

**Report of Internal Audit
CATS Fare Evasion Fines
Investigation of Embezzlement
June 25, 2014**

**City of Charlotte
City Auditor's Office
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Purpose and Scope

The purpose of this audit was to determine the reasonableness of the reported loss related to the Fare Evasion Fines Collection Process, as well as to review the new policies and procedures put into place following the embezzlement. CATS requested Internal Audit's assistance after learning that an employee of an outside contractor embezzled approximately \$50,000 of the City's Fare Evasion Fines collected.

Auditors reviewed the work performed by Central Parking Systems (CPS) staff to establish the amount of loss from its employee's theft of funds. In addition, we reviewed CATS new policies and observed new procedures which had been implemented. Tests were designed to determine whether:

- The loss calculation and proposed reimbursement reported by CPS was reasonable;
- CATS' new policies and procedures are sufficient to control collections; and
- The new policies and procedures are being followed by CATS employees.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

This report is intended for the use of the City Manager's Office, City Council and CATS.

Conclusion

The incident has been satisfactorily resolved as follows:

- Known losses from the contract employee's embezzlement have been recovered,
- CATS and Internal Audit staff have briefed CMPD, and
- Fine collections are now in house, and new procedures are in place to reduce the risk of similar losses in the future.

However, CATS personnel did not coordinate its own staff's efforts, or sufficiently involve other departments which could have assisted with the implementation of effective controls when initiating a new service. In addition, CATS did not take timely action to implement the controls.

CATS has been responsive to our recommendations. No immediate follow-up is required from Internal Audit, but we will consider their responses as we conduct future audits.

Summary of Findings

- The City accepted a reimbursement of \$50,750, which Internal Audit supported.
- Effective controls over fare evasion fine collections are in place.
- CATS can improve upon its implementation of new processes.
- Following the discovery of the loss, CATS did not implement sufficient controls timely.

Background

CATS Blue Line Light Rail operations began in 2007. Beginning that same year, the City arranged for CPS to collect the fines paid as a result of fare evasion on CATS Light Rail. CPS was already under contract with the Charlotte Department of Transportation (CDOT) to collect parking revenues and fines as part of the ParkIt! operation.

In August 2013, CPS notified CATS Safety and Security that a theft of fare evasion fines had occurred. A CPS employee assigned to collect Light Rail fare evasion fines admitted to stealing approximately \$15,000. (During the same time period, Cherry Bekaert, the outside auditor of the City, and separately, the external auditor of ParkIt! operations, also became aware of the theft.) Upon discovering the employee theft, CPS and CATS agreed that CATS would immediately take control of the collection process, using its own employees.

Audit Findings and Recommendations

1. The City accepted a reimbursement of \$50,750, which Internal Audit supported. Effective controls over fare evasion fine collections are in place.

CPS conducted its own review and subsequently offered the City a reimbursement equal to its findings. At CATS' request, City Internal Audit reviewed CPS' work which documented losses due to the actions of a former employee of CPS. We agreed that CPS' conclusion was reasonably accurate for the period documents existed. We were unable to determine whether additional losses may have occurred prior to January 2011 because CPS staff could not locate records related to any earlier time periods. (Collections had begun in 2007.) A settlement agreement was signed by CPS and the City in January 2014 and the reimbursement check was subsequently received.

Auditors conducted a detailed review of randomly and judgmentally selected daily and monthly transactions and reconciliations. Several controls that were implemented after CATS began collecting the fare evasion fines in August 2013 were found to be functioning effectively in recent months, as evidenced by the following:

- CATS has segregated collections and reconciliations. CATS Marketing Pass Sales staff collects fare evasion fines and CATS Revenue staff performs monthly reconciliations. Marketing Pass Sales staff handles over \$11 million annual sales of bus and rail fares throughout the City.

- Interviews determined that current CATS Marketing and Revenue staff possess a high level of knowledge of the new policies and procedures, and the understanding to execute them.
- Audit staff conducted a walk-through at the City Transit Center where cash collections are made. Auditors examined supporting documentation and noted that appropriate controls were in place.
- An aged accounts receivable report is current and is being updated monthly.

2. CATS can improve upon its implementation of new processes.

We noted that CATS was required to implement multiple processes related to the start-up of a large, complex operation. However, our review focused on the deficiencies related to controlling the collections of fines. CATS did not adequately manage the initiation and subsequent monitoring of light rail fine collections. As new processes are developed, CATS needs to make improvements in the following areas:

- *Planning for new processes*

No plan was developed to supervise the contractor, monitor results or reconcile citations to collections. A reconciliation attempt would have raised questions early on, and possibly stopped any losses immediately. CDOT's existing contract with CPS required an annual CPA audit which was conducted by Cherry Bekaert, also the City's independent auditor, but CATS did not formally amend that contract, or establish a similar audit requirement. Over a six year period, this lack of control enabled a CPS employee to embezzle City funds undetected, while the Fare Evasion receivable balance was rising.

- *External Coordination*

Fine collections are a very small part of revenues generated by CATS' normal operations. However, best practices suggest that the establishment of new operations should consider input from others with expertise in the areas of finance, legal and internal controls. While informal discussions may have been held, CATS should coordinate more formally with other City departments and divisions.

- *Internal Coordination*

The responsibility over fare evasion fines was not clearly defined among three internal groups. Safety and Security maintains oversight of the contractors who issue fines, the system (CODY) in which the fines are documented, and the contract with Central Parking. Marketing oversees some revenue contracts, ticket and pass sales. CATS Finance was initially (2007) responsible for CATS' budget activity. Revenue has evolved since then to oversee accounting, financial planning, reporting, controls, and the monitoring of construction expenditures.

In February 2013, CATS Revenue staff met with CPS staff in response to a CATS Safety and Security employee noting discrepancies in data related to citation revenue deposited. The Safety and Security employee had noted that the collections for the first half of FY2013 appeared very low – approximately \$700. Subsequently, CATS Safety and Security began requesting and reviewing documentation of daily activity from CPS. A review of this activity indicates that deposits increased substantially following the meeting between CATS and CPS, but then declined after about two months. In March 2013, CATS Revenue staff issued an internal memorandum (Subject: Park It! Fare Citation Collection and Processing Audit) suggesting that controls should be improved. However, the Revenue staff's efforts did not address the root problems, or uncover the results of poor controls. Also, CATS Revenue and CATS Safety/Security did not work together to recognize the potential impact of these events – rising receivables, no reconciliations, changes in the contractor's deposit activity.

Actions Taken: Collections have been moved in-house. By January 25, 2014, CATS Revenue staff completed comprehensive monthly cash reconciliations for August through November 2013. They continue to perform monthly reconciliations.

Recommendations:

- A. In the future, CATS should inquire with City departments that may be affected by their actions prior to implementing policy or procedure changes. Specifically, the City's Cash Collection Guide ("FIN 1," adopted in 1989) provides guidance that would have been helpful to CATS.
- B. Monthly reconciliations and trend analysis should be performed by CATS Revenue. Any unusual patterns should be further investigated.
- C. As stated in CATS Procedure S&S12 (i.e., Safety & Security #12), CATS Revenue should audit overall procedures and reconciliations and provide a report to CATS Management, Safety & Security, and Customer Service.

CATS Response: CATS concurs.

3. Following the discovery of the loss, CATS did not implement sufficient controls timely.

In response to the theft and after taking control of the fare evasion fines collection process in August 2013, CATS took several immediate steps to remedy the control deficiencies. These steps included the development of appropriate policies (with which Internal Audit concurred), and efforts to train staff to implement new responsibilities. Despite these actions, CATS did not implement sufficient control measures in a timely manner. The requirements of a policy which became effective October 31, 2013, were not completed until January 24, 2014.

When Internal Audit attempted to review CATS' documentation in January 2014, CATS was unable to comply with the request. In response, the first documentation submitted was a

combined four-month reconciliation. A few days later, CATS completed the individual monthly reconciliations for August-November, as indicated in its October 2013 policy.

Recommendation: Upon adoption of its own controls, CATS should undertake appropriate supervisory efforts to ensure that employees are performing the duties committed.

CATS Response: CATS agrees that its goal is to ensure adherence to all of its policies; and that processes are in place for supervisors to review duties performed by their employees.