



A Wolf Financial Group Member

Have a question?

Contact Vito Loisi
at 630-545-4554 or
vloisi@wolfco-fs.com

Want to improve your chances of obtaining a loan?

Check out our white paper on Contractor Financing on our web site at <http://www.wolffinancialgroup.com/Other-Resources>

Points to Ponder

"Be not dumb, obedient slaves in an army of destruction! Be heroes in an army of construction."

-Helen Keller

In a Difficult Economy, Guard Against Fraud

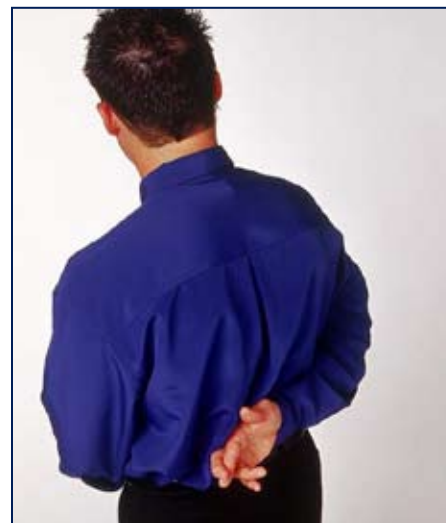
The most recent Federal Reserve report shows home construction is still down or stagnant in nearly all of the 12 Federal Reserve districts, and commercial construction remains slow, except for some minor boosts from federal stimulus projects and public construction. With unemployment in the industry still above 27 percent, we are obviously a long way from recovery, which means the financial pressures on contractors, subcontractors and suppliers will remain severe.

In times like these it is doubly important to be alert to possible fraud. The vast majority of companies you deal with are run honestly, but economic uncertainty can tempt some of them to cut corners or take unfair advantage, making your already challenging situation even worse.

Supplier fraud often depends on an insider within the victim company, such as an accounts payable clerk who goes along with a vendor kickback. In a 2009 ProfitCrew™ survey, those construction companies that were rated as top performers were found to be significantly more likely to take precautions against this type of fraud. Among the most-cited precautions:

- Systematic billings reconciliation
- Matching vendor invoices against estimates and purchase orders
- Defined monthly closing procedures for company books
- Dual controls and segregation of duties
- Internal control audits

Other supplier frauds may involve no one within your own company – bid-rigging, for example, or the use of substandard materials, which could



expose you to long-term risk and potential liability. Here are several good practices that can reduce your risk of supplier fraud:

- Grow and cultivate relationships. Find three or four trustworthy subcontractors or suppliers for every craft or material. Be open and transparent with them and expect the same.
- Vet new subcontractors and suppliers carefully. Check their credit, ask competitors about their performance, and bid trusted subs against each other on every job.
- If you're a subcontractor, take the same approach to any new GC you are working with. Be sure the financing for every major project is secure, and always purchase materials from trusted suppliers.
- Rely on a full set of plans and specs. Contractors and subcontractors should all sign off on the same detailed plans and specifications.
- Verify quality. Test and inspect work at every stage – from counting studs and inspecting joints to gauging wire and analyzing concrete cores – and document everything. ■

The Danger of Fraud on the Job Site

While fraud schemes can originate almost anywhere, many of the most damaging schemes occur on the job site itself. After all, that's where the bulk of most contractors' assets are found – and where fraudulent activity can be most difficult to detect.

Job site fraud commonly involves misuse of company equipment or theft of hard-to-measure materials, since it can be difficult to determine precisely what actually ended up in the job.

Case in point: To cope with personal financial pressures, one project manager ordered an extra spool of conduit and sold it at a scrap yard. No one noticed, and with no internal controls to stop him, he gradually grew bolder.



Questions & Answers

Finally he made his big move when he induced the owner to hire a new bookkeeper he recommended – one who was ready to join his scheme.

With invoices being paid routinely, the diversion scheme eventually expanded to include fuel, concrete, and even topsoil. The scheme ran successfully for months – until a newly hired employee noticed something wrong.

The honest employee blew the whistle – but not before hundreds of thousands of dollars had been stolen. Even worse, not wanting to expose his company to scandal, and with little hope of collecting restitution, the owner declined to press charges and ate the loss. ■

Who's Who in ProfitCrew™

Who: *David Kot, CPA, CFE is a senior audit manager and a member of Wolf & Company LLP's Construction and Real Estate Industry Group. He works with closely held businesses in the construction, distribution, and consulting/service industries. David is a member of the American Institute of Certified Public Accountants, Illinois CPA Society and the Association of Certified Fraud Examiners.*

What he does best: *David provides each client with an unparalleled level of commitment, quality and service to meet their financial and consulting needs. He became a Certified Fraud Examiner to gain a better understanding of how people act when given an opportunity. He has utilized that understanding to help his clients fine-tune their internal control procedures and gain efficiencies.*

In his spare time: *David enjoys spending time with his wife and two sons. A former college baseball player, he plays in numerous softball leagues and roots for all Chicago sports teams. On summer weekends, you can find him on a lake bare footing or cruising on a boat with family and friends.*

Question

I know I need to take steps to protect against employee fraud, but I don't want my employees to think I don't trust them. How can I be sure I'm doing enough – without establishing an atmosphere of mistrust?

Answer

Most employee fraud – accepting vendor kickbacks, loading up a friend's truck with cement, embezzling, kiting checks, or putting phantom employees on the payroll – can be prevented with common-sense controls that do not have to be offensive. For example:

- Segregate duties. Don't let one single person prepare checks, sign them, and then process the bank statements, too.
- Set authorization and access controls. Limit physical access to assets – not only building supplies but also cash and checks. Establish strong password requirements for computer accounting systems. And make "positive pay" arrangements with your bank to head off unauthorized payroll checks.
- Be known for your inquisitive nature. Always be the first to open the bank statement. Ask about expenditures. Compare cash receipts to accounts receivable, and compare reported withholdings to deposited withholdings.

You can't eliminate employees' access to valuable assets – they need access to do their jobs. But you can monitor access and make it clear you are paying attention.