



Office of the Washington State Auditor
Pat McCarthy

Fraud Investigation Report

Terrace Heights Sewer District

For the investigation period May 1, 2021 through November 3, 2022

Published August 21, 2023

Report No. 1033110



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**Office of the Washington State Auditor
Pat McCarthy**

August 21, 2023

Board of Commissioners
Terrace Heights Sewer District
Yakima, Washington

Report on Fraud Investigation

Attached is the official report on a misappropriation at the Terrace Heights Sewer District. On December 2, 2022, the District notified the Office of the Washington State Auditor of a potential loss of public funds. This notification was submitted to us under the provisions of state law (RCW 43.09.185).

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 (564) 999-0800. Otherwise, please contact Special Investigations Program Manager Stephanie Sullivan at (360) 688-0858.

Pat McCarthy, State Auditor
Olympia, WA

cc: Annette Garcia, Office Manager

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FRAUD INVESTIGATION REPORT

Background and Investigation Results

On December 2, 2022, the District notified our Office regarding a potential loss of public funds, as required by state law (RCW 43.09.185). In November 2022, a utility customer received an overdue balance notice despite having already paid the bill. When the customer provided a copy of the receipt as proof of the payment, the District discovered that records of the receipt had been deleted, and the payment was not posted to the customer's account. The District then found several additional receipts had been deleted without authorization through a login associated with its Receptionist. The Receptionist voluntarily left employment on November 29, 2022.

We investigated and determined a misappropriation totaling \$6,378.45 occurred at the District between July 13, 2021, and September 6, 2022.

Our investigation focused on cash receipting. We found the Receptionist deleted cash receipts totaling \$2,262 without justification or approval, and collected \$214 in cash payments without initially receipting them. She later receipted and deposited all these cash payments, with delays ranging from five to 46 days – indicating she borrowed the funds and later paid them back. The District was able to assign responsibility for this misuse of funds to the Receptionist in part because she emailed the list of accounts and cash payments to her personal email account.

We identified an additional \$3,581 of deleted receipts posted through the Receptionist's username that were reposted at a later date, and one payment totaling \$321 that was never reposted. Since another person had administrative access to the employee's username and password, the District could not assign responsibility for this loss.

In December 2022, a Yakima County Sheriff's Office Deputy interviewed the Receptionist, who denied deleting or retaining cash payments. She said it was possible that she walked away from the computer after logging in, and another employee used the computer to process and void the payments, which made it appear that she was responsible. We contacted the Receptionist for an interview in May, June and July 2023 by phone and email, but she did not respond to our requests. The Yakima County Sheriff's Office recommended charges to the County Prosecuting Attorney's Office, based on the District's investigation.

Control Weaknesses

The District's internal controls were inadequate for safeguarding public resources. We found the following weaknesses allowed the misappropriation to occur, and prevented the District from assigning responsibility:

- Staff can delete receipts within the system without a second person's approval, and the District does not review the deleted receipts report to verify that these transactions are appropriate.

- One person has administrator access to the utility billing system, which gives them full access to all usernames and passwords.

Recommendations

We recommend the District improve its internal controls over cash receipting to ensure it adequately safeguards public funds from loss or misappropriation. Specifically, the District should independently review all deleted cash receipts to verify they were deleted for a valid purpose, and maintain separate and secure login passwords.

We will refer this case to the Yakima County Prosecuting Attorney's Office for any further action it determines is necessary.

We also recommend the District seek recovery of the related investigation costs of \$10,500 from the former Receptionist and/or its insurance bonding company, as appropriate. Any compromise or settlement of this claim by the District must be approved in writing by the Attorney General and State Auditor as directed by state law (RCW 43.09.260). Assistant Attorney General Matt Kernutt is the contact person for the Attorney General's Office and can be reached at (360) 586-0740 or Matthew.Kernutt@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.

District's Response

Terrace Heights Sewer District must operate within practical fiscal restraints necessitated by its status as a small utility/ Special purpose district. A consequence is that it has previously been necessary to consolidate several responsibilities in a single staff position, which might otherwise be delegated amongst several employees in a larger district. This necessity for consolidation created an opportunity for prior Receptionist to effectuate the discovered fraud.

Before the former Receptionist vacated her position, but prior to discovery of the fraudulent activity the district hired an additional office staff member. This allowed the coverage needed to review processes and be able to have an extra set of eyes to uncover the misappropriations of funds.

The misappropriation of funds was initially uncovered when a customer brought a missing cash payment to the attention of the additional staff member who reported it to management. The customer was able to produce a receipt showing a cash payment that had not been posted to their account as well as describing the Receptionist to whom they had given the cash payment to. This led to management review and extensive work to uncover the extent of the fraud. The district immediately turned over all our findings to the Yakima County Sheriff and the Washington State Auditor for further investigation.

While the hiring of additional staff was instrumental in uncovering the initial fraud, we have also changed the internal controls, access, and internal review processes we use to determine the validity of adjusted or deleted payments. Each staff member has always had their own log in and password but the ability to view, change, or update passwords has been transferred from management to our software administrator. New processes require staff to log out of their terminal if they step away from their work area. Management is now actively reviewing all adjusted and/or deleted payments regularly as well as working with our software provider to find a solution to their lack of a two-person approval for the deletion of receipts.

In conclusion, while the district cannot entirely protect itself against a bad actor, the safeguards we have put into place have each significantly reduced the likelihood of future of fraudulent behavior. The district plans to pursue all avenues available to us to recoup the misappropriated funds as well as the costs incurred for the investigation of fraud from the former receptionist.

Auditor's Remarks

We thank District officials and personnel for their assistance and cooperation during the investigation. We will follow up on the District's internal controls during the next audit.

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

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