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# STATE OF MINNESOTA

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Article for *Minnesota Counties*

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## Economic Downturn and Counties

By *Rebecca Otto, Minnesota State Auditor*

As a county commissioner, the last thing you want to have happen under your watch is theft of county funds. Some think, "It would never happen in our community." Unfortunately, employee theft happens. Therefore, to be proactive and prevent employee theft, it is important to have sound internal controls in place.

In an economic downturn, studies show that there is an increase in fraud. County commissioners play an important role in ensuring that proper internal control policies and procedures are developed and consistently implemented to protect tax dollars. This article will provide guidance on implementing procedures that reduce the risk of theft and increase the chance of early detection.

### Types of Employee Thefts

Employee thefts may take several forms. It may be as simple as a county employee writing a check to himself/herself, but recording in the county records that the check was written to a vendor or the check is "void." It may involve a failure to deposit all county funds into county accounts, or depositing a check intended for the county into a personal account. It may involve submitting personal expenses as employee expenses, or altering invoices presented to the county for payment.

### Procedures to Reduce the Risk of Theft

To reduce the risk of employee theft, every county should implement basic safeguards. An environment of accountability should be created.

*Segregation of Duties.* Simply put, no employee should be in a position to commit an irregularity and then conceal it. To help prevent that from happening, responsibilities in financial transactions should be divided amongst more than one person, or segregated. An example of segregation of duties taken from everyday life is a movie theater, where one person sells tickets and another person collects the tickets. This separation of duties helps

prevent the person selling the tickets from: (1) collecting the price of the ticket, but allowing entry without a ticket (allowing the ticket seller to pocket the ticket payment without being detected), or (2) allowing entrance without the purchase of a ticket.

Examples of incompatible duties that should be performed by separate individuals are:

- Receipting collections, posting collections to registers, and making bank deposits;
- Signing checks, and reconciling the bank accounts.

Even with personnel cuts, financial duties should remain segregated. Counties may need to be creative and segregate duties by involving employees who have not previously played a role in financial transactions.

*Internal Control Procedures.* Many internal control procedures are common-sense methods used to track county funds. Here are a few procedures that may help prevent thefts or allow earlier detection of thefts:

- Have checks written to the county;
- Endorse checks for deposit as they are received;
- Make daily deposits;
- Reconcile receipts with deposits;
- Contact your bank to:
  - prohibit cash withdrawals and check cashing from the county account, and
  - be sure authorized signatures are up-to-date;
- Reference approved claims and amounts in the minutes;
- Do not pre-sign any checks;
- Reconcile bank statements monthly;
- Require detailed original receipts for the reimbursement of employee expenses;
- Have written policies (e.g., checks may only be for the amount of purchase, or no cashing of personal checks).

We also encourage counties to obtain from their banks, if possible, the county's cancelled checks or optical images of the checks. By comparing the cancelled checks with the register each month, discrepancies will be detected.

During tough economic times, internal control procedures help reduce the opportunity for an employee to commit fraud.

*Environment.* Finally, counties should promote an environment of accountability. Everyone should comply with the county's internal control procedures. This message needs to come from the top, starting with the county commissioners.

The pressure on an employee to commit fraud may increase during an economic downturn. Therefore, a strong control environment becomes increasingly important.

## **Red Flags in Detecting Theft**

Theft can result from poor segregation of duties. Possible indicators of theft, or “red flags”, include instances when an employee:

- takes records home;
- takes on duties that should be segregated;
- works hours when others are absent;
- refuses to take vacations.

Theft can also result from noncompliance with internal control procedures. Some red flags to watch out for:

- submitting copies, rather than original invoices for payment, may indicate that an altered document is being submitted;
- deposits are late;
- old checks remain outstanding;
- receipts are not reconciling with deposits;
- checks are written out of order.

Situations involving cash transactions present special risks and require extra diligence. Even smaller departments must implement basic safeguards to reduce theft.

## **When Theft is Suspected**

Whenever a county employee or officer discovers evidence of theft, embezzlement, or the unlawful use of public funds or property, the person is required to promptly submit a written report to the Office of the State Auditor providing a detailed description of the alleged incident(s). *See* Minn. Stat. § 609.456, subd. 1. The person must also report the incident(s) to law enforcement.

Employee thefts may implicate disciplinary actions as well as criminal charges. Before approaching the employee or officer involved, consult with a supervisor, the county attorney, local law enforcement, or the Office of the State Auditor for guidance on what actions to take.

To contact the Office of the State Auditor regarding evidence of employee theft or with further questions, please call (651) 296-2551 or e-mail us at [state.auditor@state.mn.us](mailto:state.auditor@state.mn.us).

For additional information on internal controls or investigative reports, visit the Office of the State Auditor website: [www.auditor.state.mn.us](http://www.auditor.state.mn.us).