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Financial Misconduct: Best Practices for **Prevention & Investigation**

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Presenters

- **Edward J. Heath:** Ed is a partner at Robinson & Cole, the largest Connecticut-based law firm. Ed chairs the firm's Business Litigation, Government Enforcement, and Internal Investigations practices. During his two decades in private practice, Ed has routinely conducted internal investigations for Connecticut municipalities, public and private companies, and nonprofit organizations in response to actual and anticipated employee misconduct, civil litigation and criminal proceedings.
- **Jeffrey W. Rossi:** Jeff is a partner at CohnReznick, the 10th largest certified public accounting tax and advisory firm in the United States. Jeff is both a certified public accountant and certified fraud examiner with over 25 years of experience. Jeff has a diverse industry background including municipal, manufacturing, construction, retail, and not for profit. Jeff is also an internal control specialist and while he has done many fraud investigations he enjoys proactive, preventative consulting to help prevent asset misappropriation.

Disclaimer

While we have designed this program to provide accurate information about its subject matter, today's discussion is general and does not constitute legal advice or the creation of an attorney-client, or accountant-client, relationship. If you would like legal, tax, or other professional advice about a particular matter, please feel free to contact the speakers directly after the program.

Scope of “Financial Misconduct”

- Diversion of cash disbursements/receipts
- Payment for purchases/services never received
- Payroll scheme
- Theft of physical property
- Budget manipulation
- Fraudulent financial reporting

Overview

- Prevention



- Detection



- Investigation



We begin in Dixon, Illinois...



Does Rita Crundwell work for you?

- Ms. Crundwell served for more than four decades as a city employee.
- Dixon's was Comptroller and Treasurer from 1983 to 2012.
- Sterling reputation: "She looks after every dollar as if it were her own."



Does Rita Crundwell work for you?

- From 1991-2012, she stole **\$53.7 million** from Dixon
 - Fake bank account scheme
 - Outside auditor's work not sufficient
- **Red Flags**
 - Employee had opulent lifestyle
 - Others had limited access to City financials
 - No segregation of duties
 - Invoices lacked typical elements + unusually high amounts

Prevention & Detection

- A properly designed system of internal controls should include both preventative and detective controls:
- An ounce of prevention is worth a pound of cure.....
- Preventative controls are designed to be proactive to discourage errors and irregularities
- Examples of preventative controls
 - Appropriate system access safeguards/passwords, etc
 - Appropriate approvals/authorizations
 - Segregation of duties
 - Cross training / mandatory vacation
 - Timely account reconciliations
 - Proper documentation
 - Physical security

Prevention & Detection

- Detective controls are designed to detect errors or irregularities on a timely basis
- Walk softly carry a big stick.....
- Examples of preventative controls
 - Timely account reconciliation/financial reporting
 - Budget to actual reporting with variance analysis
 - Journal entry review
 - Internal auditing/process review
 - Physical inventories
 - Appropriate, Relevant Governance/Board oversight

An external audit is neither a preventative nor a detective control....it is the process of determining if the financial statements are in compliance with the appropriate accounting standards

Investigation

- Handling the initial employee tip
- Consider the end game
- *Resist the urge to immediately:*
 - confront the suspected wrongdoer,
 - start questioning witnesses or searching for documents,
 - tell other employees, or
 - send emails about this issue
- First step: Contact legal counsel

Investigation

- Developing the Investigation Plan with Legal Counsel
 - Scope should be appropriate to the concerns
 - Plan for execution in stages
 - Timeline for stages
 - Projected estimate of fees/costs
 - Who will supervise counsel

Investigation

- Investigation Plan – Key Questions
 - Should employment action be taken against the target now?
 - Are interim internal financial controls required?
 - Are forensic (accounting/technology) consultants needed?
 - What electronic/paper records must be preserved?
 - Which policies and procedures are relevant?
 - Who will be interviewed, when, where, and in which order?
 - Who should attend the interviews, aside from counsel?
 - Should we notify anyone with the municipality?
 - Should we alert law enforcement now?
 - Will there be a final report, oral or written?

Investigation

- Response to the Investigation's Findings
 - Corrective action to prevent similar misconduct in the future.
 - Appropriate employee disciplinary action of target, others
 - Consider insurance claim
 - Evaluate litigation options
 - Disclosure to law enforcement
 - Disclosure to public and the media

Thank You and Q&A



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