

THE BOARD OF COMMISSIONERS

TONI PRECKWINKLE

PRESIDENT

EARLEAN COLLINS	1st Dist.	PETER N. SILVESTRI	9th Dist.
ROBERT STEELE	2nd Dist.	BRIDGET GAWER	10th Dist.
JERRY BUTLER	3rd Dist.	JOHN P. GALEY	11th Dist.
WILLIAM M. BEAVERS	4th Dist.	JOHN A. FRITZHEY	12th Dist.
DEBORAH SIMS	5th Dist.	LARRY SUFFREDIN	13th Dist.
JOAN PATRICIA MURPHY	6th Dist.	GREGG GOSLIN	14th Dist.
JESUS G. GARCIA	7th Dist.	TIMOTHY G. SCHNEIDER	15th Dist.
ERWIN RETES	8th Dist.	JEFFREY R. TOBOLSKI	16th Dist.
		ELIZABETH ANN DOODY GORHAM	17th Dist.



OFFICE OF THE INDEPENDENT INSPECTOR GENERAL

PATRICK M. BLANCHARD

INSPECTOR GENERAL

69 West Washington
Suite 1160
Chicago, Illinois 60602
TEL (312) 603-0350
FAX (312) 603-9948

July 5, 2011

President Toni Preckwinkle
and Members of the Board of Commissioners
of Cook County
118 North Clark Street
Room 517
Chicago, Illinois 60602

Re: Review of Accounting Errors (IIG11-0027)

Dear President Preckwinkle and Members of the Board of Commissioners:

This letter is written in accordance with Section 2-289(c)(2) of the Independent Inspector General Ordinance, Cook County, Ill., Ordinances No. 07-O-52 (2007) (“OIG Ordinance”) in connection with an investigation conducted in relation to the accounting errors totaling approximately \$90 million disclosed by the Office of the President on June 10, 2011. In accordance with the OIG Ordinance, this statement is made to apprise you of the completion and results of this investigation.

Background

On June 1, 2011, we were informed that the financial management team (“Financial Team”) of Cook County government identified revenues in the aggregate of approximately \$106.4 million that had been erroneously reported in Cook County’s public financial report for fiscal year 2009. The \$106.4 million error was attributed to \$39.9 in home rule tax misclassification and the double counting of \$66.5 million in sales tax revenue. Cook County has subsequently reduced the estimated error to \$90 million.¹ (Exhibit A) The Financial Team asserted that these accounting errors were attributed to mistakes made by the former Director of Financial Reporting for Cook County. It is our understanding that the Director of Financial Reporting was responsible for the final preparation of the County’s Financial Reports. Additionally, the Director of Financial Reporting worked closely with the County’s external auditors from Deloitte to complete their audit of the County’s fiscal 2009 financial report. We conducted a review of this matter to determine whether the County’s financials were misstated due to an accounting error or accounting fraud and whether other deficiencies exist that expose the process to reoccurring financial reporting misstatements.

¹ We were subsequently informed by the Comptroller’s Office that the tax misclassification was reduced from \$39.9 million to approximately \$21.7 million. The Comptroller claimed that a more detailed review was conducted which revealed that approximately \$18.2 million was properly recorded in the 2009 CAFR.



Summary of Investigation

The evidence developed during the course of this investigation does not support a contention that Cook County employees intended to commit accounting fraud. We believe, however, that the accounting errors were directly related to weak or non-existent internal controls, the lack of effective communication and a reoccurring failure to review and approve manual journal entries. The Financial Team decided to make an accounting adjustment to the County's 2009 financial reports in order to accurately reflect the County's financial position for fiscal year 2009. We believe there should be significant attention focused on improving internal controls within the Comptroller's Office to prevent such accounting errors from reoccurring in the future.

OIG Findings and Conclusions

Cook County's Accounting Methods

This office conducted interviews of various members of the Financial Team, employees of the Comptroller's Office, as well as internal and external auditors. We also conducted a review of Cook County's methods and financial reporting obligations. During this review, we discovered that the Comptroller's Office generates internal budgetary reports that are based on actual cash receipts from taxes. These reports are restricted to internal use by Cook County government.² The Comptroller's Office is also required to generate external financial reports that are distributed to outside investors and made available to the general public (referred to as "CAFR").³ The CAFR must adhere to Generally Accepted Accounting Principles ("GAAP"). Cook County uses the "modified-accrual basis" of accounting to prepare the CAFR and to comply with external financial reporting obligations pursuant to GAAP.⁴

Pursuant to the modified-accrual basis of accounting, sales tax revenues for 2009 that are held by the State at the County's fiscal year-end and are transmitted to the County within 60 days of fiscal year-end can be recorded in 2009. Accordingly, the Comptroller's Office had to perform the following adjustments to the 2009 Budgetary Report to convert it to the 2009 CAFR in order to include the proper revenues for 2009:

Starting Point	Fiscal 2009 Budgetary Report
Add: December 2009 sales tax receipts	
Add: January 2010 sales tax receipts	
Subtract: December 2008 sales tax receipts	

² In this case, Cook County government is the Office of the President and the Board of Commissioners.

³ The CAFR is the Comprehensive Annual Financial Report. The CAFR requires that management provide a narrative introduction, overview and analysis to accompany the basic financial statements in the form of a management discussion and analysis.

⁴ Under the modified-accrual basis of accounting, revenues are recognized when measurable and available for financing current obligations.

Subtract:	January 2009 sales tax receipts
Ending Point	2009 CAFR

The Accounting Errors

During our investigation, we discovered that the accounting errors occurred when the Comptroller's Office added December 2009 and/or January 2010 sales taxes to the internal budgetary reports in order to generate the CAFR for financial reporting purposes. The accounting errors comprised of (i) a \$21.7 million home rule tax misclassification and (ii) double counting \$66.5 million in sales tax revenue.

1. *Home Rule Tax Misclassification*

According to the Financial Team, the Director of Financial Reporting erroneously recognized approximately \$21.7 million in home rule tax revenue for fiscal year 2009 that belongs to fiscal year 2010.⁵ Moreover, the Financial Team has indicated that the home rule tax figure can be reclassified to the proper period and the accounting error will be inconsequential to the County's financial position for internal purposes. During our investigation, we interviewed witnesses and obtained a sample of supporting documentation to verify these assertions.

The Comptroller's Office represented in the CAFR that the County's home rule taxes were overstated by \$21.7 million in fiscal year 2009. According to testimony and supporting documentation, the Director of Financial Reporting recorded December 2009 home rule taxes for fiscal year 2009.⁶ (Exhibit B) Pursuant to Cook County's accounting policies, however, these home rule taxes rightfully belong to fiscal year 2010. (Exhibit C) As such, the CAFR must be adjusted so that fiscal year 2009 will be \$21.7 million lower than originally thought and fiscal year 2010 will reflect \$21.7 million higher than originally thought.

Importantly, this accounting error does not affect the internal budgetary reports and is a matter of matching revenue and expenses to the proper financial period for external reporting purposes. The "matching principle," however, is a keystone accounting principle pursuant to GAAP. Accordingly, this accounting error may be the focus among outside investors who purchase the County's municipal debt. The sales tax double entry accounting error, however, is an entirely different matter because that accounting error recognized revenue that the County did not earn.

⁵ With respect to the accounting error, the home rule taxes were primarily from cigarette, gasoline, and parking taxes.

⁶ The OIG interviewed the employee who originally discovered the accounting error, employees from the Comptroller's Office, and the external Auditors. The OIG received confirmation from these individuals that this was indeed an accounting error.

2. Sales Tax Double Entry

According to the Financial Team, the 2009 CAFR was misstated partially due to double counting approximately \$66.5 million of certain State of Illinois sales tax revenues.⁷ (Exhibit D) During our investigation, we obtained financial records that displayed the following manual journal entries made by two Cook County employees:

Fiscal Period	Explanation	Amount	Batch Date	Tax Date	Business Unit	User Id
11/27/2009	Rev FY 09 60 Days	-33,397,287.00	4/20/2010	2/28/2010	1809	User A
11/27/2009	Rev FY 09 60 Days	-32,473,603.00	4/20/2010	2/28/2010	1809	User A
11/30/2009	09 60 Days Receivables	-33,397,287.28	4/22/2010	11/30/2009	1809	User B
11/30/2009	09 60 Days Receivables	-32,473,602.91	4/22/2010	11/30/2009	1809	User B
Grand Total		-131,741,780				

Source: The Comptroller's Office

On April 20, 2010, User A entered the first set of entries totaling \$66 million. User A is a Business Manager in the Financial Controls Section of the Comptroller's Office. He directly reports to the Director of Financial Controls. Additionally, User A is normally responsible for recording routine transactions on a daily basis for the internal budgetary report. User A has asserted that he has entered the same sale tax accrual journal entry during the closing process for the last five years. Moreover, he indicated that the Director of Financial Controls provides him with the figure to enter into the accounting system each year.

On April 22, 2010, User B, the Director of Financial Reporting, entered the second set of entries totaling \$66 million.⁸ User B is primarily responsible for the conversion of the internal budgetary reports to the CAFR, which requires him to accrue for tax revenue.

Insufficient evidence exists to support a concern that these journal entries were entered into the accounting system with an intention to deceive or defraud. The evidence has revealed, however, that the Comptroller's Office does not have a very basic though extremely important internal control protocol over the journal entry process on the CF ledger or CAFR process. There should be segregation of duties between the person who enters the

⁷ The overstatement primarily consists of State of Illinois sales taxes also referred to as the IPTIP revenue accounts (Illinois Public Treasurer's Investment Pool tax allotments). The double recording comprised of two manual journal entries which were for \$32,397,287.28 and \$32,473,602.91.

⁸ The supporting work papers maintained by the Director of Financial Reporting for fiscal year 2009 cannot be located by the Comptroller's Office. The unavailability of documentation to supply an audit trail reveals a material record keeping deficiency that also requires corrective action.

journal entry and the person who can approve the journal entry for posting to the CAFR. For example, the internal budgetary reports (a/k/a AA ledger) has an internal control built into the accounting system that prevents a person from entering a journal entry and posting that same journal entry to the internal budgetary reports. Likewise, the CAFR should have the same computer fail-safe to offer additional protection against accounting errors.

An additional system problem was discovered involving the accounting system whereby users have the capacity to input "one-sided" journal entries on the CF ledger. According to generally accepted accounting principles, the accounting equation requires assets to equal equity and liabilities. In order to achieve this balance, double-entry accounting is required. That is, a credit entry for every debit entry and vice versa. We found that the CF ledger or CAFR side of the system allows users to input just a debit or credit. We discovered this was done, in some cases, in order to balance the books. These one-sided journal entries serve to mask a flaw in the accounting system.

Finally, our investigation revealed a lack of communication, supervision and documentation within the Comptroller's Office during the period at issue. These problems also contributed to creating an environment that made accounting errors more likely.

OIG Recommendations

We believe the fiscal year end 2009 accounting misstatements were unintentional errors. During that period, the Comptroller's Office experienced a substantial amount of turnover of key employees. This resulted in a confused environment contributing to the accounting errors. Moreover, these conditions continue to exist in the Comptroller's Office. Accordingly, we recommend the Comptroller's Office address the weaknesses in internal controls by adopting accounting fail-safe procedures in its system, establishing protocol to cure the lack of communication and ensure documentation is maintained to support journal entries.

These matters are of fundamental importance because the accounting errors contributed to the recent Cook County credit rating downgrade by Moody's Investment Services which carries the potential for a negative financial impact for Cook County. In light of the facts developed during this investigation, we recommend the implementation of the following measures to assist in rectifying these conditions.

- The Comptroller's Office should thoroughly review the CF ledger for any incorrect journal entries performed in prior years. The target time period should extend far enough to provide reasonable assurance that these particular revenue accounts do not contain similar accounting errors.
- The Comptroller's Office should further examine the one-sided journal entries issue to determine the source of the problem and whether such entries misrepresent the County's financial position. Additionally, the Comptroller's Office should

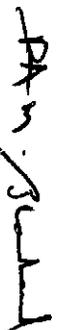
Hon. Toni Preekwinkle and Members of the
Board of Commissioners
July 5, 2011
Page 6

collaborate with Cook County Management Information Systems to identify the application failure and implement corrective action to prevent the capacity to make one-sided entries in the future.

- The Cook County Audit Committee should confer with outside auditors to determine whether the audit methodology, scope and testing should be modified to detect any similar accounting errors in the future.
- The Comptroller's Office should segregate duties between those who enter journal entries to the CF ledger and those who post these entries to the CF ledger. Specifically, the CF ledger should contain the same restrictions on entering and posting journal entries that are found in the AA ledger. Further, this segregation of duties should contain a supervisory component to ensure accountability for improper journal entries posted to the CAFR.
- The Comptroller's Office should create specific job descriptions with clearly defined duties.
- Documentation to support manual journal entries must be maintained by the Comptroller's Office in accordance with a standardized record keeping protocol.

In accordance with Section 2-285(e) of the OIG Ordinance, we will be in contact with the Comptroller's Office to follow-up with regard to the remedial action being implemented by that office. Thank you for your consideration to these issues. Should you have any questions, please do not hesitate to contact me.

Very truly yours,



Patrick M. Blanchard
Independent Inspector General

cc: Mr. Kurt Summers, Jr., Chief of Staff, Office of the President
Ms. Laura Lechowicz Felicione, Special Assistant to the President
Mr. Tariq G. Malhance, Chief Financial Officer
Ms. Constance M. Kravitz, Cook County Comptroller

IG-11-0027

EXHIBIT A

THE BOARD OF COMMISSIONERS
TONI PRECKWINKLE

PRESIDENT

EARLEAN COLLINS	1st Dist.	PETER N. SILVERSTEIN	9th Dist.
ROBERT STEELE	2nd Dist.	BRIDGET GAINER	10th Dist.
JERRY BUTLER	3rd Dist.	JOHN F. DALRY	11th Dist.
WILLIAM M. BEAVERS	4th Dist.	JOHN A. BRITZGERY	12th Dist.
DEBORAH SIMS	5th Dist.	LARRY SUPEREDIN	13th Dist.
JON PATRICIA MAURPHY	6th Dist.	GREGG GOSULIN	14th Dist.
JESUS G. GARCIA	7th Dist.	TIMOTHY O. SCHNEIDER	16th Dist.
EDWIN REYES	8th Dist.	JEFFREY R. TOROGLSKI	18th Dist.
		ELIZABETH ANN DOODY GERMAN	17th Dist.



COOK COUNTY
BUREAU OF FINANCE

TARIQ MALHANCE
CHIEF FINANCIAL OFFICER

County Building
118 North Clark Street, Room 1127
Chicago, Illinois 60602-1423
TEL (312) 603-5287
FAX (312) 603-3681
TDD (312) 603-5255

June 10, 2011

To Whom It May Concern:

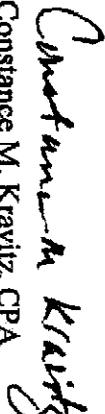
In May 2011, the financial management team of The County of Cook, Illinois (the "County") identified, in connection with the on-going fiscal 2010 external audit process, that revenues had been erroneously reported in fiscal year 2009 on the modified accrual basis of accounting in the general fund financial statements, and on the full accrual basis of accounting in the government-wide financial statements. The County financial management team determined that the errors were primarily the result of improper journal entries recorded during the fiscal year 2009 financial closing process which resulted in (i) the double-recording of certain non-property tax revenues, primarily including State of Illinois sales taxes, and (ii) the over-accrual of revenues that should have been attributed to December 2009 (fiscal year 2010) from certain taxes imposed by the County under its home rule powers (i.e. cigarette tax) and/or from fee office charges. In the general fund, the combined result of the errors was to overstate County assets and revenues on the modified accrual basis of accounting by approximately \$90 million. The government-wide financial statements on the full accrual basis of accounting were misstated by approximately \$55 million. As restated, the general fund balance for fiscal year 2009 is approximately \$100 million.

In consultation with the President's Office, the Chairman of the Audit Committee of the Cook County Board of Commissioners and its independent auditors, the County's financial management team has determined to restate the beginning fund balance for the general fund and the beginning net deficit for the governmental activities of the government-wide financial statements in its fiscal 2010 basic financial statements.

The County has appointed a new Director of Financial Reporting, effective June 6, 2011, to ensure that proper financial closing and reporting policies, procedures, and internal controls (specifically journal entry recording and authorization controls) will be implemented to mitigate the future risk of material misstatement.

The financial management team has concluded that these errors are material to the previously issued basic financial statements and auditor's report thereon; accordingly, the County has removed the 2009 basic financial statements and auditor's report thereon from its website and disseminated this statement by (i) delivering it to the Municipal Securities Rulemaking Board through its Electronic Municipal Market Access System for municipal securities (ii) posting it to the Cook County website and (iii) submitting it to the U.S. Federal Audit Clearinghouse.


Tariq G. Malhance
Chief Financial Officer


Constance M. Kravitz, CPA
Cook County Comptroller

IG-11-0027

EXHIBIT B

HC-11-0027

EXHIBIT C

COLLECTION WARRANT OR BILL

Chicago, January 27, 2010

TO COOK COUNTY, ILLINOIS, DR.

Address

Name of Debtor

County Clerk
Office of Issue)

(To be sent to County Clerk by

COPY - FOR COUNTY COMPTROLLER

20

Dated, Chicago,

Respectfully,

COUNTY CLERK'S ORDER TO TREASURER TO RECEIVE MONEY
(Prescribed by R.S.Ch. 120, Sec. 291.)

TO THE TREASURER OF COOK COUNTY:

Dear Sir: Please receive the within mentioned sum of money from debtor named, and mail and deliver to him the receipt thereof, after being countersigned by me, furnishing me a duplicate receipt, and credit the same to Cook County's General fund, for payment of the Collection Warrant as per within copy.

County Clerk No.

County Comptroller

Robert A. Kistly

County Treasurer

56 and 100 DOLLARS

the sum of TWENTY FIVE MILLION TWO HUNDRED SIXTY NINE THOUSAND, SIXTY NINE *****
in payment of the above stated account. COUNTERSIGNED:

Received, this 27th day of January 20 10

RECEIPT

Make checks, drafts or money orders payable to the County Treasurer of Cook County. Remit to the County Comptroller, Room 500, County Bldg, with this bill, and the bill will be returned to you duly receipted. Any correspondence relative to this bill should be with the Office of Issue, shown in upper right hand corner, and should mention the Office Number shown above.

Notice-

CERTIFIED CORRECT:

FOR	AMOUNT
Revenue collected for the month of December 2009	9,176,152.81
CREDIT: 1100.110110/1809.	
Obj. Acctf	
Cigarette Tax	422112
Gasoline Tax	422032
Diesel Fuel Tax	422034
Alcoholic Beverage Tax	422042
Retail Sale of Motor Vehicles	422052
Wheel Tax (Vehicle Stickers)	422062
Off Track Commission Fees	422072
County Amusement Tax **C-21**	422082
Ball Bond Forfeitures **C-5**	470010
Commissions on Public Telephones (D4)	4991619.501620
Health Insurance - 499-176	470050
Parking Lot & Garage Operations tax	431738
Sheriff Police Alarm-Permit	422086
Batch #	
Real estate management fees (D7)	470040
Doc Type JZ	
TOTAL	\$ 25,216,069.56

No. 55033

ISSUED FROM OFFICE OF
County Comptroller
Room 500, County Bldg.

IG-11-0027

EXHIBIT D

COLLECTION WARRANT OR BILL

Chicago, December 22, 2009

ISSUED FROM OFFICE OF
County Comptroller
Room 500, County Bldg

No. 54846

COOK COUNTY, ILLINOIS

Address: **COOK COUNTY, ILLINOIS, DR**

Name of Debtor

County Clerk
(To be sent to County Clerk by
Office of Issue)

PUBLIC SAFETY FUND

AMOUNT

R./D./Object Acct

From 713016310
Illinois State Income Tax-County Home Rule
1100.110110/1809.422010

From 713014320
Illinois/Reseller's Service Occupation
1100.110110/1809.422124

From 713014302
Illinois/State Income Tax
1100.110110/1809.422092

Illinois/State Income Tax-Local Use Tax
1100.110110/1809.422094

Illinois/State Income Tax-Photo Process
1100.110110/1809.422096

From 713014304
Illinois/Personal Property Tax-Exempt Tax
1100.110110/1809.421105

From 713014344
Illinois/Reimbursement Sheriff's
1100.110110/2101098.501020

TOTAL

\$ 33,397,287.28

33,397,287.28

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COPY FOR COUNTY COMPTROLLER

COUNTY CLERK'S ORDER TO TREASURER TO RECEIVE MONEY

(Prescribed by R.S.Ch. 120, Sec. 261.)

TO THE TREASURER OF COOK COUNTY:

Dear Sir: Please receive the within mentioned sum of money from debtor named, and mail and deliver to him the receipt thereof, after being countersigned by me, furnishing me a duplicate receipt, and credit the same to Cook County's General Fund, for payment of the Collection Warrant as per within copy.

Respectfully,

Dated, Chicago,

20

County Clerk
(To be sent to County Clerk by
Office of Issue)

County Clerk No.

FORM NO. 2269 REV. 5/93

County Comptroller

William H. Kirby

DEC 22 2009

the sum of the said stated account
THIRTY THREE MILLION THREE HUNDRED NINETY SEVEN THOUSAND,

100

DOLLARS

Received, this 22nd day of December, 20 09

RECEIPT

Notice-

Make checks, drafts or money orders payable to the County Treasurer of Cook County. Remit to the County Comptroller, Room 500, County Bldg. With this bill, and the bill will be returned to you only if received. Any correspondence relative to this bill should be with the Office of Issue, shown in upper right hand corner, and should mention the Office Number shown above.

County Treasurer

