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Introduction

In an era of tighter budgets and more competitive markets, organisations are looking for innovative ways to reduce costs and increase profits. Many strategies and innovative ideas have been pursued and advocated by gurus, from contracting out to flatter management structures. Much is made of their potential to achieve what is often described as ‘competitive advantage’.¹ Business schools in universities around the world are full of academics who advocate lots of ways to achieve this. One measure, however, has not been on the ‘radar’ of the vast majority – investing in measures to counter fraud. This is largely because fraud is a hidden cost. Frequently it is not measured, or it is gauged using detected fraud losses, which hide the true costs. This book will show that it is reasonable to assume that in most organisations fraud losses are around 5 per cent, something ACFE, through less valid research, have been showing for some time.² Now consider 5 per cent of the procurement budget or payroll in your organisation; in most cases that would amount to a significant sum of money. The good news is that there are measures to substantially reduce this, and the application of appropriate methods can reap 30 per cent plus reductions in fraud losses. This can be done relatively cheaply, thus producing returns on investment of 12 × or more.³ This book will outline a model to achieve this: the professional approach to reducing fraud – the last great hidden cost – to reap competitive advantage.

There are lots of books on the market which tell you how to prevent or investigate fraud. Some of these are very good. However, they all miss one obvious point – fraud is a business cost like staff, capital, marketing etc. All organisations suffer from fraud, even if they think they don’t because there have been no detected frauds. Most frauds by their nature are undetected, and fraud costs money. Because of the lack of accurate measurement, it is the last great cost many organisations unknowingly have, which could also be substantially reduced. In the commercial sector this could reap a competitive advantage, and in the increasingly financially strained public sector, it could stave off cuts in services. *Countering Fraud for Competitive Advantage (CFCA)* therefore offers

more than a book on how to prevent and investigate fraud. It offers a completely new way of looking at the problem and a holistic model for countering it.

There are some organisations which don't even compile regular statistics on detected frauds, because they are seen as unusual and rare. Others do use statistics, but focus on detected frauds. Such measures are flawed because many frauds are undetected and many go on for a long time before they are detected. Our research shows that average losses from fraud and error are around 5 per cent. In many organisations this is even higher. So consider an organisation with a \$100 million turnover: if they are performing in an average way they could be losing around \$5 million to fraud. Now just answer the four questions below about what you are currently doing to counter fraud:

- Do you *accurately* measure fraud losses?
- Do you have an independent hotline which is well publicised to report fraud and abuse?
- Do you pursue measures to develop an anti-fraud culture?
- Do you use data-mining and matching to conduct pro-active investigations?

If the answer to any of these is no you are at higher risk of fraud and you are likely to be above average in fraud losses, so the \$100 million organisation could be losing well over \$5 million to fraud. Similarly consider the traits of an organisation at higher risk from fraud from its staff:

- Staff with perception that they are poorly paid;
- Staff with perception that they have poor conditions of employment;
- Staff with high levels of job dissatisfaction;
- Large number of staff wanting to leave;
- Tolerance of petty crime/fraud; and
- Immoral/unethical working practices.

If any of these apply to your organisation you may be at greater risk of fraud. Also consider one of the most common reasons perfectly law-abiding and honest employees turn to fraud: personal financial problems. The USA, UK and many other countries are in the midst of one of the worst recessions since the end of the Second World War. This has led to many people losing their jobs, downgrading to lower-paid work, having to take pay cuts, losing over-time, living in houses with negative equity

so they are unable to move, amongst many others. Indeed in America an article on the impact of the recession found that:

- More than half the adult workforce has experienced a ‘work-related hardship’ of unemployment, a pay cut, reduction in working hours or an involuntary move to part-time employment;
- Over 70 per cent of Americans over the age of 40 have been affected by the economic crisis;
- The net worth of the average American household has shrunk by 20 per cent;
- Long-term unemployment is at the highest levels since the 1940s; and
- 20 per cent of Americans have seen a 25 per cent or greater reduction in household income.⁴

Consider some of the impacts on the UK which have been noted:

- Around 1.2 million local government workers have experienced a pay freeze for three years, which amounts to a 15 per cent pay reduction in real terms;⁵
- From 2011, UK public sector workers were told to expect pay rises of no more than 1 per cent for two years with 710,000 workers to lose their jobs by 2017;⁶
- Since the recession began, unemployment in the UK has risen from 1.61 million in December 2007 to 2.67 million in December 2011 – an increase of over 1 million;⁷
- All this has occurred at a time when inflation has regularly been between 3 and 5 per cent; and⁸
- A study for the Yorkshire and Clydesdale Banks has also claimed that 2 million families feel under strain due to financial and money worries.⁹

Consider how many of your staff and families might be experiencing some of the above. Most will not turn to fraud as a consequence, but some will.

CFCA, however, will set out a holistic strategy to counter fraud which has been shown to produce a 12 to 1 return on investment.¹⁰ Fraud losses can be reduced at a very reasonable cost and those saved resources can be used to enhance profitability in the commercial sector, or be invested in frontline services in the public and not-for-profit sectors.

This book is aimed at those who run organisations and want them to be more financially healthy and stable. It is aimed at those who directly undertake counter-fraud work and who want to be more effective and

see greater tangible results. And it is aimed at all those who suffer from the cost of fraud currently being too high – shareholders whose companies are not as profitable as they might be; employees whose job security is undermined; taxpayers who do not get the quality of public services that they pay for; and those donating to charities where the charitable purpose is undermined. We all have a stake in fraud being tackled effectively.

1.1 BOOK OUTLINE

In the next chapter we begin by considering what fraud is; the diversity of it as well as the scale of it. It will show how diverse it can be as well as how significant a drain it can represent on an organisation. The chapter will also consider what the impact of fraud on an organisation can be.

In Chapter 3 the book considers the fraudster and the culture of fraud. There has been limited interest in fraud amongst researchers, but the chapter unpicks some of the research to reveal types, profiles and the motivation of fraudsters. Culture also plays a very important part in influencing levels of fraud and this chapter examines some of the factors contributing to this.

The resilience of organisations and countries to fraud is the subject of Chapter 4. The chapter shows that resources and attention on fraud at a national level is often lacking. This is also often replicated in the strategies to counter fraud. Data on the quality of organisations' strategies to counter fraud are explored.

In Chapter 5 the book turns to strategies which can be used to reduce fraud. This chapter focuses upon the mechanics of measuring fraud and how this is very important in the overall strategy to counter fraud. The chapter describes the basic principles of fraud measurement and examines how this should shape the overall counter-fraud strategy.

Changing attitudes towards fraud is as important as measures to prevent fraud. There are a very wide range of measures which can be used to achieve these aims. Chapter 6 builds upon the research on fraudsters, as well as the extensive crime prevention research to demonstrate a wide range of tools to prevent fraud and create an anti-fraud culture.

Unfortunately it is never possible to prevent all frauds and those that do occur need to be detected quickly, and investigated to the highest standards. In Chapter 7 the tools to detect and investigate fraud effectively are examined. In doing so the chapter draws upon some of the extensive research from psychology for detecting deception.

Once an investigation has been completed there is a wide range of options open to an organisation to sanction the fraudster and secure redress. Chapter 8 will show that the traditional criminal sanctions are only one of many that a fully equipped counter-fraud professional can use.

Central to this book is making fraud a cost. In Chapter 9 the importance of this metric, as well as many others, is identified. The chapter examines the importance of metrics (or key performance indicators as some call them) and how they can be created for an organisation. Some of the potential drawbacks are also explored.

Much of what is advocated in this book could not be undertaken without professional counter-fraud staff who possess the appropriate knowledge and skills. They are needed to influence the organisation towards this professional approach, to develop the strategy, to lead on developing an anti-fraud culture and prevention, to detect and investigate fraud, to pursue sanctions and redress, and to manage performance. Chapter 10 explores the origin of these functions, what they need to do and why organisations should invest in them.

In the final chapter the model is drawn together and reasonable reductions in fraud losses are applied to the leading companies in the world, the USA, UK, France and Germany. The chapter shows the substantial gains in profitability some companies could achieve if they pursued the professional approach to countering fraud.

END NOTES

1. See for example Porter, M.E. (2004) *Competitive Advantage*. New York: Free Press; Briggs, R. and Edwards, C. (2006) *The Business of Resilience*. London: Demos; Champy, J. and Hammer, M. (1993) *Reengineering the Corporation: a Manifesto for Business Revolution*. New York: Harper Collins; Hamel, G. and Prahalad, C.K. (1996) *Competing for the Future*. Harvard: Harvard Business School Press. See also <http://www.time.com/time/specials/packages/completelist/0,29569,2086680,00.html> for the 25 most influential business books.
2. See ACFE (2010) *Report to the Nation on Occupational Fraud and Abuse*. Austin: ACFE; and Gee, J. Button, M. and Brooks, G. (2011) *The Financial Cost of Fraud. What the data from around the world shows*. London: PKF/CCFS.
3. NHSCFSMS (2007) *Countering Fraud in the NHS: Protecting Resources for Patients. 1999–2006 Performance Statistics*. London: CFSMS.
4. Warner, J. (2010) What the Great Recession Has Done to Family Life. *New York Times*. <http://www.nytimes.com/2010/08/08/magazine/08FOB-wwln-t.html>.
5. New Policy Institute (2012) Living on the Edge: Pay in Local Government. Retrieved 12 April 2012 from <http://www.unison.org.uk/acrobat/5821.pdf>.

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10. NHSCFSMS (2007) op. cit.

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