



Ethics and Fraud Prevention in School Districts

PRESENTED BY

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Today's Schedule

Part 1 – The F word.

Part 2 – Reality checks close to home.

Part 3 – Take back control!



What is Fraud?

- A false representation of a matter of fact—whether by words or by conduct, by false or misleading allegations, or by concealment of what should have been disclosed—that deceives and is intended to deceive another so that the individual will act upon it to his or her legal injury.



2016 Fraud Facts

- Association of Certified Fraud Examiners 2016 Global Fraud Study



5%

Fraud costs the average organization
5% OF ITS REVENUES EACH YEAR.



58.4% OF VICTIM ORGANIZATIONS
don't recover any of their losses.



2016 Fraud Facts

- Association of Certified Fraud Examiners 2016 Global Fraud Study
 - In **94.5%** of the cases in our study, the perpetrator took some efforts to **conceal** the fraud. The most common concealment methods were creating and altering physical documents.
 - The most common detection method in our study was **tips** (39.1% of cases), but organizations that had reporting **hotlines** were much more likely to detect fraud through tips than organizations without hotlines (47.3% compared to 28.2%, respectively).
 - Small organizations had a significantly lower implementation rate of anti-fraud controls than large organizations. This gap in fraud prevention and detection coverage leaves small organizations **extremely susceptible** to frauds that can cause significant damage to their limited resources.



The Average Perpetrator



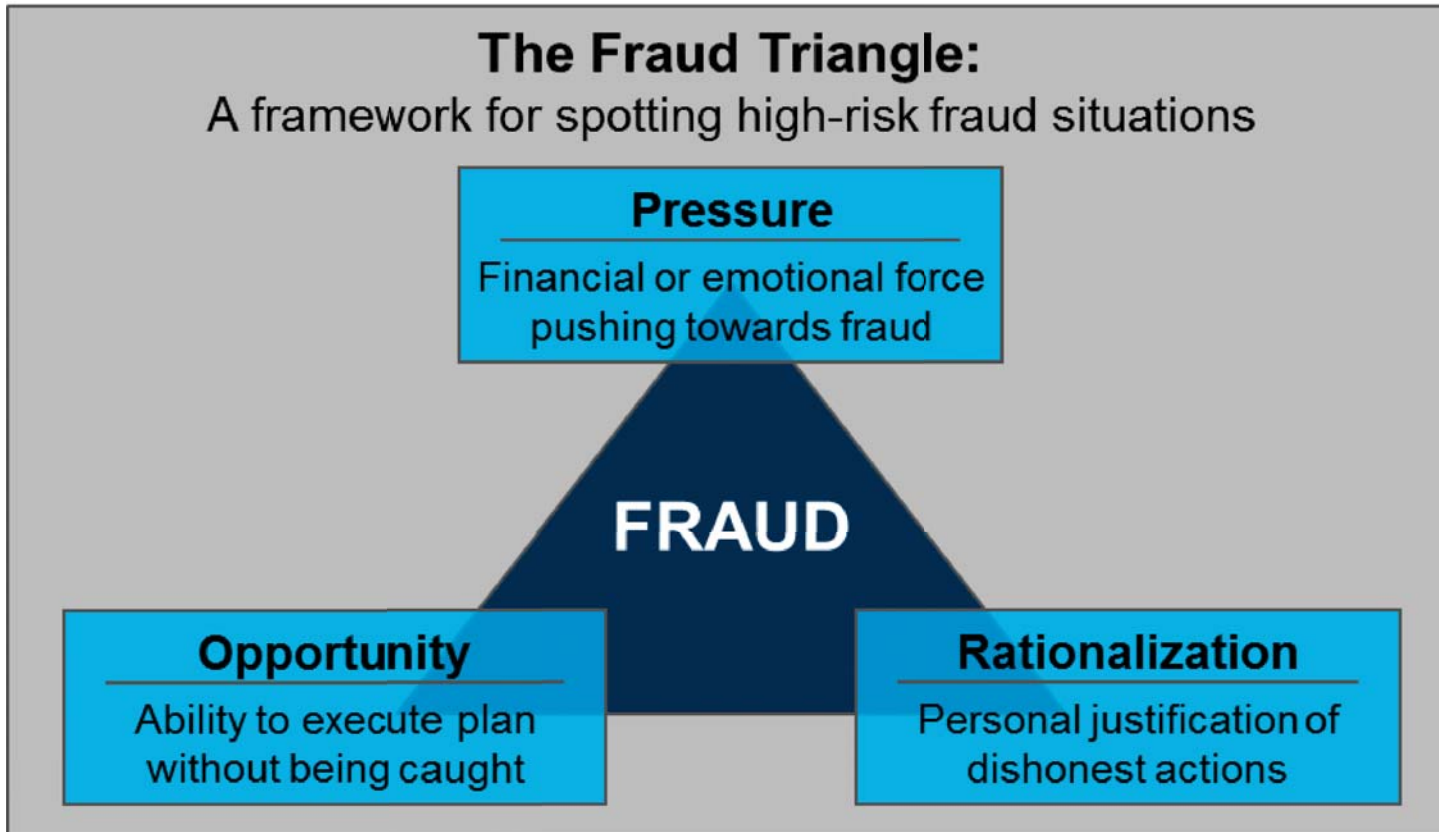
- There are typically no distinguishing factors.
- Most occupational fraudsters are first-time offenders.
- Perpetrators typically have profiles that look like honest people.
- Correlation between fraud losses and the level of authority.
- Fraud losses tend to increase with longer tenured employees.
- 69% male, 31% female (may be more related to labor force makeup).

In nearly 80% of fraud cases, at least one red flag is present.



The Fraud Triangle:

A framework for spotting high-risk fraud situations



Pressure

- Financial hardship
- Personality changes
- Living beyond one's means
- Outside business interests
- Unwillingness to share workplace duties



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**I am
underpaid!**

**I volunteer, I
deserve something.**

**The boss steals,
why not me!**

**I am working
more and getting
paid less!**

It's just a loan!



Opportunity

- Fraudsters don't wish to be caught, so they must believe their activities will be undetected
- Opportunity is created through WEAK internal controls and poor oversight
- Districts have the most control over this leg of the fraud triangle



Common Red Flags

- Individuals living beyond their means
- Unusually close associations between employees and vendors
- Financial or marital difficulties at home
- Excessive control issues
- A general “wheeler-dealer” attitude involving unscrupulous behavior

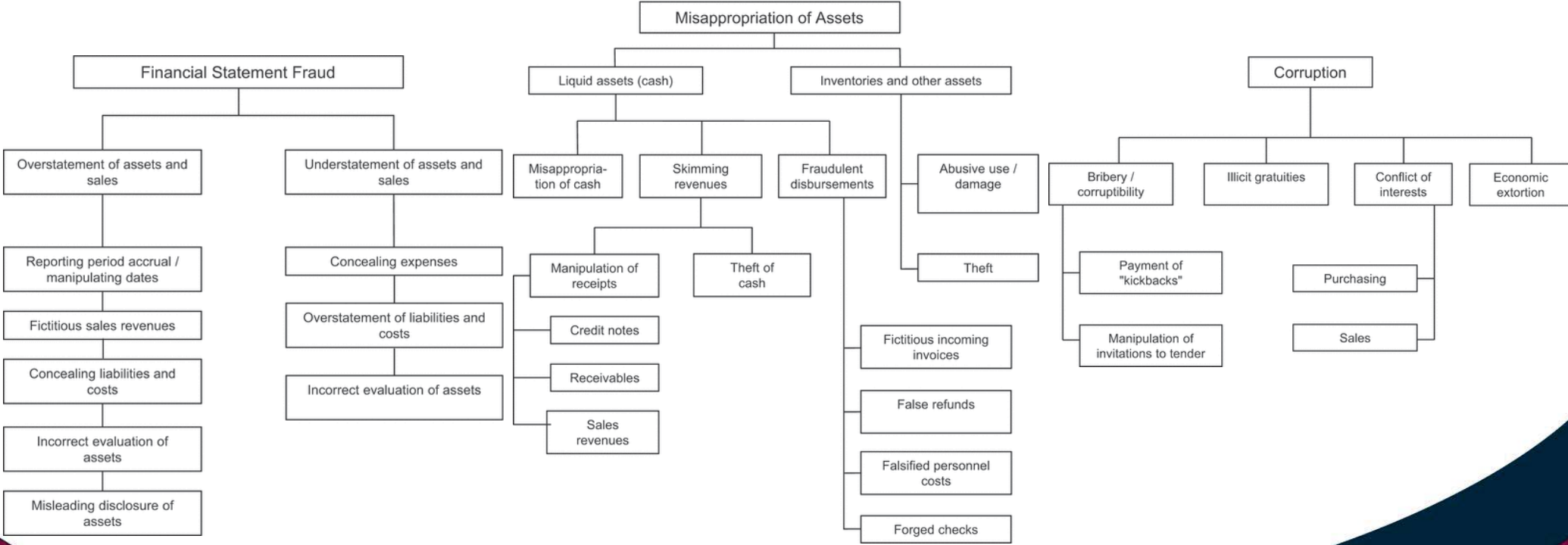


Three Most Common Types of Fraud

- Financial Statement Fraud
 - Least Common – Less than 10% of Cases
 - Largest \$\$ - Median Loss \$975,000
- Corruption
- Asset Misappropriation
 - Most Common – 83% of Cases
 - Smallest \$\$ – Median Loss \$125,000



The Fraud Tree



Michigan Schools in the News

- Ecorse Public Schools (2009) – Former assistant superintendent was charged with steering contracts to a company that he controlled, and required to repay over \$1 million in restitution for fraudulent conduct related to the district's e-rate program.
- Montcalm Area Intermediate School District (2009) – Similar to Ecorse, former superintendent indicted for engaging in a conspiracy to accept a bribe from a vendor to ensure vendor's company was selected for e-rate service contract.
- Royal Oak (2011) - High School principal was sentenced to 2 years probation after embezzling thousands of dollars from student activity accounts.



Michigan Schools in the News

- Sand Creek Schools (2016) - The former president of the High School music program booster club entered a plea deal in exchange for reduced charges related to his theft of \$13,000 from the club and was sentenced to 30 days in jail instead of the five-year prison term he might have received.
- Mona Shores Public Schools (2016) – The district has recovered about a third of the \$3.7 million it lost in a Ponzi Scheme operated by the district's former financial advisor. The advisor never purchased bank certificates of deposit that his clients had given him money for. Instead, he used the money to pay off other investments, gamble, buy personal items and real estate and make loans.
- Jackson Public Schools (2017) – Former middle school principal pled guilty to embezzling school funds. She fraudulently wrote checks out of the school's Principal Fund for personal use in excess of \$97,362.



Detroit Public Schools

- Employee received \$50,000 in salary overpayments
- \$2,500 of field trip collections disappeared
- Employee manipulated a lottery process to benefit his tutoring company in an estimated \$1.3 million contract
- \$59,000 of falsified overtime paid out to an employee
- Vendor received payment for services not rendered
- \$1.275 million over seven years of grant billings for tutoring services never delivered
- Vendor fraud for textbooks and other supplies that cost the District an estimated \$2.7 million



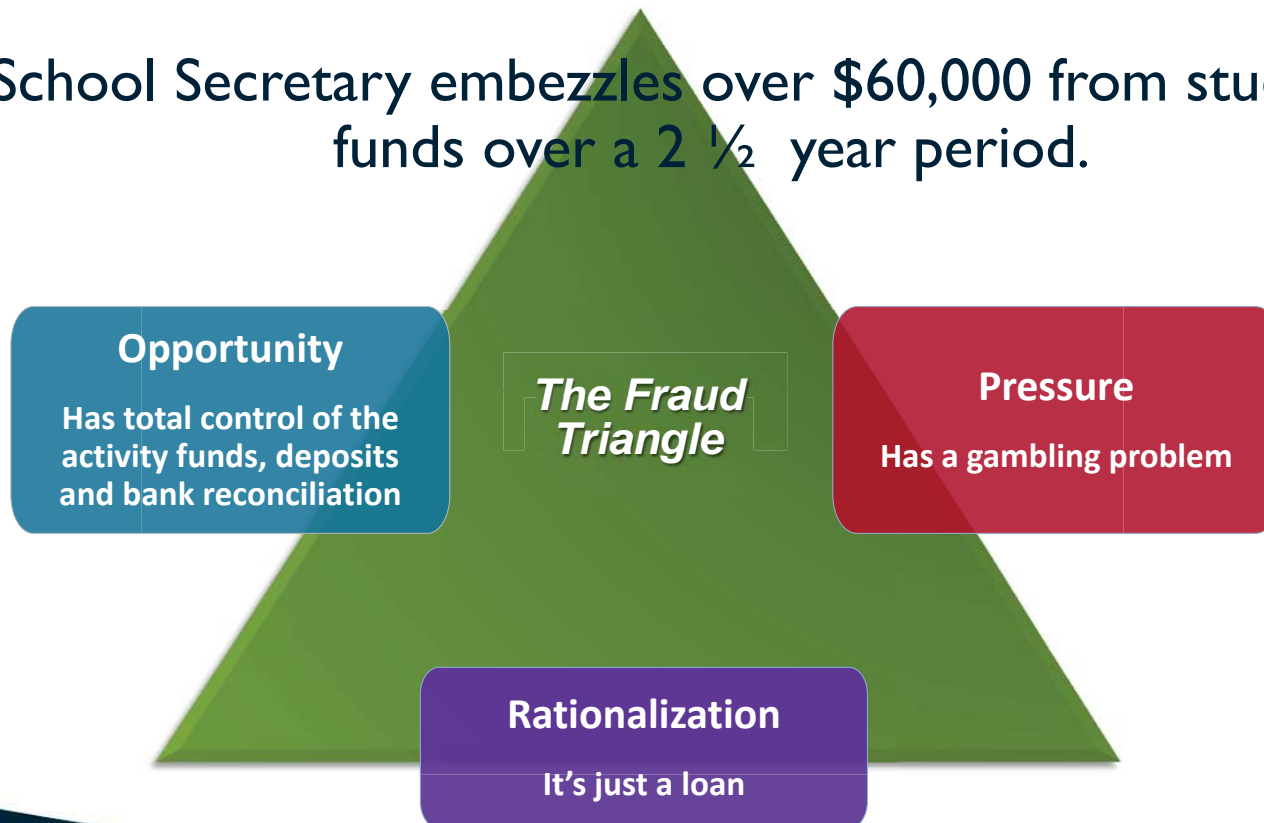
Fraudster – I, School District – 0

- Fictitious vendors
- Theft of athletic receipts
- Use of food service supplies for personal catering business
- Phantom employees
- Skimming payroll taxes
- Purchasing construction supplies for residence from bond money
- Falsification of records by third party service provider



Example

High School Secretary embezzles over \$60,000 from student activity funds over a 2 ½ year period.



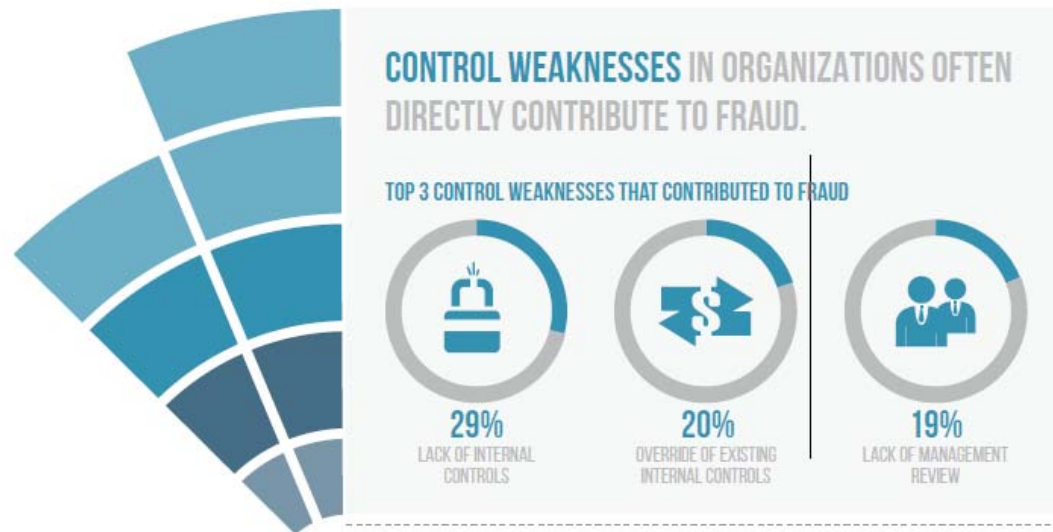
Five Tools for Fraud Prevention

1. Establish strong internal controls
2. Implement hotlines
3. Perform surprise audits
4. Utilize data analysis
5. Train employees



Establish Strong Internal Controls

Association of Certified Fraud Examiners 2016 Global Fraud Study



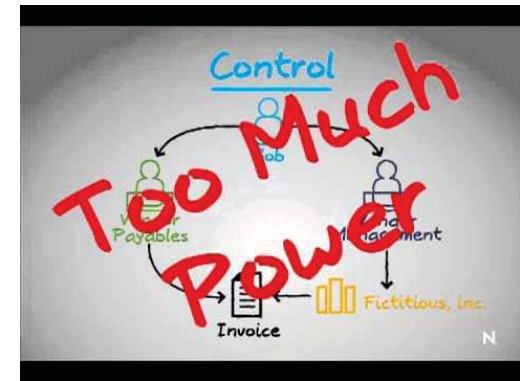
Best Defense is a Good Offense

- Solid internal controls, implemented and followed correctly, are the **BEST** deterrent to fraud.
- Policies and procedures designed to provide reasonable assurance that assets are safeguarded against unauthorized use and disposition.
- Imperative controls include:
 - Segregation of duties
 - Examining supporting documentation
 - Reconciling bank statements (timely)
 - Safeguarding assets



Segregation of Duties

- Certain accounting functions are designed to cross reference each other for accuracy.
- Giving a single person unquestioned authority of finances is not a wise business practice.
- Checks and balances eliminate the opportunity for fraud or abuse.



Segregation of Duties

Activity	Collecting Cash/ Payments	Depositing/ Recording	Control Activity
Handles and processes currency, checks, and credit cards.	XXXX		
Enters transactions into the cash register system.		XXXXX	
Prepares cash balancing or reconciling cash register to cash on hand.			XXXXX
Performs reconciliation of credit card receipts to end of day report.			XXXXX
Prepares bank deposit and bank deposit slip.		XXXXX	
Review of cash balancing			XXXXX
Compares cash balancing report to bank deposit.			XXXXX

For proper segregation of duties, an individual should not be performing duties in different columns of the matrix.



Examining Supporting Documentation

- Enhances communication and serves as a final checkpoint.
- Verify cash deposited agrees to records of cash collected.
- Never sign a blank check or check without original supporting documentation.
- Question new vendors or non-recognizable vendors before authorizing purchases.



Reconcile Bank Statements

- Reconciliations only flag discrepancies if they are performed on a timely basis.
- Unusual or unexplained reconciling items should always be questioned.
- Should not be performed by the person writing the checks or making deposits.
 - Person writing the checks should not have authority to sign checks.



Safeguard Assets

- Access to important documents and supplies should be limited
- Cash and checks should be deposited timely
- Blank check stock should be secured
- Individuals with access to these items should be screened and monitored



Cash Handling Guidelines

- Separate the components of cash handling – collecting, depositing, and reconciling
- Pre-numbered receipts for cash received in person
 - Sequentially numbered tickets at events
- Stored in a secure location until deposited
- Timely reconciliation prepared, reviewed, and maintained



Think Like an Auditor

- All copies of voided receipts are retained and show the reason for cancellation across the face of the receipt
- Mathematical accuracy of receipt reports is periodically verified
- Support is reviewed for appropriate signatures
- No receipts are missing
- Receipts are issued in numerical order



Implement Hotlines

- Provide a confidential service for reporting fraud through email, telephone, or a website.
- This can allow tips from internal/external sources to be pursued immediately.
- Ensures an open-door policy for employees to speak freely about pressures and threats.
- Helps employees to have the peace of mind that they can report suspicious activity without fear of reprisal.



Perform Surprise Audits



- Call local banks to determine if there are accounts you are not aware of being used by your District.
- Verify addresses on new vendor invoices to ensure it is a legitimate company.
- Review cleared checks for a break in sequences.
- Perform an unplanned audit of petty cash, inventory, etc.
- Observe cash collections at a sporting event or lunch service.



Utilize Data Analysis

- Association of Certified Fraud Examiners 2016 Global Fraud Study:

“The 36.7% of victim organizations that were using proactive data monitoring and analysis techniques as part of their anti-fraud program suffered fraud losses that were 54% lower and detected the frauds in half the time compared to organizations that did not use this technique.”



Train Employees

- Train employees as to what constitutes fraud, and how it impacts the District (publicity, job loss, morale, etc.)
- Ensure employees understand where to seek advice when they are faced with uncertain ethical decisions.
- Communicate a policy of zero-tolerance through words and actions.
- Provide employees a confidential outlet to report suspicious or fraudulent activity.
- Instruct employees on how to recognize red flags and early warning signs.



Fraud Prevention Tips

- Set a strong tone at the top
- Enforce internal controls
- Evaluate segregation of duties
- Train staff
- Think like a thief
- Know your employees
- Don't allow exceptions
- Trust, but verify!





See the Association of Certified Fraud Examiners Checklist at:
<https://www.acfe.com/rtnn2016/docs/2016-report-to-the-nations.pdf>

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A photograph of three business professionals in a modern conference room. A woman in a light blue blazer stands in the center, holding a folder and smiling. Two men in suits are seated at a long, reflective table. One man on the left is gesturing with his hand while talking to the woman. The man on the right is looking at a laptop. The room has large windows in the background, and the table reflects the people and the room.

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Thank you!

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