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Five basic steps to effectively prevent fraud

By Salih Ahmed Islam, CIA, MBA

Fraud is a black hole for every company in the world. According to statistics, around 5% of companies' revenues go to fraud.^[1] This negatively affects companies' profits. Companies generally do not take precautions or preventive measures until they face fraud. Unquestionably, it is important to detect fraud, but ideally, companies should aspire to avert fraud before it happens. In other words, preventive medicine is preferred over performing an autopsy on a dead body. Essentially, we should make the fraudster's job very difficult. Companies and organizations should be on alert for fraud risks.

There are five basic steps and strategies for companies to prevent fraud.

Internal control system

The first thing companies must do is establish an internal control system to prevent and detect fraud. Internal control means "taking under control," not "checking." Control points should be placed in every business process of the company, which enables easier detection and prevention of fraudsters.

Internal control is also a managerial tool that significantly inflates the quality of management. Properly designed, internal control structures increase both efficiency and effectiveness in organizations. Examples of good practices include:

- Clarifying duties, authorities, and responsibilities
- Creating acceptance of ethics throughout the organization
- Increasing the quality of decision-making processes by producing data, information, and knowledge in a healthy and accurate manner, and by delivering the right information to the right people at the right time
- Reducing losses with effective risk management
- Protecting from legal risks and protecting reputation by full compliance with internal and external regulations

There are fundamental steps to take to establish a solid and tight internal control system:

- Ensure duties are segregated

- Identify the risks
- Develop policies and procedures
- Perform reconciliations regularly
- Review and approve processes and transactions
- Maintain adequate supporting documentation

If an organization has no internal control, it leaves that entity open to theft, embezzlement, and liability. If there are no internal operations controls, then there is no control over cash flow, profitability, sustainability, etc.

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