

Fraud in Dixon Illinois: Who's to Blame?

INTRODUCTION

Rita Crundwell was the type of person that everyone trusted. As the comptroller and treasurer of the small town of Dixon, Illinois, she was well-versed in company finances. Whenever anyone had a question, they were advised to “ask Rita.” In 2011, the city commissioner praised Rita as someone who “looks after every tax dollar as if it were her own.” What the commissioner and the rest of Dixon did not realize until the next year was that Rita Crundwell took this view quite literally.

In addition to her trusted position with the city, Rita was also a champion quarter horse breeder. She had won 52 world thoroughbred championships and owned hundreds of horses. The competitions often took Rita away from her city job, but she would dock her pay for the extra time she took off. In 2011 during one of her trips, a city clerk took over Rita’s job while she was away and came across a bank account in the city’s name that made no sense to her. Money from the account was being used to purchase lavish items such as jewelry and boats. The suspicious account was reported to the mayor and then the FBI. After taking five months to build their case, the FBI arrested Rita Crundwell for municipal fraud on April 17, 2012.

The extent of the fraud was staggering. Rita Crundwell had first opened the fictional account in 1990, meaning that she had successfully stolen from the city for 22 years before being arrested. In those two decades she stole over \$53 million from a city of less than 16,000 people. Dixon, Illinois—known for being the boyhood home of President Ronald Reagan—has now gained the distinction of being the victim of the largest municipal fraud to date.

BACKGROUND

Rita Crundwell was born in 1953 to Ray and Caroline Humphrey. Although a family of modest means, Caroline loved showing quarter horses, a passion that Rita inherited as she grew up on her family’s farm. While one family member has expressed the belief that Rita was entitled as a child, nothing much about her situation growing up was indicative of the massive fraud she would one day orchestrate.

At age 17 Rita was hired as an intern at City Hall as part of a work-study program for high schoolers. In 1974, she married Jerry Crundwell and later divorced in 1986. Rita continued her position at City Hall and proved to be a quick learner. Everyone was so impressed with her skills that she assumed the position of city comptroller and treasurer in 1983. In 1978 Rita began showing horses at shows. This started her long-time passion with breeding and showing quarter horses. At the time of her arrest Rita Crundwell owned 400 quarter horses at different farms in Illinois and Wisconsin.

The year 1990 was a landmark year for Rita Crundwell. She began expanding her quarter horse operations and her home. In December of that year, she also opened a secret bank account under

the city's name called the Reserve Sewer Capital Development Account (RSCDA). Crundwell used false invoices made out to "treasurer" to deposit city money into this account, which she then used to finance the beginnings of a highly lavish lifestyle. At first she started out stealing thousands of dollars from the city a year. However, as time went on without her getting caught, she increased the amount of money she stole. Before her arrest, she was stealing millions each year. To hide her fraud, Rita collected all the city mail from a post office box and had a relative collect the mail for her when she was out of the office.

During the two decades of the fraud, Rita purchased hundreds of horses, expanded her home, bought a home in Florida, and purchased a number of vehicles and motor homes. Among her purchases was a luxury motor home worth \$2.1 million. Meanwhile, Rita established a name for herself in the quarter horse industry and won 52 competitions. Her trophies took up an entire room at her house. Eight years before her arrest, Rita was named the leading owner for the American Quarter Horse Association.

One of the city clerks that worked with Rita Crundwell, Kathe Swanson, was the one who discovered the fraud. Kathe was used to Rita telling her which bank accounts she should request from the bank. But in 2011 Kathe was taking over Rita's job while Rita was out on vacation. In a hurry, Kathe called the city's bank, Fifth Third Bank, and requested *all* of the accounts under the city's name. Among the accounts she received was the RSCDA account, an account of which Kathe had never heard. Looking at the transactions, she was surprised to see that money from the account was being spent on items that were clearly not city business, such as horses and jewelry.

Kathe took the information to the mayor of Dixon, Jim Burke. Mayor Burke reported the fraud to the FBI, and for the next five months both he and Kathe worked with the FBI to build a case against Rita as she continued to siphon city funds for her own personal use. In April Rita was arrested. She reportedly showed little emotion at her arrest.

During the next year, the extent of the fraud came out. Citizens were stunned when they realized the person they had trusted had stolen more than \$53 million in city funds over the years. What upset many individuals is that in order to steal the money, Rita had to make cuts in other areas. This included denying resources to city departments. For instance, the superintendent of Dixon's street department claims that streets could not be resurfaced or vehicles replaced. He was constantly told by Rita that the city did not have enough money.

In November Rita pleaded guilty to fraud in a federal court. Prosecutors asked for 20 years of jail time. Rita's attorney asked for a lighter sentence because of her cooperation with authorities. However, U.S. District Judge Philip Reinhard was disgusted by the magnitude of the crime and sentenced Crundwell to serve 19.5 years in prison. Before her sentence was announced, Rita Crundwell tearfully apologized to the city of Dixon for the fraud. The judge told Rita Crundwell that she cared more about her horses than the people she represented.

The city of Dixon hired the law firm Power, Rogers & Smith to investigate and file a lawsuit against those gatekeepers who were expected to detect fraud. Devon Bruce, a partner at the law firm, was able to obtain \$40 million for the city of Dixon. The accounting firm responsible for auditing Dixon's

financials –Clifton Gunderson – was charged \$35.15 million for what Devon Bruce called negligence for failing to detect the theft of city funds for over two decades. Fifth Third Bank paid \$3.85 million, and the accounting firm Janis Card Associates paid \$1 million.

WHO IS TO BLAME?

While obviously the biggest culprit in this fraud is Rita Crundwell herself, there is a number of stakeholders that could have asked relevant questions about suspicious activity who failed to do so. Attorney David Bruce places much of the blame on Dixon’s auditor, CliftonLarsonAllen (formerly known as Clifton Gunderson). However, the role of the bank and of the city itself has also been questioned. The following sections examine these stakeholders.

THE CITY OF DIXON

The problem with small towns is the lack of resources available. In Dixon’s case, while it was able to hire a few full-time employees such as Rita, it did not employ a full- or a part-time accountant. Even the position of mayor was part-time. Therefore, those who were knowledgeable about the finances beyond Rita Crundwell were few and far between.

Does this mean that city officials should escape any type of culpability? Many people believe that while leaders cannot have knowledge of every detail in their companies or governments, they do have a responsibility to exert oversight over employees and investigate anything that does not make sense to them. Mayor Jim Burke maintains that he grew suspicious of Crundwell’s rising wealth, not understanding how she could live such a lavish lifestyle on a city worker’s salary. He claims he even approached the company’s accounting firm Clifton Gunderson but was shut down when he starting asking questions about Rita.

Mayor Burke was not the only one who had questions. Other people in town were also wondering how Rita was able to live so expensively. There was a general belief that Rita, who had won so many championships, maintained the horses with her prize money. However, prize money would not be enough to pay for the high costs of maintaining so many championship horses. Others believed she had an inheritance. Nobody could say for sure, and Rita herself was not particularly close to anyone in the town. Mayor Burke describes her as friendly but as also having a “cold angle” about her as if she was maintaining her distance from other townspeople.

CLIFTON GUNDERSON

The accounting firm Clifton Gunderson paid the most in fines for not detecting the misconduct. In reviewing the case, it is important to note the significant conflicts of interest that existed between Clifton Gunderson and Rita Crundwell. During the 1980s Rita Crundwell played on the accounting firm’s softball team. She had friends at the firm and would sometimes get together for lunch or beers after work. However, these in themselves are not necessarily unethical. What could be construed as a major conflict of interest is the fact that Clifton Gunderson was not only the city’s accountant, but Rita’s personal accountant as well.

There are also signs that Clifton Gunderson tried to circumnavigate against new regulations. In 2005 it was mandated that auditors could not provide both non-attest services and auditing services. Clifton Gunderson therefore resigned from auditing assignments for Dixon so it could focus on other accounting services for the city. According to the lawsuit that Dixon filed against Clifton Gunderson, however, Clifton Gunderson continued to perform auditing services and simply had a CPA from the nearby town of Sterling, Samuel Card (owner of Janis Card Accounting), sign off on the financials to make it appear that a different firm was performing the audit. As already noted, Janis Card Accounting paid \$1 million to settle the allegations. Clifton Gunderson maintains that it compiled very basic financial information to help Samuel Card after 2005.

If the city's allegations are true, it shows that Clifton Gunderson did not place much emphasis on guarding against conflicts of interest. Attorney Devon Bruce believes that Clifton Gunderson was downright negligent in not recognizing signs that fraud was occurring. Among the alleged failures he cited against Clifton Gunderson includes the company's failure to detect clearly fraudulent invoices Rita Crundwell produced, failure to verify that city funds were being used for their intended purpose, and a failure to request appropriate documentation for income Rita Crundwell was receiving outside of her city job.

SUSPICIOUS INVOICES

Rita Crundwell perpetuated much of the fraud with fraudulent invoices she developed for phony projects. She attempted to make these invoices appear authentic. For instance, she would produce invoices allegedly from the Illinois Department of Transportation. However, these invoices did not adhere to the same standards as authentic invoices. They were missing key information, including the state logo and phone number of a contact person. On some invoices the word "section" was also spelled wrong. In examining emails, Attorney Devon Bruce also found an invoice dated as November 31, 2004 from the Illinois Department of Transportation—a date which does not exist.

In defense of Clifton Gunderson, auditing firms will examine a sample of documents in their audits. In a city with thousands of invoices and transactions each year, it might be possible that most of the invoices examined by Clifton Gunderson were authentic. The firm also claims that the types of audits it did perform did not require the additional tests necessary to try and detect fraud. However, critics point out that the firm would most likely have come across some of the fake invoices and should have noticed the discrepancies between them and the real ones. Once the auditor determined that these invoices looked different, they should have taken additional steps to verify where the money actually went.

NO VERIFICATION

In addition to detecting the fraud, Attorney Devon Bruce also pointed out that Clifton Gunderson failed to verify that money was going toward city projects. He claims that it would have been simple for the firm to check and make sure that large capital projects such as bridges were actually being built. Another method of verification is to request meeting minutes from City Hall. Any large-scale projects for the town would have had to be discussed during meetings, which would have been

recorded in the minutes. Fictitious projects that Rita made up would not have shown up in the minutes and should have acted as a red flag. Concerning the one invoice's nonexistent date, Bruce felt like the auditing firm should simply have called the Illinois Department of Transportation to check on the authenticity of the invoice. A simple attempt at verification, he believes, would have detected and stopped the fraud much sooner.

NO DOCUMENTATION

Finally, there were the discrepancies in Rita Crundwell's income. Rita Crundwell's tax returns had large sums of money that were not accounted for. For instance, a 2007 tax return showed gross receipts of \$700,000. All legitimate transactions—even prize money from competitions—would have been documented. There is no indication that Clifton Gunderson requested documentation. When asked about certain unexplainable activities or transactions, Rita would always have an answer ready. Attorney Devon Bruce claims that the accounting firm had a duty to impose “healthy skepticism,” meaning that it should not have trusted an individual at his or her word but worked to verify these finances. In this case, Clifton Gunderson appeared to be too trusting of Rita Crundwell's character.

While many people cast blame on Clifton Gunderson, it is also necessary to realize that an auditor's job does not involve going out looking for fraud. Additionally, many clients shop around for accounting firms with the best rates, creating an incentive for accounting firms to keep prices low. These reduced prices might compromise the quality of the work, with firms placing newer (and less expensive) auditors on accounts when they do not have enough experience in the area. This is leading some people to call for changes in the way audits are conducted. One proposed solution is using rotating accountants so that different people can analyze the information. It is believed that the more people who examine the financials, the better chance there will be for someone to detect suspicious behavior.

FIFTH THIRD BANK

Finally, Fifth Third Bank was also charged with a failure to exercise due diligence. For instance, when Rita Crundwell first opened the fictitious account in 1990, she was the only person to open the account. Many banks, including Fifth Third, require additional people or entities to be involved so as to prevent fraudulent activities. A resolution is also required to open up an account at the bank. This resolution never took place.

The bank also had access to statements showing that money was being funneled from the city to the fictitious account and was being spent on items that did not involve city business. A major red flag, however, is that Rita would make “fictitious” checks simply addressed to “treasurer” rather than under her name or the city's name and deposit them into the fictitious account. This is not usual behavior, and according to a former manager at Fifth Third, checks should have been addressed to “treasurer of the City of Dixon” or “City of Dixon.” Crundwell also wrote lots of checks for large sums of money, which, Attorney Devon Bruce maintains, acted as a clear red flag. It appears that the bank had proper procedures in place in theory but did not enforce them.

DIXON GOING FORWARD

The city of Dixon, Illinois has dramatically changed many of its practices to ensure nobody has the extent of power Rita had to commit fraud for so long. After she was fired, the city hired a new finance director who reorganized the city's finances and restructured the department. She implemented more internal controls so that no one person could complete an entire process by him- or herself—including her. Today the city has hired more clerks that specialize in specific areas such as payroll and billing. Mail is no longer picked up by one person. Instead, it is delivered straight to City Hall.

In terms of Rita Crundwell's assets, they are being auctioned off. The auction of Crundwell's prize-winning horses was major news to the industry, and many breeders came from all around the world. Her horse Good I Will Be, which had won several championships, sold for \$775,000. Her 767 trophies and 122 plaques were also auctioned, as well as her numerous possessions. The money will go toward the city.

Many people in the town are relieved that Rita Crundwell is in prison. Those who were acquainted with her, even those who had worked with her for years, felt like they never truly knew her. Interestingly, Crundwell still earns \$13,000 to \$14,000 a year in royalties from her horses. This money has frozen by the government. Eventually, officials hope to give the funds to the city. In the meantime, city business has gone on as usual, but with a new structure and greater wisdom to make certain that no one person has full and exclusive power of city finances.

QUESTIONS

1. What were some of the red flags that fraud was occurring?
2. Describe some of the ways that Rita Crundwell was able to get away with the fraud for so long.
3. What are some of the internal controls Dixon, Illinois has implemented to prevent fraud in the future?

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