

Fraud Prevention Tip of the Month from



DO YOU KNOW WHO YOU'RE PAYING?

September 2010

Did you know that small businesses are the hardest hit by fraud? The median loss suffered by organizations with fewer than 100 employees was \$200,000 in 2008! That's the bad news. The good news is that implementation of anti-fraud controls has a measurable impact on an organization's exposure to fraud.

PAYROLL FRAUD HAPPENS EVERY DAY

Payroll fraud can take many forms - from falsifying hours worked on timecards and the addition of "ghost" employees, to commission schemes and workers compensation fraud. Payroll fraud makes up nearly 9% of all fraud cases globally, with a median loss of \$72,000. For some small businesses, this level of loss can be crippling.

Source for statistics: 2010 Report to the Nation on Occupational Fraud & Abuse - Association of Certified Fraud Examiners.

HOW ARTHUR GAVE HIMSELF A RAISE

Let's take a look at an example of a ghost employee scheme perpetrated by Arthur, a payroll clerk at XYZ Manufacturing, a company with 65 employees and \$15 million in revenue.



Arthur was a nice guy, by all accounts. That made it all the more surprising when his employers began to implement anti-fraud controls and determined that Arthur had stolen \$830,000 over a period of three years. As the payroll clerk, Arthur had access to the employee master file. He had authorization to add and delete employees from the system as the company hired and terminated personnel. It wasn't long until Arthur realized that if he did not delete terminated employees from the master file, he could continue to pay these "ghost" employees who no longer worked for the company and deposit their pay directly into his bank account! Since the company was growing rapidly and the controller only seemed concerned

with the total amount of payroll expense, Arthur was able to continue his scheme undetected for over 3 years!

PROTECTING YOURSELF AND YOUR COMPANY FROM PAYROLL FRAUD

Segregation of duties for payroll job functions such as timekeeping, authorization of timecards, payroll preparation, payroll distribution, paycheck signing, payroll bank reconciliation, and human resource department functions is probably the single most important payroll fraud control.

Following are examples of additional controls that can greatly reduce the risk of payroll fraud losses:

- Require written supervisor authorization on time cards.
- Require written supervisor authorization for all overtime.
- Keep check stock, signature stamps, and automated check signers under lock and key.
- Look periodically for anomalies in employee master file, including duplicate social security numbers, addresses and bank account numbers.
- Review payroll for checks in round dollar amounts (e.g., \$500, \$750, \$1000)

For more information on fraud prevention and detection, please call Lori Payne at (805) 527-1499.

About Payne Financial Forensics

Payne Financial Forensics is a financial consulting firm, specializing in Forensic Accounting; Fraud Investigations; Litigation Support, including Bankruptcy and Insolvency related litigation; and Expert Testimony.

With a middle market focus, our professionals have broad experience in financial consulting and are credentialed as Certified Public Accountants, Certified Fraud Examiners, Certified in Financial Forensics, and Certified Insolvency and Restructuring Advisors. Payne Financial Forensics provides personalized service by senior professionals with big firm experience and expertise at a reasonable cost.

Lori L. Payne, CPA/CFF, CFE, CIRA
Payne Financial Forensics
(805) 527-1499
www.PayneFF.com