

What is Your Fraud Cost Per Mile?

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Fraud is seldom discussed in many small to medium-sized transportation companies because there is a tendency to trust the colleagues with whom we have built relationships. Unfortunately, the risk is significantly greater in small to medium-sized carriers than in larger carriers as many small business owners believe they will not become victims of fraud and therefore, do not take precautions.

Temptation or personal financial pressures can push even the hardest working, most trusted employee to commit fraud. The incentives are in the headlines daily: unemployment is on the rise and the economy is in a recession. Furthermore, many transportation companies have downsized their workforce in order to continue operations. Workforce reductions may create additional opportunities for employees to perpetrate fraud as segregation of duties becomes more difficult. Additionally, the remaining employees, who may have also had pay cuts, and are now asked to perform additional tasks, have more reasons to rationalize perpetrating fraud.

The goal should not be to suspect every employee of theft, but to remove or minimize the temptation and opportunity to commit fraud. Most employees have good intentions, but even the best

intentions can be overcome by basic human needs. The first step is to inform employees that the company is looking for discrepancies. The employees' perception can be a strong ally in minimizing the risk of fraud.

Areas that present significant opportunities for fraud in transportation companies include:

Ghost Employee Schemes

Ghost employee schemes consist of payments made to workers who are not legitimate company employees. Since payroll represents a significant part of a transportation company's expenses, it is logical to believe that this is an area where a trusted employee may perpetrate fraud. Given the overall number of drivers and the high turnover rate, it is critical to track drivers as they are hired and terminated. Access to the driver master file should be evaluated to see if there are any unauthorized individuals who have access to the file. If a member of the accounting department has access to the driver master file, there is a chance a fictitious driver could be set up and funds improperly disbursed.

Management should evaluate who has access to the driver master file and who prepares and reviews the payroll. Management should also consider performing a weekly reconciliation of the miles billed versus miles paid to drivers.

Fictitious Vendor Schemes

Fictitious vendor schemes consist primarily of disbursements to shell company vendors set up by accounting staff. These disbursements are often made by trusted employees to a vendor who may have a similar name as another vendor that is frequently used. An employee misappropriates the funds by setting up a legal entity with a similar name, then sets up a bank account under the shell company's name, and cuts a check to the company. These schemes may be difficult to detect unless the vendor master file is reviewed periodically, proper procedures are established to set up vendors, and disbursement registers and invoices are reviewed and signed off before checks are released for payment. In smaller trucking companies, the owner may want to receive the monthly bank statements directly from the bank and review the statement for any unusual checks clearing each month.

Lapping of Accounts Receivable

Applying cash receipts to customer invoices as they are received may seem like a fairly simple task; however, due to the number of transactions that occur within most transportation companies, this area presents a risk. Without proper segregation of duties, an accounts receivable clerk may have the opportunity to

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misappropriate receipts when they are received from the customer. As future payments are received from the customer, the accounts receivable clerk will apply the payment to the oldest invoices. By applying receipts to the oldest invoices, the accounts receivable aging does not deteriorate. Lapping schemes can be very costly if management does not review their accounts receivable aging periodically and have the proper segregation of duties in the cash application process.

Owners should also review the company's financial results with the CFO or controller on a monthly basis. Any unusual variances should be questioned and any unreasonable responses should be further investigated. Additionally, reviewing income statement line items as a cost per mile may bring unusual variances to the forefront.

There is not one specific strategy to identify fraud. Warning signs may vary and may not even exist, depending on the situation. Consider these factors in assessing your current risk:

- Do internal accountants have direct supervision?
- Are they responsible for all aspects of the accounting process with limited segregation?
- Do they often work after hours or at home and continually misplace files and other documentation?
- Are there any sudden changes in behavior (i.e. standard car traded in for a luxury car)?
- Is there a reluctance to take extended vacations?

While some of these traits indicate a hard-working, trusted employee, they

are factors to consider in assessing fraud risks in today's environment.

Fraud is a cost of business that typically goes unnoticed until it is too late. The key is to be proactive. Identifying weaknesses and taking action before the fraud occurs will help you manage the risk.

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