadership of crisis communication protocols
 - Limit access to staff & students
 - All inquiries go to Communications Office
- ☛ Ask leadership to monitor, evaluate reactions
- ☛ Notify all staff
- ☛ Encourage all staff to counter misinformation

The Communications Plan

☛ Actions/Timing (cont'd.)

■ Community

- ☛ Inform key stakeholders of overview and steps
- ☛ Superintendent Guest Column in local papers
- ☛ Article in District newsletter
- ☛ Articles for building newsletters

The Communications Plan

☛ Actions/Timing (cont'd.)

■ Media

- ☛ Press release announcing incident and our findings/actions
- ☛ Increase flow of positive PR to media
 - Both from buildings (PR Liaisons) and District
- ☛ Create media statement for frontline
 - "This matter has been turned over to the authorities. I'm not free to comment further. You can contact our Communications Office....."

Public Relations in the Aftermath

☛ President's Statement:

"This demonstrated to the community that our administration takes its responsibility to safe guard the assets of the District very seriously." Further, Squires indicated, "Given the complexity and sophistication of this crime, we could have incurred considerably more losses had it not been for the experience and skill of our business staff."

Establish Your Media Contacts

- ☛ Communications Director
- ☛ Superintendent
- ☛ Asst. Supt. of Administrative
- ☛ Legal Counsel
- ☛ CPA or Independent Fraud Examiner

The Press Release

Huron Valley Controls UnCOVERS Fraud
The Huron Valley Schools' internal audit controls uncovered that a clerk in its business operation had embezzled funds totaling approximately \$150,000 from the District. The employee has been dismissed and is currently under investigation of the FBI. The District will recover all funds.

103

Telling Key Stakeholders

- ❖ As this story unfolds in the media, community members may ask you about it. Share the facts I have presented. *Reassure them Huron Valley Schools is committed to its accountability to the community—we take our role as stewards of the public trust very seriously.*
- ❖ In talking to community members, I encourage you to use this opportunity to share the goals and direction we will pursue this year. Under the year-three initiatives in the District's Strategic Plan, we expanded our educational options to provide more opportunity, flexibility and choice for staff, students and parents.

104

Consistent Messaging

Leadership & Management Overview & Talking Points for Staff/Community

Reassure them that "Your District" is committed to its accountability to the community—we take our role as stewards of the public trust very seriously.

105

Tell Staff The Whole Story

Superintendent Update Sent to All Employees before press release
(also sent via email to HVS employees)

106

Revisions Along the Way

- Inform key leaders/spokespeople of any changes as new information arises.
- Integral to this plan is sticking to the statement, referring all media inquiries to the Communications Department and reinforcing the positive attributes of the District.

107

The Seven Questions

- Provide leadership with “Seven Question” review of the fraud
- Allows you to create concise, factual overview of the incident
- Think in terms of who, what, how, why, etc.

108

Extra Support for Key Persons

- **Talking Points for President and Treasurer—provides more detail as media scrutiny increases**
- **Staff and remaining Board members stick to simple media statement**

109

Plan Your Release

- **Timeline of Events**
 - Board & legal counsel approve final press release
 - Exercise option to “leak” to local weekly press
 - Notify leadership of release (who in turn notifies their staff)
 - Notify union of former employee
 - Follow up message from Superintendent to all staff
 - Fax out release to all media (Supt. makes personal contact with key media)
 - Key communicator letter sent out
 - Put articles in district and building newsletter

110

Mari McKenzie
Yeo & Yeo, P.C.

Roles, Responsibilities & Ethics

111

ETHICS

112

DOING WHAT IS RIGHT

- Extends outside business and accounting office

- Board members

- Administrators

113

Responsibilities

- Duty of care

- Duty of loyalty

- Duty of obedience

114

Prevent, Deter and Detect Fraud

- Culture of honesty and high ethics
- Antifraud processes and controls
- Appropriate oversight process

115

Tone at the Top

- May seem obvious, but it goes a long way toward preventing fraud in an organization
- Establish core values

116

Code of Ethics

- Important role
- Tone at the top
- Foster culture of honesty and accountability
- Communicate to all employees

117

Code of Ethics

- Protection and proper use of district assets
- Compliance with laws, rules and regulations
- Encourage the reporting of any illegal or unethical behavior

118

Code of Ethics

- Guidance to personnel
- Definitions of what is acceptable
- Consequences for unacceptable behavior

119

Code of Ethics Considerations

- Organizational code of conduct
- General employee conduct
- Conflicts of interest
- Outside activities, employment and directorships
- Relationships with clients and suppliers

120

Code of Ethics Considerations

- Gifts, entertainment and favors
- Kickbacks and secret commissions
- Organization funds and other assets
- Organization records and communications

121

Code of Ethics Considerations

- Dealing with outside people and organizations
- Prompt communications
- Privacy and confidentiality

122

Ethics

- Doing what is right
- Set the tone at the top
- Communicate to all employees

123

Fred Hailer Plante & Moran, PLLC

Roles, Responsibilities & Ethics

124

Expectations

Recap of Program Thus Far:

- Provided examples of Fraud & Abuse
"It could happen to you"
- Discussed the legal do's and don'ts
- Outlined how to handle public relations
- Described an environment that promotes ethical behavior

125

Expectations

Understand our world has changed:

- Almost daily reminders of Sarbanes-Oxley Act of 2002
- Schools & School Boards are not covered by this act – however...
- Public expectation that you are maintaining the same standards

126

Expectations

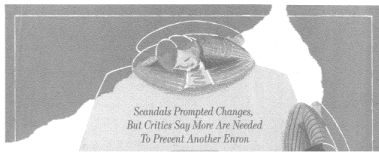
- Auditors under increased pressure and scrutiny
 - Arthur Andersen
 - GAO Independence Standards
- Examples

MARKETPLACE

THE WALL STREET JOURNAL

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Boardrooms Under Renovation



Independence Of Directors Is Elusive Goal

By Joseph B. Lohr III

THE UNLIMINATED NUMBER OF ENRON'S board members across the board. The corporate oversight and business as business. Enron faced with rules proposed to increase independence of corporate directors. The goal is for states that so members of a board's watchdog will ensure they take time from the company other than for their board service.

Private Companies Also Feel Pressure to Clean Up Acts

By Matt Miazar

THE SARBANES-OXLEY act is aimed at making publicly traded companies more accountable. But it's having a big impact on privately owned companies as well. Dick Jackson, chief financial officer of Road & Rail Services Inc., doesn't have to file public reports on his company's operations. The logistics and transportation concern, based in Lancaster, Pa., has just three owners. But in recent months, Road & Rail, which has 60 employees and about \$2 million in annual sales, has been treating its corporate governance practices. Mr. Jackson has added layers of review to the process of compiling financial results, and boosted accountability by ensuring that different managers are responsible for approving invoices and signing checks. The board is contemplating limiting one or more independent directors about. Why the changes? Mr. Jackson says his

company, like others, has been learning from the scandals at Enron Corp., WorldCom Inc. and elsewhere. So have a growing number of its clients—along with its banks and insurance companies—and they want to ensure Road & Rail can hold up its books as well as its promises. Many of its clients are public companies that have overhauled their own governance in response to the new regulations. Mr. Jackson says, "Philosophically, as a privately held company, you don't want everything exposed to the world," he says. "On the other hand, the world is changing, and there's a lot more sharing of information between customers and suppliers and business partners. I think everything eventually is an external event." Indeed, the Sarbanes-Oxley act is having a ripple effect, "much more far-reaching than any of us knew," Mr. Jackson says. Among the changes, closely held companies are quietly overhauling their boards and upgrading their accounting standards. In addition to addressing their own concerns, managers are being pressured to make changes by customers, investors, accountants and venture capitalists. Many compa-

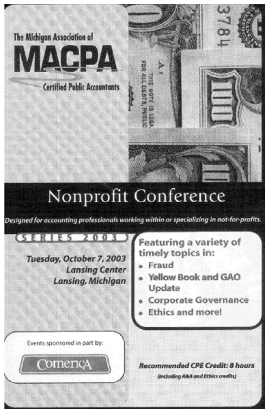
Moved to Action

● 44% Review or change current accounting procedures
● 39% Create or expand internal audit function
● 35% Hire an independent firm for consulting work
● 23% Restructure executive compensation plans
● 8% Clear

● 2% Note: Multiple answers were allowed. Source: BoardNet Management Resources

nies also are reacting to the rising cost of insurance for directors and officers. Just last month, a federal judge in New York City ruled that directors of bankrupt Trane Interna-

tional Holdings Inc. failed in their responsibilities by allowing its chairman and controlling shareholder, Michael Cogan, to avoid funds through excessive compensation, dividends and loans. The decision makes it clear that "private company directors and officers are going to be held to the same standard as public company officers and directors to determine whether or not they are fulfilling their fiduciary duties," says John P. Camacho, a partner at Leibovitz, Lash, Greene & MacFarlane LLP, who represents the bankruptcy trustee in that case. "In so many, most private companies being stopped far short of the measures adopted by their public peers, and executives at many remain tight-lipped about their operations to outsiders and even employees and some investors. After all, avoiding the spotlight and the paperwork that comes with being public is part of the reason that many stay private. "I want the right disciplines in place," says Marjorie Carlson Nelson, chairman of PricewaterhouseCoopers. Please turn to Page 85, Column 1



Expectations

Of the Central Office:

- Cultivate a District climate of honesty & integrity
- Identify & deploy appropriate internal control procedures
- Develop internal audit functions where appropriate
- Avoid/disclose related party transactions

Expectations

Of The Central Office:

- Consider use of anonymous hotline for employees to report fraud
- Insure auditors have appropriate access to the Board
- Inform Board of any significant financial issues

Expectations

Of The Board:

- Cultivate a district climate of honesty & Integrity
- Avoid/Disclose related party transactions
- Support central office efforts to institute and monitor strong internal control measures

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Expectations

Of The Board:

- Allocate sufficient resources to insure proper oversight & safeguarding of district operations
- Adopt a policy of zero tolerance for fraud & abuse

137

Expectations

How to accomplish these expectations:

- Teamwork in developing accountability
- Ask your auditors for help
- Operate with the best interest of the district & community in mind
- Be flexible – it's a changing environment for Boards, Central Office & Auditors

138

Mari McKenzie
Yeo & Yeo, P.C.

Roles, Responsibilities & Ethics

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AUDIT

140

Accounting

● **Gathering and presenting financial information**

141

Auditing

- Independent review of the fairness of financial statements
- Systematic examination and appraisal of systems in an opinion

142

Stakeholders in the Audit Process

- Board
- Citizens
- Administration
- Parents
- Employees
- Bondholders

143

Objectives

- Accountability to the public
- Financial information presented in accordance with GAAP
- Financial statements free of material misstatements

144

Objectives

- Adherence to financial compliance requirements
- Deficiencies in the accounting system

145

Objectives

- Provides board and management an opportunity to establish working relationships with individuals who specialize in school financial management and accounting and who are familiar with the latest developments in the field

146

Evolution

- New fraud standard SAS 99
Consideration of Fraud in a Financial Statement Audit

147

Auditor Responsibility

- **SAS 99 does not increase the auditor's responsibility to detect fraud**

148

Auditor Responsibility

- **Responsibility to plan and perform the audit to obtain reasonable assurance that financial statements are free of material misstatement, whether caused by error or fraud**
- **Additional guidance and requirements**

149

Management Responsibility

- **SAS 99 does not alter management's responsibility with respect to fraud**
- **Management is responsible for designing and implementing controls to prevent, deter and detect fraud**

150

Ric Peterson

Michigan School Business Officials

Is it Time for your District to Establish an Audit Committee?

151

What is an Audit Committee?



- Includes
 - Executive Branch of the Organization
 - Legislative Branch of the Organization
 - Members of the Public

152

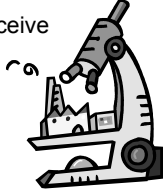
What Does it Do?

- Manages Auditor Acquisition Process
- Manages Acquisition of Services Outside the Attest Function
- Discusses Audited Financial Statements with Auditor
- Discusses Management Letter with Auditor
- Discusses Reportable Conditions with Auditor

153

What Does it Do?

- Meets with District Internal Audit Personnel
- Maintains Procedures to Receive and Address Complaints



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Audit Committee Members

- District Chief Financial Officer
- Member(s) of the Board
- Community Person(s) with Financial Expertise



155

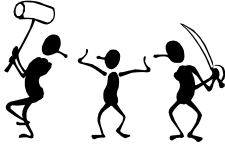
Enhance District's Financial Reporting

- Auditor Meets with Audit Committee
 - Committee meets with executive and legislative branches
 - Discuss financial reporting decisions
 - Discuss financial statements and opinion
 - Discuss internal controls
 - Discuss audits of significance not reflected in financial statements

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Enhance District's Financial Reporting

- Audit Committee Approach Provides for Direct Auditor/Board Committee Interaction



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Questions?

Please e-mail your questions to:

MSBO@wkar.org

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Thank You!

- Please fill out your evaluations at www.msbo.org, www.gomasa.org, www.masb.org or www.gomiem.org.
- If you are a site that is offering SB-CEU, please be sure and turn in your forms at the end of the program.

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