Forensic Accounting: Perpetrators of Fraud

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ABSTRACT

Fraud can be perpetrated by an individual, two or more individuals, or by many groups or 'separate entities'. Most fraud cases are not reported due to risk of embarrassment and resulting reduction in the level of customer or shareholder confidence. Reported fraud cases (a majority of the worst kind) are committed by a company's own employees or managers.

Introduction

Professional Bodies, Investigative Services, Forensic Accountants, Pressure Groups, Corporate Crime Experts, Researchers, Authors on Fraud Studies, have dedicated years (intensified since 1940) in fighting fraud.

Fraud can be perpetrated by an individual, two or more individuals, or by many groups or 'separate entities', namely, third parties, a company's employees, the company's management, suppliers or customers. Most fraud cases are not reported – probably (assumption by the author of the article) due to risk of embarrassment and resulting reduction in the level of customer or shareholder confidence. However, the reported fraud cases (a majority of the worst kind) are committed by a company's own employees or managers (blue collar and white-collar crimes).

KPMG's Survey

KPMG in Malaysia, recently launched the KPMG Fraud Survey Report 2004 containing the results of KPMG in Malaysia's Fraud Survey 2004. The survey, which was sent out to all public listed companies on the Bursa Malaysia, indicates that 83 percent of the respondents have experienced fraud in their organisation. This is an increase of 33 percent from the 2002 survey. 87 percent of the frauds were perpetrated internally (69 percent by non management employees and 18 percent by management employees).

KPMG in Ireland (1995) distinguished fraud between external and internal fraud and classified internal and external fraud by perpetrators. The types of fraud listed by KPMG are:

Internal Fraud

Employee Fraud	**Management Fraud**
Stock theft	Teeming and lading (lapping)
Misappropriation of cash	Expense account
Teeming and lading	False financial statements
Cheque forgery	Misappropriation of cash
Expense account	Unnecessary purchases
Petty cash	Cheque forgery
Kickbacks	Kickbacks
Loans	Phantom vendors
Investments	Diversion of sales

External Fraud

- Cheque forgery
- False insurance claims
- Credit card fraud

- False invoices
- Product substitution
- Bribe, secret commission
- Bid rigging
- Price fixing
- False representation of funds

The list is not exhaustive. Based on recent cases cited, areas of fraud and crime that can be added to the above list are: antitrust violations, computer fraud, internet fraud, phone/telemarketing fraud, bankruptcy fraud, health care fraud, environmental law violations, bribery, counterfeiting, money laundering, economic espionage, mail fraud, government fraud, tax evasion, financial fraud, securities fraud, insider trading, public corruption, embezzlement and trade secret theft.

Perpetrators of Fraud

(1) Australian Version

There has been no clear-cut classification for perpetrators of fraud to date. However, Adam Graycar, Director of The Australian Institute of Criminology, Trends & Issues journal (2001) claimed that:

> *although there has not been a definitive attempt to "criminally profile" fraud offenders, we begin to examine possible differences by setting out our four general categories of fraud.......*

Fraud committed against an organisation by a principal or senior official of that organisation

Entrepreneurial fraud, or misappropriation of corporate assets by senior management, appears to be related to a constellation of factors.

Fraud committed against an organisation by an employee

At least two major themes emerge in the phenomenon of employee theft. In the first theme, an employee perceives, that he is treated unfairly by his employer. In the second theme, the employee has a feeling of 'territorial ownership'. Employees especially those in large organisations or government departments, may presume personal ownership or entitlement by virtue of occupation (of a position or space) or through regular use/access.

Fraud committed against one individual by another in the context of face-to-face interaction

The direct person-to-person deception of another individual can involve utter ruthlessness. This may take such extreme forms as the person who takes a widow into his confidence and leaves her penniless.

Fraud committed against a number of individuals through print or electronic media, or other indirect means

For those unable to look a prospective victim in the face, a variety of media permit indirect dealing. Terms like 'mail fraud', 'postal fraud', telemarketing fraud' and 'wire fraud' fall under this category of fraud. The advent of digital technology is said to have facilitated instantaneous communication with millions of prospective victims through the use of the Internet and email.

Moulton (1994), identifies "red flags" to watch for in trying to spot fraudsters. These include large egos, substance abuse problems or gambling addiction, living beyond apparent means, self-absorption, hard working (taking few holidays), under financial pressure from, let us say, heavy borrowings and sudden mood changes. Duffield and Grabosky (2001) refers to these red flags as 'motivational and psychological correlates' of fraud offending.

(2) U.S. Version

Edelhertz (1970), classified white-collar crime by perpetrators into four categories:

Ad hoc violations committed by persons for personal gain, operating in a non-business context, for example, credit purchases (where there is no intention to pay), purchase by mail in another person's name, income tax offences, credit card fraud, bankruptcy fraud, social welfare fraud, insurance fraud.

Criminal abuses of trust committed by persons operating inside business, government, a profession or other entity, in violation of their duty of fidelity to employer or client, for example, commercial bribery and kickbacks, banking abuses by bank officials, employees and directors, embezzlement, share frauds (insider trading), using company funds to buy shares, petty theft and expense account frauds, computer fraud resulting in unauthorized payments.

Business crimes committed incidental to and in furtherance of business operations, but which are not the central purpose of the business, for example, tax fraud, infringement of competition laws, use of false financial statements to obtain credit, cheque "kiting" to obtain short-term finance, share violations (manipulation of the market).

Fraudulent activities which are the central purpose of the business, for example, medical or health frauds, share and commodities fraud, chain referral schemes, buying or pyramid schemes.

Conclusion

Perpetrators of fraud can be classified according to the **methods, categories, types of fraud,** or according to the

psychological aspects (correlates) of fraudsters. What is apparent from the literature is that fraud is a product of both personality and environmental or situational variables. This has two implications for understanding fraud risk. First, it means that individuals will vary in their propensity to commit fraud even when they are subject to similar environmental pressures. Second, it means that situations will vary in their impact on individuals according to the inherent risk factors at any given time.

In summary, the key to understanding and eventually controlling fraud is to consider both the individual and the environment in which the perpetrator operate. While this paper has examined some individual factors associated with fraud, there are many situations in which personality and motivations lie beyond the reach of policy. In these cases, those who would prevent and control fraud must look at reducing opportunities and to exercising a degree of surveillance.

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