



Stopping Internal Theft

With

Robert Burton, CPA, CFE

Moss Adams, LLC

Moderated by

Mike Bowers

Editorial Director, DealersEdge

Presented by DealersEdge



ROBERT L. BURTON, CPA, CFE - Moss Adams LLP, Dealer Services Group. Robert Burton has many years of experience providing a full range of financial and consulting services to over 200 dealership clients in over 15 states. Robert is also a Certified Fraud Examiner (CFE). He works exclusively with dealerships, from single-point to mega-dealers to public groups to manufacturers, in all areas of dealership accounting, tax, consulting and operations. Other experience includes internal controls analysis, buy/sell due diligence, fraud investigation and cash management. His industry experience includes:

- Dealership consulting, including financial, operational and internal controls engagements
- Dealership financial statements, including audits, reviews and compilations
- Dealership eSCORETM "dial-in" operational analysis engagements
- Dealership tax return preparation, including all entity formations
- Dealership accounting systems and procedures
- Merger and acquisition services, including due diligence
- Dealership fraud investigations, litigation support and fraud prevention training

Professional Affiliations And Certifications

- Certified Public Accountant, State of California and State of Washington
- Member, Orange County Automobile Dealers Association
- Member, Southland Motor Car Dealers Association
- Member, California Motor Car Dealers Association
- Board Member and Officer, Orange County Council of the Boy Scouts of America
- American Institute of Certified Public Accountants
- California Society of Certified Public Accountants
- Association of Certified Fraud Examiners



Detecting and Preventing Fraud in Dealerships

Robert Burton, CPA & Certified Fraud Examiner
Moss Adams LLP – Dealer Services Group

Moss Adams Dealer Services Group

- Serving over 450 dealerships nationwide, including:
 - Mega-dealers
 - Public groups
 - Manufacturers
 - Many single-point dealerships
- 11th Largest CPA Firm in the US
- Largest West Coast CPA Firm

Agenda

- Be Afraid – Most dealerships will get burned!
 - Potential Losses
 - Who are the Perps
 - Your Dealership
- Overall Solutions – Controls and Segregation
- Popular Dealership Fraud Examples / Solutions

Be Afraid! - Potential Cost

- About 85% of fraud = Checks (75%) & Cash (25%).
- Average scheme lasts 18 months before detected.
- Fraud committed by:
 - Employees (65%) average \$60,000
 - Managers (35%) average \$140,000
 - If conspiring, the average is \$200,000
- Average recovery = 20% of losses found
- 62% of inventory shrinkage is managers/supervisors.

Be Afraid! - Character

Employee Profile:

- Typical perpetrator is a first-timer – 88%!

On Average:

- 30% Honest
- 30% Dishonest
- 40% Potentially dishonest if conditions exist.

And dealerships are ripe with conditions!

Be Afraid! - Character

- MOST OFTEN A HIGHLY TRUSTED PERSON.
- Changes in financial situations.
- Excessive lifestyle.
- Drugs.

Ease of Opportunity Brings Rationalization

Never Forget Background Checks!

Got Insurance?

Be Afraid! - Environment

Where Fraud is More Likely:

- Poor Internal Controls
- Lack of Trust and Loyalty
- Lack of Ethical Standards
- Lack of Policies and Procedures

"Tone from the Top"

How Do We Catch Them?

How the Perps Get Caught:

- 40% – Getting a Tip from Empl, Vend, Cust
- 35% – External and Internal Audits
- 21% – By Accident
- 18% – Internal Controls

Internal Controls – A Necessity

Procedures to Protect Company Assets

- Accurate Financial Records
- Segregation of Duties
- Policies and Procedures
- Tone from the Top

Segregation of Duties

Employees that record transactions =

should NOT have access to company assets.

- Mail & Cashier / A/R Recording / Bank Deposits
- Check Signer / Bank Reconciliation Prep
- Closing ROs & Parts Tickets / Cashier Function
- Open POs / Accounts Payable Function
- Office employees paid on bottom line / Sched.

Where To Begin?

THE BIG FOUR!

- Bank Reconciliations
 - Every month, Timely and a Review Process
- Flooring Reconciliation
 - Every month, Timely and a Review Process
- Manufacturer Statement Reconciliation
 - Every month, Timely and a Review Process
- Parts Pad to G/L Reconciliation
 - Quick Rec. Monthly / Detailed Qtrly or Semi-Annual

Where To Begin?

Guard the MONEY!!

- Bank Statements and Cancelled Checks
 - Sent to Dealer's home for quick review:
 - No Signatures / Strange Payees / Credit Cards / Employees
 - Transfers Out / Wires Out / Unusual Debits
- Disbursement Controls
 - Always require two signatures and support
 - Positive Pay
- Mail Segregation – PO Box / Dealer opened / Check log

Company Credit Card Fraud

- Business office employee pays his/her personal credit card with company funds. Two authorized check signers were used.

- Potential losses greater than \$75,000

Company Credit Card - Solutions

- Run query of all payments to credit cards. Don't forget supply cards.
- Review cancelled checks monthly.
- Require statements with all checks.
- Keep a current vendor list for review.
- Statements mailed & initialed by holder

Cash Spiff Fraud

- Managers paid cash spiffs to sales people. Manager takes the money and falsifies vouchers (with or without collusion of the sales staff).

- Potential Losses = Significant over time.

Cash Spiffs – Solutions

- Require two signatures on all vouchers.
- Use petty cash drawer for voucher reimb.
- If not, post amounts given to Managers' A/R.
- Retain & cancel all spiff vouchers.
- Query journal entries to commission expense accounts.

Used Vehicles Fraud

- “Horse Trading”
 - Used car manager in collusion with wholesaler receives kickbacks
- Lack of ACV documentation in jackets
- Potential Losses = \$500/unit adds up fast!

Used Vehicles – Solutions

- Use Auctions / Use multiple wholesalers
- Analyze used units purchased and subsequently wholesaled by vendor
- Month-end analysis of wholesale journal
- Have dealer review all wholesale losses greater than \$X,XXX
- Use third party valuation of inventory
- Make sure all jackets have ACV & valuation

Parts Department Fraud

- Parts Department Stealing Cash
 - Voided Parts Tickets w/ Cash Drawers / eBay
- Parts Department Stealing Parts
 - Back door sales by changing PAD/price/costs
 - Usually Tires, Wheels, Stereos & Aftermkt
- Parts manager over-inflated parts inventory to increase gross profit

Parts Inventory - Solutions

- NO CASH DRAWERS IN PARTS DEPARTMENT
- Analyze user access to voiding tickets
- Voided document report by counterperson
- Manual pad adjustments – Parts Mgmt. Rpt.
- Missing document report
- Pending ticket report

Parts Inventory - Solutions

- Query user access to key functions
- Query journal entries to parts inventory
- Review parts exception reports
- Review the parts mgmt/spec reports
- Download parts pad and sort by ext value

Flooring Account Fraud

- Employee writes checks to self (or own bank) and offsets flooring. Based on in-transit balances or reconciling items, flooring appears reasonable.
- Potential losses > \$150,000

Flooring Account – Solutions

- Schedule Inventory & Flooring together
- Review system out-of-trust report
- Download inventory schedules and sort
- Review of flooring reconciliations
- Query manual journal entries to flooring

Work in Process Fraud

- Technicians are “ghost flagging.” Payroll is relying on service department to provide technician hours.
- Technician pay programs are inconsistent with repair order costing.
- Potential losses = Both small and large

Work in Process – Solutions

- Service Manager to match flags to ROs
- Business office to spot-check
- Post overstatements back to Service Gross
 - Service manager naturally follows up.
- Analyze manual journal entries to WIP account
- We query repair orders with labor losses.
- Review user access and costing setups.

Payroll Fraud

- Fictitious, or Ghost Employees
- Increasing Rates / Hours
- Carrying Old Employees
- Double payroll checks
- Falsifying additions to paychecks

Payroll Fraud – Solutions

- Manager to run/review payroll register
 - Segregate paycheck distribution
 - Scan for unusual issues
 - Follow-up on every unusual issue
 - Review overtime reports for reasonableness
- Signer to review stub information
- Review residual amounts in P/R accruals
- Require signed pay plans / labor board

False Vendors

- Employee sets up a false vendor or related party vendor.
- Payments for services and products are made to false vendor close in name to actual vendor:
 - S&T Tire vs. T&S Trim
 - Payments expensed to normal expense accounts.
- Potential losses = \$75,000 on up.....

False Vendors – Solutions

- Approved Vendor List for Check Signers
 - Creates controls, efficiencies, cost savings
- Determine who has electronic purchase order authorization access
- Query total vendor payments by vendor
- Review open purchase order listing

Computer Access

- Make password changes mandatory and periodic
- Print out/analyze access for all employees
- Understand segregation issues by dept.
 - i.e., Purchase Orders

Final Thoughts

- Inspect what you Expect
- Tone from the Top
- Get periodic professional help
 - A “new” set of eyes and ideas

MOSS ADAMS LLP



Thank you.

Robert Burton, CPA & Certified Fraud Examiner
Moss Adams LLP – Dealer Services Group