



REBECCA OTTO
STATE AUDITOR

STATE OF MINNESOTA OFFICE OF THE STATE AUDITOR

SUITE 500
525 PARK STREET
SAINT PAUL, MN 55103-2139

(651) 296-2551 (Voice)
(651) 296-4755 (Fax)
state.auditor@state.mn.us (E-mail)
1-800-627-3529 (Relay Service)

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Prevent and Detect Employee Theft in Your Township

By Rebecca Otto, State Auditor

As township supervisor, the last thing you want to have happen under your watch is theft of township 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.

This article will provide guidance on implementing procedures that reduce the risk of theft and increase the chance of detection.

Types of Employee Thefts

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

Procedures to Reduce the Risk of Theft

To reduce the risk of employee theft, every township 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. An example taken from everyday life is a movie theater where one person sells tickets and another person collects the tickets. This 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; and

- Signing checks, and reconciling the bank accounts.

In many townships, it may not be possible to segregate duties completely. In those cases, town supervisors may need to assist staff to keep the functions separated. **At the very least, the functions of check writing and bank statement reconciliation must be separated.**

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

- Have checks written to the town
- Endorse checks for deposit as they are received
- Make daily deposits
- Reconcile receipts with deposits
- Contact your bank
 - prohibit cash withdrawals and check cashing from the town account
 - do not allow fund transfers without a resolution from the board of supervisors
 - 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, no cashing of personal checks)

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

Environment. Finally, townships should promote an environment of accountability. Everyone should comply with the town's internal control procedures.

Red Flags in Detecting Theft

Some red flags result from poor segregation of duties. Employees who take records home, take on duties that should be segregated, work hours when others are absent, and refuse to take vacations should raise concerns. Rather than being model, indispensable employees, they may be engaging in theft or fraud.

Other red flags result from noncompliance with internal control procedures. For example, submitting copies rather than original invoices for payment may indicate that an altered document is being submitted. Additional red flags include:

- Deposits are late
- Old checks remain outstanding
- Receipts are not reconciling with deposits
- Checks are written out of order

Special Situations Presenting Risks

Situations involving cash receipts by a town present special risks and require extra diligence. When cash receipts are involved, the need to implement internal control procedures to safeguard the receipts is crucial.

When Theft is Suspected

Whenever a town employee or supervisor 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 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, consider consulting with a supervisor, the township attorney, local law enforcement, or the Office of the State Auditor.

To make the reporting obligation easier, a “Report a Concern to the Office of the State Auditor” form is contained on our website at:

http://www.auditor.state.mn.us/other/reportconcern_govtofficial_form.pdf.

Use of the form is not required. However, it provides an outline for making a report. The form asks about the facts, and requests that supporting documentation be provided. The form also asks whether law enforcement has been notified, and whether internal control changes have been put in place in response to the incident. Finally, the Office of the State Auditor generally does not bill local government for services provided in response to section 609 reports.

Reports should be sent to: Office of the State Auditor, Legal/Special Investigations Division, 525 Park Street, Suite 500, St. Paul, Minnesota 55103.

If you have questions about whether a report should be made, please feel free to contact Nancy Bode, Assistant Legal Counsel, at (651) 297-5853.