Employee theft

Are the wrong hands in your cookie jar? **Interviewed by Marcia Passos Duffy**

Your home telephone rings on a Saturday morning. It's your CFO. She says the external auditors have detected a problem: Your comptroller of 10 years who earns a six-figure salary has been stealing from the company. During the past six years, he has skimmed more than $500,000 by intercepting receivables, forging checks and falsifying financial reports.

If you think this nightmarish scenario will never happen at your company, think again, says Reed Archambault, an attorney with Newmeyer & Dillion LLP in Newport Beach. "Recent studies show that employee embezzlement has become so widespread that it accounts for a majority of business losses suffered by employers," says Archambault. Some estimates indicate that more than $600 billion is stolen annually, or roughly $4,500 per employee.

Smart Business spoke with Archambault about how business owners can protect themselves from employee theft and the right steps to take once theft or forgery is suspected.

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What types of employee embezzlement are the most common?

It varies. But generally, the schemes involve larceny, skimming or fraudulent payments.

Larceny is easiest to detect because the cash has already been recorded on the books and adequate controls usually exist.

Skimming is the embezzlement of cash from an entity prior to its being recorded on the company's books. Skimming can take the form of sales skimming, in which an employee has the customer pay him/her directly for goods or services. Receivables skimming is when the amount owed is reduced on the books by write-off schemes.

Fraudulent disbursements can take several forms, including billing schemes, payroll schemes, register disbursement schemes, expense reimbursement schemes and check tampering.

Why should owners, CEOs and CFOs worry about employee theft?

Because, sooner or later, every company will suffer from it. When it happens, the theft has ramifications that go beyond financial loss. There is also a risk of jeopardizing customer/client confidence, risk of decreasing employee morale and even a risk of liability (and potential fines) because of underreported income.

Public companies are required under federal law (Sarbanes-Oxley) to evaluate and test the design and operating effectiveness of antifraud controls on an annual basis. However, regardless of whether it is a public or private company, companies need to have an antifraud plan in place.

How does a company manage against these risks?

A fraud avoidance and assessment plan is an effective tool to use to identify vulnerabilities and to make informed, cost-effective decisions on how to prevent and detect employee theft and fraud. Proper planning maximizes the chances of a full recovery.

What does a fraud avoidance and assessment plan contain?

A comprehensive fraud avoidance plan usually includes some or all of the following elements.

- Pre-employment and periodic background investigations.
- Check safes and access passwords for computers.
- Anonymous reporting systems.
- Separate accounting functions.
- Internal and/or external auditors.
- An audit committee with the responsibility of implementing an effective ethics and compliance program that is periodically tested.

What is involved in the investigation?

If the loss is potentially large or the theft appears complex, the employer should seek the advice of the company's risk manager and an experienced legal counsel. Obtaining good legal advice and using experienced professionals maximizes the company's chances of avoiding unnecessary disruptions to the workplace and increase the possibility of recovery.

Without the right advice, a bad situation can grow worse. Accusing an employee without these first steps could result in important evidence lost, innocent people falsely accused, careers jeopardized and the organization sued for libel, slander or wrongful discharge. Legal counsel also can assist in assessing the need for additional experts, including forensic accountants and investigators.

Experienced coverage counsel also can help evaluate the company's rights under its insurance policies. Fidelity and commercial theft insurance policies generally require the insured to provide prompt notice and to furnish a sworn proof of loss within a short period of time. Business owners should approach this with caution, since the way a theft is categorized (for example, if theft is covered but forgery is not) can result in coverage being denied.

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