



The Commonwealth of Massachusetts  
Office of the Inspector General

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January 4, 2011

Mayor Elaine Pluta  
City of Holyoke  
City Hall  
536 Dwight Street  
Holyoke, MA 01040

Dear Mayor Pluta:

As you are aware, the Office of the Inspector General (OIG) has been investigating the suspected misappropriation of funds by the former Deputy Collector of the Holyoke (City) Collector's office. The funds at issue involve the City Collector's delinquent excise and parking ticket accounts. This letter addresses the findings and recommendations resulting from our investigation.

*Background*

According to the City's current budget appropriations, the Office of the City Collector (the Collector's office) is a four person office with a budget of nearly \$222,000. The City Collector (the Collector) is "responsible for the collecting of the city's real estate, personal property, and motor vehicle excise tax...[the] office also handles the issuance of municipal lien certificates and parking ticket payments...."<sup>1</sup> In FY10, the Collector's office processed \$49,242,329.48 in City revenue receipts. The Collector is appointed by the City Council and the current Collector has held the position since 1993. The Collector also contracts with an outside private agency, hereinafter referred to as the "Deputy City Collector,"<sup>2</sup> to manage and collect delinquent parking ticket and excise tax account balances.

In 2009, the City notified the OIG that the City's external auditor, Melanson Heath & Co., working in conjunction with the Collector had identified

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<sup>1</sup> City of Holyoke website

<sup>2</sup> Massachusetts General Laws, Chapter 60, Section 2B states in relevant part:

"For the purposes of collecting municipal taxes, the collector is authorized to enter into agreements with one or more private persons, companies, associations or corporations doing business in the commonwealth to provide collection services with respect to unpaid municipal taxes, other than taxes for real property, for which a demand has already been made...."

approximately \$82,000 in missing funds from the Collector's office for 2008. The OIG has established that at least \$64,158.92 is unaccounted for in the period of July – December 2008. This discovery is troubling, coming after critical reviews of the City Treasurer's office by the OIG, and years of critical management letters from the City's outside auditors, and the December 2007 *Financial Management Review* conducted by the Massachusetts Department of Revenue's Division of Local Services/Technical Assistance Section (DOR). The DOR report highlighted significant negative findings with the Collector's office in addition to confirming the findings of the OIG's May 2007 report concerning the City Treasurer's office. The DOR report specifically stated that their "review goes beyond the treasurer's office to include *all* [emphasis added] the financial management functions of city government...."

### *Status of Investigations*

Unfortunately, prosecution is not an option in this case due to significant deficiencies in recordkeeping and internal controls combined with an inadequate computer-based accounting system for the delinquent excise and parking ticket accounts at the Collector's office. These deficiencies prevent a definitive determination of the total amount of missing funds. Moreover, these deficiencies make it impossible to state with certainty whether someone misappropriated the missing funds or those funds remain unaccounted for due to bookkeeping and other errors. The difficulty of identifying the cause is compounded by weak controls and breaches of procedure that mandate daily bank deposits. During our investigation, we learned that large amounts of cash remained in the Collector's office for possibly weeks at a time. This resulted in one or more employees (or other individuals) having access to this cash. As such, it is virtually impossible, absent an admission, to definitively identify any one person as being responsible for the possible misappropriation of funds. The lack of proper account reconciliation, and an inability to track information about precisely who made payments on behalf of delinquent excise tax or parking ticket payers when payments were made at the Collector's office, makes it impossible to rule out the possibility that a bookkeeping error is to blame for part or all of the missing funds.

The OIG investigation revealed that the former Deputy Collector, who according to the Collector's office earned a City salary of approximately \$37,000 in FY2008, gambled almost \$42,000<sup>3</sup> at two New England casinos during the same period in 2008 (July – December) initially identified by Melanson Heath & Co. (and later confirmed by the OIG) as the period when funds appeared to be missing from the Collector's office. According to casino records obtained by the

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<sup>3</sup> This amount includes the total amount gambled by the former Deputy Collector including any winnings that the former Deputy Collector may have also gambled. During the six month period in question, the former Deputy Collector lost \$4,700 more than (s)he won.

OIG, the former Deputy Collector visited the two casinos 14 times during this period in 2008. The casinos have virtually no gambling activity on record prior to 2008 for the former Deputy Collector (for example, the former Deputy Collector is on record at one casino as having only gambled \$46 on slot machines in 2005). As of the conclusion of our investigation, there are no records of gambling activity at these casinos by the former Deputy Collector subsequent to the former Deputy Collector's termination from City employment in December 2008.

The OIG investigation disclosed that the former Deputy Collector had sole responsibility to handle and deposit delinquent excise and parking ticket payments into City bank accounts. The OIG review of bank deposit information around the 2008 period under investigation shows that the records maintained by the Collector's office for these accounts are markedly different in quality and completeness from same type of records maintained by the former Deputy Collector in prior periods. Prior to the beginning of the former Deputy Collector's 2008 gambling activity, bank deposits for these accounts could be generally reconciled to Collector's office receipts. Beginning around the time the former Deputy Collector's gambling activity began, the recordkeeping for these accounts became shoddy and so incomplete that reconciliations could not subsequently be performed.

For example, during the six month period in question, the deposits prepared or "batched" by the former Deputy Collector had an adding machine tape attached to the front of the batch of delinquent excise receipts that purported to be the total of the payments to be deposited in the bank. Both the auditor for Melanson Heath & Co., assigned to conduct the outside audit for the City of Holyoke, and later an investigator for the OIG independently attempted to "tie" payments in each batch to the deposits and those to the adding machine tapes. This reconciliation could not be completed because the receipts in each batch did not correspond to either the adding machine tapes or the bank deposit records. When asked by the OIG, the Melanson Heath & Co. auditor opined that this might represent a deliberate attempt by an individual to hide any missing money from these accounts. However, it should be noted that during the former Deputy Collector's frequent absences from the office, another employee of the Collector's office batched the deposits and those deposits could be "tied" to daily collections.

The OIG attempted to interview the former Deputy Collector in an effort to ask questions about the missing funds, the failure to follow established procedures relating to the batching and depositing of funds collected, and the source of the funds for the gambling activities. This attempt included contacting the former Deputy Collector's attorney to seek permission for an interview. The attorney for the former Deputy Collector declined to make his client available for an interview.

The OIG notes the following internal control deficiencies that allowed the suspected misappropriation to occur: 1) Significant gaps in the record keeping system of the Collector's office make it impossible to prove beyond a reasonable doubt that a theft of as much as \$82,000 actually occurred; 2) The failure of the Collector to implement procedures that require all funds collected to be deposited in the bank no later than the next business day (This failure made it impossible to determine the actual amount of cash that should have been deposited by the former Deputy Collector at any given time)<sup>4</sup>; 3) The failure of the Collector to require that all funds collected be deposited no later than the next business day allowed the former Deputy Collector to keep unknown amounts of cash unsecured in the Collector's office which in turn allowed other employees of the Collector's office access to that cash; and lastly, 4) The lack of any witnesses who could state that (s)he had observed the former Deputy Collector or anyone else misappropriating the money.

The OIG believes the following findings and recommendations may assist the City to strengthen bookkeeping and accounting practices, and to develop the administrative capacity to prevent apparent misappropriation, mishandling, or miscounting of funds.

### *Findings*

1) *The Collector's office lacked basic internal controls including segregation of duties.*

Lacking adequate segregation of duties created an opportunity for fraud that led directly to the possible misappropriation of funds that the OIG believes occurred in this case. Segregation of duties is an internal control mechanism that ensures that the same parties responsible for program functions do not also provide oversight functions. Maintaining segregation of duties creates meaningful checks and balances within an organization. Unfortunately, the Collector's office did not maintain adequate segregation of duties among its staff persons. The former Deputy Collector had the responsibility for counting, preparing bank deposits, and reconciling those bank deposits against bank statements for the delinquent excise tax and parking ticket accounts. As a result, this process had no checks and balances. Even if the Collector reviewed deposited amounts or asked for collection balances, these would not provide a

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<sup>4</sup> The Collector informed the OIG that it was the practice of the Collector's office to make daily deposits but, because of the former Deputy Collector's frequent absences, a "day or two" might go by before deposits were made. The Collector further stated that on "ordinary" days, deposits were made every day and that, prior to the Deputy Collector's termination, he was unaware that deposits in the deputy excise account often included deposits from monies collected over multiple days.

check against the potential theft of funds. Having one employee responsible for every aspect of a particular revenue stream creates ample opportunities for not only errors but for theft and fraud.

Melanson Heath & Co. also identified other internal control lapses including a multi-year failure to reconcile balances, a failure to report information to the City Auditor, and what Melanson Heath & Co. described as “virtually no oversight” by the Collector over work performed by the former Deputy Collector and possibly other employees. For example, the Collector informed the OIG that he had been unaware that the former Deputy Collector failed to make daily deposits as required. A simple review of relevant bank statements would have revealed this major problem to the Collector.

In more recent discussions with OIG staff, the Collector noted that his office has instituted some of Melanson Heath & Co.’s recommendations and has attempted to segregate duties whenever possible given the small number of employees in the office. For example, the Collector stated that the delinquent accounts managed previously by the former Deputy Collector are now divided between two staff members. One staff member prepares the deposits while another staff member makes the deposits. The Collector is responsible for reconciling the deposit information to bank statements. However, in the event that a staff member is unavailable (on vacation, out sick, etc.), one employee may perform multiple functions again thereby negating the segregation of duties<sup>5</sup>. Also, reconciling deposits to bank statements alone does not allow for the possibility that misappropriation or errors can occur before the deposit is prepared.

For example, Melanson Heath & Co. informed the OIG (and the OIG confirmed) that adding-machine tapes supposedly created by the former Deputy Collector to prepare and “batch” deposits did not match either the contents of the batch they purported to total or the actual amounts deposited. Batches often included checks received by the Collector’s office many days apart including one batch containing two checks received ten days apart. As a result, neither Melanson Heath & Co. nor the OIG (after an extended and exhaustive effort) could reconcile daily collections to the amounts deposited based on those daily collections. Similarly, City computer-based accounting records also did not agree with daily deposit amounts. Reconciliations must be performed throughout the transaction process from the point that a payment is made to the transfer of funds from the Collector’s bank account to the Treasurer’s office. Only through this process can errors or theft be identified.

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<sup>5</sup> The Collector should ascertain if staff is available in other City offices (like the Treasurer or Finance Department) who might be cross trained and available on a temporary basis to assist the Collector’s office with these functions in those circumstances.

Because the Collector's office did not have a meaningful reconciliation process in place, no one was able to detect whether funds were missing or stolen. In fact, until the Deputy City Collector retained by the City to assist with the collection of parking and overdue excise taxes (among other functions) inquired about why he had not received revenue reports for a significant period of time, no one questioned the lack of proper controls. The Deputy City Collector needed these reports to perform his duties and to ensure that he had been invoicing the City appropriately for his fees. The former Deputy Collector's failure or reluctance to produce these reports led the Collector, himself, to assume responsibility for their production. As a result, the Collector identified approximately \$82,000 in missing or unaccounted for funds. The Collector immediately reported that fact to the former Mayor who quickly brought it to the attention of Melanson Heath & Co. and the OIG.

2) *The Collector should follow "best practices" for the procurement of contract services.*

The Collector maintains multiple bank accounts and, as stated earlier, uses the services of a private firm under contract with the City for the collection of delinquent parking tickets and excise taxes. Although the procurement of banking and deputy collector services are exempt from the provisions of M.G.L. c.30B, the Uniform Procurement Act, the OIG strongly recommends that as a "best practice" the City should periodically seek competition for these services.

In the case of banking services, the Collector should work with the City Treasurer to identify the banking needs of the Collector's office and seek to competitively procure these services. This process could assist the Collector in identifying what additional services such as reconciliation and reporting that banks could provide at the lowest cost. As mentioned previously, the Collector has stated that his budget will not support enough resources to provide adequate oversight and control for its collections. Using bank services to augment these functions could remedy some of the Collector's office's weakness. For example, on several occasions the former Deputy Collector had made two or fewer deposits a week – something the bank could flag for the Collector if the bank is notified to expect daily deposits. The OIG offers guidance for the procurement of banking services on its website <http://www.mass.gov/ig/publ/bankadv.pdf>.

Regarding Deputy City Collector services, the Collector should consider a competitive procurement as well. Even if the Collector believes that the incumbent has performed satisfactorily, testing the market through competition may identify lower overall service costs through increased efficiency or an overall better value. For example, even though the fees paid to a Deputy City Collector are limited by M.G.L. c.60, a different vendor might offer additional services as

part of the fee they would be paid. Periodic competition also ensures that a vendor does not get too “cozy” in a relationship with a public entity. Long-standing relationships could lead to relaxed oversight by the public entity and the willingness of both parties to overlook contractual lapses. The City’s current vendor has held the deputy collector contract since 1997.

Long-term vendor relationships could also hinder improvements in accountability and transparency. For example, Melanson Heath & Co. recommended in at least three audit reports, changes in controls that could improve vendor oversight. The Collector has not adopted these recommendations. Melanson Heath & Co. wrote: “As reported... we noted that Deputy Collector fees earned by the City’s Deputy Tax Collector [vendor] are paid directly from the Deputy Tax Collector’s checking account and thereby not subject to the warrant approval process. While this is allowable under Massachusetts General Laws, items not subject to the warrant process have a diminished level of review and approval and thereby weaken internal controls. We recommend the City... ensure Deputy Collector fees are paid from a warrant. This would provide greater control over the disbursement... and enhance internal controls....” This is a sound business practice that allows officials outside the Collector’s office to know the cost of Deputy City Collector services. This transparency acts as a check against unreasonable costs. The costs of competitively procured services are generally more widely known.

Also, the OIG review identified potential improvements that could be made in the reporting of financial information for the collections overseen by the vendor. For example, the vendor uses what the Collector referred to as a vendor developed “proprietary” system for maintaining collection information. The Collector’s staff has the ability to access this system but cannot generate reporting from this system. As a result, the Collector’s office is completely reliant upon the vendor to provide reporting. The OIG has already suggested that the Collector seek to improve his office’s ability to obtain information. In response, the Collector stated that he would “bring it up” with the vendor. The competitive procurement of these collection services would enable the Collector’s office to specify in a solicitation the required type of reporting, controls, and data capture.

According to the Collector, the Deputy City Collector’s computerized accounting system does not differentiate between cash, check, or credit card payments when payments are made through the Collector’s office for delinquent excise tax payments. However, when the payments are made to the deputy collector at his place of business, he does record that information on his office system. So, if a payment is made to the Collector’s office, rather than the vendor, the accounting system does not identify who made the payment (for example, did Jane Doe use her credit card or her check to pay the bill for John Q. Public?) This disconnect occurs because the Deputy City Collector and the

Collector fail to capture the same information for similar transactions. The OIG identified this as a flaw in the accounts receivable process because it makes the reconciliation of collected funds to amounts deposited and the tracking of payments difficult.

Not being able to track payments by type of payment would enable dishonest employees to manipulate accounts to conceal theft (a typical fraud scheme often has a dishonest employee being able to misappropriate funds by substituting non-cash payments for cash payments). During the investigation, Melanson Heath & Co. and OIG could not reconcile deposits to collections, in part, because of the lack of this information. The Collector and the Deputy City Collector need to develop a protocol under which taxpayer information is consistently obtained for the same transaction types regardless of whether the Deputy City Collector or the Collector is responsible for recording the transaction. Use of this protocol with other recommendations might have prevented the funds from being lost to suspected misappropriation or other error and may have flagged these issues earlier.

### 3) *Other issues*

The reports issued previously by DOR and Melanson Heath & Co. identified issues that may remain unaddressed by the City. For example, since 2001, Melanson Heath & Co. has made a number of recommendations concerning the Collector's office that remained unaddressed. Melanson Heath & Co. wrote in 2009: "Strong internal controls are integral to any accounting system. We recommend that City improve the controls in the Collector's office by increasing the frequency of turnovers to the Treasurer's office, providing copies of turnover forms directly to the City Auditor's office, implementing regular reconciliations of turnovers to cash in bank, and regular reconciliations of detailed receivable reports to the Office of the Collector's control and general ledger."

Again, Melanson Heath & Co. made some of these recommendations for at least six consecutive fiscal years and the City failed to take action or provide Melanson Heath & Co. with a reasonable explanation for why the City had not or would not implement the recommendations. Melanson Heath & Co. wrote in the same 2009 report: "As you can see the issues noted for both the Treasurer's office and the Collector's office have been repeated for many years in some instances escalating to the point of creating material weaknesses. A material weakness occurs when a significant deficiency, or a combination of significant deficiencies result in a more than remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal controls."



In 2007, DOR issued a *Financial Management Review* that noted that the “office of the collector...function[s] in virtual isolation...there is no leadership mechanism that connects departments....This structure fails to create strong reporting relationships...which will over time increasingly impact financial operations.” DOR also echoed many of Melanson Heath & Co.’s prior findings including the infrequent turnover of cash receipts to the Treasurer in violation of M.G.L. c.60, §2, the need for reconciliation of balances, and the need for greater controls over the deputy collector account.

DOR also encouraged “the mayor, city council and others, when formulating overall strategies for improving the city’s financial management, to consider the observations, analyses and recommendations contained in this [DOR] report.”

#### *Recommendations*

City employees who handle or manage cash and other revenue collections should be required to account for their time and attendance and should be instructed that they must maintain high ethical standards and appropriate conduct. Employees should be required to sign a statement acknowledging their understanding of this responsibility. According to the Collector, the City now uses written time and attendance records that must be signed by relevant managers and the use of compensatory time has been eliminated. (Prior to this change, City departments used “comp time” despite there being no official City policy regarding its use, monitoring, or control.)

The City should also consider bonding and/or insuring all, rather than just some, Collector’s office employees and adhering to any insurance requirements that may be applicable to this bonding such as routine auditing, drug testing, etc. City staff has informed the OIG that the former Deputy Collector had been bonded by the City. As such, the City should consider whether it has sufficient evidence to file a claim for the potential losses suffered by the City if they have not already done so.

The City should also require annual anti-fraud and ethics training for all employees that handle cash and other collections. A meaningful anti-fraud training program would help employees identify strong indicators of high fraud risk.

The City should also institute a more thorough review/background check process for the hiring of new employees for responsible positions such as persons who collect and handle City funds. According to the Collector and published newspaper reports, the former Deputy Collector had been terminated

by a previous public employer for “dereliction of duty.” Hiring an employee with a checkered employment history or criminal background to handle money should only be done, if at all, when internal controls have been determined by an outside auditor to be strong, the office conducts a reasonable review of the candidate, has an understanding of the risks involved, and only with full confidence that prior bad acts will not reoccur.

The Collector should consider conducting competitive procurements for banking and deputy collector services. These procurements should include any services and/or procedural elements that will augment and improve service delivery and accountability. For Example, this office strongly urges the Collector to heed a prior Melanson Heath & Co. recommendation that delinquent excise tax and parking collections be tracked similarly as other collections in the City’s MUNIS accounting package. This would avoid the use of dual systems and a system controlled exclusively by a vendor.

The Collector should implement reasonable internal and management controls including those recommended previously by DOR, Melanson Heath & Co. and the OIG in their reports relating to the City of Holyoke. If current staffing levels prove inadequate for the use of reasonable management controls, then the Collector should take greater advantage of computer based tracking systems and use other resources including the City Auditor, the City’s external auditor, and the banks that handle City accounts. The Collector and other City officials must weigh the cost of increased controls against the risk of future financial losses and/or errors.

If not already done, the City should ensure that all reasonable recommendations made by oversight agencies be implemented as soon as possible. Ultimately, the City Council must recognize its obligation to ensure that the Collector’s office functions free from vulnerability to fraud, waste, and abuse.

### *Conclusion*

In recent discussions with the OIG, the Collector stated that his office has instituted a number changes such as, dividing the account reconciliation work formerly done by one employee amongst three employees and providing reports to the City Auditor. The Collector also believes that current controls are “a lot better” now than what had been in place before. However, there appears to be more remaining to do including the implementation of additional recommendations that have been made by Melanson Heath & Co., DOR, and the OIG.

The OIG remains concerned that the Collector failed to respond to Melanson Heath & Co.’s prior audit findings and recommendations year after

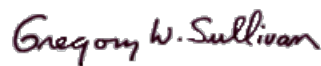
year, apparently provided limited oversight of office functions, and failed to react to “red flags” of potential problems in his office. In fact, if not for the Deputy City Collector repeatedly requesting reconciliation documents that were months overdue from the Collector’s office, then the financial discrepancy and the possible misappropriation of funds might not have been identified. Despite numerous oversight agency warnings, it took an outside party to bring to light a possible theft of funds occurring within the Collector’s office.

Of particular concern to this office is that notwithstanding the virtual drum beat of warnings repeatedly detailed in the management letters from Melanson Heath & Co., the DOR and the OIG, the Collector suggested to OIG staff that most of the findings that had been made by the OIG, DOR, and Melanson Heath & Co. referred to issues with the Treasurer’s office rather than the Collector. Although many findings and recommendations offered by the oversight agencies did reference the Treasurer’s office, the OIG is concerned that this may be misconstrued by the Collector and other City officials as an indication that the Collector’s office or other City offices bear less responsibility for addressing any internal control and financial management weaknesses and for ensuring that City funds are protected against fraud, waste, and abuse. This report highlights numerous weaknesses in the way the Collector’s office is managed and provides numerous practical suggestions to tighten its systems. Without changes, the Collector’s office will continue to be vulnerable to fraud, waste, and abuse.

Lastly, the OIG notes the full cooperation of the Collector, the current members of his staff, and the Deputy City Collector. We thank the Collector and his staff and the Deputy City Collector for their full cooperation.

If the OIG can be of further assistance to you, or if you have any questions or concerns, please do not hesitate to contact Senior Investigator Eric Knight.

Sincerely,



Gregory W. Sullivan  
Inspector General

cc: Sen. Michael Knapik  
Robert Kane, Holyoke Collector  
Jon Lumbra, Holyoke Treasurer  
Brian Smith, City Auditor  
Patricia Devine, City Councilor  
Melanson Heath & Co.  
Gerard Perry, Bureau of Accounts, Department of Revenue