



Reduce Fraud with Strong Parts Inventory Management

Fraud continues to be a real threat for automobile dealerships with a likely target being a dealer's parts inventory. This is because a typical parts inventory contains products that can be easily converted into cash.

Often the frauds are small scale and difficult to detect. So, how do you know if fraud is being committed in your parts department? Short of catching the person in the act, or being tipped off by unusual circumstances, it is difficult to know for certain. There are, however, steps that can be taken to reduce the likelihood of fraud.

It is important to know what contributes to fraud. Three conditions must exist in order for it to occur: situational pressures, opportunity and rationalization. Combined, these make up what is known as the "fraud triangle," a need (usually financial), together with the chance to commit and hide a dishonest act (usually a theft), combined with a self-rationalization that the act is justified.

The best way to deter fraud is to remove elements of the triangle. For example, situational pressures and rationalization may exist; but if opportunity is removed or decreased, the likelihood of fraud will diminish.

To prevent actual fraud or possible fraud opportunities from arising, five actions - identified by the acronym CLEAR: Check, Lock, Enforce, Access and Record - are recommended. Consider the following basic measures for each action:

Check:

- Perform random "bin checks."
- Investigate unusual consumptions or shortages immediately.
- Routinely check outgoing freight, especially the parts department's delivery trucks. The quantity and type of parts being delivered must agree with the delivery tickets.
- Check incoming freight against bills of lading and packing slips. Record discrepancies and note any changes.
- Review purchase orders regularly. They should be filled out completely and include a corresponding work order or parts ticket.
- Perform a physical inventory annually.
- Check cash register balances regularly.
- Require customer's full name, address and telephone number for refunds issued against returns. Randomly call to verify that returns are legitimate.
- Check new employees' references and background.
- Spot check trash periodically to be sure saleable items are not being removed.

Lock:

- Securely lock entrances and exits after business hours.
- Require the parts department to have separate access from the rest of the dealership.
- Consider having a locked security area with limited access for valuable items.
- Store all inventory items in a locked or secured area after business hours.

Enforce:

- Inform all parts department employees of your security policy; emphasize that no exceptions are to be made.
- Require all parts department personnel to administer the policy.

Access:

- Limit access to parts department - employees only.
- Post signs indicating “no admittance” areas.
- Require employees from other departments to have clear authorization and to be accompanied by parts department personnel to enter the parts department.
- Rigidly control parts department keys.
- Install entrance locks unique to the parts department.
- Limit inventory file access to authorized parts department staff; change restricted computer passwords frequently.
- Use parts counters as adequate barriers with no open access.
- Design layout of bins to assure a clear view of access doors, including shipping and receiving areas.
- Install mirrors to monitor hidden areas.

Record:

- Document all parts leaving inventory.
- Maintain accurate records.
- Number counter tickets sequentially and account for them daily.
- Document parts on loan to the service department.
- Record “at no charge” on invoice if parts used by the owner are provided at no charge.
- Document returns to the manufacturer or supplier and check against any credits. A counter ticket can be used as documentation.
- Have only parts personnel charge parts against shop work orders.

Considering the potential losses, it is necessary that dealership owners make the prevention of fraud a priority in their businesses. The small investments that may have to be made to the facility and the time and effort of management to implement these safeguards are well worth the effort.

If you have any dealership management questions, please contact Paul McGovern at pmcgovern@downeycocpa.com.

Please visit our website at www.DowneyCoCPA.com.