

FORENSIC RISK MANAGEMENT

What Employers *Do Not Know* Will Hurt Them

Deanna O. Burgess and Carl Pacini*

Recent reports suggest that employee fraud is pervasive. According to the 1996 *Report to the Nation on Occupational Fraud and Abuse* [The Report to the Nation], fraud and abuse cost U.S. organizations more than \$400 billion annually.¹ A 1998 KPMG Peat Marwick fraud survey of large and mid-size firms found that 62 percent of those companies had expected fraud during the past year.² It is estimated that the average organization loses about 6 percent of its total annual revenue to fraud and abuse committed by its own employees.³

The *Report to the Nation* classified fraud schemes into three types: asset misappropriation, corruption, and fraudulent financial statements. Asset misappropriation is typically accomplished by embezzling receipts, stealing, or causing an entity to pay for goods or services not received. Asset misappropriation accounts for more than four out of five fraud offenses.⁴

¹ Association of Certified Fraud Examiners (ACFE). 1996. *Report to the Nation on Occupational Fraud and Abuse* (The Wells Report). ACFE, Austin, TX.

² KPMG Peat Marwick. 1998. 1998 Fraud Survey. KPMG Peat Marwick.

³ Association of Certified Fraud Examiners, *supra* note 1.

⁴ ACFE, *supra* note 1.

Perhaps this makes asset misappropriation the most dangerous of the three fraud types.

This raises the question: "What steps can be taken to prevent, deter, and detect fraud?", particularly asset misappropriation. Such a query takes on added importance when one considers that more firms in 1998, compared to 1994, cite an insufficient emphasis on fraud prevention and detection as contributing to a rise in fraud.⁵ Thus, it is imperative for CPAs to understand the basics of fraud so they can better assess fraud risk and assist employers or clients in implementing effective preventive and detective measures.

The following case illustrates the calamitous consequences that can result when a seemingly trustworthy employee commits fraud and the basics of fraud prevention and detection are ignored.

The Facts of the Case

The Tenth Circuit Court of Appeals, a federal intermediate appellate court, upheld the conviction of a company controller on three counts of knowingly filing a false tax return. The controller

⁵ KPMG Peat Marwick, *supra* note 2.

The authors are respectively, Assistant Professor of Accounting and Assistant Professor of Accounting and Business Law at Florida Gulf Coast University, Fort Myers, FL. USA.