



INFORMATION MEMO

Safeguarding Your City Against Employee Theft

City staff and elected officials have a responsibility to protect city assets because they are publicly funded. Find out how to safeguard city assets through awareness of the “Fraud Triangle,” that place where opportunity, financial pressure and rationalization intersect. Learn the elements of the triangle and common procedures you can implement to reduce employee theft.

RELEVANT LINKS:



I. Employee theft in Minnesota cities

Many people downplay the idea of employee theft saying, “It could never happen in my city.” Why could it not happen in your city? The unfortunate truth is that employee theft is not uncommon in Minnesota cities.

II. Fraud triangle

Understanding the ways in which employees may steal from the city can help to prevent and discover employee theft. Famed sociologist and criminologist Donald Cressey developed the “fraud triangle” to explain why people commit theft. The three key elements in the fraud triangle are opportunity, financial pressure, and rationalization. Cities can prevent theft by working on the portion of the fraud triangle over which they have the most control: the opportunity to commit theft.

A. Opportunity

Opportunity is the element over which cities have the most control. Limiting opportunities for employee theft is one way to reduce it. The opportunity to commit theft is possible when employees have access to assets and information that allows them to commit and conceal the theft.

This material is provided as general information and is not a substitute for legal advice. Consult your attorney for advice concerning specific situations.

B. Financial pressure

Financial pressure comes from a “non-shareable” financial problem that cannot be shared or solved in a legitimate manner. It may be a home foreclosure, medical bills, or a drug or gambling addiction. Non-shareable problems often involve some sort of embarrassment or shame. Financial pressure also may be perceived – a person may have a desire for material goods to impress others, but doesn’t have the means to get them.

C. Rationalization

Rationalization lets employees justify the crime in a way that makes it acceptable or justifiable to themselves. They may say they were “borrowing” money, felt entitled to it, had to look after family, or felt they were underpaid and therefore deserved it. It may be difficult for management to do anything about an employee’s needs or rationalizations, but by limiting opportunities for theft, the city can reduce it to some extent.

III. Who commits theft

You can never be sure who might embezzle city funds, even long-standing, trusted employees with sterling reputations sometimes steal. Most people who commit theft against their employer are not career criminals. The vast majority are trusted staff who have no criminal history and don't even consider themselves lawbreakers.

Cressey says most employees who steal are first-time offenders with no criminal record. They see themselves as ordinary, honest people caught in a bad situation.

Since a thief can be anyone, cities should exercise something accountants like to call “professional skepticism.” Basically, cities should always consider any coworker or boss capable of committing theft. This does not mean that you should constantly be suspicious of everything employees do, but it does mean that you should not trick yourself into thinking someone would never steal.

IV. Procedures to reduce risk of theft

The best way to reduce employee theft is to take away the opportunity for employees to commit theft. There are three key ways to reduce opportunity.

RELEVANT LINKS:

State Auditor Statement of Position,
[The Importance of Internal Controls.](#)

State Auditor Statement of Position,
[Internal Controls for Municipal Liquor Stores.](#)

A. Segregation of duties

Segregation of duties means all the responsibility for a given function does not rest with one individual. Not only does segregating duties protect the city, but it also protects employees. If a mistake is made, it is less likely to be deemed intentional where there is segregation of duties. Accordingly, an honest mistake is not likely to be construed as an employee trying to steal from the city.

Functions related to the handling of funds should be distributed among as many people as possible to reduce the risk that one person may successfully divert funds. For example, when looking at city utilities, one person should be responsible for preparing and sending utility bills and another person should be responsible for recording payments and reconciling bills with collections. A third person should maintain custody over the funds and deposit the collections in the city's account.

In small cities where staff is limited, it is certainly more difficult to segregate duties. Nevertheless, cities should make an effort to segregate some duties. One idea is to involve city council members in segregation of duties. For example, a city council member may be able to make daily deposits with the bank or to reconcile monthly bank statements.

B. Internal controls

The most important aspects of internal controls are well-trained employees and careful establishment of an audit trail to provide physical evidence of each transaction. Some simple internal control procedures include the following:

- Require checks be written to the city, not city employees.
- Endorse checks for deposit as they are received.
- Keep paper checks under lock and key.
- Make daily deposits.
- Reconcile receipts with deposits.
- Reconcile bank statements monthly; should be done by someone not involved in receiving and depositing funds.
- Reference approved claims and amounts in the city council meeting minutes.
- Contact city's bank to prohibit cash withdrawals and check cashing.
- Do not allow fund transfers without a city resolution.
- Do not pre-sign checks.

RELEVANT LINKS:

[Minn. Stat. § 609.456.](#)

LMC information memo, [LMCIT Property, Crime, Bond, and Petrofund Coverage Guide](#), Section VI-A, Bond coverage.

- Require detailed original receipts for reimbursement of employee expenses; do not allow photocopies.
- Obtain cancelled checks or obtain optical images of checks.
- Require a supervisor review voids and over-rings.

Cash represents the greatest risk of loss requiring additional internal controls. The following cash controls will help protect the city's funds:

- Maintain written guidelines for handling cash.
- All forms and receipts should be pre-numbered in consecutive order.
- Pre-numbered forms should not be printed in-house.
- More than one person should be present when cash is collected.
- Rotate persons collecting cash.
- No cash collections should be given to another person without a receipt.

C. Environment of accountability

It is important that cities create an environment of accountability. This means not only creating internal control procedures, but requiring that everyone follow them—no exceptions. Management must lead by example. Remember, it is the public's money and city officials and employees have a duty to safeguard city assets.

V. Suspicion of theft

State law requires that whenever a public employee or public officer of a city discovers evidence of theft, embezzlement, unlawful use of public funds or property, or misuse of public funds by any person authorized to expend public funds, the employee or officer shall promptly report such evidence to law enforcement and shall promptly report in writing to the state auditor a detailed description of the alleged incident.

VI. LMCIT bond coverage

LMCIT offers public employee bond coverage as part of the overall package of coverage for cities. The minimum bond coverage available is \$50,000 and limits up to \$1,000,000 are available. The LMCIT bond coverage forms are specifically designed to meet the needs and requirements of Minnesota cities. Coverage for a city's relief association is included as a standard feature of the city's bond coverage.

RELEVANT LINKS:

Minnesota State Auditor, [Report a Concern](#).

Other city-related organizations such as EDAs, port authorities, and HRAs can also be included under the city's bond coverage.

All LMCIT bond coverage is written on a blanket faithful performance basis. This means the city is protected from an employee stealing the city's money as well as the risk that the employee might steal someone else's money. Besides covering dishonesty, LMCIT bond coverage also covers losses that result from other ways employees might fail to faithfully perform their duties.

VII. Further assistance

For more information on reporting employee theft, consult your city attorney or the Minnesota State Auditor's Office.