



Introduction and Application of GAO's Fraud Risk Management Framework

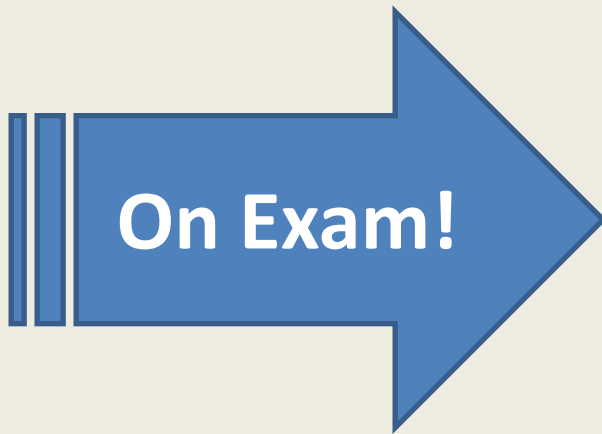
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Questions/Comments?



Caveats

- Information provided include personal views/opinions, not that of GAO. Just sharing some leading practices that I have learned in my professional career.
- Not receiving financial compensation from the AIG or GAO.
- GAO's Fraud Risk Management Framework is located on GAO's website at:
<http://gao.gov/products/GAO-15-593SP>
- For questions about the Fraud Risk Management Framework, please contact: Johana R. Ayers at (202) 512-6722; AyersJ@gao.gov

Learning Objectives

At the end of this course, participants will be able to:

- understand how GAO’s Fraud Risk Management Framework relates to existing federal standards for internal control (the Green Book);
- describe the four components of GAO’s Fraud Risk Management Framework and the leading practices related to each component; and
- apply the Fraud Risk Management Framework to audits involving fraud risks.

- **The Fraud Reduction and Data Analytics Act of 2015**, enacted in June 2016, required the Office of Management and Budget (OMB) to establish guidelines for federal agencies to create controls to identify and assess fraud risks and to design and implement antifraud control activities. The act further required OMB to incorporate the leading practices from GAO's Fraud Risk Framework in the guidelines.
- **The Payment Integrity Information Act of 2019** (which repealed the Fraud Reduction and Data Analytics Act of 2015) still requires the GAO's framework guidelines to remain in effect, subject to modification by OMB as necessary and in consultation with GAO. Source: **GAO-20-606 FCC's E-rate Program** (Note: for specific federal law, see specific handout titled "3d GAO Fraud Risk- Martinez - FRDAA revoked" on PDF pp. 19 and 21, R1s.)

What is Fraud Versus a Fraud Risk?



- Fraud involves intentionally obtaining something of value through willful misrepresentation.
- Types of fraud, if proven, can include
 - Fraudulent financial reporting
 - Misappropriation of assets
 - Corruption
- So, what are fraud risks?
- To what extent can fraud be identified and determined by OIG auditors? Why? What about fraud risks? Why?

Why is Fraud Risk Management Important?

- Fraud poses significant risks to the integrity of federal, state, and local programs, eroding public trust in and reputation of government services.
- Why should management proactively manage fraud risks?
 - help facilitate the program’s mission and reputation;
 - ensure taxpayer funds and services serve their intended purpose (intent, objectives, and mission);
 - help ensure funds are spent effectively, and assets are safeguarded.

Why Did GAO Develop the Framework?

- Based on our prior reviews, we recognized:
 - need for federal managers to take a more strategic, risk-based approach to managing fraud risks; and
 - managers were perceiving a conflict between the program's mission and fraud risk management (e.g., not seeing connection between the two).

How Does the Framework Relate to Existing Federal Criteria?

- complements *Standards for Internal Control in the Federal Government* (Green Book)
- fraud-specific and applies to nonfinancial, as well as financial, fraud risks

WHAT'S THE INTERNAL TEMPERATURE OF A TAUNTAUN?



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Relationship Between GAO's Yellow Book, Green Book, and Fraud Risk Framework?

Yellow Book (**Golden Rules of Auditing**) says that auditors should plan and perform procedures to develop the elements of a finding necessary to address the audit objectives.

- **Condition:** current
- **Criteria:** primary criteria (laws, regs..) and secondary criteria (GB and FRF)
- **Root Cause:** difference between C & C
- **Effect:** actual/potential (until R.C. addressed)

How Does the Framework Relate to GAO's Green Book?

Green Book

Provides standards required for managers.

Requires managers to assess fraud risks (Principle 8).

Includes principles and attributes related to all aspects of internal control.

Fraud Framework

Provides leading practices to help managers comply with Green Book's standards.

Provides guidance for implementing this requirement.

Adapts Green Book principles and attributes to a fraud-specific context.

Users of the Fraud Risk Management Framework

The Framework is designed for **federal program managers, but can be used by all**. In particular, it

- provides guidance for managers to strategically manage fraud risks;
- describes leading practices and conceptualizes these practices into a risk-based framework; and
- can be tailored to a program's operations and environment, including existing risk management efforts.



Where Can You Find Leading Practices in the Framework?

All **leading practices** are listed in tables (highlighted in light blue in the 2015 version).

Table 1: Leading Practices for Creating a Culture and Structure to Manage Fraud Risks

1.1 Create an Organizational Culture to Combat Fraud at All Levels of the Agency

Demonstrate a senior-level commitment to integrity and combating fraud.

Involve all levels of the agency in setting an antifraud tone that permeates the organizational culture.

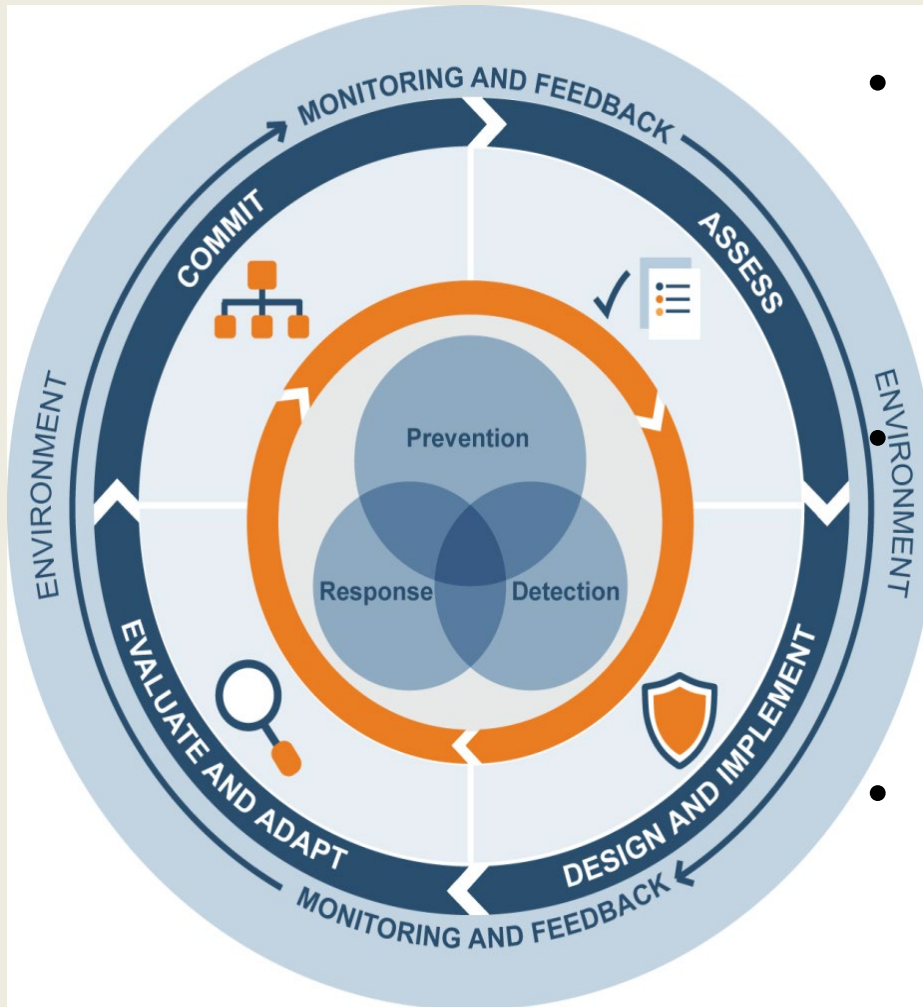
1.2 Create a Structure with a Dedicated Entity to Lead Fraud Risk Management Activities

Designate an entity to design and oversee fraud risk management activities that

- understands the program and its operations, as well as the fraud risks and controls throughout the program;⁴
- has defined responsibilities and the necessary authority across the program;
- has a direct reporting line to senior-level managers within the agency; and
- is located within the agency and not the Office of Inspector General (OIG), so the latter can retain its independence to serve its oversight role.

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The Fraud Risk Management Framework



- Encompasses control activities to **prevent, detect, and respond** to fraud, with an **emphasis on prevention**.
- Recognizes **environmental factors** that influence or help managers achieve their objective to mitigate fraud risks.
- Highlights the importance of **monitoring and incorporating feedback**.

First Component: Commit



Commit: to combating fraud by creating an organizational culture and structure conducive to:

- Demonstrating a senior-level commitment to combating fraud.
- Involving all levels of the program in setting an antifraud tone.
- Designating an entity to design and oversee fraud risk management activities (not the OIG).



Second Component: Assess



Assess: plan regular fraud risk assessments and assess risks to determine a fraud risk profile by:

- Tailoring the assessment to the program
- Involving relevant stakeholders and brainstorm.
- Assessing likelihood and impact of fraud risks, determine risk tolerance, and examine existing controls.
- Documenting program’s fraud risk profile, including risk tolerance, prioritization of risks, and other key findings and conclusions.



Benefits and Opportunities of Assessing Fraud Risks

Benefits

- Prioritize organization's most significant fraud risks
- Reflect organization's efforts to address fraud risks
- Assess the impact and probability of fraud risk in relation to objectives
- Targeted fraud risk discussion to include risk appetite, tolerance, and accountability

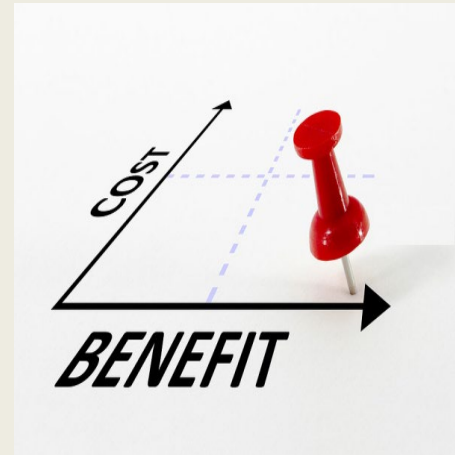
Opportunities

- Identify immediate and longer term improvement opportunities
- Drive consistency in approaches to assessing fraud risks

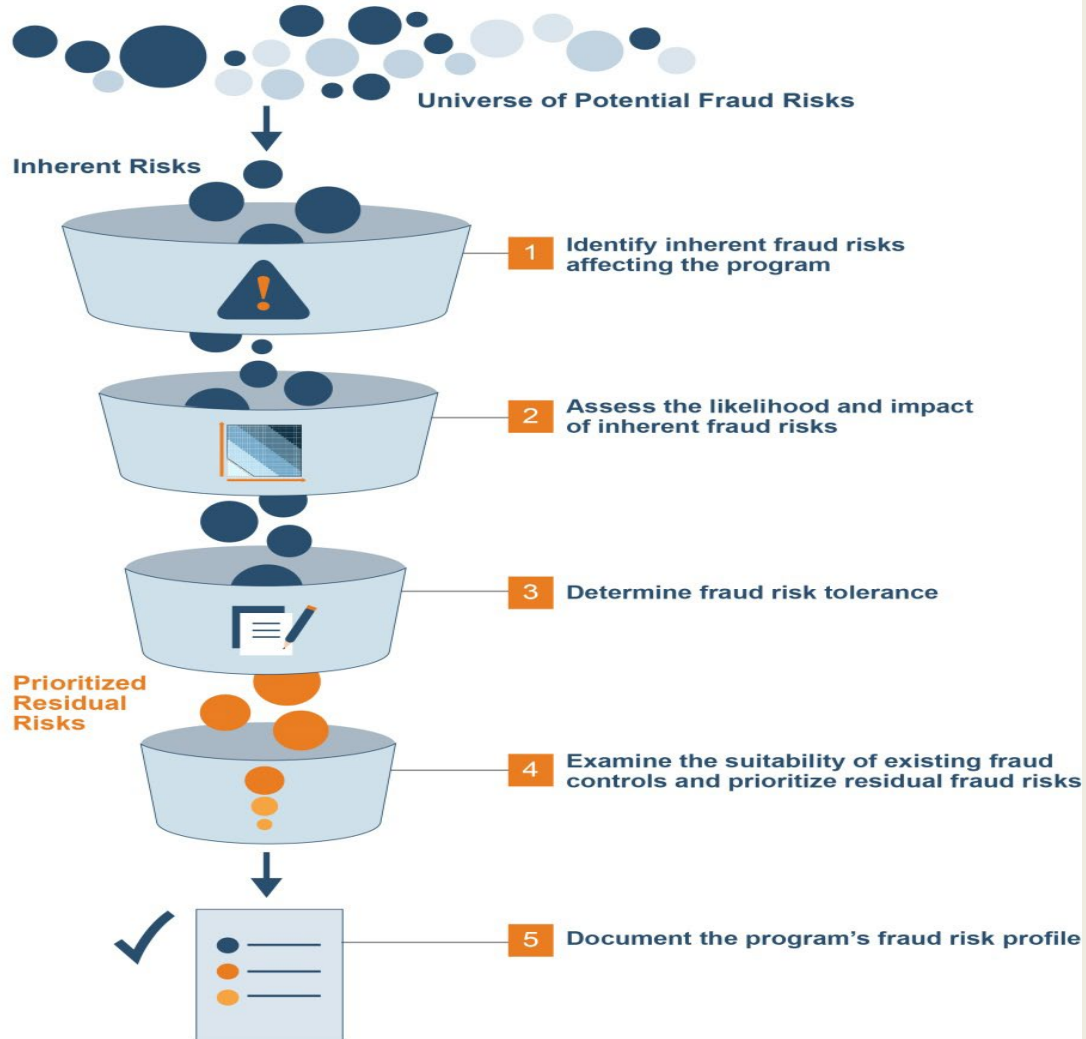
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Reminders when assessing fraud risks!

- Measure the “Likelihood (L)” and “Impact (I)” of fraud risk(s);
- Determine its significance as it relates to managers’ tolerance levels (i.e., $L \times I = \text{Significance}$) to understand the extent of the appropriate internal control response;
- Weigh internal control response against environmental factors, including costs and benefits and prioritize the fraud risks and responses.
- Document all steps above (show your work!)



Key Elements of the Fraud Risk Assessment Process



Source: GAO. | GAO-15-593SP

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How can we identify fraud risks?

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BRAINSTORMING

Some of the **best ideas** were found through it.

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Who to invite to brainstorming sessions?

- Organization's management. This ensures commitment to the understanding and management of fraud risks!
- Accounting and financial personnel who are familiar with the financial reporting processes and internal controls
- Non-financial operations personnel to leverage their knowledge of daily operations and issues within a program or process
- Attorneys, auditors, and investigators
- IT audit specialists.
- **Note:**
 - These are sensitive sessions, so all should have “need-to-know” access.
 - Management should engage the OIG at some point; it may be willing to share fraud risks indicated in adjudicated fraud cases/schemes involved.

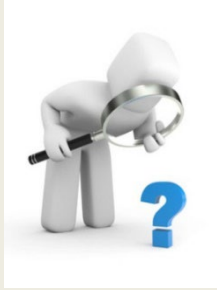
Fraud Brainstorming Reminders

- No thought is bad; all thoughts are considered. At the end of the sessions, all the walls in the meeting rooms are papered with ideas!
- Examine the control processes or program flows.
- Stimulate discussion by considering where those processes/controls can breakdown.
- Ensure attendees keep on time and on track.
- When identifying fraud risks, follow the money; where an organization is spending money, you will find fraud risks.

Use of surveys to learn about fraud risks?

Program managers can engage employees through internal control questionnaires to get more details on extent of fraud risks.

- Inquire about ways management might perpetrate fraud.
- Use care and auditor judgment; don't insinuate fraud is present or that employees or managers are suspects.
- Set the proper tone for the survey/questionnaires.
- Be sure to ask follow up questions. (critical thinking is key here!)



Third Component: Design and Implement

Design and implement a strategy with specific control activities to mitigate assessed fraud risks and collaborate to help ensure effective implementation by:

- Developing, documenting, and communicating an antifraud strategy.
- Considering the benefits and costs of controls to prevent and detect potential fraud, and develop a fraud response plan (**this leading practice can begin as early as the “Assess” component**).
- Establishing collaborative relationships (such as working groups) and create incentives and disincentives.



Fourth Component: Evaluate and Adapt



Evaluate outcomes using a risk-based approach and **adapt** activities to improve fraud risk management by:

- Conducting risk-based monitoring on an ongoing basis and conduct evaluations periodically.
- Collecting and analyzing data on instances of detected fraud to monitor fraud trends.
- Using results of monitoring, evaluation, and investigations to improve prevention, detection, and response.



When Should You Consider Using the Framework?



Auditors should consider using the Framework when audit objectives relate to managers' efforts to

- identify and assess fraud risks; or
- prevent, detect, or respond to fraud or fraud risks/indicators.

Reminder: the Framework can be applied to audits involving all fraud risk types/indicators, including

- internal and external fraud risks/indicators;
- financial and nonfinancial fraud risks/indicators; and
- beneficiary or contract fraud risks/indicators, etc.

Reminder: How Can You Use the Framework?



- The **leading practices** in the Framework can be used as criteria to help assess managers' fraud risk management efforts.
- The Framework can be used in conjunction with related criteria, such as the Green Book.
- Other information in the Framework can provide additional detail (e.g., to describe the “effect”).

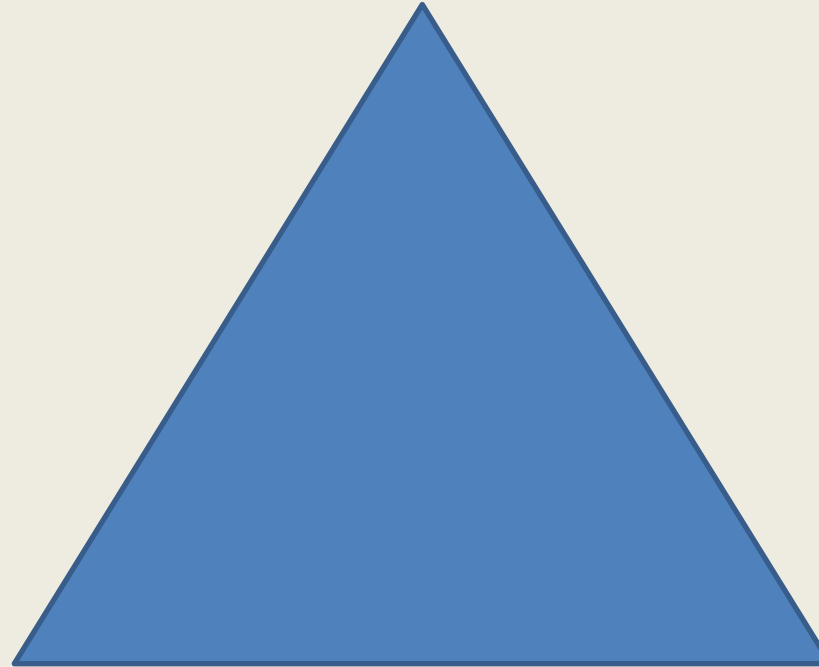
Fraud Risk Factors Help Determine Fraud Risks (Fraud Triangle)



**Opportunities
(Weak Controls)**

**Incentives and
Pressures**

**Attitudes and
Rationalization**



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Fraud Risk Factors-Misappropriation of Assets



Incentives/ Pressures	Opportunities	Attitudes/ Rationalization
Personal financial obligations create pressure to misappropriate assets	Presence of large amounts of cash on hand or inventory items	Disregard for the need to monitor or reduce risk of misappropriating
Adverse relationships between management and employees motive to misappropriate assets	Inadequate internal control over assets	Disregard for internal controls

Case Study: Federal Communications
Commission's (FCC)
Lifeline Program

**(See Handout “3c GAO Fraud Risk -
Martinez - Fraud Risk Management
Case Study”)**

Where Can You Get More Information About the Framework?

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<http://gao.gov/products/GAO-15-593SP>
- For questions about the Fraud Risk Management Framework, please contact: **Johana R. Ayers** at (202) 512-6722; AyersJ@gao.gov