

FRAUD INSIGHTS

# The psychology of fraud



*From huge financial accounting scandals, such as Enron and Lehman Brothers, to the robocalls from what seems like the Canada Revenue Agency trying to steal personal information, fraud is in the news almost every day.*

At Alberta Blue Cross®, our Claims Audit and Investigation Services department focuses on benefits fraud—when a person or group deliberately deceives the claims process for financial or personal gain. We also identify benefits abuse—when a person or group utilizes their benefits for services that they don't require, receives incentives to get a product or service, shares benefits with others or submits false claims.

All acts of fraud are illegal, and they cost Canadians hundreds of millions of dollars each year. More than that, they threaten the sustainability of benefit plans. Benefits fraud can be committed in one of three ways:



#### **By a service provider**

Providers who submit claims directly to Alberta Blue Cross may submit false claims, misrepresent ineligible benefits as eligible ones, or claim for a service that is more expensive than the one provided. This is the most common type of benefits fraud.



#### **By a plan member**

Members may submit false claims, forge receipts, share benefits with others, or misrepresent services.



#### **Through collusion**

Collusion occurs when multiple parties work together for mutual gain to exploit a benefit plan. For example, a service provider and plan member can work together to submit a false claim, then split the money they receive from the transaction.

We take an integrated and proactive approach to prevent, detect and respond to instances of fraud and plan abuse. To accomplish this, we need to understand both how a person can commit an act of fraud and what motivates them to do it.

There is a vast body of research in the field of criminology that identifies theories of why people engage in criminal behaviour, including fraud. The three major schools of criminology are biological, sociological and psychological.<sup>1</sup> Current research trends show that no single theory can explain criminal behaviour; therefore, researchers have begun to integrate theories in hopes of providing a more complete picture of why individuals break the law.<sup>2</sup>

#### **BIOLOGICAL THEORIES**

Early biological theories of crime focused on physical characteristics, such as the shape of criminal's skulls, their physical build or whether there were genetic predispositions towards crime. More current theories look at abnormalities in brain structure and function as well as biochemical explanations. These include the following:

- Underdevelopment or damage to the prefrontal cortex—the part of the brain responsible for reasoning and self-control.<sup>3</sup>
- Neurotransmitters in the brain that can affect behaviour. Low levels of serotonin can trigger aggressive behaviour and high levels of dopamine decreases emotional regulation and increases impulsivity.<sup>4</sup>
- Hormonal imbalances, including high levels of testosterone, which is related to aggression and violence.<sup>5</sup>

#### **SOCIOLOGICAL THEORIES**

There are multiple theories that examine the role of social and environmental factors that influence or drive individuals to commit crime. The social disorganization theory is the most studied of all sociological concepts. It argues that neighbourhood dynamics such as poor housing, poor health, socioeconomic disadvantages and transient populations influence crime rather than individuals.<sup>6</sup> Strain theories state that stressors such as the inability to reach goals, the loss of a positive stimulus or the addition of a negative stimulus increase the likelihood of crime.<sup>7</sup>





### PSYCHOLOGICAL THEORIES

There are three main psychological theories of crime. The first is psychodynamic theory, originated by Sigmund Freud, which states that an individual's early childhood experiences influence their likelihood for committing crime in the future. Criminal offenders are likely to have had a negligent or unhappy childhood and they are frustrated and aggravated by the events that occurred when they were children.<sup>8</sup>

The second theory is cognitive theory, which looks at how individuals solve problems. It states that people go through stages of moral judgment development and criminals remain in lower stages of this development. In addition, they make decisions using flawed cognitive thought processes based on violence or rejection in childhood.<sup>9</sup>

Finally, a large part of understanding criminal behaviour can be attributed to B. F. Skinner's behavioural theory.<sup>10</sup> By looking at people's actions, their behaviour can be altered using reinforcement and punishment. In other words, crimes are learned responses to situations.

### PSYCHOLOGICAL THEORIES AND FRAUD

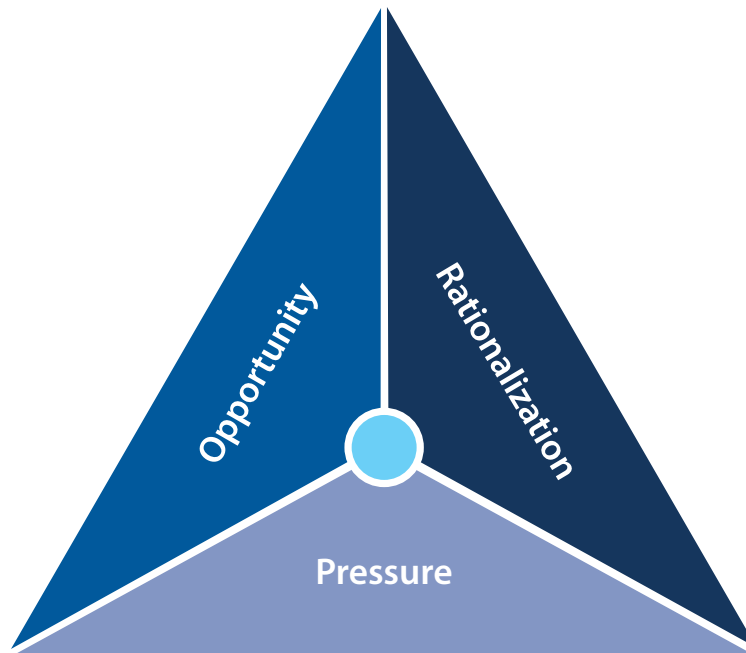
All three school of criminological thought have been applied by researchers and criminologists in criminal areas such as homicide, robbery and assault, but there has been a lack of application toward fraud offenders.<sup>11</sup>

In 1939, Edwin H. Sutherland published his social learning theory in *Principles of Criminology*. Social learning theory expands on B.F. Skinner's behavioural approach and contains nine points, which can be summarized as follows:

- Criminal behaviour is learned through interaction with other people, mostly within intimate personal groups.
- The criminal learning process includes techniques to commit crime as well as shaping of motives, rationalizations and attitudes.
- Criminal behaviour occurs when motives and drives are influenced more by favourable or pro-criminal definitions of legal codes that by conforming or non-criminal definitions.<sup>12</sup>

Sutherland continued his research by applying social learning theory to understand why people commit occupational fraud and abuse, or "white-collar crime", a term he coined in 1939. White-collar crime is defined as violations of law that involve the use of a person's position of economic power, trust or influence in legitimate organizations for the purpose of illegal gain or to commit an illegal act for personal or organizational gain.<sup>13</sup>

In the 1940s, a student of Sutherland's, Donald R. Cressey, began using social learning and behavioral theories to research the circumstances that led to employees embezzling money from their employers. This research led to the classic model of occupational fraud known as the Fraud Triangle.<sup>14</sup>



## THE FRAUD TRIANGLE

The fraud triangle model states that the following three elements are necessary for a person to commit fraud:

- pressure,
- rationalization, and
- opportunity.

At Alberta Blue Cross, we employ methods to address the fraud triangle to identify, detect, investigate and prevent benefits fraud.

### **Pressure**

This is what motivates a person to commit fraud and it generally relates to financial pressure that can be alleviated by the theft of cash. Examples of financial pressure can include personal or business financial problems, the desire for status symbols such as vacations, luxury cars or big houses or addictions such as drugs or gambling.

Other pressures that do not generally impact a person's motivation to commit benefits fraud specifically include unrealistic deadlines or performance goals set by the company they work for.

### **Rationalization**

Most people who commit fraud do not have any previous criminal record and they don't see themselves as criminals. They justify the fraud to make it seem acceptable to themselves. By finding reasons to excuse their behaviour, people remove their internal moral objections to committing fraud.<sup>15</sup>

Common rationalizations for benefits fraud include the following:

- "They're my benefits, so it's my money."
- "My employer is taking advantage of me and not compensating me fairly."
- "Everyone is doing it."
- "It's not really a crime."
- "I need to provide for my family."

### **Opportunity**

People who commit fraud are typically in a position of trust or power that provides them with the opportunity and capability to do so. They abuse their position to resolve their financial or other motivation and believe that there is little chance that their fraudulent acts will be discovered.

## **USING THE FRAUD TRIANGLE FOR FRAUD PREVENTION**

It can be difficult for organizations to address the pressure aspect of the fraud triangle, as they are usually factors outside the organization's control and differ for each person. Organizations can influence both the opportunity and rationalization arms as part of a strong anti-fraud program.

Organization can reduce the opportunity to commit fraud by limiting access to systems, implementing and enforcing effective internal controls and regular auditing. The use of data analytics and anomaly detection, business rules and automated red flags, like we use at Alberta Blue Cross, are the most effective anti-fraud technology measures.<sup>16</sup>

In addition, organizations can impact rationalization through fraud education. This includes what constitutes fraud, the impact that fraud can have on their benefit plans and the consequences to them personally if they get caught. Members often rationalize fraud as a low risk, high reward crime. Education efforts can provide a strong deterrent that counteracts a person's rationalizations.

Alberta Blue Cross uses an integrated fraud mitigation approach with five stages where we can minimize the opportunity for providers or members to commit fraud and the rationalization that providers and members may use.

### **1. Fraud awareness and education**

Alberta Blue Cross provides anti-fraud education to plan sponsors, members and providers through multiple channels. This education highlights our detection methods, as well as the consequences of fraud, including repayment of funds, loss of benefits plans, loss of employment, criminal charges or reporting to regulatory bodies.

### **2. Plan design and management**

We provide plan design and management expertise and recommend changes to reduce the risk of exploiting a benefit plan. This includes feedback from audits and investigations that identify trends in benefits fraud.

### **3. Proprietary claims adjudication system**

Alberta Blue Cross has a robust provider onboarding system as well as processes to delist providers who commit benefits fraud or abuse. In addition, we have real-time claims adjudication systems with hundreds of system edits that can stop inappropriate claims before they are paid.

### **4. Detection and predictive analytics**

Our analytics areas continuously monitor claims behaviours of providers, groups and members. They use advanced analytics and machine learning to identify high-risk claiming behaviour.

### **5. Audit and investigation**

Claims Audit and Investigation Services conducts risk-based claims verification, member and provider audits and investigations to identify fraudulent claims. We apply a zero-tolerance policy and take corrective actions including recovery of funds, reporting to the group plan sponsor, delisting a provider or making a criminal complaint.

Every person has a different set of circumstances and combination of pressure, rationalization and opportunity that leads them to commit fraud. Understanding these conditions allows Alberta Blue Cross to design fraud mitigation strategies that protect benefit plans.

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