

The Legal Strategist

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THIRD QUARTER 2008

TEXAS ESOTERIC FACTS

- ◆ In Texas, it is illegal to put graffiti on someone else's cow.
- ◆ The milk for Blue Bell Ice Cream comes from the Texas city of Corsicana, not Brenham.
- ◆ 40% of the farm grown Catfish in the U.S. is consumed by Texans.
- ◆ The smallest Catholic Church in the world still in operation claims to be in Warrenton, Texas. Measuring 12 feet by 15 feet, the church seats 15 and is only open once a year.

This quarter's topic is based upon an article I wrote for the Nebraska State Bar and American Bar Association's Law Practice Magazine entitled *Embezzlement: A Cottage Industry Within Law Firms* in December of 2004. My article has been reprinted numerous times and has been used as source for a number of speeches and White Papers.

With the current economic outlook being somewhat less than stellar, I thought it would be appropriate to make the general issue of embezzlement this quarter's Feature Topic. I have updated the statistics and added some new material that I think every business, especially a small business, should know.

As with all of our "Featured Topics" we are only presenting a highlighted overview; if you would like more information on this or any other topic previously covered in our newsletter (which can be viewed on [The Legal Strategist](#) tab of our web site), please contact our office to set up a consultation.

Hopefully, this quarter's topic will peak your awareness of the potential hazards and pitfalls your business faces as well as give you a few basic tips that will go a long way in discouraging embezzlement. As always, we invite all comments and suggestions as well as ideas for new topics to be included in future issues.

Scott Barrett

FEATURE TOPIC: EMBEZZLEMENT: IT IS CLOSER THAN YOU THINK!

Embezzlement is a crime based on trust, or better yet, the act of breaking that trust for personal financial gain. Often a single long tenured employee is trusted with the A/R, A/P, payroll and other accounting functions. Without separation of duties and no direct oversight, this employee has complete control of the funds entering and exiting the business. Another vulnerability especially resident to small and mid sized businesses is the owner(s) may be constantly out of the office, whether it be meeting with clients or for other out of office activities. This absence of a physical presence and tangible oversight sets the stage for embezzlement. Finally, most business owners are not schooled in the finer points of operations management or audit accounting, thus making it easy for the employee to concoct schemes that look legitimate, but in actuality, line the pockets of the embezzler.

Think you are not at risk? Think again. Here are some eye opening statistics compiled by the Association of Certified Fraud Examiners:

- ◆ In 2006, the median loss suffered by organizations with fewer than 100 employees was \$190,000;
- ◆ Less than 10% of small businesses have anonymous fraud reporting systems, and less than 20% have internal audits;
- ◆ A *Psychology Today* study found that 48% of Americans are involved in unethical conduct at work;
- ◆ Losses from occupational fraud caused by managers (supervisors) were 16 times greater than those caused by rank and file employees;
- ◆ Losses caused by people 60 and older were 28 times those caused by people 25 and under;
- ◆ Research shows 90% of embezzlers have no previous criminal record.

Are you at risk? Now that you know what you are up against, here are some points to contemplate to quickly assess your vulnerability:

- ◆ Do you know the amount of funds in your account(s)? Not to the exact penny, but do you have a good idea of these balances?
- ◆ Is the person preparing checks and /or authorizing accounts payable the same person who signs the checks?
- ◆ Does the person entrusted with the collection and disbursement of funds also prepare and reconcile the bank statements and ledgers?
- ◆ Do you require a detailed explanation with all supporting documentation verifying any large or unusual items on your statement or ledger?
- ◆ Does someone other than your payroll manager reconcile your employee time sheets with funds expended on salaries?
- ◆ Does the person who is responsible for your accounting function assist your CPA in year end statements, tax preparation or audits?

Depending on your answers to these questions, you may be giving a green light to the potential embezzler. It is virtually impossible to protect 100% against embezzlement, short of performing all financial tasks yourself. So how do you minimize the risk of embezzlement? Common sense can only take you so far. You must be proactive and aggressive to counter the potential of embezzlement.

Statistics show that the average bank robbery nets the criminal around \$100,000 with a 90% chance of getting caught. The average embezzlement scheme nets the criminal around \$250,000 with only a 33% chance of being caught.

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Here are a few solid practices that will make embezzlement a much more difficult undertaking:

- ◆ Develop a sound system of checks and balances complete with internal controls;
- ◆ Limit check signing authority and access. Never solely rely on the honesty of the check preparer by giving them more than nominal authority;
- ◆ Review the bookkeeper's work. You should maintain a clear mental and physical oversight of this position;
- ◆ Question all reports or transactions which are vague, complex, abnormal, or just don't add up;
- ◆ Reconcile, Reconcile, Reconcile. All financial transactions must have a credit and a debit and must have adequate documentation unambiguously detailing the transaction along with proper approval.

Remember, embezzlement is a crime of opportunity. Based upon your answers to the earlier questions, you may be providing the opening; the embezzler will find a motive and the rationalization to steal when presented the opportunity. By employing some basic protective measures, you can greatly reduce the risk of embezzlement. If you are interested in learning more about embezzlement and ways to protect your business from potential embezzlers, please contact [Scott Barrett](#) to set up a consultation.