

## Factors Affecting Fraud in Local Governments

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This study determines the factors related to fraud in state and local governments. Data for the study was collected by questionnaire from internal auditors employed by local governments. The study found that cities and counties experienced significant differences in the rate and types of fraud. The study also found that the strength of a local government's ethical environment is negatively related to its incidence of fraud. Thus, the study corroborates the findings of earlier studies such as the Treadway Commission, COSO, and the AICPA.

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### INTRODUCTION

This study determines the factors related to fraud in local governments. This is important because these governmental units are delivering a greater amount of services to their constituents than in the past and thus, face greater exposure to loss from fraud. Second, when fraud does occur in these governmental units it tends to be well publicized and the resultant political repercussions may be disproportional to the fiscal loss incurred.

### PREVIOUS STUDIES

Several studies were conducted to determine the extent of fraud. The National Commission on Fraudulent Financial Reporting (The Treadway Commission [1987]) completed its study of fraud in financial reporting in 1987. Many of the recommendations contained in the Treadway Report were later implemented by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in its 1992 report, *Internal Control – Integrated Framework* [1992]. Both of these reports based their recommendations on the finding that fraud occurred in organizations because of weak internal controls such as a poor control environment (attitude toward controls by management) or control procedures (lack of segregation of duties and independent checks).

KPMG Peat Marwick [1993 and 1994] conducted two studies of fraud in for-profit corporations. The questionnaire developed by KPMG Peat Marwick was modified for the public sector and used in this study. The Association of Certified Fraud Examiners (ACFE) [1995] sponsored a national study of fraud entitled, *Report to the Nation Occupational Fraud and*