

Liberty Township forensic review
Executive Summary

As in many small organizations, too much power is entrusted to one individual and there is not enough supervision. Internal controls either do not exist or are not observed.

Despite all the irregularities that occurred over the past 12 years, every set of Board Meeting minutes mentioned approval of both the Treasurer’s Report and the paying of all bills. This was true even when the Treasurer’s Report beginning balances for one month did not match the ending balances for the previous month, and also when the exact same Treasurer’s Report was submitted two months in a row. Paying of bills apparently was authorized without supporting documentation.

Records were not properly maintained at the township. Payments were often made late, incurring penalties, late fees and interest. Payroll sheets were missing; invoices were missing. The documents that *were* available were in complete disarray, piled on shelves or into boxes in no particular order. Without invoices, it is impossible to determine whether the secretary was committing fraud or was simply sloppy and inept.

Substantiated irregularities include:

1. Over-paid wages, with taxes and benefits, 2013 – 2016	\$24,174.40
2. Over-paid hours, with taxes and benefits, 2008 - 2012	22,298.18
3. Over-paid mileage, 2007 – 2013	<u>2,890.52</u>
Total	<u>\$49,363.10</u>

Other allegations included:

1. \$16,000 in cash was missing and simply written off by the auditors. This is not true. I traced every entry the auditors made and agree with each. The \$16,000 in question dated back to an error in 2004 together with an unusual habit of reporting some things on an accrual basis and others on a cash basis...but no money was missing.
2. Insurance was handled improperly. This is true. The secretary made an error in calculating one employee’s cost to insure himself and his spouse. Instead of \$673.52 per pay, she calculated and withheld only \$269.46 per pay. According to her records, the township paid \$34,231.68, while the withholding was only \$13,080.77, a difference of \$21,150.91.

Details to support the above and outline the work done are on the following pages.

Karen Frey, CPA, PhD

To: Supervisors of Liberty Township, Adams County, Pennsylvania:
From: Karen Frey, CPA, PhD
Subject: Liberty Township report
Date: August 31, 2017

You asked me to look at the books and records of Liberty Township to investigate an allegation that the township secretary/treasurer was acquiring more of the township's funds than she was entitled to. This was an investigation and not an audit. Standard audit procedures were not performed and I express no opinion on the presentation of the financial statements. This information is presented in summary fashion; details to support the figures presented are available upon request.

Documentation

In conducting this investigation, I spoke to individuals at the township and reviewed the following documents:

1. Liberty Township Employees Handbook
2. Profit and Loss reports from 2002 – 2015, and 2016 through September
3. Budget reports from 2002 – 2015
4. General ledger reports from 2002 – 2015, and 2016 through September. 2002 – 2004 contained no details and were not pursued further.
5. Trial balances from 2005 – 2015
6. Bank statements from 2005 – 2015; three were missing
7. Employee time sheets from 2008 - 2015
8. Board Meeting minutes from December, 2002 – December 2015
9. Paid invoices from 2005 – 2015
10. Credit card statements from 2005 – 2015, and 2016 through September
11. Payroll records from 2008 – 2015, and 2016 through September
12. Smith, Elliott, Kearns audit reports 2014 – 2016
13. Treasurer Reports as available, 2002 - 2015

Procedures followed and observations made included:

Comparing Profit and Loss reports to the budget for each year.

The first year secretary wages exceeded the budget was 2008, when actual wages exceeded the budget amount by about 6% (\$1991.82 excess / \$32600 budget). The complete summary is:

<u>Year</u>	<u>Excess</u>	<u>Budget</u>	<u>Over budget</u>
2008	1991.82 / 32600 =		6.1%
2009	3669.48 / 33904 =		10.8%
2010	4317.02 / 35260 =		12.2%
2011	4408.68 / 36670 =		12.0%
2012	6159.68 / 38137 =		16.2%
2013	5857.84 / 39662 =		14.8%
2014	5713.57 / 41497.94 =		13.8%
2015	6569.69 / 41248.48 =		15.9%

The year 2016 is not presented here because I do not have the full year's information.

Wages, 2013- September 2016

Smith, Elliott, Kearns (SEK) analyzed the payroll excesses for the later years, and my results agree with theirs for the entire 2013 - September 2016 time period. For those years, excess pay and related contributions totaled \$24,174.40 (see the SEK report for details).

Wages, 2008 - 2012

Prior to that, however, was a four and one half year period, from July 2008 through December 2012, in which the secretary was paid for 90 hours every two weeks, instead of 80 hours. These extra hours were not paid at overtime rates. They were not authorized in the minutes when they began, nor were they mentioned in the minutes when they ended. The employee handbook states:

“The workday for Secretary/Treasurer Liberty Township shall be from 8:00am to 3:00pm. This assumes that lunch is eaten on-the-job. The Secretary/Treasurer also works during the regularly scheduled Supervisors’ meetings and the Planning Commission meetings.”

That's a seven-hour day plus meetings, for about a 40-hour week. The handbook further states:

“Administration employees who work overtime will instead of overtime pay receive compensatory time-off. **After the forty hour point has been reached,** compensatory time will be calculated at actual time for hours worked.”

(Emphasis is mine)

Thus there should be no payment in excess of 40 hours per week or 80 hours per two week pay period.

Time sheets records for the period 2008-2012 were not complete. Files in 2008 contained 24 pay periods of time sheets; there were 17 pay periods in 2009, 21 pay periods in 2010, 16 pay periods in 2011 and 8 pay periods in 2012. Of those 86 pay periods, 25 had time sheets for the road crew and police, but no time sheet at all for the secretary. Not one of the existing 61 secretary's forms was signed to authorize the hours claimed. Usually only the police sheets contained authorization signatures.

Through QuickBooks, I determined how many hours and at what rates the secretary was paid. With no evidence to support payment of extra hours, I conclude that excess wages, taxes and benefits were paid as follows:

<u>Year</u>	<u>Excess Hours</u>	<u>Hourly Rate</u>	<u>Excess Pay</u>
2008	140.50	\$15.61	\$2,193.20
2009	238.50	\$16.23	\$3,870.85
2010	266.00	\$16.87	\$4,487.42
2011	262.00	\$17.54	\$4,595.48
2012	272.00	\$18.24	<u>\$4,961.28</u>
Sub-Total			\$20,108.23
Social security/medicare @ 7.65% for 2008-2010			807.19
Social security/medicare @ 5.65% for 2011-2012			539.96
Pension contribution @ 1% for 2008-2009			60.64
Pension contribution @ 2.5% for 2010			112.19
Pension contribution @ 7% for 2011-2012			<u>668.97</u>
Total			<u>\$22,298.18</u>

Mileage

Through the same time period, secretary mileage reimbursement increased by a great deal. Only one mileage log was found, for February, 2006, claiming 49 miles. Total mileage claimed in 2005 and 2006 was 1197 and 659, respectively; 2007 exceeded the budget significantly for the first time, at 35% above budget:

<u>Year</u>	<u>Miles claimed</u>	<u>Average Rate</u>	<u>Mileage paid</u>	<u>\$Budget</u>	<u>\$Excess</u>	<u>Over budget</u>
2007	1377	.49	\$ 674.73	500	174.73	34.9%
2008	2408.5	.4894	\$1178.72	700	478.72	68.4%
2009	2730	.55	\$1501.50	900	601.50	66.8%
2010	2775	.5332	\$1479.70	1100	379.70	34.5%
2011	2767	.5418	\$1499.25	1100	399.25	36.3%
2012	3097	.55	\$1703.35	1100	603.35	54.9%
2013	2446.2	.5532	\$1353.27	1100	253.27	23.0%
2014	1646	.5652	\$ 930.40	1100	(169.60)	(15.4%)
2015	620	.5539	\$ 343.43	1100	(756.57)	(68.8%)

Note that miles claimed dropped significantly in 2014 and again in 2015. In 2016 through the end of September, only 322.4 miles were claimed; that's an annualized rate of about 443.2 miles, and far fewer than the thousands of miles claimed in earlier years.

The supervisors approved the budgeted mileage figures submitted in each year's budget. If we accept that the budgeted dollar amount is reasonable for each year, then the amounts overpaid from 2007 through 2013 total \$2,890.52. However, the supervisors also approved each actual payment.

To illustrate that mileage is not an inconsequential amount that can be safely ignored, consider this example: If we believe that a more reasonable budget would reflect many fewer miles, then the amounts overpaid would be substantial. Keeping in mind vacation time, even 1,000 miles per year would represent driving more than 20 reimbursable miles per work week. Re-calculating the over-payment based on 1,000 miles per year and the average yearly rates implied by the table above, the over-payment would be approximately \$6,048. (In some years the reimbursement rate fluctuated, so the average was not a constant 49 cents per mile or 55 cents per mile as in other years).

General ledger and invoices

I reviewed general ledger reports from 2005 through mid-September and compared them to paid invoices that support the expenses recorded. The records at the township office were quite jumbled and invoices required sorting by both year and vendor.

Accounting for expenditures was haphazard and inconsistent. For example:

Loan payments for various vehicles were charged to accounts such as Bank Charges OR Debt Principal and Debt Interest OR Miscellaneous Expense OR Yukon Loan OR GMC Truck OR Vehicle Loan Repayment.

In 2005, JP Harris was paid \$128.26 and the Equipment Rental account was charged. But JP Harris is a tax collection agency, and the check had the names of two employees on it.

In 2014, checks written to the IRS, likely involving penalties and interest, were charged to Return of Prior Year Revenue.

In 2012, one check written to "Treasury Department" was charged to Computer Supplies and Software. Most checks to that payee were for federal withholding and social security deposits. This was likely penalties and interest, but no documentation establishes that.

In general, invoices were missing for an alarming number of bills paid. This is particularly troublesome in accounts like office supplies and computer supplies, and also the Capital One credit card payments. There is no sure way to determine whether the missing invoices represented Liberty Township expenses or represented funds diverted for personal use by the secretary.

Many invoices showed past due amounts, some of 60 days and more; some were second requests for payment; some had late fees added. Other invoices appeared to have been paid two or three times. All of these are indications of sloppiness or ineptness, but not necessarily of fraud.

Bank Statements and Treasurer Reports

I reviewed the general fund bank statements from 2005 – 2015, reconciling them with amounts in the general ledger cash account and also the Treasurer reports included in the Board Meeting minutes. Through 2009, differences were either small or easily reconciled. A few bank statements were missing, but that did not prove to be a problem.

Beginning in 2010, the Treasurer Reports showed different amounts of dollars in the General Fund than the general ledger showed, sometimes more and sometimes less. Many Treasurer Reports were missing. By April 2015, the Treasurer Reports and general ledger amounts were once again equal.

The differences noted may be because the format of the Treasurer Reports changed during this time period. Through October 31, 2010 they were as one would expect and easily reconciled:

- Beginning balance (equal to the ending balance of the previous month)
- + Receipts
- Disbursements
- = Ending balance

No Treasurer Reports were found for November 2010 to May 2011. By June 2011 the format had changed to more of a bank reconciliation than a Treasurer Report:

- Bank statement balance at month end
- Outstanding checks
- = Available balance per books

This new format had no tie between last month's figures and this month's and seemed an odd way to present the information. As mentioned above, these reports showed dollar figures much different from the general ledger for some time, but the issue was resolved by 2015. I found no evidence of fraud, just an odd way of reporting.

One thing I did notice from reviewing the bank statements is that, even though payroll tax deposits were recorded in the general ledger on approximately the correct dates, the actual cash transfers to the IRS or Pennsylvania from the bank account often occurred several months later. This resulted in late fees and penalties that the township should not have incurred, but it is not fraud.

Credit card transactions

I looked at the Capital One credit card account in detail. No invoices supported the transactions on the card. Township records show payments to Capital One beginning in 2005, but the credit card statements do not go back that far. There is only one credit card statement from March, 2010 and then all of them from February 2012 to November 2016.

The March 2010 statement shows “Total fees this year” of \$54 and “Total interest this Year” of \$31.86, a substantial amount for just the third month of the year, and evidence that at least some of the payments for 2005 – 2010 included penalties and interest. The credit card was not being paid in a timely manner, and between 2012 and 2016 the statements showed \$1,172.86 of penalties and interest on purchases of \$15,844.76. This amounts to an additional 7.4% on top of the purchases.

As noted earlier, it was impossible to determine which amounts might be appropriate charges to the township and which were not. I particularly question charges to Old Navy, Pizza Hut, Sunoco, Flower Boutique, Back the Alley, WalMart, House of Bender, and ChickCoop. I also question the sheer number of purchases from MicroSoft, QuickBooks and Intuit, as well as Staples. Whether Liberty Township was paying for software and office supplies for other entities cannot be determined without evidence. Perhaps a case could be made that each of them is a legitimate township expense; without invoices we cannot tell.

There is no excuse for failing to pay bills on time year after year and incurring penalties and interest that your employer must pay, but that constitutes doing a poor job, not fraud.

Holiday pay

At least one part-time employee has been receiving holiday pay to which he was not entitled. Per the employee handbook, an employee must average 24 hours per week in the three months preceding a holiday in order to be paid for that holiday. That provision was not always met.

Employee health insurance

The secretary erred in calculating insurance deductions on the PSATS Trustees Insurance Fund. Once again I attribute that to poor work rather than fraud, especially since she herself is not the only who was under-charged. Semi-annual premiums were quoted by the insurer on a form, with hand-written “per check” amounts that she had calculated:

For an employee only, Plan B-1 had a semi-annual premium of \$4,220.28. She calculated $\$4,220.28 * 2 = \$8,440.56$ per year. Subtract the \$3,500 that the township had been paying and you get \$4,940.56. Divide that by 26 paychecks per year to equal \$190.02. This is the plan she chose, and \$190 or \$190.02 was deducted from her paycheck from 2011 to the beginning of 2013.

For an Employee w/spouse she did not double the semi-annual payment of \$10,505.82:

Plan B – 1: $(\$10,505.82 - \$3,500)/26 = \$269.46$ (rounded up), and this is what she withheld from the employee. It should have been $(\$10,505.82 * 2 - \$3,500)/26 = \$673.52$, so this employee was paying \$404.06 less per pay than he should have.

This continued for about one and one-half years before it was noticed. At some point the employee’s withholding was increased by \$40.33 per pay to try to catch up, but of course that was woefully short. In all, the township paid \$34,231.68 on this specific policy while the withholding was only \$13,080.77, a difference of \$21,150.91.

Recommendations

Establish internal controls to separate duties of the secretary between two or more people.

A website at nonprofitaccountingbasics.org can help with this.

Have someone other than the secretary/treasurer reconcile the bank statements.

Require invoices or other documentation for every bill submitted for payment.

Approve payments twice per month to avoid late fees and interest.

Have someone approve hours for payroll and miles for reimbursement.

Have appropriate forms for these items. Consider out-sourcing payroll.

Require that records be maintained in an orderly and easily-retrieved system, kept by year and then by vendor or file type (e.g. payroll).