

## How to Avoid Employee Fraud

Fraud prevention expert Christopher Eiben says that to reduce the chance of fraud, businesses should at the very least “separate the money from the record keeping.” That means:

A. Don't let the same person who receives and records receipts also book sales, generate invoices and reconcile receivables.

B. Don't let the same person who approves purchases also pay for them (and the person who pays for purchases should be able to make a payment only when it is accompanied by appropriate approval documentation).

For very small businesses, achieving the above may mean the business owner must be involved in some of these tasks. For example, many business owners personally receive all incoming mail, stamp each check on the back with deposit information, and match daily check receipts with daily deposit totals.

Experts recommend that owners of small businesses directly receive (unopened) and review credit card statements and bank statements. Alternatively, have them sent to your accountant before they go to the bookkeeper.

As long as it is feasible, experts also recommend that business owners personally sign all outgoing checks and require expenditure-approving paperwork to be attached to each check submitted for your signature.

Here are more ideas for reducing your risk of employee theft:

- *Higher authority for higher check amounts:* If you don't personally sign all checks, require that you sign all checks over a certain amount. Make sure all employees, vendors and your banker know the policy and threshold amount.
- *Get preprinted checks with preprinted check numbers:* Keep track of each check by number and reconcile bank statements immediately on receipt.
- *Thorough employee screening:* Conduct thorough background checks, including personality profiles, on all employment candidates ... especially those that will hold senior positions or work in accounting or finance.
- *Annual review of credit report:* Check to make sure no unauthorized person has taken out a credit card in your company's name.
- *Insurance:* Consider purchasing bonding insurance, i.e., insurance against employee theft and fraud.
- *Use a payroll service.* Doing so will substantially reduce risk for theft of payroll tax funds.
- *Run a journal entry report every month:* The person who runs the report should not be the person who makes the entries. Go over any adjustments with the people who made them. Make sure the vendor is legitimate and not set up by an employee or someone in cahoots with an employee.

- *Watch for an increase in bad debts:* Similarly, watch for lengthening of the age of receivables. Personally investigate accounts that slow-pay or don't pay.
- *Mandatory vacations:* Require all employees (especially finance, accounting and management) to take at least a full week off per year. More important, don't allow paperwork to pile up during the break. Have someone else perform ALL of the regular duties of the vacationing employee.
- *Educate employees about the prevalence of employee fraud:* Make sure they're aware of the risk that employee fraud poses to the organization and internal controls that are necessary and prudent. Finally, educate them on the warning signs (see accompanying article "Warnings Signs of Fraud").
- *Rotate jobs:* Periodically, have employees change jobs. Preferably, unannounced. This will substantially reduce the risk of fraud and also can raise employee satisfaction, uncover inefficiencies and dampen the hurt caused by unexpected turnover.
- *Periodic checks and surprise audits:* If employees know that their work will be checked randomly, they're much less likely to attempt to steal.
- *Promote and sustain an ethical culture:* Draft and ratify, as an organization, an ethics policy that clearly declares an expectation of ethical behavior at all levels of the organization ... and compliance with all applicable laws and regulations. Fraud prevention expert Christopher Eiben says, "Companies that countenance thievery will eventually be victimized by it."
- *Don't tolerate abuse:* Persons who have addictions to drugs, alcohol or gambling have much higher incidences of deviance. Similarly, don't tolerate other forms of abuse at work such as verbal or sexual.
- *Create a confidential reporting mechanism.* Install a message box and encourage comments. Better yet, hire a service that will take calls and allow you to offer your employees an 800 number ("hotline").
- *Investigate and approve all new vendors:* The owner should personally visit with the vendor or its representative.

Separation of duties is the most fundamental, effective fraud prevention measure. No single employee should have complete control over an entire transaction, from writing checks to making deposits and reconciling statements. Ideally, a different person should handle each function.

"If you are not making 50 mistakes a day, you are not trying hard enough." Dr. Robert Anthony