

Dendro Resource Management, Inc.
*provides audit, security and consulting services
designed to raise the theft and fraud prevention stance of the timber industry.*



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About Us

With over 23 years' experience in the forest products industry, Dendro Resource Management, Inc. (DRM) is a leader in timber audit services. DRM is committed to supporting the integrity of the forest industry by providing independent analysis and recommendations regarding internal controls as well as actively detecting and documenting theft and fraud incidents. Customer programs can be tailored with your Company's needs in mind. With DRM you are guaranteed independence and confidentiality.

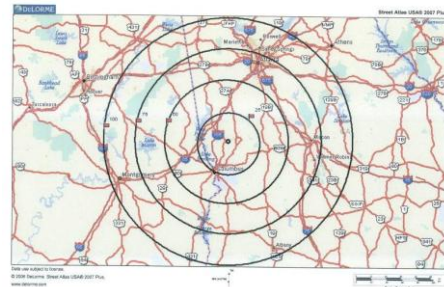
Zone Jumping: What is it and Should I Worry?



A recent case of zone jumping

occurred in the last few months and I thought we could take a few minutes to talk about zone jumping - an often over-looked window into fraud for the timber industry.

It is common for mills to utilize zone, county or other distance-based pricing structures to pay wood suppliers a higher delivered price as haul distance increases. Zone jumping occurs when loggers and truckers attempt to sweeten the price they receive by claiming to haul from a greater distance than is actually the case. They can claim a delivery is from one tract when in reality it came from a much closer distance. Pretty straight-forward, isn't it?



But loggers and truckers aren't the only ones to blame. Interestingly enough, zone jumping is also used by foresters and timber buyers to increase income for themselves and maybe for the logger. Sometimes kickbacks are involved, but not always.

Many people think this is a harmless thing that doesn't need attention. They just haven't done the math. An extra 10 cents per ton for a mill that purchases 3 million tons per

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year comes to \$300,000 in added wood costs. If not legitimate, it can have a significant impact on profits.

Sometimes, the solution is simple. By ensuring that there is a new contract for each tract instead of giving blanket approval for the logger to use the existing contract again and again is often all it takes to keep these costs in line. But sometimes, random and timely audits conducted by company employees or outside contractors are the best way to keep alert for unusual situations and red flags. If you are interested in knowing more about our audit services go to www.dendroresourcegmt.com or feel free to call us directly.

What are you doing about zone jumping in your company's timber security plan? Learn more about zone jumping prevention and detection strategies below. I've also included summaries of case studies to help you see how this is perpetrated and discovered and the potential impact of this easily overlooked fraud practice.

Aaron Gilland, DRM, Inc.

Zone Jumping Case Studies and Recommendations

As Gas Prices Rise, So Does the Chance of Fraud

In the latter half of the 20th century as gas prices began to rise, pulp mills created "zones" to facilitate common pricing points based on mileage to the mill. With the possibility of greater prices for hauling timber further distances came the added potential loss of paying those increased prices when distances aren't really involved. Even though some mills no longer pay by zone, they all base the delivered price on the mileage in one way or another.

Whether through laziness, purposeful efforts to give additional income or outright fraud, the losses may seem small but can be misleading.

Case 1. Earlier this year, a client of mine contracted with a

supplier on a tract containing 5000 tons of pine and 450 tons of hardwood located approximately 80 miles from the mill. The supplier was given a higher price to cover the extra transportation costs. When the managing forester checked the deliveries against the projected volume in the contract, he realized the tract had significantly overcut. This led him to visit the tract during normal working hours. He found the equipment was present on the tract but clearly the logging crew had not worked that day. However, when he checked the receipts for that day, the record showed that eight (8) loads had been reported as delivered. An additional six (6) loads were recorded the following day as well. He returned to the site a few days later and the equipment had not moved from the date the tract was first inspected. The next day, he stayed at the tract for three hours and no logging crew showed up, but the record indicated three (3) loads were delivered that day. Going back to the scale house, the forester waited for the supplier's trucks to return to the mill with a delivery. Then he followed the truck back to another tract approximately 40 miles from the mill. The company had no knowledge of this tract. It was determined that the supplier had defrauded the company on approximately 1600 tons for a total cost of around \$13,000.

Other cases of zone jumping

Case 2. An independent wood supplier in the Appalachians had requested and received a particular delivered price from a mill based on loads hauled from a distance of more than 100 miles. During the course of a conversation with another logger, the forester learned that the wood was actually hauled from a source that was less than 50 miles from the mill. The mill's procurement forester did business with scores of wood suppliers and had not visited this independent gate wood supplier recently. When confronted, the logger seemed to shrug off the security breach, justifying his behavior by citing an incident in the past where he felt he had made out poorly in a business dealing with the mill. The supplier was terminated and no specific amount of loss was identified or recovered. However, all other suppliers knew this company would take action and were placed on alert.

Case 3. A contractor owned a wood yard and operated

harvesting crews and was paid a premium for wood handled at the wood yard of around \$10 per ton. An audit conducted by following trucks from the mill back to the tract discovered that the trucks were hauling direct from the woods and telling the mill it came from the wood yard, netting the extra \$10 per ton for the contractor. When confronted, the contractor pleaded ignorance and said the truck drivers did that on their own. The company overpaid approximately \$80k to the contractor in this scheme.

Case 4. A pine sawmill was delivering hardwood pulpwood to Company X utilizing the company trucks which had a company logo on each truck (a 295 mile haul rate). An enterprising logger purchased a used truck from the pine sawmill that still had the company logo. Then the logger began harvesting wood from a tract 25 miles from the company and turning in the wood as being from the pine sawmill (295 miles away), capturing an enormous "bonus" for himself. This was noticed by a forester who saw the truck coming to the mill from the wrong direction. This led to a camera audit, restitution for the company and the logger was asked to vacate the salvage tract he was working.

Case 5. Company Y decided to conduct a zone jumping audit for the first time in over ten years. The audit was a surprise for the contractors and the company foresters. The audit was performed over a one week period using three different sampling methods. The results of the audit were 6% of deliveries for the week were "from the wrong zone." Basically 36 loads of 600 delivered were paid incorrectly. For the mill, that amount, extrapolated for a year, resulted in an estimated loss of \$250,000. Offending contractors were required to pay back the differences in zones. That action, and continued zone jumping audits have reduced the "wrong zone deliveries" to less than ½ of 1%.

Recommendations

1. Require all contractors provide location maps, descriptions and/or GPS coordinates for all tracts delivered to the mill.
2. Require all contractors notify mill personnel when

moving to new tracts. Then require new contracts for every price change or new tract. And have a system in place to collect old or expired delivery cards.

3. Conduct regular, unannounced audits on tract locations.

- Follow the empty truck back from the mill to verify the tract location.
- Visit the tract based on the contract data provided.
- Utilize GPS as a tool to verify tract locations.
- Possible use of Google Maps to verify tract locations using GPS coordinates.

4. Check weekly scale tickets or delivery information from each supplier to become aware of any locations that don't seem to make sense or that don't match wood procurement's expectations. Obtain truck ID's and monitor truck turn-around times.

5. Aggressively pursue any cases of zone jumping and terminate business agreements. If the violation appears willful and/or ongoing, consider bringing in a security consultant to gather evidence while the security breach continues, in preparation for legal action.