Ten Ways to Reduce Employee Theft

Small businesses are especially vulnerable to occupational fraud or employee theft. Some businesses lose more to employee theft than they make in profit.

According to the Association of Certified Fraud Examiners in the 2008 Report to the Nation (The Report), occupational fraud is defined as “The use of one’s occupation for personal enrichment through the deliberate misuse or misapplication of the employing organization’s resource or assets.”

The Report also states that the median loss suffered by organizations with fewer than 100 employees was $200,000. The reported $200,000 median loss was higher than the median loss in any other category, including the largest organizations.

Employee theft is a significant problem faced by organizations of all types, sizes and industries. As such, reducing occupational fraud opportunities in businesses is a priority for small business owners and corporate boards of directors alike.

Here are ten ways for a small business owner to take control of the fraud risk at his/her business and reduce employee theft.

First, set the tone at the top for the rest of the organization. An organization’s culture plays an important role in preventing, detecting, and deterring fraud. Employees observe and follow the example set by management. If employees see management cheating customers, vendors and employees, they are more likely to follow suit. By creating a culture through words and actions where it is clear that fraud is not tolerated and that any such behavior is dealt with swiftly and decisively, management sends a clear signal to employees. As a result, employee theft will decrease and profits for the business will increase.

Second, run background checks on prospective employees. Among other information available, certain judgments against persons for fraud show up in employee background checks and give a prospective employer more information for decision-making when hiring a new employee.
Companies specializing in services like this can do a nationwide background check efficiently and inexpensively. This is especially important when a prospective employee is coming from out of state. Often employees inclined to de-fraud their employers move from business to business without difficulty.

**Third, check the references** provided by prospective employees. Do not skip this process! Do not simply talk to the people whose names are provided. Dig a little deeper since applicants may provide names of their friends only.

**Fourth, check the details!** Verify as much information as possible on the resume of a job applicant. A component of a situation where fraud is likely to occur is rationalization of the fraudster. Rationalization is defined by Joseph T. Wells, CPA, CFE, in *Occupational Fraud Abuse*, as “a frame of mind or ethical character that allows employees to intentionally misappropriate cash or other organizational assets and justify their dishonest actions.” If an applicant is comfortable misrepresenting information on his/her resume, who knows what behavior will follow once employed!

**Fifth, require random drug testing** of employees. Another component that causes fraud to be perpetrated is perceived pressure/incentive by an employee. Pressures can be anything from overwhelming medical bills from a loved one’s illness to a need to fund one’s drug addiction. Almost no one can afford to support a drug addiction without stealing money from somewhere. Drug testing can at least give a business owner a warning that he/she has an employee who is using illegal drugs. The employer can use this information to protect his assets as well as to offer help to the individual.

**The sixth way to control fraud risk at a business is to alternate duties among staff.** Occasionally, on an unannounced basis, business owners and managers should perform duties routinely handled by other employees. The largest occurrence of fraud in small business is misappropriation of assets. These assets are usually cash and inventory. Especially important tasks involving vulnerable assets include reconciling bank accounts, inventory accounts, reviewing payroll reports, and mailing invoices and statements.

**Seventh, beware of the trusted employee.** Employees with longer tenure at an organization commit more expensive frauds than employees with shorter tenure. More than likely, long-term employees are trusted at a higher level than short-term employees. Therefore, they have greater responsibilities and less supervision, giving them more opportunity to commit fraud.

**The eighth way for a business owner to prevent fraud is to get involved.** Businesses with absentee owners always seem to be the ones with the most employee theft. Talk directly to employees at all levels and customers on a regular basis. Getting involved also

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2 Ibid
includes implementing adequate internal controls and monitoring the controls to ensure they are working properly. Lack of internal controls is the most common factor that allows fraud to occur.³ Business owners cannot interact as effectively if they are not present during day-to-day operations.

Ninth, set up surveillance cameras. If your business involves handling cash or inventory, a deterrent for theft is to strategically place video recording surveillance cameras. These can now be installed inexpensively. Let the employees know there are cameras present at the business and periodically review the tapes for irregularities. The tapes can also be used if a specific transaction is questioned. Often, a business owner can pinpoint the times problems are occurring, review the tape and catch the thief in the act!

The tenth method for business owners to prevent fraud is to set up a ‘whistle blower’ system. This provides a way for employees to anonymously report their suspicions. Tips from an employee are the number one source of fraud detection. Also, median losses in organizations without a hotline were twice as high as organizations with a hotline.⁴

Whistle blowing methods can be as simple as a suggestion box or establishing a tip hotline. The Association of Certified Fraud Examiners website can help with setting up a hotline (http://www.ethicsline.com/services/default.asp).

When business owners and managers make use of these ten precautionary steps to reduce employee theft, they become more proficient in the services they provide to the community and increase their profits.

³ Ibid
⁴ Ibid