



CITY AUDITOR'S OFFICE

FY 2015/16 Report on the City Auditor's Integrity Line

June 8, 2016

REPORT NO. 1613

CITY COUNCIL

Mayor W.J. "Jim" Lane
Suzanne Klapp
Virginia Korte
Vice Mayor Kathy Littlefield
Linda Milhaven
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June 8, 2016

Honorable Mayor and Members of the City Council:

Enclosed is the *FY 2015/16 Report on the City Auditor's Integrity Line*, which was included on the Council-approved FY 2015/16 Audit Plan. The Integrity Line hotline serves to provide City employees and the public with a method for reporting suspected fraud, waste or abuse of City resources.

For this fiscal year, we received nine hotline contacts, most of which were appropriate for referral to other departments. As well, two situations were identified during recent audits.

If you need additional information or have any questions, please contact me at (480) 312-7867.

Sincerely,

A handwritten signature in blue ink that reads "Sharron Walker". The signature is written in a cursive style.

Sharron E. Walker, CPA, CFE, CLEA
City Auditor

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BACKGROUND

The Council-approved FY 2014/15 Audit Plan included establishing an Integrity Line hotline to provide the public and employees with a method for reporting suspected fraud, waste or abuse of City resources.

In July 2014, we established a phone number and an email account and created a web-based form to receive information. In November 2014, the City’s Communications staff helped launch the Integrity Line by putting informational updates in the mid-November issues of CityLine and Scottsdale Update.

Concerns can be reported to the Integrity Line anonymously; however, contact information is encouraged in case further information is required. To the extent allowed by law, the City Auditor’s Office will maintain confidentiality of all complaints, associated workpapers and other files.¹

City Auditor’s Integrity Line

(480) 312-8348

Audit@ScottsdaleAz.gov

www.ScottsdaleAZ.gov,
search “Integrity Line form”

Table 1 summarizes the guidance provided on types of concerns commonly investigated through an auditor-based hotline.

Table 1. Description of Fraud, Waste and Abuse

	Definition	Examples
Fraud	Intentional act or omission designed to deceive others and deprive the City of its resources or rights. These acts may be committed by persons who are internal or external to the City.	<ul style="list-style-type: none"> » Theft of City money, equipment or other assets » Use of City property for personal gain » Submitting invoices for fictitious goods or services » Falsifying records, such as timesheets or expense claims
Waste	Intentional or unintentional careless expenditure or mismanagement of City resources. Waste may not involve private use or personal gain.	<ul style="list-style-type: none"> » Purchasing supplies, goods or services at inflated prices » Failure to reuse or recycle major resources » Making unnecessary purchases
Abuse	Behavior that is seriously deficient or improper when compared to behavior that a prudent person would consider reasonable and necessary in the circumstances. Abuse includes misusing one’s position or authority as a City employee.	<ul style="list-style-type: none"> » Unauthorized disclosure of confidential or proprietary information » Providing a benefit for someone for which they do not qualify » Directing staff to perform personal errands for a supervisor

SOURCE: www.scottsdaleaz.gov/auditor/integrity-line

¹ Arizona Revised Statute §9.305(b) provides for confidentiality of audit files.

At the time concerns are reported, the source may not be able to prove that all elements have been met, such as an intentional act or omission, but should provide the details that lead to the belief that they have occurred.

Occupational fraud is defined as the use of one's occupation for personal enrichment through deliberate misuse or misapplication of the employer's resources or assets.

According to the Association of Certified Fraud Examiners, almost 40% of occupational fraud cases are detected by a tip, which is the most common detection method.² Also, the Association found that hotlines are an effective method of collecting tips. In organizations *with* hotlines, tips led to identifying 47% of frauds detected, while less than 30% of detections resulted from tips in organizations *without* hotlines. As a further sign of effectiveness, organizations *with* hotlines experienced frauds that were less costly and detected more quickly than in organizations *without* hotlines.

Table 2 illustrates the Association's analysis of case data studied.

Table 2: Median Loss and Duration Effect of a Hotline

	Hotline in Place	Hotline Not in Place	Percent Reduction
Median Loss	\$100,000	\$200,000	50%
Median Duration of Occurrence	12 months	24 months	50%

SOURCE: *Report to the Nations on Occupational Fraud and Abuse: 2016 Global Fraud Study*, Association of Certified Fraud Examiners

The benefits of having the Integrity Line include the deterrence of fraud, waste and abuse; improvement in controls, policies and procedures; and increased operational efficiencies.

Internal control audit recommendations are often seen as added "red tape" or too time-consuming. However, the Association's report identifies internal control weaknesses as contributing to the fraudster's ability to perpetrate the crime in 29% of frauds. And in another 20%, the perpetrator had overridden intended controls to carry out the fraud. Effective internal controls provide the checks and balances needed to reduce the risk of such losses.

Figure 1, on page 5, illustrates the primary steps in the City Auditor's Integrity Line complaint review process.

² *Report to the Nations on Occupational Fraud and Abuse: 2016 Global Fraud Study*, Association of Certified Fraud Examiners. Since 2002, the Association has performed this study by surveying its members biennially about certain characteristics of their cases. The study's purpose is to analyze how occupational fraud occurs, how it is discovered and its financial impact.

Figure 1. Integrity Line Information Review Process



SOURCE: Summary of City Auditor's Integrity Line procedures

The Integrity Line page on the City's website outlines examples of matters that should *not* be reported to the City Auditor's Office, including:

- Complaints against private businesses, unless the issue involves City operations, resources or employees
- Disputes between individuals
- Potential fraud related to county, state or federal assistance programs unless the program is being operated by the City of Scottsdale
- Emergencies or other public safety concerns

Anyone with knowledge of potential fraud, waste or abuse of City resources may submit the information via the City's website (search for "integrity line" or "integrity form"), call (480) 312-8348 or email Audit@ScottsdaleAZ.gov.

RESULTS

The Integrity Line received nine unique reports in FY 2015/16, and two issues were identified during audits.

Email and phone have consistently been the most common contact methods through which concerns are relayed to the Integrity Line, as shown in Table 3.

Table 3. Source of Integrity Line Information

Source	FY 2014/15	FY 2015/16
Email	3	3
Phone	0	4
Web form	0	2
Mail	1	0
Referral	1	0
Audit	0	2
Total	5	11

SOURCE: Analysis of City Auditor's tracking database.

The fraud-related issues identified during audits included a \$700 theft from a City safe, which we learned of during our Cash Handling and Accountability audit for FY 2015/16, and an overbilling, which we learned of during our Transit Contracts audit.

The theft was reported to the Police Department, but controls were insufficient to identify the responsible party. We again recommended in the Cash Handling audit that the number of employees with safe access be reduced to the minimum possible.

When Transit staff identified vendor overbillings, the vendor was not paid for the questioned transactions and is no longer used to provide services. We will be reviewing earlier transactions to evaluate whether some were paid before this discovery.

In situations like these, reporting the issue to the City Auditor for review can help to ensure the full extent of loss has been identified as well as determine whether internal control procedures may be improved to avoid future losses.

Of the FY 2015/16 reported issues, as shown in Table 4, most were referred to other departments for resolution. The referrals included such matters as construction debris noncompliance, a need for senior support services and similar nonaudit concerns.

Table 4. Disposition of Integrity Line Information

Disposition	FY 2014/15	FY 2015/16
Open	0	2
Closed:		
Referral	2	6
Report *	2	1
No Action	1	2
Total	5	11

* - The Report category includes a separate report or the annual report.

Two contacts in FY 2015/16 were not pursued further due to insufficient information or they did not relate to potential fraud, waste or abuse of City resources.

The theft from a City safe is reflected as a "Report" in Table 4 as it was included in the FY 2015/16 Cash Handling audit.

Two items remain pending further investigation.

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The City Auditor's Office conducts audits to promote operational efficiency, effectiveness, accountability, and integrity.