

## THE COST OF FRAUD

At the inception of every fraud engagement there is plenty of anxiety to go around. For the victim organization, a newly discovered fraud such as embezzlement leads to many questions without specific answers. The business owner(s) are experiencing an unsettling array of emotions as they venture into the world of fraud. The financial impact to the victim organization is unknown. The potential that a long-term trusted employee has broken the “trust” relationship creates a sense of disbelief, a sense of outrage. The questions, emotions and expectations run high:

- “How much money was taken?”
- We have never experienced anything like this!”
- We treat our employees like family.”

Depending on the specific circumstances of the case, decisions must be made regarding whether or not to conduct an investigation, the costs involved, the likeliness of successfully prosecuting a case and eventually the question of whether the victim organization will receive full restitution. Filing an insurance claim offers little comfort, as the reality of restitution rests not only with the ability to investigate and document the losses but it is also impacted by an insurance company, which may work very hard to find reasons not to pay the claim.

For those of us who work in the “world of fraud” the statistics are sometimes sobering. All too often frauds go undetected, if detected, fraudsters are not always prosecuted and when prosecuted the sentences sometimes are light. In a recent article regarding the theft of \$500,000 from an ambulance association, the following comments summarize the results of the investigation:

*“More than a year after a Warwick Community Ambulance Association official was charged with stealing \$500,000 in agency funds, things are finally starting to return to business as usual. Last Wednesday, before a Lancaster County Judge, the agency official was sentenced to 2 ½ to 5 years in state prison for his theft from the association”. Published comments stated the following, “I thought the sentencing was going to be a lot harsher (citing the severity of the deceit). The fact that the judge ran the sentences concurrently rather than consecutively was a slight disappointment.” Association officials were stunned that the fraudster could be released on parole within a year. “It just doesn’t seem right”, one official was quoted as saying.*

The good news in the above mentioned case is that the organization carried a fidelity bond on those individuals who had access to financial information and accounts. For many organizations and businesses, the same outcome may not be realized because many businesses do not carry employee dishonesty insurance or the amount of coverage is inadequate when compared to the

amount of the theft. Given the passage of time, many organizations return to old habits and increase the potential that they could become victims again.

Take the case of Barry Webne. The former corporate crime consultant got off light the first time. Webne served six months in prison for embezzling \$1 million from a Cleveland manufacturer in the early '90s. During a meeting I had with Webne, Barry commented that he got in shape during his six month boot camp and was able to run ten miles a day at the time of his release. The six month jail sentence option didn't seem to fit the crime. Given access to stealing \$1 million, how many people would be tempted to commit the crime risking a six month jail sentence? After he served the six months in a prison boot camp, he "turned the corner" and later set up Webne Consulting Group, giving presentations to companies and anti-fraud groups on outsmarting fraudsters. In 2008, a federal judge in Toledo gave him the maximum under sentencing guidelines, 63 months, for embezzling another \$1 million from a different employer. Assistant U.S. Attorney Thomas Karol said Webne embezzled from two Block Communication Inc. subsidiaries from 2001 to 2006 by writing company checks to himself, falsifying payrolls among other ploys.

In addition to his jail sentence, Webne also was ordered to pay \$1,138,334.90 in restitution. Webne is currently serving his sentence in a federal prison in Morgantown, West Virginia and is scheduled to be released on July 15, 2013.

The above cases only cover the direct loss from the thefts. The real costs to a victim organization far outweigh the direct loss. For example, in the Block Communication case, the insurance deductible was \$100,000. Add to that the costs of hiring attorneys, fraud examiners and other specialists and the costs escalate. Another cost to a victim organization is the time spent by management on all aspects of the case, from beginning to end. The value of those lost hours can be substantial and are generally not recoverable, either from the insurance company or the fraudster themselves. Additional costs come in all forms, from necessary changes to organization policies and procedures, external auditor's costs, etc. and may affect the operations of the organization for years to come. Nonprofit organizations are particularly affected by the effects of embezzlement, because donors may stop donating to that organization.

As professional fraud examiners, we offer a unique skill set in combatting fraud. Unfortunately many organizations become victims simply because of the trust factor and don't effectively respond to auditors' comments about the need for improved internal controls, segregation of duties and the like.

In summary, the true cost of fraud far outweighs the dollars quoted in numerous media accounts of these cases. Victims of fraud may suffer for years or never recover at all. Our job as professional fraud examiners is to remain vigilant in our pursuit of fraud and provide the best professional service to organizations in the prevention and detection of fraud.

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