RISK NOTE

Subject: **EMPLOYEE FRAUD**

Health Care Agencies (HCAs) across the province are at risk of experiencing significant losses due to employee theft and fraud. In addition to the actual sum lost to a fraudster, these losses can be very disruptive to a workplace due to the time and cost involved in undertaking investigations and corrective measures, as well as recruiting and training replacement staff. Employee fraud can also have negative impacts on staff morale and productivity, and may cause an HCA to suffer reputational harm. As such, it is beneficial for an HCA to take proactive measures to manage its risk of employee theft and fraud.

There are a number of red flags which may signal that an employee is partaking in fraudulent activities. While none of the below factors are conclusive evidence of employee fraud, they are important indicators that personnel at every level should be able to recognize.

Red flags related to employees may include:

- The employee is in financial trouble, such as having significant personal debt or credit problems.
- There is instability in the employee's personal life including family situations causing financial stress such as a divorce, or habits such as gambling, or alcohol or drug abuse.
- The employee refuses to take their vacation or sick leave.
- The employee requests to work outside normal business hours, is often the first to arrive at work, or is the last to leave.
- The employee refuses to share work responsibilities, particularly relating to the control of financial records.

- The employee is easily annoyed at reasonable process-related questions about their work.

- The employee has started to make purchases which seem inconsistent with their personal or family income such as new properties, vehicles, or other expensive goods.

Red flags related to accounting practices may include:

- Payments made at unusual times of the day or the week, or payments which are out of season.

- Transactions being processed too frequently or not enough, or just generally outside of what the expected pattern should be.

- Payments being made for unusual accounts such as too many large or small transactions, or too many transactions involving round numbers.
- A high number of refunded, altered, or voided transactions.

- Questionable parties involved in the transactions such as outside parties which do not typically receive payments from the HCA.

HCAs should strive to create a "risk aware culture," which brings every level of the organization together to effectively identify, assess, and manage risks. There are five key principles or processes that can provide guidance to organizations of various sizes and types in establishing an environment to manage their risk of fraud. These principles or processes are as follows:

1. Including a **Fraud Risk Management Program** in an organization's governing structure, which conveys the expectations of the board of directors and senior management regarding how to properly manage risks of fraud through written policies that encourage ethical behaviour.

2. Conducting periodic **fraud risk assessments** tailored to the organization's size, complexity, and industry, which include risk identification, an assessment of risk likelihood and significance, and risk response. Fraud risk assessments should include input from various individuals throughout the organization, including accounting or finance personnel, risk management personnel, operations personnel, internal audit personnel, and legal personnel.

3. Establishing **fraud prevention techniques** such as written policies, procedures, and training to avoid potential fraud risk events. Prevention techniques could include background checks on potential employees, anti-fraud training, tailoring the authority of personnel to their level of responsibility, rotating employees through different positions, dividing responsibility among multiple employees, requiring employees to take vacations, not allowing the signing of blank cheques, and reviewing third-party and related-party transactions.

4. Implementing **fraud detection techniques** to uncover fraud events if they do occur. One of the strongest fraud deterrents is awareness that the organization has effective detection techniques. Educating employees about the "red flags" listed above is an example of an effective fraud detection technique. Other techniques include reconciliations, independent reviews, physical inspections, data analysis, and unannounced audits.

5. Designing both an effective **reporting process** to obtain input on potential fraud, and a coordinated approach to **investigative and corrective action** to address allegations of potential fraud and instances of non-compliance. Organizations that investigate and prosecute cases of employee fraud reduce their crime losses by receiving compensation from those who are found liable, and also by establishing a reputation for being tough on crime, therefore dissuading employees from attempting to commit fraud against the organization.[1]

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[1] Institute of Internal Auditors, the American Institute of Certified Public Accountants & Association of Certified Fraud Examiners, Managing the Business of Risk: A Practical Guide (2009). Note: This publication has been endorsed by the Chartered Accountants of Canada and the Association of Certified Fraud Examiners.

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