

RISK MANAGEMENT SERVICE **INTEGRITY**
INDEPENDENCE KANE COUNTY BEST PRACTICES **PUBLIC ACCOUNTABILITY**
AUDITOR
 BOARD ANALYSIS FINANCIAL INFORMATION **INNOVATION**

AUDIT WATCH
 February 2013

Kane County Auditor's Office

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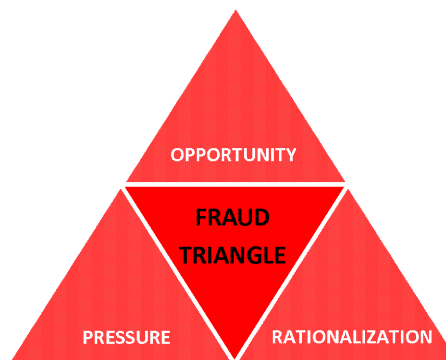
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FOCUS ON FRAUD DETERRENCE

With the recent sentencing of the former Dixon Comptroller, governmental fraud has become an all too familiar local news item. This month's edition of the Audit Watch will continue on that same topic with commentary and recommendations for best practice policies from groups such as the Association of Certified Fraud Examiners, the Illinois Policy Institute and the Association of Government Accountants.

The **FRAUD TRIANGLE** is commonly credited to Donald Cressey, a well known criminologist. The basis for Cressey's theory is that there are three factors that must be present at the same time for an ordinary person to commit fraud—



PRESSURE, OPPORTUNITY and RATIONALIZATION.

Audit Watch—Suggestions

I welcome your thoughts and suggestions for how to make the Audit Watch more useful and enjoyable. Please feel free to share it with anyone who might be interested. This month we will be sending it out to about 200 individuals, and are looking forward to growing that number over the coming months. Thanks.

Terry Hunt





UNAUDITED GENERAL FUND EXPENSES OVER BUDGET
TWO MONTH PERIOD ENDED JANUARY 31, 2013
FOR FISCAL YEAR ENDING NOVEMBER 30, 2013

DEPARTMENT	EXPENDITURES IN EXCESS OF YTD	NOTES
INFORMATION TECHNOLOGIES *	1%	Encumbrances for Contractual Services and Commodities
COUNTY CLERK **	6%	Elections Contractual Services

Please note: Year to date departmental transactions are calculated by combining actual expenditures and any recorded encumbrances. This report covers transactions recorded during the first two month period of the fiscal year that will end November 30, 2013. These expenditures are unaudited, and subject to change. We monitor expenses throughout the entire year. Cyclical activities, especially at such an early stage of the year can create apparent budget overages when compared to a linear budget.

For example, debt service expenditures are paid in accordance with the terms of the bond issue which will generally call for annual, or semi-annual payments of principal and accrued interest. To avoid confusion debt service will not be included on these interim reports, but will be included at year end.

Memo

* Information Technologies is slightly (1%) over budget at this point due primarily to commitments recorded in January for services to be provided over the entire year.

** The County Clerk has already incurred expenses related to the February Consolidated Primary Election. As a result the department is 6% over budget through January. Added expenses will be incurred for the April 9th Consolidated Elections, but the department is projected to be well within its budget before the end of the year.



UNAUDITED SPECIAL FUND EXPENSES OVER BUDGET
TWO MONTH PERIOD ENDED JANUARY 31, 2013

DEPARTMENT FUND	EXPENDITURES IN EXCESS OF YTD BUDGET AS A %	NOTES
TRANSPORTATION COUNTY HIGHWAY FUND	11%	Encumbrances for Contractual Services, Commodities, and Capital
TRANSPORTATION MOTOR FUEL TAX FUND	34%	Encumbrances for Contractual Services, and Commodities
TRANSPORTATION MOTOR FUEL LOCAL OPTION FUND	11%	Encumbrances for Contractual Services, Commodities, and Capital
TRANSPORTATION TRANSPORTATION SALES TAX FUND	36%	Encumbrances for Contractual Services, and Capital
TRANSPORTATION TRANSPORTATION CAPITAL FUND	48%	Encumbrances for Contractual Services, and Capital

Please note: The same principles are applied for the departments that receive special funds, and can be misleading due in large part to the cyclical nature of the operations involved (the Transportation Department is especially affected by seasonal factors and encumbrances recorded early in the year when they are applicable to the entire year).

These expenditures cover the two months ended January 31st. They are unaudited, and subject to change. Cyclical activities, can result in budget overages when compared to a chronologically linear budget. Forecasting the timing of the receipt of grant monies is sometimes imprecise which can also affect expenditure patterns on related projects.

To avoid confusion Matching Funds will not be included on these interim reports, but will be included at year end. Similarly SSA and SBA activity will only be reported at year end.

INTERNAL AUDITS ~ WHY ALL THE FUSS?



AUDIT WATCH
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Over the past several weeks the Kane County Auditor's office has developed an ICQ which has been distributed to every office and department. I had planned to have all the follow-up meetings completed by the end of February, but as we have actually expanded to include some sub-departments in the process, we will not be finished until sometime in March. While the delay will push back the overall internal audit plan a little, the meetings themselves have been very successful and proven to be a worthwhile, if time consuming, effort. Thanks to all the elected officials, department heads and staff members for your cooperation.

At the risk assessment meetings we have occasionally been asked, *"Why are you looking at my department?"* The simple answer is that we are looking at *all departments*. The focus on documentation of organizational charts and policies and procedures may seem burdensome, but it is only a part of a continued emphasis on developing better practices countywide.

Similarly, while this month's version of the Audit Watch deals with fraud and, more importantly, fraud deterrence it is the situation in Dixon—*not Kane County* - that makes the topic timely.

INTERNAL AUDITS ~ WHY THEY ARE PART OF BEST PRACTICES



The Association of Government Accountants (AGA) convened a special work group of government officials to develop special [Tool Kit](#) because:

- The typical organization loses 5 percent of its annual revenue to fraud.
- Governments are the second most frequent victims of fraud (after banking).
- The median duration of those fraud schemes that are discovered is 18 months.
- Nearly half of victim organizations do not recover any losses that they suffer due to fraud.

Source: Association of Certified Fraud Examiners'
2012 Report to the Nations

INTERNAL CONTROLS ARE NO GUARANTEE, BUT NO INTERNAL CONTROLS IS A TICKING TIME BOMB



The following excerpts are from an [article by Brian Costin](#) which was recently published in the Illinois Policy Institute . The article has been edited to fit the available space. My sincere thanks go to Brian for his permission. Click on the hyperlink above to read the entire article.

Former Dixon Comptroller Rita Crundwell was sentenced to 235 months in prison. Crundwell pleaded guilty to wire fraud and stealing more than \$53 million from the city of Dixon during a period of more than 20 years; a shocking amount, even by Illinois standards. She still must face 60 separate state charges that may add to her prison time.

Taxpayers and lawmakers alike must ask what can be done to prevent this type of fraud from ever happening again. Central to the fraud Crundwell perpetrated on the people of Dixon was the fact that *she was almost solely responsible for all of the accounting and treasury duties* for the city. All local governments need to have multiple people responsible for the accounting and treasury duties. Local governments can also enact *proactive online transparency best practices to protect against public fraud*.

Will County Auditor Duffy Blackburn had the following to say about how proactive transparency is key in preventing future cases like the Crundwell case: “Important to the discussion of preventing these type of events, beyond the specialized assistance with *internal controls or proper segregation of duty or accounting work*, is the perception of being somehow detected to someone who considers committing fraud. The perception of being detected is one of the strongest deterrents to fraud, according to fraud experts. This is why adopting a policy of transparency in governments, especially local governments, is so important. *Transparency and continuous oversight* are key tools in creating this type of perception, in addition to their benefits as good governing policy.”

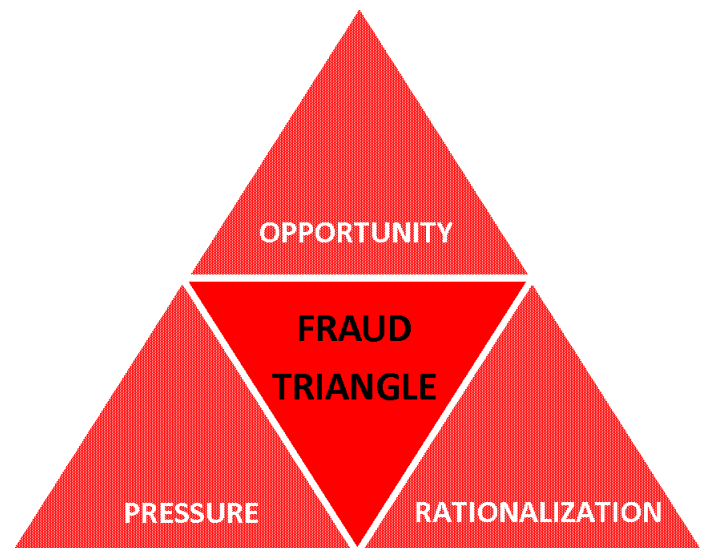
It's too late to prevent the Crundwell crime against the taxpayers of Dixon, but this situation is a stern warning to the rest of the country to enact *better transparency standards* before the next public fraud crisis strikes somewhere else.

The FRAUD TRIANGLE



The [Association of Certified Fraud Examiners](#) is a great resource for its members. I have summarized the following information from their website.

- The first component of the fraud triangle is **pressure**. Whether it is real or perceived, this pressure is the original motivation for the crime. For example, a person may be faced with a financial problem that cannot be solved by legitimate means. As a result that person might consider the commission of an illegal act, such as stealing cash or falsifying a document, to solve the problem.



- The second aspect of the fraud triangle is perceived **opportunity**, which defines the method by which the crime can be committed. The person must see some way to abuse their position of trust to solve a financial problem with a low perceived risk of being caught. It is also critical to a fraud perpetrator that the problem can be solved in secret.
- The third element of the fraud triangle is **rationalization**. Statistically, the vast majority of fraudsters are first-time offenders with no criminal past. Often they view themselves as honest, ordinary people caught in a bad set of circumstances.

Editor's Note: Better practice policies are focused more on fraud deterrence. Through the combination of (a) reducing the perceived opportunities to successfully commit a fraud in secret and (b) increasing the emphasis on oversight through well documented internal controls, the potential for fraud can be minimized, but never eliminated.