

Issue #17
January 2012

GREAT AMERICAN and LOWERS & ASSOCIATES

Fidelity & Crime Observer

Keeping Up With The Joneses

Employees embezzle from their employers for various reasons. Sometimes a person gets behind on the bills due to medical emergencies. The employee rationalizes the theft as “borrowing” from the company. He intends to pay it back but never does. Disgruntled employees steal because they didn’t get the promotion or raise they felt they deserved. Others embezzle to support a vice, gambling, drug addiction, or extramarital affairs. Then there is a more basic reason — greed.

In this case, the embezzler was the highly regarded Regional Vice President of Marketing for a retail company with stores around the country. Let’s call her Samantha Owens. As head of marketing in her region, Ms. Owens had broad discretion over a substantial marketing budget. Ms. Owens routinely submitted bills to accounts payable for payment however because she was the boss, questions were never asked.

The company never suspected Ms. Owens of any wrongdoing until they received an anonymous letter from a whistle blower claiming Ms. Owens was paying bogus entities that performed no services to the company. The company pulled all invoices from the suspected entities. There were no phone numbers or street addresses on the bills. Further investigation disclosed Ms. Owens owned these bogus companies. When confronted she admitted to embezzling “maybe \$200,000.” The final forensic analysis disclosed she issued payments totaling \$3 million over an eight year period to her companies.

How did Ms. Owens get away with the thefts for so long? First, she was always thought of as a trustworthy employee. She had a family, lived in a nice neighborhood, was active in her community, and appeared to be living the American dream. No one ever suspected she would embezzle from the company. Plus, as head of the region, no one under her ever questioned any of her payment requests. Unfortunately, the company did not have a vendor program in place. There was no list of approved vendors. They did not confirm the validity of entities doing busy with them. Even in the absence of an approved vendor list, there was no periodic checking of vendors. Had someone pulled one of the bogus invoices, it would have been readily apparent that the company was a sham. And what about the whistle blower? The company suspects it was an employee who became suspicious of the invoices but was afraid to come forward.

So what was her motivation for stealing? Gambling? Drugs? Boyfriend? None of the above. For Ms. Owens it was greed. She wanted the nice house with the swimming pool and hot tub, luxury cars, the waterfront condo in Florida, a 34 foot boat, jewelry, and vacations. Her children had to attend the best private schools. And then there was the country club membership. Unlike some embezzlers who lose their ill gotten gains on the black jack tables in Las Vegas, Ms. Owens actually had something to show for her misdeeds. However, in the end, her assets were not enough to cover the amount of the loss, much less account for the wrecking of her reputation and family. Hers is yet another example that crime doesn’t pay.

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In Tough Economy, Employee Theft Climbs To 'Epidemic Proportions,' Experts Say

Evidence against a young bookkeeper was in the photos she brought to work — her frequent Vegas trips, the \$1,000 exotic puppy, and \$18,000 in house renovations.

She didn't need photographic proof of her sudden breast augmentation surgery. All on a \$20,000 annual salary.

Finally, her boss became suspicious when she bought a Mercedes — with cash. "This woman did everything but come to work with a sign on her back saying, 'I'm stealing your money,'" said James Ratley, president and CEO of the Association of Certified Fraud Examiners, an Austin, TX based organization with more than 50,000 members worldwide.

Not every dishonest employee, of course, flaunts his or her clandestine wealth as much as the young bookkeeper. Ratley said fraud by employees is more widespread than most employers realize.

It is difficult to gauge the losses, but a survey of fraud examiners estimates that businesses lose as much as 5 percent of their revenues to various forms of fraud by employees, from bookkeepers to CEOs. **A survey by the National Retail Federation put employee fraud ahead of shoplifting as the primary cause for retailers' losses.**

"Fraud has grown to epidemic proportions," Ratley said. "It is so pervasive, it can no longer be ignored."

Ratley doesn't have to search his files for examples.

Consider just a few of the frauds that made news in Austin, TX: A couple discovers that their bookkeeper of three decades has stolen \$1 million from them when they go to sell their company and retire. A banker underwrites his NASCAR racing team with almost \$1 million in phony loans to friends and relatives. A national charity employee steals almost \$600,000 by inflating invoices for cell phones and selling the devices on the Internet.

But headlines are the exception, not the rule, for fraud by employees.

Fraud A 'Loss Leader'

Ratley said occupational fraud is difficult to prosecute because the risk of punishment is low and managers — concerned about the company's image or their incompetence in preventing the fraud — often prefer to deal with the crime quietly.

Fraud is a problem for businesses of all sizes, but firms with fewer than 100 employees are twice as likely to be victimized, according to the fraud examiners' survey.

"Fraud is a loss leader for a lot of small companies," said Bob Stocker, a founder of Bookkeeping Express, a national company with 33 franchises, including one in Austin.

Too often small firms have the same person writing checks, doing the billing, and reconciling the books each month.

The owner is focused on sales or managing the staff or, in the case of a professional, practicing law or medicine, without focusing on the books.

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Employee theft has reached an all-time high with over \$40 billion lost per year.

According to statistics, 33% of business bankruptcies are directly related to employee theft.



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In Tough Economy, Employee Theft Climbs To 'Epidemic Proportions,' Experts Say

"Doctors, dentists, and lawyers make excellent fraud victims," Ratley said. If the firm is large enough, the duties of writing checks, billing, and reconciling the books should be split among employees, experts say. If that's not practical, an outside bookkeeper can be hired to reconcile the books each month.

"It's not that expensive," Stocker said. "It takes us a couple of hours, maybe \$200 a month."

At a minimum, Stocker said, credit card and bank statements, preferably with check images, should be sent unopened to the owner, not an employee. "And really look at them," Stocker said. "Any credit charges they don't recognize, call the credit card company and get the backup information."

Audits Aren't Enough

Ratley said an employer shouldn't assume that the company's annual audit protects the firm from fraud. Audits, he said, are just a sampling of a company's finances to give a picture of the firm's financial health, not a thorough search for fraud.

"Audits only uncover 13 percent of frauds," Ratley said. Tipsters, whether co-workers, vendors, or competitors, expose 40 percent of the frauds, according to the fraud examiners' report.

For that reason, Ratley recommends a hotline for reporting suspicious activity.

Who Steals From An Employer?

"Most fraud perpetrators are trusted and well-liked," Ratley said. "The more trust an owner puts in their employees, the greater the opportunity for them to cross the line." A picture of perpetrators emerges from the survey of fraud examiners and Ratley's interviews of suspects.

"Bad people are supposed to look a certain way," Ratley said. "They don't." Most of them had never stolen previously from their employer. Their stories usually share three traits: opportunity, financial need, and the ability to rationalize.

Among the common rationalizations: "I'm just borrowing this money. I've worked here a long time. They passed over me for a promotion. The company doesn't care about me."

In some instances, the employee may repay the money the first couple of times they steal it. Eventually, they become accustomed to the extra cash and can't stop.

"People don't intend to steal as much as they did," Ratley said. "Often they don't even know how much they stole." And they are surprised when they get caught. "Most of them get caught," Stocker said. "The question is, how long they get to do it."

According to the survey of fraud examiners, schemes last a median of 18 months and the median loss is \$160,000. But nearly a fourth of the frauds involved losses approaching \$1 million.

Bad Times Expose Fraud

A sluggish economy exposes many schemes.

The majority of employee theft goes undetected by supervisors and management for a substantial period of time.



Opportunity remains the leading cause of employee theft.

Employee theft is prevalent in every type of business.

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"When the economy is good, there is more money flowing. You've got more business coming in, so you are more likely to hand off the bookkeeping," Stocker said. "There's more money in the checking account. Your costs are going up with revenue, so you don't notice the higher (fraud) costs." When money gets tight, however, it becomes harder to conceal the fraud. Once the fraud is exposed, the issue becomes trying to recoup the losses. "Catching them is one thing," Stocker said. "Getting your money back is another." Ratley agrees.

In some instances, the dishonest employee has bought houses or cars or boats that can be sold. Often, there is little to show for the crime. "People do not steal money to save it," Ratley said. "They steal it to replace money already spent."

Tips For Preventing or Detecting Employee Theft

- ⇒ **Separate** bookkeeping, billing, and account reconciliation functions.
- ⇒ **Company owners** should receive bank and credit card statements.
- ⇒ Establish a **hotline** for receiving tips of suspicious activity.
- ⇒ **Educate** employees on the cost of fraud to the company.
- ⇒ **Encourage** co-workers to report fraud.
- ⇒ **Create a climate** of honesty and integrity.
- ⇒ Use continuous **auditing software**.
- ⇒ **Rotate** sensitive jobs.
- ⇒ Use **background checks** in hiring.



Sources:
 Association of Certified Fraud Examiners
 Laylan Copelin, American-Statesman Staff

Employee Theft Statistics

- The FBI calls employee theft one of the **fastest growing crimes** in America.
- Nearly **one-third of all employees** commit some degree of employee theft, according to the U.S Department of Justice.
- The U.S Chamber of Commerce estimates that employee theft costs businesses **\$40 billion each year** — ten times the value of street crime losses annually in the U.S.
- The Chamber also reports that **one of every three business failures** is the direct result of employee theft.
- The **banking industry** reports losses of **over one billion dollars annually** due to employee theft, greater than the amount taken in bank robberies many times over.
- Recent reports have found that employee theft is increasing at a rate of **15% annually**.
- Government research has found that **every family** pays an estimated **three hundred dollars** each year to subsidize business losses due to employee theft.

For more information about Lowers & Associates and any of the risk mitigation services that we offer, please visit our website at www.lowersrisk.com or give us a call today!