

Kids Central, Inc. System of Care Policy & Procedure

Series: Finance, Accounting and Contracts

Policy Name: Fraud Prevention

Policy Number: 905

Origination Date: 08/23/06

Revision Date:

Authority:

Policy:

In order to establish a method of identifying and assessing fraud risk and when possible, developing ways to reduce the risk the board of directors and management of Kids Central, Inc. accept the responsibility of designing and implementing effective systems and procedures for preventing, deterring and detecting fraud. These systems and procedures are formalized in this fraud risk policy. It is the intent of Kids Central to promote consistent organizational behavior by providing guidelines and assigning responsibility for assessing fraud risk, developing controls and conducting any necessary investigations.

Procedure:

A. Scope of Policy

This policy applies to any irregularity, suspected or real, involving employees and board members as well as consultants, vendors, providers, contractors, outside agencies and any other parties with a business relationship to Kids Central.

While irregularities do not in themselves prove fraudulent acts have occurred, they are often indicators that company policies are not being followed and therefore, all reported irregularities will be investigated. Any investigative activity required will be conducted without regard to the suspected wrongdoer's length of service, position, title or relationship to Kids Central.

B. Definition of Fraud

While no precise or standard definition of fraud exists, the term is used to describe such acts as deception, bribery, forgery, extortion, corruption, theft, conspiracy, embezzlement, misappropriation, false representation, concealment of material facts and collusion. In general, each of these acts involves depriving someone of something of value by deceit.

Kids Central considers fraudulent actions to include, but not be limited to:

1. Any dishonest or misleading act.

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2. Misappropriation of funds, supplies or other assets.
3. Impropriety in the handling or reporting of money or financial transactions.
4. Disclosing confidential and proprietary information to outside parties.
5. Providing inappropriate authorizations or forged authorizations.
6. Misrepresenting unfinished work as being completed.
7. Altering documentation, providing untruthful statements or withholding information during the investigation of a case or irregularity.
8. Seeking or accepting anything of material value from contractors, vendors or providers of services or materials to the company. Exception: gifts less than \$50 in value that have been reported to senior management.
9. Destruction, removal or inappropriate use of company records, furniture, fixtures and equipment; and/or
10. Any similar or related action.

C. Roles and Responsibilities in the Fraud Prevention Process

1. Board of Directors – this role is mainly that of fraud risk oversight, however this oversight also acts a fraud deterrent. Their responsibilities include:
 - a. Evaluating management’s identification of fraud risks, implementation of antifraud measures and creation of the appropriate “tone at the top” in regards to the ethical manner in which Kids Central conducts business and interacts with the community.
 - b. Reinforcing management’s commitment to creating a culture of “zero tolerance” for fraud.
 - c. Reviewing management’s level of fraud risk acceptance and the plan for managing fraud risk, for example, insurance policies, input from attorneys or other professionals, or special contract provisions.
2. Finance Committee – this role is also that of fraud risk oversight. Their responsibilities include:
 - a. Assessing management’s efforts to reduce fraud risk.
 - b. Reviewing investigations of irregularities and any actions that resulted from the investigations.
 - c. Assisting in the evaluation of the effectiveness of internal controls.
3. Independent Auditors – this group also addresses the oversight role by:
 - a. Assessing the fraud risk policy.
 - b. Discussing openly and candidly with the finance committee and board of directors on the risk assessment process and internal controls.

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4. Senior Management – this group fulfills the roles of fraud risk ownership, fraud risk tolerance and fraud risk management. For the purposes of this policy, senior management is defined as the Chief Executive Officer, Chief Financial Officer, Chief Operating Officer and Chief of Administrative Services. Their responsible for:
 - a. Accepting ownership and responsibility of all the fraud risks identified within the departments that report to them.
 - b. Determining the levels of fraud risk tolerance for different types of fraud risk.
 - c. Developing a plan to manage each type of fraud risk.
 - d. Communicating to their department managers their responsibilities to manage the fraud risks within their departments.
 - e. Creating a method to report fraud and irregularities.
 - f. Setting an ethical tone that includes an attitude of “zero tolerance” for fraud.
5. All Management – this group’s role is fraud risk assessment and anti-fraud controls implementation. These responsibilities are:
 - a. Assessing fraud risks within the company.
 - b. Providing input on the plan to manage fraud risk.
 - c. Implementing appropriate anti-fraud programs to reduced the identified fraud risks.
 - d. Evaluating the effectiveness of internal controls.
 - e. Building on senior management’s ethical tone.
6. Employees – this is the most important group, as employees are the first line of defense against fraud. To help prevent fraud employees need:
 - a. Written policies that explain the Kids Central’s ethics and “zero tolerance” for fraud.
 - b. Encouragement to report irregularities.
 - c. Communication from management that anti-fraud programs are not a matter of distrust of employees, but one of protection for employees and Kids Central.

D. Fraud Risk Assessment

Identify risk areas.

At least twice each fiscal year, the Kids Central management team will meet to identify and assess fraud risks that the company may encounter. However, if a manager becomes aware of a new risk or an increase in the level of a pre-existing risk, they will immediately report this to senior management rather than wait for the next fraud risk assessment meeting.

Each fraud risk assessment meeting will include discussion on the changes that have occurred at Kids Central since the previous assessment including changes to:

- The manner in which we conduct business.
- The organizations we conduct business with.
- The services we provide.

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- Our table of organization.
- Our system of internal controls.
- Our policies and procedures.
- Staffing levels and staff turnover.
- The reasons and manner in which our departments interact with each other.
- Regulations and oversight.
- The technology we use.

The team will then consider how these changes affect the components of fraud:

- Incentives and Pressures – have changes occurred that could increase someone’s perceived need to commit fraud?
- Opportunities – have changes made company assets more accessible for someone to misuse, or have any changes decreased our ability to prevent or detect fraud?
- Attitudes and Rationalizations – have changes occurred in the moral and ethical conduct of our employees or in our business partners’ perception of Kids Central that would make it easier for them to commit fraud?
- Any new fraud risks or change to pre-existing fraud risks will be noted.

Access Scale of Risk

Management will then determine the degree of each fraud risk based on two factors. First, the probability that each risk could result in a significant fraud loss will be considered. Risk with higher the probability of a loss will usually require a higher degree of response. Second, the impact of a potential fraud resulting from each risk will be gauged. Again, risk associated with higher impact will usually require a higher degree of response. However, these factors must be considered jointly. For example, a fraud risk may have a low probability of occurring, but a huge impact if it were to occur.

Allocate Responsibility for Risk

Following the risk assessment, senior management will meet and identify which members of the senior management team will take ownership of each fraud risk. The owner of each risk will be responsible for developing a plan to manage the risk. Options include changes to insurance policies, company procedures, internal controls, business practices, staff, vendors or business partners.

The senior management team will submit the fraud risk assessment and the fraud risk management plan to the board of directors for their approval. Once approved the senior management members will be responsible to communicate the fraud risk management plan to their department managers.

Identify Need for Revised Controls

The need for new or adjusted internal control procedures will be evaluated for each significant fraud risk that is identified. Two types of control procedures will be

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considered. First, process level controls will be examined and adjusted if necessary for fraud risks that involve a particular process. For example, fraud risk in the procurement process would require an evaluation of those controls. Are procurement duties adequately segregated? Are proper authorizations mandatory before placing an order? Would it be difficult for an individual to commit fraud by themselves without it being detected? If not the controls for the procurement process need to be improved.

Second, environment level controls will be examined and adjusted if necessary for fraud risk that exist throughout the organization and can be addressed by promoting ethical behavior, deterring wrongdoing and promoting two – way communication between staff and management. A strong sense of ethics and a written code of conduct are examples of controls that can create an environment that reduces fraud risk.

Implement Revised Controls

Any necessary changes in internal controls will be implemented as soon as possible. All affected staff will be given adequate training on the new controls as well as an explanation on the need for the procedure. The affected policies manuals will also be updated as soon as possible to reflect any changes.

On rare occasion, an internal control procedure may require a management override. This must be done only out of absolute necessity and be immediately reported to senior management. Frequent management overrides of control not only make the control ineffective, but also erode the control environment, by making it look to staff as though management does not take internal controls seriously.

Monitor Implementation of Controls

The senior management members that own the responsibility for fraud risks will monitor the progress of control implementation. They will report to the board of directors the progress or delays on implementing the controls. The risk owners will also be responsible for periodically verifying and documenting that the new controls are being utilized.

Evaluate Effectiveness of Controls

Kids Central management, the finance committee and the independent auditors will all assist in evaluating the effectiveness of internal controls. The effectiveness of the controls will be gauged on the control structure's ability to reduce fraud risk. Proof that the controls are being routinely utilized with low incidences of management overrides and reported irregularities indicate the controls are effective. Low utilization and evidence of irregularities or fraud are evidence that the controls are ineffective and need further adjusting.

The independent auditors will provide an object assessment of the internal control structure and this fraud risk policy. They will discuss these items directly to the finance committee and the board of directors. The independent auditors' comments and

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suggestions will be incorporated into Kids Central's internal control and fraud risk policies as the board of directors deems necessary.

Response to Fraud or Reported Irregularities

Kids Central, Inc. is committed to the highest possible standards of integrity, openness and accountability in all of its affairs. In line with that commitment, we strongly support our employees, business partners or members of the public to voice any concerns about observed irregularities or suspected fraud or corruption. Senior management will quickly ensure any reported concerns are adequately investigated. Senior management will also quickly inform the finance committee of any reported concerns and then report the results of the investigations to the committee.

Kids Central encourages our staff to raise concerns within the company rather than overlooking a problem or raising the concern first to the media or other external bodies. Employees should report any irregularities to their supervisor. If they are not comfortable discussing the irregularity with their supervisor, employees can report it to any member of the senior management team.

Members of the public who suspect fraud or corruption are encouraged to contact the Chief Executive Officer.

Kids Central recognizes that the decision to report a concern can be a difficult one to make. An individual may even fear reprisal from those responsible for the wrongdoing. In order to alleviate these concerns, the following safeguards will be used.

- The company will not tolerate any harassment or victimization and will take action to protect those who raise a concern in good faith.
- The company will do its best to protect an individual's identity when a concern is reported and the originator does not want their name disclosed. However, it must be understood that the investigation process may reveal the source of the information and a statement by the individual may be required as part of the evidence.
- The company encourages individuals to put their names to allegations. Concerns expressed anonymously are much less powerful, but they will be considered at the discretion of the company. In exercising this discretion, the company will consider factors such as, the seriousness of the issues raised, the credibility of the concern and the likelihood of confirming the allegation from attributable sources.
- If an allegation is made in good faith, but not confirmed by the investigation, no action will be taken against the originator. If however, an individual makes malicious or purely vindictive allegations, action may be considered against the individual making the allegation.
- Any investigative activity required will be conducted without regard to the suspected wrongdoer's length of service, position, title or relationship to Kids Central.

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Within 5 working days of a concern being received, a member of the senior management team will write to the complainant:

- Acknowledging the concern has been received.
- Indicating how it proposes to deal with the concern
- Giving an estimate of when a final response can be provided.
- Informing if any initial enquiries have been made.
- Explaining if further investigation will take place, and if not, why not.

All reported irregularities and concerns will be investigated by Kids Central. Concerns that have the potential for uncovering material levels of fraud may also be referred to the police. The company will also seek legal advice if a significant fraud is suspected.

If a significant loss has occurred due to fraud, Kids Central will also seek legal assistance about recovering the loss from the perpetrator. The company would normally expect to recover costs in addition to losses.

Review

This plan will be reviewed at least annually or after each use. Necessary changes will be submitted to the finance committee for approval.

Approved By:

Cynthia A. Schuler, Chief Executive Officer

Date