



Review of the Office of the Treasurer, City of Harrisburg, PA

February 2016





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EXECUTIVE SUMMARY



I. EXECUTIVE SUMMARY

- The City of Harrisburg hired Alvarez & Marsal (“A&M”) following the arrest of the former City Treasurer to review the policies, procedures, and processes of the Office of the Treasurer as well as any unusual financial activity in the Treasurer’s office during 2014.
- A&M conducted a high-level review of the Treasurer’s office by interviewing certain employees in the Treasurer’s office and other City offices; examining selected bank statements, wire transfers documentation, and other documents and data; and performing process walk-throughs.
- A&M did not conduct an investigation of any individual or of the Treasurer’s office as a whole and does not provide any assurance related to any possible wrongdoing by any City employees. To provide such assurance would have required a much longer and more comprehensive project, especially since there are issues with the City’s financial records in terms of timeliness, accuracy, and completeness. Based on conversations with City employees, it appears that these issues have existed for a number of years.
- No instances of suspicious financial activity in the Treasurer’s office in 2014 came to A&M’s attention during the review. Therefore no additional procedures were performed. However, A&M did identify several significant internal control weaknesses. A&M also noted that the issues with the City’s financial records made it less likely that suspicious financial activity would be detected in the course of this high-level review.
- A&M did not conduct an audit and is not expressing an opinion on the effectiveness of the City’s internal controls or the reliability of the City’s financial statements.

I. EXECUTIVE SUMMARY

- **Key Finding: Segregation of Duties**

- Deputy Treasurer is both initiating and approving/releasing outgoing wire transfers.
 - The Deputy Treasurer uses a generic bank token [REDACTED] to initiate and/or approve outgoing wire transfers. This allows one person to initiate and approve wire transfers and prevents the formation of a reliable audit trail.
 - The [REDACTED] bank token has apparently been in use for years in the Office of the Treasurer.
- Deputy Treasurer initiating and approving wire transfers is also responsible for conducting the monthly bank account reconciliations.
- Too many processes/functions are concentrated with the Deputy Treasurer, which weakens checks and balances and negatively affects operations of the office (e.g., outgoing wire transfers cannot be processed while she is on vacation).
- The lack of segregation of controls related to the wire transfers results in an environment where the opportunity for fraudulent activity exists.

- **Key Finding: Account Reconciliations**

- Treasurer's office is not reconciling all of the City's bank accounts (bank to book) on a monthly basis.
- For those accounts that are being reconciled, the reconciliations are not being completed in a timely manner.
- Reconciling items identified during the reconciliation process are not being booked to the City's general ledger in a timely manner.

BACKGROUND AND SCOPE



II. BACKGROUND AND SCOPE

- **Background**

- Former Harrisburg City Treasurer, John Campbell, was arrested in August 2014 and charged with embezzling funds from a local non-profit organization.
- In the wake of that event, the City of Harrisburg sought an independent review of the internal controls in place in the Office of the Treasurer as well as any unusual financial activity that may have occurred in the Office of the Treasurer during 2014.

- **Scope**

- Conduct a limited high-level review of the policies, procedures, and processes in the Office of the Treasurer, and make internal control improvement recommendations based on this review.
- Analyze any unusual financial activity that may have occurred during 2014 if uncovered in the course of performing the review, and perform additional procedures as necessary.
- The review period for this assessment was generally defined as January 1, 2014 – December 31, 2014. However, A&M also reviewed transactions, documents, and processes outside this time period on an *ad hoc* basis as necessary.
- **A&M did not conduct an investigation of any specific individual(s) or transaction(s). Such an investigation would have been a much more comprehensive project, especially considering the current state of the City's financial records in terms of timeliness, accuracy, and completeness.**
- **A&M did not conduct an audit and is not expressing an opinion on the effectiveness of the City's internal controls or the reliability of the City's financial statements.**

WORK PERFORMED



III. WORK PERFORMED

- **Reviewed prior year Comprehensive Annual Financial Reports, audited financial statements, Management Letters, and other background information**
- **Interviewed and had discussions with the following City of Harrisburg employees and service providers:**
 - Charlie DeBrunner – City Controller
 - Bill Leinberger – Deputy Controller
 - Tyrell Spradley – City Treasurer
 - Celia Spicher – Deputy Treasurer
 - [REDACTED] – Assistant Deputy Treasurer (former)
 - [REDACTED] – Auditor, Office of the Treasurer
 - [REDACTED] – Accounting Clerk, Office of the Treasurer
 - [REDACTED] – Cashier, Office of the Treasurer
 - Bryan McCutcheon – Accounting Manager, Bureau of Financial Management
 - [REDACTED] – Database Administrator, Bureau of Information Technology
 - Neil Grover – City Solicitor
 - [REDACTED] – Audit Partner, Maher Duessel (City’s independent auditor)
 - [REDACTED] – Senior Manager, Maher Duessel (City’s independent auditor)
- **Reviewed select City of Harrisburg bank statements from 2014 and outgoing wire transfer activity on the statements**
 - Reviewed all bank statements maintained in Treasury records for Aug. - Dec. 2014 and reviewed select bank statements maintained in Treasury records for Jan. - Aug. 2014.
 - However, the City could not provide a current inventory of all City bank accounts, so it was unclear if the statements in the records were complete.
- **Reviewed supporting documentation for select wire transfer activity in 2014**
- **Reviewed bank account reconciliations for Central Depository Account and Reconciliation Account**
- **Conducted walk-throughs of various Treasury activities**

FINDINGS



IV. FINDINGS: SEGREGATION OF DUTIES

- **Segregation of duties and bank account reconciliation are two of the most fundamental internal financial control concepts in fraud prevention**

“The most important practice for preventing and detecting electronic payment fraud is a separation of duties. ... For wire transfers, duties for creating, approving, and releasing wires should be segregated. And to prevent attempts to conceal fraudulent electronic payment activity, no individual involved in the payment process should reconcile the bank statement or even have access to it.”

Prevention and Detection of Electronic Payment Tampering, 2015 Fraud Examiners Manual, Association of Certified Fraud Examiners, p. 1.435.

“Segregation of duties. Assigning different people the responsibilities of authorizing transactions, recording transactions, and maintaining custody of assets. Segregation of duties is intended to reduce the opportunities to allow any person to be in a position to both perpetrate and conceal errors or fraud in the normal course of the person’s duties.”

Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement, Statement on Auditing Standards AU-C § 315.A157, American Institute of CPAs.

“Some fraudsters attempt to conceal their schemes by altering the bank statement, miscoding transactions in the accounting records, or sending fraudulent payments to a shell company with a name similar to that of an existing vendor. Others merely rely on the company’s failure to monitor or reconcile its accounts.”

Prevention and Detection of Electronic Payment Tampering, 2015 Fraud Examiners Manual, Association of Certified Fraud Examiners, p. 1.435.

IV. FINDINGS: SEGREGATION OF DUTIES

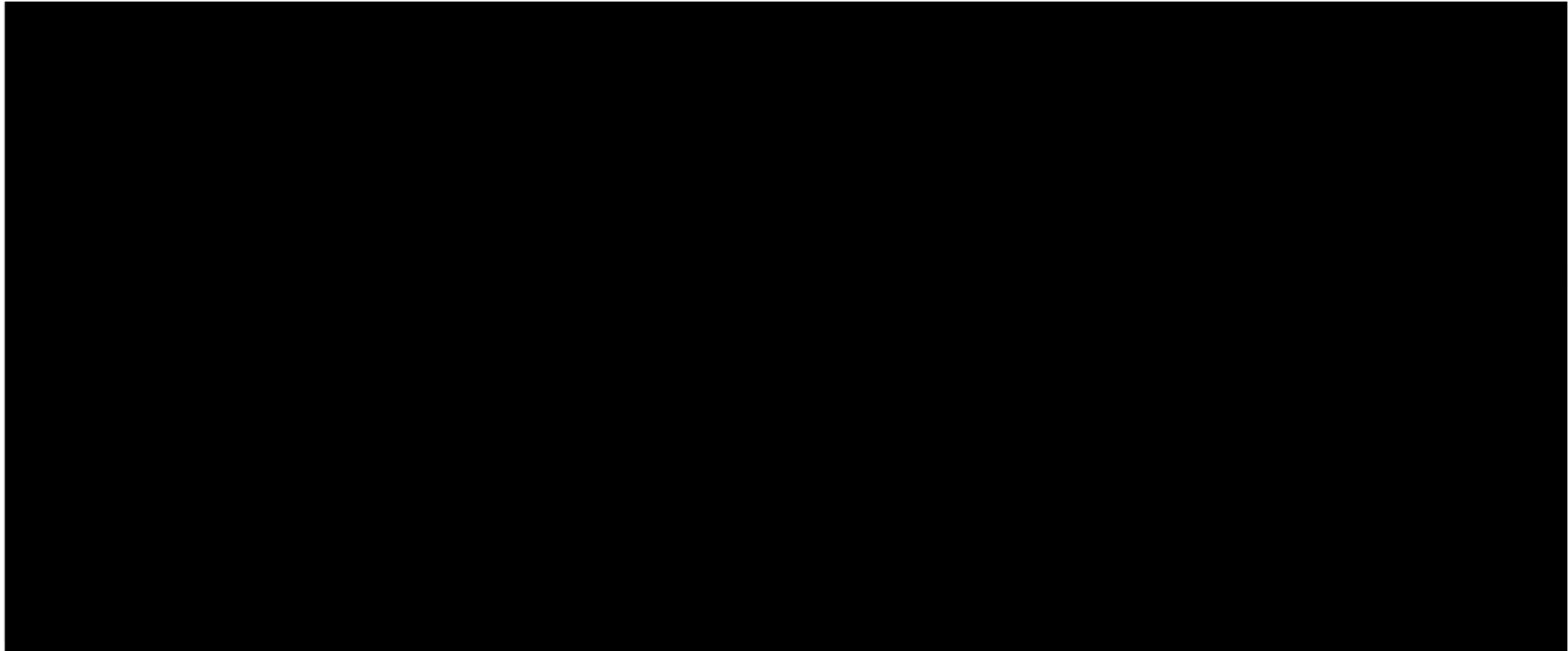
- **The Deputy Treasurer is both initiating and approving/releasing outgoing wire transfers**
 - Finance and the Controller's Office have to sign off on wire transfer request memos, but are not involved at all with the actual process of wiring money from the City's bank accounts. That entire process occurs in the Treasurer's Office.
 - The Deputy Treasurer maintains two bank logins/tokens for the wire transfers. She logs in with a generic login/token to set up wire transfers, then logs in with her personal login/token to approve and release those same wire transfers. (See example on next page.)
 - Because the same person is initiating and approving the wire transfers, there is a complete lack of segregation of duties related to outgoing wire transfers.

- **The Treasurer's Office has a generic login and banking token (called "Wires") that is not assigned to a specific person**
 - According to the Deputy Treasurer, this generic login and token, which appears as [REDACTED] in the system, has existed and been used for years in the Office of the Treasurer.
 - The use of a generic login and token prevents an accurate audit trail from being created and maintained in the City's books and records.

- **The Treasurer's Office currently has responsibility for making wire transfer payments and for the bank account reconciliations**
 - The lack of segregation of duties related to the initiation and approval of wire transfers is exacerbated by the fact that the same person - the Deputy Treasurer - is also responsible for reconciling the bank accounts.
 - During the review period, at times the Assistant Deputy Treasurer position was vacant and at times the Deputy Treasurer delegated the reconciliations to the Assistant Deputy Treasurer. However, the Deputy Treasurer ultimately took control of the reconciliation process for quality purposes.

IV. FINDINGS: SEGREGATION OF DUTIES

- **Below is an example of an outgoing wire transfer initiated and approved by the Deputy Treasurer using the generic [REDACTED] login**
 - The example below is a wire payment to [REDACTED] for one month of employee benefits from the [REDACTED].
 - Initiated at 9:59 a.m. using the [REDACTED] bank login/token – presumably by the Deputy Treasurer
 - Approved at 10:36 a.m. by the Deputy Treasurer [REDACTED]
- **A&M noted numerous examples of similar transaction histories during the review of wire transfer documentation**



IV. FINDINGS: ACCOUNT RECONCILIATIONS

- **The Treasurer's Office does not maintain an updated master inventory of all City bank accounts**
 - Neither the Deputy Treasurer nor the Assistant Deputy Treasurer maintains an updated master inventory of all of the City's 60+ bank accounts, including account details, purpose of each account, and authorities associated with each account (e.g., wire transfer, check writing, direct debit)
 - The Deputy Treasurer claimed to be familiar with all of the City's bank accounts, but only maintains this information in her head.
 - Dormant and/or unidentified bank accounts can be used to facilitate or hide unauthorized activities.
- **Not all City bank accounts are being reconciled**
 - The Treasurer's Office currently receives all bank statements, but is not reconciling all accounts on a monthly basis.
- **Accounts that are being reconciled are not up to date**
 - For example, as of Sept. 2015:
 - Central Depository account – working on reconciliation of April 2015 bank statement
 - Concentration account – working on reconciliation of January 2015 bank statement
- **Reconciling items from prior reconciliations have not historically been recorded on the general ledger**
 - Adjusting items from past reconciliations are not always recorded in the general ledger by Finance, so the same reconciling items keep appearing month after month on reconciliations.
 - Deputy Treasurer reported that some reconciling items have appeared for years.
 - Deputy Treasurer stated that she places a low priority on account reconciliations due, in part, to her belief that adjustments identified by the reconciliation process are not made in the accounting system.

IV. FINDINGS: ACCOUNT RECONCILIATIONS

Examples of unresolved issues with the account reconciliation process include:

- **Per the Deputy Treasurer and Deputy Controller, as of August 17, 2015, there was a ~\$2 million difference between the General Fund book balance and the General Fund bank balance**
 - \$7,552,539 General Fund G/L cash account balance
 - \$9,572,799 General Fund bank account balance
 - Various open reconciling items (perhaps going back as far as 2009) built up over time. This was exacerbated by the fact that audits were not performed for several years beginning in FY2009, only to be completed years later.
 - A properly-functioning account reconciliation process would have identified and rectified these discrepancies when they first appeared.
 - A&M did not perform procedures to determine if any portion of this difference was caused by defalcation. However, A&M did note that the bank balance was higher than the book balance.
- **As of September 2015, there was ~\$300,000 of Petty Cash (account 109000) reported on the G/L that is not actually petty cash**
 - Per the Accounting Manager, the ~\$300,000 recorded in the Petty Cash account is the result of two adjusting journal entries related to the double funding of a payment (two checks for electricity payment to Direct Energy were voided in 2012, then two new checks were written and the Central Disbursements bank account was funded a second time).
 - The extra money in the Central Disbursements bank account – due to the double funding - was never moved back to the originating accounts and has been held ever since in the Central Disbursements checking account.
 - The Central Disbursements account should be a zero-balance (a.k.a. imprest) account, and should not have a running \$300,000 balance.
 - The Accounting Manager stated that he is working on moving the money back to the original accounts; however, this issue is three years old.
 - It is unclear why money related to an electricity payment was accounted for as Petty Cash in the City's books and records.
 - A properly-functioning account reconciliation process would have identified and rectified this issue soon after the double-funding occurred.
 - A&M did not perform procedures to determine if any portion of this difference was caused by defalcation.

IV. FINDINGS: OTHER FINDINGS

- **There appears to be a culture at the City where errors are accepted and expected.**
 - During interviews, there was a general acceptance and/or resignation among City employees regarding errors in the City's financial records. This was blamed on a variety of factors, including personnel shortages, the City's past fiscal problems and budget cuts, mistakes by previous City employees and Administrations, and lack of competence or work ethic displayed by other current City employees.
 - For example, multiple City employees have been aware of the issues described in this report (i.e., late/incomplete reconciliations, General Fund book-to-balance inconsistency, and "petty cash") for months or years, and yet the issues have not been corrected.
 - In a culture where errors are accepted as commonplace, it is much easier for someone to commit a fraud and avoid detection. Unusual or undocumented transactions will be less likely to raise red flags.
- **The Assistant Deputy Treasurer ("ADT") position has had a great deal of turnover in recent years**
 - The ADT is a key position in terms of segregation of duties within the Treasurer's Office, as the ADT is the only other management-level role in the office. With an ineffective or vacant ADT, more and more financial responsibilities and processes are consolidated at the Deputy Treasurer level.
 - The ADT in place during this review was terminated at the end of his probationary period, creating another vacancy in the ADT role.
 - Hiring a strong, well-qualified ADT will be key to improving the internal controls in the Treasurer's Office.
- **No written policies or procedures in place in the Treasurer's Office**
 - None of the employees in the Treasurer's Office were aware of any current documents outlining the policies, procedures, and processes of the office.
 - Written policies and procedures are one of the most basic aspects of a system of internal controls.

[REDACTED]

POTENTIAL INTERNAL CONTROL ENHANCEMENTS



V. POTENTIAL INTERNAL CONTROL ENHANCEMENTS

- **Segregate the approval/release of the wire transfers from their initiation in the system**
 - Require at least two sets of eyes on each wire before it is released from the City's bank account
 - Until a new Assistant Deputy Treasurer is hired and trained, responsibility for approving wire transfers can be assigned to another City employee or official (e.g., City Treasurer)
 - Train additional employees in the Treasurer's Office on the wire transfer processes, which would eliminate the need for Deputy Treasurer to "do it all"
- **Eliminate the generic [REDACTED] bank token**
 - All actions taken with regard to wire transfers should be associated with a specific person
 - Increases accountability and creates a stronger audit trail
 - Discourages sharing of bank tokens among employees
- **Move responsibility for account reconciliations out of Treasury and into another City office, such as the Controller's Office**
 - The same office responsible for wire transfers should not be reconciling the bank accounts.
 - Bank statements should be received directly by the office that will be responsible for the reconciliations.
- **In the future, the initiation of outgoing wire transfers, the approval of outgoing wire transfers, and the reconciliation of City bank accounts should be performed by different people**
 - For example:
 - Deputy Treasurer and Assistant Deputy Treasurer could initiate and approve wire transfers
 - Controller's Office could reconcile bank accounts to general ledger
 - Finance could record any adjusting journal entries on the City's books and records
- **Bring all account reconciliations up-to-date and record all prior adjusting entries**
 - Eliminate differences between bank balances and general ledger balances
 - Initiate a consistent process to ensure that all bank accounts are reconciled monthly
 - Reconcile the ~\$2 million difference between the General Fund's bank balance and book balance and make any necessary adjusting entries in the City's general ledger

V. POTENTIAL INTERNAL CONTROL ENHANCEMENTS

- **Tone at the Top - address cultural issues related to acceptance and expectation of errors**
 - Quickly address any errors found and update the City's financial records accordingly
 - Change expectations: the default expectation should be that the City's financial records are correct and any error is an exception
- **Create a master inventory of all City bank accounts, including authorities associated with each account (e.g., check-writing, direct debit, ATM cards, wire transfer)**
 - Close any unnecessary and/or dormant bank accounts
- **Address all known discrepancies in the City's books and records in a timely manner**
 - If known discrepancies (e.g., \$300k in "petty cash") are allowed to linger, then incorrect and/or inconsistent accounting entries, fund balances, journal entries, etc. may become expected and accepted. In such an environment, future discrepancies may appear less extraordinary and therefore draw less attention.
- **Hire a strong Assistant Deputy Treasurer and ensure that person is empowered to act independently**
 - Allows for greater segregation of duties
 - Reduces dependence on any one individual for smooth functioning of the office
- **Provide additional staffing in Treasurer's Office and other City offices as needed to allow for proper segregation of duties**
- **Create a set of written policies and procedures for all major processes in the Treasurer's Office**
 - Documents practices, promotes consistency, and reduces dependence on any one individual
 - Reference tool for all employees and training tool for new employees
- **Improve physical security of Treasurer's Office**

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