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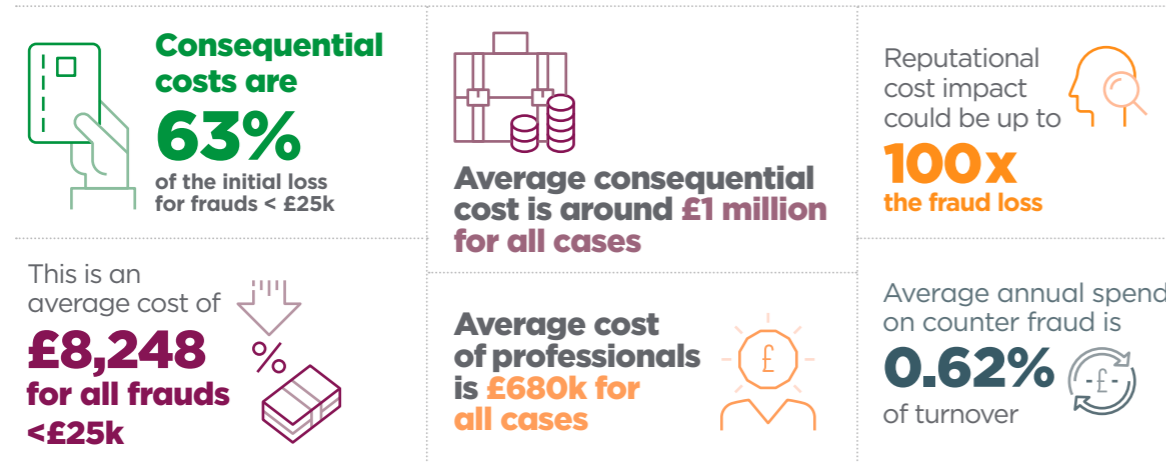


THE REAL COST OF EXTERNAL FRAUD

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EXECUTIVE SUMMARY



There are a wide variety of estimates of costs of fraud but most focus upon the fraud loss alone, failing to take into account the collateral damage and costs of dealing with it.

There have been two other studies looking at the wider costs and these focused upon internal fraud and recruitment fraud. This project plugs the gap by exploring external fraud.

Additional costs and damage associated with external fraud include: the cost of investigation, external justice costs, costs related to the suspension and replacement of internal staff, aftermath costs (e.g. reviewing and revising procedures), miscellaneous costs (e.g. regulatory sanctions) and intangible costs (e.g. reputation damage and lost business).

The researchers distributed an online survey through their networks and also sought interviews securing 39 usable cases.

The profile of the respondents was largely private sector with 23 responses, 8 from the charity, 7 public sector and 1 other.

Respondents were asked to comment on the largest fraud they were prepared to discuss, but some focused upon a particular case they had data on. Frauds ranged in size from 0 to £1.25 billion with the initial loss exceeding £100k for 22 of the participants.

Respondents were asked to identify the % of turnover spent on counter fraud. The average was 0.62%: the private sector average was 1.49% compared to 0.02% in the public sector and 0.4% in the charity sector.

The offender types were 14 customers, 12 suppliers, 10 professional fraudsters, 2 benefit claimants and 1 other.

The total cost of fraud is in many cases substantially higher than the initial fraud loss. These additional costs can be difficult to measure and very challenging to manage, e.g. the loss of business or charity funding as a result of reputational damage. Comparing the total cost impact of fraud with the initial fraud loss, the total cost is 33% higher for frauds under £25k and 997% higher for frauds in the £25k-£100k range. For frauds above £100k, the overall outcome cost is less than the initial loss. This indicates that organisations are rationally more likely to invest in recovering losses from offenders when the losses are in excess of £100k.

The results also show that the private sector is more effective at recovering costs than the charity and public sectors for frauds in excess of £25k. On the other hand, the public sector is more successful in dealing with the small frauds under £25k. A weak cost-benefit calculation means that the private sector tends not to seek recovery of small fraud losses. The justification in the public sector is stronger when the frauds involve routine transactions, traceable money flows and identifiable offenders, e.g. welfare benefit frauds.

If recoveries are excluded and just the costs of dealing with the fraud and its consequences are considered, the average additional costs are £8k for frauds under £25k; £584k for frauds in the £25k to £100k range; £100k for £100k to £1 million frauds; £2.4 million for frauds over £1 million. Given recoveries are never guaranteed, these figures provide an indicator of the costs involved in dealing with external fraud.

Comparing the data with the previous internal fraud cost studies, the average total cost of external frauds are lower than internal frauds - except in the high value, private sector cases. The higher cost associated with the internal frauds reflects organisations' motivations for investing in dealing with and removing internal problems. The high value private sector cases reflects the increased vulnerability of the private sector, especially the finance sector, to very high value external fraud.

The study also sought data on the types of justice pursued by the victim organisations. Criminal prosecution was the most common type of justice pursued by the participating organisations, accounting for 44% of all cases, followed by civil litigation (21%). No action was taken in 31% of cases.

INTRODUCTION

The cost of and extent of fraud is frequently reported in the media with a variety of organisations producing estimates of fraud based upon methodologies of varying quality. There are two factors that generally unite these estimates. The first is that they usually show fraud is a major problem and secondly they focus upon only the actual loss from the fraud. Estimates do not generally take into account the collateral damage fraud does to an organisation and the costs that are incurred in dealing with the consequences.

There have been very few studies that have sought to estimate the wider costs of dealing with fraud and its consequences. Two of these studies the authors were involved with. The first was a project that sought to investigate the real costs of internal fraud and the second was a study that explored the true costs of recruitment fraud (Button et al, 2013; and Gee et al, 2019). These two studies identified a variety of costs that organisations incur in dealing with fraud, such as the costs of investigation, staff suspension costs, internal disciplinary costs, justice costs, staff replacement costs, miscellaneous costs and intangible costs. These studies showed significant costs on top of the actual fraud loss.

The gap in the research to date, has been estimates of the real costs of external fraud. There are clear, practical differences between internal and external fraud. Firstly, victim organisations are usually able to identify internal fraudsters whereas external scammers are often unknown persons, e.g. account redirection fraudsters. Secondly, evidence against internal fraudsters is often more accessible. Thirdly, if the organisation is satisfied with dismissal or other disciplinary sanctions, the quality of evidence required is lower than that necessary for obtaining legal outcomes against external fraudsters.

This report addresses this gap by exploring the full costs of external fraud and compares them to the costs of internal fraud. This research was commissioned by Synectics Solutions and is the first study the authors are aware of to identify the full cost of external fraud. It is based upon 39 cases of external fraud from a diversity of organisations. The report begins by identifying the type of costs that are likely to be incurred in dealing with external fraud. It then moves on to explore the findings starting first with the demographic data of the sample before moving on to explore some of the costs identified from the research. Before we embark upon this, however, it is important to define external fraud:

A fraud primarily perpetrated by person(s) not directly employed by the organisation who is the victim. This could include: contractors, suppliers, customers and opportunistic and organised criminals targeting the organisation.

THE ADDITIONAL COSTS OF DEALING WITH FRAUD

Organisations respond to fraud in varying ways, all of which involve time, money and other resources to deal with the immediate impacts and longer term consequences. The types of responses have varying associated costs, but generally they involve the following types:

Costs of investigation

Once a fraud is discovered organisations want to determine basic questions such as who is responsible, how did it occur and how much was lost. This might involve the time of staff who have discovered it, line management, specialist investigative staff and frequently the use of professional contractors, e.g. investigators, accountants, lawyers, business consultants and IT specialists. Indeed the interviews revealed it was common for some organisations to go to a specialist contractor with a budget, such as £20k to £50k and ask them to discover as much as possible within that budget. These reports inform decisions about further actions and costs.

Justice costs

If organisations identify a culprit they may decide to pursue the perpetrator. This might include civil, regulatory or criminal options. Sometimes it involves a combination of these routes. In addition to the investigative costs, justice costs may include internal or contracted lawyers to help prepare and present the case at court. Management and other staff time may also be incurred in helping to prepare legal files for the purposes of the action.

Costs related to suspension and replacement of internal staff

Previous research showed that these Human Resources costs are significant in dealing with internal fraud. We assumed such costs would not be significant for external fraud. However, there were a number of cases where an external fraud exposed competency issues, which led to internal disciplinary sanctions, dismissal and recruitment for replacements. There were also cases where collusion involving internal staff was suspected but not provable. In these cases competence based disciplinary procedures were used to remove staff and recruit replacements. Such costs could include staff to cover suspended, sick or removed staff until a new appointment, the costs associated with the disciplinary processes and the costs of hiring and training new staff.

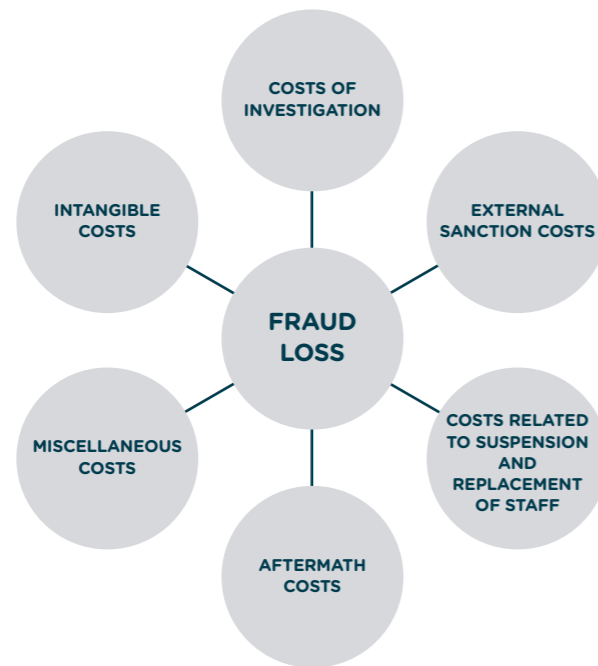
Aftermath costs

External fraud incidents are learning opportunities in that they expose inadequacies in an organisation's procedures and competences. Many organisations use their own staff and sometimes external contractors to review and improve their fraud resilience.

Intangible costs

There are a wide range of consequential costs that are very difficult to measure. Reputational impacts can lead to the loss of customers. The reputational impact for charities can be severe if it leads to a reduction in donor funds. Fraud incidents can also damage the morale of staff, especially if management are seen to avoid dealing with the problem, or conversely if employees are wrongly suspected of involvement. Staff may lose faith in management and the organisation's policies, so undermining their commitment, their performance and ultimately whether they remain with the organisation. Whilst robust estimates of these types of impact are not possible, it is important to recognise that they do apply in most cases, consequently the measurable costs do not reflect the totality of costs.

Figure 1. The real costs of external fraud



FINDINGS

The findings from the research will now be explored. The section will begin by examining the demographics of the respondents. However, in presenting these findings it is important to note the following issues.

Firstly, reflecting reputational concerns, organisations are generally very reluctant to disclose details of fraud incidents and how they deal with this sensitive issue. Although the organisations are victims, their victimhood can be seen as a symptom of failed management. Consequently securing inside data is very challenging. The research participants were only willing to discuss their experiences on the basis of anonymity and that no details would be published that would enable their re-identification. This limited the number of participants to 39, similar to the sample sizes in the previous research.

Secondly, the researchers sought extensive data from respondents. In the interviews that were conducted it was clear that the respondents were not in a position to offer accurate responses. In such cases either no cost or a minimal nominal cost was recorded. It is likely survey respondents took the same approach. As such the data should be considered as a conservative estimate.

Thirdly, respondents were asked to report on the largest external fraud they had experienced over the previous three years. These cases are therefore atypical in that they represent the participants' experiences of only their high value cases.

Profile of respondents

Details of the research were publicised through the researchers' and Synectics' networks. From the interviews and survey the team were able to extract 39 usable responses for the purposes of data analysis – some were excluded. The participants include three international organisations which were victims in overseas territories. Financial values were converted at the appropriate exchange rate.

The respondents were drawn from the following sectors:

- 23 responses from the private sector, with 11 of these from the financial services sector;
- 8 from charity sector;
- 7 from the 'public sector'; and
- 1 other.

The sizes of the participating organisations ranged from the small to the very large. There were 8 organisations in the sample with turnovers over £1 billion and 2 with less than £1 million. The largest group were 12 respondents in the £100 million to £500 million.

Table 1. Respondents by turnover

	Public	Charity	Private	Finance	Private other	All sectors
Less than £1 million	0	1	1	0	1	2
£1 million to £5 million	0	0	2	1	1	2
£5 million to £50 million	0	1	6	2	4	7
£50 million to £100 million	1	1	2	0	2	4
£100 million to £500 million	3	3	6	4	2	12
£500 million to £1 billion	2	0	2	2	0	4
More than £1 billion	1	2	5	3	2	8
Total	7	8	24	12	12	39

Categorised by the number of employees, there were two organisations with less than two employees and 1 with more than 100,000. The largest group were 10 respondents in the 101 to 1000 category.

Table 2. Respondents by number of employees

	Public	Charity	Private	Finance	Private other	All sectors
Less than 10	0	1	1	0	1	2
10 to 100	0	0	4	2	2	4
101 to 1,000	1	2	7	5	2	10
1,001 to 5,000	1	1	6	1	5	8
5,001 to 10,000	4	3	1	0	1	8
10,001 to 100,000	1	1	4	3	0	6
More than 100,000	0	0	1	0	1	1
Total	7	8	24	11	12	39

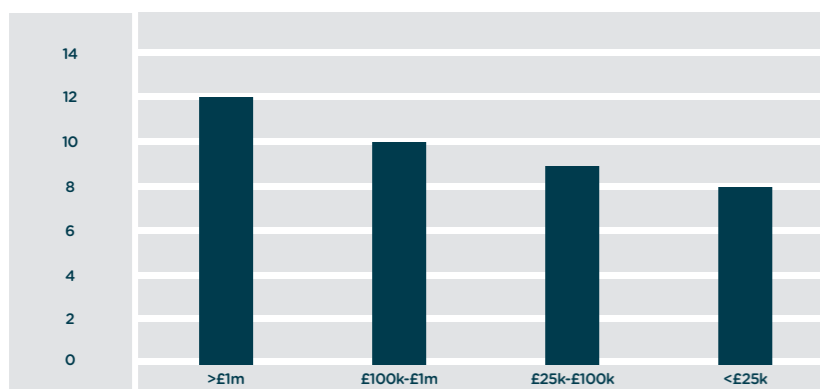
The research sought to determine the organisations' annual spend on counter fraud. The average in the sample was £821,795 per year or 0.62% of turnover. Given the spread in the sizes of the organisations sampled, the average figure is of limited use. One must also consider that some respondents would not accurately know the full costs because of the complexities of their organisations. However, the proportion of turnover spent on counter-fraud activities is relevant. At 0.62%, investment in counter-fraud is very small compared to other cost categories. The private sector participants (1.49%) spend proportionately far more than the charity (0.4%) and public sectors (0.02%). These figures are not generalizable but they do indicate a significant differential across the sectors.

Table 3. Annual expenditure on counter fraud

	Public	Charity	Private	Finance	Private other	All sectors
Number of Respondents	7	8	23	12	11	39
£ annual expenditure	50,000	481,250	1,210,870	1,808,333	559,091	821,795
% of turnover	0.02%	0.40%	1.49%	0.66%	1.16%	0.62%

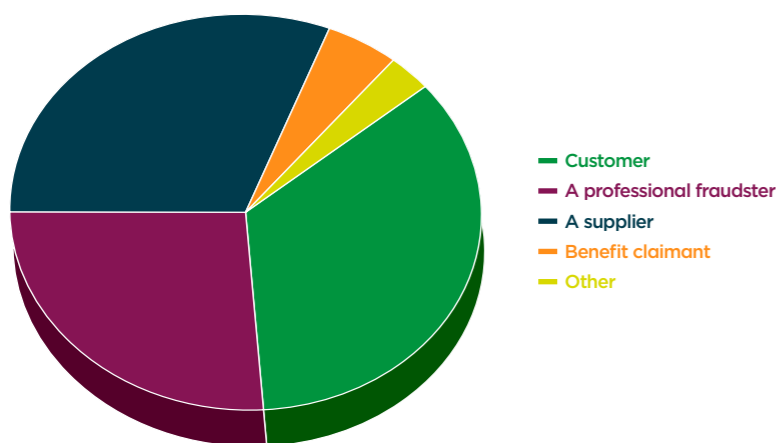
The distribution of fraud values is categorised in Figure 2. It represents the range of just the largest external frauds experienced by the participants over the last three years. Consequently it does not represent the average or typical fraud.

Figure 2. Respondent by size of initial fraud



As noted in the definition above, external fraud can be perpetrated by a range of actors. Figure 3 illustrates the breakdown of the fraudster types in the sample. Customers were the most common type with 14 responses, followed by supplier (12), professional fraudster (10), 2 were benefit claimants and 1 was other.

Figure 3. Types of external fraudsters in the sample



Costs of external fraud

The 39 cases range in size from an initial loss of £0 to £1.25 billion. There were 12 cases well over £1 million which distorts the overall average figures. For this reason, it is better to consider the costs in bands, hence the main analysis focuses upon cases under £25k, £25k to £100k, £100k to £1 million and £1 million plus. The tables below provide an analysis of the initial size of fraud and the industry sector where the fraud was committed. The private sector is further divided into financial sector and other private sector.

Average initial loss

The average initial loss before costs are presented in the table below. As noted above there is one large fraud that distorts the averages for > £1 million and more. The average loss for frauds under £25k was £13,159, for those £25k to £100k it was £56,778 and for £100k to a £1 million it was £417,100.

Table 4. Average initial loss

	Public	Charity	Private	Finance	Private other	All sectors
<£25k	11,858	22,200 ⁽¹⁾	11,875	12,500 ⁽¹⁾	11,667	13,159
£25k to £100k	39,500	81,250	35,667	40,000 ⁽¹⁾	33,500	56,778
£100k to £1m	120,000 ⁽¹⁾	200,000 ⁽¹⁾	427,889	487,500	475,250	417,100
>£1m	2,500,000 ⁽¹⁾	15,000,000	170,475,000	252,933,333	5,558,333	130,564,583
All frauds	390,654	3,818,400	64,095,021	126,633,542	1,556,500	40,296,469

⁽¹⁾ Single data points, not averages

Average total loss (initial fraud + costs - recoveries)

Table 5 provides the real picture in terms of the costs of fraud as it incorporates the initial fraud loss plus the consequential costs less any recoveries. When the table is compared to Table 4 above it shows that some organisations have been successful in reducing losses through some form of recovery. Nevertheless, the total cost of fraud is in many cases substantially higher than the initial fraud loss. The overall costs are expressed as a percentage increase over the initial fraud loss in Table 6: the negative figures indicate a reduction in the loss amount due to recovery.

Across all sectors, the real total cost of the fraud increases by 33% for frauds under £25k, and 997% for £25k-£100k frauds. Thereafter, the size of the total fraud actually diminishes for the frauds with the initial value in the £100k to £1 million and £1 million plus regions, which generally reflects the ability to recover monies. For frauds above £100k, the overall outcome cost is less than the initial loss. This indicates that organisations are rationally more likely to invest in recovering losses from offenders when the losses are in excess of £100k.

The results also show that the private sector is more effective at recovering costs than the charity and public sectors for frauds in excess of £25k. On the other hand, the public sector is more successful in dealing with the small frauds under £25k. A weak cost-benefit calculation means that the private sector tends not to seek recovery of small fraud losses. The justification in the public sector is stronger when the frauds involve routine transactions, traceable money flows and identifiable offenders, e.g. welfare benefit frauds.

Table 5. Average total cost (initial fraud + costs - recoveries)

	Public	Charity	Private	Finance	Private other	All sectors
<£25k	5,080	23,200 ⁽¹⁾	25,330	52,500 ⁽¹⁾	16,273	17,470
£25k to £100k	39,935	1,359,360	29,933	20,000 ⁽¹⁾	34,900	623,012
£100k to £1m	144,500 ⁽¹⁾	245,960 ⁽¹⁾	278,614	223,911	402,970	289,798
>£1m	2,588,080 ⁽¹⁾	15,074,750	131,911,776	194,408,863	6,917,600	101,661,963
All frauds	403,956	4,482,013	49,579,359	97,285,110	1,873,608	31,502,267

⁽¹⁾ Single data points, not averages

Table 6. Average total loss (initial fraud + costs – recoveries) as a percentage increase on initial loss

	Public	Charity	Private	Finance	Private other	All sectors
<£25k	-57%	105% ⁽¹⁾	113%	320% ⁽¹⁾	39%	33%
£25k to £100k	1%	1573%	-16%	-50% ⁽¹⁾	4%	997%
£100k to £1m	20% ⁽¹⁾	23% ⁽¹⁾	-35%	-54%	-15%	-31%
>£1m	4% ⁽¹⁾	0%	-23%	-23%	24%	-22%
All frauds	3%	17%	-23%	-23%	20%	-22%

⁽¹⁾ Single data points, not averages

Average consequential costs

Table 7 provides an indication of the wider costs of fraud, excluding any recoveries. The average additional cost is £8k for frauds under £25k; £584k for frauds in the £25k to £100k range; £100k for £100k to £1 million frauds; £2.4 million for frauds over £1 million. Given recoveries are never guaranteed, these figures provide an indicator of the costs involved in dealing with the consequences of external fraud.

The experience of one charity participant distorted the overall average (£584k) in the £25k to £100k category as it was one of the few responses to offer a significant estimate of intangible costs: a £50k purchasing fraud was reported in the media and it led to an estimated £5 million reduction in donations. Consequently, the average for the charity sector (£1.3 million) in the £25k-£100k category is far higher than the public (£8k) and private (£11k) sector. This charity example illustrates how an external fraud can lead to unpredictable and highly damaging consequences. In this case the beneficiaries of the charity's work were the ultimate victims.

For frauds in the £100k to £1 million the average organisational costs were just under £100k. This category is dominated by the private sector with an average cost of £102k. These costs include investment in reinforcing the resilience of the organisations' practices.

For frauds over £1 million the average additional costs were £2.4 million. This category is dominated by the private sector with an average cost of £3.3 million, principally directed to recovery of losses. The average finance sector cost is £4.2 million compared to the non-financial sector at £1.4 million. These higher values for the private sector, especially the finance sector, reflects its increased vulnerability to very high value frauds.

Table 7. Average consequential costs

	Public	Charity	Private	Finance	Private other	All sectors
<£25k	3,721	1,000 ⁽¹⁾	13,455	40,000 ⁽¹⁾	4,607	8,248
£25k to £100k	7,935	1,301,610	10,933	0 ⁽¹⁾	16,400	583,901
£100k to £1m	24,500 ⁽¹⁾	45,960 ⁽¹⁾	102,392	52,661	177,720	99,198
>£1m	88,080 ⁽¹⁾	74,750	3,286,776	4,208,863	1,442,600	2,484,880
All frauds	19,945	675,363	1,274,547	2,125,319	423,775	926,452

⁽¹⁾ Single data points, not averages

Table 8 presents the cost data as a percentage of the initial loss. It shows that the costs relative to the fraud loss are generally higher for lower value frauds. There are two drivers for this proportional imbalance. Firstly, the effort and resources required to investigate and address a small fraud can be similar to, or greater than a larger fraud. Secondly, consequential impacts can be disproportionate: the main component of the charity sector figure (1602%) is the £5 million loss in donor funding as a result of a £50k fraud, i.e. 100 x the initial loss.

Table 8. Average costs as a percentage of initial loss

	Public	Charity	Private	Finance	Private other	All sectors
<£25k	31%	5% ⁽¹⁾	113%	320% ⁽¹⁾	39%	63%
£25k to £100k	20%	1602%	31%	0% ⁽¹⁾	49%	1028%
£100k to £1m	20% ⁽¹⁾	23% ⁽¹⁾	24%	11%	37%	24%
>£1m	4% ⁽¹⁾	0%	2%	2%	26%	2%
All frauds	5%	18%	2%	2%	27%	2%

⁽¹⁾ Single data points, not averages

Case Study 1 - Charity sector supplier fraud

Charity X suspected fraud was occurring with a supplier in an overseas territory. Consultancy Y was hired to investigate. They uncovered a procurement fraud amounting to around \$200,000. There were suspicions of potential conflicts of interest with those awarding the contract, but nothing was provable. Evidence for a prosecution or any other sanctions was also insufficient. However, they did 'black-list' the supplier as a result of the investigation. The consultancy costs amounted to \$45,000. The charity had very little involvement in the case other than assessing initial allegations, hiring the consultancy, and acting on the report. That was estimated at 2 days of management time.

Consequential costs by category

Table 9 categorises the total costs for the whole 39 respondent sample. The most significant consequential costs are professional costs (£680k), followed by intangible costs (£218k) and management time dealing with the immediate repercussions of the fraud (£10k). The low average values associated with the remaining costs reflect the organisations' reliance on external professionals and the desire of many to limit their efforts to discovering the cause of their system failures. However, these additional costs can be very significant in specific cases.

For example, following a £3.4 million supplier fraud, a catering/hospitality firm spent a total of £170,000 across management time, purchasing and professional to develop a delivery and collection tracking system. Another participating organisation invested £80,000 in risk profiling database services only after suffering an £85,000 fraud. Organisations often only become aware of their vulnerabilities after a fraud has occurred.

Table 9. Costs of dealing with external fraud by cost category

Type of cost	Average amount
Professional costs dealing with the fraud	£680,068
Internal costs dealing with the fraud - management	£10,442
Costs dealing with aftermath of fraud - purchased services	£7,487
Costs dealing with aftermath of fraud - management	£4,248
Other	£5,512
Intangible costs	£217,948
Regulatory costs	£743
Overall average cost	£926,452

However, when the analysis is focused upon frauds under £25k this reveals a different distribution with the internal costs of management amounting to the most significant costs, followed by other costs (Table 11). This reflects the likelihood that smaller external frauds do not warrant investment in external consultants and advisers, consequently internal costs are proportionately higher.

Table 10. Costs of dealing with external fraud by cost category for frauds under £25k

Type of cost	Average amount
Professional costs dealing with the fraud	£1,250
Internal costs dealing with the fraud - management	£3,498
Costs dealing with aftermath of fraud - purchased services	£250
Costs dealing with aftermath of fraud - management	£125
Other	£3,125
Intangible costs	0
Regulatory costs	0

Generally respondents were happy with the services they received from professional services companies as the following table reveals, with very few responses rating it a waste of money.

Table 11. Were the external professional costs in dealing with the fraud worth it?

	<£25k	£25k-100k	£100k-1m	>£1m	All frauds	All sectors
Number of Respondents	8	9	10	12	39	2
4 - Very worth it	63%	22%	50%	67%	44%	2
3 - Somewhat worth it	13%	22%	20%	8%	13%	7
2 - Somewhat a waste of money	0%	11%	10%	0%	8%	4
1 - A complete waste of money	0%	0%	0%	0%	0%	12
0 - NA	25%	44%	20%	25%	36%	4
More than £1 billion	1	2	5	3	2	8
Total	7	8	24	12	12	39

Case Study 2 - Public sector welfare fraud

A woman claimed she had been forced to leave the family home due to domestic abuse and no longer had financial means. The woman could not claim state benefits because she had an immigration status of 'Not Recourse to Public Funds' (NRPF). Section 17, Children's Act 1989 sets a statutory duty on councils that a child cannot be left destitute. As such, the council was required to provide financial support to the woman and her children. Over a two-and-a-half-year period the council paid more than £43,000 in accommodation costs, financial allowance and utility bills to the woman.

Council officers, who visited the woman's property, became suspicious that the woman may be in receipt of additional income and an adult male was living in the house. A fraud investigation that lasted a total of 200 hours discovered that the woman was running an online business and her partner, whom she said she had left because of domestic violence, was living in the property and had done so since almost the beginning of the claim.

Social workers time were estimated at least 10 days, 1 day of their management time and 1 day of counter fraud management time. Sufficient evidence was obtained to substantiate a prosecution. However, the council were of the view that prosecution costs meant it was not in the public interest to follow this course of action. All council support for the woman stopped and the loss was categorised as a bad debt. Debt recovery proceedings are underway.

Comparisons to the costs of internal fraud

In this section some comparisons are made between the real cost of internal fraud and external fraud. This involves some slightly different calculations as the previous research used frauds under £25k, then all frauds under £100k, which included the under £25k frauds and so on. The comparison only includes the public and private sectors as there were insufficient charity sector respondents in the previous research.

Tables 12 and 13 show that the average total cost of external frauds are lower than internal frauds - except in the high value, private sector cases. This reflects organisations' motivations for investing in dealing with and removing internal problems. The high value private sector cases reflects the increased vulnerability of the private sector, especially the finance sector, to very high value external fraud.

Table 12. Average total loss (initial fraud + costs - recoveries) as % of initial loss compared between internal and external fraud in the public and private sectors

	Public External	Public Internal	Private External	Private Internal
<£25k	£5,080	£24,563	£25,330	£35,903
<£100k	£19,022	£65,559	£27,303	£47,344
<£1m	£39,935	£130,542	£168,665	£130,285
All frauds	£403,956	£414,337	£49,579,359	£548,321

Table 13. Percentage increase on mean initial loss to mean total cost (minus recoveries) in public and private sectors compared

	Public External	Public Internal	Private External	Private Internal
<£25k	-57%	420%	113%	227%
<£100k	-17%	204%	24%	75%
<£1m	2%	57%	-33%	38%
All frauds	3%	11%	-23%	15%

Case Study 3 - Private sector insurance fraud

Three individuals took out an insurance policy for a shop they were running and then blew it up several days later. The police were immediately suspicious of this and began investigating before we had even contacted them, in fact the insured never actually got around to making a claim. They were arrested shortly after and are now all serving life sentences.

Unusually the police in this case reported their suspicions to the targeted victim. As a result the £350,000 claim was not paid. Nevertheless the insurance company spent £42,564 with hired investigators and £4,480 on internal management costs to ensure it had a defensible position in refusing the claim. The overall cost impact was £47,044.

Justice routes

The research also sought data on the types of justice sought by the participants (Table 14). Criminal prosecution was the preferred option, accounting for 44% of all cases, followed by civil litigation (21%). No action was taken in 31% of cases. A key advantage of criminal prosecutions is that costs are far lower than civil litigation. Whilst it is unlikely that complaints actually lead to prosecutions, simply reporting incidents to the police supports organisations' internal policies and moral climate.

Table 14. Justice outcomes

	<£25k	£25k-100k	£100k-1m	>£1m	All frauds	All sectors
Number of Respondents	8	9	10	12	39	2
None	25%	22%	30%	42%	31%	2
Criminal	38%	56%	50%	33%	44%	7
Civil	13%	33%	20%	17%	21%	4
Disciplinary	13%	22%	20%	17%	18%	12
Regulatory	25%	11%	10%	0%	10%	4
Other	13%	22%	0%	8%	10%	8

CONCLUSION

This research has undertaken an analysis of the costs of dealing with external frauds based upon a sample of 39 cases. The nature of the data means that it is not generalisable, nevertheless it is an important source of research data as it represents the largest collection of research data on the costs of external fraud. Low level external frauds under £25k are dominated by management time costs, whilst frauds over £25k trigger substantial external expenditure for investigators, legal costs and other advisors. Comparing the data with the previous internal fraud cost studies, the average total cost of external frauds are lower than internal frauds - except in the high value, private sector cases. The higher cost associated with the internal frauds reflects organisations' motivations for investing in dealing with and removing internal problems.

The strong association of high value external fraud cases in the private sector reflect the increased vulnerability of the finance sector in particular to carefully planned, very high value fraud schemes. The additional costs associated with these high value external frauds are proportionally less than the costs associated with low value frauds. This is mainly due to the economic justification for investing in recovering high value losses. However, investing in recovery is a poor substitute for investing in robust defences. The best and most cost effective solution is to prevent the fraud in the first place.

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