



**MITIGATING FRAUD IN MANUFACTURING:
A COMPREHENSIVE APPROACH FOR RISK
MANAGEMENT**

INTRODUCTION



The manufacturing industry is one of the industry sectors most vulnerable to asset misappropriation and fraud. Manufacturing environments present unique opportunities for employees, contractors, vendors, and cyber hackers alike to take advantage of unsuspecting companies—which makes them vulnerable to significant financial loss and the potential for reputational damage.

There is often a lack of understanding of potential exposures and minimal oversight over the manual or automated system controls designed to address such risks within a manufacturing organization. These gaps put manufacturers at a higher risk to individuals who are willing to commit fraudulent activities, waste valuable resources, and abuse their authority.

The practical understanding of fraud is not “will it happen to me” but rather “when will it happen to me?” As incidences of large-scale fraud scandals become publicly known, organizations may consider assessing their own fraud detection efforts. Instead of asking themselves “what are we doing to respond to fraud?” organizations should ask the questions, “are we doing it well? Are our fraud response efforts effective and efficient? Are we as prepared as we should be?”

The odds are that fraudulent activities have unknowingly already taken place, and will continue to happen until you do something about it. However, detecting and proving fraud is not an easy task, so how can you identify and prevent fraud?

This solution sheet outlines a brief approach to fraud risk management including:

- The expense of fraud—how doing nothing can cost you more
- Fraud prevention techniques and controls
- Recommendations for developing an anti-fraud program

THE EXPENSE OF FRAUD—QUANTIFYING LOSS

The Association of Certified Fraud Examiners (ACFE) estimated in its [2016 Report to the Nations on Occupational Fraud and Abuse](#) that organizations typically lose 5 percent of annual revenues to occupational fraud. If we apply this percentage to the 2014 estimated Gross World Product, the potential total fraud loss is \$3.7 trillion worldwide.

In manufacturing, this is particularly relevant as during times of economic turmoil, rates of fraud increase. According to the ACFE 2016 report, the following was revealed about fraud in manufacturing:

- Manufacturers had the third highest reported fraud cases and the highest average loss due to fraud at **1.1 percent of revenue**
- **82 percent of manufacturing companies** were affected at least once by a case of fraud
- The most common fraud schemes were corruption, fraudulent disbursements and fraudulent statements
- **9 out of 10 manufacturing companies** believe their exposure to fraud has increased over the past 12 month
- Fraud typically lasts up to **two years before detection** and occupational fraud is most often detected though anonymous tips or by accident, versus internal / external audits
- Almost half of the reported fraud is committed by staff in finance and upper/ executive management, with operations and sales accounting for a third
- Implementing anti-fraud controls including a comprehensive risk management program resulted in lower losses

SAFEGUARDING YOUR REPUTATION—INTANGIBLE LOSS



Fraud risk management is critical to an organization's reputation and financial well-being. Even with the reported 7 percent of annual revenues lost to occupational fraud, the true cost is much greater and has a rippling effect on your brand and finances, that is often non-recoverable.

An effective fraud and reputation risk assessment strengthens the organization's ability to prevent and detect fraud and misconduct, that could lead to potential scandals.

A loss to reputation can cost you more than the loss of money due to the fraud itself.

Fraud or potential exposure to fraud, significantly harms an organization's reputation—and reputation is what trust is built on. It's not only consumers who are concerned, but partners, vendors, and shareholders who potentially view a company as unworthy of business and investment.



FRAUD PREVENTION AND CONTROLS



A 360° Approach to Fraud Risk Management with Continuous Improvement Strategies



MEASURE, MONITOR, AND IMPROVE



People

Most people do not originally set out to commit fraud. Often fraudsters simply take advantage of an opportunity; many times the first fraudulent act was an accident such as mistakenly processing the same invoice twice. However, when people realized the error went unnoticed, the fraudulent acts became deliberate and more frequent.

Generally, fraud occurs because of a combination of opportunity, rationalization, and pressure. An opportunity to commit a wrong-doing arises, a person feels that the act is not entirely wrong, and then has pressure pushing them to commit the fraud.

Fraud investigators talk about the "10-80-10" law which states that 10 percent of people will never commit fraud; 80 percent of people will commit fraud under the right circumstance and how they rationalize a particular opportunity; and 10 percent actively seek out opportunities to commit fraud.

MEASURE, MONITOR, AND IMPROVE



People

Most people who are likely to commit fraud in an organization will be deterred if:

- They are aware of what constitutes as fraud
- They know the company has an anti-fraud program in place
- They know there's a risk of being caught
- They understand the consequences of committing fraud

MEASURE, MONITOR, AND IMPROVE



People

Effective fraud awareness should include training programs that educate employees as to the role they play in preventing fraud.

Training and awareness programs should encompass:



Comprehensive ethics training



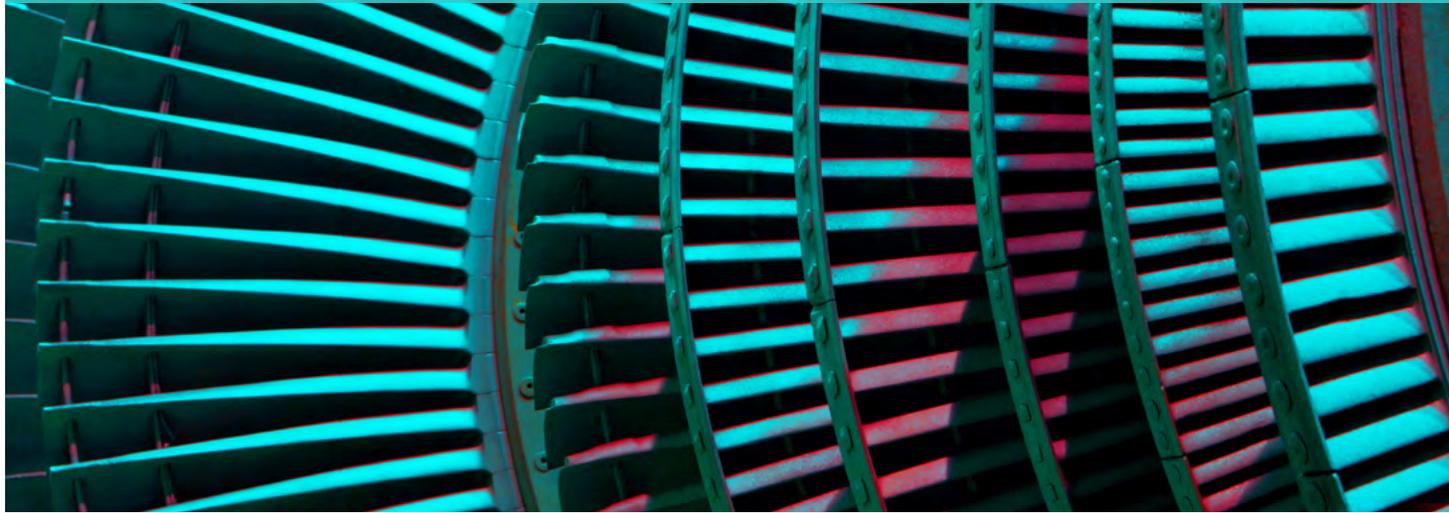
A code of conduct policy



Techniques for reporting fraud

Organizations need to stay vigilant against the 10 percent of people who are out to do harm to their business, and business leaders need to try and protect the 80 percent of people at risk of making an inadvertent mistake leading to on-going fraud, with sufficient internal controls.

MEASURE, MONITOR, AND IMPROVE



Process

To reduce the risk of fraud and unauthorized transactions, no single individual should have control over two or more parts of a business process. This is known as segregation (or separation) of duties (SoD).

A simple example would be someone in an accounting department, who has been assigned access to amend supplier master file details and to make payments. This situation could lead to fraud, as the individual could create a fake supplier and process fraudulent payments to themselves.

Consider your access and control over “sensitive” duties such as accounts payable, receivables, and vendor master files, as they open you up to fraud risk.

There is frequently a lack of focus and attention given to the design, operation, and monitoring of segregation of duties within organizations.

MEASURE, MONITOR, AND IMPROVE



Technology (and data)

Several techniques for detecting fraud in manufacturing organizations include a variety of manual and/or automated solutions, which are reliant on technology solutions and accurate data. Having automated and technology solutions in place mitigates the manual controls of human error and inaccurate information.

Enterprise Resource Planning (ERP) solutions are widely utilized as first line defense in helping prevent and monitor fraud risks. Configurable controls and levels of access in your ERP can mitigate risk to sensitive data, and any ability to override or enter conflicting or unauthorized transactions, such as vendor orders and payments.

Companies who use ERP solutions can leverage the built-in controls to reinforce the checks and balances, that will help prevent fraud.

Unfortunately, fraudsters are becoming more savvy and come up with new techniques all the time, requiring your internal controls to be robust enough to stop them in their tracks. In the end, the risk of doing nothing can cost you more.

Manual controls for fraud detection are no longer sufficient.

Forensic data analytics techniques can play a significant role in the early stages of detection and monitoring risks of fraud. These techniques can allow your organization to extract, analyze, and interpret your business data to help detect potential instances of fraud.

ANTI-FRAUD PROGRAMS



Anti-fraud programs and controls are measures taken by organizations to prevent, detect, and respond to instances of fraud and misconduct.

When anti-fraud training programs are implemented, fraud-related loss drops by 48 percent and the average time of fraudulent activity reduces by 40 percent ([2015 -16 Global Fraud Report, Kroll](#))

Evaluating anti-fraud programs, controls, ethical conduct, and compliance with policies and procedures in the business by assessing their vulnerability to fraud is the foundation on which effective anti-fraud processes are built.

ANTI-FRAUD PROGRAMS



Components of an anti-fraud program and corresponding fraud controls vary by organization. Some basic elements include (but are not limited to):

- Fraud control policy
- Code of conduct/ethics and affirmation process
- Conflicts disclosure
- Fraud awareness (communication and training)
- Fraud risk assessment
- Reporting procedures and whistleblower protections
- Investigative process
- Remediation and corrective action
- Continuous monitoring (preventive/detective controls)



 Prevention	 Detection	 Response
<ul style="list-style-type: none"> ■ Internal audit and compliance functions ■ Fraud and misconduct risk assessment ■ Codes of conduct ■ Employee communication and training ■ Process-specific fraud risk controls ■ Proactive forensic data analysis (continued monitoring) 	<ul style="list-style-type: none"> ■ Hotlines and whistleblower reporting mechanisms ■ Substantive testing ■ Proactive forensic data analysis (retrospective review) 	<ul style="list-style-type: none"> ■ Internal investigation protocols ■ Remedial action protocols ■ Enforcement and accountability protocols ■ Disclosure protocols

CONCLUSION



The reality is that both management and employees have important roles to play in the prevention and detection of fraud. Furthermore, people, process and technology and their internal controls alone are not sufficient to mitigate fraud. Corporate culture, the attitudes of executive management and all employees combined, must be aligned in the best interest of the business, so that the company remains resistant to fraud.

ABOUT SYSPRO



SYSPRO software is an award-winning, best-of-breed Enterprise Resource Planning (ERP) software solution for cost-effective on-premise and cloud-based utilization.

Industry analysts rank SYSPRO software among the finest, best-in-class enterprise-resource planning solutions in the world. SYSPRO software's powerful features, simplicity of use, scalability, information visibility, analytic/reporting capabilities, business process and rapid deployment methodology are unmatched in its sector.

SYSPRO, formed in 1978, has earned the trust of thousands of companies globally. SYSPRO's ability to grow with its customers and its adherence to developing technology, based on the needs of customers, is why SYSPRO enjoys one of the highest customer retention rates in the industry.



NEXT STEPS:

If you want to learn how SYSPRO can help mitigate and monitor fraud risks, contact us today at info@ca.syspro.com or +1 (888) 259-6666.