"WoYD 3 process" fraud risk identification method

(according to Thinus Barnard)

This method was developed based on experience obtained during the past 16 years of conducting external audits, internal audits and numerous fraud investigations. This method is just an extension of one of my mantras: "*Never focus on the known suspects only – understand the process.*" Why? By only focussing on and taking out a suspect (figuratively speaking of course) you are just providing his replacement with the same opportunities and the syndicate gains more confidence.

How will this method help you?

Firstly, it will assist you in investigating syndicate activities more effectively. It will help you in identifying those individuals who are key to the success of a syndicate. A syndicate has a similar structure to that of your organisation, i.e. there is "senior to middle management", "foot soldiers" / "worker bees" and the "distribution channels".

I have lost count of how many syndicate investigations I have been involved in, but more often than not the list of suspects presented to me at the start of an investigation will reflect some of the foot soldiers, some individuals involved on the distribution side and a "possible maybe" reference to a senior person. The client will often inform me that there were numerous allegations in the past against this one and that one, but rarely any concrete evidence was found.

War story #1 – The missing links

A recent syndicate investigation emphasised the importance of the "WoYD 3 process" method. My client had a list of 16 suspects, which included forklift drivers & stock pickers at their factory, as well as employees at one of their depots. But not one senior person! Within four days we walked through the process – from when raw material is ordered and delivered until the final product is sold and delivered to the client. We managed to identify 5 senior personnel at the factory – one was aged 53 and reporting directly to EXCO – and the manager of the depot. They were all part of the syndicate. The syndicate operated for more than 10 years. The one individual was in a key position where she (let's call her Ms Link) was responsible for collating information from the production lines, regarding actual versus planned production, wastage reports and stock count results. She was responsible for capturing these results onto the SAP system. She was in the ideal position to manipulate the results from the various sources in order to hide the losses and to ensure that the losses remained within acceptable levels. Your immediate question was hopefully: "But surely they should have known that Ms Link was performing conflicting duties?!" I read through the standard operating procedures – focussing on her duties as reflected within these prescribed processes. According to these records, the "Production clerk" is required to capture actual versus planned production results, the "Wastage clerk" is required to capture wastage results and the "Finished goods clerk" is required to capture the daily stock count results. But unbeknownst to the internal auditors, these three clerks were the same person. They missed this link purely because different internal auditors were assigned to each relevant process. Therefore, by not comparing notes or applying their minds they neglected to identify this crucial control break down. Could this be happening right now at your organisation?

Secondly, this method will assist you in understanding your processes better. It provides you with a "rubber sole" approach in understanding what your staff is actually doing. This is crucial in identifying fraud risks. Any experienced fraud investigator will quickly tell you that what you thought is happening on the floor and what is actually happening are two different things. When assessing fraud risks within your organisation, you have to perform a "rubber sole" walk through of the systems and processes. No desktop review or workshop can do this effectively.

Thirdly, this method will greatly assist in other pro-active fraud risk management initiatives, such as data mining and continuous control monitoring. In this regard please refer to www.crisp-dm.org which provides a cross industry standard protocol for data mining. One of the key elements of this model is "business understanding", which refers to the actual processes and procedures performed by your staff. Various consultants will tell you about their unique model or approach – but it is all based on CRISP-DM which has been around for ages.

There are various other benefits of this method, but these three stand out for me.

What does the "WoYD 3 process" method entail and what the hell is "WoYD"?

"WoYD" is my acronym for "What's on Your Desk". It is my version of the "rubber sole" approach to identify fraud risks and to understand your staff's daily activities. This requires you to actually sit down and ask a person what is on their desk, where did this set of documents come from, who provided him/her with these instructions, what checks will he/she be performing on these documents, when and what will they be capturing on the system, where are these documents going next, etc, etc, etc.

Clients often provide me with their standard operating procedures (aka "SOP's"), documented procedures or flow charts of an environment to be investigated. My response has always been: "Thanks, but no thanks!" Those SOP's will be welcome at the disciplinary hearings when you want to take someone on for not complying with prescribed procedures, but it will not help me to identify a fraud. Fraud is in the detail and the detail is not recorded in the SOP's.

When investigating a fraud I always ask myself questions such as: "Who allowed this to happen?", "Who should have picked this up?" "Who did not perform the necessary checks and balances earlier in the process?" This is when you start knocking on a syndicate's door!

Furthermore, the "WoYD 3 process" method is based on the following premise:

Within any organisation, business unit or process there are always 3 processes at play, i.e.:

1) The procedures which management assume are being adhered to (this is normally the standard operating procedures, documented procedures or flow charts, which forms the basis of most external or internal audit reviews);
2) The procedures which are actually performed by staff during their daily activities (usually slightly different from number 1); and
3) The IT system (i.e. the system which your staff updates or have access to during the performance of their daily duties such as SAP, Oracle or a legacy stock management system which interfaces with your ERP system).

When applying this method it is also advisable to consider the following:

There is actually a formula for fraud/corruption, i.e. C = M + D – A

(this is based on an article written by Professor Robert E Klitgaard – Cape Times 1 March 2010 – local newspaper in Cape Town)

C = Fraud or corruption

M = Monopoly

D = Discretion

A = Accountability

Therefore, fraud / corruption will occur where:

- A person or group has full "*control*" over a process or commodity;
- The same person or group use their discretion in managing the process or commodity; and
- They are not accountable to anyone or they use their discretion on how to account for their activities.

Well this made sense to me. If not for you please phone or email and we can discuss. I placed the word "control" in parenthesis, because control does not mean "in charge" of a process such as one would expect from a manager of the process, but rather the person or group who has a significant influence over that process.

War story #2 – The secret manager

At one of my clients we identified – again with the "WoYD 3 process" method – that a very senior person (let us call him Mr John "Almost" Doe – I will explain later) in their quality control department was operating a syndicate.

He was second in command in this department at the age of 55, but he reported to a youngster aged about 30. Now the youngster was still learning the ropes and relied heavily on Mr Doe, because firstly Mr Doe declined the promotion to manager of the department due to his alleged early retirement plans, EXCO wanted someone in the management role for at least 5 or more years continuously and Mr Doe has been with the company for 35 years. He had a reputation for being very knowledgeable of the company's processes and almost everyone would come to him for advice. Therefore, if stock moved without paperwork on Mr Doe's instructions, it was accepted as being OK. He would often request stock from the warehouse for quality control testing – no paperwork.

Therefore, although there was a clear management structure within the factory and warehouses, Mr Doe called the shots.

And why do I call him Mr John "Almost" Doe – his "clients" want more stock at the bargain prices of the past and he made the mistake of taking significant deposits from some of his "clients". Basically they want their money back and he is in jail. Put one and one together!

Please also read my article about which processes within you organisation could be susceptible to fraud, because sometimes it is the processes which you least suspect.