Private Edge Knowledge Bank

Employee Infidelity – Supplier / Customer Collusion

CRIME

What do we mean by supplier / customer collusion in the context of employee infidelity?

These are frauds where there is collusion between a company's employee and one or more of it's suppliers / customers. This can occur in a number of ways.

A common example is where an employee colludes with a supplier to arrange payment of the supplier's invoices for work that has not been completed or goods that have not been received. The employee is typically sufficiently senior or trusted to authorise the payment of the invoice. The invoice is recorded in the company systems in the normal way and the company then pays the supplier without receiving anything in exchange. The supplier then typically pays a "kickback" to the employee.

Frauds involving customer collusion may involve instances where a portion of the company's income is paid directly to an employee in return for some sort of benefit given to the customer, for example granting a discount.

Are certain types of businesses vulnerable to this form of fraud?

Most businesses can fall victim to supplier collusion fraud. It is, however, generally easier for employees to collude with suppliers of services rather than goods.

This is because the receipt of goods into a business is generally more closely monitored than the supply of services. With respect to services, businesses often rely on employees confirming that a service has been received and this may be the same person who is responsible for liaising with the supplier to make the order.

As far as customer collusion is concerned, any business can potentially fall victim to this provided employees are in a position to manipulate the amount charged to customers for goods or services, Businesses which agree different prices with different customers, rather than selling their products or services for a fixed price are therefore more vulnerable.

How can this type of fraud be detected in a business?

This type of fraud is very difficult to identify. This is because the company is unlikely to be able to obtain any concrete evidence that their employee has received any benefit from the fraudulent transactions since the third party will likely pay the employee directly. Further, employees can maintain that they authorised supplier invoices in good faith and believed that the invoices were legitimate. As a consequence, supplier / customer collusion often comes to light by chance or through a whistleblower.

An awareness that this type of fraud exists, however, helps management remain sceptical and be mindful of possible exploitation of their systems and controls.

The monitoring of margins can also assist. Any instances of unexplained margin changes should be thoroughly researched. It should be noted, however, that where a fraud involves supplier collusion all increased costs will likely be evidenced by supplier invoices. A review of or reconciliation with the goods / services received would, therefore, be necessary.

All employees should also be encouraged to discuss any unusual behaviour in other employees. It may be that a fraudster's colleagues notice that something appears odd but that they do not voice their concerns.

This could be unusual / inappropriate relationships with suppliers / clients or possible indications of gambling problems that have motivated an employee to act dishonestly.

What steps can be taken to help prevent this type of fraud?

Although preventing this type of fraud is not straightforward, there are some controls that will assist.

A key area of control is ensuring that there is a segregation of duties and dual control. Ideally, supplier / customer contact should not solely be handled by one employee. Authorisation processes should not be completed by one individual alone and, if possible, individuals who are responsible for ordering goods / services should not also be responsible for confirming receipt of those goods/ services or for authorising the payment of associated invoices. The implementation of such controls can be assisted by an effective purchase order system that is integrated into the accounting system.

Further, it is much easier for employees to conduct this type of fraud if they operate autonomously and spend significant periods away from the office. Ways to ensure effective monitoring of such employees should be considered.

As far as client or customer collusion is concerned careful monitoring of any discounts which are agreed by a person not involved with the customer or the ordering process is recommended,

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