

# 21ST CENTURY FINANCIAL CONTROLS

## USING TECHNOLOGY TO STOP FRAUD IN ITS TRACKS

The impact of fraud on today's businesses is staggering. According to the Association of Certified Fraud Examiners, U.S. organizations alone lose approximately \$65 billion annually—or an estimated 5% of their revenues. Research by the same organization shows internal controls are failing to stem the tide and successfully detect *less than two out of 10* fraud cases.

Nowhere is the risk greater than in the procure-to-pay cycle, which typically represents a company's largest annual outlay. Fraudsters simply follow the money.

But why do internal controls fail to catch disbursement fraud? One reason is that the vast majority of perpetrators are trusted employees. Many are familiar with internal financial controls and know how to fly beneath the radar. When a member of the accounts payable team for a Fortune 50 company decided to bilk her employer, she simply established her brother as a fake vendor and paid him \$9,999 weekly. The invoice amount was a dollar shy of the \$10,000 limit requiring a second authorization. This well-constructed scam put the employee on track to net more than \$500,000 a year.

Internal controls also fail because of the sheer volume of transactions that pass through an accounts payable shop. Most companies find it virtually impossible to manually screen each vendor or invoice for fraudulent trends and anomalies—especially in time to catch errors *before* dollars go out the door. So instead they rely on periodic sampling.

The sampling approach has serious limitations, though. Experience shows the greatest potential for fraud is at lower spending limits where businesses have the

largest number of vendors and invoices. That means huge data sets are needed for sampling to be effective. Both the time and expense involved are simply beyond the reach of most organizations.

### THE POWER OF CONTINUOUS FRAUD MONITORING

For decades, accounts payable teams have searched for a way to cost-effectively analyze every vendor and every invoice for fraud before payments are disbursed. The good news is that software programs for continuous fraud monitoring are now readily available. These automated tools can help

*For decades accounts payable teams have searched for a way to cost-effectively analyze every vendor and every invoice for fraud before payments are disbursed. The good news is that software programs for continuous fraud monitoring are now readily available. These automated tools can help a company shore up its internal controls and detect and prevent fraud comprehensively.*

a company shore up its internal controls and detect and prevent fraud comprehensively.

Effective fraud detection programs analyze vendor databases, employee records, and invoice and payment activity for suspicious patterns and high-risk characteristics—from vendors and employees who

share the same mailing address to invoice or payment amounts that fail to match expected patterns.

Companies can use these powerful new fraud detection tools in two ways. First, they can perform a retroactive audit to uncover and halt fraudulent activity overlooked in the past. Many find they recoup their investment in fraud detection software with this single data sweep. For example, a large retailer recently used detection software to analyze 100,000 vendors and rank the 100 most risky. Investigations confirmed approximately 40 of the top 100 were indeed fraudulent, representing *tens of millions* in revenue.

In addition to retroactive audits, fraud detection software can be used to intervene and prevent losses proactively before a payment is disbursed. Companies can easily and cost-effectively monitor ALL data continuously—not just a sample.

In both instances, the software produces an automated report rank ordering risky vendors and invoices. Using the report, companies can further investigate potential fraud or policy violations, intervene and protect hard-earned revenues, or shore up controls and policy enforcement. These same reports can be used to uncover systemic process weaknesses.

Finally, continuous fraud detection has the added benefit of helping companies comply with Sarbanes-Oxley regulations and readily demonstrate to independent auditors an ongoing, proactive commitment to improved financial accountability.

### BEST PRACTICES: WHAT TO LOOK FOR IN FRAUD DETECTION SOFTWARE

Companies who want to add automated fraud detection to their arsenal should look for a solution that adheres to industry best practices and is backed by experts who can help them get the most out of their technology investment. Here are a



few of the important features of best-in-class fraud detection software:

- » Reviews *all* data routinely, not just a sample.
- » Provides a continuous auditing framework from supplier setup through invoice reconciliation.
- » Analyzes a wide range of vendor and invoice attributes right out of the box without the need for costly scripting.
- » Features ready-to-use templates that are easily configured to precise specifications.
- » Requires minimal IT involvement to produce the data to be analyzed.
- » Spots internal collusion by comparing employee data to vendor files and payment information.
- » Protects companies from stiff penalties by incorporating current information from government “watch lists” of 7,000+ individuals, companies, and countries.
- » Provides actionable results packaged in easy-to-read reports that rank order potential risks, minimize the number of false positives, and capture the information needed to intervene.
- » Is backed by a company that invests in R&D and evolves its analytics to keep up with savvy fraudsters.

There are three deployment models companies can use to integrate fraud monitoring into their accounts payable operations. First, the software can be licensed for use on a company's own premises. You simply install it on a server and immediately begin to reap the benefits.

As an alternative, companies can access fraud detection software over the Web as a managed service. The advantage of this approach is that on-demand subscription pricing options allow you to add new licenses quickly in response to changing demands.

If you're not ready to invest in fraud detection software or to sign up for a managed service, you can look for a recovery audit partner who incorporates fraud detection applications into the recovery audit process.

### **Risk Factors for Fraud**

*Here are a few of the risk factors for fraud that can be monitored by continuous detection software:*

- *Initials in a vendor's name*
- *Multiple vendors at the same address*
- *High risk zip codes or country codes*
- *Use of a private mail service*
- *Prison addresses*
- *Match between employee and vendor data*
- *Consecutive invoice numbering*
- *Lack of a purchase order*
- *Even dollar gross amount*
- *Small first payment relative to the average payment*
- *Government-prohibited vendors*
- *Known scam vendors*

One caution: There are a number of popular enterprise resource management solutions on the market that support accounts payable operations. Don't be lulled into thinking these systems are enough to help your company detect and prevent fraud. They aren't set up for that purpose and don't have the in-depth capabilities required to get the job done. Instead, look for a provider who specializes in accounts payable disbursement audits and in industry best practices for fraud detection.

### **SLEEP-AT-NIGHT INSURANCE**

Much of what companies lose to fraud is never recovered. The cost of prosecution can be high, and it often exceeds the amount lost. Guilty individuals may be unable to make restitution. In addition, a company's reputation among shareholders and customers can be damaged if word gets out—making it appear that you have inadequate internal controls and have failed to be a good financial steward. That makes prevention the best solution of all. If you've incorporated comprehensive prevention controls, you can sleep at night and rest assured that you're protecting your firm's hard-earned assets and reputation. ■

APEX Analytix is an innovative audit recovery firm serving more than a third of the Fortune 100. The company has transformed the audit recovery industry with FirstStrike™, a highly functional family of standards-based software that detects and prevents both errors and fraud and improves performance across the procure-to-pay process. To date FirstStrike™ has saved businesses more than \$1.5 billion in overpayments and is the most widely used software of its type. For more information, call 800.284.4522 or visit [www.apexanalytix.com](http://www.apexanalytix.com).

### **Free fraud risk evaluation**

To schedule a free evaluation of your fraud risk, contact APEX Analytix today at 1.800.284.4522.

