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FOCUS ON ACCOUNTING

Exposing, curbing insider thefts

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Connecticut boasts of being among the nation's highest in per-capita income and the percentage of residents with college degrees.

Yet its dubious rank as one of the nation's leaders in embezzlement losses last year is a sober reminder that smart but desperate people can be tempted into criminal shortcuts, mostly to sustain lavish lifestyles, accounting investigators say.

Marquet International Ltd.'s fourth annual report on white-collar theft ranked Connecticut sixth, with identified 2011 embezzlement losses totaling \$16.7 million in 18 cases for an average loss of \$925,667.

The biggest was the \$6.2 million embezzlement perpetrated by a former Webster Bank employee. Another was the \$1.1 million fraud by a highly trusted finance worker at Hartford's Mark Twain House.

Nationally, Marquet tracked 473 embezzlement cases last year that resulted in nearly \$355 million in losses to businesses — big and small — nonprofits, schools, state and municipalities, and, increasingly, social organizations. The firm sampled 485 cases in 2010.

"Embezzlement isn't going away anytime soon," said Chris Marquet, a 29-year veteran who started his suburban Boston security-consulting firm six years ago.

Stephen Pedneault runs Forensic Accounting Services LLC in Glastonbury, which had one of his busiest years ever, including investigation of the \$1.8 million embezzlement involving a Torrington electronics firm's controller sentenced to 5 ½ years in prison.

Pedneault says he aids clients in retracing embezzlers' tracks and then helps them to "build a better mousetrap."

"The last 12 to 18 months, it's the busiest I've been in 25 years," Pedneault said. "We had to start turning them away. I just couldn't take anymore [clients]."

Experts stress that the number of public cases and losses grossly understate the fiasco's true scope. The reason is many embarrassed victims are reluctant to admit their



Chris Marquet, founder/CEO, Marquet International Ltd.



Stephen Pedneault, CEO, Forensic Accounting Services

financial assault to employees, customers and competitors, experts say.

"Only one in nine hit the press," Pedneault said. "When you see one in the press, there's eight others you aren't seeing."

In most cases, business insurance fills the void. Also, many are resolved with the perpetrator agreeing to make restitution to avoid criminal charges. In others, state and federal prosecutors are hesitant to pursue cases that involve small sums relative to the cost to win a conviction.

"The age-old question is," Pedneault said, "are more thefts occurring or are we more aware of what it is and better at finding it?"

Marquet, a former investigator for Kroll International, a leading U.S. employment screener, argues for the latter. He debunks as myth that embezzlement worsens with the economy.

Indeed, he notes that frauds average five years in length, and points out that the Webster scam spanned six years, while the Twain House theft lasted an astounding eight years.

"These are long, long, long times for a crime to be going on," Pedneault said. "Embezzlement happens all the time. In good times, it's easy to disguise. But in bad times... it's when these frauds tend to surface."

According to Pedneault, embezzlers are turning to unsuspecting turf to ply their frauds: probate, trusts, guardianships, estates, even powers of attorney. Most victims are elderly, authorities say.

"Last year, we probably got 16 cases from probate courts throughout the state," said John "Jack" Whalen, a veteran supervisory prosecutor for the financial-crimes unit in the

Office of the Chief State's Attorney.

Also untrue, authorities say, is the existence of a stealth network of embezzlers awaiting opportunities to plunder their next victims. Fewer than one in 10 embezzlements probed involved a repeat offender, they say.

More typical is the once-loyal insider who sees weakness in an employer's system of checks and balances and exploits it, experts say.

Offenders usually are driven by a warped sense of entitlement, either because of a long history with an employer or a feeling their talents are underappreciated, authorities say. Other dominant factors are the need for cash to pay debts, a drug habit, or to support a lifestyle beyond their means. One in five steals to sustain a gambling addiction.

Therein, observers say, lies opportunity for companies, nonprofits and volunteer organizations to limit their exposure. That means closing the door via prevention.

Marquet recommends dividing up the responsibilities for tracking finances. Require multiple signatures on checks. Do random audits of customers' invoices, paying close attention to vendor names and amounts paid. Ditto with company credit cards.

Ask questions, he says, especially in identifying unfamiliar vendors and regular sums paid to one or more of them.

Pedneault goes further.

"One of the best internal controls is to know your employees," he said.

Note behaviors and lifestyles that don't add up to what you know about them. For instance, the big house or luxury automobile that suddenly appears for a person only making a blue-collar salary.

"There are usually reasons why people are doing what they are doing," Pedneault said.

The second best internal control is know who you're hiring, he said.

That means looking beyond the resume to verify job candidates' employment history and education. Pick up the phone and call references, even former employers, for verifications, he says.

"You won't do that with all 100 applicants," Pedneault said. "But when you're down to the final couple, spend the time and money to check out their backgrounds." ■