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## Employee Fraud - A Breach of Trust!

The petty cash box was left unlocked. Everyone who had access to the business premises was trusted. There was no sign of a break in to the business premises, but by Monday \$400 which was only put into the petty cash box the previous Friday was gone.

Every year millions of dollars are lost by businesses throughout New Zealand because of employee theft, especially in small businesses. Most employers are unsuspecting, and in the past have usually placed a lot of trust on the employee who committed fraud. There are many factors that increase the risk of employee fraud and there are signs to look for.

Fraud is committed when employees believe there is minimal risk of their actions being discovered. Common advice when attempting to prevent fraud is to share tasks between employees and have adequate supervision from other staff members. It is the employee who solely manages accounts and the reconciling and balancing of bank statements, those who generate invoices and then approve them, who write cheques and sign them themselves and those who submit orders and handle the shipping who are more likely to take a chance at committing fraud undetected. Employees realise when they are considered trustworthy, and some employees choose to take advantage of this - taking advantage of people who are unsuspecting.

There are several methods that employees tend to use when committing fraud. A common one is for an employee to create a fake creditor, and generate 'invoices' from that creditor to their company. The employee will 'pay' the invoice from the company's funds, but pocket the cheque themselves. Another method is when an employee has an agreement with the creditor, who charges the company a higher price, but then reimburses the employee a percentage of that. Theft can also occur when clients pay in cash, and an employee pockets some of the money. Employees who steal equipment or inventory tend to take advantage of low security systems and come in to the workplace after hours.

Employers can also take secondary actions to help eliminate fraud. Having external auditors review accounts and criminal screening or credit checking potential employees sends a message to staff that employers are aware of the potential risk of fraud and that it will not be tolerated. Being trustworthy and showing integrity

themselves, creating a fair workplace and rewarding positive behaviour are all other obvious ways to discourage employees from acting dishonestly. Trust is a two way street, and employees can decide to 'give what they get' - if they feel they are being treated unfairly or cheated of a better wage by their employer. Fair employment practices and positive employee recognition will deter fraudulent behaviour.

There are behaviours and actions that can show that an employee is committing fraud. Arriving to work early and leaving late, not accepting help and not taking leave are signs of a person who is protective about their responsibilities and potentially fears being discovered. An unexplained increase in an employee's living standards may also be suspicious. Research indicates that fraud is most commonly committed by employees under 35 years of age, who have been with a company for more than 3 years and are in a position of trust.

There are many reasons that employees turn into thieves. Financial pressures, greed, thinking that taking money secretly and repaying it later is acceptable, arguing that the business doesn't need the money and thinking their boss owes them more than what they are getting. However unjustifiable, many employees experience financial pressures, and when adequate steps have not been taken by the business to protect their assets, temptation can become too great for an employee to resist.

Revealing theft usually happens by accident, or by another employee discovering it and bringing it to the attention of the employer. It usually takes about 18 months for theft to be discovered.

Pilfering, larceny and embezzlement of money are not the only type of employee fraud. Wasting an employer's time by arriving late, working slowly, taking extended lunch breaks, making use of unentitled benefits, taking sick leave when not sick are all examples of stealing from a company, and should be treated as seriously as monetary theft.

When an employer discovers that fraud has taken place, their lawyer or accountant should be the first port of call. Accusing an employee who turns out to be innocent could make the company liable for defamation. Lawyers assist you in notifying the authorities at the appropriate time, and accountants can arrange for forensics to examine company books to discover the thief and confirm the value of stolen goods.

# Taking 'Emergency Action' in the Context of a Business Turnaround

“The opportunities will be defined very largely by the circumstances of the individual business and the imagination of those trying to turn it around. As we said in relation to management change, there is no “one size fits all”.”



With Thanks to Nigel Foster, Armillary Management Limited  
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This is the fourth article in this series.

Our news has recently been peppered with stories of emergencies, often in the wake of a natural disaster - earthquake, tsunami, flood. Perhaps, against

the backdrop of these often dramatic and tragic events the words "emergency action" seem excessive in the more placid business environment.

However, these words are part of the common vocabulary of the business turnaround arena. Even if a little dramatic, they do appropriately convey the sense of urgency that needs to be brought to fixing things as quickly as possible in the early stages of a turnaround.

The analysis phase may, hopefully, have identified some areas where changes could be quickly introduced to get some quick wins-early financial benefits.

- Such opportunities for emergency action could come from a wide range of areas:
- plant closure/location rationalisation (perhaps limited to larger businesses);
- management/staff reductions;
- other (non-staff) areas of cost reduction;
- rent concessions from landlords;
- entering into informal/formalised arrangements with creditors (possibly including IRD).

The opportunities will be defined very largely by the circumstances of the individual business and the imagination of those trying to turn it around. As we said in relation to management change, there is no "one size fits all".

Irrespective though of the wide range of emergency actions that might be considered, there are some important principles that should be consistently applied to their implementation:

- Treat them as a package and announce them as a package so that stakeholders understand what is being done and are prevented from wondering "when is this all going to end?"
- Consider carefully how they are going to be presented to affected parties, stakeholders and the broader audience who will inevitably get to know about them;
- Present them positively, acknowledging their negative impact on affected parties but focusing on their necessity in the creation of a more robust foundation for the future;
- Implement them with dignity and authority;
- Implement them as quickly as possible (consistent with dignity) and move on. In short, minimise the period of chaos.

Similarly to management change, deciding on and implementing emergency action, is not easy. But it can be vital both in achieving quick wins and proving to key stakeholders ("the banker") that you are serious about turning this business around.

## Tax Simplification?

When GST was introduced, it was initially described as a simple tax. A full GST claim was made for goods purchased with the sole purpose of making taxable supplies, and private use adjustments were made if the goods were used partially for personal use. However, since 1 April 2011, there have been some changes in regards to goods purchased (other than land) for partial personal use. The initial GST claim is based on the percentage of estimated business use. Instead of one adjustment being made, various adjustments must be made depending on the amount and also on the percentage of personal use (if greater than 10% of the actual use, unless the adjustment is greater than \$1,000).

Cost	Number of adjustments
\$1,000 - \$5,000	0
\$5,001 - 10,000	2
\$10,001 - \$500,000	5
\$500,001 +	10

We see this as a major headache for annual reconciliations and GST audits. Another major change is that assets purchased before 1 April 2011, and later introduced into the business cannot be used to claim GST. However, if it asset was purchased after 1 April 2011 then GST can be claimed on it. You have to wonder who dreams these things up.

So is tax simplification a thing of the past? It flies in the face of what is publically said by IRD about simplification.

## Unit Titles Regulations 2011

The Unit Titles Regulations come into effect on 20 June 2011. Bodies Corporate need to ensure their rules are in compliance with the Regulations within the next 15 months and that they can offer new owners compliance with the new requirements.

Some areas that will affect Bodies Corporate are:

- Requirement to keep a register of unit owners, including their preferred method of contact.
- When calling meetings, a notice of intent to call the meeting needs to be circulated prior to a notice of the meeting.
- Chairpersons and members of the committee need to be unit owners.
- Bodies Corporate must have, and review at 3 yearly intervals, a maintenance plan. Each item on the plan must include an estimated cost and duration.
- New owners must be provided with information about the Body Corporate, including information regarding the financial position and levies. Potential owners may investigate whether the property has been subject to a claim under the Weathertight Homes Resolution Services Act 2006.
- Potential new owners can request an additional disclosure statement, seeking for detailed information regarding contracts entered into by the Body Corporate, the rules and recent and future maintenance. This will require Bodies Corporate to have up to date records.

## Forestry Emissions Trading Scheme (ETS)

The time is fast approaching where the ETS will come into force for land owners of forestry. This is mandatory for all forests (excluding indigenous forests) originally planted prior to 1990, (known as pre-1990 forests). The cutoff date for applications of carbon credits for pre-

1990 forests is 30 September 2011 with allocations being made 30 November 2011. Forests planted after 1989 (post -1989) may voluntarily participate. If you are a landowner of any forests and are unsure what to do, please contact us.

## Business Interruptions ('BI') Insurance Claims

Your BI cover and the extent of it, will depend on your policy wording. Cover may be extended to include prevention of access to the premises (for example as happened with the red zone in Christchurch) and may include loss caused by the interruptions to supplied goods and services.

Importantly, hopefully the policy is not subject to exclusions such as loss arising from property damage caused by natural disasters including earthquakes! Often, the cover may not include the financial loss arising from the general decline and demand following an earthquake. And that may have a critical affect on your business.

So what your BI policy provides is extremely important to how well you will be recompensed after any claim.

The indemnity period provided for in the policy begins from the date of what caused the claim and ends when the business is back fully operating or when the indemnity period has expired, whichever is the sooner.

The policy probably requires the business premises or either property to be damaged although the business interruption may be covered by some extension. After the

Christchurch experience it seems important to ensure that your policy includes, if your insurance underwriter, extensions involving:

- Prevention of access to the business premises, including premises which are inside some exclusion zone.
- Interruption or loss of the supplies of goods and services such as electricity and water.
- Interruption caused by the damage to the premises belonging to your supplier and customers. In other words, your premises and business may have come through an earthquake unscathed, but others on which your rely may not be so lucky.

We have heard of situations where the cover with the extensions may be limited to a percentage of the total sum insured.

This is very much a specialised area, but the days of simply accepting your insurance policy without properly reading it through in detail or thinking about the situations in which business interruption could happen and the extent to which your policy will or will not cover you has become (as it always was of course) an extremely important aspect. Take good advice!

“The Unit  
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Bodies  
Corporate  
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with the  
Regulations  
within the  
next 15  
months.”



# Qualifying Company Reforms - New look-through company rules; "shareholder employees" and "working owners" are not necessarily the same

“As of April 2011, your level of entitlement to Working for Families Tax Credits may be affected.”

Previously two shareholders in a QC (qualifying company) owned equal amounts of shares, but only one of them performed services for the company. The shareholder employee can receive his or her salary without deducting PAYE (assuming tax compliance).

It is important when considering the LTC (Look Through Company) regime to realise that tax outcomes are different for 'shareholder employees' and 'working owners'. A worker owner is:

a) An owner of the LTC

b) Someone who is employed through a contract of employment (in writing - specifying terms, conditions and salary) by the company to carry out business related tasks

However, if this company is now a LTC, a shareholder who performed services under a contract - a 'working owner' - must have PAYE deducted from their salary. That is not allowed for a shareholder employee, who is not a working owner. This new rule could be hard on closely held property and investment companies.

## Working for Families Tax Credits

As of April 2011, your level of entitlement to Working for Families Tax Credits may be affected, as the definition of 'income' has been broadened to include all the following:

1. Attributable trustee income.
2. Attributable fringe benefits.
3. PIE income (Other than registered superannuation schemes such as KiwiSaver and Retirement Benefit schemes).
4. Passive income earned by children (includes interest, dividends and rent). Amounts over \$500 per child will be included as family income.

5. Worldwide income received by a non-resident.
6. Tax exempt salary or wages under specific international agreements.
7. Income equalisation deposits made by you, your trust, or a company controlled by you or your trust.
8. Certain pensions and annuities (excludes New Zealand Superannuation).
9. Other payments received from any sources that are used for your family's day-to-day living expenses totalling more than \$5,000 (eg Board received).

## PAYE Deductions Sacrosanct

If you run into cash-flow problems, don't use PAYE money to pay your creditors. A director of a company has previously been convicted of aiding and abetting an offence by knowingly allowing PAYE deductions to be used by the

company for some other purpose. IRD might also succeed if it prosecuted an officer of a company. The person aiding and abetting not paying PAYE does not have to be a company director.



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