

## The psychology of fraud

- According to a recent survey, the typical organization loses about five percent of its revenues to fraud each year.
- Agencies have both financial and nonfinancial assets that are valuable and susceptible to fraud.
- Taking away the opportunity to commit fraud is an agency's best deterrent.

According to a recent survey conducted by the Association of Certified Fraud Examiners, participants estimated that the typical organization loses about 5 percent of its revenues to fraud each year. The survey also concluded that governments are commonly victimized. The survey focused on occupational fraud schemes, in which an employee uses his or her occupation "for personal enrichment through the deliberate misuse or misappropriation of the employing organization's resources or assets." You can find the Association of Certified Fraud Examiner's 2012 Global Fraud Study, *Report to the Nations on Occupational Fraud and Abuse*, at <http://www.acfe.com/rtnn.aspx>.

It is important to remember that, in the context of fraud, assets are not only items of direct financial value, such as cash or sensitive electronics. Rather, misappropriation of assets also includes misuse of agency data or misuse of the employee's influence in a way that violates his or her duties. It is therefore important to consider the possibility of both financial and non-financial fraud in your organization.

Most people who commit fraud are not career criminals and are often trusted staff with no past criminal history. Usually, something in the person's life motivates or prompts him or her to commit fraud. The situation could be lifestyle related, such as lavish spending or addiction problems, or could be outside of the person's control, such as a family member's catastrophic illness or job loss. These motivations can make an honest person turn to fraud. Often, people are embarrassed to find themselves in the situation and consider the circumstances to be unshare-able with others in the organization.

Basically honest people who are contemplating fraud must also be able to justify their actions. Rationalizations can include feelings of overwork and lack of appreciation, a belief that they are acting in the best interest of their family, or intent to make restitution when they get back on their feet. These rationalizations allow fraudsters to

knowingly and intentionally commit a dishonest act while still functioning in the workplace.

Finally, for fraud to occur, the organization needs to give the person an opportunity, through poor segregation of duties or other weak internal controls, to commit the fraud. Ineffective or absent controls allow people to believe they will not get caught because no one will review their work or investigate anomalies.

These three factors; motivation, rationalization, and opportunity, are most often present when ordinary people commit fraud. Together, they are referred to as the "fraud triangle". The goal of any good internal control system is to break the triangle by removing one of the factors. It is unlikely that an employer can significantly influence people's motivations or rationalizations. Therefore, taking away the opportunity to commit fraud by implementing and maintaining a strong internal control structure is an agency's best deterrent.

Do the results of the recent fraud survey mean that fraud is a fact of life in government? That despite our best efforts, fraud will always occur? Unfortunately, this is probably true. No government agency has enough time, people, and resources to guard against every possible fraudulent action. However, with well-planned and implemented internal controls in place, we can all decrease the opportunities for fraud to occur.

*Suggested action steps:* What are your agency's most valuable financial and non-financial assets? Do you have sufficient controls in place over those assets to adequately decrease the opportunities for fraud?

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