



Office of the Washington State Auditor
Pat McCarthy

Fraud Investigation Report

Pierce County Housing Authority

For the investigation period January 1, 2015 through July 17, 2019

Published December 16, 2019

Report No. 1025349





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December 16, 2019

Board of Commissioners
Pierce County Housing Authority
Tacoma, Washington

Report on Fraud Investigation

Attached is the official report on a misappropriation at the Pierce County Housing Authority. In July 2019, our regularly scheduled financial statement audit detected a potential loss of public funds.

This report contains the results of our investigation of the former Finance Director's unallowable activities at the Housing Authority from March 18, 2016 through July 17, 2019. The purpose of our investigation was to determine if a misappropriation had occurred.

Our investigation was performed under the authority of state law (RCW 43.09.260) and included procedures we considered necessary under the circumstances.

If you are a member of the media and have questions about this report, please contact Director of Communications Kathleen Cooper at (360) 902-0470. Otherwise, please contact Fraud Investigation Manager Sarah Walker at (509) 454-3621.

Pat McCarthy
State Auditor
Olympia, WA

cc: Elinor Ottey, Acting Executive Director

FRAUD INVESTIGATION REPORT

Investigation Summary

During a regularly scheduled audit, we identified unusual bank transfers from the Pierce County Housing Authority's (Housing Authority) bank account. We investigated and determined the former Finance Director misappropriated \$6,948,277 of public funds between March 18, 2016, and July 17, 2019.

The Housing Authority has filed a report with the Federal Bureau of Investigation and the U.S. Department of Housing and Urban Development Office of Inspector General, which are investigating this case. We will refer this report to both agencies.

Background and Investigation Results

The Pierce County Housing Authority provides housing opportunities for eligible individuals in Pierce County. The Housing Authority owns and manages nine apartment complexes and provides housing assistance through the Low Income Public Housing program. The Housing Authority's operating expenses were roughly \$33.9 million in 2018, which includes \$23.2 million of housing assistance payments. The Housing Authority's former Finance Director started working for the Housing Authority in 1998, was responsible for overseeing Housing Authority finances, and supervised between five and eight people.

While performing a regularly scheduled audit of the Housing Authority's 2018 activity, we noticed three wire transfers totaling \$635,000 from the Housing Authority's bank account to a title company and a bank that was not on the Housing Authority's list of banks it used. We inquired with the Finance Director about two of the transfers, and she said they were investment purchases that she later canceled.

When contacted, the bank confirmed the Housing Authority did not have an account there. Additionally, the title company is based in Oklahoma, and an online search of County Assessor information in Oklahoma showed the Finance Director purchased property for the same dollar amount and in the same month as the wire transfers to the title company. We also reviewed the Housing Authority's 2019 bank records and identified several wire transfers listing the Finance Director, by name, as the beneficiary.

The Housing Authority placed the Finance Director on administrative leave on August 2, 2019, after our audit uncovered these irregularities, and fired her effective August 8, 2019.

One week later, we obtained a court order authorizing the issuance of a subpoena for the former Finance Director's personal bank account records. We found 10 additional wire transfers totaling \$3.05 million from the Housing Authority's bank account to the Finance Director's personal account between January 2019 and July 2019.

In addition to the wire transfers, we found 78 Automated Clearing House (ACH)¹ transactions totaling \$3,237,712 from the Housing Authority’s bank account to the Finance Director’s personal account between July 2016 and February 2019. The Housing Authority pays several vendors through ACH instead of issuing a check. As we traced these transactions, we determined the Finance Director had created invoices to appear they were from legitimate Housing Authority vendors, and then changed the bank payment information to redirect the payments to her own personal account.

Finally, to determine if any additional misappropriations occurred, we examined systems to which the former Finance Director had access, including credit cards. We found she used the Housing Authority’s credit card for personal purchases totaling \$25,565 between March 2016 and April 2016.

In total, the former Finance Director misappropriated \$6,948,277 as shown in the table below:

Type	2016	2017	2018	2019	Total
Automated Clearing House (ACH) payments	\$387,604	\$1,272,871	\$1,316,477	\$260,760	\$3,237,712
Wire transfers to Finance Director’s bank account	\$0	\$0	\$0	\$3,050,000	\$3,050,000
Wire transfers to title company and out-of-state bank	\$0	\$0	\$635,000	\$0	\$635,000
Credit card payments	\$25,565	\$0	\$0	\$0	\$25,565
Total	\$413,169	\$1,272,871	\$1,951,477	\$3,310,760	\$6,948,277

The former Finance Director acknowledged responsibility for the misappropriation in a recorded deposition on October 10, 2019, a written declaration she subsequently filed with a court, and a November 25, 2019, interview with state auditors. However, she said her supervisor, the Housing

¹ An Automated Clearinghouse (ACH) payment is an electronic money transfer made through the Automated Clearinghouse – a network of banks that are batching transactions between them. In contrast, a wire transfer is an individual transaction, electronically moving money from one bank account to another. Banks tend to charge a fee for wire transfers and as such, many entities reserve wire transfers for large, infrequent electronic payments, while using ACH for smaller, frequent payments such as payroll direct deposits.

Authority Executive Director, pressured her into the scheme and directed her to give him a portion of the misappropriated funds in cash.

We interviewed the Executive Director on October 22, 2019, examined his personal bank records, and performed additional tests in response to the former Finance Director's statements. We did not find any evidence that indicates the Executive Director was involved in, or benefitted from, the misappropriation. We did find evidence that contradicts some of the statements the former Finance Director made in her deposition. Further, we found a correlation between withdrawals from her account and 46 subsequent parcel shipments to a man in Oklahoma who is now her husband. These shipments occurred on the same day as the withdrawals or within a week thereafter, and started with her first large cash withdrawal. In our interview, the former Finance Director said she was mailing personal items, and that the timing must have been a coincidence.

Control Weaknesses

The Housing Authority did not have adequate internal controls to safeguard public resources. We found the following weaknesses allowed the misappropriation to occur:

- The Finance Director had full access to all systems and had wire transfer capability with little to no oversight or monitoring of her activities.
- At the time of the audit, the Housing Authority had 13 bank/fiduciary accounts. The number of accounts made it more difficult to monitor transactions and reconcile accounts.
- The Finance Director did not consistently provide adequate financial information to the Board of Commissioners so it could monitor operations.
- Staff members who reconciled bank statements focused solely on the cleared dollar amounts, not on the vendors or the nature of the transactions.
- ACH payments are processed in batches, not individually, and show up as a batched dollar amount on the Housing Authority's bank statements. Further, journal entries to record the batches in the accounting system were confusing and not always entered in a timely manner.
- Reviewers did not have the expertise to fully understand and review ACH payments, nor did they have firsthand knowledge of vendor or employee bank account numbers to recognize when payments were diverted to the former Finance Director's bank account.
- Housing Authority finance staff told us the Housing Authority's software systems were not optimal for operations, so they used a second software system for certain functions. These duplicate systems made it easier for the Finance Director to conceal transactions.
- The Accounts Payable Clerk reconciled all credit card activity, including the Finance Director's credit card. However, the Finance Director supervised the Clerk, and directed the Clerk to forward any questions about credit card activity to her.

Recommendations

We recommend the Housing Authority re-evaluate and strengthen its internal control systems. Specifically, the Housing Authority should:

- Increase monitoring of all financial transactions processed by the Finance Director and bank statement activity
- Evaluate each employee's job responsibilities along with their accounting system and bank account permissions, then restrict access and segregate duties when needed, and implement robust monitoring of these functions
- Limit wire transfer capabilities and consider requiring dual authorizations
- Train employees on how to conduct a meaningful review of financial information, such as journal entries, bank statements, and ACH payments
- Re-evaluate the software systems it uses
- Close unnecessary bank accounts

The misappropriation caused a \$6.9 million loss, while the Housing Authority had just \$500,000 in employee theft insurance coverage. We recommend the Housing Authority evaluate its insurance and performance bond coverages to better protect itself in the future.

We also recommend the Housing Authority seek recovery of the misappropriated \$6,948,277 and related investigation costs of \$83,638 from the former Finance Director and/or its insurance bonding company, as appropriate. Any compromise or settlement of this claim by the Housing Authority must be approved in writing by the Attorney General and State Auditor, as directed by state law (RCW 43.09.260). Assistant Attorney General Matthew Kernutt is the contact person for the Attorney General's Office and can be reached at (360) 586-0740 or matk1@atg.wa.gov. The contact for the Office of the Washington State Auditor is Brandi Pritchard, Assistant Director of Local Audit and Special Investigations, who can be reached at (360) 489-4591 or Brandi.Pritchard@sao.wa.gov.

Housing Authority's Response

Thank you for providing the Pierce County Housing Authority the opportunity to review and respond to the State Auditor's Office (SAO) investigation Report No. 1025349

Pierce County Housing Authority (PCHA) is committed to ensuring that all necessary controls are implemented to protect both PCHA's and the public's assets. PCHA has reviewed this report and agrees with all the recommendations presented by the State Auditor's Office.

Upon notification of the fraud by the Office of the Washington State Auditor, PCHA has supported and cooperated with the investigative process and law enforcement while acting with civil attorneys to secure assets and prevent further loss.

The Housing Authority's goal was to ensure that programs and services remained available to members of the Pierce County community throughout this process; that PCHA obligations were met, and; to implement corrective actions as soon as possible as the investigative process unfolded and actions informed.

Specifically, PCHA took the following actions:

Immediately placed the finance director on administrative leave while the investigation was implemented.

Terminated the former finance director's employment as soon as it became clear that she had perpetrated the fraud.

Eliminated the former finance director's access to all PCHA accounts and systems

Hired civil attorneys who filed a temporary restraining order preventing the former finance director from disposing of assets in both Pierce County and Oklahoma. A preliminary injunction was obtained in both jurisdictions.

Restricted access to all banking and other financial systems. After assessing access needs by job function, limited access was restored to select staff.

Placed the Executive Director on administrative leave for investigation of allegations regarding fraud.

Contracted with a nationally recognized firm with deep knowledge and understanding of public housing authorities to conduct a complete assessment of current financial processes and procedures and to implement strong internal control systems in the agency's financial systems, including:

- System of review for all financial transactions pre and post processing by both finance and executive staff*
- Dual review of bank statements by executive staff*
- Restriction of wire transfer capabilities and limits on amounts allowed in a single transfer*
- Implementation of dual approval procedures for all wire transfers*
- Ongoing training for finance staff, executive staff and board members on review of journal entries, bank statements, and ACH payments*
- Collaboration with software provider to expand the current system's capabilities or transition to more appropriate financial software*
- Identification of bank accounts needed to avoid co-mingling restricted funds and eliminating all unnecessary accounts.*

The Housing Authority will seek recovery of the misappropriated \$6,948,277 and related investigation costs of \$83,638 from the former Finance Director and/or its insurance bonding company, as appropriate.

The Housing Authority will implement all necessary controls to protect both PCHA's and the public's assets and integrate ongoing oversight and monitoring to assure those controls are maintained over time. The Housing Authority staff, management and Board of Commissioners are dedicated to our mission of safe, clean and affordable housing. We will make every effort to re-build the trust and confidence of our housing clients, landlords, renters and our community to fulfill that mission.

We thank the SAO for their calm professionalism and deft touch displayed while working with the Housing Authority during the investigation. The Authority was able to maintain our administration of public housing funds and affordable rental properties, keeping fellow citizens in their homes, making payments to our landlords and maintaining our facilities.

Auditor's Remarks

We thank Housing Authority officials and personnel for their assistance and cooperation during the investigation.

ABOUT THE STATE AUDITOR'S OFFICE

The State Auditor's Office is established in the state's Constitution and is part of the executive branch of state government. The State Auditor is elected by the citizens of Washington and serves four-year terms.

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