



HOW I WORK...

TRISHA STRAIN



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Six Steps to Combating Internal Fraud

The Association of Certified Fraud Examiners has released a report entitled “Occupational Fraud 2022: Report to the Nations,” a review of over 2,110 occupational fraud cases, reflecting losses of over \$3.6 billion dollars. The report reveals that the average case of fraud lasted 12 months before it was discovered, and cost around \$100,000. In addition, the annual losses for internal theft are estimated by this report at 5% of an organization’s revenue for the year.

HOW DOES INTERNAL FRAUD HAPPEN, AND WHO IS RESPONSIBLE FOR IT?

This has always been a topic of discussion when Management and Security get together. All institutions will eventually face cases of internal fraud, and this may be a sign that bigger problems exist. If an organization has faced numerous incidents of internal crime, this could reflect a lack of internal controls, a Management that doesn’t require accountability, or poor hiring practices.

Q. Tell us your background/how you got here.

A. My background is a little different. I graduated with a degree in Hospitality Management. I managed hotels and resorts for almost 20 years. Then I moved back to my hometown of 1,200 people, which was not exactly a booming town of hospitality opportunities. I had to do some soul searching and figure out what I wanted to do. I knew I didn’t want to work nights, weekends, or holidays anymore. I started working at the bank as a teller, since it met all these requirements. I really enjoyed it; I got to use my hospitality skills when interacting with customers

Continued on page 2

Continued on page 2 »

Another factor in determining how prone an organization is to internal fraud is the attitude of Senior Management and the Board. Let's review three questions critical in determining if an institution is dysfunctional and prone to fraud:

- » Does Management view itself as superior to Staff?
- » Has an elitist attitude been displayed by the Board or Senior Management?
- » Does Middle Management try to make things easier for Staff because of perceived abuse by Senior Management?

Warning signs such as these should be reviewed by anyone looking at an organization for signs of internal problems. People don't work well in an environment where budget restrictions, cost-cutting programs, and benefit reductions apply only to those at the bottom of the organizational pyramid. When such behavior is identified as typical of an institution, Staff will begin to strike back against perceived injustices. Staff members may take advantage of what few perks they have or may become sloppy in their job performance because it doesn't seem to matter what they do.

If Management operates via intimidation of Staff, then job performance might remain acceptable and the institution's financial performance might appear fine. However, the seeds for internal fraud have been planted.

STEPS TO REDUCE INTERNAL FRAUD

1. First, Management Must Be Ethical.

If budgeting and cost-cutting reductions are needed, they must apply to everyone, including Senior Management and the President. Elitism cannot be tolerated. Those who don't believe this should consider such cases in point as Enron, WorldCom, and Bernie Madoff. The Sarbanes-Oxley Act of 2002 is designed to make future abuses more difficult. However, this will not prevent internal fraud from happening altogether.



Continued on page 3

and got to learn new skills. After 10 months, the COO talked to me about training as the internal auditor. The current internal auditor was going to retire in three years so I would have plenty of time to learn and get certified. After a year of training, our compliance officer retired, and the internal auditor took over that position and so I started training for compliance as well.

Q. Briefly describe how you construct your day for optimal productivity.

A. I start my morning by organizing what I have in my come-up file. I organize by priority; what has to get done that day, what should get done, and what can wait until I have time to get it done.

Q. How do you keep track of what you have to do?

A. Each year, I create my folders for the audits/reports that must be completed throughout the year. Each folder gets filed in the month that they will be completed in. On the first day of each month, I pull that month's folders and decide when each audit or report will be completed, and they get filed in that day. Each morning I pull the folders for the day and organize what I need to complete for the day. I also have a monthly schedule in a spreadsheet to make sure nothing gets missed.

Q. Take us through a typical workday.

A. Who has a typical day? Yes, there are always audits or reports to complete. But there is usually

Continued on page 3 »

2. The Second Step to Reducing Internal Fraud Is Setting up the Proper Framework in Your Organization.

A Risk Management Committee should be established and should consist of at least two members from the Board of Directors; the Security Officer; and Senior Officers with responsibilities for Human Resources, Security, and Facility Management.

3. The Third Step Is to Develop an Ethics Policy for the Institution.

The Board of Directors should develop and approve an ethics policy and charge the Risk Management Committee with the task of designing and monitoring it. The committee should review the steps to be taken when a violation of policy occurs. Considerations include:

- » Suspending all suspects until an investigation is over.
- » Reprimanding immediate supervisors who violate internal controls.
- » Prosecuting identified thieves.
- » Firing employees who violate procedures.
- » Protecting employees who report internal problems from future retaliation by management.

In one case I observed, a branch manager never implemented dual control procedures with vault currency. When questioned about this, the manager stated that it was impossible to institute dual control with only six employees. Failure to reprimand a manager in this case would have destroyed internal controls across the entire organization.

4. The Fourth Step Requires the Risk Management Committee to Determine Who Will Investigate a Reported Incident and How.

While this step may seem simple, in many organizations this may not be the case. The Security Officer is normally the only person in the organization trained in conducting investigations. When internal theft occurs, this person will need to work with Human Resources and have access to files, credit reports, and employee evaluations. The Human Resources Director can, therefore, be the greatest help or the greatest hindrance in an internal investigation. Likewise, Internal Audit may also be a problem if it decides to investigate internal fraud without including the Security Department or Human Resources in these investigations.

5. The Fifth Step Is to Open the Lines of Communication Between Staff and Management.

Staff must always feel safe discussing problems with Management. People fail to report fraud for several reasons. Some of these are:

- » Fear of being wrong about someone.

Continued on page 4

a problem that comes up or regulation changes to read that throw kinks into a “typical” day.

Q. What tools/software/resources can't you live without?

A. I cannot live without Excel. I keep my schedule, audit findings and follow-up, report tracking, etc. in Excel. Most of my day is spent using Excel.

Q. Can you share a problem/challenge you're working on or trying to solve?

A. I'm currently working with our core provider on a (hopefully) one-of-a-kind participation loan.

Q. What's the best advice you have for other people in your role?

A. Get certified through ICBA and go to the Annual Certification Conference. Interact with the other attendees. Not only do you meet new friends, but they can also be a resource when you have a problem you can't solve or need help with regulation changes.

Q. What are you currently reading?

A. Miracle Morning by Hal Elrod. I just started reading but it is already impacting how I view life and spend my mornings.

Q. Who are the people who help you get things done?

A. Data processing is great at helping me with issues with our core. Our assistant internal auditor is a huge help when

Continued on page 4 »

- » The person suspected is one's immediate supervisor.
- » A belief that Management just isn't interested.

To reduce these fears, Management should institute a reporting system. Two people should be selected and identified to Staff as the appropriate contacts to whom to report problems. I suggest that the Risk Management Committee select one male and female for this position, with one of them being the Security Officer. This allows Staff to avoid reporting to people by whom they may be intimidated, or with whom they may have personality conflicts. In addition, the organization should have an anonymous hotline-reporting system, an 800 number that employees can access to report suspicions without having to state their names.

6. The Sixth Step Is to Institute a Fraud-Training Program for Employees, or the Steps Recommended Above Will Be Fruitless.

When developing the program, select actual case scenarios of situations the financial institution hopes to avoid. Stress that there will be no retaliation against anyone who reports suspected fraud and be prepared to enforce this. Make sure that fraud training is mandatory for all new hires, from Maintenance to the Board. Everyone should be trained annually and should sign an ethics statement after training or before job promotions. This will ensure that no one can claim ignorance of ethics problems or situations that should be reported to Management. Finally, make sure that the 800 number, the members of the Risk Management Committee, and the names of the two-contact people are common knowledge for all employees.

THE INCIDENT OCCURS



Eventually, an incident will occur, and a suspicion will be reported. When this happens, Management must investigate every reported situation and work together to resolve the problem. If the Staff member who reported the situation identifies him/herself, Management should explain to that person what steps were taken to resolve the situation.

If internal fraud is exposed, Management should follow the steps outlined in its ethics policy. If for any reason it doesn't do so, the reason why should be reported to Staff. A fraud-prevention program is doomed when Staff knows that a report has in fact been submitted but was then overlooked or buried.

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issues arise. She can take over what needs to get done so I can focus on problem solving.

Q. How does your bank use training to solve for succession planning?

A. The assistant internal auditor is trained in the same areas as I am. We try to train those below us for them to step in. We also keep detailed checklists/procedures so anyone could step in and follow to complete the report/audit.

Q. What is your favorite thing about the Annual Current Issues Certification Conference?

A. I always get ideas for new audits or areas to check. During each day of the conference, I'm taking notes of things to bring back to the bank. I really enjoy the interaction with other bankers. Finding out how they operate, what software they use and their opinions. I've made new friends at every conference.

Q. How has your designation affected your career/role at the bank?

A. I got certified as internal auditor for my new position at the bank. I also received my certificate for BSA/AML professional to help me be a better auditor. Then I got certified for compliance for the new role I took on when my former boss retired. I keep up all three certifications because each one helps me better at the other.

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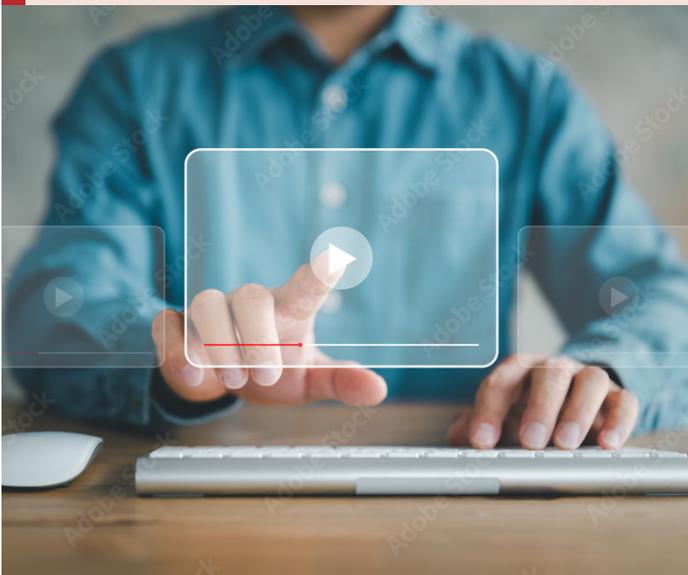
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