

## **PERSONAL PURCHASES FRAUD**

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According to a 2004 commentary by ABC News' John Stossel, the General Accounting Office reported that government employees had used government credit cards to purchase computers, digital cameras, women's lingerie, jewelry, engagement rings, Elvis photos from Graceland, and escort services in New Jersey. Another government employee used government funds to buy his girl friend breast implants. He was forced to pay the money back, but other employees who bought themselves laptops, palm pilots and digital cameras did not. In June 2003, an inspector general discovered that Army government credit cards had been used to purchase Santa suits and Internet porn. An audit of the Defense Department revealed that it could not account for over \$1 *trillion* in expenditures, which costs each American about \$4,000 per year. The outrage generated by ABC's 20/20 "Give Me a Break" segment with John Stossel prompted the following response by Mitch Daniels of the Office of Management and Budget:

"Taxpayers should thank 20/20 for its look at credit card abuse at the Department of Defense. Your viewers should know that this problem extends well beyond the Pentagon, but that reform is under way. By the end of October, DOD alone will have cancelled 400,000 cards...Other agencies have begun calling in thousands more....We have commenced action to prosecute major offenders, garnish wages, and suspend security clearances when appropriate."

After the above statement was made, an audit of the Department of Agriculture revealed that employees used their government credit cards for personal purchases such as Ozzy Osbourne concert tickets, tattoos, lingerie, bartender school tuition, car payments and cash advances. The total cost to American taxpayers: \$5.8 million. During this time of year when we reflect upon the amount of taxes we pay to the government, it is instructive to know of the government's efforts—or lack thereof—to safeguard taxpayers' hard-earned money.

### ***The Problem***

Personal purchases fraud occurs when the fraudster purchases goods or services for personal use and then tricks his/her employer into paying for them. According to the 2004 National Fraud Survey, billing schemes—which include personal purchases fraud—cause victim companies median losses of about \$140,000. The most common ways to commit this fraud are:

- ***Submit invoices for personal purchases to accounts payable as business expenses.*** For example, one office manager brought her personal utility bills in to work and submitted them to accounts payable as business expenses. The company paid the bills.
- ***Charge personal expenses on company credit cards.*** For example, one company executive used the company credit card to purchase airline tickets for his family of six to go on vacation. The company then paid for the personal charges in full.

### ***Detection***

To avoid detection, the fraudster who submits invoices for personal purchases must either (1) be in a position to approve payment on the fraudulent invoices, or (2) falsify/alter the invoice documentation so that the purchases appear to be legitimate. However, if the authorized check signer has a reputation for not thoroughly examining the supporting documentation, the fraudster can avoid detection without doing either of these two things. The fraudster who charges personal expenses on company credit cards must either (1) be in a position to approve payment on the credit card bills, or (2) be confident that whoever is paying the credit card bills will not take the time to request and reconcile original receipts to each of the charges appearing on monthly credit card statements. Effective techniques for detecting personal purchases fraud include:

- Carefully examine supporting documentation for reasonableness and legitimacy. For example, make sure the address on a utility bill is the business address and not an employee's address.
- Examine the trend in expenditures and investigate all unexpected increases in expenditure accounts. For example, an unexpected increase in utility expense prompted an investigation that revealed that 24 checks had been issued during the year to pay the local power company, instead of the expected 12 checks.
- Request original receipts and reconcile them to each of the charges appearing on monthly credit card statements. Question the employee making the charge about any questionable charges that appear on the monthly statements.
- Monitor credit card use by employee and sort them from high to low. High credit card usage may indicate personal purchases fraud.

### ***Prevention***

To effectively prevent personal purchases fraud, an organization needs to implement a strong system of internal controls over cash disbursements. Ideally, the duties of approving payment on invoices and signing checks should be performed by different people. Most disbursement frauds—such as personal purchases fraud—are possible because of a lack of

diligence on the part of the authorized check signer. Too many check signers simply “rubber stamp” whatever is put in front of them, without bothering to examine the underlying documentation for reasonableness and legitimacy. In addition, all charges made on company credit cards need to be carefully monitored and reviewed for reasonableness and legitimacy. Employees making charges must be required to submit original receipts for all charges made on the company credit card. All charges without original receipts are presumed to be personal for which the employee in question must reimburse the company. Even though you may not suspect fraud, periodically question employees about credit card charges or supporting documents for invoices so that they know you are closely monitoring their activities. Such active monitoring creates a “perception of detection,” which is the most effective deterrent to fraudulent activity. Since even good internal controls can be circumvented by dishonest employees, the company should engage a certified fraud examiner to annually examine expenditures along with all of the supporting documentation, looking for anomalies.