

THIEVES AMONG US

WHILE EMPLOYEE FRAUD IS A BUSINESS REALITY AND THE ECONOMIC COSTS ARE HIGH, A FEW PROTECTIVE STEPS CAN SERVE AS EFFECTIVE DETERRENTS.

by Don Dobesh

The robber, we'll call him Mark, drives up to the bank and finds a parking spot conveniently near the door. "Not busy for noon on Tuesday," he thinks. He takes his note, places his weapon in his pocket and calmly walks into the bank.

While this may seem like the start of a typical bank robbery, Mark was not there to rob the bank. He was there to rob his employer. His weapon was a ballpoint pen, and his note was a deposit slip.

Mark works as the controller for a small distribution company. The company operates with limited staff and, therefore, lacks many of the internal controls that would be present in larger organizations. Mark had taken a check payable to his company and deposited it into an account that he has recently established with a name similar to his employer's. To cover the missing payment, Mark has issued a credit memo for defective goods to clear the customer's account. Mark felt that he was underpaid and was envious of the owner's lifestyle. He justified his larceny as necessary to maintain his comfortable standard of living.

In its 2008 Report to the Nation on Occupational Fraud & Abuse, the Association of Certified Fraud Examiners estimates that U.S. organizations lose 7 percent of their annual revenues to fraud. The median loss to a small business with fewer than 100 employees was \$200,000.

The financial impact of fraud on a business goes far beyond the monetary value of the loss. The corresponding decreases to the bottom-line impact the working capital necessary for future growth as well. They also affect bank-funding criteria for the firm and its ability to repay debt, not to mention its profitability calculations should the owners contemplate sale or merger.

While fraud cannot be prevented with absolute certainty, it can be deterred. Even businesses with relatively small staffs can implement a few practices that will greatly reduce the likelihood that they will be victimized:

Tone at the top.

It is not likely that the staff will strive for high ethical standards if the owners

don't set a proper example in their dealings with customers, vendors and employees. Management should establish an objective business climate in which the employees perceive that the business values its reputation and demonstrates that on a daily basis.

Staffing.

It may seem obvious that companies should not hire employees who have stolen previously, but unfortunately, it often occurs. At minimum, references to prior employers should be contacted, and drug tests and criminal background checks should be conducted to eliminate potential problems.

Perception of detection.

Employees who perceive that they may be caught committing fraud will be less likely to attempt it. Employee training and related documents should include a section on ethics and the code of conduct for the business along with a statement of acceptance that each employee should sign.

Internal controls.

Even a small business can take steps to reduce the possibility of fraud. Mandatory vacations, cross-training and job rotation can almost always be initiated. The bank statements can be delivered to the owner's home if limited staffing requires that the same person who processes accounts payable also completes the bank reconciliation. Compare your operating results to industry standards and prepare ratio analysis and multi-year comparative financial statements to determine whether your operating results trend out of the norm.

Management oversight and communication.

Almost half of fraud schemes are

discovered by tips. Maintain an open-door policy and encourage employees to discuss their concerns. Take your staff to lunch occasionally, discuss the opportunities and challenges of the business and encourage their contribution.

The outside accountants.

Typical audit programs aren't designed to specifically look for fraud and misappropriations, and they certainly don't test every transaction. Often, the outside accountants provide only a compilation of the company's financial reports and prepare the tax returns. An occasional unscheduled visit by your auditor or a certified fraud examiner is a powerful deterrent to inappropriate activities.

While small, privately owned businesses may be vulnerable due to the reasons just outlined, public corporations, government agencies, nonprofit organizations and even religious organizations also are often victims.

The current economic business climate can be viewed as a sea of uncertainty. Business owners are continually challenged by customer demands, fluctuations in prices for goods and services, government regulations and their ability to attract and retain the best employees. Following the recommendations discussed in this article will help business owners assure that they have adopted ethical practices and controls and that they can appropriately focus their attention to steering their ship of state through this turbulent sea.

Don Dobesh is a Certified Fraud Examiner in Orlando and teaches forensic accounting and fraud examination as an adjunct instructor at the Keller Graduate School of Management in Orlando.

