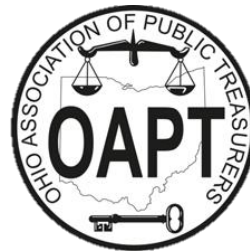


Ohio Association of Public Treasurers

Embezzlement & Fraud in Government

Presented by Sara M. Costanzo

October 6, 2021



1

Today's Agenda

- Embezzlement versus fraud
- Federal and state laws
- Red flags
- Avoiding losses
- Case examples



2

2



Embezzlement Versus Fraud

3

Embezzlement

- Involves the fraudulent appropriation of property or money that someone has been entrusted with, to utilize it for their own benefit
- Could be cash, company checks, jewelry, electronics, or even postage stamps



4

Embezzlement Cont.

- Different from regular theft because the person who takes the money or property generally has trusted and legitimate access to the valuables before they take them for their own use
- Can take a variety of forms:
 - A cashier taking a small amount of cash out of a cash register on a single occasion
 - A more sophisticated embezzlement scheme, using phony vendors and invoices to steal millions of dollars over a period of years



5

5

Embezzlement Cont.

- In 2017, state audits uncovered \$3.4 million in missing funds over the decade prior from 77 government groups across the state.
- Many cases were connected to theft, with 53 convictions resulting.
- 20 of those 77 cases were inside the utility clerk's office, most often involving cashier-level employees who deal directly with community members for payment intake.

**Ohio Auditor's Office*



6

6

Embezzlement Cont.

Entities with Findings since 2007	
Villages	22
School Districts	15
Courts	8
Counties	7
Cities	6
Agricultural Societies	3
Libraries	3
Health Departments	2
Sheriff's Departments	2
Townships	2
County Treasurer's Office	2
Ambulance District	1
Charter School	1
Environmental Services District	1
Park District	1
Water and Sewer District	1

Weltman
Weltman, Weinberg & Reis Co., LPA



*Ohio Auditor's Office

7

7

weltman

Types of Embezzlement

8

Types of Embezzlement

- Adjusting journal entries
- Void schemes
- Check substitutes
- Fictitious vendors
- Expense report padding



**Hiscox Embezzlement Watchlist*

Weltman
Weltman, Weinberg & Reis Co., LPA



9

9

Adjusting Journal Entries

- Background:
 - Certain situations require changes to the balance on a customer's account to correct billing errors, such as inaccurate meter readings or erroneous late fees.
 - Employees typically remedy these mistakes by creating entries in the entity's billing system, called non-cash adjustments.
 - This either increases or decreases the account balance to the proper amount owed.

Weltman
Weltman, Weinberg & Reis Co., LPA



10

10

Adjusting Journal Entries Cont.

- For example: an employee who receives a customer's payment does not record the transaction as a payment in the billing system.
 - The employee pockets the cash and creates a fraudulent adjustment to lower the customer's account balance back to zero.
 - Employees are more discreet and steal only part of a customer's payment, adjusting the account balance only enough to offset the stolen amount.



11

11

Void Schemes

- Background:
 - As many entities transition to web-based payment options, cash registers still prove useful for citizens who prefer to pay in person for utility payments, title and permit fees, and other public services.
 - Wherever cash registers are present, there also exists a need to cancel erroneous payments through voids.
 - When this procedure goes unchecked, local government dollars are left vulnerable to thieves who characteristically seek opportunities for fast money and an easy way to sweep their crimes under the rug.



12

12

Void Schemes Cont.

- The tactic works by manipulating an entity's paper trail to appear as if a customer's payment was refunded.
 - After a customer makes a payment, the offending employee re-enters the billing system and voids the transaction.
 - This maneuver shows the funds exiting the entity's system, allowing the employee to pocket the customer's payment with little evidence left on the government's side of the transaction.



13

13

Substitute Check Scheme

- Local governments occasionally receive atypical revenue in the form of mailed checks for rebates, insurance claims, and other one-off payments.
 - These unexpected checks are a welcome sight for thieves looking for fast money and an easy cover-up.
- In a check-substitution scheme, an employee with access to the entity's mail stumbles upon one of these checks and sets it aside until it is time to strike.



14

14

Substitute Check Scheme Cont.

- For example: a fiscal officer receives a letter that contains a \$100 rebate check for an equipment purchase.
 - Instead of recording the check in the accounting system, the fiscal officer discretely slides the check into a desk drawer and waits for a few customers to make cash payments.
 - The perpetrator must wait for enough customer cash payments to accumulate to a sum that covers the check amount and avoids drawing attention.
 - Then the fiscal officer substitutes the rebate check for an equal value of \$100 from the customer payments.



15

15

Substitute Check Scheme Cont.

- A deposit slip that lists \$500 in cash will no longer match the actual amount of cash inside the bank bag if someone substitutes a \$100 check.
 - While the overall amount recorded on the deposit slip is still accurate, only \$400 in cash is present in the bank bag.
 - The bank bag now contains an extra \$100 check that is absent from the deposit slip and the accounting system.



16

16

Fictitious Vendors

- Background:
 - Fictitious vendor fraud generally involves an employee in a position where they can create, authorize, or approve payments to vendors.



17

17

Fictitious Vendors Cont.

- An employee may set up a legitimate-looking business and create invoices from that business, submitting them to the company for work that was never done, or goods that were never provided.
 - The company or employee will approve the payment and send it to fraudulent company.
 - The employee will deposit the payment for their own use, in some cases using money laundering techniques to distance themselves from the cash.



18

18

Fictitious Vendors Cont.

- Employees who engage in fictitious vendor embezzlement may start out converting small amounts of money, testing their scheme, and later get more ambitious, possibly taking millions of dollars before their fraud is ever detected.
- A man in Ohio was charged with embezzling almost \$9 million in his position as an accountant through a fictitious vendor scheme over the course of more than 10 years.



19

19

Expense Report Padding

- Background:
 - Expense reimbursement fraud makes up about 15% of business fraud.*
 - It takes an average of about 24 months before expense report fraud is detected.

*The Association of Certified Fraud Examiners



20

20

Expense Report Padding Cont.

- Types of expense report fraud:
 - Claiming non-business related items
 - Inflating acceptable expenses – a \$5 Uber turns into a \$15 Uber charge (generally receipt is missing)
 - Overcharging the company card
 - Double billing – charging an item more than once, under separate events/trips
 - Exceeding the limits for allowable expenses - splitting large amounts into two or three items on the expense report



21

21

weltman

Fraud

22

Fraud

- Involves the improper appropriation of property or money that someone has been entrusted with, to utilize it for their own benefit
 - Chapter 2913 of the Ohio Revised Code states that fraud, as a criminal act of deception, means knowingly deceiving another or causing another to be deceived by any false or misleading representation, withholding information, preventing another from acquiring information, or by any other conduct, act, or omission.

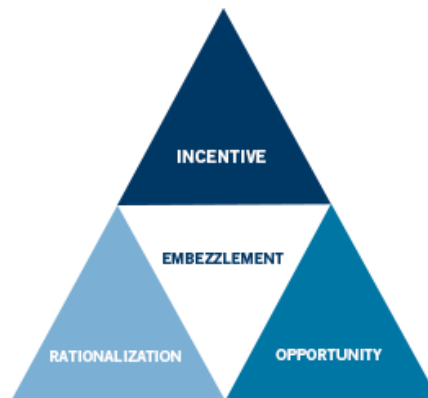


23

23

Fraud Triangle

- Incentive/pressures
- Opportunity
- Rationalization



24

24

Incentives or Motivation/Pressures

Personal financial pressures:

- Standard of living
- Living beyond means
- High personal debts or poor credit
- Student loan repayments
- Extended family issues
- Vices
- Unexpected crisis
- Change in life situation

Organizational financial pressures:

- Staffing issues
- Workload increase for those who remain
- Reimbursement reductions
- Shrinking budgets
- Increase in costs
- Regulatory pressures

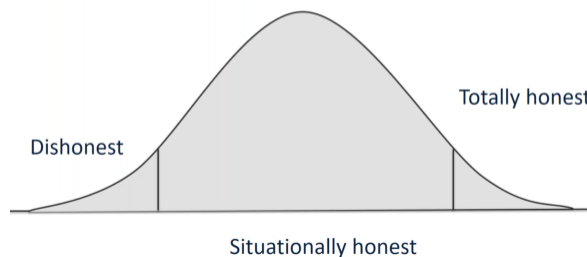


25

25

Rationalization

Rationalization theory



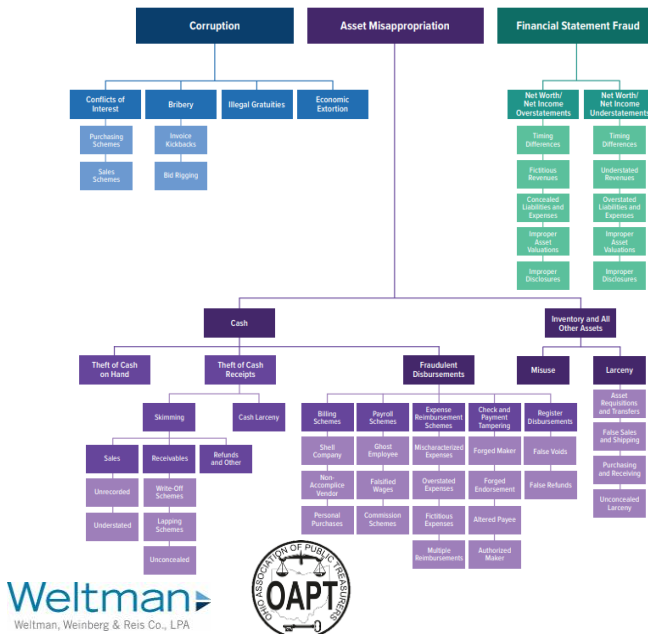
26

26

Who Commits Fraud

27

Fraud Classification (Fraud Tree)



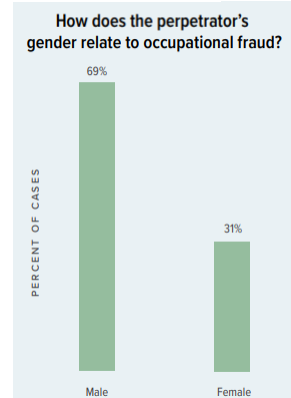
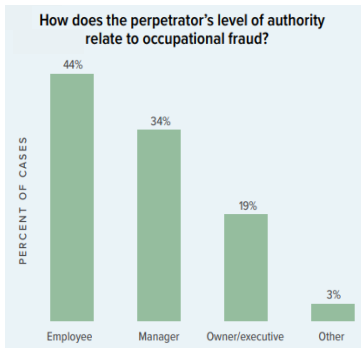
28

28

Fraud – Who Commits

2,690

real cases of occupational fraud



*2018 ACFE Report to the Nations

Weltman
Weltman, Weinberg & Reis Co., LPA

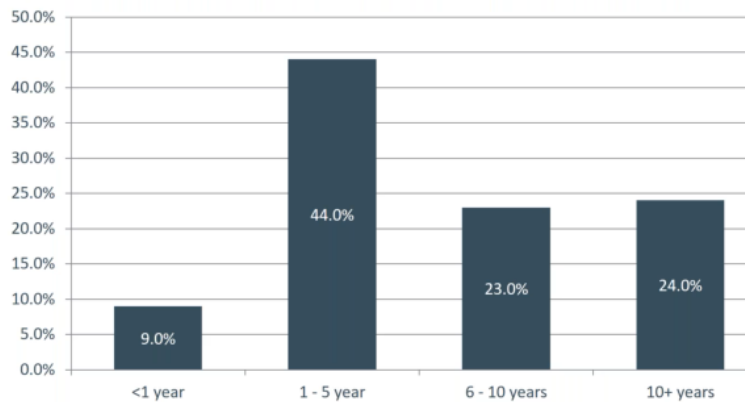


29

29

Fraud – Who Commits Cont.

Tenure of Perpetrator in Organization-amount of loss increases with more years employed



ACFE Report to the Nations 2018 Global Study on Occupational Fraud and Abuse

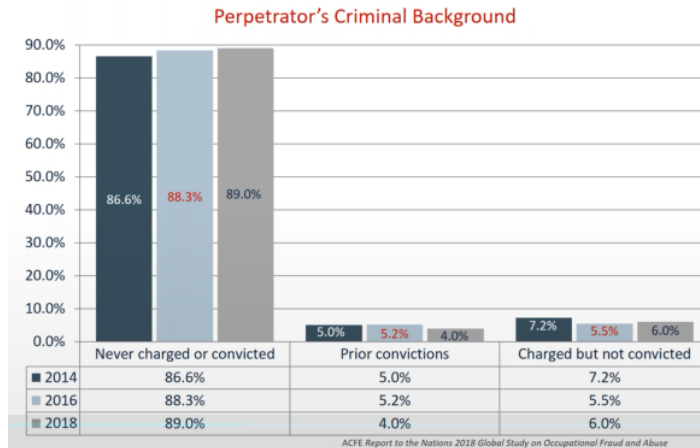
Weltman
Weltman, Weinberg & Reis Co., LPA



30

30

Fraud – Who Commits Cont.



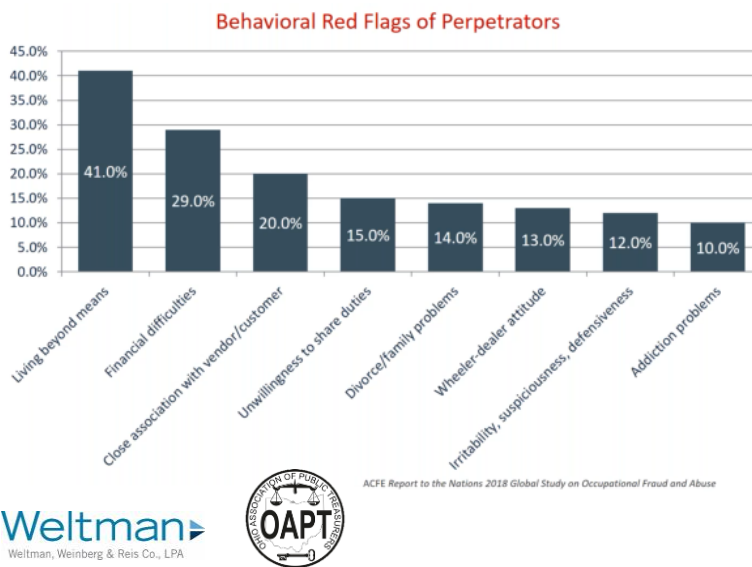
Weltman
Weltman, Weinberg & Reis Co., LPA



31

31

Fraud – Who Commits Cont.



Weltman
Weltman, Weinberg & Reis Co., LPA



32

32

Federal and State Laws

33

Federal and State Laws

- Fraud crimes can be prosecuted at either the state or federal level, depending on a number of factors:
 - Type of fraud scheme and amount of money stolen
 - Laws violated (federal, state, or both)
 - Method of operation
 - Use of public services (such as the U.S. Postal Service, telecommunication systems, and Medicare) that fall under federal or state regulation and authority
 - Location of the crime (within a state or across state or national borders)

34

Federal Laws - Penalties

- Federal fraud crimes are typically charged as felony offenses, though misdemeanor convictions are possible in certain situations.
 - The difference between a misdemeanor offense and a felony offense is that a felony has a potential sentence of a year or more in prison, while misdemeanor convictions can result in a prison sentence of up to one year.
 - There are a wide range of potential penalties for any federal fraud conviction, though they typically involve prison, fines, or probation.



35

35

Federal Laws – Penalties Cont.

- **Prison:** Someone convicted of a federal fraud crime faces serving time in a federal.
- **Fines:** The fine for any conviction of a federal fraud law can be extremely high.
- **Restitution:** Restitution is paid by perpetrators of fraud to the victims in order to compensate them for their losses.
- **Probation:** A federal judge can impose a federal probation sentence individually or in combination with a fine or a term of imprisonment in some situations.



36

36

Ohio Laws

- Under Section 2315.21 of the Ohio Revised Code, fraud victims can sue for:
 - Compensation, which represents the dollar value of the fraud, often with interest
 - Damages, which represent emotional distress and other harms that do not have a fixed dollar value, such as the negative impact on reputation
 - Punitive damages, which are noncriminal fines assessed by a judge or jury to discourage fraud in the future and to serve as an example to other people who may think of perpetrating a similar fraud



37

37

Ohio Laws - Statutes of Limitations

- Felonies and misdemeanors
 - Like many states, Ohio's law sets time limits for a host of specific crimes. For crimes not specifically listed in the statute, a general statute of limitations applies based on the category of the crime.
 - The general time limits are:
 - Six years for felonies
 - Two years for misdemeanors
 - Six months for minor misdemeanors
 - (Ohio Rev. Code Ann. § 2901.13 (2019).)



38

38

Ohio Laws - Statutes of Limitations Cont.

- Theft-related and fraud offenses
 - **Identity fraud:** Six years after the crime, or if this period has expired, five years after discovery of the offense
 - **Misconduct by public servant:** Any time while the person remains in office or in their position, or two years after leaving office or the position
 - **Offenses involving fraud or breach of fiduciary duty:** One year after discovery of offense (if the underlying time limit has expired)
 - **Felony theft (\$1,000 or more):** Six years after the crime
 - **Misdemeanor theft (less than \$1,000):** Two years after the crime



Ohio Laws - Statutes of Limitations Cont.

- Coronavirus and criminal statutes of limitations
 - In response to the coronavirus pandemic, the Ohio Legislature passed a bill tolling criminal statutes of limitations set to expire between March 9, 2020 and July 30, 2020 (A.B. 197, § 22.)





Red Flags

41

Red Flags

- Depending on the individual, their job, and the type of fraud, it can take years to discover fraud. In some cases, fraud may never be discovered at all.
- A number of red flags can alert an employer or company to possible fraud.
- Be aware of behavioral red flags.
- Set up and monitor a strong system of internal controls.
- Utilize anti-fraud controls.
- Utilize data analysis software.



Weltman, Weinberg & Reis Co., LPA



42

42

Red Flags Cont.

- Things to watch for:
 - An employee living a lifestyle that appears beyond their means or having financial difficulties
 - Increased depletion of petty cash
 - A suspiciously low inventory of goods
 - An employee who is defensive about taking time off
 - An employee that has too close of a relationship with some vendors
 - May also put some employers on notice of a possible inside theft



43

43

Red Flags Cont.

- In some cases, discovery of the fraud will come from a tip from a co-worker or someone who suspects the employee is taking money or property.
- Upon discovery of possible fraud, a company may conduct an internal investigation or take the information directly to law enforcement.



44

44

Risk Assessment

- Business/fraud risk assessment
 - Specific to your organization
 - Safeguard assets
 - Prevent fraud
 - Manage accuracy and reliability of accounting assets
 - Promote operational efficiency
 - Consider the size and complexity of your organization
 - Become part of the culture from top to bottom



45

45

Risk Assessment Cont.

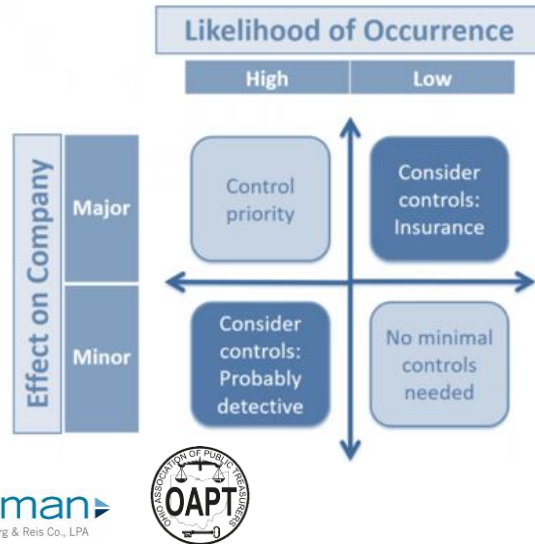
- Business/fraud risk assessment
 - Two types:
 - **Preventative:** Controls designed to discourage errors and irregularities.
 - **Detective:** Controls designed to identify an error or irregularity after it has occurred.



46

46

Risk Assessment Cont.



47

47

weltman

Avoiding Losses

48

Avoiding Losses – Any Recovery



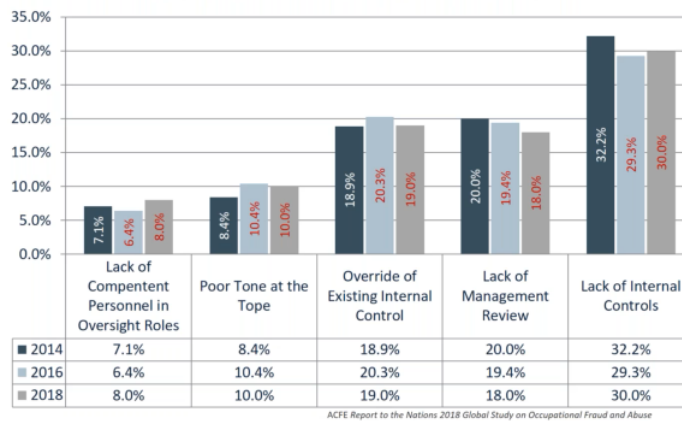
Weltman
Weltman, Weinberg & Reis Co., LPA



49

49

Avoiding Losses – Internal Control Weaknesses



Weltman
Weltman, Weinberg & Reis Co., LPA



50

50

Avoiding Losses

- Control cash receipts – issuing for all cash transactions in duplicate.
- Post all payments to a billing system.
- Routinely reconcile money in hand with documented deposits.
- Prepare bank deposit slips daily.



51

51

Avoiding Losses Cont.

- Review spending trends over time between similarly-situated employees.
- Educate employees and train managers on approving expense reports.
- Consider an automated expense management system.
- Use purchase orders.



52

52

Case Examples

53

Case Examples

- Former RTA board president plead guilty to theft charges.
 - Accumulated unpaid health insurance premiums during his more than two decades with the Greater Cleveland RTA
 - Signed up for, but did not pay, the costs associated with RTA-provided health insurance
 - Ordered to repay \$132,000 in restitution

54

Misuse of Credit Card / ATM & Unauthorized Expenses

- Highland Heights – Scott Coleman (former Mayor)
 - Embezzled \$160,000 from U.S. Rep. Dave Joyce's campaign
 - As treasurer of the Bainbridge township Republican's re-election operation between 2015-2018
 - Plead guilty to grand theft charges – a fourth degree felony
 - Repaid \$341,983.06 in restitution and investigative fees
 - Sentence still pending



55

55

Adjusting Journal Entry Scheme

- Village of Ripley – Katherine Lang
 - Drained nearly \$1 million from small community of 1,750 people
 - Had been in charge of the entire collection process:
 - Creating utility accounts
 - Collecting and posting payments
 - Making deposits
 - Indicted in 2010 on three counts of theft in office and seven counts of tampering with records
 - Sentenced to 13 years in prison
 - Restitution of \$1.1 million



56

56

Void Scheme

- Montgomery County – Rozalin Smith
 - Stole \$2,092 and an additional \$12,987 through other means
 - Incoming dollars from customer solid waste payments did not match the amounts transferred to the county treasurer's office
 - Plead guilty in 2015 to one count of theft in office and was sentenced to five years of probation and 40 hours of community service
 - Ordered to repay the stolen money



57

57

Check Substitute Scheme

- Cuyahoga County – Debbie Bosworth
 - Stole \$238,000
 - She worked for the Village of Chagrin Falls as a clerk in the building and utility departments, processing payments, making deposits, registering contractors, and other tasks. She would take cash from water bills and swap out checks from contractors for permits.
 - Plead guilty in 2021 after being charged with two counts of theft in office, 13 counts of tampering with records, and seven counts of money laundering (22 felonies)
 - Ordered restitution of \$310,000 (to cover the cost of her theft and the forensic audit) and probation



58

58

Pocketed Payments

- Cuyahoga County – Karla Hopkins
 - Stole \$40,000 from Maple Heights High School
 - Handled deposit of revenue from class dues, yearbook fees, auto tech, student council, flag-drill teams, book fines, and ID badge fines
 - Plead guilty in 2021 to one count of theft in office (a third degree felony)
 - Sentenced to 18 months in prison, and restitution
 - She had emptied her pension prior to being charged, which prevented the state from seizing those funds to pay back the district.



59

59

Pocketed Payments Cont.

- City of Marion – Brenda Nwosu
 - Stole \$34,276
 - Pocketed \$17,375 from customer payments and another \$16,901 in proceeds from incoming checks
 - Plead guilty in 2015 to one count of theft in office and was sentenced to 18 months of probation
 - Ordered to repay the stolen money



60

60

Pocketed Payments Cont.

- Belmont County – David Smith
 - Stole \$24,467
 - Former mayor, had proceeds from mayor's court deposited into his personal account
 - Plead guilty in 2020 to one count of theft in office and conflict of interest.
 - Ordered restitution of \$24,467, plus the cost of an audit – \$2,467. Also sentenced to 36 months incarceration for theft in office and 6 months for conflict of interest (to run concurrently)



61

61

Check Substitute Scheme

- Arlington Heights Mayor's Court – Donna Covert & Laura Jarvis (mother and daughter)
 - Stole \$260,000
 - Processing payments for fines, costs, and bonds, resulting in a shortage between collections and deposits
 - Covert pled guilty in 2013 and Jarvis in 2015 to one count of theft in office and were sentenced to one year and to nine months in prison
 - Ordered to repay the stolen money



62

62

Check Substitute Scheme Cont.

- Hillsboro City School District – Pam Ward
 - Stole \$6,548
 - Doctored financial records, failing to deposit lunch money collected
 - Plead guilty in 2012 to one count of theft in office and was sentenced to five years of probation
 - Ordered to repay the stolen money



63

63

weltman

About Weltman

64

About Weltman

- Nationally-recognized full service creditors' rights firm
- We represent creditors in:
 - Real estate default matters
 - Bankruptcy
 - Consumer and commercial collections
 - Commercial litigation
 - Municipal debt collections
 - Tax
 - Utility
 - Nuisance
 - Property damages



65

65

About Weltman

- We strictly adhere to compliance and security standards, with a premium on reputation management.
- To learn more about our leadership in accounts receivable management, visit weltman.com.



66

66

Questions?



Please feel free to contact me anytime:



Sara M. Costanzo
Shareholder

216.685.1039

scostanzo@weltman.com

The content of this presentation is not intended to constitute legal advice on specific matters, create an attorney-client relationship, or be legally binding in any way.

67