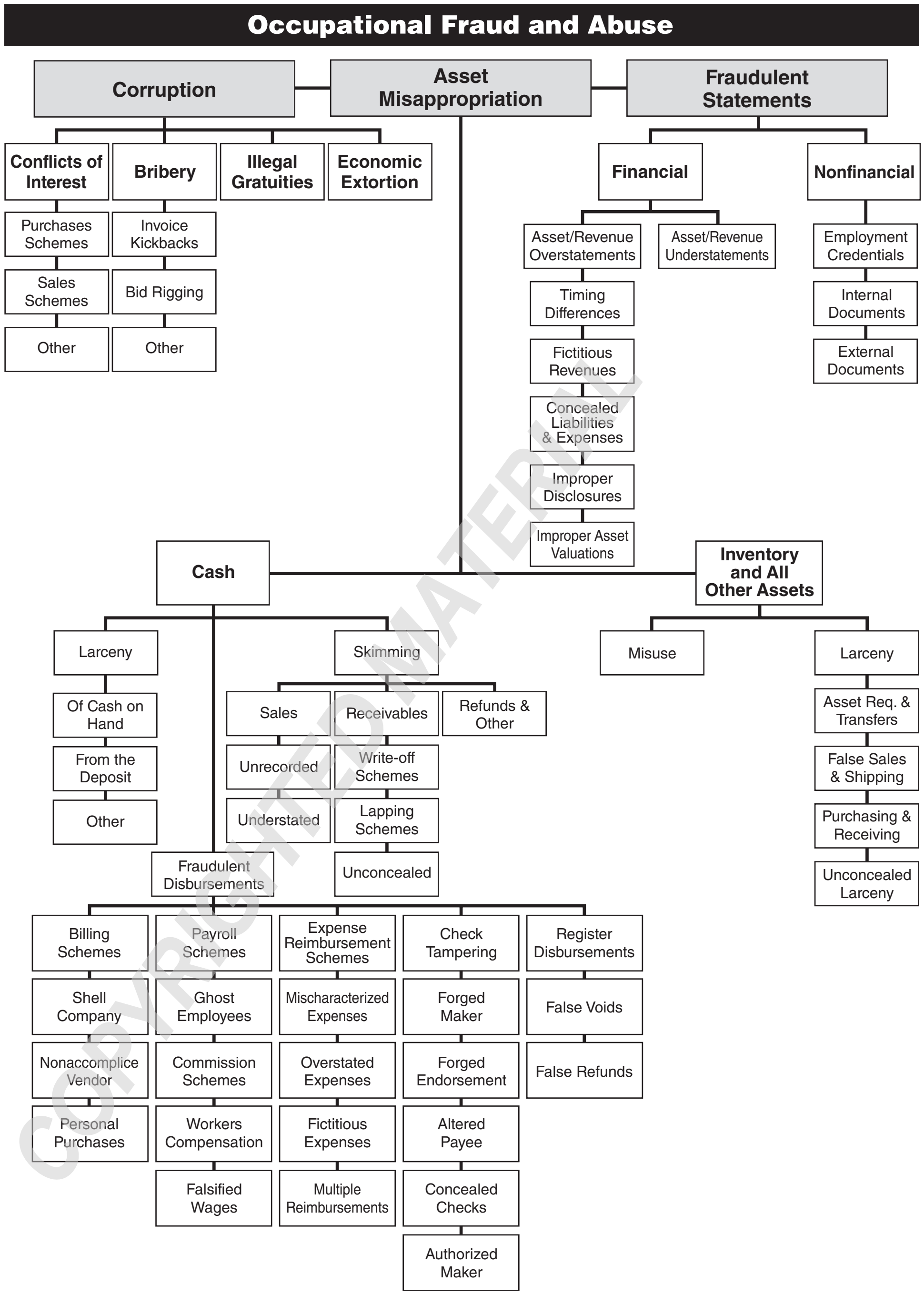
Occupational Fraud and Abuse
Corruption
Asset Misappropriation
Fraudulent Statements
Conflicts of Interest
Bribery
Illegal Gratuities
Economic Extortion
Purchases Schemes
Sales Schemes
Other
Invoice Kickbacks
Bid Rigging
Other
Financial
Nonfinancial
Asset/Revenue Overstatements
Asset/Revenue Understatements
Timing Differences
Fictitious Revenues
Concealed Liabilities & Expenses
Improper Disclosures
Improper Asset Valuations
Employment Credentials
Internal Documents
External Documents
Cash
Inventory and All Other Assets
Larceny
Of Cash on Hand
From the Deposit
Other
Skimming
Sales
Unrecorded
Understated
Receivables
Write-off Schemes
Lapping Schemes
Unconcealed
Refunds & Other
Misuse
Larceny
Asset Req. & Transfers
False Sales & Shipping
Purchasing & Receiving
Unconcealed Larceny
Fraudulent Disbursements
Billing Schemes
Shell Company
Nonaccomplice Vendor
Personal Purchases
Payroll Schemes
Ghost Employees
Commission Schemes
Workers Compensation
Falsified Wages
Expense Reimbursement Schemes
Mischaracterized Expenses
Overstated Expenses
Fictitious Expenses
Multiple Reimbursements
Check Tampering
Forged Maker
Forged Endorsement
Altered Payee
Concealed Checks
Authorized Maker
Register Disbursements
False Voids
False Refunds

EXHIBIT 1-1

CHAPTER 1

INTRODUCTION

LEARNING OBJECTIVES

After studying this chapter, you should be able to:

1-1 Define fraud examination and differentiate it from auditing
1-2 Understand the fraud theory approach
1-3 Define occupational fraud
1-4 Define fraud
1-5 Define abuse
1-6 Know the difference between fraud and abuse
1-7 Describe the criminological contributions of Edwin H. Sutherland
1-8 Understand Donald Cressey's hypothesis
1-9 Give examples of nonshareable problems that contribute to fraud
1-10 Understand how perceived opportunity and rationalization contribute to fraud
1-11 Explain W. Steve Albrecht's "fraud scale"
1-12 Summarize the conclusions of the Hollinger-Clark study
1-13 Summarize the findings of the *2011 Global Fraud Survey*

Assume that you are an auditor for Bailey Books Corporation of St. Augustine, Florida. With $226 million in annual sales, Bailey Books is one of the country's leading producers of textbooks for the college and university market and of technical manuals for the medical and dental professions.

On January 28, you received a telephone call. The caller advised that he did not wish to disclose his identity. However, he claimed to have been a long-term supplier of paper products to Bailey Books. The caller said that since Linda Reed Collins took over as purchasing manager for Bailey Books several years ago, he was systematically squeezed out of doing business with the company. He hinted that he thought Collins was up to something illegal. You queried the caller for additional information, but he hung up. What do you do now?

This case is fictional, but the situation is a common one in the world of commerce. Organizations incur costs in order to produce and sell their products or services. And such costs run the gamut: labor, taxes, advertising, occupancy, raw materials, research and development—and yes, fraud and abuse. The last cost, however, is fundamentally different from the others—the true expense of fraud and abuse is hidden, even if it is reflected in the profit-and-loss figures. Sometimes these offenses can constitute multibillion-dollar accounting misstatements, but much more frequently, they involve asset misappropriations or corruption, such as the fraud alluded to by the caller in the example above.

Resolving allegations of fraud—whether from tips, complaints, or accounting clues—is the discipline of fraud examination. It involves obtaining documentary evidence, interviewing witnesses and potential suspects, writing investigative reports, testifying to findings, and assisting in the general detection and prevention of fraud. Fraud examination has similarities to the field of *forensic accounting*, but the two terms are not precisely equivalent. Forensic accounting is the use of any accounting knowledge or skill for courtroom purposes and can therefore involve not only fraud, but also bankruptcy, business valuations and disputes, divorce, and a host of other litigation support services. On the other hand, though fraud examinations are typically performed by accountants, they can also be conducted by professionals in other fields, such as law enforcement officials, corporate security specialists, or private investigators.

Similarly, fraud examination and auditing are related, but are not identical. Because most occupational frauds are financial crimes, a certain degree of auditing is necessarily involved. But a fraud examination encompasses much more than just the review of financial data; it also involves techniques such as interviews, statement analyses, public records searches, and forensic document examination. Furthermore, there are significant differences between the two disciplines in terms of their scopes, objectives, and underlying presumptions. The following table summarizes the differences between the two disciplines.

Auditing vs. Fraud Examination

Issue	Auditing	Fraud Examination
Timing	**Recurring** Audits are conducted on a regular, recurring basis.	**Nonrecurring** Fraud examinations are nonrecurring. They are conducted only with sufficient predication.
Scope	**General** The audit is a general examination of financial data.	**Specific** Fraud examinations are conducted to resolve specific allegations.
Objective	**Opinion** An audit is generally conducted to express an opinion on financial statements or related information.	**Affix blame** The fraud examination determines whether fraud has occurred, and if so, who is responsible.
Relationship	**Nonadversarial** The audit process does not seek to affix blame.	**Adversarial** Fraud examinations involve efforts to affix blame.
Methodology	**Audit techniques** Audits are conducted primarily by examining financial data.	**Fraud examination techniques** Fraud examinations are conducted by (1) document examination, (2) review of outside data such as public records, and (3) interviews.
Presumption	**Professional skepticism** Auditors are required to approach audits with professional skepticism.	**Proof** Fraud examiners approach the resolution of a fraud by attempting to establish sufficient proof to support or refute an allegation of fraud.

FRAUD EXAMINATION METHODOLOGY

Fraud examination methodology requires that all fraud allegations be handled in a uniform, legal fashion, and that they be resolved in a timely manner. Assuming there is sufficient reason (predication) to conduct a fraud examination, specific steps are employed in a logical progression that is designed to narrow the focus of the inquiry from the general to the specific, eventually centering on a final conclusion. The fraud examiner begins by developing a hypothesis to explain how the alleged fraud was committed, and by whom. As each step of the fraud examination process uncovers more evidence, that hypothesis is amended and refined.

Predication

Predication is the totality of circumstances that would lead a reasonable, professionally trained, prudent individual to believe that a fraud has occurred, is occurring, or will occur. All fraud examinations must be based on proper predication; without it, a fraud examination should not be commenced. An anonymous tip or complaint, as in the Linda Reed Collins example cited earlier, is a common method for uncovering fraud; such a tip is generally considered sufficient predication. However, mere suspicion, without any underlying circumstantial evidence, is not a sufficient basis for conducting a fraud examination.

Fraud Theory Approach

In most occupational fraud cases, it is unlikely that there will be direct evidence of the crime. There are rarely eyewitnesses to a fraud, and it is unlikely—at least at the outset of an investigation—that the perpetrator will come right out and confess. Thus a successful fraud examination takes various sources of incomplete circumstantial evidence and assembles them into a solid, coherent structure that either proves or disproves the existence of the fraud.

To solve a fraud without complete evidence, the fraud examiner must make certain assumptions, not unlike a scientist who postulates a theory based on observation and then tests it. When investigating complex frauds, the fraud theory approach is almost indispensable. Fraud theory begins with an assumption, based on the known facts, of what might have occurred. That assumption is then tested to determine whether it can be proven. The fraud theory approach involves the following sequence of steps:

1. Analyze available data
2. Create a hypothesis
3. Test the hypothesis
4. Refine and amend the hypothesis

Let us illustrate using the Linda Reed Collins scenario. When you received the telephone call from a person purporting to be a vendor, you had no idea whether the information was legitimate. There could have been many reasons why a vendor would feel unfairly treated. Perhaps he just lost Bailey's business because another supplier provided inventory at a lower cost. Under the fraud theory approach, you must analyze the available data before developing a preliminary hypothesis about what may have occurred.

Analyzing Available Data If an audit of the entire purchasing function was deemed appropriate, it would be conducted at this time and would specifically focus on the possibility of fraud resulting from the anonymous allegation. For example, a fraud examiner would look at how contracts are awarded and at the distribution of contracts among Bailey Books' suppliers.

Creating a Hypothesis Based on the caller's accusations, you would develop a hypothesis to focus your efforts. The hypothesis is invariably a "worst-case" scenario. That is, with the limited information you possess, what is the worst possible outcome? In this case, for Bailey Books, it would probably be that its purchasing manager was accepting kickbacks to steer business to a particular vendor. A hypothesis can be created for any specific allegation, such as a bribery or kickback scheme, embezzlement, a conflict of interest, or financial statement fraud.

Testing the Hypothesis After the hypothesis has been developed, it must be tested. This involves developing a "what-if" scenario and gathering evidence to either prove or disprove the proposition. For example, if a purchasing manager like Linda Reed Collins were being bribed, a fraud examiner likely would find some or all of the following:

- A personal relationship between Collins and a vendor
- Ability of Collins to steer business toward a favored vendor
- Higher prices or lower quality for the product or service being purchased
- Excessive personal spending by Collins

In the hypothetical case of Linda Reed Collins, you—using Bailey Books' own records—can readily establish whether one vendor is receiving a proportionally larger share of the business than other vendors. You can ascertain whether Bailey Books was paying too much for a particular product, such as paper, simply by calling other vendors and determining competitive pricing. Furthermore, purchasing managers don't usually accept offers of kickbacks from total strangers; a personal relationship between a suspected vendor and the buyer could be confirmed by discreet observation or inquiry. And whether Collins has the ability to steer business toward a favored vendor could be determined by reviewing the company's internal controls to ascertain who is involved in the decision-making process. Finally, the proceeds of illegal income are not normally hoarded; such money is typically spent. Collins's lifestyle and spending habits could be determined through examination of public documents such as real estate records and automobile liens.

Refining and Amending the Hypothesis In testing the hypothesis, a fraud examiner might find that the facts do not fit a particular scenario. If this is the case, the hypothesis should be revised and retested. Gradually, as the process is repeated and the hypothesis is continually revised, the examiner works toward the most likely and supportable conclusion. The goal is not to "pin" the crime on a particular individual, but rather to determine, through the methodical process of testing and revision, whether a crime has been committed—and if so, how.

Tools Used in Fraud Examinations

Three tools are available regardless of the nature of a fraud examination. First, the fraud examiner must be skilled in the examination of financial statements, books and records, and supporting documents. In many cases, these will provide the indicia of fraud upon which a complete investigation is based. The fraud examiner must also know the legal ramifications of evidence and how to maintain the chain of custody over documents. For example, if it is determined that Linda Reed Collins was taking payoffs from a supplier, checks and other financial records to prove the case must be lawfully obtained and analyzed, and legally supportable conclusions must be drawn.

The second tool used by fraud examiners is the interview, which is the process of obtaining relevant information about the matter from those who have knowledge of it.

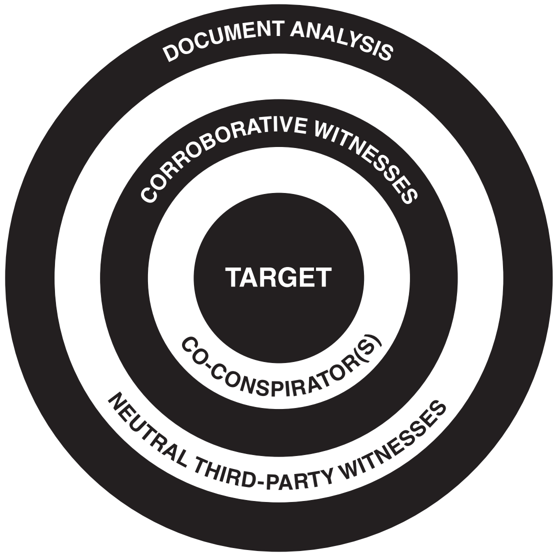

EXHIBIT 1-2 Evidence-Gathering Order in Fraud Examinations

For example, in developing information about Linda Reed Collins, it might be necessary to interview her coworkers, superiors, and subordinates.

In a fraud examination, evidence is usually gathered in a manner that moves from the general to the specific (see Exhibit 1-2). That rule applies both to gathering documentary evidence and taking witness statements. Thus, a fraud examiner would most likely start by interviewing neutral third-party witnesses, persons who may have some knowledge about the fraud but who are not involved in the offense. Next, the fraud examiner would interview corroborative witnesses—those people who are not directly involved in the offense, but who may be able to corroborate specific facts related to the offense.

If, after interviewing neutral third-party witnesses and corroborative witnesses, it appears that further investigation is warranted, the fraud examiner proceeds by interviewing suspected co-conspirators in the alleged offense. These people are generally interviewed in a particular order, starting with those thought to be least culpable and proceeding to those thought to be most culpable. Only after suspected co-conspirators have been interviewed is the person who is suspected of committing the fraud confronted. By arranging interviews in order of probable culpability, the fraud examiner is in a position to have as much information as possible by the time the prime suspect is interviewed. The methodology for conducting interviews will be discussed in Chapter 16.

The third tool that must be used in a fraud examination is observation. Fraud examiners are often placed in a position in which they must observe behavior, search for displays of wealth, and, in some instances, observe specific offenses. For example, a fraud examiner might recommend a video surveillance if it is discovered that Linda Reed Collins has a meeting scheduled with a person suspected of making payoffs.

Fraud examination methodology can be applied to virtually any type of fraud investigation. Although suspected frauds can be categorized by a number of different methods, they are usually referred to as “internal frauds” or “external frauds.” The latter refers to offenses committed by individuals against other individuals (e.g., con schemes), by individuals against organizations (e.g., insurance fraud), or by organizations against individuals (e.g., consumer frauds), but the former refers to offenses committed by the people who work for organizations; these are the most costly and the most common frauds. A more descriptive term for these crimes, as we shall see, is *occupational fraud and abuse*. This book will concentrate exclusively on occupational fraud and abuse: how it is committed, how it is prevented, and how it is investigated.

DEFINING OCCUPATIONAL FRAUD AND ABUSE

For purposes of this book, *occupational fraud and abuse* is defined as

> *The use of one's occupation for personal enrichment through the deliberate misuse or misapplication of the employing organization's resources or assets.*[1]

This definition's breadth means that occupational fraud and abuse involves a wide variety of conduct by executives, employees, managers, and principals of organizations, ranging from sophisticated investment swindles to petty theft. Common violations include asset misappropriation, fraudulent statements, corruption, pilferage and petty theft, false overtime, use of company property for personal benefit, and payroll and sick time abuses. Four elements common to these schemes were first identified by the Association of Certified Fraud Examiners in its *1996 Report to the Nation on Occupational Fraud and Abuse*, which stated: "The key is that the activity (1) is clandestine, (2) violates the employee's fiduciary duties to the organization, (3) is committed for the purpose of direct or indirect financial benefit to the employee, and (4) costs the employing organization assets, revenues, or reserves."[2]

An "employee," in the context of this definition, is any person who receives regular and periodic compensation from an organization for his labor. The employee moniker is not restricted to the rank-and-file, but specifically includes corporate executives, company presidents, top and middle managers, and other workers.

Defining Fraud

In the broadest sense, fraud can encompass any crime for gain that uses deception as its principal modus operandi. Of the three ways to illegally relieve a victim of money—force, trickery, or larceny—all offenses that employ trickery are frauds. Since deception is the linchpin of fraud, we will include *Merriam-Webster's* synonyms: "'Deceive' implies imposing a false idea or belief that causes ignorance, bewilderment, or helplessness; 'mislead' implies a leading astray that may or may not be intentional; 'delude' implies deceiving so thoroughly as to obscure the truth; 'beguile' stresses the use of charm and persuasion in deceiving."[3]

Although all frauds involve some form of deception, not all deceptions are necessarily frauds. Under common law, four general elements must be present for a fraud to exist:

1. A material false statement
2. Knowledge that the statement was false when it was uttered
3. Reliance of the victim on the false statement
4. Damages resulting from the victim's reliance on the false statement

The legal definition of fraud is the same whether the offense is criminal or civil; the difference is that criminal cases must meet a higher burden of proof.

Let's assume an employee who worked in the warehouse of a computer manufacturer stole valuable computer chips while no one was looking and resold them to a competitor.

This conduct is certainly illegal, but what law has the employee broken? Has he committed fraud? The answer, of course, is that it depends. Let us briefly review the legal ramifications of the theft.

The legal term for stealing is *larceny*, which is defined as "felonious stealing, taking and carrying, leading, riding, or driving away with another's personal property, with the intent to convert it or to deprive the owner thereof."[4] In order to prove that a person has committed larceny, we would need to prove the following four elements: (1) There was a taking or carrying away (2) of the money or property of another (3) without the consent of the owner and (4) with the intent to deprive the owner of its use or possession. In our example, the employee definitely "carried away" his employer's property, and we can safely assume that this was done without the employer's consent. Furthermore, by taking the computer chips from the warehouse and selling them to a third party, the employee clearly demonstrated intent to deprive his employer of the ability to possess and use those chips. Therefore, the employee has committed larceny.

The employee might also be accused of having committed a tort known as *conversion*.[5] Conversion, in the legal sense, is "an unauthorized assumption and exercise of the right of ownership over goods or personal chattels belonging to another, to the alteration of their condition or the exclusion of the owner's rights."[6] A person commits a conversion when he takes possession of property that does not belong to him and thereby deprives the true owner of the property for any length of time. The employee in our example took possession of the computer chips when he stole them, and by selling them he has deprived his employer of that property. Therefore, the employee has also engaged in conversion of the company's property.

Furthermore, the act of stealing the computer chips also makes the employee an embezzler. According to *Black's Law Dictionary*, to *embezzle* means "willfully to take, or convert to one's own use, another's money or property of which the wrongdoer acquired possession lawfully, by reason of some office or employment or position of trust."[7] The key words in that definition are "acquired possession lawfully." In order for an embezzlement to occur, the person who stole the property must have been entitled to possession of the property at the time of the theft. Remember, "possession" is not the same thing as "ownership." In our example, the employee might be entitled to possess the company's computer chips (to assemble them, pack them, store them, etc.), but clearly the chips belong to the employer, not the employee. When the employee steals the chips, he has committed embezzlement.

We might also observe that some employees have a recognized fiduciary relationship with their employers under the law. The term *fiduciary*, according to *Black's Law Dictionary*, is of Roman origin and means:

> *a person holding a character analogous to a trustee, in respect to the trust and confidence involved in it and the scrupulous good faith and candor which it requires. A person is said to act in a "fiduciary capacity" when the business which he transacts, or the money or property which he handles, is not for his own benefit, but for another person, as to whom he stands in a relation implying and necessitating great confidence and trust on the one part and a high degree of good faith on the other part.*[8]

In short, a fiduciary is someone who acts for the benefit of another.

A fiduciary has a duty to act in the best interests of the person whom he represents. When he violates this duty he can be liable under the tort of *breach of fiduciary duty*. The elements of this cause of action vary among jurisdictions, but in general they consist of the following: (1) a fiduciary relationship between the plaintiff and the defendant, (2) breach of the defendant's (fiduciary's) duty to the plaintiff, and (3) harm to the plaintiff or benefit to the fiduciary resulting from the breach. A fiduciary duty is a very high standard of conduct that is not lightly imposed on a person. The duty depends on the existence of a fiduciary relationship between the two parties. In an employment scenario, a fiduciary relationship will usually be found to exist only when the employee is "highly trusted" and enjoys a confidential or special relationship with the employer. Practically speaking, the law will generally recognize a fiduciary duty only for officers and directors of a company, not for ordinary employees. (In some cases a quasi-fiduciary duty may exist for employees who are in possession of trade secrets; they have a duty not to disclose that confidential information.) The upshot is that the employee in our example most likely would not owe a fiduciary duty to his employer, and therefore would not be liable for breach of fiduciary duty. However, if the example were changed so that an officer of the company stole a trade secret, then that tort would most likely apply.

But what about fraud? Recall that fraud always involves some form of deceit. If the employee in question simply walked out of the warehouse with a box of computer chips under his coat, this would not be fraud because there is no "deceit" involved. (Although many would consider this a deceitful act, what we're really talking about when we say *deceit*, as reflected in the elements of the offense, is some sort of material false statement upon which the victim relies.)

Suppose, however, that before he put the box of computer chips under his coat and walked out of the warehouse, the employee tried to cover his trail by falsifying the company's inventory records. Now the character of the crime has changed. Those records are a statement of the company's inventory levels, and the employee has knowingly falsified them. The records are certainly material because they are used to track the amount of inventory in the warehouse, and the company relies on them to determine how much inventory it has on hand, when it needs to order new inventory, and so forth. Furthermore, the company has suffered harm as a result of the falsehood, as it now has an inventory shortage of which it is unaware.

Thus, all the elements of fraud have now been satisfied: The employee has made a *material false statement;* the employee had *knowledge* that the statement was false, the company *relied* on the statement, and the company has suffered *damages*.

As a matter of law, the employee in question could be charged with a wide range of criminal and civil conduct: fraud, larceny, embezzlement, conversion, or breach of fiduciary duty. As a practical matter, he will probably be charged only with larceny. The point, however, is that occupational fraud always involves deceit, and acts that look like other forms of misconduct such as larceny may indeed involve some sort of fraud. Throughout this book we will study not only schemes that have been labeled "fraud" by courts and legislatures, but any acts of deceit by employees that fit our broader definition of occupational fraud and abuse.

Defining Abuse

Obviously, not all misconduct in the workplace amounts to fraud. There is a litany of abusive practices that plague organizations, causing lost dollars or resources but not actually constituting fraud. As any employer knows, it is hardly out of the ordinary for employees to:

- Use equipment belonging to the organization
- Surf the Internet while at work
- Attend to personal business during working hours
- Take a long lunch or break without approval

- Come to work late or leave early
- Use sick leave when not sick
- Do slow or sloppy work
- Use employee discounts to purchase goods for friends and relatives
- Work under the influence of alcohol or drugs

The term *abuse* has taken on a largely amorphous meaning over the years, frequently being used to describe any misconduct that does not fall into a clearly defined category of wrongdoing. *Merriam-Webster's* states that the word *abuse* comes from the Latin word *abusus*—to consume—and that it means "1. A corrupt practice or custom; 2. Improper or excessive use or treatment: misuse; 3. A deceitful act: deception."[9]

Given the commonality of the language describing both fraud and abuse, what are the key differences? An example illustrates: Suppose a teller was employed by a bank and stole $100 from his cash drawer. We would define that broadly as fraud. But if the teller earns $500 a week and falsely calls in sick one day, we might label that as abuse—even though each has the exact same economic impact to the company, in this case, $100.

And of course, each offense requires a dishonest intent on the part of the employee to victimize the company. Look at the way each is typically handled within an organization, though: In the case of the embezzlement, the employee gets fired; there is also a possibility (albeit remote) that he will be prosecuted. But in the case in which the employee misuses sick time, the person perhaps gets reprimanded or his pay might be docked for the day. In many instances there would be no repercussions at all.

But we can also change the "abuse" example slightly. Let's say the employee works for a governmental agency instead of in the private sector. Sick leave abuse—in its strictest interpretation—could be a fraud against the government. After all, the employee has made a false statement (about his ability to work) for financial gain (to keep from getting docked). Government agencies can and have prosecuted flagrant instances of sick leave abuse. Misuse of public money in any form can end up being a serious matter, and the prosecutorial thresholds can be surprisingly low.

Here is one real example: Many years ago I was a rookie FBI agent assigned to El Paso, Texas. That division covered the Fort Bliss military reservation, a sprawling desert complex. There were rumors that civilian employees of the military commissary were stealing inventory and selling it out the back door. The rumors turned out to be true, albeit slightly overstated. But we didn't know that at the time.

So around Thanksgiving, the FBI spent a day surveying the commissary's back entrance. We had made provisions for all contingencies—lots of personnel, secret vans, long-range cameras—the works. But the day produced only one measly illegal sale out the back door: several frozen turkeys and a large bag of yams. The purchaser of the stolen goods tipped his buddy $10 for merchandise valued at about $60. The offense occurred late in the day. We were bored and irritated, and we pounced on the purchaser as he exited the base, following him out the gate in a caravan of unmarked cars with red lights. The poor guy was shaking so badly that he wet his pants. I guess he knew better than we did what was at stake.

Because he did the wrong thing in the wrong place at the wrong time, our criminal paid dearly: He pled guilty to a charge of petty theft. So did his buddy at the commissary. The employee was fired. But the thief, it turned out, was a retired military colonel with a civilian job on the base—a person commonly known as a "double dipper." He was let go from a high-paying civilian job and now has a criminal record. But most expensively, he lost several hundred thousand dollars in potential government retirement benefits.

Would the same person be prosecuted for petty theft today? It depends entirely on the circumstances. But it could, and does, happen.

The point here is that abuse is often a way to describe a variety of petty crimes and other counterproductive behavior that have become common, even silently condoned, in the workplace. The reasons employees engage in these abuses are varied and highly complex. Do abusive employees eventually turn into out-and-out thieves and criminals? In some instances, yes. We'll discuss that later. But next, we turn to some classic research into why so-called good employees turn bad. Although some of these studies are decades old, they are landmarks in the antifraud field.

RESEARCH IN OCCUPATIONAL FRAUD AND ABUSE

Edwin H. Sutherland

Considering its enormous impact, relatively little research has been done on the subject of occupational fraud and abuse. Much of the current literature is based on the early works of Edwin H. Sutherland (1883–1950), a criminologist at Indiana University. Sutherland was particularly interested in fraud committed by the elite upper-world business executive, whether against shareholders or against the public. As Gilbert Geis noted, Sutherland said, "General Motors does not have an inferiority complex, United States Steel does not suffer from an unresolved Oedipus problem, and the DuPonts do not desire to return to the womb. The assumption that an offender may have such pathological distortion of the intellect or the emotions seems to me absurd, and if it is absurd regarding the crimes of businessmen, it is equally absurd regarding the crimes of persons in the economic lower classes."[10]

For the uninitiated, Sutherland is to the world of white-collar criminality what Freud is to psychology. Indeed, it was Sutherland who coined the term *white-collar crime*, in 1939. He intended the definition to mean criminal acts of corporations and individuals acting in their corporate capacity, but since that time the term has come to mean almost any financial or economic crime, from the mailroom to the boardroom.

Many criminologists, myself included, believe that Sutherland's most important contribution to criminal literature lay elsewhere. Later in his career, Sutherland developed the "theory of differential association," which is now the most widely accepted theory of criminal behavior. Until Sutherland's landmark work in the 1930s, most criminologists and sociologists held the view that crime was genetically based: that criminals beget criminal offspring.

Although this argument may seem naïve today, it was based largely on the observation of non-white-collar offenders—the murderers, rapists, sadists, and hooligans who plagued society. Numerous subsequent studies have indeed established a genetic base for "street" crime, which must be tempered by environmental considerations. (For a thorough explanation of the genetic base for criminality, see *Crime and Punishment* by Wilson and Herrnstein.) Sutherland was able to explain crime's environmental considerations through the theory of differential association. The theory's basic tenet is that crime is learned, much as are math, English, and guitar playing.[11]

Sutherland believed that learning of criminal behavior occurred with other persons in a process of communication. Therefore, he reasoned, criminality cannot occur without the assistance of other people. Sutherland further theorized that the learning of criminal activity usually occurred within intimate personal groups. This explains, in his view, how a dysfunctional parent is more likely to produce dysfunctional offspring. Sutherland believed that the learning process involved two specific areas: the techniques for committing crime and the attitudes, drives, rationalizations, and motives of the criminal mind. You can see how Sutherland's differential association theory fits with occupational offenders: dishonest employees will eventually infect a portion of honest ones, but honest employees will also eventually have an influence on some dishonest ones.

Donald R. Cressey

One of Sutherland's brightest students at Indiana University during the 1940s was Donald R. Cressey (1919–1987). Although much of Sutherland's research concentrated on upper-world criminality, Cressey took his own studies in a different direction. Working on his Ph.D. in criminology, he decided his dissertation would concentrate on embezzlers. To serve as a basis for his research, Cressey interviewed about 200 incarcerated inmates at prisons in the Midwest.

Cressey's Hypothesis Embezzlers, whom he called "trust violators," intrigued Cressey. He was especially interested in the circumstances that led them to be overcome by temptation. For that reason, he excluded from his research those employees who took their jobs for the purpose of stealing—a relatively minor number of offenders at that time. Upon completion of his interviews, he developed what still remains as the classic model for the occupational offender. His research was published in *Other People's Money: A Study in the Social Psychology of Embezzlement*. Cressey's final hypothesis was:

> *Trusted persons become trust violators when they conceive of themselves as having a financial problem which is non-shareable, are aware this problem can be secretly resolved by violation of the position of financial trust, and are able to apply to their own conduct in that situation verbalizations which enable them to adjust their conceptions of themselves as trusted persons with their conceptions of themselves as users of the entrusted funds or property.*[12]

Over the years, the hypothesis has become better known as the "fraud triangle" (see Exhibit 1-3). The first leg of the triangle represents a *perceived nonshareable financial need*, the second leg represents *perceived opportunity*, and the third leg stands for *rationalization*.

Nonshareable Financial Problems The role of the nonshareable problem is important. As Cressey said, "When the trust violators were asked to explain why they refrained from violation of other positions of trust they might have held at previous times, or why they had not violated the subject position at an earlier time, those who had an opinion expressed the equivalent of one or more of the following quotations: (a) 'There was no

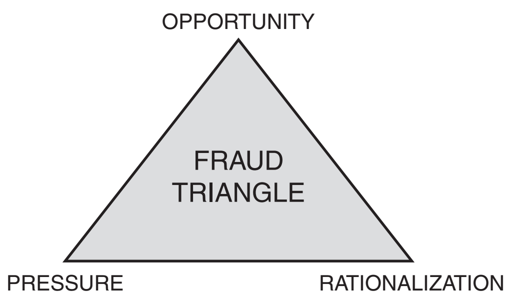

EXHIBIT 1-3 The Fraud Triangle

need for it like there was this time.' (b) 'The idea never entered my head.' (c) 'I thought it was dishonest then, but this time it did not seem dishonest at first.'"[13]

"In all cases of trust violation encountered, the violator considered that a financial problem which confronted him could not be shared with persons who, from a more objective point of view, probably could have aided in the solution of the problem."[14]

What is considered nonshareable is, of course, wholly in the eyes of the potential occupational offender, Cressey noted:

> *Thus a man could lose considerable money at the race track daily but the loss, even if it construed a problem for the individual, might not constitute a non-shareable problem for him. Another man might define the problem as one that must be kept secret and private, that is, as one which is non-shareable. Similarly, a failing bank or business might be considered by one person as presenting problems which must be shared with business associates and members of the community, while another person might conceive these problems as non-shareable.*[15]

In addition to being nonshareable, the problem that drives the fraudster is described as "financial" because these are the types of problems that generally can be solved by the theft of cash or other assets. A person saddled with large gambling debts, for instance, would need cash to pay those debts. Cressey noted, however, that some nonfinancial problems could be solved by misappropriating funds through a violation of trust. For example, a person who embezzles in order to get revenge on his employer for perceived "unfair" treatment uses financial means to solve what is essentially a nonfinancial problem.[16]

Through his research, Cressey also found that the nonshareable problems encountered by the people he interviewed arose from situations that fell into six basic categories:

1. Violation of ascribed obligations
2. Problems resulting from personal failure
3. Business reversals
4. Physical isolation
5. Status-gaining
6. Employer-employee relations

All of these situations dealt in some way with status-seeking or status-maintaining activities by the subjects.[17] In other words, the nonshareable problems threatened the status of the subjects or threatened to prevent them from achieving a higher status than the one they occupied at the time of their violation.

Violation of Ascribed Obligations Violation of ascribed obligations has historically proved a strong motivator of financial crimes:

> *Financial problems incurred through non-financial violations of positions of trust often are considered as non-shareable by trusted persons since they represent a threat to the status which holding the position entails. Most individuals in positions of financial trust, and most employers of such individuals, consider that incumbency in such a position necessarily implies that, in addition to being honest, they should behave in certain ways and should refrain from participation in some other kinds of behavior.*[18]

In other words, the mere fact that a person holds a trusted position carries with it the implied duty to act in a manner becoming that status. Persons in trusted positions may feel they are expected to avoid conduct such as gambling, drinking, drug use, or other activities that are considered seamy and undignified.

When these persons then fall into debt or incur large financial obligations as a result of conduct that is "beneath" them, they feel unable to share the problem with their peers because this would require admitting that they have engaged in the dishonorable conduct that lies at the heart of their financial difficulties. By admitting that they had lost money through some disreputable act, they would be admitting—at least in their own minds—that they are unworthy to hold their trusted positions.

Problems Resulting from Personal Failure Problems resulting from personal failure, Cressey writes, are those that a trusted person feels he caused through bad judgment, and for which he therefore feels personally responsible. Cressey cites one case in which an attorney lost his life's savings in a secret business venture. The business had been set up to compete with some of the attorney's clients, and though he thought his clients probably would have offered him help if they had known what dire straits he was in, he could not bring himself to tell them that he had secretly tried to compete with them. He also was unable to tell his wife that he'd squandered their savings. Instead, he sought to alleviate the problem by embezzling funds to cover his losses.[19]

> *While some pressing financial problems may be considered as having resulted from "economic conditions," "fate," or some other impersonal force, others are considered to have been created by the misguided or poorly planned activities of the individual trusted person. Because he fears a loss of status, the individual is afraid to admit to anyone who could alleviate the situation the fact that he has a problem which is a consequence of his "own bad judgment" or "own fault" or "own stupidity."*[20]

In short, pride goeth before the fall. If a potential offender has a choice between covering his poor investment choices through a violation of trust or admitting that he is an unsophisticated investor, it is easy to see how some prideful people's judgment could be clouded.

Business Reversals Business reversals were the third type of situation Cressey identified as leading to the perception of nonshareable financial problems. This category differs from the class of "personal failure" described above, because here the trust violators tend to see their problems as arising from conditions beyond their control: inflation, high interest rates, economic downturns, and so on. In other words, these problems are not caused by the subject's own failings, but rather by outside forces.

Cressey quoted the remarks of one businessman who borrowed money from a bank using fictitious collateral:

> *Case 36. "There are very few people who are able to walk away from a failing business. When the bridge is falling, almost everyone will run for a piece of timber. In business there is this eternal optimism that things will get better tomorrow. We get to working on the business, keeping it going, and we almost get mesmerized by it . . . Most of us don't know when to quit, when to say, 'This one has me licked. Here's one for the opposition.'"*[21]

It is interesting to note that even in situations where the problem is perceived to be out of the trusted person's control, the issue of status still plays a big role in that person's decision to keep the problem a secret. The subject of Case 36 continued, "If I'd have walked away and let them all say, 'Well, he wasn't a success as a manager, he was a failure,' and took a job as a bookkeeper, or gone on the farm, I would have been all right. But I didn't want to do that."[22] The desire to maintain the appearance of success was a common theme in the cases involving business reversals.

Physical Isolation The fourth category Cressey identified consisted of problems resulting from physical isolation. In these situations, the trusted person simply has no one to whom to turn. It's not that the person is afraid to share his problem, it's that he has no one with whom to share the problem. He is in a situation in which he has no access to trusted friends or associates who would otherwise be able to help. Cressey cited the subject of Case 106: a man who found himself in financial trouble after his wife had died. In her absence, he had no one to whom to go for help, and he wound up trying to solve his problem through an embezzlement scheme.[23]

Status Gaining The fifth category involves problems relating to status-gaining, which is a sort of extreme example of "keeping up with the Joneses." In the categories previously discussed, the offenders were generally concerned with maintaining their status (i.e., with not admitting to failure or with keeping up an appearance of trustworthiness), but here the offenders are motivated by a desire to *improve* their status. The motive for this type of conduct is often referred to as "living beyond one's means" or "lavish spending," but Cressey felt that these explanations did not get to the heart of the matter. The question was: What made the desire to improve one's status nonshareable? He noted:

> *The structuring of status ambitions as being non-shareable is not uncommon in our culture, and it again must be emphasized that the structuring of a situation as non-shareable is not alone the cause of trust violation. More specifically, in this type of case a problem appears when the individual realizes that he does not have the financial means necessary for continued association with persons on a desired status level, and this problem becomes non-shareable when he feels that he can neither renounce his aspirations for membership in the desired group nor obtain prestige symbols necessary to such membership.*[24]

In other words, it is not the desire for a better lifestyle that creates the nonshareable problem (we all want a better lifestyle); rather, it is the inability to obtain the finer things through legitimate means, and, at the same time, an unwillingness to settle for a lower status, that creates the motivation for trust violation.

Employer-Employee Relations Finally, Cressey described problems resulting from employer-employee relationships. The most common situation, he stated, was that of an employed person who resents his status within the organization in which he is trusted, yet who at the same time feels that he has no choice but to continue working for the organization. The resentment can come from perceived economic inequities, such as inadequate pay, or from feeling overworked or underappreciated. Cressey said that this problem becomes nonshareable when the individual believes that making suggestions to alleviate his perceived maltreatment will possibly threaten his status in the organization.[25] There is also a strong motivator for the employee experiencing such perceptions to want to "get even" when he feels ill-treated.

The Importance of Solving the Problem in Secret Cressey's study was done in the early 1950s, when the workforce was obviously different from that of today. But the employee who is faced with an immediate, nonshareable financial need hasn't changed much over the years. That employee is still placed in the position of having to find a way to relieve the pressure that bears down upon him. But simply stealing money is not enough; Cressey found that it was crucial that the employee be able to resolve the financial problem in secret. As we have seen, the nonshareable financial problems identified by Cressey all dealt in some way with questions of status; trust violators were afraid of losing the approval of those around them and thus were unable to tell others about the financial problems they encountered. If they could not share that they were under financial pressure, they would not be able to share the fact that they were resorting to illegal means to relieve that pressure. To do so would be to admit that the problems existed in the first place.

The interesting thing to note is that it is not the embezzlement itself that creates the need for secrecy in the perpetrator's mind, but the circumstances that led to the embezzlement (e.g., a violation of ascribed obligation, a business reversal). Cressey pointed out, "In all cases [in the study] there was a distinct feeling that, *because of activity prior to the defalcation*, the approval of groups important to the trusted person had been lost, or a distinct feeling that present group approval would be lost if certain activity were revealed [the nonshareable financial problem], with the result that the trusted person was effectively isolated from persons who could assist him in solving problems arising from that activity"[26] (emphasis added).

Perceived Opportunity According to the fraud triangle model, the presence of a nonshareable financial problem will not by itself lead an employee to commit fraud. The key to understanding Cressey's theory is to remember that all three elements must be present for a trust violation to occur. The nonshareable financial problem creates the motive for the crime to be committed, but the employee must also perceive that he has an opportunity to commit the crime without being caught. This *perceived opportunity* constitutes the second element.

In Cressey's view, there were two components of the perceived opportunity to commit a trust violation: general information and technical skill. *General information* is simply the knowledge that the employee's position of trust could be violated. Such knowledge might come from hearing of other embezzlements, from seeing the dishonest behavior of other employees, or just from generally being aware of the fact that the employee is in a position in which he could take advantage of the employer's faith in him. *Technical skill* refers to the abilities needed to commit the violation. These are usually the same abilities that allowed the employee to obtain—and that allow him to keep—his position in the first place. Cressey noted that most embezzlers adhere to their occupational routines (and their job skills) in order to perpetrate their crimes.[27] In essence, the perpetrator's job will tend to define the type of fraud he will commit: "Accountants use checks which they have been entrusted to dispose of, sales clerks withhold receipts, bankers manipulate seldom-used accounts or withhold deposits, real estate men use deposits entrusted to them, and so on."[28]

Obviously, the general information and technical skill that Cressey identified are not unique to occupational offenders; most if not all employees have these same characteristics. But because trusted persons possess this information and skill, when they face a nonshareable financial problem they see it as something that they have the power to correct. They apply their understanding of the *possibility* for trust violation to the specific crises that face them. Cressey observed, "It is the next step which is significant to violation: the application of the general information to the specific situation, and conjointly, the perception of the fact that in addition to having general possibilities for violation, a specific position of trust can be used for the specific purpose of solving a non-shareable problem."[29]

Rationalizations The third and final factor in the fraud triangle is the *rationalization*. Cressey pointed out that the rationalization is not an *ex post facto* means of justifying a theft that has already occurred. Significantly, the rationalization is a necessary component of the crime *before* it takes place; in fact, it is a part of the motivation for the crime. Because the embezzler does not view himself as a criminal, he must justify the misdeeds before he ever commits them. The rationalization is necessary so that the perpetrator can make his illegal behavior intelligible to himself and maintain his concept of himself as a trusted person.[30]

After the criminal act has taken place, the rationalization will often be abandoned. This reflects the nature of us all: The first time we do something contrary to our morals, it bothers us. As we repeat the act, it becomes easier. One hallmark of occupational fraud and abuse offenders is that once the line is crossed, the illegal acts become more or less continuous. So an occupational fraudster might begin stealing with the thought, "I'll pay the money back," but after the initial theft is successful, he will usually continue to steal until there is no longer any realistic possibility of repaying the stolen funds.

Cressey found that the embezzlers he studied generally rationalized their crimes by viewing them (1) as essentially noncriminal, (2) as justified, or (3) as part of a general irresponsibility for which they were not completely accountable.[31] He also found that the rationalizations used by trust violators tended to be linked to their positions and to the manner in which they committed their violations. He examined this by dividing the subjects of his study into three categories: *independent businessmen, long-term violators*, and *absconders*. He discovered that each group had its own types of rationalizations.

Independent Businessmen The *independent businessmen* in Cressey's study were persons in business for themselves who converted "deposits" that had been entrusted to them.[32] Perpetrators in this category tended to use one of two common excuses: (1) they were "borrowing" the money they converted, or (2) the funds entrusted to them were really theirs—and you can't *steal* from yourself. Cressey found the "borrowing" rationalization to be the one most frequently used. Such perpetrators also tended to espouse the idea that "everyone" in business misdirects deposits in some way, a fact that they considered would make their own misconduct less wrong than "stealing."[33] Also, the independent businessmen almost universally felt that their illegal actions were predicated by an "unusual situation" that Cressey perceived to actually be a nonshareable financial problem.

Long-Term Violators Cressey defined *long-term violators* as individuals who converted their employer's funds, or funds belonging to their employer's clients, by taking relatively small amounts over some duration of time.[34] Similar to independent businessmen, the long-term violators also generally preferred the "borrowing" rationalization. Other rationalizations of long-term violators were noted, too, but they almost always were used in connection with the "borrowing" theme: (1) they were embezzling to keep their families from shame, disgrace, or poverty, (2) theirs was a case of "necessity"—their employers were cheating them financially, or (3) their employers were dishonest toward others and deserved to be fleeced. Some even pointed out that it was more difficult to return the funds than to steal them in the first place, and claimed that they did not pay back their "borrowings" because they feared that would lead to detection of their thefts. A few in the study actually kept track of their thefts, but most did so only at the outset. Later, as the embezzlements escalated, it is assumed that the offender would rather not know the extent of his "borrowing."

All the long-term violators in the study expressed a feeling that they would like to eventually "clean the slate" and repay their debt. This feeling usually arose even before the perpetrators perceived that they might be caught. Cressey pointed out that at this point, whatever fear the perpetrators felt in relation to their crimes was related to losing their social position by the exposure of their nonshareable problem, not the exposure of the theft itself or the possibility of punishment or imprisonment; this was because their rationalizations still prevented them from perceiving their misconduct as criminal. "The trust violator cannot fear the treatment usually accorded criminals until he comes to look upon himself as a criminal."[35]

Eventually, most of the long-term violators finally realized they were "in too deep." It is at this point that an embezzler faces a crisis. While maintaining the borrowing rationalization (or whatever other rationalizations), the trust violator is able to maintain his self-image as a law-abiding citizen; but when the level of theft escalates to a certain point, the perpetrator is confronted with the idea that he is behaving in a criminal manner. This is contrary to his personal values and to the values of the social groups to which he belongs. This conflict creates a great deal of anxiety for the perpetrator. A number of offenders described themselves as extremely nervous and upset, tense, and unhappy.[36]

Without the rationalization that they are borrowing, long-term offenders in the study found it difficult to reconcile stealing money with seeing themselves as honest and trustworthy. In such a situation, long-term offenders have two options: (1) they can readopt the attitudes of the (law-abiding) social group with which they identified with before the thefts began; or (2) they can adopt the attitudes of the new category of persons (criminals) with whom they now identify.[37] From his study, Cressey was able to cite examples of each type of behavior. Those who sought to readopt the attitudes of their law-abiding social groups "may report their behavior to the police or to their employer, quit taking funds or resolve to quit taking funds, speculate or gamble wildly in order to regain the amounts taken, or 'leave the field' by absconding or committing suicide."[38] On the other hand, those who adopt the attitudes of the group of criminals to which they now belong "may become reckless in their defalcations, taking larger amounts than formerly with less attempt to avoid detection and with no notion of repayment."[39]

Absconders The third group of offenders Cressey discussed was *absconders*—people who take the money and run. Cressey found that the nonshareable problems for absconders usually resulted from physical isolation. He observed that these people "usually are unmarried or separated from their spouses, live in hotels or rooming houses, have few primary group associations of any sort, and own little property. Only one of the absconders interviewed had held a higher status position of trust, such as an accountant, business executive, or bookkeeper."[40] Cressey also found that the absconders tended to have lower occupational and socioeconomic status than the members of the other two categories.

Because absconders tended to lack strong social ties, Cressey found that almost any financial problem could be defined as nonshareable for these persons, and also that rationalizations were easily adopted because the persons had to sever only a minimum of social ties when they absconded.[41] The absconders rationalized their conduct by noting that their attempts to live honest lives had been futile (hence their low status). They also adopted an apathetic attitude about what happened to them, as well as a belief that they could not help themselves because they were predisposed to criminal behavior. The latter two rationalizations, which were adopted by every absconder in Cressey's study, allowed them to remove almost all personal accountability from their conduct.[42]

In the 1950s, when Cressey gathered this data, "embezzlers" were considered persons of higher socioeconomic status who took funds over a limited period of time because of some personal problem such as drinking or gambling, whereas "thieves" were considered persons of lower status who took whatever funds were at hand. Cressey noted,

"Since most absconders identify with the lower status group, they look upon themselves as belonging to a special class of thieves rather than trust violators. Just as long-term violators and independent businessmen do not at first consider the possibility of absconding with the funds, absconders do not consider the possibility of taking relatively small amounts of money over a period of time."[43]

Conjuncture of Events One of the most fundamental observations of the Cressey study was that it took all three elements—perceived nonshareable financial problem, perceived opportunity, and the ability to rationalize—for the trust violation to occur. If any of the three elements were missing, trust violation did not occur.

> *[A] trust violation takes place when the position of trust is viewed by the trusted person according to culturally provided knowledge about and rationalizations for using the entrusted funds for solving a non-shareable problem, and that the absence of any of these events will preclude violation. The three events make up the conditions under which trust violation occurs and the term "cause" may be applied to their conjuncture since trust violation is dependent on that conjuncture. Whenever the conjuncture of events occurs, trust violation results, and if the conjuncture does not take place there is no trust violation.*[44]

Conclusion Cressey's classic fraud triangle helps explain the nature of many—but not all—occupational offenders. For example, although academicians have tested his model, it still has not fully found its way into practice in terms of developing fraud prevention programs. Our sense tells us that one model—even Cressey's—will not fit all situations. Furthermore, the study is nearly half a century old; there has been considerable social change during the interim. Now, many antifraud professionals believe there is a new breed of occupational offender—one who simply lacks a conscience sufficient to overcome temptation (even Cressey saw the trend later in his life).

After his landmark study in embezzlement, Cressey went on to a distinguished academic career, eventually writing thirteen books as well as nearly 300 articles on criminology. He rose to the position of Professor Emeritus in Criminology at the University of California, Santa Barbara.

I was honored to know Cressey personally. Indeed, he and I collaborated extensively before he died in 1987, and his influence on my own antifraud theories has been significant. Our families are acquainted; we stayed in each other's homes, we traveled together—he was my friend. In a way, we made the odd couple: he the academic, me the businessman; he the theoretical, me the practical.

I met him as the result of an assignment, in about 1983, when a Fortune 500 company hired me on an investigative and consulting matter. They had a rather messy case of a high-level vice president who was put in charge of a large construction project for a new company plant. But the $75 million budget for which he was responsible proved too much of a temptation. Construction companies wined and dined the vice president and eventually provided him with tempting and illegal bait: drugs and women. He bit.

From there, the vice president succumbed to full kickbacks. By the time the dust settled, he had secretly pocketed about $3.5 million. After completing the internal investigation for the company, assembling documentation and interviews, I worked with prosecutors, at the company's request, to put the perpetrator in prison. Then the company came to me with a very simple question: "Why did he do it?" As a former FBI agent with hundreds of fraud cases under my belt, I must admit I had not thought much about the motives of occupational offenders. To my mind, they committed these crimes simply because they were crooks. But the company—certainly progressive on the antifraud front for the time—wanted me to invest the resources required to find out why and how employees go bad, so that the company could do something to prevent it. This quest took me to the vast libraries of the University of Texas at Austin, which led me to Cressey's early research. After reading Cressey's book, I realized that he had described to a T the embezzlers I had encountered. I wanted to meet him.

Finding Cressey was easy enough. I made two phone calls and found that he was still alive, well, and teaching in Santa Barbara. He was in the telephone book—I called him. Immediately, he agreed to meet me the next time I came to California. That began what became a very close relationship between us that lasted until his untimely death in 1987. It was he who recognized the real value of combining the theorist with the practitioner; he used to proclaim that he learned as much from me as I from him. And in addition to Cressey's brilliance, he was one of the most gracious people I have ever met. Although we worked together professionally for only four years, we covered a lot of ground. Cressey was convinced there was a need for an organization devoted exclusively to fraud detection and deterrence. The Association of Certified Fraud Examiners, started about a year after his death, is in existence in large measure because of his vision. Moreover, although he didn't know it at the time, he created the concept of what eventually became the certified fraud examiner. Cressey theorized that it was time for a new type of "corporate cop"—one trained in detecting and deterring the crime of fraud. Cressey pointed out that the traditional policeman was ill equipped to deal with sophisticated financial crimes—as were traditional accountants. A hybrid professional was needed, someone trained not only in accounting, but also in investigation methods: someone as comfortable interviewing a suspect as reading a balance sheet. Thus, the certified fraud examiner program was born.

Dr. W. Steve Albrecht

Another pioneer researcher in occupational fraud and abuse—and another person instrumental in the creation of the certified fraud examiner program—was Dr. Steve Albrecht of Brigham Young University. Unlike Cressey, Albrecht was educated as an accountant. Albrecht agreed with Cressey's vision: traditional accountants, he said, were poorly equipped to deal with complex financial crimes.

Albrecht's research contributions in fraud have been enormous. He and two of his colleagues, Keith Howe and Marshall Romney, conducted an analysis of 212 frauds in the early 1980s under a grant from the Institute of Internal Auditors Research Foundation, leading to their book *Deterring Fraud: The Internal Auditor's Perspective*.[45] The study's methodology involved obtaining demographics and background information on the frauds through the use of extensive questionnaires. The participants in the survey were internal auditors of companies that had experienced frauds.

Albrecht and his colleagues believed that taken as a group, occupational fraud perpetrators are hard to profile and fraud is difficult to predict. His research included an examination of comprehensive data sources to assemble a complete list of pressure, opportunity, and integrity variables, resulting in a list of fifty possible red flags or indicators of occupational fraud and abuse. These variables fell into two principal categories: perpetrator characteristics and organizational environment. The purpose of the study was to determine which of the red flags were most important to the commission (and thus to the detection and prevention) of fraud. The red flags ranged from unusually high personal debts and belief that one's job is in jeopardy to a lack of separation of asset custodial procedures and inadequate checking of potential employees' backgrounds.[46] Following is the complete list of occupational fraud red flags that Albrecht identified:[47]

Personal characteristics	Organizational environment
1. Unusually high personal debts	**24.** Defendant in a civil suit (other than divorce)
2. Severe personal financial losses	**25.** Not taking vacations of more than two or three days
3. Living beyond one's means	**26.** A department that lacks competent personnel
4. Extensive involvement in speculative investments	**27.** A department that does not enforce clear lines of authority and responsibility
5. Excessive gambling habits	**28.** A department that does not enforce proper procedures for authorization of transactions
6. Alcohol problems	**29.** A department that lacks adequate documents and records
7. Drug problems	**30.** A department that is not frequently reviewed by internal auditors
8. Undue family or peer pressure to succeed	**31.** Lack of independent checks (other than internal auditor)
9. Feeling of being underpaid	**32.** No separation of custody of assets from the accounting for those assets
10. Dissatisfaction or frustration with job	**33.** No separation of authorization of transactions from the custody of related assets
11. Feeling of insufficient recognition for job performance	**34.** No separation of duties between accounting functions
12. Continuous threats to quit	**35.** Inadequate physical security in the employee's department such as locks, safes, fences, gates, guards, etc.
13. Overwhelming desire for personal gain	**36.** No explicit and uniform personnel policies
14. Belief that job is in jeopardy	**37.** Failure to maintain accurate personnel records of disciplinary actions
15. Close associations with suppliers	**38.** Inadequate disclosures of personal investments and incomes
16. Close associations with customers	**39.** Operating on a crisis basis
17. Poor credit rating	**40.** Inadequate attention to details
18. Consistent rationalization of poor performance	**41.** Not operating under a budget
19. Wheeler-dealer attitude	**42.** Lack of budget review or justification
20. Lack of personal stability, such as frequent job changes, changes in residence, etc.	**43.** Placing too much trust in key employees
21. Intellectual challenge to "beat the system"	**44.** Unrealistic productivity expectations
22. Unreliable communications and reports	**45.** Pay levels not commensurate with the level of responsibility assigned
23. Criminal record	**46.** Inadequate staffing
	47. Failure to discipline violators of company policy
	48. Not adequately informing employees about rules of discipline or codes of conduct within the firm
	49. Not requiring employees to complete conflict-of-interest questionnaires
	50. Not adequately checking background before employment

The researchers also gave participants both sets of twenty-five motivating factors and asked which factors were present in the frauds with which they had dealt. Participants were asked to rank these factors on a seven-point scale indicating the degree to which each factor existed in their specific frauds. The ten most highly ranked factors from the list of personal characteristics, based on this study, were:[48]

1. Living beyond their means
2. An overwhelming desire for personal gain
3. High personal debt
4. A close association with customers
5. Feeling pay was not commensurate with responsibility
6. A wheeler-dealer attitude
7. Strong challenge to beat the system
8. Excessive gambling habits
9. Undue family or peer pressure
10. No recognition for job performance

As you can see from the list, these motivators are very similar to the nonshareable financial problems Cressey identified.

Additionally, the ten most highly ranked factors from the list dealing with organizational environment were:[49]

1. Placing too much trust in key employees
2. Lack of proper procedures for authorization of transactions
3. Inadequate disclosures of personal investments and incomes
4. No separation of authorization of transactions from the custody of related assets
5. Lack of independent checks on performance
6. Inadequate attention to details
7. No separation of custody of assets from the accounting for those assets
8. No separation of duties between accounting functions
9. Lack of clear lines of authority and responsibility
10. Department that is not frequently reviewed by internal auditors

All the factors on this list affect employees' opportunity to commit fraud without being caught. Opportunity, as you will recall, was the second factor identified in Cressey's fraud triangle. In many ways, the study by Albrecht et al. supported Cressey's model. Like Cressey's study, the Albrecht study suggests that there are three factors involved in occupational frauds:

> *[I]t appears that three elements must be present for a fraud to be committed: a situational pressure (non-shareable financial pressure), a perceived opportunity to commit and conceal the dishonest act (a way to secretly resolve the dishonest act or the lack of deterrence by management), and some way to rationalize (verbalize) the act as either being inconsistent with one's personal level of integrity or justifiable.*[50]

The Fraud Scale To illustrate this concept, Albrecht developed the "Fraud Scale," which included the components of: *situational pressures, perceived opportunities*, and *personal integrity*.[51] When situational pressures and perceived opportunities are high and

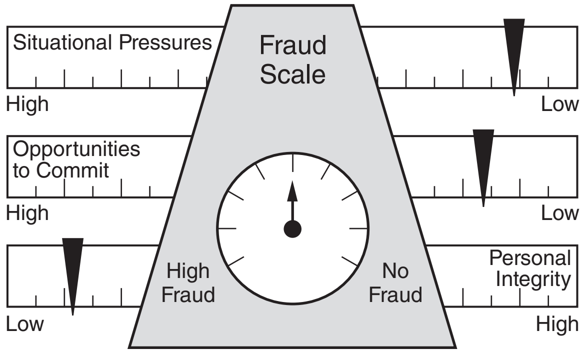

EXHIBIT 1-4 The Fraud Scale

personal integrity is low, occupational fraud is much more likely to occur than when the opposite is true[52] (see Exhibit 1-4).

Albrecht described situational pressures as "the immediate problems individuals experience within their environments, the most overwhelming of which are probably high personal debts or financial losses."[53] Opportunities to commit fraud, Albrecht says, may be created by individuals, or by deficient or missing internal controls. Personal integrity "refers to the personal code of ethical behavior each person adopts. While this factor appears to be a straightforward determination of whether the person is honest or dishonest, moral development research indicates that the issue is more complex."[54]

In addition to its findings on motivating factors of occupational fraud, the Albrecht study also disclosed several interesting relationships between the perpetrators and the frauds they committed. For example, perpetrators of large frauds used the proceeds to purchase new homes, expensive automobiles, recreation property, and expensive vacations; to support extramarital relationships; and to make speculative investments. Those committing small frauds did not.[55]

There were other observations: Perpetrators who were interested primarily in "beating the system" committed larger frauds. However, perpetrators who believed their pay was not adequate committed primarily small frauds. Lack of segregation of responsibilities, placing undeserved trust in key employees, imposing unrealistic goals, and operating on a crisis basis were all pressures or weaknesses associated with large frauds. College graduates were less likely to spend the proceeds of their loot to take extravagant vacations, purchase recreational property, support extramarital relationships, and buy expensive automobiles. Finally, those with lower salaries were more likely to have a prior criminal record.[56]

Richard C. Hollinger

The Hollinger-Clark Study In 1983, Richard C. Hollinger of Purdue University and John P. Clark of the University of Minnesota published federally funded research involving surveys of nearly 10,000 American workers. In their book, *Theft by Employees*, the two researchers reached a different conclusion than Cressey: They found that employees steal primarily as a result of workplace conditions. They also concluded that the true costs of employee theft are vastly understated: "In sum, when we take into consideration the incalculable social costs . . . the grand total paid for theft in the workplace is no doubt grossly underestimated by the available financial estimates."[57]

Hypotheses of Employee Theft In reviewing the literature on employee theft, Hollinger and Clark noted that experts had developed five separate but interrelated sets of hypotheses to explain employee theft. The first was that external economic pressures, such as the "non-shareable financial problem" that Cressey described, motivated theft. The second hypothesis was that contemporary employees, specifically young ones, are not as hard working and honest as those in past generations. The third theory, advocated primarily by those with years of experience in the security and investigative industry, was that every employee can be tempted to steal from his employer; this theory assumes that people are greedy and dishonest by nature. The fourth theory was that job dissatisfaction is the primary cause of employee theft, and the fifth was that theft occurs because of the broadly shared formal and informal structure of organizations: that is, over time, the group norms—good or bad—become the standard of conduct. The sum of Hollinger and Clark's research led them to conclude that the fourth hypothesis was correct—that employee deviance is primarily caused by job dissatisfaction.

Employee Deviance Employee theft is at one extreme of employee deviance, which can be defined as conduct detrimental to the organization and to the employee. At the other extreme is counterproductive employee behavior, such as goldbricking and abuse of sick leave. Hollinger and Clark defined two basic categories of deviant behavior by employees: (1) acts by employees against property, and (2) violations of the norms regulating acceptable levels of production. The former includes misuse and theft of company property, such as of cash or inventory; the latter involves acts of employee deviance that affect productivity.

Hollinger and Clark developed a written questionnaire that was sent to employees in three different sectors: retail, hospital, and manufacturing. The employees were presented with lists of category 1 and category 2 offenses and were asked which offenses they had been involved in, and with what frequency. The researchers eventually received 9,175 valid employee questionnaires, representing about 54 percent of those sampled. Below are the results of the questionnaires. The first table represents category 1 offenses—acts against property.[58] Hollinger and Clark found that approximately one-third of employees in each sector admitted to committing some form of property deviance.

Combined Phase I and Phase II Property-Deviance Items and Percentage of Reported Involvement, by Sector

	Involvement				
Items	Almost daily	About once a week	Four to twelve times a year	One to three times a year	Total
Retail Sector (*N* = 3,567)					
Misuse the discount privilege	0.6	2.4	11	14.9	28.9
Take store merchandise	0.2	0.5	1.3	4.6	6.6
Get paid for more hours than were worked	0.2	0.4	1.2	4	5.8
Purposely under-ring a purchase	0.1	0.3	1.1	1.7	3.2
Borrow or take money from employer without approval	0.1	0.1	0.5	2	2.7
Be reimbursed for more money than spent on business expenses	0.1	0.2	0.5	1.3	2.1
Damage merchandise to buy it on discount	0	0.1	0.2	1	1.3
Total involved in property deviance					35.1

(*Continued*)

(*Continued*)

Items	Involvement				
	Almost daily	About once a week	Four to twelve times a year	One to three times a year	Total
Hospital Sector ($N = 4{,}111$)					
Take hospital supplies (e.g., linens, bandages)	0.2	0.8	8.4	17.9	27.3
Take or use medication intended for patients	0.1	0.3	1.9	5.5	7.8
Get paid for more hours than were worked	0.2	0.5	1.6	3.8	6.1
Take hospital equipment or tools	0.1	0.1	0.4	4.1	4.7
Be reimbursed for more money than spent on business expenses	0.1	0	0.2	0.8	1.1
Total involved in property deviance					33.3
Manufacturing Sector ($N = 1{,}497$)					
Take raw materials used in production	0.1	0.3	3.5	10.4	14.3
Get paid for more hours than were worked	0.2	0.5	2.9	5.6	9.2
Take company tools or equipment	0	0.1	1.1	7.5	8.7
Be reimbursed for more money than spent on business expenses	0.1	0.6	1.4	5.6	7.7
Take finished products	0	0	0.4	2.7	3.1
Take precious metals (e.g., platinum, gold)	0.1	0.1	0.5	1.1	1.8
Total involved in property deviance					28.4

Adapted from Richard C. Hollinger, John P. Clark, *Theft by Employees*, Lexington, MA: Lexington Books, 1983, p. 42.

Following is a summary of the Hollinger and Clark research with respect to production deviance. Not surprisingly, they found that this form of employee misconduct was two to three times more common than property violations.[59]

Combined Phase I and Phase II Property-Deviance Items and Percentage of Reported Involvement, by Sector

Items	Involvement				
	Almost daily	About once a week	Four to twelve times a year	One to three times a year	Total
Retail Sector ($N = 3{,}567$)					
Take a long lunch or break without approval	6.9	13.3	15.5	20.3	56
Come to work late or leave early	0.9	3.4	10.8	17.2	32.3
Use sick leave when not sick	0.1	0.1	3.5	13.4	17.1
Do slow or sloppy work	0.3	1.5	4.1	9.8	15.7
Work under the influence of alcohol or drugs	0.5	0.8	1.6	4.6	7.5
Total involved in production deviance					65.4

Hospital Sector ($N = 4{,}111$)					
Take a long lunch or break without approval	8.5	13.5	17.4	17.8	57.2
Come to work late or leave early	1	3.5	9.6	14.9	29
Use sick leave when not sick	0	0.2	5.7	26.9	32.8
Do slow or sloppy work	0.2	0.8	4.1	5.9	11
Work under the influence of alcohol or drugs	0.1	0.3	0.6	2.2	3.2
Total involved in production deviance					69.2
Manufacturing Sector ($N = 1{,}497$)					
Take a long lunch or break without approval	18	23.5	22	8.5	72
Use sick leave when not sick	0	0.2	9.6	28.6	38.4
Do slow or sloppy work	0.5	1.3	5.7	5	12.5
Work under the influence of alcohol or drugs	1.1	1.3	3.1	7.3	12.8
Come to work late or leave early	1.9	9	19.4	13.8	44.1
Total involved in production deviance					82.2

Adapted from Richard C. Hollinger, John P. Clark, *Theft by Employees*, Lexington, MA: Lexington Books, 1983, p. 45.

Income and Theft In order to empirically test whether economics had an effect on the level of theft, the researchers sorted their data by household income, under the theory that lower levels of income might produce higher levels of theft. However, they were unable to confirm such a statistical relationship. This would tend to indicate—at least in this study—that absolute income is not a predictor of employee theft.

Despite this finding, Hollinger and Clark were able to identify a statistical relationship between employees' *concern* over their financial situation and the level of theft. They presented the employees with a list of eight major concerns, ranging from personal health to education issues to financial problems. They noted, "Being concerned about finances and being under financial pressure are not necessarily the same. However, if a respondent considered his finances as one of the most important issues, that concern could be partially due to 'unshareable [*sic*] economic problems,' or it could also be that current realities are not matching one's financial aspirations regardless of the income presently being realized."[60] The researchers concluded, "In each industry, the results are significant, with higher theft individuals more likely to be concerned about their finances, particularly those who ranked finances as the first or second most important issue."[61]

Age and Theft Hollinger and Clark found in their research a direct correlation between age and the level of theft. "Few other variables . . . have exhibited such a strong relationship to theft as the age of the employee."[62] The reason, they concluded, was that the younger employee generally has less tenure with his organization and therefore has a lower level of commitment to it than the typical older employee. In addition, there is a long history of connection between youth and many forms of crime. Sociologists have suggested that the central process of control is determined by a person's "commitment to conformity." Under this model—assuming employees are all subject to the same deviant motives and opportunities—the probability of deviant involvement depends on the stakes that one has in conformity. Since younger employees tend to be less committed to the idea of conforming to established social rules and structures, it follows that they would be more likely to engage in illegal conduct that runs contrary to organizational and societal expectations.

The researchers suggested that the policy implications from the commitment to conformity theory are that rather than subjecting employees to draconian security measures, "companies should afford younger workers many of the same rights, fringes, and privileges of the tenured, older employees. In fact, by signaling to the younger employee that he is temporary or expendable, the organization inadvertently may be encouraging its own victimization by the very group of employees that is already least committed to the expressed goals and objectives of the owners and managers."[63] Although this may indeed affect the level of employee dissatisfaction, its policy implications may not be practical for non-fraud-related reasons.

Position and Theft Hollinger and Clark were able to confirm a direct relationship between an employee's position and the level of the theft, with thefts being highest in jobs affording greater access to the things of value in the organization. Although they found obvious connections between opportunity and theft (for example, retail cashiers with daily access to cash had the highest incidence), the researchers believed opportunity to be "only a secondary factor that constrains the manner in which the deviance is manifested."[64] Their research indicated that job satisfaction was the primary motivator of employee theft; the employee's position affects the method and amount of the theft only *after* the decision to steal has already been made.

Job Satisfaction and Deviance The research of Hollinger and Clark strongly suggests that employees who are dissatisfied with their jobs—across all age groups, but especially younger workers—are the most likely to seek redress through counter-productive or illegal behavior in order to right the perceived inequity. Other writers, notably anthropologist Gerald Mars and researcher David Altheide, have commented on this connection. Mars observed that among both hotel dining room employees and dock workers it was believed that pilferage was not theft; rather, it was "seen as a morally justified addition to wages; indeed, as an entitlement due from exploiting employers."[65] Altheide also documented that theft is often perceived by employees as a "way of getting back at the boss or supervisor."[66] Jason Ditton documented a pattern in U.S. industries called "wages in kind," in which employees "situated in structurally disadvantaged parts [of the organization] receive large segments of their wages invisibly."[67]

Organizational Controls and Deviance Hollinger and Clark were unable to document a strong relationship between control and deviance in their research. They examined five different control mechanisms: company policy, selection of personnel, inventory control, security, and punishment.

Company policy can be an effective control. Hollinger and Clark pointed out that companies with a strong policy against absenteeism have a lesser problem with it. As a result, they would expect policies governing employee theft to have the same impact. Similarly, they believed that employee education as an organizational policy has a deterrent effect. Control through selection of personnel is exerted by hiring persons who will conform to organizational expectations. Inventory control is required not only for theft, but for procedures to detect errors, avoid waste, and ensure that a proper amount of inventory is maintained. Security controls involve proactive and reactive measures, surveillance, internal investigations, and others. Control through punishment is designed to deter the specific individual as well as others who might be tempted to act illegally.

Hollinger and Clark interviewed numerous employees in an attempt to determine their attitudes toward control. With respect to policy, they concluded, "The issue of theft by employees is a sensitive one in organizations and must be handled with some discretion. A concern for theft must be expressed without creating an atmosphere of distrust and paranoia. If an organization places too much stress on the topic, honest employees may feel unfairly suspected, resulting in lowered morale and higher turnover."[68]

Employees in the study also perceived, in general, that computerized inventory records added security and made theft more difficult. With respect to security control, the researchers discovered that the employees regarded the purpose of a security division as taking care of outside—rather than inside—security. Few of the employees were aware that security departments investigate employee theft, and most such departments had a poor image among the workers. With respect to punishment, the employees who were interviewed felt that theft would result in job termination in a worst-case scenario. They perceived that minor thefts would be handled only by reprimands.

Hollinger and Clark concluded that formal organizational controls provide both good and bad news. "The good news is that employee theft does seem to be susceptible to control efforts. Our data also indicate, however, that the impact of organizational controls is neither uniform nor very strong. In sum, formal organizational controls do negatively influence theft prevalence, but these effects must be understood in combination with the other factors influencing this phenomenon."[69]

Employee Perception of Control The researchers also examined the perception—not necessarily the reality—of employees who believed they would be caught if they committed theft: "We find that perceived certainty of detection is inversely related to employee theft for respondents in all three industry sectors—that is, the stronger the perception that theft would be detected, the less the likelihood that the employee would engage in deviant behavior."[70]

This finding is significant and is consistent with other research. It suggests that increasing the perception of detection may be the best way to deter employee theft, whereas increasing the sanctions that are imposed on occupational fraudsters will have a limited effect. Recall that under Cressey's model, embezzlers are motivated to commit illegal acts because they face some financial problem that if shared with others would threaten their status. It follows that the greatest threat to the perpetrator would be that he might be caught in the act of stealing, which would bring his nonshareable problem out into the open; the possibility of sanctions is only a secondary concern. The perpetrator engages in the illegal conduct only because he perceives an opportunity to fix his financial problem *without getting caught*. Thus, if an organization can increase in its employees' minds the perception that illegal acts will be detected, it can significantly deter occupational fraud. Put simply, occupational fraudsters are not deterred by the threat of sanctions because they do not plan on getting caught.

Control in the workplace, according to Hollinger and Clark, consists of both formal and informal social controls. Formal controls can be described as external pressures that are applied through both positive and negative sanctions; informal controls consist of the internalization by the employee of the group norms of the organization. These researchers, along with a host of others, have concluded that—as a general proposition—informal social controls provide the best deterrent. "These data clearly indicate that the loss of respect among one's acquaintances was the single most effective variable in predicting future deviant involvement." Furthermore, "in general, the probability of suffering informal sanction is far more important than fear of formal sanctions in deterring deviant activity."[71] Again, this supports the notion that the greatest deterrent to the fraudster is the idea that he will be caught—not the threat of punishment by his employer.

Other Conclusions Hollinger and Clark reached several other conclusions based on their work. First, they found that "substantially increasing the internal security presence does not seem to be appropriate, given the prevalence of the problem. In fact, doing so may make things worse."[72] Second, they concluded that the same kinds of employees who engage in other workplace deviance are also principally the ones who engage in employee theft. They found persuasive evidence that slow or sloppy workmanship, sick leave abuses, long coffee breaks, alcohol and drug use at work, late arrival, and early departure were more likely to be present in the employee-thief.

Third, the researchers hypothesized that if efforts are made to reduce employee theft without reducing its underlying causes (e.g., employee dissatisfaction, lack of ethics), the result could create a "hydraulic effect" whereby tightening controls over property deviance may create more detrimental acts affecting the productivity of the organization—for example, pushing down employee theft may push up goldbricking. Fourth, they asserted that increased management sensitivity to its employees would reduce all forms of workplace deviance. Fifth, they concluded that special attention should be afforded young employees, the ones statistically most likely to steal. However, it must be pointed out that although the incidence of theft is higher among younger employees, the losses associated with those thefts are typically lower than the losses caused by more senior employees, who have greater financial authority.

Hollinger and Clark asserted that management must pay attention to four aspects of policy development: (1) clearly understanding theft behavior, (2) continuously disseminating positive information reflective of the company's policies, (3) enforcing sanctions, and (4) publicizing sanctions.

The researchers summed up their observations by saying, "perhaps the most important overall policy implication that can be drawn . . . is that theft and workplace deviance are in large part a reflection of how management at all levels of the organization is perceived by the employee. Specifically, if the employee is permitted to conclude that his contribution to the workplace is not appreciated or that the organization does not seem to care about the theft of its property, we expect to find greater involvement. In conclusion, a lowered prevalence of employee theft may be one valuable consequence of a management team that is responsive to the current perceptions and attitudes of its workforce."[73]

The 2012 Report to the Nations on Occupational Fraud and Abuse

In 1993, the Association of Certified Fraud Examiners (ACFE) began a major study of occupational fraud cases with the goal of classifying occupational frauds and abuses by the methods used to commit them. There were other objectives, too. One was to get an idea of how the professionals—the certified fraud examiners (CFEs)—view the fraud problems faced by their own companies. After all, they deal with fraud and abuse on a daily basis. Another goal was to gather demographics on the perpetrators: How old are they? How well educated? What percentage of offenders are men? Were there any correlations that we could identify with respect to the offenders? What about the victim companies: How large were they? What industries did they cover? For good measure, the ACFE also decided to ask the CFEs to take an educated guess—based upon their experience—of the extent of fraud and abuse within their own organizations.

Beginning in 1993, the ACFE distributed a detailed four-page questionnaire to about 10,000 CFEs, asking them to report the details of one fraud case they had investigated.

By early 1995, 2,608 surveys had been returned for analysis, including 1,509 usable cases of occupational fraud. Although the survey design was not perfect, the sheer number of responses made it—to the ACFE's knowledge—the largest such study on this subject at the time. Of the cases analyzed, the total loss caused by fraud was about $15 billion, ranging from a low of $22 to a high of $2.5 billion. From that survey, the ACFE developed in 1996 the first *Report to the Nation on Occupational Fraud and Abuse*. Association President Gil Geis decided that the name *Report to the Nation on Occupational Fraud and Abuse* was a bit long, so he alternatively titled it, *The Wells Report*.

Since 1996, the ACFE has released six updated editions of the Report—in 2002, 2004, 2006, 2008, 2010, and the most recent version in 2012. Each edition has been based on detailed case information provided by CFEs and has built on the findings of its predecessors.

The ACFE's most recent survey was conducted in late 2011 and resulted in the *2012 Report to the Nations on Occupational Fraud and Abuse*. The current edition of the Report is based on 1,388 actual cases of occupational fraud that were investigated worldwide between January 2010 and December 2011. The CFEs who participated were asked to provide information on the single largest case they investigated during this time period; from this information, researchers were able to observe trends in and draw conclusions about how fraud is committed, how it can be classified, and how it affects business across the globe.

The majority of statistical data pertaining to the ACFE's research on occupational fraud that is cited in this book is derived from the results of the *2011 Global Fraud Survey*, as reported in the *2012 Report to the Nations on Occupational Fraud and Abuse*.

Measuring the Costs of Occupational Fraud Participants in the *2011 Global Fraud Survey* were asked what percent of gross revenues they believe—based on their personal experience and general knowledge—the typical organization loses to fraud and abuse. The median response was 5 percent, which was consistent with estimates provided by respondents in previous editions of the survey.

However, because the responses provided were only estimates, the data should not be read as a literal representation of the true rate of fraud in organizations throughout the world. Nevertheless, even at a rate of 5 percent, this estimate of the cost of fraud is astounding. Applying this figure to the Gross World Product—which, for 2011, was estimated to be $69.11 trillion[74]—results in a projected total global fraud loss of nearly $3.5 trillion annually. It is a staggering sum, to say the least.

But what does the figure really mean? It is simply the collective opinions of those who work in the antifraud field. Unfortunately, finding the actual cost of fraud may not be possible by any method. One obvious approach would be to take a scientific poll of the workforce and ask them the tough questions: Have you stolen or committed fraud against your organization? If so, how? How much was the value of the fraud or abuse you committed? But the unlikelihood of people answering such questions candidly would make any results obtained by this method unreliable at best.

Another approach to finding the cost of fraud would be to do a scientific poll of a representative sample of organizations. Even assuming the respondents answered the poll correctly, there would still be an obvious flaw in the data: Organizations typically don't know when they are being victimized. And, of course, there is the definitional issue which plagues all the methods: Where do we draw the line on what constitutes occupational fraud and abuse? So asking the experts—the approach used here—may be as reliable as anything else. But the reader must be cautioned that, by any method of estimation, the numbers on fraud and abuse are soft and subject to various interpretations.

Whatever the actual costs, organizations are unwittingly paying them already as a part of their total operating expenses. What can be done about a problem with such an insidious nature? And how can we possibly detect something we don't know about in the first place? It's as if a secret "fraud tax" has been levied on organizations. Interestingly, many organizations may silently condone fraud and abuse, which is committed from the top down. Indeed, some sociologists see abuse as an informal employment benefit and have even suggested that chronic pilferage and certain other abuses might actually have a positive effect on morale and therefore increase productivity.[75]

The Perpetrators of Fraud By definition, the perpetrators of occupational fraud are employed by the organization they defraud. Participants in the 2011 survey provided information on the perpetrators' position, gender, age, education, department, tenure, and criminal histories. In cases where there was more than one perpetrator, respondents were asked to provide data on the *principal perpetrator*, which was defined as the person who worked for the victim organization and who was the primary culprit.

The Effect of the Perpetrator's Position Data gathered about the perpetrators indicated that most of the frauds in this study were committed by either employees (42 percent) or managers (38 percent). Owners/executives made up less than one-fifth of the perpetrators (see Exhibit 1-5).

Although the highest percentage of schemes was committed by employees, these frauds had the lowest median loss, at $60,000 per incident. Frauds committed by managers caused median losses of $182,000 per incident, while the median loss in schemes committed by owner/executives was $573,000—more than nine times higher than the typical loss in employee schemes. The differences in the loss amounts were most likely a result of the degree of financial control exercised at each level: Those with the highest positions also have the greatest access to company funds and assets (see Exhibit 1-6).

The Effect of Gender The results of the *2011 Global Fraud Survey* showed that male employees caused median losses more than twice as large as those of female employees; the median loss in a scheme caused by a male employee was $200,000, while the median loss caused by a female employee was $91,000 (see Exhibit 1-7). The

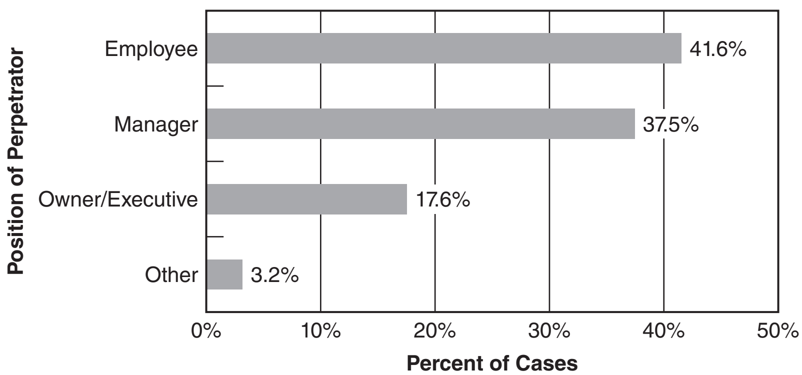

EXHIBIT 1-5 *2011 Global Fraud Survey*: Percent of Cases by Position

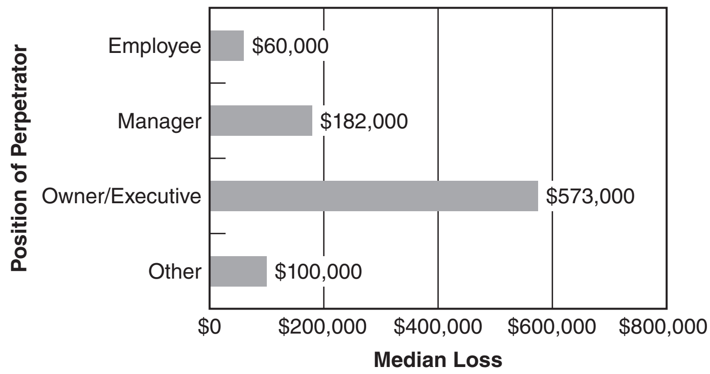

EXHIBIT 1-6 *2011 Global Fraud Survey*: Median Loss by Position

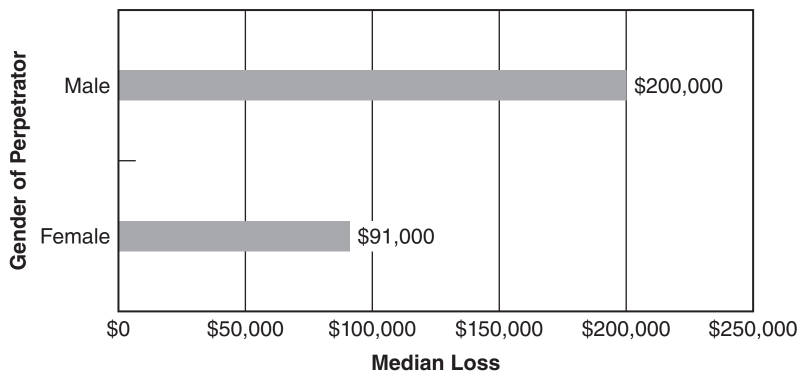

EXHIBIT 1-7 *2011 Global Fraud Survey*: Median Loss by Gender

most logical explanation for this disparity seems to be the "glass ceiling" phenomenon: generally, men occupy higher-paying positions than their female counterparts, and, as we have seen, there is a direct correlation between median loss and position.

According to survey data, males are also the principal perpetrator in a majority of cases, accounting for 65 percent of frauds in the study versus the 35 percent in which a female was the primary culprit (see Exhibit 1-8).

The Effect of Age The ACFE *Reports* continually reveal a direct and linear correlation between the perpetrator's age and median loss. The reason for the trend, ACFE researchers believe, is that those in an organization who are older generally tend to occupy higher-ranking positions with greater access to revenues, assets, and resources. In other words, researchers believe age to be only a secondary factor to that of position as a predictor of relative fraud losses.

As illustrated in Exhibit 1-9, those in the oldest age group were responsible for median losses ten times higher than the youngest perpetrators. Furthermore, although some studies, including Hollinger-Clark, have suggested that younger employees are more likely to commit occupational crime, only 6 percent of the frauds in the study were committed by

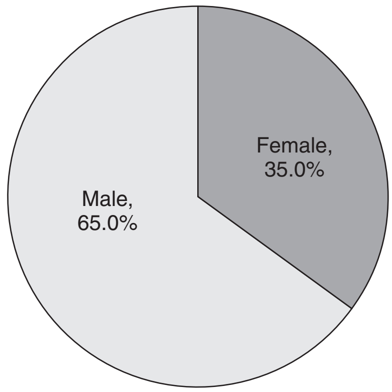

EXHIBIT 1-8 *2011 Global Fraud Survey*: Percent of Cases by Gender

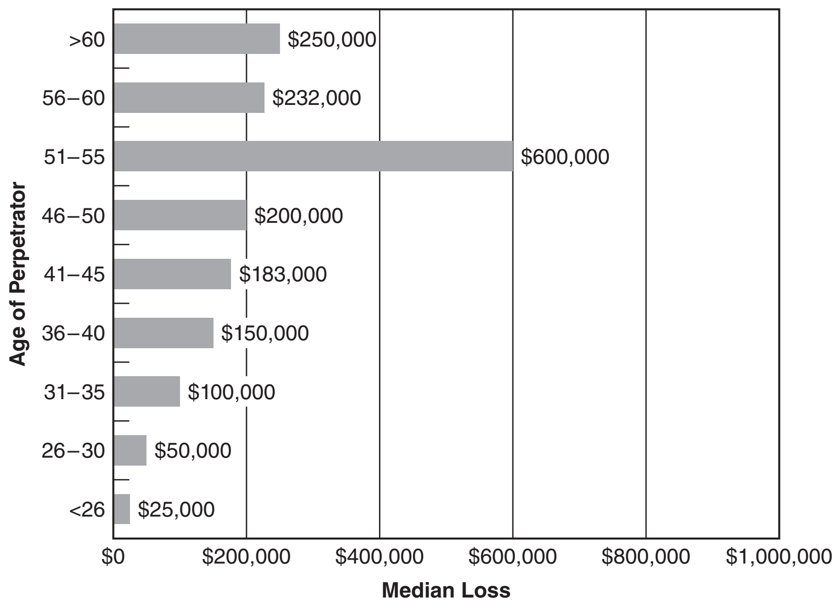

EXHIBIT 1-9 *2011 Global Fraud Survey*: Median Loss by Age

individuals below the age of twenty-six, while more than half the frauds were committed by persons over the age of forty (see Exhibit 1-10).

The Effect of Education Nearly three-quarters of the perpetrators in the study had completed some college (see Exhibit 1-11). Additionally, those with higher education levels would generally be expected to occupy higher positions in an organization and to have greater access to organizational assets. Therefore, researchers expected a fairly linear correlation between education and median loss. This was evident in

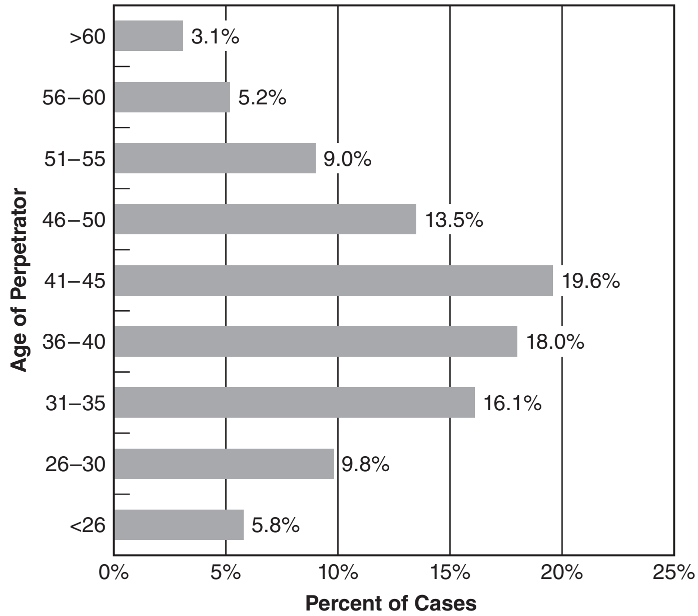

EXHIBIT 1-10 *2011 Global Fraud Survey*: Percent of Cases by Age

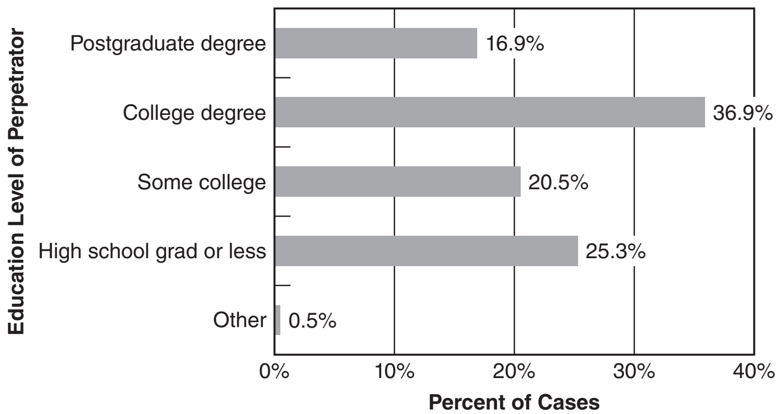

EXHIBIT 1-11 *2011 Global Fraud Survey*: Percent of Cases by Education Level

the study, as shown in Exhibit 1-12. Fraudsters with only a high school education caused median losses of $75,000, but that figure more than doubled for perpetrators who had a college degree. The median loss caused by those with postgraduate degrees was $300,000.

The Effect of Collusion It was not surprising to see that in cases involving more than one perpetrator, fraud losses rose substantially. The majority of survey cases

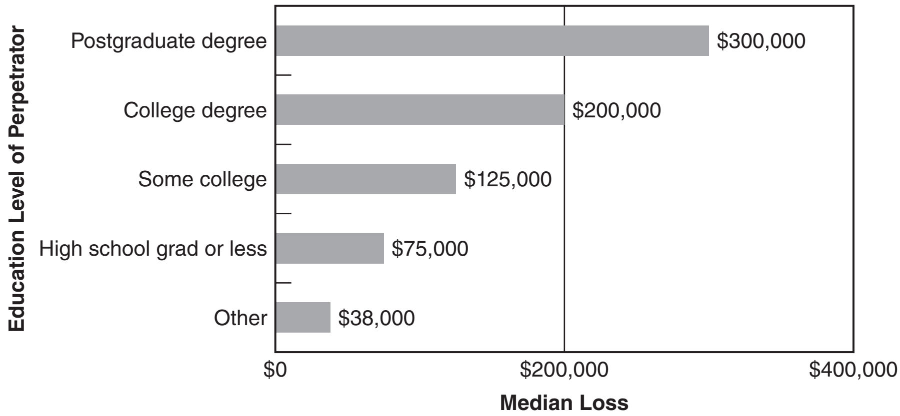

EXHIBIT 1-12 *2011 Global Fraud Survey*: Median Loss by Education Level

(58 percent) only involved a single perpetrator, but when two or more persons conspired, the median loss was two-and-a-half times as great (see Exhibits 1-13 and 1-14).

The Perpetrator's Department Of the fraud cases studied, 22 percent were perpetrated by an employee in the accounting department. Further, 77 percent of all the frauds were committed by employees in six departments: accounting, operations, sales, executive/upper management, customer service, and purchasing (see Exhibit 1-15). The perpetrators holding the highest levels of autonomy and authority inside the organization—those in executive/upper management roles—caused the greatest losses to the victim organizations, at $500,000 (see Exhibit 1-16).

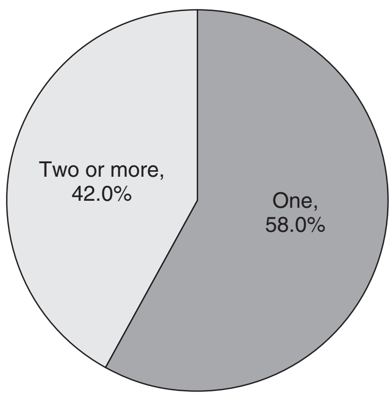

EXHIBIT 1-13 *2011 Global Fraud Survey*: Percent of Cases by Number of Perpetrators

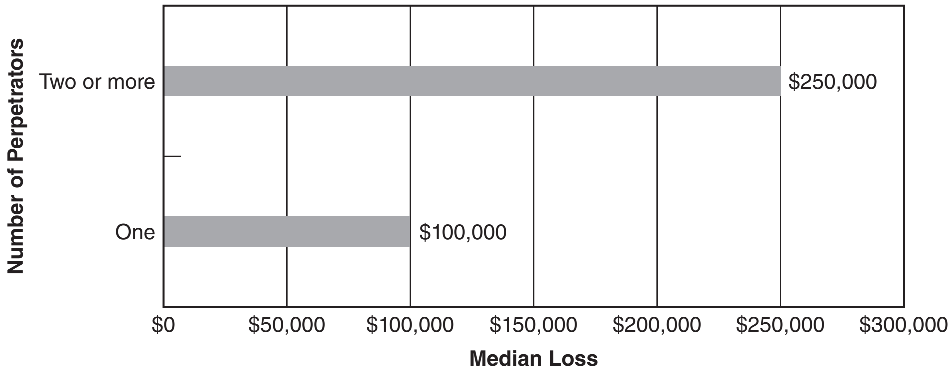

EXHIBIT 1-14 *2011 Global Fraud Survey*: Median Loss by Number of Perpetrators

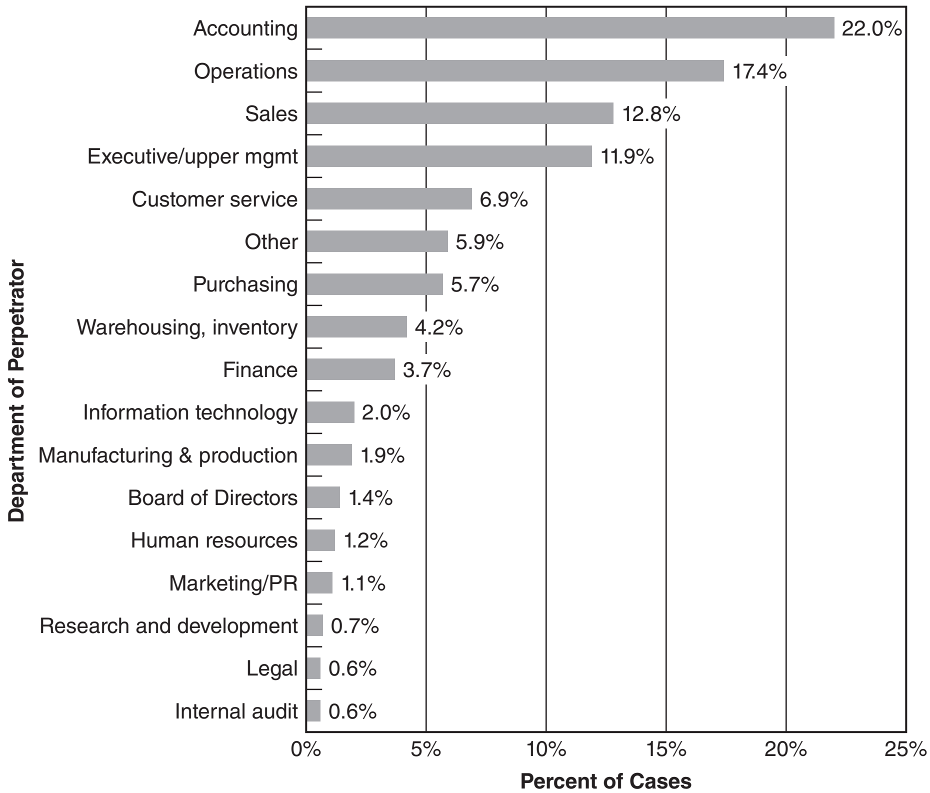

EXHIBIT 1-15 *2011 Global Fraud Survey*: Percent of Cases by Department of Perpetrator

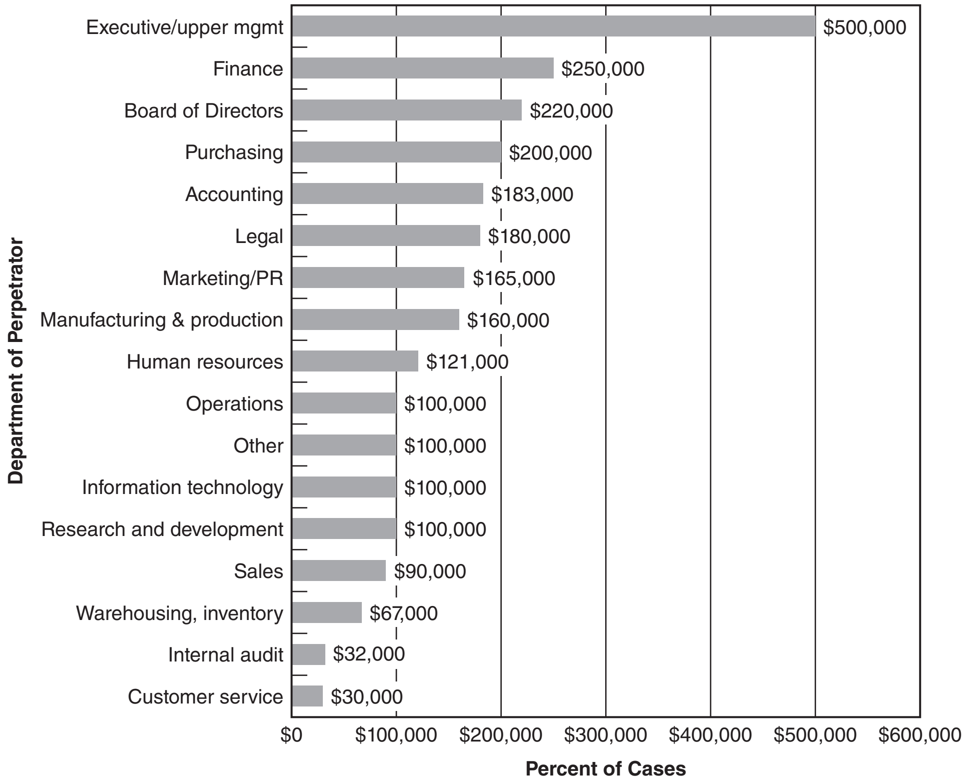

EXHIBIT 1-16 *2011 Global Fraud Survey*: Median Loss by Department of Perpetrator

The Effect of Tenure The results of the 2011 survey revealed a direct correlation between the length of time an employee had been employed by a victim organization and the size of the loss in the case. Employees who had been with the victim for ten years or more caused median losses of $229,000, whereas employees who had been with their employers for one year or less caused median losses of $25,000 (see Exhibit 1-17). Interestingly, Exhibit 1-18 shows that employees with tenure of one to five years were involved in the greatest percentage of fraud cases.

Criminal History of the Perpetrators Less than 6 percent of the perpetrators identified in the 2011 study were known to have been convicted of a previous fraud-related offense. Another 6 percent of the perpetrators had previously been charged, but had never been convicted. These figures are consistent with other studies that have shown that most people who commit occupational fraud are first-time offenders. The findings are also consistent with Cressey's model, in which occupational offenders do not perceive themselves as lawbreakers (see Exhibit 1-19).

The Victims The victims of occupational fraud are organizations who are defrauded by those they employ. The 2011 survey asked respondents to provide information on, among other things, the size and type of organizations that were victimized and the antifraud measures those organizations had in place at the time of the frauds.

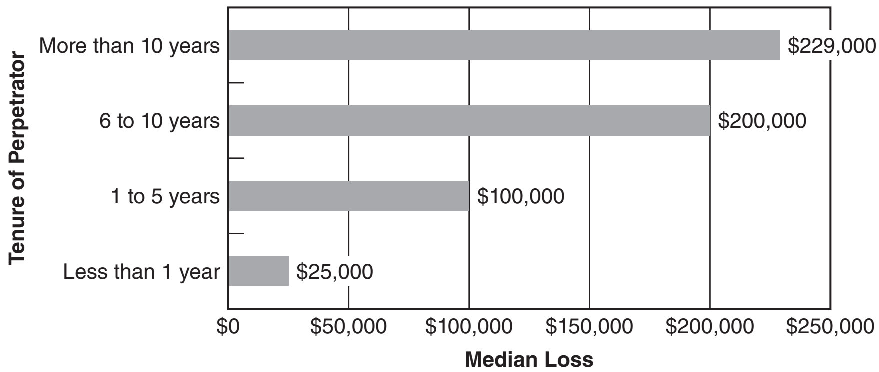

EXHIBIT 1-17 *2011 Global Fraud Survey*: Median Loss by Years of Tenure

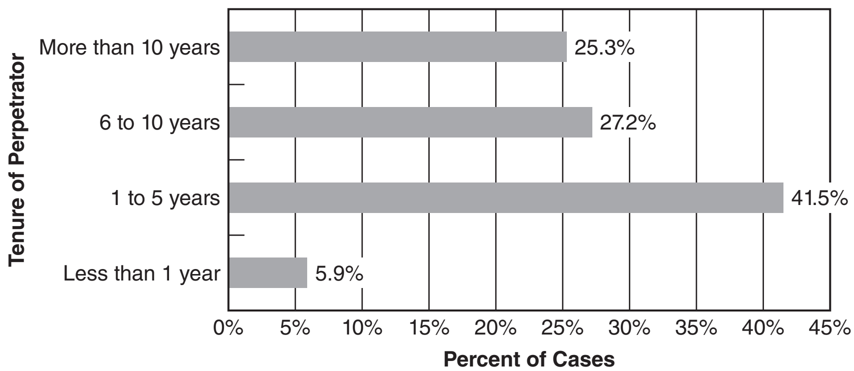

EXHIBIT 1-18 *2011 Global Fraud Survey*: Percent of Cases by Years of Tenure

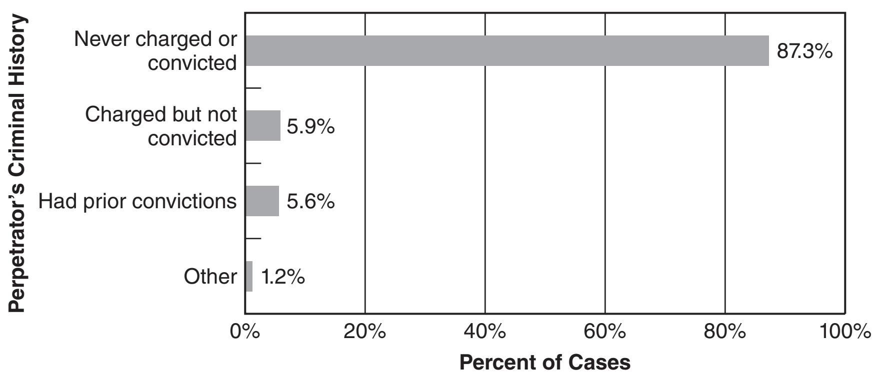

EXHIBIT 1-19 *2011 Global Fraud Survey*: Percent of Cases by Criminal History

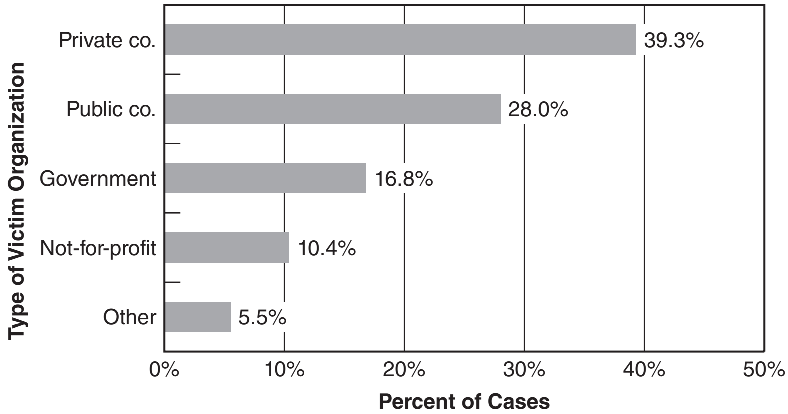

EXHIBIT 1-20 *2011 Global Fraud Survey*: Percent of Cases by Organization Type

Type of the Victim Organization Most of the cases reported in the *2011 Global Fraud Survey* involved victims that were privately held companies (39 percent), whereas not-for-profit organizations had the lowest representation (10 percent) (see Exhibit 1-20). It should be noted that researchers made no effort to obtain a random sample of business organizations. The *Report* was based on a survey of CFEs throughout the world; consequently, the demographics of the victim organizations in the study depended in large measure upon the organizations that retain CFEs.

The study revealed that privately held companies were not only the most heavily represented organization type, but they also suffered the largest median loss, at $200,000. In comparison, the median losses in public companies ($127,000), not-for-profit organizations ($100,000), and government agencies ($81,000) were notably lower (see Exhibit 1-21).

Size of the Victim Organization Exhibit 1-22 shows the breakdown of victim organizations in our study based on their size (as measured by the number of employees).

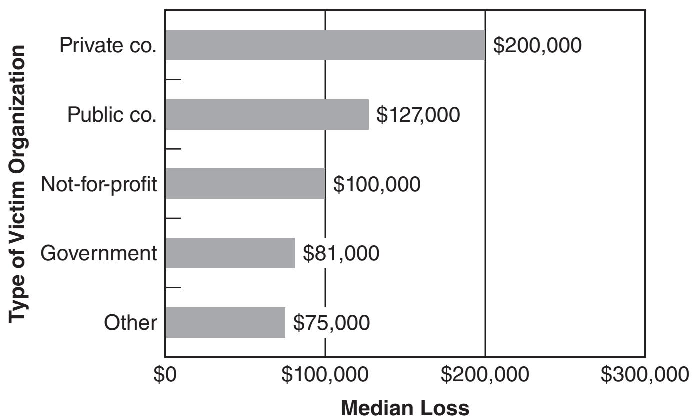

EXHIBIT 1-21 *2011 Global Fraud Survey*: Median Loss by Organization Type

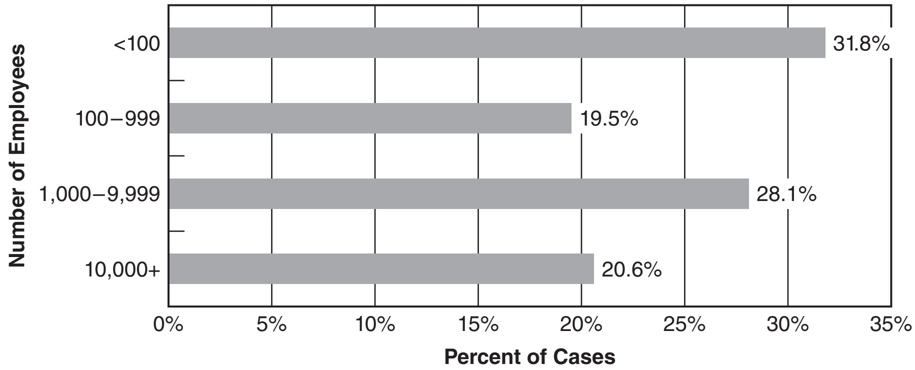

EXHIBIT 1-22 *2011 Global Fraud Survey*: Percent of Cases by Number of Employees

Over 31 percent of the cases in the study occurred in small organizations—those with fewer than 100 employees.

The two categories of the smallest organizations—those with fewer than 100 employees and those with 100 to 999 employees—experienced the largest median losses ($147,000 and $150,000, respectively), whereas organizations employing 1,000 to 9,999 had the lowest median loss ($100,000). Although the smallest organizations did not experience the largest median loss in absolute terms, the relative size of the median loss for small companies indicates that these entities are disproportionately vulnerable to occupational fraud and abuse. Put more simply, absorbing a $147,000 loss is typically a much bigger burden on a small company than absorbing a $140,000 loss is on an organization with 10,000 or more employees (see Exhibit 1-23).

Researchers theorize that the disproportionate nature of fraud losses at small companies exists for two reasons. First, smaller businesses have fewer divisions of responsibility, which means that fewer people must perform more functions. One of the most common types of fraud encountered in the ACFE studies involved small business operations that had a one-person accounting department—a single employee wrote checks, reconciled the

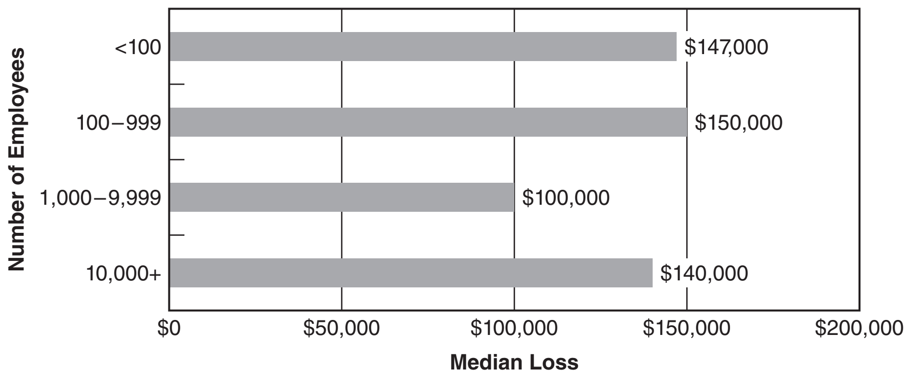

EXHIBIT 1-23 *2011 Global Fraud Survey*: Median Loss by Number of Employees

accounts, and posted the books. An entry-level accounting student could spot the internal control deficiencies in that scenario, but apparently many small business owners cannot, or simply do not.

Second, there is a greater degree of trust inherent in a situation in which everyone knows each other by name and face. Who of us would like to think our coworkers would, or do, commit these offenses? As a result, our defenses are naturally relaxed. There, again, is the dichotomy of fraud: It cannot occur without trust, but neither can commerce. Trust is an essential ingredient at all levels of business—we can and do make handshake deals every day. Transactions in capitalism simply cannot occur without trust. The key is seeking the right balance between too much trust and too little.

Antifraud Measures at the Victim Organization CFEs who participated in the *2011 Global Fraud Survey* were asked to identify which, if any, of sixteen common antifraud measures were utilized by the victim organizations at the time the reported frauds occurred. More than 80 percent of the victim organizations had their financial statements audited by external auditors, whereas 68 percent had dedicated internal audit or fraud examination departments, and the same percentage had independent audits of their internal controls over financial reporting. Additionally, 78 percent of the organizations had a formal code of conduct in place at the time of the fraud, though only 47 percent extended that to include a formal antifraud policy (see Exhibit 1-24).

To examine the effectiveness of these common antifraud controls, researchers also compared the median loss for those organizations that had a particular antifraud control in place against the median loss for those organizations without that control at the time of the fraud (excluding all other factors). The results indicate that the mechanisms most associated with a reduced cost of fraud were management review of internal

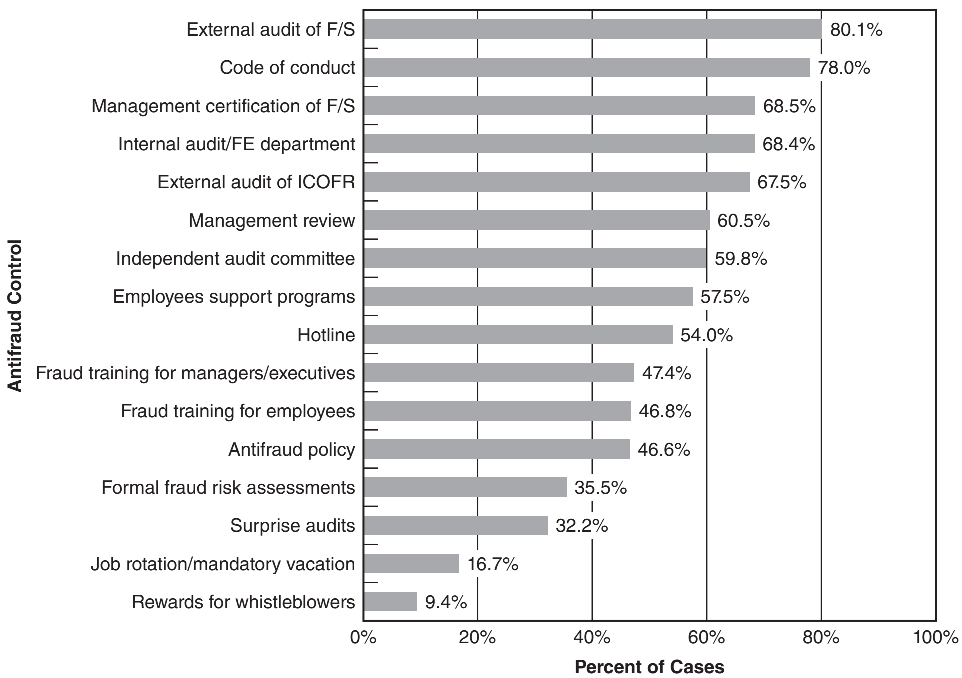

EXHIBIT 1-24 *2011 Global Fraud Survey*: Frequency of Antifraud Controls

Median Loss Based on Presence of Antifraud Controls				
Control	% of cases implemented	Yes	No	% Reduction
Management review	60.5%	$100,000	$185,000	45.9%
Employee support programs	57.5%	$100,000	$180,000	44.4%
Hotline	54.0%	$100,000	$180,000	44.4%
Fraud training for managers/ execs	47.4%	$100,000	$158,000	36.7%
External audit for ICOFR	67.5%	$120,000	$187,000	35.8%
Fraud training for employees	46.8%	$100,000	$155,000	35.5%
Antifraud policy	46.6%	$100,000	$150,000	33.3%
Formal fraud risk assessments	35.5%	$100,000	$150,000	33.3%
Internal audit/FE department	68.4%	$120,000	$180,000	33.3%
Job rotation/mandatory vacation	16.7%	$100,000	$150,000	33.3%
Surprise audits	32.2%	$100,000	$150,000	33.3%
Rewards for whistleblowers	9.4%	$100,000	$145,000	31.0%
Code of conduct	78.0%	$120,000	$164,000	26.8%
Independent audit committee	59.8%	$125,000	$150,000	16.7%
Mgmt certification of F/S	68.5%	$138,000	$164,000	15.9%
External audit of F/S	80.1%	$140,000	$145,000	3.4%

EXHIBIT 1-25 *2011 Global Fraud Survey*: Impact of Antifraud Controls on Median Loss

controls, processes, accounts, or transactions; employee support programs; and hotlines. Organizations with these mechanisms in place at the time of the fraud experienced frauds that cost 44 to 46 percent less than organizations that lacked these mechanisms. Conversely, external audits—the antifraud measure most commonly utilized by victim organizations—showed the lowest impact on median losses in the ACFE study (see Exhibit 1-25).

Detecting and Preventing Occupational Fraud

Initial Detection of Frauds The obvious question in a study of occupational fraud is: What can be done about it? Given that the ACFE study was based on actual fraud cases that had been investigated, researchers thought it would be instructional to ask how these frauds were initially detected by the victim organizations. Perhaps by studying how the victim organizations had uncovered fraud, researchers would be able to provide guidance to other organizations on how to tailor their fraud-detection efforts. Respondents were given a list of common detection methods and were asked how the frauds they investigated were initially detected. As illustrated in Exhibit 1-26, the frauds in the study were most commonly detected by tip (43 percent). Unfortunately, as shown earlier in Exhibit 1-24, 46 percent of fraud victims did not have established reporting structures in place at the time they were defrauded. It is also interesting—and rather disconcerting—to note that accident was the fourth-most common detection method, accounting for 7 percent of the fraud cases in the survey, while external audits detected approximately 3 percent of the reported frauds.

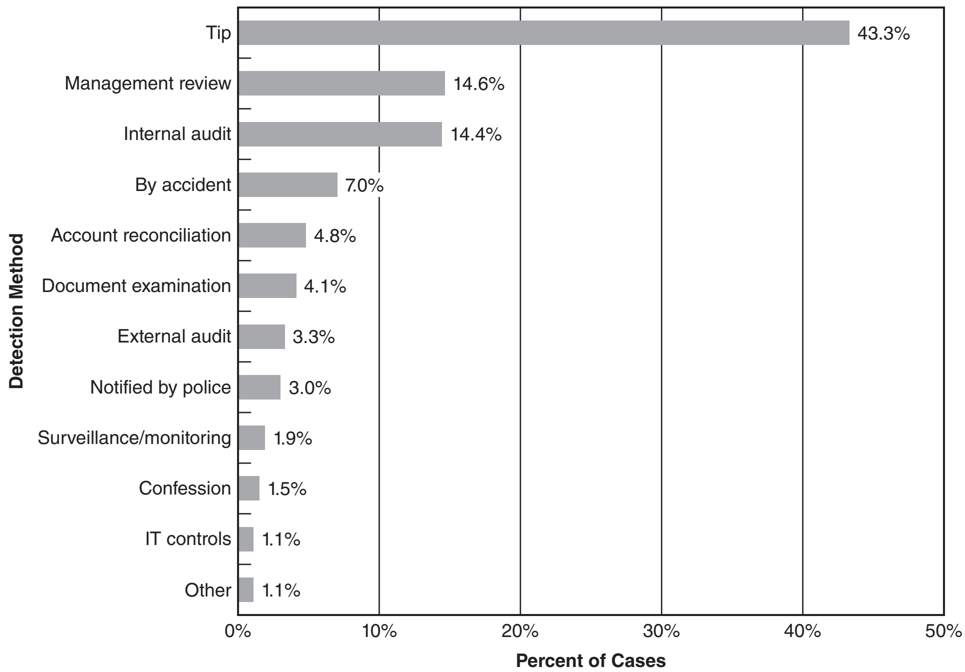

EXHIBIT 1-26 *2011 Global Fraud Survey*: Initial Detection of Occupational Fraud

The Methods The principal goal of the first *Report to the Nation* was to classify occupational frauds and abuses by the methods used to commit them. As a result of the 1996 study, researchers were able to develop a classification system known informally as the *fraud tree* (see page 2, Exhibit 1-1) that accounts for most, if not all, of the most common occupational fraud and abuse schemes. Researchers tested the structure of the fraud tree against the cases in all subsequent ACFE surveys to make sure that the classification system accounted for every scheme that was reported. Among the seven studies, ACFE researchers have applied the fraud tree classification system to thousands of cases of fraud and have found that it has covered them all.

By classifying and categorizing occupational frauds, the researchers are able to study these crimes in more detail. Instead of lumping every case under the general heading of "fraud," researchers observe discrete groups of frauds with similar characteristics in order to learn what methods are most commonly used to commit occupational fraud and what schemes tend to cause the biggest losses. Also, by comparing schemes in well-defined categories, researchers can identify common methods used by the perpetrators as well as common vulnerabilities in the victim organizations that allow such frauds to succeed. This, in turn, should help in the development of better, more efficient antifraud tools.

According to the fraud tree, there are three major categories of occupational fraud:

1. *Asset misappropriations*, which involve the theft or misuse of an organization's assets. (Common examples include skimming revenues, stealing inventory, and payroll fraud.)

	Percent of Cases[a]	Median Loss
Asset misappropriation	86.7%	$120,000
Corruption	33.4%	250,000
Financial statement fraud	7.6%	$1,000,000

[a]The sum of percentages listed in this column exceeds 100 percent because some cases involved fraud schemes that fell into more than one category. The same is true for every scheme classification chart in this book that is based on the *2011 Global Fraud Survey*.

EXHIBIT 1-27 *2011 Global Fraud Survey*: Major Occupational Fraud Categories

2. *Corruption*, in which fraudsters wrongfully use their influence in a business transaction in order to procure some benefit for themselves or another person, contrary to their duty to their employer or the rights of another. (Common examples include accepting kickbacks and entering into conflicts of interest.)
3. *Financial statement fraud*, which involves purposeful misreporting of financial information about the organization with the intent to mislead those who rely on it. (Common examples include overstating revenues and understating liabilities or expenses.)

The data from the study on frequency and median loss for the three major occupational fraud categories are presented in Exhibit 1-27 above. Asset misappropriations made up nearly 87 percent of the cases encountered but were by far the least costly in terms of median loss. Meanwhile, financial statement fraud schemes were the least common, accounting for less than 8 percent of cases, but they caused far greater harm, on average, than schemes in the other two categories. Corruption schemes were the "middle children" of the study; they were more common than fraudulent statements and more costly than asset misappropriations.

Within each of the three major categories there are several subcategories of fraud scheme types. In coming chapters we will address each of these subcategories in turn, looking at research on their costs and effects, identifying how the schemes are committed, and discussing how organizations can defend against them.

SUMMARY

This chapter defines the field of fraud examination, gives an overview of fraud and abuse, and points out the differences between the two terms. It also describes various criminological theories as to why "ordinary" people engage in these illegal behaviors. Included are Sutherland's *theory of differential association*, which argues that criminal behavior and attitudes toward crime are learned from family and peers; Cressey's *fraud triangle*, which explains fraud as a result of the conjunction of a nonshareable financial problem, perceived opportunity, and rationalization; Albrecht's *fraud scale*, which contends that committing fraud is the interaction of situational pressures, opportunities, and personal integrity; and the *Hollinger-Clark Study*, which hypothesizes that occupational fraud is primarily caused by workplace dissatisfaction. The chapter concludes by providing the resulting data from the Association of Certified Fraud Examiners' *2011 Global Fraud Survey*, which demonstrates that losses from fraud are affected by such factors as the perpetrator's position and tenure, the size of the victim organization, and the antifraud controls that the victim had in place at the time of the fraud.

ESSENTIAL TERMS

Fraud examination A process of resolving allegations of fraud from inception to disposition. It involves not only financial analysis, but also taking statements, interviewing witnesses, writing reports, testifying to findings, and assisting in the detection and prevention of fraud.

Fraud theory approach The methodology used to investigate allegations of fraud. It involves developing a theory based on a worst-case scenario of what fraud scheme could have occurred, then testing the theory to see if it is correct.

Occupational fraud and abuse The use of one's occupation for personal enrichment through the deliberate misuse or misapplication of the employing organization's resources or assets.

Fraud Any crime for gain that uses deception as its principal modus operandi. There are four legal elements that must be present: (1) a material false statement, (2) knowledge that the statement was false when it was uttered, (3) reliance on the false statement by the victim, and (4) damages as a result.

Abuse Petty crimes committed against organizations, such as taking excessively long lunch hours or breaks, coming to work late or leaving early, using sick time when not sick, and pilfering supplies or products.

Fiduciary relationship In business, the trusting relationship that the employee is expected to hold toward the employer, requiring the employee's scrupulous good faith to act in the employer's best interests.

Conversion The unauthorized assumption of a right of ownership over the goods of another to the exclusion of the owner's rights. When an employee steals company assets, he is converting the use of them.

Larceny The unlawful taking and carrying away of property of another with the intent to convert it to one's own use.

White-collar crime Coined by Edwin Sutherland, originally defined as criminal acts only of corporations and of individuals acting in their corporate capacity (e.g., management fraud or crime), but now used to define almost any financial or economic crime.

Fraud triangle A model developed to explain the research of Cressey, who noted that most occupational frauds were caused by a combination of three elements: nonshareable financial problems, perceived opportunity, and the ability to rationalize conduct.

Nonshareable problems Financial difficulties that would be hard for a potential occupational offender to disclose to outsiders, such as excessive debt, gambling, drug use, business reversals, or extramarital affairs.

Rationalization The thought process by which an occupational fraudster explains and justifies his illegal conduct. Examples include: "I was only borrowing the money," "the company doesn't treat me fairly," and "I must commit financial statement fraud because, otherwise, employees will lose their jobs."

Employee deviance Conduct by employees that is detrimental to both employer and employee, such as goldbricking, work slowdown, and industrial sabotage.

Organizational controls Deterrence mechanisms used by organizations to discourage employee deviance and fraud; includes company policies, selection of personnel, inventory control, security, and punishment.

Social controls Informal deterrence mechanisms that help discourage employee deviance and fraud, such as loss of prestige and embarrassment of friends and family.

REVIEW QUESTIONS

1-1 (Learning objective 1-1) What is fraud examination?

1-2 (Learning objective 1-2) What is the fraud theory approach?

1-3 (Learning objective 1-3) Occupational fraud and abuse includes any personal enrichment that results from misuse or misapplication of the employing organization's resources or assets. There are four key elements to this activity. What are they?

1-4 (Learning objective 1-4) Under the common law, fraud generally consists of four elements, all of which must be present. List them.

1-5 (Learning objectives 1-4 and 1-5) What is the difference between occupational fraud and occupational abuse? Give examples.

1-6 (Learning objective 1-7) Edwin H. Sutherland, a criminologist, coined the phrase "white-collar crime." What did he mean by this term? How has the meaning of this phrase changed over time?

1-7 (Learning objective 1-7) Sutherland developed what is known as the "theory of differential association." What is the principal tenet of his theory?

1-8 (Learning objective 1-8) Cressey interviewed nearly 200 embezzlers in order to develop his theory on the causation of fraud. As a result of his research, what was Cressey's final hypothesis?

1-9 (Learning objective 1-9) Cressey believed that nonshareable problems provide the motivation for employees to commit occupational fraud. What did he mean by "nonshareable"?

1-10 (Learning objective 1-9) Cressey divided the nonshareable problems of the subjects in his research into six different subtypes. What are they?

1-11 (Learning objective 1-11) Albrecht concluded that three factors lead to occupational fraud. What are they?

1-12 (Learning objective 1-12) What factor did Hollinger and Clark identify as the primary cause of employee deviance?

1-13 (Learning objective 1-13) The *2011 Global Fraud Survey* covered a number of factors that are related to occupational fraud. List these factors.

DISCUSSION ISSUES

1-1 (Learning objective 1-1) How does "fraud examination" differ from "forensic accounting"?

1-2 (Learning objective 1-2) There are several steps involved in the fraud theory approach. What are they?

1-3 (Learning objectives 1-3 through 1-6) How does occupational fraud and abuse differ from other kinds of fraud? Give examples of other fraud types.

1-4 (Learning objectives 1-7 and 1-8) How does the study of criminology relate to the detection or deterrence of fraud? How does it differ from the study of accounting or auditing?

1-5 (Learning objective 1-7) Sutherland's contribution to criminology, in addition to giving us the term "white-collar crime," involved developing the theory of differential association. What are the implications of this theory with respect to occupational fraud?

1-6 (Learning objective 1-8) Cressey's "fraud triangle" states that three factors—nonshareable financial need, perceived opportunity, and rationalization—are present in cases of occupational fraud. Which of these three factors, if any, is most important in causing executives, managers, and employees to commit occupational fraud?

1-7 (Learning objectives 1-8 and 1-9) Cressey described a number of nonshareable financial problems that he uncovered during his research. Which of these, if any, apply to modern-day executives who are responsible for large financial statement frauds? In the fifty-plus years since Cressey did his study, are the factors he described still valid? Why, or why not?

1-8 (Learning objectives 1-8 through 1-11) Albrecht, in his research, developed the "fraud scale" and furnished a list of the reasons employees and executives commit occupational fraud. How are Albrecht's conclusions similar to Cressey's? How are they different?

1-9 (Learning objective 1-13) The ACFE's *2011 Global Fraud Survey* found that, among other things, the frauds committed by women resulted in smaller median losses than those committed by men. What are some possible reasons for this finding?

ENDNOTES

1. The Association of Certified Fraud Examiners, *Report to the Nation on Occupational Fraud and Abuse* (Austin, TX: ACFE, p. 4. 1996).
2. The Association of Certified Fraud Examiners, p. 9.
3. Henry Campbell Black, *Black's Law Dictionary*, 5th ed. (St. Paul, MN: West Publishing, 1979), p. 792.
4. *Merriam-Webster's Collegiate Dictionary*, 11th ed. (Merriam-Webster, Incorporated, 2008), p. 321.
5. A tort is a civil injury or wrongdoing. Torts are not crimes; they are causes of action brought by private individuals in civil courts. Instead of seeking to have the perpetrator incarcerated or fined, as would happen in a criminal case, the plaintiff in a tort case generally seeks to have the defendant pay monetary damages to repair the harm he has caused.
6. *Black's*, p. 300.
7. *Black's*, p. 468.
8. *Black's*, 6th ed., p. 563.
9. Gilbert Geis, *On White Collar Crime* (Lexington: Lexington Books, 1982).
10. *Merriam-Webster's*, p. 6.
11. Larry J. Siegel, *Criminology*, 3rd ed. (New York: West Publishing, 1989), p. 193.
12. Donald R. Cressey, *Other People's Money* (Montclair: Patterson Smith, 1973), p. 30.
13. Cressey, p. 33.
14. Cressey, p. 34.
15. Cressey, p. 34.
16. Cressey, p. 35.
17. Cressey, p. 36.
18. Cressey, p. 36.
19. Cressey, p. 42.
20. Cressey, p. 42.
21. Cressey, p. 47.
22. Cressey, p. 48.
23. Cressey, pp. 52–53.

24. Cressey, p. 54.
25. Cressey, p. 57.
26. Cressey, p. 66.
27. Cressey, p. 84.
28. Cressey, p. 84.
29. Cressey, p. 85
30. Cressey, pp. 94–95.
31. Cressey, p. 93.
32. Cressey, pp. 101–102.
33. Cressey, p. 102.
34. Cressey, p. 102.
35. Cressey, pp. 120–121.
36. Cressey, p. 121.
37. Cressey, p. 122.
38. Cressey, p. 121.
39. Cressey, p. 122.
40. Cressey, p. 128.
41. Cressey, p. 129.
42. Cressey, pp. 128–129.
43. Cressey, p. 133.
44. Cressey, p. 139.
45. W. Steve Albrecht, Keith R. Howe, and Marshall B. Romney, *Deterring Fraud: The Internal Auditor's Perspective* (Altamonte Springs, FL: The Institute of Internal Auditor's Research Foundation, 1984).
46. Although such red flags may be present in many occupational fraud cases, Albrecht's caution must be reemphasized: perpetrators are hard to profile, and fraud is difficult to predict. To underscore this point, Albrecht's research does not address—nor does any current research—whether nonoffenders have many of the same characteristics. If so, then the list may not be discriminating enough to be useful. In short, though one should be mindful of potential red flags, they should not receive undue attention in the absence of other compelling circumstances.
47. Albrecht, pp. 13–14.
48. Albrecht, p. 32.
49. Albrecht, p. 39
50. Albrecht, p. 5.
51. Albrecht, p. 6.
52. Albrecht, p. 5.
53. Albrecht, p. 5.
54. Albrecht, p. 6.
55. Albrecht, p. 42.
56. Albrecht, p. xv.
57. Richard C. Hollinger and John P. Clark, *Theft by Employees* (Lexington: Lexington Books, 1983), p. 6.
58. Hollinger and Clark, p. 42.
59. Hollinger and Clark, p. 57.
60. Hollinger and Clark, p. 57.
61. Hollinger and Clark, p. 57.
62. Hollinger and Clark, p. 63.
63. Hollinger and Clark, p. 68.
64. Hollinger and Clark, p. 77.
65. Hollinger and Clark, p. 86.
66. Hollinger and Clark, p. 86.
67. Hollinger and Clark, p. 86.
68. Hollinger and Clark, p. 106.
69. Hollinger and Clark, p. 117.
70. Hollinger and Clark, p. 120.
71. Hollinger and Clark, p. 121.
72. Hollinger and Clark, p. 144.
73. Hollinger and Clark, p. 146.
74. United States Central Intelligence Agency, *The World Factbook* (https://www.cia.gov/library/publications/theworld-factbook/geos/xx.html).
75. Albrecht, p. 5.