



### **SAME SONG SECOND VERSE**

A couple of years ago BancInsure paid a fidelity claim involving the “head bookkeeper” for a bank. She was a long time employee of the bank and was very knowledgeable of the bank’s customers. She began transferring funds from various customers’ checking accounts to her own account by the use of internal debit and credit memos and using the funds for her own personal use. She would utilize accounts, generally of elderly customers, that she knew statements were not being mailed to the customers or she would intercept the statements before they could be mailed to them. On occasion she would use a counter check made out as though it was being drawn on her checking account, but she would MICR encode the check with the account number for one of the accounts she was utilizing to perpetuate her fraud. When the check was processed, naturally it posted to the account of the MICR encoded number and not the head bookkeeper’s account. The scheme continued for several years until one day a customer received a statement that contained an unauthorized transaction. The customer came to the bank to inquire as to the nature of the transaction. The head bookkeeper was not in the bank. The bank officer responding to the inquiry called the head bookkeeper at home and she confessed to the embezzlement.

At the time of discovery the embezzlement was over \$238,000. The bank was able to recover approximately \$55,000 from the head bookkeeper. After the application of the bank’s deductible, BancInsure paid approximately \$158,000 for the loss. Because the bank had purchased claims expense coverage, BancInsure reimbursed the bank an additional \$16,500 for their expenses of documenting their loss.

There is nothing unique about the situation described above. Similar embezzlements have happen before and will happen again, if proper internal controls are not in place. However, this true story re-enforces the need for sufficient fidelity coverage with an appropriate deductible and proper internal controls. In addition the bank had wisely purchased claims expense coverage. Employee embezzlements that have been on going for several years can be very time consuming and expensive to investigate. Often times, as in this case, it requires the hiring of outside accountants or consultants. BancInsure’s Claim Expense Rider provides coverage for reasonable expenses incurred in preparing a covered fidelity claim subject to its terms and conditions of the bond.

While the bank had sufficient fidelity coverage with an apparently appropriate deductible, the internal controls were lacking.

Some of the internal controls to consider are:

1. The use of internal debit and credit memos should require supervisory review and approval.
2. Access to MICR encoding equipment should be limited.
3. All entries to customer accounts other than computer generated entries (interest calculations, etc.) should flow through a teller window. Tellers should not process their own transactions.
4. Account statements on all accounts should be mailed periodically.
5. Employees should be required to be absent from the bank for two continuous weeks each year.
6. Bank should consider review of employee accounts by the internal audit department or other independent persons for unusual activity. (Be careful of privacy concerns.)

These and possibly other internal control methods or procedures will assist your bank in avoiding situations similar to the one described above.

We trust that these comments have been helpful.

BancInsure has become a leading writer of Financial Institution Bonds in the United States by providing a sound, stable market, excellent service and fair claims treatment. If you would like to learn more about BancInsure's Financial Institution Bond or other coverages, please contact your BancInsure marketing representative.