

Internal Control and Fraud Risk Vulnerability Study

City of Lee's Summit, Missouri

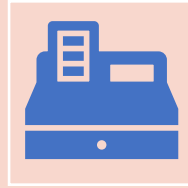
Why an internal control and fraud risk vulnerability study?

- Across the country, there have been hundreds of recent local government fraud incidents. Many have gone on for years undetected and undeterred – costing taxpayers millions.
- External audit is generally ineffective at detecting fraud. Only about 4% of cases are identified by external audit, and external auditors do not express an opinion as to the organization's effectiveness of internal controls.
- Identify vulnerabilities not previously known and fix them.
- Improve both preventive and detective controls.
- Improve processes to best protect the organization and its resources.

About 65th North Group

- Local government internal control and fraud risk vulnerability experts.
- Numerous studies have been conducted nationwide for city, county, and state government organizations.
- Staff qualifications:
 - Certified Fraud Examiners
 - Certified Internal Control Auditors
 - Have decades of Public Sector Leadership Experience
 - Hold a Certificate in Internal Control from the IIA and COSO
 - Have over 150 years of combined government experience
 - Ph.D. in financial management with a dissertation specific to local government fraud risk reduction and internal control modernization

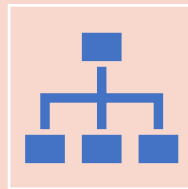
Why is fraud in local government operations a problem?



There is routine cash flow with a lot of opportunity to steal, should someone have that desire.



Good people sometimes experience incredible financial pressure. They don't always know how to deal with it, and sometimes, the most trusted people do the unthinkable.



Organizations sometimes believe that everything is good because nothing has been discovered, they have long-time employees, they have established policies, and they have regular audits.

Examples of areas of risk in government organizations – generally

Vendor payment fraud	IT & cybersecurity risks
Cash, check, and credit card payments	Fuel use management
Purchasing operations	Utility operations, including utility billing
HR functions	Inventory management
Payroll	Permitting
Subrogation	Accounts payable and accounts receivable
Refunds, voids, and chargebacks	Fictitious vendors
Travel advances / expense reimbursements	Much more

Audit Process

The audit process included the following:

- A comprehensive data review, including existing policies and procedures
- Employee interviews from every department
- On-site observations
- A best management practices diagnostic assessment
- A GAP analysis, identifying opportunities to reduce vulnerabilities
- Completion of a prioritized and phased implementation plan and a comprehensive written report with recommendations

Audit Process

The study is not designed to look for fraud but to identify the city's vulnerabilities that fraud could occur.

The study does not look at individual people but rather processes performed by people in specific job classifications.

Summary of results - POSITIVES

- The organization embraces the concept of effective internal controls
- There is a means for employees to report suspected wrongdoing anonymously
- The organization uses payee-positive pay
- The organization uses a professional fuel management system
- The organization conducts verification checks of vendors before vendor setup
- The city has a written ethics statement
- City employees were cooperative through all phases of this study
- Much more

Summary of results – Areas for improvement

- Several opportunities for improvement were identified, and the city has vulnerabilities that, when mitigated, will significantly reduce its risk of fraud.
- Reducing risks related to inventory management, purchasing, vendor maintenance, and fuel use management are areas for improvement.
- Implementing regular physical verification of inventory, fuel use analytics, physical verification of purchases, performing advanced data analytics, and completing an annual internal control and fraud risk vulnerability study will significantly reduce the city's inherent and residual internal control risks.

Next Steps

1

RECOMMENDATIONS
INCLUDE A PRIORITIZED
AND PHASED
IMPLEMENTATION PLAN

2

ADDRESS THE “LOW-
HANGING FRUIT” AND
HIGH-PRIORITY RISK
AREAS

3

YOU ARE DOING WELL –
BUT CONTINUE WITH
YOUR EFFORTS