


Three-Step Fraud Detection
*How to Brainstorm & Document
 Fraud Risks on Every Audit Project*

The Conference That Counts
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John J. Hall, CPA
 John@JohnHallSpeaker.com
 (312) 560-9931
 www.FraudPreventionPro.com
 www.JohnHallSpeaker.com



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Call Us: (312) 560-9931

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Fraud Prevention & Detection Skills Training
Your #1 Proven Defense

JOHN J. HALL, CPA

More than half of all tips are provided by employees of the victim organization

Will your people let you know?
 Click Here and Let's Chat

DOWNLOAD YOUR FREE 6-STEP FRAUD PREVENTION GUIDE




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Fraud Risk Management Framework


1. **Deterrence and Prevention**
2. **Early Detection**
3. **Effective Handling**

**ORGANIZATIONS (and their auditors)
 MUST BE PREPARED AT ALL THREE LEVELS**



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“Be aware of fraud risks”
is imprecise and
leads to
confusion and
uncertainty



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Precision & Clarity

- Thinking
- Planning
- Actions
- Solutions




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POP QUIZ #1

Estimated 'Fraud' Losses
Most Recent Fiscal Year

\$ _____



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POP QUIZ #2

**What types of fraud
account for most
of your losses?**

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'M<P? !-JNN# >JM@><M?

1	
2	
3	
4	
5	
6	
7	
8	

8

'M<P? !-JNN# >JM@><M?

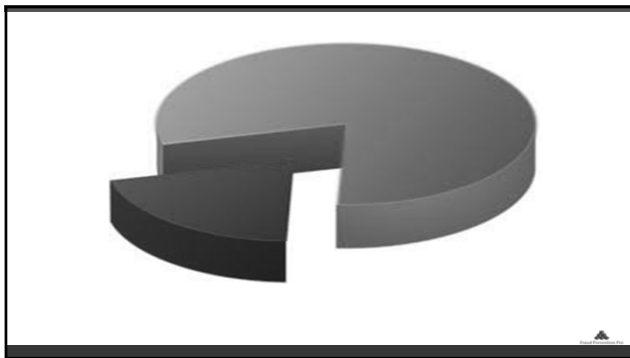
1	Disbursements
2	Inventory
3	Construction/Facilities
4	Health Care Costs
5	Payroll
6	T&M contracts
7	T&E reimbursement
8	Other – Unique to You
	TOTAL

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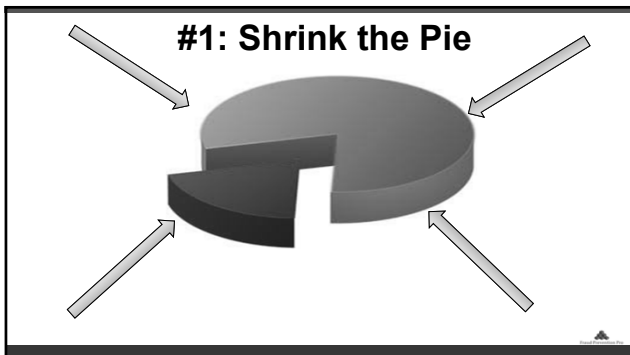
'M<P? !-JNN# >JM@><M?

		HIGH	LOW
1	Disbursements	\$ XXX	\$ XXX
2	Inventory		
3	Construction/Facilities		
4	Health Care Costs		
5	Payroll		
6	T&M contracts		
7	T&E reimbursement		
8	Other - Unique to You		
	TOTAL	\$ XXX	\$ XXX

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**#2: Find More of What's Left
FASTER**

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How Fraud is Found

1. Managers and staff
2. Internal & government audit, compliance and fraud specialists
3. External auditors
4. Other third parties
5. The thief (fraudster)
6. Luck or accident

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Fraud Risk Management Framework

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High-Leverage Behaviors

A few simple but critical behaviors

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Three-Step Fraud Detection

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 - a) Root Cause Analysis

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Ask and Answer

W.C.G.W.
What Could Go Wrong?


W.W.I.L.L.
What Would It Look Like?



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THE CHALLENGE

**Fraud Risk
Brainstorming
Think Like A Thief**
(when we don't know how)



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**Precision & Clarity
from asking three
"Hey Boss!"
Questions**



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THE SECRET SAUCE

● ...begin (plan)
with the
PRESUMPTION
that a fraud event
has already occurred



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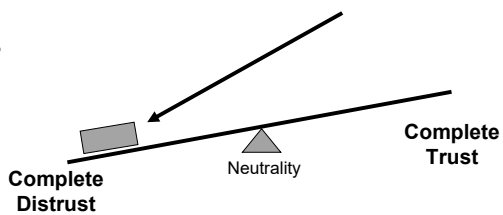
THE SECRET SECRET SAUCE

● Assume you
are committing
the fraud

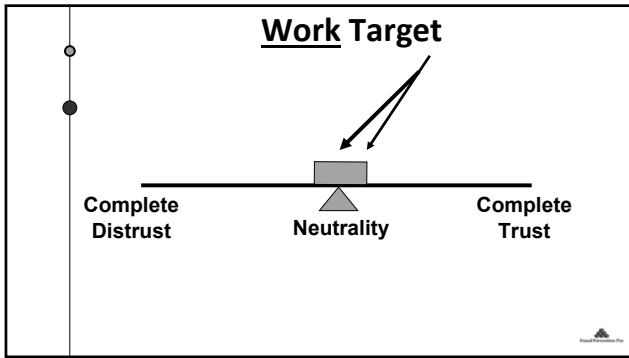


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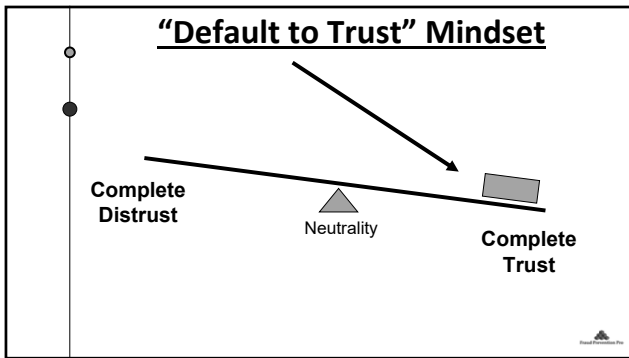
Planning Target



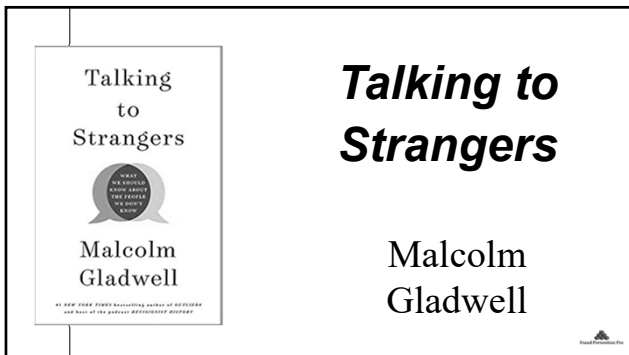
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THE THREE C's


- **Commit**
- **Convert**
- **Conceal**



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Backend of Brainstorming


- **Nature**
- **Extent**
- **Timing**



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Discovery-Based Tests

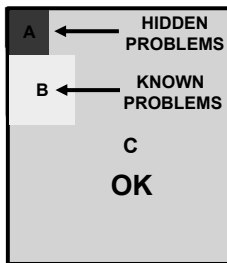
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Choose 'Valid' Samples

1. There are only two types of samples:
 - ✓ Valid
 - ✓ Invalid
2. Should answer "Do we have this issue?"
3. Every sample item chosen should have a 'valid' chance of success

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ALL TRANSACTIONS



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Probability of 1 in Sample, if population = 100,000

Sample Size	Number of Problem Transactions				
	10	15	25	<u>50</u>	100
25	0.002	0.004	0.006	0.012	0.025
50	0.005	0.007	0.012	0.025	0.049
<u>100</u>	0.010	0.015	0.025	0.049	0.095
250	0.0250	0.037	0.061	0.118	0.221
500	0.049	0.072	0.118	0.222	0.394
1000	0.096	0.140	0.222	0.395	0.634

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**100% testing
produces
reliable results**

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Detection-Focused Interviews

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Interview or Interrogation

Interview – non-accusatory, structured, dialog-based, question and answer, held for a specific purpose

Interrogation – accusatory, held when there is sufficient evidence to accuse the suspect of fraud and seek a confession

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For Consideration

1. Most people we interview believe telling the truth is the morally right thing to do.
2. We have all learned that lying might help us to avoid punishment.

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Impact of Increased Tension

1. Deception causes anxiety
2. Behavior symptoms are revealed as anxiety in the subject increases
3. Be aware of techniques used – intentionally or unintentionally – to release tension and anxiety
4. A deceptive person, if given the choice, will usually choose to reduce anxiety within their response

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“Behavioral Norm”

1. Ask background questions that result in truthful answers
2. Probe short and long term memory
3. Ask questions that require creative responses
4. Look for behaviors that do not make sense relative to the words spoken
5. Look for body movements and analyze in relation to what was just said

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“Behavioral Norm”

- 7. Evaluate behaviors before, during and immediately following an answer
- 8. Look for gross body movements, and analyze in relation to what was just said
- 9. Be aware of the cumulative impact of verbal and non verbal responses




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CUMULATIVE



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Signs of Deception - Nonverbal

- 1. Change in pattern of eye contact
- 2. Increased breathing, perspiration or swallowing
- 3. Change in coloring or facial tone
- 4. Posture becomes closed, stiff or defensive
- 5. Movement away from the interviewer
- 6. Reluctance to physically handle documents or other evidence presented
- 7. Passive reaction to direct accusation
- 8. Grooming gestures & physical adjustments



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Signs of Deception - Verbal

1. Denial confined to only to specific aspects of the issue
2. Delayed, evasive, or vague answers
3. Uses reinforcements in answers
4. Fragmented or incomplete sentences
5. Mixture of unusually poor and exact memory
6. Answers consistently lack detail
7. Answers start with repeating the question

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Signs of Deception - Verbal

8. Question or challenge factual information
9. Mental blocks
10. Throat clearing or coughing
11. Mumbling
12. Swearing, oaths or religious statements
13. Inappropriate laughter
14. Passive or weak denial

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Four Magic Words

“Tell me
what happened”

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Powerful Follow-Up Question

“How could we prove that?”




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ACFE Self-Study

“Finding the Truth”
www.ACFE.com

Finding the Truth: Effective Techniques for Interview and Communication




CPE Credit: 16
Course Level: Basic
Prerequisite: None



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Data Analysis and Monitoring

1. Standard reconciliations
2. Poor performance
3. Top performance
4. Timing differences
5. Suspense and clearing accounts
6. Complaints
7. Overtime by employee type
8. Top travelers and earners



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Data Analysis and Monitoring

9. Consulting and other third party services billing
10. Warranty activity
11. Adjustments and overrides:
 - Sales prices
 - Receivable accounts
 - Cash accounts
 - Inventory
12. Closing entries
13. Failures



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Data Analysis and Monitoring

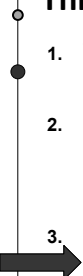

14. Common names and addresses for refunds or credits
15. Goods purchased in excess of needs / slow turnover
16. Duplicate payments
17. Regular meetings with key executives in departments that handle fraud-like issues



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Determine the Real Cause of Indicators



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Root Cause Analysis

1. What happened
2. Why did it happen

V
A
L
U
E


3. What options are available
4. The cost/benefit of each option
5. The best option

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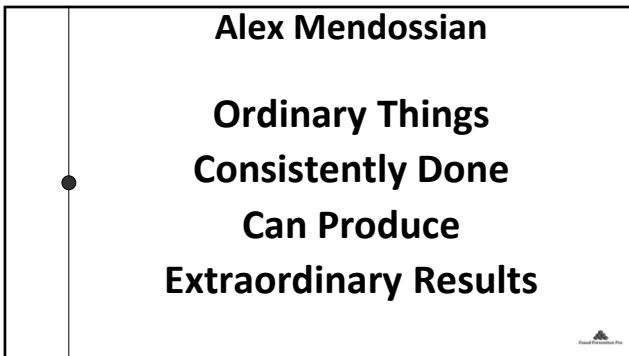
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Thank You

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