

How to Detect and Stop Fraud, Waste, and Misuse in Employee Expenses

A Best Practices Guide for Mitigating Purchase Card and Travel & Expense Risks

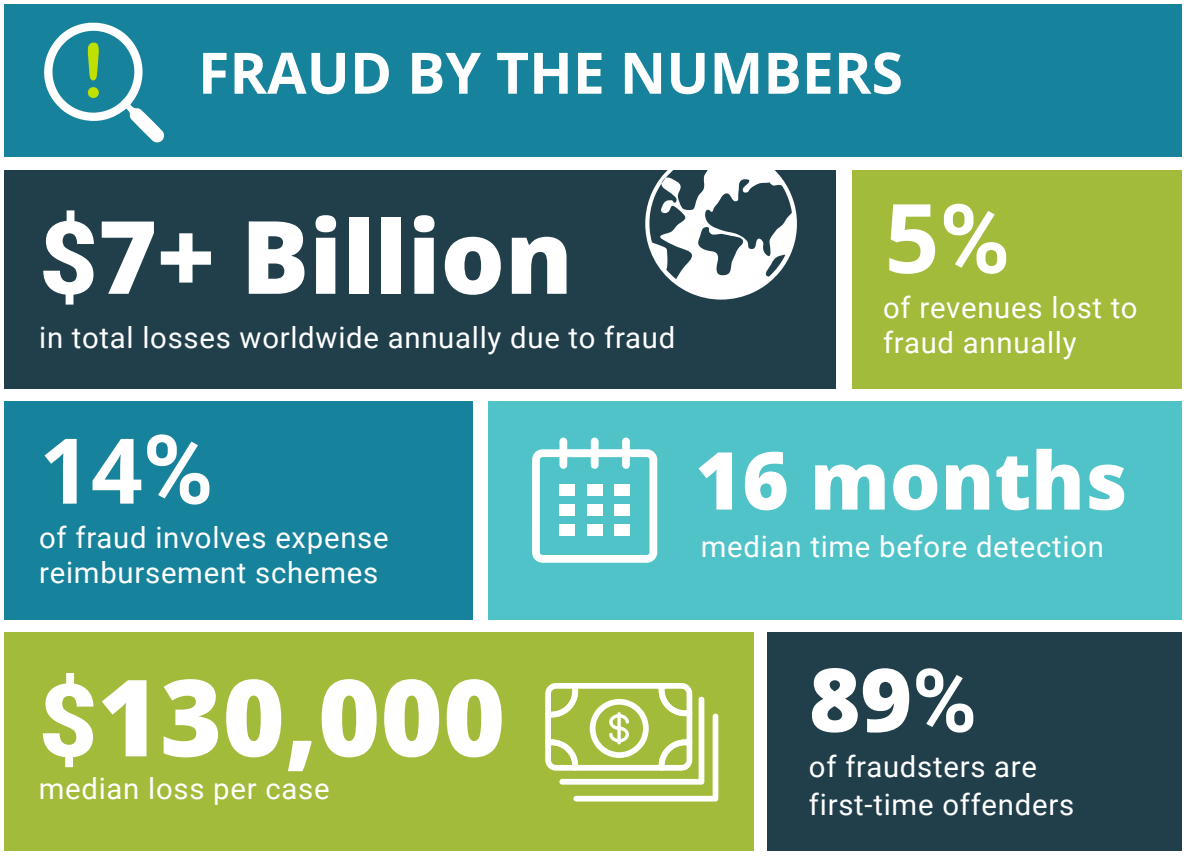
Oversight

Occupational fraud is the silent killer of business. It is universally faced by all companies, whether large corporations or small- to mid-sized business—no one is immune. According to the Association of Certified Fraud Examiners' (ACFE) 2018 Global Fraud Study, the typical organization **loses 5% of revenues each year to fraud with a median loss of $130,000 per fraud case.**

The type of business you're in doesn't seem to matter either. Fraudsters can be found in every industry and across all geographies. Perpetrators range from high-level executives to regular employees.

What's eye-opening is that roughly 89% of fraudsters are first-time offenders with clean employment histories. This means they are hard to spot before you hire them. In fact, they usually don't take a job with the intention to defraud their employer, but nonetheless they seize the opportunity and employers fall victim to their schemes.

Among the most common types of fraud involves the use of purchase cards (P-Cards) and travel & expense (T&E) reimbursements, accounting for 14% of all fraud, according to the ACFE. Often, employees start with cheating on expense reports, then progress to other types of fraud.



Source: ACFE 2018 Global Study on Occupational Fraud and Abuse

Mitigating T&E and Purchase Card Risks

Total losses from T&E and P-Card fraud, waste, and misuse can add up. Bad behavior can become epidemic as it spreads across organizations as the “everyone else does it” mentality takes over.

So, what can you do to stop it?

Policies, training, and well-planned controls are the right place to start. Most companies have some form of policies and controls in place. These preventive measures are aimed at reducing the opportunity for fraud, waste, and misuse, and removing the temptation from potential offenders. They focus on guiding employees to make the right decisions before the transaction.

Prevention has a role to play, but the reality is that even the most clearly defined policies will be ignored and that no internal controls are perfectly effective. Prevention will not mitigate all T&E and P-Card risk, so systems need to be in place to detect issues in a timely manner. Organizations need both prevention and detection to mitigate the risk of fraud and misuse.

Detection should involve use of analytical procedures that highlight anomalies and reporting mechanisms that communicate and remediate suspected problematic spending. A comprehensive detection system includes exception reporting, data mining, trend analysis, and ongoing risk assessment. Many fraudsters exploit deficiencies in control systems. Through detection of such problems, controls can be tightened to make it more difficult for potential perpetrators to act, and training can be provided to correct behavior.

Automated data analytics, powered by Artificial Intelligence (AI), has become critical to detecting patterns of problematic behavior and preventing future occurrences.



Focus Where it Matters

Humans make errors. Most of these mistakes are honest, but sometimes they’re intentional.

Oversight data proves this point. Our research shows that 70% of employees comply with policy and 25% slip up on occasion. It’s the remaining 5% who contribute to 95% percent of high-risk spending.

Identifying the 5% and having visibility into their spending behavior helps you effectively escalate the matter and drive change that improves business outcomes.

How Data Analytics Uncover Fraud & Misuse

Automated data analytics provides a clearer picture of the risks within T&E and P-Card programs. Each transaction and the complete context of the transaction are analyzed with the same level of scrutiny that an internal auditor or fraud examiner would employ. This complex analysis is a combination of rules-based, behavioral, and deductive analysis, evidential reasoning, and standard business intelligence. Through continuous transaction monitoring and analysis, organizations can flag suspicious activities and clearly distinguish the highest-priority concerns from hundreds of indicators of fraud, misuse, and waste.

The ability of data analytics to apply these approaches in combination is what enables an automated solution to identify issues that warrant further human investigation and efficiently investigate and resolve problems.

A comprehensive data analytics solution for mitigating T&E and P-Card risk will have the following capabilities:

- ☐ ***Pre-built analytics:*** Provides prescriptive analytics using rules-based scenarios
- ☐ ***Behavioral analytics:*** Uses text, statistical, time-based, similarity, evidential reasoning, guided machine learning, and adaptive analytics to detect anomalies
- ☐ ***Multi-dimensional risk analysis:*** Provides comprehensive visibility across all expense reports and employees. Finds and shows high-risk patterns, including attendee risk, expense category risk, geographical risk, timing risk, and behavioral risk
- ☐ ***Cross-departmental and cardholder analysis:*** Combines data sources from other systems to maximize insights and present a holistic view
- ☐ ***Configurable audit settings:*** Fine-tunes best-practice analytics for different risk preferences
- ☐ ***Continuous monitoring:*** Continually reviews 100% of transactions across all expense reports and purchase card transactions over all time and automatically flags exceptions or violations for investigation and resolution
- ☐ ***Flexible timing of analysis:*** Monitors purchase card and other transactions before expense submission all the way through post-payment analysis
- ☐ ***Case management:*** Uses built-in workflows and email capabilities to quickly and efficiently investigate suspicious activities rather than ad-hoc emails and phone conversations
- ☐ ***Logging / audit trail:*** Automatically documents all procedures performed and creates a complete audit trail

Can data analysis be done within existing systems?

Some organizations believe that their travel expense management (TEM) systems or their ERP systems can protect them from fraud and misuse. While TEM solutions provide spend reports and decrease the reimbursement lifecycle and ERP systems streamline processes and deliver information across an organization, most are not designed with the analytics necessary to detect fraud, misuse, and waste across the organization. Purpose-built data analytics provide continuous monitoring for suspicious transactions and patterns as part of an effective financial risk mitigation strategy.

Effective Controls: How to Reduce T&E Risks

Opportunity for fraud and misuse occurs when there are weaknesses in controls.

Comprehensive data analytics monitoring solutions should automatically check for fraud schemes and common misuse issues. With a detailed view of T&E spending habits and the ability to pinpoint the employees with patterns of non-compliant activities, you can better adjust policy, procedures, controls, and training to prevent them from recurring.

By monitoring and analyzing all transactions across all expense reports and across all time — not just a sample or slice in time, organizations can ensure that employees follow corporate travel and expense policies. Companies that monitor expense transactions will identify out-of-compliance spending, allowing managers, human resource professionals, and general counsel to take appropriate action. At the same time, companies will see a significant improvement in employee compliance with T&E policies.



Automated checks to identify fraud and misuse in T&E should include:

- ☐ ***Duplicate Submissions:*** TEM systems do a good job of spotting the same expense being reported twice on the same expense report. But things get more challenging, for example, when expenses are duplicated across multiple reports or by multiple travelers.
- ☐ ***Personal Expenses:*** A common area of misuse involves submitting expenses that are not legitimate business expenses. Employees may be tempted to submit personal expenses when they know it may be difficult for a reviewer to recognize when an expense or a trip was for personal rather than business purposes. For example, "bleisure" trips complicate this issue when business and personal travel overlap.
- ☐ ***Unapplied Transactions:*** Outstanding card transactions that have not been applied to expense reports can cause wrinkles in your T&E program. These unapplied transactions are accruing unreconciled, unjustified, and uncategorized corporate liability.
- ☐ ***Suspicious or Misclassified Purchases:*** Drop-down menus on TEM systems make it easier than ever to select expense types. But when travelers erroneously select an expense type or intentionally misclassify the transaction, it impacts the deductibility of expenses, misrepresents the distribution of spending, and conceals non-compliant purchases.
- ☐ ***Suspicious Out-of-Pocket Expenses:*** Out-of-pocket expenses are an unavoidable fact of life for business travel. But they are often used to circumvent merchant category code (MCC) detection or to accumulate points, miles, and rebates on personal credit cards.
- ☐ ***Meals and Lodging Outliers:*** Hotels and meal prices vary by city and country. They can also vary greatly by season. For instance, hotel stays in Scottsdale, AZ, are three times more expensive in the winter months. Also, make sure any excessive meals and lodging expenses are justified. Understanding and incorporating this logic into your solution allows you to understand what is normal for your travelers and to spot when expenses for travelers at these locations are out of balance with the norm.
- ☐ ***Refunded Expenses:*** Make sure every credit is accounted for – to the penny. A common fraud involves employees submitting expenses and then canceling the transaction. The employee receives the refund amount personally but doesn't return the credit to the company. Another variation of this is an employee booking a business class ticket and changing to an economy ticket, keeping the airline credit for themselves.
- ☐ ***Unusual Mileage:*** Overstating mileage and submitting duplicate mileage, public transport, or car rentals are common schemes.
- ☐ ***Excessive Personal Spend:*** Unusually high or frequent expenses can indicate potential fraud or misuse. The key to cutting waste and abuse is to understand what is normal for your travelers and to spot when expenses for certain travelers are out of balance with the rest.

How To Reduce Employee Purchase Card Risk

P-Cards can significantly reduce the cost of traditional procurement processes and maximize P-Card rebates. While P-Cards offer convenience and distributed buying power, their ease of use and accessibility significantly increase the chances for fraud, waste, and policy abuse.

Many companies use merchant category codes (MCC) blocks to control purchase card use, such as precluding the use of the card for purchases from department stores, liquor stores, gentleman's clubs, and other venues where spending should never occur.



Although partially effective, this preventive control is not foolproof. Problems can arise when merchants self-identify their MCC very broadly. This can allow valid merchants to be excluded and invalid ones to slip through the cracks. MCC exclusions can also become overly restrictive to the point that employees become frustrated, stop using their cards, resulting in decreased usage and rebates.

By monitoring and analyzing all P-Card and associated expense transactions, you can ensure employees follow corporate T&E and P-Card policies. By implementing automated analysis of 100% of card transactions, card program administrators can focus on the highest risk transactions and outlier activities.

A comprehensive data analytics solution for mitigating P-Card risk will have the following capabilities:

- ☐ ***Duplicate Purchases:*** Double dipping costs the organization. P-Cards can be used to intentionally duplicate purchases that benefit the employee but are prone to unintentional errors whereby a P-Card transaction is also expensed on a T&E expense report or when the vendor also sends an invoice and it gets paid via Accounts Payable.
- ☐ ***Unusual or Out-of-Policy Purchases:*** Cardholders can be cunning. High or frequent use of P-Cards can indicate potential fraud or misuse. Policy violations that slip past MCC exclusions, patterns of misuse, split transactions that circumvent single transaction limits, and potential fraudulent activity associated with unusual spending and outlier purchases need to be monitored closely, so you can determine where policy and spending limits should be adjusted.

Continuous Monitoring Finds Fraud, Waste & Misuse Sooner

Continuous automated data monitoring can serve as a powerful deterrent by influencing compliant employee behavior from the start. Research shows people behave differently when they know they are being watched. For example, individuals who are tempted to cheat on their expense reports may think twice if they know they are being monitored.



reduction in out-of-policy transactions with continuous monitoring in place

Timing Matters

According to the ACFE, the median time of detection for fraud schemes is 16 months. However, organizations that proactively monitor data using an automated risk management solution detected frauds in less than half the time, with 52% lower fraud losses.

Of course, the sooner a fraud or misuse is found, the sooner the risk can be addressed—before it has the chance to escalate into something that causes greater internal damage and external reputational risk. Our solutions have helped companies detect cases where employees have expensed online psychics, pet boarding, online dating services, multiple visits per week to the liquor store, funerals, family vacations, and wedding receptions.

Most companies with T&E or P-Card programs want to influence employee behavior, rather than "slapping wrists" during a given period or playing "gotcha!" many months later. Monthly automated analysis works well, because it is better at getting to the "why" of spending, which allows companies to course-correct, adjust policies, and create powerful communications, training, and coaching to catch and influence employee behavior early on before it becomes a habit.

A T&E and P-Card continual monitoring solution should provide the ability to deliver automated policy education and feedback to employees. By outlining specific policy violations, companies have been able to improve employees' future spending decisions and reduce policy violations by as much as 70%.

Efficient Resolution of Identified Fraud & Misuse Issues

Detecting P-Card and T&E fraud when it occurs is a good first step. But an automated risk management and compliance monitoring solution should also provide tools to help you efficiently investigate and remediate the potential fraud and misuse issues.

Your automated data analytics solution should deliver a ROI by identifying true positives — issues that turn out to be actual cases of fraud, misuse, or error.

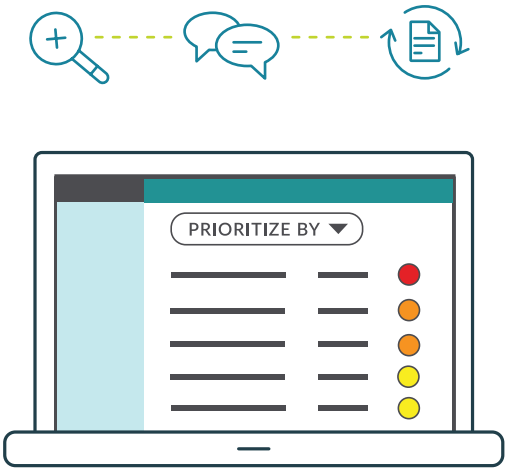
False positives are an obvious cost, requiring an equivalent effort to determine if corrective action is necessary. One of the primary keys to avoiding false positives is to employ time-based reasoning by viewing transactions in context of their relationships through time to determine usual and unusual transactions. A risk management analytics solution should continually reduce false positives, so you can focus your limited resources on addressing those high-risk transactions.

The Power of Automated Analytics

Advanced AI-based data analytics identifies the high-risk transactions for you and lets you focus on correcting issues — instead of spending hours trying to find the issues in the first place. When best-in-class solutions detect a high-risk activity, they automatically assign the issue to the audit team for remediation.

Truly automated monitoring goes beyond static reporting to provide integrated and interactive case management and workflow tools that:

- ☐ Presents exceptions in a risk-prioritized list
- ☐ Identifies and shows both underlying patterns and supporting data for a high-priority risk as part of an integrated case management system
- ☐ Presents plain-language descriptions of all indicators that flagged the transaction as a potential issue
- ☐ Offers click-through access to all supporting data to facilitate investigation
- ☐ Documents all resolution steps

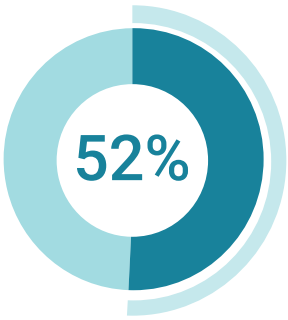


The Takeaway

A best-in-class solution should accurately and clearly identify high-risk transactions. It should provide an integrated case management workflow to help you efficiently resolve issues, communicate, and collaborate with employees and internal stakeholders. It should also create a permanent audit log that records case ownership, state changes, and notes, while validating corrections were made. From a compliance standpoint, if it's not documented, then it didn't happen.

Built-in dashboards, generated from the data analytics and workflow, allow your operations and senior management to review trends, make informed decisions, adjust policies, and implement strategies to influence employee behavior. Lastly, the results of the resolution process need to be fed back into the next data analytics run so the system gets smarter with each iteration.

The best way to manage T&E and P-Card risk is to employ an AI-powered, automated data analytics tool coupled with your TEM software. This combination is the only truly effective way to mitigate your T&E and P-Card program risks, reducing fraud, misuse, and waste and driving employee behavior to create a more compliant organization.



Proactive data monitoring/analysis was associated with 52% lower losses and 58% faster fraud detection.

Source: ACFE 2018 Global Study on Occupational Fraud and Abuse

ABOUT OVERSIGHT

Oversight is the most trusted audit and risk management partner for the Fortune 5000 and large public sector organizations. Our AI-powered platform provides an enterprise-wide view of spend risk, detecting errors, policy violations, and fraud through continuous monitoring and analysis. With Oversight, you have full visibility into spend data to improve compliance, establish better controls, and protect your bottom line.

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