



Facing the Threat of Inside Fraud

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While business owners may be quick to react to efficiency problems or find ways to cut costs, they are often oblivious to signs of embezzlement. It can be difficult to confront because this problem often involves trusted employees who have recently encountered financial difficulties.

How can you protect your company from this threat? A good place to start is with an examination of your accounting procedures. Be sure to completely separate the accounts payable from the accounts receivable. In addition, have two employees handle the payroll—one to write the checks and the other to distribute them. Having just one person handle both tasks can provide a temptation hard to resist.

Key point: The employee who receives cash should not be the same person who maintains the company records. When one employee performs both functions, embezzlement can be hidden for years without detection.

Furthermore, the owner of a small business should approve all checks over a certain amount. Payments should be made with an original invoice—not a copy. In addition, make sure all bank statements are reconciled. It is recommended that you have an outside accounting firm perform surprise audits periodically.

Of course, even with these safeguards in place, there is no guarantee that you won't be victimized. What should you do if you find out an employee has embezzled from the company? Consider the following steps.

- Consult with an attorney to find out the civil and criminal legal remedies that may be available to you. For instance, you might sue the employee to recover the embezzled money.
- With your attorney by your side, contact the police. Frequently, owners feel partly to blame for allowing the theft to take place, but hiding it does no good.

In most cases, the employee will simply move on to the next victim, and you will be left holding the bag.

- Try to recover the funds. Unfortunately, reporting the crime does not mean you will be reimbursed in full. Before paying claims, insurance companies want solid proof of embezzlement, which is not always easy to provide. For example, when inventory is stolen, it is hard to show that the loss is actually theft and not an inventory mistake.
- One possible way to get your money back is to have the dishonest employee return it. If the employee is basically an honest person, he or she may jump at the opportunity to make restitution in exchange for another chance.

Caution: If you allow the employee to stay on and you suffer another loss, be aware that your insurance claim on that loss will most likely be denied. The insurance company may consider your actions as a conscious business risk.

You might decide to notify the IRS about the embezzlement. This becomes an added incentive for the employee to make restitution, since embezzled funds are considered to be taxable income. If you report the crime to the IRS, the employee will owe tax on the total amount stolen. This amount will be reduced to the extent that restitution is made by the employee.

If your business involves sensitive matters or security is a critical issue, you might obtain a bond to cover your employees. In some cases, this may be a prerequisite.

Reminder: Don't assume that embezzlement cannot happen to your firm. Take the necessary precautions to protect your company.

If you would like more information on this topic, please contact Honkamp Krueger & Co., P.C. at 888-556-0123.

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