



First Friday Fraud Facts+

August 3, 2018

The Office of Idaho State Controller Brandon Woolf distributes this newsletter as a public service and as a cost-effective method of increasing awareness about ways to detect and prevent fraud, waste, and abuse in government.

The Lap Trap

Lapping is the fraudster’s version of “robbing Peter to pay Paul”. It is the extraction of money from one account to cover shortages in another account. A lapping scheme is a fraudulent practice that involves altering accounts receivables to hide a stolen receivables payment. The method involves taking a subsequent receivables payment and using that to cover the theft. The next receivable is then applied to the previous unpaid receivable, and so on.⁴ For example, a fraudster steals the payment intended for customer A’s account. When a payment is received from customer B, the thief credits it to A’s account. When customer C pays, that money is credited to B. Repeated many times, lapping is difficult for the dishonest employee to keep track of. In time, lapping schemes will invariably reveal themselves.²

Employees involved in this sort of fraud often rationalize that they are simply borrowing the cash and plan to repay it at some future date. Lapping is usually detected when the employee leaves the organization or becomes sick and must take time off of work.

The Governmental Environment and Fraud Schemes

Governments are susceptible to a slew of schemes involving cash, receivables, and vendor payments. Governments are also susceptible to different types of fraud than the traditional for-profit entity, as net income and earning per share are not a driving factor for public entities. Combine the various fraud schemes with a small work force or a work force with lower pay and the government finds itself struggling to ensure controls are in place and are adequate to prevent and deter fraud. Another factor is that government employees are making decisions about what to do with “public funds” and may have an attitude of “spend it or lose it”.⁵

Often governmental entities have a limited work force, which undermines management’s ability to segregate functional responsibilities. The concept of segregation of duties ensures that no one person has complete control over a single transaction. For example, the same person should not be able to enter new vendors into the system, create invoices, print and mail checks to the vendor, and reconcile the bank account. By introducing a second person into the transaction cycle, an organization reduces the opportunity to commit fraud because now collusion (secret or illegal cooperation or conspiracy) may be necessary to pull off the scheme.⁵

Management must put more emphasis on its detective controls when a government has a limited number of employees to adequately segregate duties. Detective controls include tasks such as account reconciliations, budget-to-actual comparisons, exception reporting, and surprise inspections or cash counts, to name a few. One of the most important detective controls is the reconciliation of the bank account(s). That task should be performed by an individual not performing the day-to-day transactions. Furthermore, the person performing the reconciliation needs to have the

Asset misappropriation schemes are the most common and the least costly, 89% of all fraud cases at \$114,000 median loss.⁷

- ACFE 2018 Report to the Nations



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proper training to identify red flags for inappropriate activity. The reconciliation should go beyond making sure the bank statement, deposit slips, and accounting system entries match, but should also take into consideration red flags common to fraud schemes.

The following are some classic red flags of lapping²:

- Delays in posting customer payments, and/or making deposits
- A trend of decreasing payments on accounts receivable
- Customer complaints

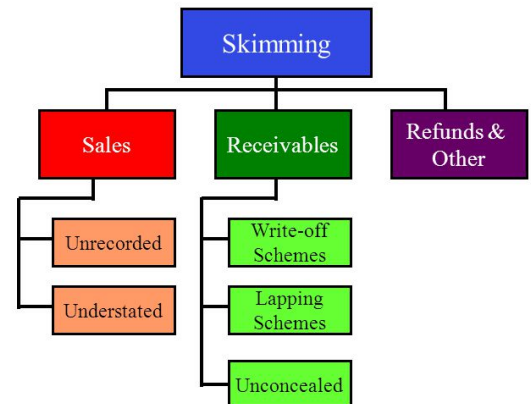
Detection and Prevention of Lapping Schemes

Controls that can be used to prevent or detect lapping include the following¹:

- Have someone other than the accounts receivable clerk send statements to customers. Customers know what they paid to the governmental agency, so they should be able to detect unusual payments ascribed to their accounts, or note that certain payments were never applied against their accounts.
- Contact customers and ask if they have received monthly statements from the governmental agency. The responsible party may have been intercepting and destroying the statements before they were mailed.
- Audit cash receipts transactions on a regular basis, as noted above.
- Require all employees in the accounting area to take all of their vacation time, without exception.
- Track the days of accounts receivable on a trend line. A gradual increase in this measurement can be caused by lapping.
- Tightly control the use of credit memos. A party committing fraud may attempt to terminate a lapping situation by writing off a receivable in the amount of the missing funds.
- Stamp all checks with "For Deposit Only," so that employees cannot deposit these checks to their own accounts.
- Have customers pay directly to a lock box, so that cash cannot be intercepted and stolen by employees.

At the end of the day, a government should remain vigilant by understanding its risks of errors and ensure it has the appropriate controls in place to provide reasonable assurance that its information remains complete, reliable, and accurate and that resources are properly secured.

Skimming Schemes



Fraud Case: 'Attorney General Conway Announces Conviction of Former Fulton County Utility Clerk in "Check-Lapping" Scheme'

Georgia Attorney General Conway announced the conviction of a former clerk at the Fulton Electric System in the theft of more than \$81,100 as part of "check-lapping" scheme.

The Attorney General's office began its investigation in December of 2009 at the request of Commonwealth's Attorney Mike Stacy after an audit identified \$81,137 in missing funds from the Fulton Electric System. The investigation found that Bivens utilized a "check-lapping" scheme where she took money from her cash drawer on a certain date and utilized checks from a later date to cover the missing cash.

Bivens was indicted on Aug. 12, 2010 on one count of theft by unlawful taking over \$10,000, a Class C felony which carries up to ten years in prison.⁶

A Fulton Circuit Court jury convicted 40-year-old Jennifer Renee Bivens, a mother of five from Dukedom, Tn., on July 12, 2011 on a lesser charge of theft by unlawful taking over \$500 but under \$10,000, a Class D felony. The jury recommended that Bivens be sentenced to one year in prison.

Citations

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³What is Lapping in Accounting? <https://bizfluent.com/info-8477979-lapping-accounting.html>. Accessed 12 June 2018.

⁴Lapping Scheme. <https://www.investopedia.com/terms/l/lappingscheme.asp>. Accessed 13 June 2018.

⁵ Fraud Schemes: How to Prevent, Deter, and Detect. <https://algaonline.org/index.aspx?NID=419>. Accessed 13 June 2018.

⁶Attorney General Conway Announces Conviction of Former Fulton County Utility Clerk in "Check-Lapping" Scheme. <http://migration.kentucky.gov/Newsroom/ag/checklapping.htm>. Accessed 13 June 2018.

⁷2018 Report to the Nations. <https://www.acfe.com/report-to-the-nations/2018/>. Accessed 13 June 2018.

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