

Fraud Risk Management

A business imperative

Even with the tightest internal controls, nearly every business is subject to fraud risk today. Yet, much of this fraud goes undetected, because auditors are focused only on frauds that are material to the company's financial statements.

Depending on the size of the company, a materiality threshold can be quite high. For example, for a company that earns \$10 million per year, auditors may only look for fraud amounting to \$500,000 or more. Often, auditors do not have a mandate or the time to detect frauds below these levels. Thus, it's no surprise that surveys by the Association of Certified Fraud Examiners indicate that U.S. businesses lose 7% of their annual revenues to fraud.¹

The risk for fraud increases as companies operate globally, rely more on information technology and generate more complex transactions. Further, a weak economy and stakeholder pressure to improve profits add additional stress and risk. With so many risk factors, it can be difficult to detect and correct fraud.

The cost of doing business

Fraud can have far-reaching impacts. It can erode profits, increase legal costs and undermine investor confidence in your company. It can also ruin a company's reputation. Consider the following fraud statistics:²

According to a study by the Association of Certified Fraud Examiners (ACFE), occupational fraud³ schemes tend to be extremely costly. The median loss caused by the occupational frauds in the study was \$175,000.⁴ More than one quarter of the frauds involved losses of at least \$1 million.

Occupational fraud schemes frequently continue for years before they are detected. The typical fraud in the ACFE study lasted two years from the time it began until the time it was caught by the victim organization.⁵

Of the 5,428 companies in 40 countries that took part in a research project, over 43% reported suffering one or more significant economic crimes during the previous two years.⁶

The government has introduced numerous regulations to curb the effects of fraud on individual businesses and the world's financial markets. These include:

- The U.S. Foreign Corrupt Practices Act of 1977 (FCPA)
- The 1997 Organisation for Economic Co-operation and Development (OECD) Anti-Bribery Convention
- The U.S. Sarbanes-Oxley Act of 2002 (SOX)
- The U.S. Federal Sentencing Guidelines of 2005
- Statement on Auditing Standards No. 99: Consideration of Fraud in a Financial Statement Audit (SAS 99)

Despite these anti-fraud initiatives, 66% of frauds are still found through tips or by accident.⁷



¹ Association of Certified Fraud Examiners, "2008 Report to the Nation on Occupational Fraud and Abuse"

² Ibid

³ Occupational fraud is defined as the use of one's occupation for personal enrichment through the deliberate misuse or misapplication of the employing organization's resources or assets.

⁴ Association of Certified Fraud Examiners, "2008 Report to the Nation on Occupational Fraud and Abuse"

⁵ Ibid

⁶ PricewaterhouseCoopers, "Economic crime: people, culture and controls"

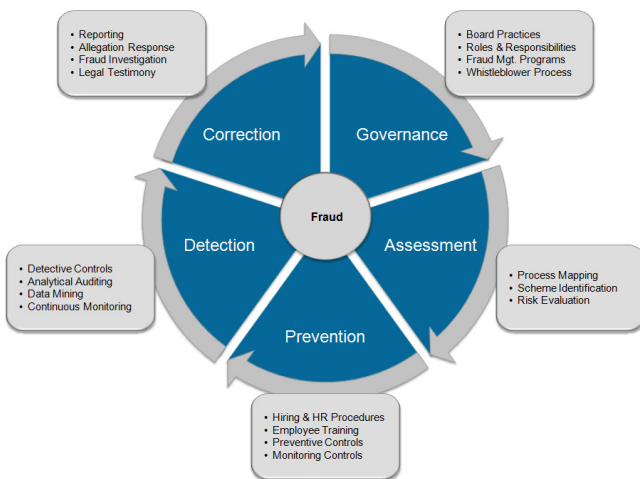
⁷ Association of Certified Fraud Examiners, "2008 Report to the Nation on Occupational Fraud and Abuse"

How we can help

At Cost Advisors, we have a well-defined method for managing fraud risk. Whether your company faces the risk of corruption, asset misappropriation or fraudulent statements, we can help. We manage fraud risk by identifying your company's known risks and assessing the controls you have in place to deal with them.

Then, we tailor our services based on your organization's size, circumstances and potential for fraud risk. We can build a fraud risk management program that is as dynamic as your business and will help you prevent, detect and respond to fraud. We can also investigate and correct suspected fraud. Whether you need help evaluating your current fraud risk management program or want us to create a new program, we provide prompt, competent and confidential service.

Our framework



Getting started with Cost Advisors

To learn more about how we can help you manage fraud risk, call us at **503.646.3500** or visit our website at **www.costadvisors.com**.

Our services

Our fraud risk management services are based on five key principles:

Governance: An organization should include a fraud risk management program in its governance structure. A written policy should explain the program in detail and convey the expectations the Board of Directors and senior management have regarding managing fraud risk. We can:

- Establish or enhance a formal fraud risk management program that:
 - Sets fraud control policies and strategies
 - Defines roles and responsibilities for the Board of Directors, the Audit Committee, management and staff
- Develop fraud investigation protocols
- Identify fraud investigation resources
- Implement a whistleblower process to track allegations

Assessment: An organization should assess fraud risk exposure periodically to identify potential schemes and events needing attention. We can:

- Document your business processes
- Develop and perform ongoing fraud risk assessments that are tailored to the organization's size, complexity, industry and goals
- Prioritize fraud risk schemes according to significance, likelihood and fraud tolerance, and link them to mitigating programs and controls

Prevention: An organization should establish prevention techniques to avoid fraud risks and reduce possible impacts to the organization. We can:

- Develop and deliver awareness programs to educate staff about your fraud risk management program and the types of potential fraud
- Recommend corrective actions and controls

Detection: An organization should establish detection techniques to uncover committed frauds when preventive measures fail. We can:

- Test that detection controls are working as they should
- Identify patterns, trends, relationships and anomalies in recorded transactions using Reperio™, our proprietary data mining tool
- Work with your staff to monitor for fraud

Reporting: An organization should establish a reporting process to solicit input on potential fraud. It should follow a coordinated approach to investigate and correct potential fraud. We can:

- Perform investigation and evidence collection processes that:
 - Improve loss recovery
 - Minimize exposure to litigation
 - Protect the organization's reputation
 - Support prosecution efforts and provide expert testimony
- Report instances of policy noncompliance and allegations involving potential fraud to management