Crime Insurance
Coverage and Current Issues

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CrimeInsurance? YES you need it !

- **Organizations lose 5% of their annual revenues to fraud**
- **Projected total global fraud loss of more than $5 trillion**
- **The average loss is estimated to be $1.7 million**

Source: Occupational Fraud 2024: A Report to the Nations

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Why do employees steal? – Fraud Triangle

Source: Lowers Risk Group

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Commercial Crime Coverage in the Marketplace
SFAA Crime Protection Policy for Public Entities (Ed. 08/19)

- Insuring Agreement 1 – Employee Dishonesty ✓
- Insuring Agreement 2 – Forgery or Alteration ✓
- Insuring Agreement 3 – Inside the Premises
- Insuring Agreement 4 – Outside the Premises
- Insuring Agreement 5 – Computer Hacking
- Insuring Agreement 6 – Money Orders & Counterfeit Paper Cash
- Insuring Agreement 7 – Loss of Clients' Property
- Insuring Agreement 8 – Funds Transfer Fraud
- Insuring Agreement 9 – Fraudulently Induced Transfers ✓

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What does your Crime underwriter need to know?

- Fill out their **application** – many of the application questions are developed from loss experience for GVT entities.
- **Loss history** – include **all occurrences** and losses whether or not paid
    - Include losses within the deductible
- **Loss prevention** - Include **Corrective measures** taken to prevent a similar loss from happening again.
- Best to have **high exposure entities** complete their own application (ex. Universities, Social Services)
- Invite your Crime Underwriter to **pre-renewal meetings** or agree to meet.
- Did you **improve** any of your internal controls since the last renewal?
- Provide your annual **CPA audit**.

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(1) Employee Dishonesty

Property Covered

- Money, Securities and Other Property

Causes of Loss Insured Against

- Dishonest acts committed by an employee with the manifest intent to:
  - Cause you to sustain loss

    and
  - Obtain financial benefit

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Your most trusted employee might be the Fraudster

By the Numbers…

- 60% of perpetrators hold the position of Manager or Executive
- Employees with 10 or more years of tenure caused the costliest losses
- Only 5% have previously been charged or convicted of a fraud-related offense
- 75% are male and 25% are female
- 67% possess a university degree or higher
- 69% are between the ages of 31 and 50
- Largest median losses were caused by fraudsters in the oldest age ranges (56 years and older)
- Most are risk takers, extroverts, decisive, career or success-oriented individuals
- 84% displayed at least one behavioral red flag: living beyond means, debt/financial difficulties, addiction problems, revenge, or family problems

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Source: Occupational Fraud 2024: A Report to the Nations:
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Identify your exposures: Common Types of Losses

- Vendor Fraud
  - Largest and Longest Current Running Trend in Crime Losses
  - Billing Schemes
  - Ghost Vendors
  - Kickbacks
- Foreign Losses
- Payroll Schemes
  - Ghost Employees
  - Improper Overtime
- Expense Reimbursements
- Social Engineering
- Check Schemes
- Valuable Metals
  - Copper Wire & Piping
  - Catalytic Converters

Many of these losses take approximately 24 months or longer to discover.

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Combatting Vendor Fraud

- **Background Checks**
  - W9
  - Face to face interview, when applicable
- **Familiarity and open communication with vendors**
- **Authorized Vendor List**
- **Purge the Vendor List annually**
- **Segregation of Duties**
  - The individual who performs background checks is unable to add a new vendor to the list
  - Signoff of multiple employees required

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Key Internal Control: Separation of Duties: Does One employee have too many duties?

- **Created** fraudulent physical documents
- **Altered** physical documents
- **Created** fraudulent electronic documents or files
- **Altered** electronic documents or files
- **Destroyed** physical documents
- **Created** fraudulent transactions in the accounting system
- Deleted or withheld electronic documents or files
- **Altered** transactions in the accounting system
- **Created** fraudulent journal entries.
- **Created** Fraudulent physical documents

- Concealing Fraud
  - An act of fraud typically involves not only the commission of the scheme itself, but also efforts to conceal the misdeeds.
  - Understanding the methods fraudsters use to cover their crimes can help organizations **better design prevention mechanisms and detect the warning signs of fraud.**

Source: 2024 Occupational Fraud: A report to the Nations

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Valuable Metals Current Market Values

- **Copper** $4.49 per troy ounce
- **Silver** $27.20 per troy ounce
- **Platinum** $932.00 per troy ounce
- **Palladium** $1,034.00 per troy ounce
- **Gold** $2,342.30 per troy ounce
- **Rhodium** $4,750.00 per troy ounce

Exactly How Much is a Troy Ounce?

One Troy Ounce = 31.1034768 grams = Approximately A Dozen Pennies

Current Market Values as of 04/22/2024
Source: CNBC.com

Metals Theft Claim Example

A County Sheriff's Office in a Southern State continues to investigate a huge theft from XYZ Company, a chemical plant. Security cameras, though dark and grainy, showed two suspects entering the property in a boat from a nearby river between 12 and 1 a.m. The burglars went into the company's warehouse and quickly removed four 100-pound barrels of palladium, which the company uses to absorb hydrogen. The thieves wore clothing that concealed their faces, arms, and legs. The total value of the palladium taken was about $300,000.

After further investigation, it was discovered that there was collusion between the suspects and a former employee who worked at the facility from 2013 until his firing in 2016.

The surveillance footage showed the former employee's vehicle towing one of the suspect's boat before and after the burglary, and captured the vehicle carrying barrels matching those stolen from the warehouse.

Luckily, all the palladium was recovered and returned to the plant.

The former employee was previously convicted on charges of assault and battery and drug trafficking.

Palladium, a rare-earth precious metal, is mined domestically in Montana but is primarily sourced from Russia and South Africa. In recent years, the value of palladium has increased and with it an increase in the theft of catalytic converters, which contain the metal.

Metals Theft Claim Example Internal Control Feedback

- **Loss prevention / controls:**
  - Robust Security Systems, 24/7 Security Guard Service, Anti-Theft Devices
  - Protective fencing around the premise
  - Central Station Burglar Alarm
  - Locked storage compartment
  - Well-Lit Facility
  - Conduct background checks on all Warehouse personnel

(2) Forgery or Alteration

Property Covered

- Negotiable instruments such as checks, drafts, promissory notes, or similar written promises, orders or directions to pay a sum certain in money that are made by you or someone acting on your behalf
- This coverage applies only to your checks, not incoming checks

Causes of Loss Insured Against

- Forgery or alteration of covered instruments
- Suit against the insured for sums the insured becomes legally obligated to pay

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(9) Fraudulently Induced Transfers

(Social Engineering Fraud)

Property Covered

- Funds (Money and Securities)

Causes of Loss Insured Against

- Fraudulently induced transfer causing the funds to be transferred from your premises or banking premises to a someone outside of your control
- Instruction received by you from a person purporting to be an Employee, Customer, or Vendor
- Callback condition precedent to coverage under some forms

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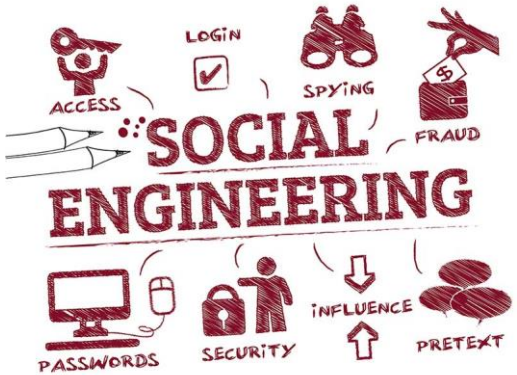

Social Engineering Fraud

- A new spin on one of the “oldest tricks in the book”
- Fraud epidemic that continues to grow and evolve targeting all sizes and classes of businesses
- Responsible for over $43.3 billion of total losses globally from 2016 - 2022
- 21,489 FBI complaints with adjusted financials losses of over $2.9 billion in 2023 alone
- Typically begins with Phishing attempts to gain access to the victims’ systems
- Impersonation of a Customer/Vendor/Employee resulting in a transfer of funds
- According to the FBI, the single best defense against these schemes is enacting a simple **callback verification procedure**!

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Source: Internet Crime Report 2023
United States Federal Bureau of Investigation

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Social Engineering

- Imposters gain access to systems or networks
- Attacks are on the rise and threatens organizations
- 98% of cyber attacks rely on social engineering in some capacity
- Relies heavily on human intervention and manipulates individuals into breaking normal security procedures and best practices
- Attacks focus on locating vital data such as account numbers, phone numbers, client contact lists, and organizational charts
- Schemes more often are simply for financial gain

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Major Causes of Social Engineering Losses

- Callbacks Not Performed
- Verification confirmed via Email by hitting “Reply” button
- No dual authorization or lack of segregation of duties in releasing wires
- Lack of security software to detect unusual activity
- Lack of education / training

Social Engineering – Business Email Compromise Claim Example

The Department of Aviation for a major City thought it was paying an approved vendor more than $1 million for services. The money almost went to what appeared to be a phishing scam that police are now investigating as a business email compromise. While the City recovered the money, the incident almost cost taxpayers seven figures and raised red flags about the integrity of the City's cyber-security system.

According to a police report obtained by the two Investigators, the Department received an email from what appeared to be a City-approved vendor, ABC Company. The company has been paid more than a quarter of a billion dollars — $284.6M – for custodial services at two locally based airports since 2008. The email requested that ABC Company's accounts payable information be changed from Bank 1 to Bank 2. The request was referred to the City's comptroller's office to make the change. Less than a month later, the City paid $1.2M for services to the updated account.

But in a call to the Department a few weeks later, ABC Company stated they had not received the payment. This is when the City discovered that ABC Company never requested an account change. Luckily, the City was able to later recover the money after Bank 2 placed a "hold for verification" on both accounts due to the "large and unusual wire transfer" and other inconsistencies with the transaction.

The scheme started off with the hacking of an ABC Company's employee's email account and purporting to be an ABC Company employee.

Social Engineering – Business Email Compromise Claim Example Internal Control Feedback

- **Loss prevention / controls:**
  - Calling Vendor back at telephone number on file previously provided when Vendor and the City signed their contract
  - Proper Computer Security and Phishing Email Reporting mechanism
  - Anti-Fraud Training for all Employees and Senior Management
  - Anti-Phishing and Social Engineering detection methods
  - Verify Bank change request directly with the Vendor
  - Dual Controls for all wire transfers including all changes to banking information

Social Engineering Fraud Loss Response
Recommended Steps to Take

- Contact the originating Financial Institution as soon as fraud is recognized to request a wire recall or reversal as well as a Hold Harmless Letter or Letter of Indemnity

- Immediately file a compliant with the FBI's Internet Crime Complaint Center (IC3) www.ic3.gov and also alert your local FBI office

- Notify your insurance broker(s) and put your crime and/or cyber insurance carrier(s) on notice of the incident being discovered

- Save all messages and evidence associated with the incident

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Corrective measures and Best practices to Mitigate Fraud

- Increased Segregation of Duties
- Code of Conduct
- External audit of Financial Statements
- Internal Audit Department/Surprise Audits
- Management Review
- Hotline
- Anti-Fraud Policy
- Fraud Training for Employees
- Fraud Training for Managers/Executives
- Dedicated fraud department, function, or team
- Job rotation/mandatory vacation
- Background Checks
- Approved vendor lists

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Key: Establish Strong Internal Controls

- Fraud losses continue to be on the rise both in terms of frequency and severity
- **Information**
  - Application – will also help you identify places where your control could be improved.
  - Loss information – also helps to identif weaknesses
- **Remember** most fraudsters have done this before
  - Pre-employment screening is critical
  - Vendor due diligence is essential
- **Report** all of your loss occurrences (a policy requirement)
  - We will help you.
- **Complacency** is one of our biggest enemies-employment screening is critical
  - Vendor due diligence is essential

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Questions?

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