

# Tackling Fraud: Make a Game Plan to Protect Your Business

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If you're a business owner, you know that workplace fraud is a legitimate threat. Recent estimates put the cost for U.S. businesses at a whopping \$20 billion to \$50 billion a year. What can you do to protect your company? Having internal controls in place will help minimize your risk of fraud and could save your business from losing thousands of dollars. Don't just sit around and wait until it happens to do something about it.

## Start at the top

It sounds simple, but the attitudes of business owners and top management set the tone for the *entire* company. That's why it's important for them to foster an environment of high ethical standards. They should show a strong interest and approval in employees doing the right thing and make it known that fraudulent or unethical behavior will not be tolerated. If you want your employees to be vigilant in preventing, identifying and reporting fraud, then you must lead by example.

## Fraud risk assessment

You need to take a "big picture" look at your company and perform a fraud risk assessment to identify areas that may be vulnerable to fraud. What types of transactions occur within the business? What types of assets does it hold where fraud could occur? These questions can help you determine which controls work best for your business.

Performing a fraud risk assessment shouldn't be a one-time deal. It should be a recurring process as your company grows, brings in new business, or adds new revenue streams. You should always be on the lookout for where things need to change. You should also incorporate a consideration of fraud risks into discussions regarding changes within the company *before* making any decisions.

## Make it a team effort

It usually takes more than one person to stop fraud, so put together a team that is responsible for the fraud risk assessment. It can be made up of management or employees. Because fraud risk assessment is an ongoing process, the team can look at and monitor issues such as internal control breakdowns or new aspects of the business that could lead to a greater risk for fraud.

Be sure to keep management in the loop on this. It is key for them to understand how the business as a whole works and how internal controls apply to all aspects of the business. This means even more eyes are on areas that could be vulnerable to fraud. Keeping management up-to-date doesn't have to be formal – discussions or progress reports can be incorporated into weekly or monthly meetings.

## Are the necessary controls in place?

You need to have two types of controls in place: preventive and detective. Yes, it is important to stop fraud before it happens – that's where preventive controls come into play. But perhaps, even more important is your ability to identify fraud that might *already* be going on. If you don't have detective controls, employees who may be committing fraud will continue to get away with it, costing you money.

### Detective controls

1. **Employee Responsibilities.** Ensure that all of your employees take vacation time. If an employee on vacation is committing fraud, the person filling in for him or her may stumble onto something fishy.

Also, have backup processes in place for certain transactions. This, again, gives someone else the opportunity to see if something unusual is happening. Have an employee who steps in on a recurring basis so that not just one person is doing the same job throughout the year. Having a backup plan also helps during busy times because you have a go-to person to help shoulder those responsibilities.

2. **Lifestyle changes.** Take note of any major lifestyle changes for your employees. For example, if someone suddenly drives a much more expensive car – that could be a warning sign that something suspicious is happening. Also, be aware of financial difficulties or gambling habits – any scenario that may put people in a situation where they feel they need to steal.

### Preventive controls

1. **Inadequate recordkeeping.** To expose fraud and, equally important, to be able to prove it, you must keep detailed records. For example, if proper accounting procedures are not put in place to cover cash disbursements, it will be difficult to find out if someone is stealing. Shoddy accounting records also give employees an opportunity to easily cover up fraud.
2. **Unusual cash transactions.** Any significant differences between cash expectations and actual receipts should be quickly investigated. Frequently, an employee will try to embezzle funds by writing checks to himself or herself and signing the employer's name on the checks. Because of the nature of cash itself, the disbursement or receipt of it is an area that is ripe for fraud opportunities to arise.
3. **Segregation of duties.** It is very important that you integrate segregation of duties within your organization to the fullest extent possible. This involves segregating incompatible duties over the custody of assets, authorization or approval of related transactions affecting those assets, and recording or reporting of the related transactions. For example, the person in your organization who authorizes inventory purchases should not be responsible for maintaining custody of the inventory nor be responsible for processing the payments for the inventory.

Many small businesses may not have adequate personnel to institute complete segregation of duties. In that case, ask yourself, *what can we do with what we have?* There are many incompatible duties that can

be segregated between as little as two employees. Furthermore, adequate management oversight and involvement in certain duties helps compensate for any incompatible duties resulting from a small office staff.

4. **Lack of physical safeguards.** Start with simple precautions such as sticking identification tags on computers or locking down expensive equipment so it cannot be moved easily. Always make sure that safes and other valuables, such as data and records, are secure. Lock office doors after hours, and limit access to sensitive areas whenever possible.
5. **Suspicious documents.** Be wary of invoices, purchase orders, checks, expense reports, time cards, etc., that do not pass the “smell test.” In some companies, the fraudsters may even arrange for fictional employees to be paid salaries. Make sure that payment procedures are carefully followed.

## What to do if you uncover fraud

If you discover that an employee is stealing from your company, you should go through your human resources department to take immediate steps to terminate the employee.

Next, you need to determine if any charges should be filed. This would be a joint effort with human resources and your corporate attorney. Bringing charges, even for something small like improper travel reimbursements, not only shows that fraud won't be tolerated, it can also help deter other employees from committing fraud in the future.

Once you've handled the employee, you will want to plug the holes you uncovered. Why and how did the fraud occur? Look to see where procedures were circumvented and put new policies in place to make sure it doesn't happen again. Use this as a lesson and an opportunity to see where improvements are needed.

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