



MGO
**Organizational Risk
Assessment
and Fraud Overview**

October 22, 2015

Presenter .



Scott Johnson

Scott is the lead partner for MGO's State and Local Government Advisory Services. He brings a wealth of experience and expertise to MGO. Prior to joining MGO, Scott's career has spanned over 29 years of high-level organizational management and leadership experience. He has led multi-billion dollar operations for local government agencies in various capacities. For example, Scott has served as the Assistant City Manager for the City of Concord, Assistant City Administrator for the City of Oakland, Director of Finance for the cities of San Jose and Milpitas, Controller-Treasurer for the County of Santa Clara and Assistant Finance Director for the City of Santa Clara. Scott is nationally recognized as a leader in managing municipal finances, investments, debt, and budgets. He and his team have received numerous state and national awards for excellence. Scott is a CPA and a Chartered Global Management Accountant (CGMA). He has also served on state-wide boards and is a Past-President of the California Society of Municipal Finance Officers (CSMFO). He is also a member of numerous national and state associations.

In his role, Scott works directly with senior government leaders to gather intelligence on the challenges and opportunities facing public entities in the coming decade – with the aim of creating a government 'center of excellence' that identifies and develops solutions and best practices in public sector operations.

Presenter .

Ric Jazaie

Ric is a senior manager for MGO's State and Local Government Advisory Services, specializing in Information Technology audits. He brings a wealth of experience and expertise to MGO. Prior to joining MGO, Ric's career spanned over 16 years of mid-level organizational management and leadership experience. He has led multiple financial, compliance, fraud investigation, and IT audits for federal, state, & local government agencies, as well as, educational institutions in various capacities. For example, Ric has served as the Internal Audit Director for the City College of San Francisco, Special Agent/Intelligence Analyst for the FBI, and a mid-level auditor with California Department of Finance. He has also testified on many depositions, Federal Grand Juries, and served one term with the San Francisco Civil Grand Jury investigating City's business practices. Ric has earned his Master of Accountancy with an emphasis in Financial Forensics from Golden Gate University. Ric is a CPA and a Chartered Global Management Accountant (CGMA), as well as, a Certified Fraud Examiner (CFE), a Certified in Financial Forensics (CFF), and a Certified Information Systems Auditor (CISA). He is also involved with local Association of Certified Fraud Examiners and provides lectures to the general membership on fraud risk assessments and the whistleblower programs.

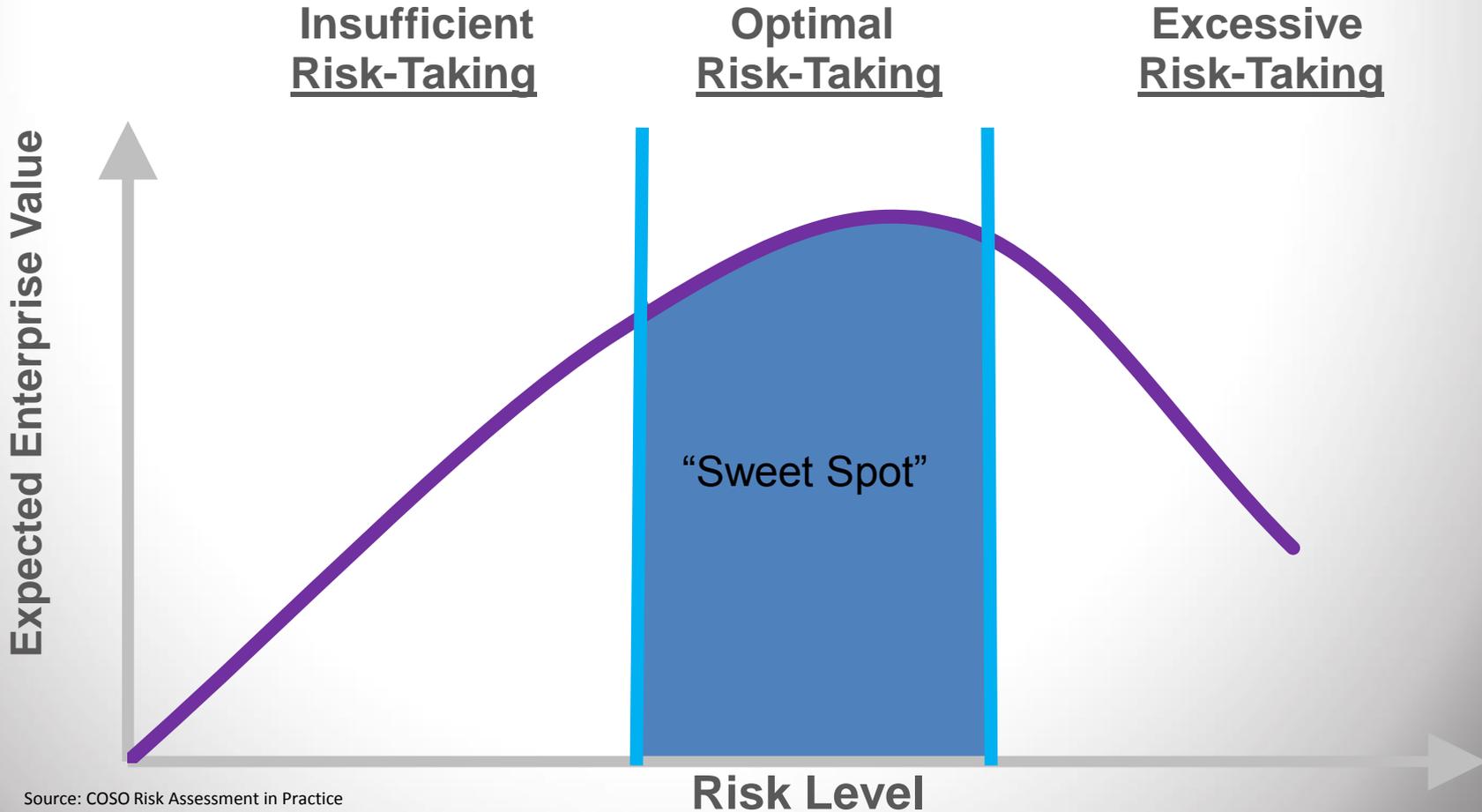
In his role, Ric works directly with various government agencies to identify and develop solutions and best practices in public sector operations, especially with their IT environments.

Agenda .

- 1 Introductions and Overview
- 2 Risk Assessment Process
- 3 Fraud Overview
- 4 Fraud Triangle and Red Flags
- 5 Case Studies
- 6 Q&A Session

Risk Assessment Process

Risk Assessment - Optimal Risk Taking



Source: COSO Risk Assessment in Practice

Risk Assessment Framework



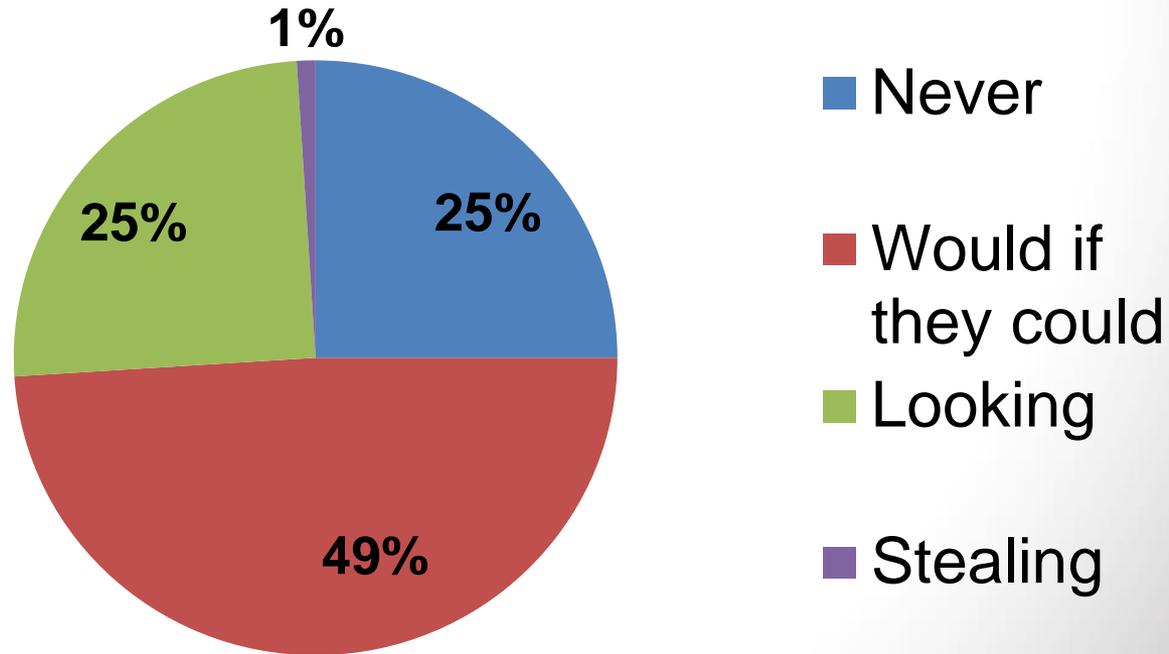
Risk Assessment - Overview

- Types of Risk Assessment:
 - Entity Wide
 - Departmental
 - Procedural
 - Regulatory Specific
 - IT Security
 - Fraud

Fraud Overview

Fraud Overview

- Internal controls are only as good as the personnel performing the activities.



Fraud Overview

- 2014 ACFE Report To The Nations
 - Organizations lose approximately 5% of revenue due to fraud
 - Asset Misappropriation – 85.4% with median loss of \$130,000
 - Corruption – 36.8% with median loss of \$200,000
 - Financial Statements – 9.0% with median of \$1 million
 - Fraud duration 18 months
 - Men (66.8%) vs. Women (33.2%)
 - 40% of cases were detected via Tip /Hotline

Fraud Overview

Figure 24: Frequency of Schemes Based on Industry

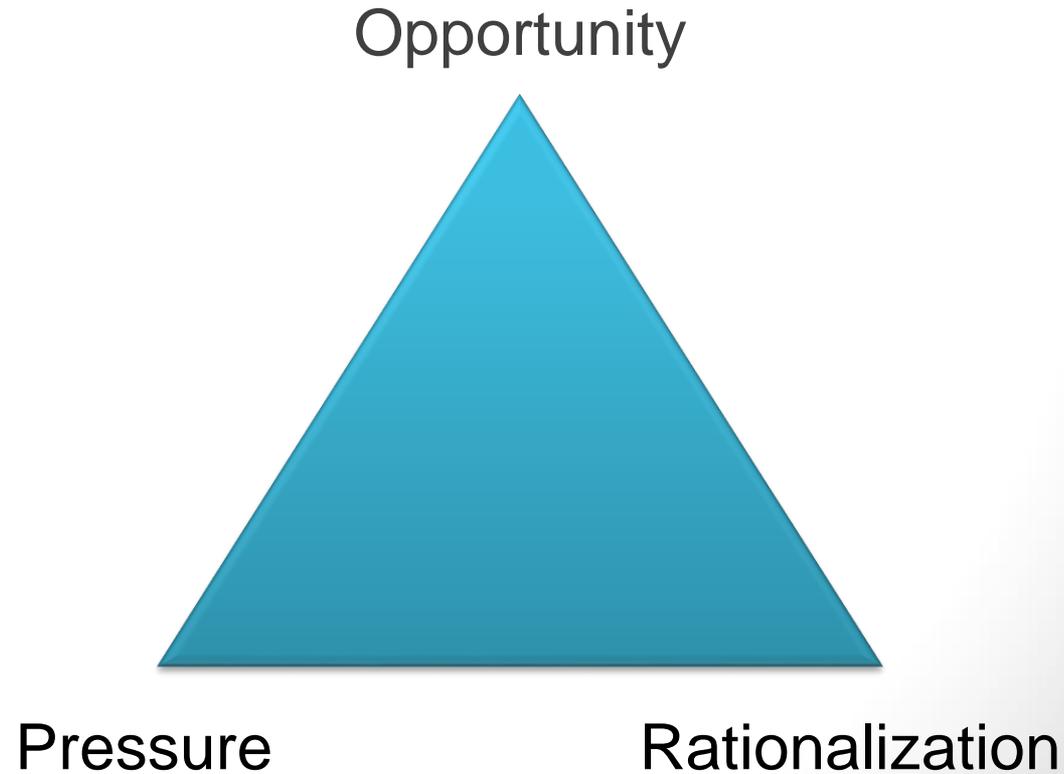
Industry/Scheme	Banking and Financial Services	Government and Public Administration	Manufacturing	Health Care	Education	Retail	Insurance	Oil and Gas	Transportation and Warehousing	Services (Other)	Construction	Religious, Charitable or Social Services
Cases	244	141	116	100	80	77	62	49	48	45	43	40
Billing	5.7%	19.1%	22.4%	29.0%	33.8%	10.4%	17.7%	24.5%	33.3%	28.9%	34.9%	32.5%
Cash Larceny	13.1%	10.6%	6.0%	12.0%	6.3%	15.6%	6.5%	2.0%	2.1%	11.1%	14.0%	7.5%
Cash on Hand	18.9%	12.1%	7.8%	16.0%	16.3%	22.1%	1.6%	2.0%	10.4%	11.1%	7.0%	12.5%
Check Tampering	5.7%	5.7%	7.8%	21.0%	10.0%	7.8%	4.8%	4.1%	20.8%	17.8%	27.9%	35.0%
Corruption	37.3%	36.2%	54.3%	37.0%	36.3%	22.1%	33.9%	57.1%	29.2%	35.6%	46.5%	30.0%
Expense Reimbursements	4.1%	12.8%	7.8%	23.0%	31.3%	3.9%	4.8%	14.3%	14.6%	17.8%	27.9%	32.5%
Financial Statement Fraud	10.2%	5.0%	13.8%	8.0%	10.0%	6.5%	3.2%	12.2%	10.4%	6.7%	11.6%	7.5%
Non-Cash	13.1%	17.7%	34.5%	12.0%	12.5%	33.8%	12.9%	16.3%	33.3%	17.8%	20.9%	15.0%
Payroll	5.3%	15.6%	8.6%	15.0%	16.3%	5.2%	8.1%	6.1%	16.7%	6.7%	18.6%	20.0%
Register Disbursements	2.5%	0.7%	2.6%	3.0%	5.0%	13.0%	0.0%	0.0%	4.2%	6.7%	2.3%	2.5%
Skimming	5.7%	11.3%	4.3%	18.0%	20.0%	18.2%	22.6%	2.0%	6.3%	33.3%	7.0%	12.5%

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Fraud Triangle and Red Flags

Fraud Triangle and Red Flags



Fraud Triangle and Red Flags

Pressure (Albrecht book)*

- Personal financial factors that may lead to fraud:
 1. Financial difficulties (33%)
 - a. High personal debts or financial losses
 - b. Inadequate income
 2. Living beyond one's means (44%)

- Personal habits that may lead to fraud:
 1. Extensive stock market or other types of speculation (starting a new business)
 2. Extensive gambling
 3. Illicit affairs
 4. Excessive use of alcohol or drugs (12%)

Fraud Triangle and Red Flags

Opportunity:

1. Amount of fraud would decrease if the opportunity did not exist
 - a. Reasons for increased fraud risk:
 - i. Crime requires a simple act
 - ii. Chances of being detected are very slim
 - iii. Punishment is very light
 - b. Mitigation factors:
 - i. What if security was tight?
 - ii. What if sound internal controls require an elaborate scheme?
 - iii. What if the likelihood of detection is high?
 - iv. What if punishment is severe?

Fraud Triangle and Red Flags



Opportunity (Continued):

2. Personally Created Opportunities:
 - a. Familiarity with operations (including cover-up capabilities)
 - b. Close association with suppliers, vendors, and other key people (22%)
 - c. Unwillingness to share duties (21%)
3. Organization Characteristics:
 - a. Weak internal controls
 - b. Absence of periodic rotation in job duties
 - c. Constantly operating under a crisis environment
 - d. Little attention to details
 - e. Poor morale
4. Opportunity is the **ONLY** thing your organization can control!

Fraud Triangle and Red Flags

Rationalization:

1. How can you be proactive and know who will rationalize fraudulent behavior?
2. Embezzlers don't fit the criminal stereotypes; they appear to be trustworthy, sincere, likeable, sociable, etc.
3. Personal emotions that may lead to fraud:
 - a. Strong community or social expectations to succeed (6%)
 - b. Perception of being treated unfairly by the organization (9%)
 - c. Resentment towards superiors
 - d. Frustration with job
 - e. Insatiable desire for self-enrichment or personal gain
 - f. Wheeler – dealer attitude (18%)

Case Studies

Case Studies

- City of Dixon, IL
- City of Pasadena, CA

Case Studies



City of Dixon, IL

Who?: Rita Crundwell, Comptroller/Treasurer

When?: From 1998 - 2012

Amount?: \$54 Million

Case Studies



City of Pasadena

Who?: Danny R. Wooten

When?: From August 2003 – March 2014

Amount?: \$6.4 Million

Questions?

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