

# ***“YES, We Do Need Ethics”!***

**Presented by**  
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# Professional Ethics is a MUST!

- Having professional ethics is to uphold integrity, objectivity, and competence in all financial dealings. We must be honest, truthful, and transparent in all professional interactions.
- We are expected to avoid conflicts of interest and respect confidentiality.
- Ethics is a system of moral principles.

# What is Ethics?

- ▶ “Ethics” is concerned with what is RIGHT and WRONG.
- ▶ Philip Wheelwright defined ethics as:  
“a branch of philosophy that is the systematic study of reflective choice, of the standards of right and wrong by which it is to be guided, and of the goods toward which it may ultimately be directed.”

***Basically, emphasizing deliberate choice, moral principles, and the consequences of decisions.***

# What is Fraud, Anyway?

- ▶ “Fraud” is any activity that relies on deception in order to achieve a gain or unfair or dishonest advantage.
- ▶ Fraud becomes a crime when it is a “knowing misrepresentation of the truth or concealment of a material fact to induce another to act to his or her detriment. So basically, ***if you lie in order to deprive a person or organization of their money or property, you are committing fraud.***

# Fraud VS Ethics?

- ▶ Fraud is a deliberate act of deception intended to benefit the perpetrator, often with financial gain, while Ethics refers to moral principles that guide behavior.
- ▶ ***Fraud*** is inherently unethical, but not all ***Unethical Actions*** constitutes fraud.

# Why do People Commit Fraud?

- ▶ The most common theory for why people commit fraud is explained with the 3 elements of The Fraud Triangle developed by Dr. Donald Cressey.
- ▶ **1. Pressure** – Refers to the incentive or motivation that pushes an individual to commit fraud, like debt or gambling, or personal problems. It is a perceived need or desire that makes fraud seem like a solution.

# Why do People Commit Fraud (cont'd)

- ▶ **2. *Opportunity*** - Refers to the perceived chance to commit fraud without getting caught. It arises from weak internal controls, lack of oversight, or insufficient monitoring.
- ▶ **3. *Rationalization*** – Refers to the process by which the person justifies their fraudulent acts to themselves. They might convince themselves that they are borrowing the money and will pay it back, that they deserve the extra compensation, or that the organization will not suffer significant harm.

# The Fraud Triangle

- ▶ *I see an opportunity! I need it! I deserve it!*





# The Association of Certified Fraud Examiners (ACFE) has a short story of WHY “Bob” committed Fraud

- ▶ Meet Bob. Bob is under **PRESSURE**, because of his personal debt. A gambling problem and his desire to live the high life.
- ▶ He is also scrambling to meet sales quotas and deliver better numbers to the investors.
- ▶ Bob sees an **OPPORTUNITY** to commit fraud.
- ▶ Bob writes checks and approves checks, without any oversight from his bosses.
- ▶ Bob knows no one is looking or paying attention.

# (short story cont'd)

- ▶ But he needs to **RATIONALIZE** it to himself.
- ▶ *I deserve this! I am only borrowing a little! I will pay it back!*
- ▶ Together these 3 factors lead “Bob” to commit FRAUD!

# Fundamental Types of Fraud

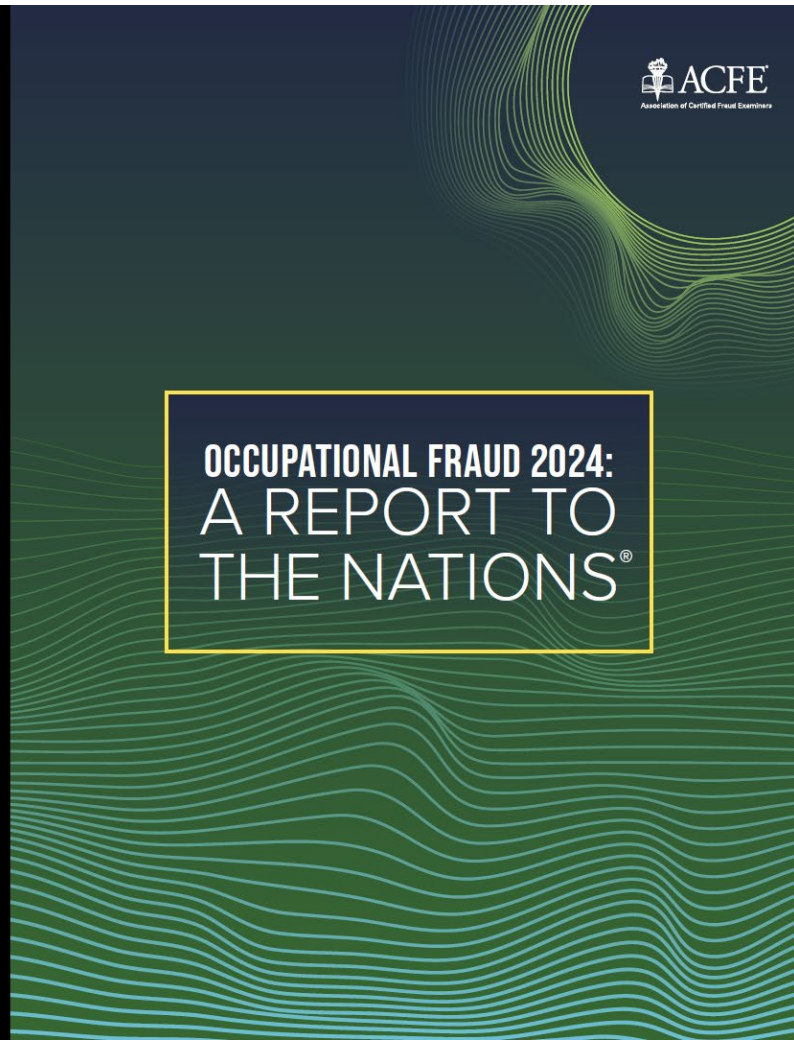
- ▶ Fundamentally, every type of fraud is either *Individual* or *Organizational*.
- ▶ ***Against Individuals*** – This is when a single person is targeted by the fraudster by theft, phishing scams, Ponzi schemes.
- ▶ ***Internal Organizational Fraud*** – “Occupational Fraud” this is when an employee, manager, or executive of the organization deceived the organization by embezzlement, cheating, lying to investors and shareholders.

# Fundamental Types of Fraud (cont'd)

- ▶ ***External Organizational Fraud*** – This is when the fraud is committed against the Organization from the outside, such as:
  - vendor lies about the work actually performed
  - demand bribes from employees
  - when bad checks are submitted
  - when stolen products or knock-offs are returned.

There is an increase with the use of technology that threatens organizations with theft of intellectual property and participant/customer information.

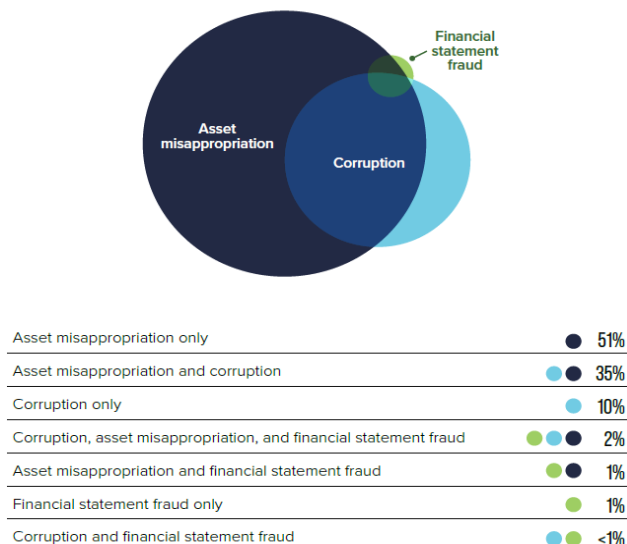
This report was prepared by the ACFE (Association of Certified Fraud Examiners) in hopes to improve collective ability to protect organizations from the harm of occupational fraud.



As indicated below, typically when a person has been caught committing Financial Statement Fraud, it is very likely they have been committing other types of fraud .

While occupational frauds can be divided into three distinct categories, perpetrators do not always limit their schemes to just one category. As shown in Figure 4, 38% of the cases in our study involved two or more types of occupational fraud, with the most common overlap occurring between asset misappropriation and corruption (35% of cases). Interestingly, only 1% of cases in our study involved financial statement fraud alone. This indicates that when a person has been caught committing financial statement fraud, it is very likely they have been committing other types of fraud as well.

FIG. 4 HOW OFTEN DO FRAUDSTERS COMMIT MORE THAN ONE TYPE OF OCCUPATIONAL FRAUD?





# 75% of Fraudsters display at least 1 of the 8 MOST COMMON Behavior Clues/ Red Flags

## BEHAVIORAL RED FLAGS OF FRAUD

Fraudsters commonly display distinct behaviors that can serve as warning signs of their misdeeds. Organizations can improve their anti-fraud programs by taking these behavioral red flags into consideration when designing and implementing fraud prevention and detection measures.



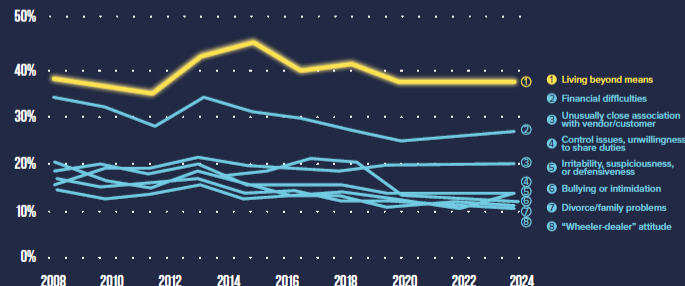
### 8 KEY WARNING SIGNS

**75%** of fraudsters displayed at least one of the **8 MOST COMMON** behavioral clues; each of these **BEHAVIORAL RED FLAGS** was observed in **AT LEAST 10%** of cases.



**FRAUDSTERS LIVING BEYOND THEIR MEANS** has consistently been the **MOST COMMON BEHAVIORAL RED FLAG** since we began tracking this data in 2008.

### COMMON BEHAVIORAL RED FLAGS



## Behavior Red Flags (cont'd)

- ▶ ***Fraudsters Living Beyond Their Means*** has consistently been the ***Most Common Behavioral Red Flag*** since the ACFE began tracking this data in 2008.



# Behavior Red Flags By Gender

- ▶ Analysis of fraudsters' behavior by gender also revealed some interesting differences based on specific red flags. For female fraudsters:
  - Living beyond their means – (41% vs 39% males)
  - Financial difficulties – (31% vs 26% males)
  - Recent divorce or family problems – (14% vs 8% males)

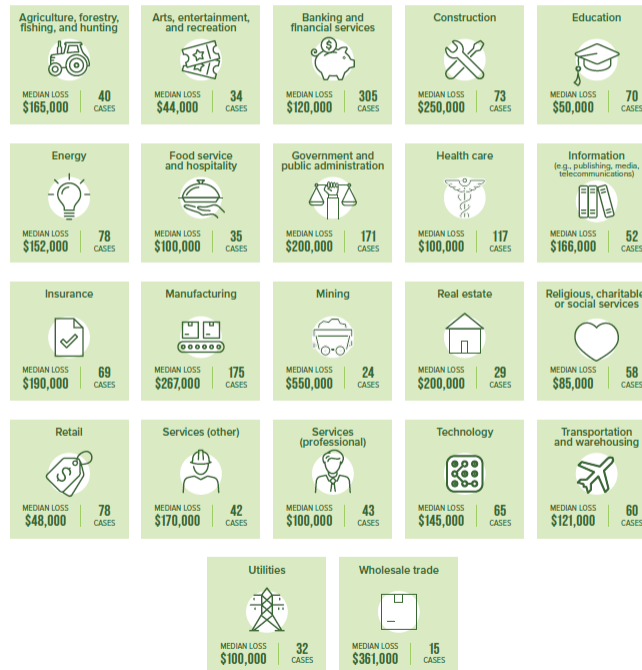
## Behavior Red Flags By Gender (cont'd)

- ▶ Behaviors more commonly attributed to male fraudsters include:
  - Unusually close associations with vendors or customers – (22% vs 13% females)
  - Wheeler-Dealer Attitude – (14% vs 6% females)
  - Irritability, suspiciousness or defensiveness – (13% vs 11 % females)

## INDUSTRY OF ORGANIZATION

Figure 25 reflects the breakdown of cases in our study based on the industry of the victim organization. Banking and financial services, along with manufacturing, were the most common industries represented. Additionally, the industries with the greatest median losses were mining (USD 550,000), wholesale trade (USD 361,000), and manufacturing (USD 267,000).

FIG. 25 HOW DOES OCCUPATIONAL FRAUD AFFECT ORGANIZATIONS IN DIFFERENT INDUSTRIES?

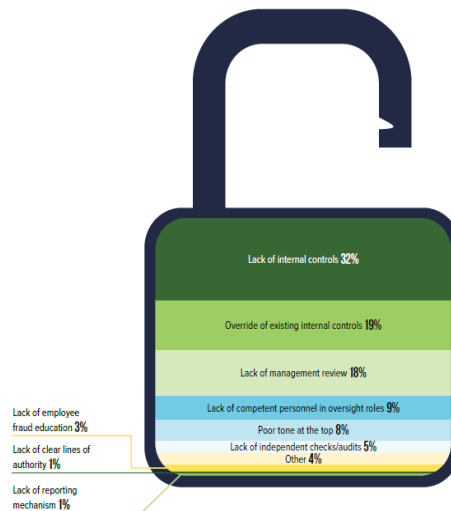


# The Primary Internal Control Weaknesses that Contribute to Occupational Fraud are:

## INTERNAL CONTROL WEAKNESSES THAT CONTRIBUTED TO THE FRAUD

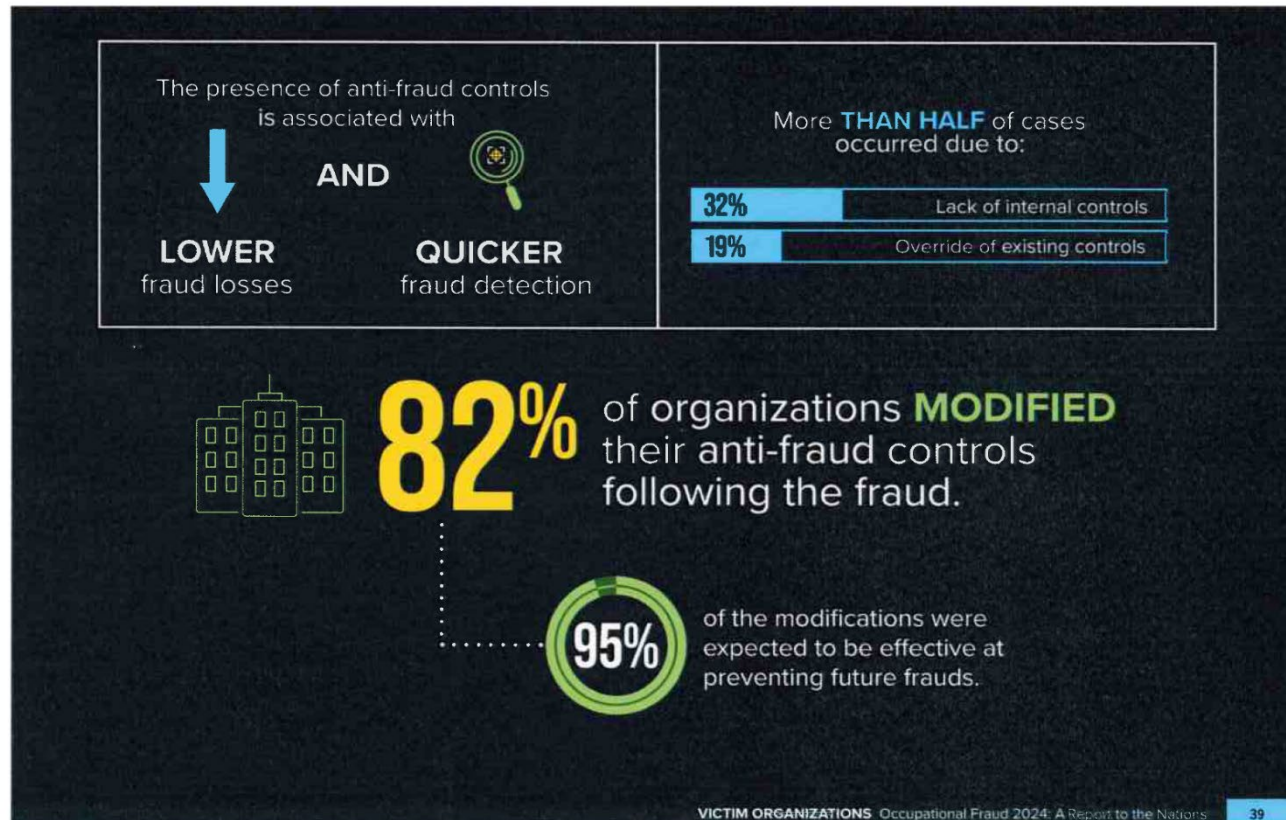
Understanding the factors that led to a fraud's occurrence can assist organizations in strengthening their anti-fraud program to protect against future frauds. Figure 37 shows that the most common contributor to the frauds in our study was a lack of internal controls (32%), followed by an override of existing internal controls (19%). Taken together, this means that more than half of the cases occurred due to an insufficient system of internal controls.

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



The presence of anti-fraud controls is associated with **LOWER** fraud losses and **QUICKER** fraud detection.

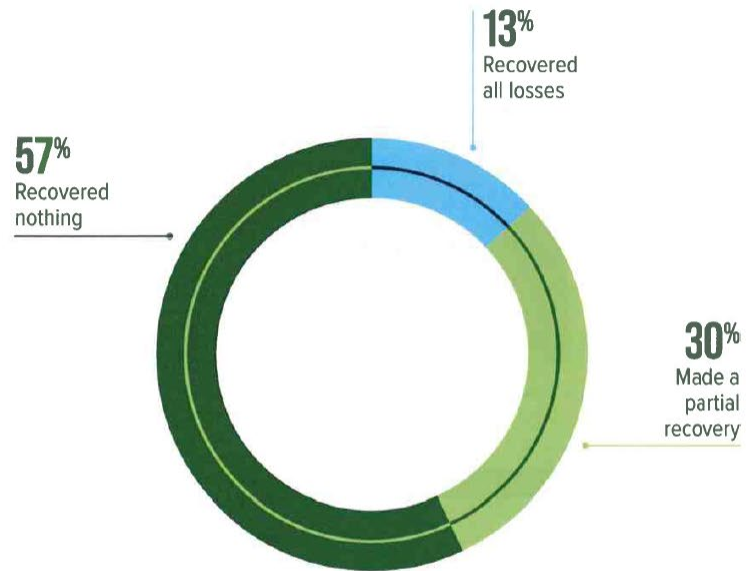
More than half of the cases occurred due to  
**32% Lack of Internal Controls** and **19% Override of Existing Controls**



# Recovering Fraud Losses

- ▶ The decision whether to pursue legal action, internally punish, or come to a settlement agreement with perpetrators is often based on the chances of successfully recovering the funds and assets lost to fraud. Unfortunately, regardless of the path chosen, Organizations frequently fail to recover any fraud losses.

FIG. 60 HOW SUCCESSFUL WERE ORGANIZATIONS AT RECOVERING LOSSES FROM FRAUD?



# Best Practices

- ▶ Think about it and ask yourself:
  - ▶ - Is what I'm doing permitted by law?
  - ▶ - Is it covered by the Professional Code of Ethics?
  - ▶ - What does my trusted colleague say?
  - ▶ - Would other people think this is right?
  - ▶ - Can I defend this action to myself?
  - ▶ - Can I perform this action with a clear conscience?
  - ▶ - What does my inner voice say?



# Let's Fraud Risk Assess Your BOE

Think about your particular BOE and the probability and possibility of a fraudulent event occurring within the BOE. Consider your specific:

- ▶ Internal Controls
- ▶ Internal Control Environment
- ▶ Resources available to prevent, detect, and deter fraud

# How are Your BOE's Physical Controls?

- ▶ Physical controls in place to control access to the accounting records and information?
- ▶ Physical controls in place to protect the assets of the BOE?

# Are there any Skimming Schemes or Cash Larceny Schemes at your BOE?

Possible Skimming Schemes that may be at your BOE or in your individual schools?

- ❑ Collecting cash but not recording the receipt? (It never goes through the accounting records)
- ❑ Collecting cash, keeping a portion of the cash and underreporting the receipt?
- ❑ Stealing cash at the point of the transaction? (Sporting Events)
- ❑ Stealing cash from bank deposits?

# Are there any Check Tampering Schemes at your BOE or individual Schools?

Possible Check Tampering Schemes that may be at your BOE or in your individual schools?

- ❑ Forged maker schemes, which involve forging an authorized signature on the check?
- ❑ Forged endorsement schemes, which consist of forging the signature endorsement of an intended recipient of the check?
- ❑ Altered payee schemes, which involve changing the payee designation on the check to the perpetrator or an accomplice?
- ❑ Authorized maker schemes, when an employee with signature authority writes fraudulent checks for their own benefit?

# Are there any Purchasing Schemes at your BOE or Individual Schools?

Possible Purchasing Schemes that may be at your BOE or in your Individual Schools ?

- ❑ Shell company schemes, which occur when an employee submits invoices for payment from a fictitious company which is controlled by the BOE employee?
- ❑ Pay-and-return schemes, which occur when an employee arranges for overpayment of a vendor invoice and pockets the overpayment amount when it is returned to the company.
- ❑ Personal purchase schemes, which occur when an employee submits an invoice for personal purchases to the BOE for payment or on the BOE's credit card.

# **Are there any Payroll Schemes at your BOE?**

Possible Payroll Schemes that may be at your BOE ?

- ❑ Ghost employee schemes, which occur when a person not employed by the BOE is on the payroll?
- ❑ Overpayment schemes, which occur when a BOE pays an employee based on falsified hours and rates?

# **Are there any Expense Schemes at your BOE?**

Possible Expense Schemes that may be at your BOE ?

- ❑ Fictitious expense schemes, which occur when an employee invents a purchase and seeks reimbursement for it?
- ❑ Multiple reimbursement schemes occur when an employee submits a single expense for reimbursement multiple times? Submitted to the BOE and the School.

# **Are there any Corruption Schemes at your BOE?**

Possible Corruption Schemes that may be at your BOE ?

- ☐ Bribery schemes?
- ☐ Kickback schemes?
- ☐ Bid-rigging schemes?
- ☐ Illegal gratuities schemes?



# **Are there any Conflict of Interest Schemes at your BOE?**

Possible Conflicts of Interest Schemes that may be at your BOE ?

- ❑ Purchase and Sales schemes, which involve the overbilling or underbilling of a company for goods or services by a vendor in which an employee or board member has an undisclosed ownership or financial interest?

# Key Takeaways



- Having Professional Ethics is to uphold integrity, objectivity, and competence in all financial dealings. We must be honest, truthful, and transparent in all professional interactions.
- We are expected to avoid conflicts of interest and respect confidentiality.
- Ethics is a system of moral principles.
- Develop strong internal controls, have sufficient oversight, and plan for a system of routine and surprise monitoring.
- Trust But Verify!



# Questions/Comments?

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