

Post-Conference Auditing and Investigating Fraud Seminar

*Auditing Track
Corruption Schemes*

Introduction to Corruption

- The employee's use of his influence in business transactions in a way that violates his duty to the employer for the purpose of obtaining a benefit for himself or someone else

Corruption Schemes

- Bribery and kickbacks
- Illegal gratuities
- Economic extortion
- Conflicts of interest



Bribery and Kickbacks

- Payments, gifts, or gratuities given to employees from contractors or vendors in order to influence a business transaction
- Involves collusion between employees and vendors
- Usually attacks the purchasing function of the victim company
- Can be very difficult to detect

Illegal Gratuity

- Something of value given to an employee to reward a decision *after* it has been made
- Similar to bribery schemes, but does not require proof of intent to influence



Economic Extortion

- Use of actual or threatened force or fear to demand money or some other consideration to make a particular business decision
- Often the other side of a bribery case

Conflict of Interest

- Employee or agent of the contracting company (or a spouse or close family member) has an undisclosed financial interest in a contract or contractor

Detection of Corruption Schemes

- Typical auditing procedures fall short
- Most often detected through tips from honest and disgruntled coworkers or vendors
- Strongest indicators:
 - Contractor(s) receiving unexplained favorable treatment from contracting employee
 - Continued purchase of high-priced, low-quality goods or services, without objection or returns

Detection of Bribery and Kickback Schemes

- Compare prices paid for goods and services to market rates.
- Analyze purchase levels by vendor.
- Analyze inventory overstocks and shortages.
- Identify continued purchases of inferior-quality goods.

Detection of Conflict of Interest Schemes

- Identify tips and complaints that might indicate that a conflict of interest is occurring.
 - Typically come from employees who are aware of a coworker's self-dealing
- Compare vendor and employee addresses and phone numbers.

Methods of Making Illegal Payments

- Gifts, travel, and entertainment
- Cash payments
- Checks and other financial instruments
- Hidden interests
- Loans
- Payment of credit card bills
- Transfers at other than FMV
- Promises of favorable treatment

Techniques to Identify Illicit Income

- Prove illicit income by showing that the subject's assets/expenditures for a given period exceed that which can be accounted for from admitted sources of income.
- Begin by compiling suspect's financial profile (net worth).

Net Worth—Asset Method

Assets
– Liabilities
= <i>Net worth</i>
– Prior year's net worth
= <i>Net worth increase</i>
+ Living expenses
= <i>Net income (or expenditures)</i>
– Funds from known sources
= <i>Funds from unknown sources</i>

- Best when subject has purchased assets
- Assets valued at cost
- Funds from known sources estimated generously
- Living expenses estimated conservatively

Net Worth—Expenditures Method

- Best when subject has spent illicit income on consumables that would not cause an increase in net worth

Known expenditures
– Funds from known sources
= <i>Funds from unknown sources</i>