WHEN WAS THE LAST TIME YOU THOUGHT ABOUT FRAUD?

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Main Focus:

Martin Cloutier joined Mazars Canada in 2000. He was appointed Partner of the firm in 2005 and, since September 2018, is Managing Partner of Mazars' new office in Toronto. Over the last 25 years, he has acquired great expertise in audit serving a wide range of local and international organizations.

Martin manages and performs audit engagements as well as special engagements related to the effectiveness of internal controls, management and good governance for private and public companies under government regulations.

Moreover, Martin is a frequent lecturer for the Ordre des comptables professionnels agréés du Québec, and is the author of several articles on professional development. He has also acted as a voting member of the Audit and Assurance Standards Board of Canada (AASB) from 2009 to 2012. He continues to participate as an advisor to CPA Canada's specific technical committees.

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People — **+23,000 professionals**
Including +1,040 partners

Offices — **310 offices**
Throughout 89 countries and territories

Skills — **44% Audit**
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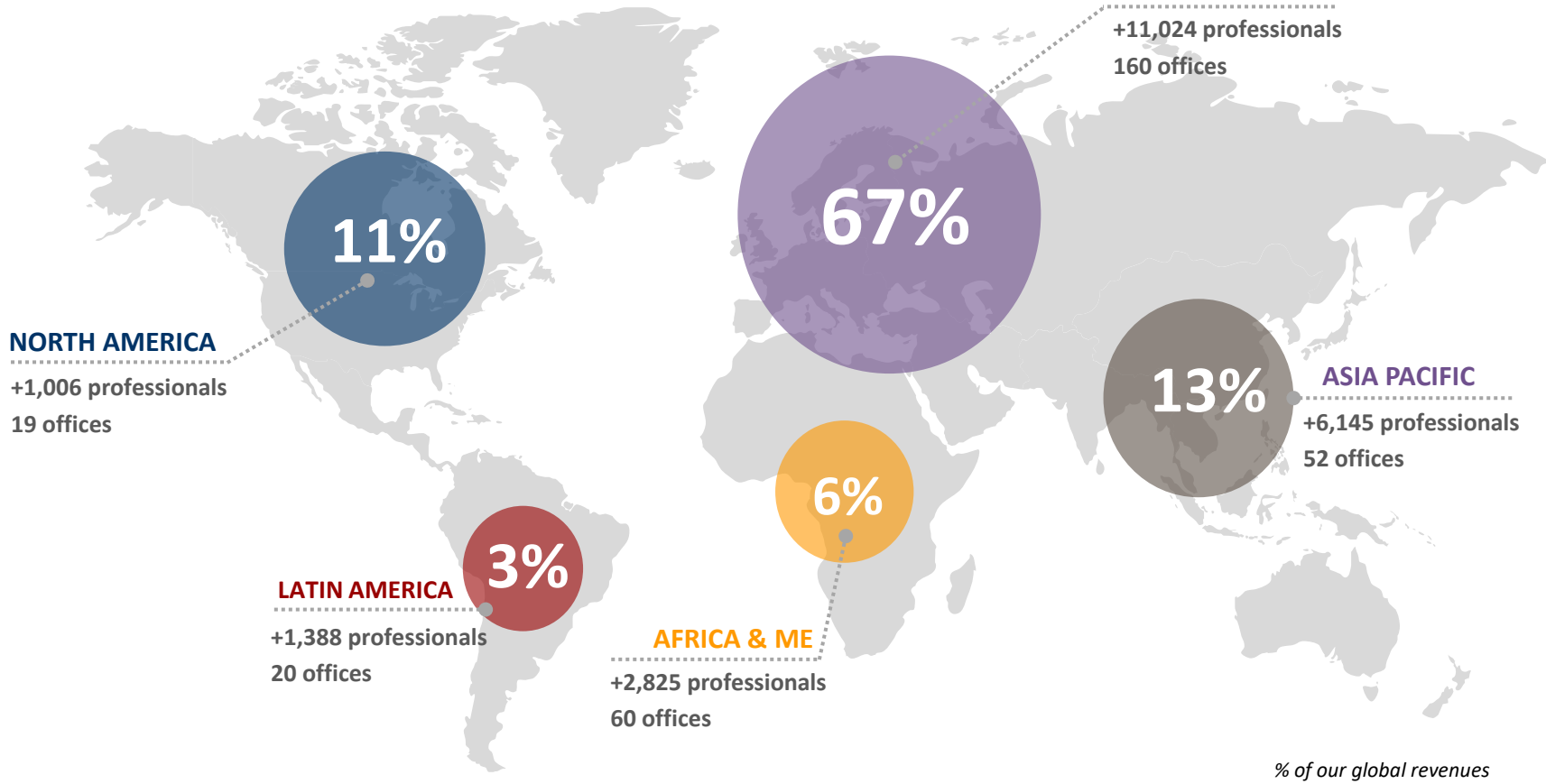

% of our global revenues

Mazars in Canada

Size — € 10m, +4% in 2016-2017
We assist SMEs, large private and public corporations, NPOs and individuals

People — +120 including 11 partners

Offices — First office opened more than 50 years ago. Today, 2 offices in Québec. **Our new office in Toronto has been inaugurated in September 2018**

Skills — 80% of revenues in Audit and Tax

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Tax Advisory

Provide tax and other services, from advisory to compliance

Consulting and Financial Advisory Services

Provide financial diagnosis for business operations, valuation and transmission, as well as support to improve the overall business performance

Accounting and Outsourcing

Provide financial and accounting management services

WHEN WAS THE LAST TIME YOU THOUGHT ABOUT FRAUD?

When was the last time you thought about fraud?

"Breaches were always happening but have become more visible and impacting everyone."

From Verizon, "*2018 Data Breach Investigations Report*"

How can we define fraud today?

"Fraud is the crime of gaining money or financial benefits by a trick or by lying."

"A fraud is something or someone that deceives people in a way that is illegal or dishonest."

Fraud triangle

Pressure
Justification of Dishonest Actions

Rationalization
Motivation or incentive to commit Fraud

Opportunity
The Knowledge and Ability to Carry Out Fraud

From The Fraud Triangle from Donald R. Cressey

What is the current context that increases the risk of fraud?

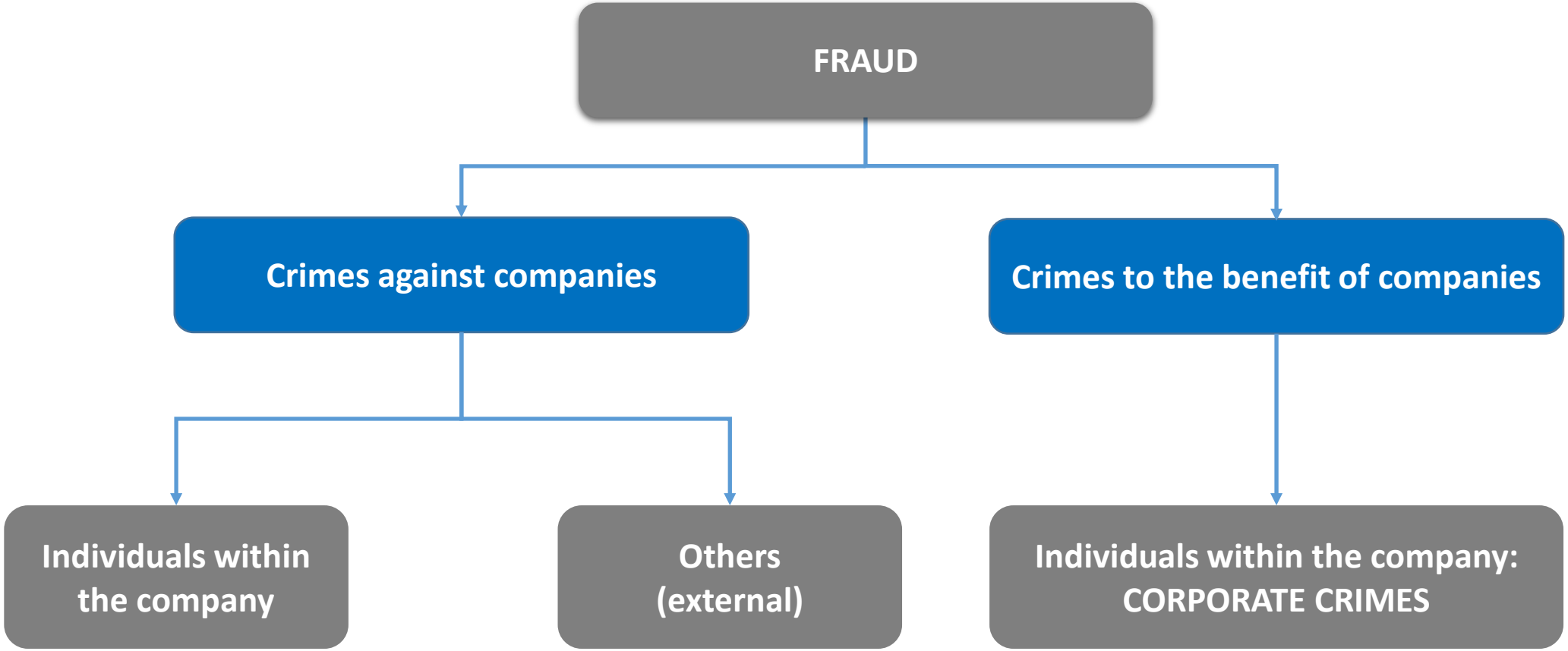
Interconnection and interdependence of activities

Quick change of environment and difficulty adapting

Cost hunting

Wider cyberspace

What kind of fraud can affect your company?



What kind of fraud can affect your company? (cont'd)

Year: *From 2007 to 2010; discovered in 2017*

Nature: *Undisclosed related-party transactions. Funnelled funds to entities controlled by the chief executive officer*

Consequences and Results: *Among stock holders of Sino-Forest was U.S. investment firm, Paulson & Co., which recorded a provision (loss) of* ***CA$660 million*** *in Sino-Forest Holding in 2011*

Year: *June 2017*

Nature: *Malware*

Consequences and Results: *More than 65 countries affected, including FedEx, Mondelez International, Merck. Damages caused by the attack are over* ***CA$13 billion***

Year: *From 2001 to 2011; the company and two subsidiaries were charged in 2015*

Nature: *Fraud and corruption*

Consequences and Results: *Allegations of bribes amounting to* ***CA$47.7 million*** *for the benefit of one or several public officials of Libya. A significant decrease in the stock value. The global loss remains unknown since legal procedures are still ongoing*

What do you know about cyberspace risks?

- ✓ In 2018, the global average **cost of a data breach is up 6.4%** and amounts to **$5 million**
  From IBM Report – 2018 Cost of a Data Breach Study
- ✓ **21,000**: Average number of identities exposed during cyberattack
- ✓ **66% of Canadians** say they are "very concerned" about the protection of their privacy

Main Areas of Risk	Possible Sources of Fraud
External (Cybercrime)	• Download of a fake antivirus by an employee • Storage of and accessibility to sensitive business data
Mobile Technology	• Allowance of mobile business technology for personal purpose • Mobile payment development • Data privacy protection
Personally-Owned Technology	• Employee-owned devices used for business purpose • Security and control procedures breaking with organization's security standards

On average, 4% of the targets in any given phishing campaign will click it

DarkHotel APT: A striking example of the threat since 2014

A new Facebook breach last week: more than 1.5 million users hit

68% of the breaches took months or longer to be discovered

Are you ready to face cyberspace risks?

Key Questions to Be Answered

- ✓ Do you have a **full understanding** of your organization?
- ✓ Do you know **where** and **what is the source** of your risks?
- ✓ Have you identified **how a breach** can affect your business?
- ✓ Do you have a full understanding of the cyberspace in which **you and your business partners** operate?
- ✓ Are your employees **aware and trained** regarding the risk of fraud?
- ✓ Have you identified the concerns of **your investors** about cybersecurity risk?

Possible Answers

IT strategy integrated in the global strategy of the company
Include **value management** and risk management
Strategy based on ISO/IEC 38500

Strong IT governance: Ensure the effectiveness of IT resources and prevent IT risks

Decide the **level of information** you should disclose regarding what is done against cyberspace risks

Segregation of Duties

Change Management Plan

Data Analytics

Data Protection

IT Governance Involved in Global Governance

Review of Manual Entries

Internal Policy and Procedures

Solution: Think Governance

The importance that the Board will give to fraud will have an impact on the company's culture (especially on the employees' behavior)

The Board can play a helpful role in the oversight of risk of fraud:

- ✓ Help the company to understand the level of risk that can be managed
- ✓ Test assumptions and fully debate them
- ✓ Recommend risk mitigation measures
- ✓ Ensure key performance indicators (KPIs) are suitable and can be used not only for business analysis but also for fraud detection

The implementation of a board is not dedicated only to big companies

Specific Committees can be used

- ✓ **Audit Committee** provides oversight of the financial reporting process, the audit process, the company's system of internal controls and compliance with laws and regulations.
- ✓ **Compensation and remuneration committees** defines the company strategy regarding compensation and remuneration, overview on the figures regarding the main remunerations.
- ✓ **Nominating and Governance committee** defines the board and company governance policies and practices.

Solution: Think Governance (cont'd)

Three levels of Board involvement depending on the risks or the circumstances threatening your organization

Level 1

When: Customary operational risks with potential adverse effect on business are moderate

=>Health, Environment, Safety

Level 2

When: High-impact risks cannot be adequately mitigated

=>Financial risk such as liquidity exposure or risk involving potential management bias

=>Strategic Risk

Level 3

When: Instances where management is clearly conflicted

=>Questioning of the performance, capability and suitability of the chief executive officer

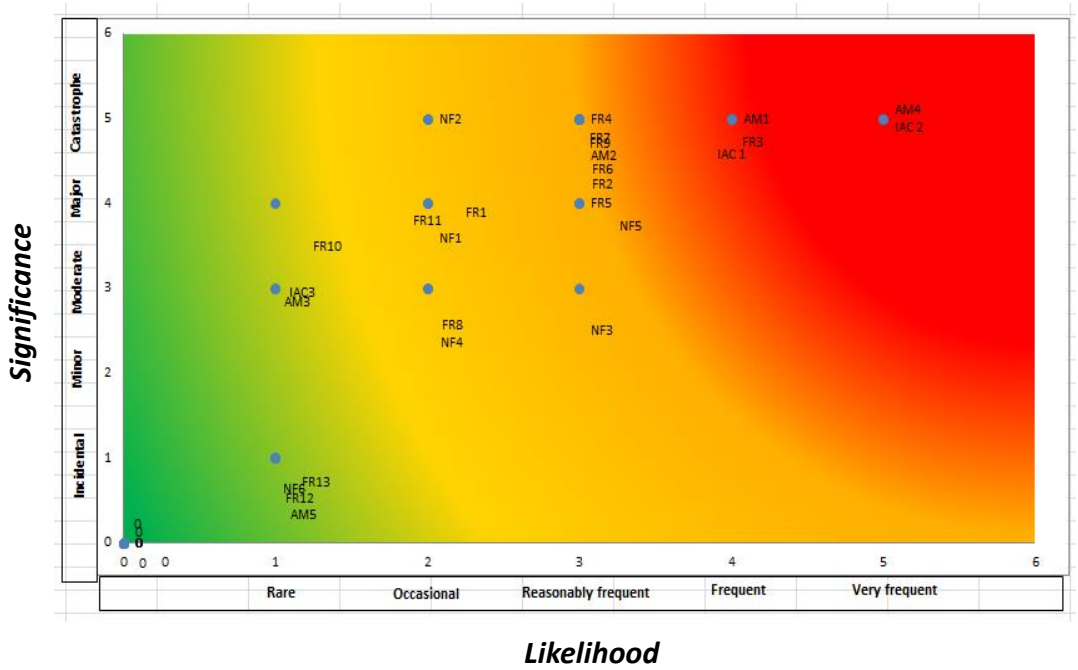
Solution: Use the Heat Map

Several tools are available to allow businesses to build their risk management strategy, including fraud risk prevention

Among them a simple tool available, prepared by the ACFE

- ✓ Establish a risk assessment scoring scale
- ✓ Elaborate a risk assessment matrix
- ✓ Put in place the control activity matrix
- ✓ Monitor actions

- ✓ Build your **Heat Map** according to the risk assessment matrix
  - ✓ Classify your fraud risk by likelihood
  - ✓ Classify your fraud risk by significance (severity)
  - ✓ Introduce other criteria as clock speed and the ability to mitigate risks



Useful Tools

- ✓ **ACFE website / fraud risk tool**
- ✓ **CPA Canada website**

Solution: Use the Heat Map (cont'd)

Example of Heat Map

- ✓ Severity of the risk
- ✓ Likelihood
- ✓ Risk clock speed
- ✓ Inability to mitigate

Risk Category	Severity	Likelihood	Risk Clockspeed	Inability to Mitigate
Strategic				
Failure to develop and execute a strategy	Very High	Moderate	Moderate	Moderate
Insufficient new customer revenue acquisition	High	Moderate	Fast	High
Failure to execute on a business model	Very high	Moderate	Moderate	Moderate
Failure to establish a viable low-cost manufacturing site	High	Moderate	Moderate	Moderate
Insufficient capital equipment replenishment	High	Moderate	Slow	Moderate
Possible opportunistic takeover bid at a depressed value	High	Low	Very Fast	High
Financial				
Failure to attain bank covenant level performance	Very High	Moderate	Very Fast	High
Failure to renew current loan facilities	Very High	Low	Very Fast	High
Change in lender and loan policies and practices	Very High	Moderate	Fast	High
Reliance on shorter-term debt to support growth	High	High	Fast	High
Insufficient availability under current loan arrangements	High	Moderate	Fast	Moderate

Solution: Internal Audit and KPIs

- **Internal audit** can help the organization to
  - ✓ Manage its risks, processes and controls impacting key strategic goals and objectives
  - ✓ Assist management in providing assurance over fraud and financial reporting controls
- **How to choose relevant KPIs:** Serve multiple purposes for different stakeholder groups and also for management to prevent and identify fraud

1	How reliable is the source? Did internal audit observe or detect the misconduct directly?
2	What additional validation (if any), or audit procedures, should be conducted by internal audit?
3	Should internal audit recommend that an investigation be required?
4	Does the behaviour contravene the organization's Code of Conduct?
5	What is the potential nature and depth of the misconduct?
6	What is the role of senior management (or even the board) in the activity (which determines whether IA should bypass management and communicate directly to board or external authorities)?

KPI Examples

	Key Performance Indicators (KPIs)			
	GAAP Financial Measures	Non-GAAP Financial Measures	Other Financial KPIs	Non-Financial/ Operational KPIs
Example	Earnings Per Share	Adjusted Earnings	Dollars of Order Backlog	Barrels of Oil Equivalent per Day
Description	a financial measure presented in the financial statements	a financial measure not presented in the financial statements, that is an adjustment to a GAAP financial measure*	a financial measure that is not a GAAP, or non-GAAP financial measure	a non-financial measure

KPI Characteristics

Relevance
Is the KPI a key metric in measuring the issuer's strategic and operational performance goals?

Transparency
Does the level of disclosure meet regulatory requirements and industry best practices (e.g., have GAAP measures been given equal or greater prominence than those of non-GAAP financial measures)?

Consistency
Is the KPI calculated in the same way as in prior reporting periods?

Comparability
Is the KPI prepared in accordance with industry standards and practices (if any)? Comparability allows stakeholders to evaluate the KPIs against those of peers.

Reliability
Has the KPI been accurately calculated, verified and subjected to internal controls?

Completeness
Do the KPIs present a balanced view of the entity's performance?

How to react when a fraud arises?

The best ways to deal with fraud, when it occurs, are mainly to

Act quickly internally

- Stop the hemorrhage
- Find the culprit
- Recover the losses: From the culprit, the insurance company or File a criminal complaint ?
- Form a multidisciplinary intervention team and protect company's assets and evidence

Involve a specialist

- To estimate the impact of fraud
- To assist you with the expertise and legal documentation

Others

- Contact your insurance company
- Implement a plan to ensure that the impact of fraud is fully identified and set up control activities to prevent recidivism
- Communicate at the right level: your Board, your auditors, any stakeholders that may have been be exposed

Valuation, Forensics and Litigation Support Services |Our expertise

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Our Expertise:

Our team offers an objective, efficient and rigorous approach with respect to any litigious or illegal matter in connection with investigations, risk management and legal disputes assistance. We also provide expertise in business valuation to support our Forensic and Investigation professionals in cases involving family or commercial litigation. We act actively and discreetly to protect your financial resources and your reputation.

Thank you!