Payroll Frauds

There are two major types of payroll fraud:

1. Ghost Employees (fictitious people on the payroll); and
2. False Claims (falsification of entitlements).

Ghost Employees

Most organizations have employees. At some point the number of employees will get so large that business owners will not know all of their employees by sight or name, and will not know what many of them do. This scheme counts on organization owners not knowing all of their employees and not recognizing a false name on the payroll.

A ghost is a fictitious employee added to the payroll. Wages or salary is paid to the ghost and is taken by the perpetrator. The scheme is usually done in large organizations, particularly when employees are spread over a number of separate geographic locations and where the payroll function is centrally controlled. This scheme is possible when the officer authorizing wage payments will not recognize the ghost's name on the payroll list. Or that officer could be the perpetrator. Hiding the fraud is not necessary as the payments are made and recorded as legitimate operational expenses.

The scheme is theoretically simple. By inserting a ghost into the payroll system, that ghost will be paid a wage, and the wage can be collected by the perpetrator. The following factors need to be considered.

1. The ghost must be added to the payroll system. This is easy if the perpetrator is in charge of the payroll section or has the function of adding new employees. One variation is to leave past employees on the system after they have left, and redirecting their wage payments.

2. Falsifying time sheets - This will not be necessary if the ghost is a salaried employee. Having to fill in time sheets or wages details on a regular basis adds another level of risk of detection to the scheme.

3. Making and collecting payments. The more automated the payroll system, the easier that the fraud will be run once it has been set up.

Creating a place for the salary to be paid may be difficult, especially if salaries are paid directly into bank accounts. Collecting cash is the easiest for the perpetrator as it is portable and untraceable, but not many types of employees are paid by cash anymore. If a cheque is issued or direct deposits are used, the perpetrator will have to create or use an account for the deposits, or cheques will have to be converted to the perpetrator.

Working around staff performance reviews and other reporting functions that are directly involved in the payroll function may be difficult. Generally ghosts are set up in roles

where performance reviews are not common and 'resign' after a while so that they do not become long standing employees.

False Payroll Claims

Payroll manipulation is common where pays are calculated on any sliding basis, whether time or piecemeal work. The most common example of this is employees clocking on early and clocking off late to increase the number of hours for which they are paid. The fraud does not need to be hidden as the payments are recorded as legitimate expenses.

Verification is often overlooked when more senior employees are submitting claims, when it is less likely that the claim will be questioned by a junior employee. The most common forms of the fraud are:

1. Falsifying time sheets to increase the hours 'worked'.
2. Have someone else clock you in and out when you are not there, or simply waiting around for some time before clocking off, to increase the recorded hours 'worked'.
3. Physically adjusting the time on the clock when you clock in and out.
4. Falsifying the type of work done to be paid a better rate on the different work.
5. Falsifying qualifications to be placed on a higher wage rate.

Prevention and Detection

Signs

- Employee files that have missing personnel file information
- A number of employees with the same mailing address, or using post boxes as mailing addresses.
- More than one employee using the same bank account for the deposit of wages.
- Similar employee names entering and leaving the system at about the same time.
- More than one employee's hours increasing for no apparent reason.
- More employees doing overtime for no apparent reason and with no apparent result.

Controls

- Do not make cash payments to employees. Cheques or direct deposits go into specific accounts and can be traced.
- Have a non-payroll supervisor approve payments to employees on at least a random basis.
- Have the addition and removal of employees approved and verified by a number of people.
- Ensure performance reviews occur for all persons that are listed on the payroll register.

- Having an independent person review time sheets (or their equivalent) on a regular basis.
- Rotate and separate responsibility for payroll functions from time to time.

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