

governmental viewpoint

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Studies show that the most common type of fraud, regardless of the industry, is asset misappropriation. Specifically, this includes misappropriation of cash, supplies, inventory and accounts receivable. This isn't surprising considering these assets are generally readily convertible to cash and easy to conceal and misappropriate. Common internal

- Custody of assets
- Periodic reconciliation of existing assets to recorded amounts.

Lack of Appropriate System of Authorization and Approval of Transactions - This internal control function is designed to make sure that transactions are recorded accurately and appropriately. It also serves as an audit trail, and thus a deterrent.

Inadequate Record-keeping - Intelligent decisions cannot be made without information.

Accounting information that cannot be retrieved on a timely basis can cripple a governmental unit as well as open the door to fraud.

Lack of Independent Checks - In order to evaluate whether an area is functioning as expected, an

area independent of the function should be responsible for evaluation. This serves two purposes: to identify fraud and to act as a deterrent to fraud.

Poor Physical Safe-guards - Access to cash, investments, fixed assets and inventory should be limited to authorized personnel. These assets should be physically guarded as needed using vaults, safes and locks with personnel assigned to enforce the security.

Failure by Management to Take an Active Role in Internal Controls - Management, including governing boards, is the key to an effective internal control system. They must take an active role and make employees aware of their commitment to it.

Failure to Enforce Policies and Procedures Designed to Strengthen Internal Control -

Internal control has two components: having the internal control in the first place and then making sure it is enforced.

Lack of Job Applicant Screening

- Many employers have caught an employee stealing only to find out that they were fired from their last job for doing the same thing.

In evaluating the internal controls of an organization, focus on those areas that are most susceptible to fraud and abuse and produce a financial impact. Identify what procedures should be in place and complied with on a regular basis. Concentration in these areas should result in a more cost effective internal control system and a reduction in the amount of fraud being committed within an organization.

Our firm has helped many governmental units address fraud prevention issues. We would be pleased to assist you in reviewing your internal controls. Please call us to discuss how we may be of service.

Parts of this article are taken from the Association of Certified Fraud Examiners.

Common Fraud Types and Their Prevention

By Casey Garan

control weaknesses that can leave an entity vulnerable to fraud are:

Lack of Management Oversight - Management, including governing boards, must be watchful. A lack of management presence, a perceived "we don't care" attitude, creates a situation that is ripe for fraud.

Lack of Appropriate Segregation of Duties - The concept behind the most recognized control, adequate segregation of duties, is to limit the opportunities a person has to commit a fraud (or error) and conceal it. As we all know, the person who writes the checks should not be the one who reconciles the bank account. Four types of responsibilities that should be performed by different personnel are:

- Authorization to execute transactions
- Recording of transactions

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GASB 34 - PART 5

by Jerry Funk, CPA

As discussed in previous issues, the issuance of GASB Statement 34, **Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments** will drastically change the way governmental units report in compliance with generally accepted accounting principles. This article discusses the presentation of fixed assets in the government wide financial statements. This is perhaps one of the most controversial areas of the new statement, drastically changing the way governmental units have reported capital assets and infrastructure. It is also an area which governmental units should allow for plenty of information gathering time prior to their unit's implementation date.

Under the old reporting method, fixed assets were only presented in the fund columns of the proprietary fund types, enterprise and internal service funds. All other assets of the governmental unit were presented in the general fixed asset account group. GASB 34 will require governments to report all capital assets, including infrastructure assets, in the statement of net assets rather than as expenditures. Thereby, eliminating the general fixed asset account group and reporting the capital assets in the governmental activities column. The proprietary funds will continue reporting assets in their respective column on the statement of net assets.

The statement provided the following definitions to apply when implementing GASB 34:

- ◆ Capital assets are land and improvements, easements, buildings and improvements, vehicles, machinery, equipment, works of art and historical treasures, infrastructure and other tangible or intangible assets used in operations that have initial useful lives longer than a single reporting period.
- ◆ Infrastructure assets are long-lived capital assets that normally are stationary in nature and can be preserved for a significantly greater number of years than most capital assets. Examples are roads, bridges, tunnels, drainage systems, water and sewer systems, dams and lighting systems.

As a basis for valuing the assets in the financial statements, the assets should be reported at historical cost. Donated assets should be reported at estimated fair value at the date of donation. The historical cost valuation received a lot of criticism upon issuance with critics stating that the costs of collecting the data would significantly outweigh the benefits received from reporting them in the financial statements.

To minimize the cost of the implementation, the GASB allowed for:

- ◆ Initial capitalization using deflated current replacement costs to represent estimated historical cost.
- ◆ Bond documents, engineering documents and capital project fund expenditures to be used as source documents when estimating historical cost.
- ◆ Limiting capitalization to major assets as defined by GASB 34.
- ◆ The required retroactive capitalization period does not need to extend beyond years ending after June 30, 1980.
- ◆ Composite depreciation rates based on groupings of similar assets or classes of dissimilar assets.
- ◆ Extending the deadline for reporting infrastructure assets retroactively for larger

governments by four years and allowing smaller governments to report on a prospective basis only.

Assets will be reported in the statement of net assets, net of accumulated depreciation. The depreciation expense will be reported in the statement of activities. The assets should be depreciated over the estimated useful life of the asset.

For qualifying infrastructure assets, such as bridges and roads, governments may use the modified approach, under which they do not

GASB, or the Governmental Standards Accounting Board, has been designated as the body to establish accounting principles for the state and local governments.

depreciate the assets, but instead focus on maintenance expenses and the annual cost to sustain the usefulness of the asset indefinitely. To be eligible for the modified approach, your government must meet two requirements for each asset network or subsystem it wishes to report this way:

1. The government must manage the assets with an asset management system that:
 - ◆ Has an up to date inventory of the assets;
 - ◆ Assesses the physical condition of the assets and summarizes the results using a measurement scale; and

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ANALYTICAL PROCEDURES

By: Jill Janssen, CPA

At first glance, your government's financial reports may just look like a lot of numbers on the page. How can you tell if the financial picture is favorable or not? How do you make decisions for the next period based on the information? One way to meaningfully interpret the financial results presented in such reports is to review them using analytical procedures.

Analytical procedures are the comparison of financial results with expectations, and the evaluation of the relationship between pieces of information. If the amount of cash held in interest bearing accounts increases for the period, you would probably expect the amount of interest income to also increase. If the collection of a new tax has been approved, you would expect to see an eventual increase in tax revenues.

Situations like those mentioned above are the basis for developing an expectation of the government's financial results. This is the starting point for using analytical procedures. An expectation can be formulated based on factors such as: prior period balances, current year budgets, the relationship between certain pieces of information, or non-financial factors.

Prior period balances

Often, it is reasonable to expect that current period results would be similar to the prior period. However, this would not be the case if conditions from the prior period have changed. Things like receiving a one-time grant or funding a large capital project may have occurred in one period and not in the other.

Current year budgets

The current year budget may be a better basis for developing expectations, as the budget is usually based on the plans and economic projections for the period. In order to provide meaningful information, the budget should be as realistic as possible.

Relationship between items

The relationship between some financial items is such that the results of one will naturally effect the results of the other. Items that will probably correspond with one another are things like payroll expense and payroll tax expense; lease payments and interest expense on leases; or accumulated depreciation and depreciation expense.

Non-financial factors

Non-financial factors can also play a role in developing an expectation. These are events that are not, in

themselves, financial, but will effect the revenue or expenses of the government. For example, an unusually heavy snowfall may result in more overtime for snowplow drivers, which in turn, increases the payroll expense. The recent Presidential election was not a financial transaction, but did result in increased costs related to voting.

The financial reports prepared each period can be formatted to easily facilitate the use of analytical procedures. Prior period and budget information can usually be included right next to the current year actual information, enabling you to simply scan the report, looking for numbers that don't seem to have a reasonable relationship to one another. Unusual items can then be further investigated in order to get a better understanding of what is causing the variance.

Analytical procedures can be used to efficiently interpret financial results. This could facilitate a better understanding of your current financial situation and aid in planning for the future. We are available to assist you in developing effective analytical procedures for your governmental unit.

- Excerpts taken from The PPC Nonprofit Update

GASB Part 5 Continued

- ◆ Estimates each year the amount needed to maintain and preserve the assets at the condition level the government has established.
- 2. Your government must document that the assets are being preserved approximately at or above the condition level it chooses. It does so by disclosing this evidence in supplementary schedules to the financial statements.

Through this brief review of the fixed asset presentation, it is clear to see that there are decisions and estimates that need to be thought of well ahead of the year in which GASB 34 will be required to be implemented for your governmental unit. Should your governmental unit have questions as to how to prepare for the implementation of this new statement, please feel free to contact us.

-Excerpts were taken from the PPC Government Update



Lindgren, Callihan, Van Osdol & Co., Ltd. is one of the leading regional accounting firms in northern Illinois, providing services to over 6,000 governmental, financial, industrial, commercial, and individual clients. The firm employs more than 100 professionals including nineteen officers and over 40 CPAs with offices located in Freeport, Rockford, Sterling and Dixon.

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INTERNET SITES

Government Related....

www.state.il.us/cms- Central Management Services home page. The local government section contains information on joint purchasing, vehicle service program and surplus property distributions available to local governmental units.

www.extension.uiuc.edu/com/com-dev- Articles, fact sheets and related links for community development

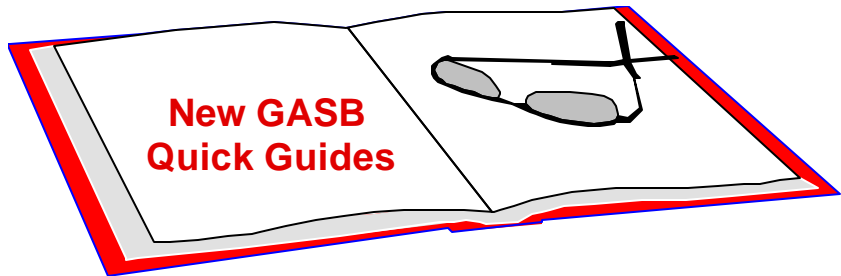
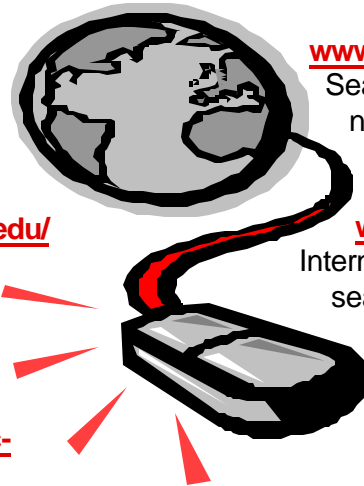
www.naatat.org/ncsc- National nonprofit organization devoted to serving the leaders of America's smaller communities.

Just for Fun...

www.jumptheshark.com- Voting for the defining moment when your favorite tv show begins its downhill slide.

www.555-1212.com- Searches based on name, address and phone number.

www.imdb.com- Internet movie database- search for movie quotes, titles, characters, cast and crew.



- The GASB has produced the following new "quick guides":
- ★ The Quick Guide to Local Government Financial Statements
 - ★ The Quick Guide to School District Financial Statements
 - ★ The Quick Guide to State Government Financial Statements

The guides were created for governments to provide to their governing boards such as city councils, school boards and other elected officials. The guides provide a short and understandable explanation of how to read and analyze governmental financial statements.

The guides can be ordered for \$4.95 each by calling the GASB at 1-800-748-0659.