

STRENGTHENING CITY INTERNAL CONTROLS

SEPTEMBER 20, 2018

AGENDA

- Fraud, Waste and Abuse
 - Examples of Poor Internal Controls
 - Financial Impact of Fraud
- Assessing Internal Controls
 - U of I Results of Reviews
 - Services Offering

Fraud Waste 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.”

Occupational Fraud and Abuse, Joseph Wells, Obsidian Publishing Company, 1997.

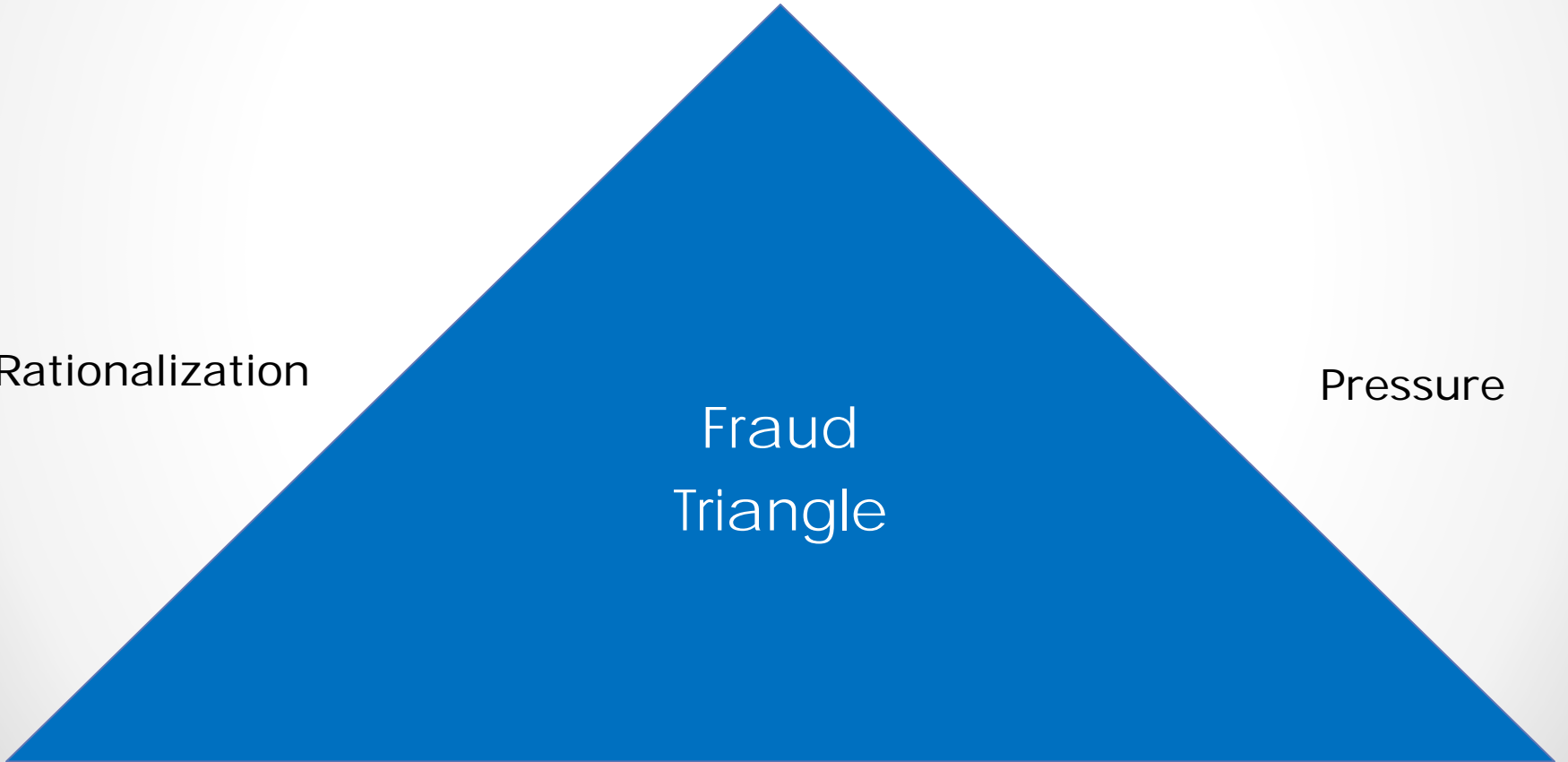
Fraud Triangle

Opportunity

Rationalization

Pressure

Fraud
Triangle



Assessing Internal Controls

- Evaluate the system's design
- Assess if system is operating as intended

Dixon Illinois

- Boyhood home of Ronald Regan
- Population: 15,000
- Annual financial audits performed on the City
- Annual budget of \$6 - \$8 million
- Controller: Rita Crundwell (Born to be a bean-counter)

Rita Crundwell

- Over 20 year period embezzled \$54 million
- Established bank account (Reserve Sewer Capital Development Account)
- Submitted fake invoices (billing scheme) and deposit into RSCDA
- Financial auditors: Approached by Mayor and stated she was excellent at her work.
- Rita was sole signee on checking account and was only person with access to accounts
- Bank account was identified while Rita was out of the office
- City notified the FBI

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PRESSURE: PERCEIVED FINANCIAL NEED

- - Rita led a lavish lifestyle.
 - lived in an extravagant house beyond the typical annual salary of a public employee in a small town.
 - operated a competitive horse breeding ranch (with 400 horses, a \$2.1 million luxury bus, a \$1 million horse trailer and semi-trailer trucks).
 - Rita often took the employees to lunch and gave them generous gifts.
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PERCEIVED OPPORTUNITY

- Lack of internal controls
 - Inadequate segregation of duties.
 - Inadequate authorization of transactions
 - Inadequate documentation
 - Adequate safeguards of assets
 - Independent reviews not performed
 - Vacations and rotation of duties were not required
 - Weak oversight and monitoring

RATIONALIZATION

- Rationalizations that Rita may have made to justify her fraudulent behavior:
 - The city was large enough to absorb the impact.
 - She deserved the cash as a just reward for her dedication and loyalty.
 - The employees deserved more pay, so she often took them to lunch and gave them generous gifts.

City of Boise

- Issue identified by member of City Council
- Poor internal controls
- Led to abuse in the areas of procurement, travel and compensation
- Recommendation: Improvements in internal controls and establishment of internal audit department

How is Fraud Committed

- Corruption (38%)
 - Conflicts of Interest
 - Bribery
 - Illegal Gratuities
- Asset Misappropriation (89%)
 - Theft of Cash on Hand
 - Theft of Cash Receipts
 - Fraudulent Disbursements

Size in Relation to Risk

Size of Organization	Percent of Cases	Median Loss
Less than 100	28%	\$200,000
100 - 999	22%	\$100,000
1,000 – 9,999	26%	\$100,000
Over 10,000	24%	\$132,000

Control Weaknesses

Control weaknesses that contribute to fraud:

- Lack of internal controls – 30%
- Override of existing controls – 19%
- Lack of management review – 18%
- Poor tone at the top – 10%

Behavioral Red Flags

Following are the most common that have been reported in every study since 2008:

1. Living beyond means
2. Financial difficulties
3. Unusually close association with vendor
4. Control issues, unwillingness to share duties
5. Divorce/family problems
6. Wheeler-dealer attitude

Anti-Fraud Controls

Percent Reduction By Control (Top out of 18 reported)

- Code of Conduct: 56%
- Proactive Data Monitoring: 52%
- Surprise Audits: 51%
- External Audits of Internal Controls: 50%
- Management Review: 50%
- Hotline: 50%

Examples of Audits

- University of Idaho operational reviews conducted by students
- Examples of four operational reviews

Unit #1

Lack of Segregation of Duties

Concerns Over Safeguarding of Checks

- Checks kept in an unlocked drawer
- Checks are not immediately endorsed
- Deposits are not made daily (up to 2 weeks)

Inadequate Documentation

- Prelist of received checks is not prepared
- Deposits not reconciled to recorded transactions
- No receipts created for customers

No Reconciliation process

- Deposits not reconciled to recorded transactions



Unit #2

Lack of Segregation of Duties

- The Administrative Assistant receives the checks, makes the deposits, and records the receipts.

Concerns Over Safeguarding of Checks

- Checks are stored in an unlocked drawer between receipt and deposit. Even though the office door is locked when the Director leaves, multiple individuals have keys to the office.
- Deposits are not made daily

Inadequate Documentation and Reconciliation

- No prelist of checks received is prepared and later reconciled to recorded transactions.
- No receipts for cash received

No Written Procedures

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Unit #3

Concerns Over Safeguarding of Checks

- Cash box stored in plain sight
- All staff had access to cash box key
- Credit card information recorded on paper forms
- Intern/summer help allowed to transport credit card information to cashier's window

Concerns of training

- In the absence of the administrative assistant, a student assistant with no training on cash handling procedures is responsible for receiving cash and checks

Unit #4

Concerns Over Safeguarding of Checks

- The safe is opened in the morning and left unlocked until the close of business
- The safe combination has not been changed in five years
- All four full-time staff and one part-time staff have access to the safe
- Several employee have access to cash register
- Deposits are not made daily
- No controls over imprest fund

Inadequate Documentation and Reconciliation

- No pre-list of checks received nor receipts
- No reconciliation of cash receipts to recorded transactions.

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Service Offering

- Offer assessment of control structure of certain key activities.
- Either students or other representative would visit city and obtain understanding of the control structure.
- Evaluate the design of the control structure.
- Determine if operating as intended.
- Make recommendations

Questions

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