

A REPORT
TO THE
ARIZONA LEGISLATURE

Special Investigative Unit

Special Investigation

City of Sierra Vista

Theft of Public Monies

JANUARY • 2005



Debra K. Davenport
Auditor General

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STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

WILLIAM THOMSON
DEPUTY AUDITOR GENERAL

January 27, 2005

Members of the Arizona Legislature

City of Sierra Vista Mayor and Council

The Honorable Terry Goddard
Attorney General

The Office of the Auditor General has conducted a special investigation of the City of Sierra Vista for the period August 1999 through August 2002. The investigation was performed to determine the amount of public monies misused, if any, during that period and the extent to which those monies had been misused.

The investigation consisted primarily of inquiries and examination of selected financial records and other documentation. Therefore, the investigation was substantially less in scope than an audit conducted in accordance with generally accepted auditing standards. Accordingly, the Office does not express an opinion on the adequacy of the financial records or the internal controls of the City of Sierra Vista. The Office also does not ensure that all matters involving the City's internal controls that might be material weaknesses under standards established by the American Institute of Certified Public Accountants or other conditions that may require correction or improvement have been disclosed.

The accompanying Investigative Report describes the Office's findings and conclusion as a result of this special investigation.

After this report is distributed to the members of the Arizona State Legislature, the Mayor and City Council, and the Attorney General, it becomes public record.

Sincerely,

Debbie Davenport
Auditor General

Enclosure

SUMMARY

In November 2002, the Arizona Attorney General's Office requested that the Office of the Auditor General investigate allegations of financial misconduct by Mr. Gary McPherran, CPA, former administrative services director, and Mr. Gary Murray, former accountant for the City of Sierra Vista. Our Office conducted an investigation and submitted our report to the Attorney General's Office. The Attorney General has taken criminal action against Mr. McPherran and Mr. Murray. Both individuals have been indicted on felony charges. See Conclusion on page 13.

Our investigation revealed that from August 1999 to August 2002, Mr. McPherran and Mr. Murray may have embezzled at least \$25,990 and \$21,277, respectively. These former employees used city money to pay for their personal travel expenses in places like Arizona, California, and Nevada, as well as other personal purchases including concert tickets, alcohol, and cigarettes.

The City's internal controls over travel, petty cash, and credit card activities were inadequate, primarily because those controls did not prevent Mr. McPherran and Mr. Murray from initiating, approving, and reconciling those types of activities. As a result, Mr. McPherran and Mr. Murray were able to embezzle city monies for at least 3 years, and the City was unable to deter or detect their thefts.

Mr. McPherran and Mr. Murray may have embezzled at least \$25,990 and \$21,277, respectively, from the City.

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INTRODUCTION & BACKGROUND

The City of Sierra Vista is located in Cochise County, approximately 70 miles southeast of Tucson, and currently has a population of nearly 40,000.

The City of Sierra Vista's management is fiscally accountable to its citizens and taxpayers for General Fund revenues totaling \$20.9 million in fiscal year 2004. General Fund monies consist primarily of taxes, intergovernmental revenues, and charges for services. Management is also responsible for establishing effective internal controls to help ensure the appropriate expenditures of those monies.

As the City's Director of Administrative Services since June 1999, Mr. Gary McPherran was responsible for managing the divisions of Human Resources, Purchasing, Finance, and Information Technology, and worked under the general supervision of the city manager. Prior to this promotion, Mr. McPherran was the City's finance manager for over 3 years.

Mr. Gary Murray began working within the City's finance department in 1995, and in November 1999 was promoted to junior accountant. As a junior accountant, Mr. Murray's responsibilities included processing cash receipts, purchase orders, travel orders, and invoices, and reconciling credit card statements. Mr. Murray reported to Mr. McPherran.

On August 6, 2002, Mr. McPherran and Mr. Murray were placed on paid administrative leave until the City completed an internal review of both employees' alleged financial misconduct. Before the City's review was completed, Mr. Murray voluntarily resigned on September 30, 2002. Mr. McPherran's employment was terminated on November 13, 2002.

FINDING 1

Employees embezzled public monies

From August 1999 to August 2002, Mr. Gary McPherran, CPA, former administrative services director, and Mr. Gary Murray, former accountant, allegedly embezzled at least \$47,267 from the City of Sierra Vista by misusing the City's travel expense process and credit card privileges to perpetrate their thefts. Over a 3-year period, these employees may have repeatedly violated state laws related to theft and fraudulent schemes.

As summarized in Exhibit 1 below, Mr. McPherran unlawfully paid himself \$19,213 by including his personal travel expenses with business travel and by fabricating travel expenses for training and business meetings that either did not exist or that he did not attend. Also, because Mr. McPherran falsely represented this time as business-related travel rather than personal time, he committed performance fraud totaling at least \$5,615 in salary costs. In addition, Mr. McPherran's subordinate, Mr. Murray, also misappropriated \$12,496 by including his personal travel expenses with business travel and arranging for the City to pay him for travel expenses already paid by another entity. Finally, both employees misused the city credit card account for personal purchases totaling \$9,943.

Exhibit 1: Alleged Theft Schemes
August 1999 to August 2002

Description	McPherran	Murray	Total
Fraudulent Travel Expenses	\$ 19,213	\$ 12,496	\$ 31,709
Performance Fraud	5,615	n/a	5,615
Personal Credit Card Purchases	<u>1,162</u>	<u>8,781</u>	<u>9,943</u>
Total	<u>\$ 25,990</u>	<u>\$ 21,277</u>	<u>\$ 47,267</u>

Source: Auditor General staff analysis of City of Sierra Vista, Bank of America, and private business records.

Fraudulent Travel Expenses

From August 1999 to August 2002, Mr. McPherran and Mr. Murray submitted 54 fraudulent travel forms to embezzle \$31,709.

Mr. McPherran embezzled at least \$10,460 by repeatedly obtaining advances for meal expenses using city checks and petty cash, and subsequently using the city credit card for those same expenses; and using city money to pay for extra hotel nights, hotel movies, and other personal luxury items such as Las Vegas entertainment tickets, chiropractor fees, photographs, personal auto repair services, and cash advances.

Mr. McPherran embezzled an additional \$8,753 by using city money for personal trips. He repeatedly misrepresented to the City that he was attending trainings that he did not attend. Examples of Mr. McPherran's actions include:

Mr. McPherran embezzled \$8,753 from the City by claiming travel expenses for:

- Trainings he did not attend or;
- Trainings and meetings that did not exist.

Mr. McPherran claimed he attended a 3-day governmental accounting training in Long Beach, California, during the summer of 2000, but instead stayed over 30 miles away, for 6 days, in Anaheim, California, at the Hilton Resort, 2 minutes from Disneyland. The City paid \$2,036 for Mr. McPherran's personal expenses including his and two children's hotel stay, room service, valet parking, car rental, fuel expenses, and meals. Although the City paid the \$575 registration fee for the conference, Mr. McPherran did not attend and was marked as absent for each morning and afternoon of the conference. He also continued to collect his normal salary without taking any vacation time.

Mr. McPherran often traveled to Phoenix and Tucson claiming to attend trainings. On at least five occasions, he did not attend the training, yet still received petty cash and check advances and then charged hotel stays, room service, and restaurant expenses on the city credit card.

Mr. McPherran also claimed expenses for meetings and trainings that never existed. For instance, Mr. McPherran claimed there was a new W2 format reporting training held in Las Vegas from December 29, 2001, through December 31, 2001. Yet, there was no record of such training, and an e-mail extracted from Mr. McPherran's computer found him planning a "rendezvous" and vacation in Las Vegas for this same time period. Despite the personal nature of this trip, Mr. McPherran claimed \$383 in expenses and did not record the use of any vacation time.

On another occasion, Mr. McPherran declared he attended a weekend insurance training in Phoenix. Although there is no record of such insurance training, city receipts show that Mr. McPherran went out for dinner, checked into a Phoenix hotel at 12:45 a.m. on Saturday morning with another adult, and went bowling that afternoon. Mr. McPherran claimed \$546 in expenses for this trip.

Moreover, the day before Mr. McPherran was released on administrative leave, he deposited a \$657 travel advancement check into his personal checking account for conferences allegedly scheduled during the next 4 months. Mr. McPherran's employment was subsequently terminated, and he never attended the conferences or returned the money to the City.

Mr. Murray embezzled \$11,496 from the City by frequently requesting checks payable to himself and withdrawing petty cash for personal travel expenses and other items such as alcohol, cigarettes, and movies. In addition, Mr. Murray received reimbursements for five conferences sponsored and paid for by the organization servicing the City's software. Mr. Murray repeatedly requested and obtained travel payments from the City despite the fact that the conference sponsor paid his expenses. Finally, Mr. Murray embezzled an additional \$1,000 by completing a fictitious travel form claiming that the City's computer software service organization held a seminar in Las Vegas in 2000. Although Mr. Murray received the \$1,000, he did not submit any supporting documentation to the City verifying that this seminar occurred nor did any records indicate that Mr. Murray left the City during this period. The City's software service organization affirmed that no seminar was held in Las Vegas in 2000.

Mr. Murray created a fictitious \$1,000 travel form.

Performance Fraud

From September 1999 to June 2002, Mr. McPherran took several personal trips during working hours, yet failed to use his vacation time. Under A.R.S §13-1802, "a person commits theft, if without lawful authority, the person knowingly obtains services or property of another by means of any material misrepresentation with intent to deprive the other party of such property or services." Mr. McPherran falsely represented that his time was spent on business-related training when, in fact, he did not attend any training or stayed beyond the training's allotted time frame. As mentioned earlier, Mr. McPherran took a week-long personal trip to Anaheim, California, and spent several personal days in Las Vegas without claiming any vacation time. He also added personal days to business-related trips without claiming any vacation time. In total, Mr. McPherran charged the City for 20 personal days that should have been taken as vacation, thereby embezzling at least \$5,615 of his salary from the City.

Mr. McPherran took a week-long personal trip to California without using any vacation time.

Personal Credit Card Purchases

By taking advantage of the City's insufficient control policies and procedures related to its credit card process, Mr. McPherran and Mr. Murray were able to charge over \$9,900 of personal items to their city credit card accounts, which were then paid by the City.

Mr. McPherran—During a 5-month period from March 2002 through July 2002, Mr. McPherran embezzled \$1,162 by making personal purchases at food and drug stores, and an electronic store, and also for veterinarian services, car maintenance, flowers, and concert tickets.

Mr. Murray admitted to using the city credit card for his own personal use.

Mr. Murray—In November 2000, Mr. Murray received his city credit card privileges and immediately began making personal purchases. By August 2002, he had charged 372 personal purchases totaling \$7,846 and incurred 49 finance and fee charges totaling \$935.

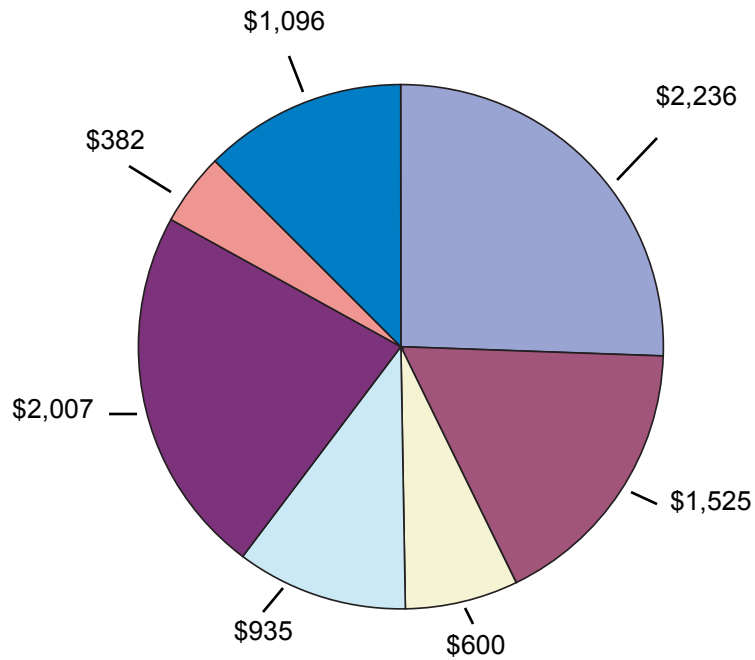
Mr. Murray would make up to three separate visits to the same convenience store in a single day and used city money to purchase alcohol at that store.

As summarized in Exhibit 2 on page 7, Mr. Murray's personal credit card charges include 213 convenience store purchases totaling over \$2,200. In fact, 188 of those charges were to the same convenience store, and Mr. Murray made up to three separate visits to this store in a single day. Mr. Murray admitted to using the city credit card for personal purchases, including the purchase of alcoholic beverages, at this particular store. Mr. Murray also charged a total of \$1,525 at food and drug stores. Other personal purchases include items such as automobile maintenance, cash advances, health club fees, dry cleaning services, and expenses at a Tucson adult entertainment club.

In addition, Mr. Murray circumvented normal city practice and controlled the processing of his city credit card payments; still, he failed to make timely payments on the account. As a result, the City was charged \$935 for late fees, overlimit fees, and finance charges.

Only approximately 10 percent or \$1,100, of Mr. Murray's total credit card charges were for legitimate city purchases.

Exhibit 2: Gary Murray—Personal Credit Card Purchases
November 2000 to August 2002



- | | |
|--------------------|--|
| Convenience stores | Food and drug stores |
| Hotel/car rental | Late fees, overlimit fees, finance charges |
| Other ¹ | Restaurant/bar |
| Retail stores | |

1 Other personal purchases include automobile maintenance, cash advances, health club fees, dry cleaning services, telephone charges, optometry fees, credit report access fee, and expenses at an adult entertainment club.

Source: Auditor General staff analysis of City of Sierra Vista and Bank of America records.

FINDING 2

City management failed to ensure adequate controls

The City's management failed to implement an adequate system of internal controls for their travel, petty cash, and credit card purchase cycles. In fact, the City's insufficient segregation of duties and ambiguous or absent policies weakened their control environment and allowed Mr. McPherran and Mr. Murray to embezzle public money.

Controls over travel expenses—Employees' travel expenses and supporting documentation should be independently reviewed and approved at a supervisory level prior to any payment of city monies. However, Mr. McPherran and Mr. Murray were able to approve their own travel expenses. They were able to individually authorize checks and withdraw petty cash. Because no controls were established to prohibit Mr. McPherran and Mr. Murray from approving their own travel expenses or adding more expenses after approval, they had complete discretion over their own expense requests. Further, Mr. Murray reconciled Mr. McPherran's as well as his own travel forms, which allowed the thefts to continue without being detected.

Controls over petty cash—Petty cash withdrawals should be controlled to ensure a specific city purpose and independently reconciled to the travel forms and supporting documentation. Yet, city management did not enforce existing policy or have adequate controls in place to deter or detect unauthorized or excessive withdrawals of petty cash. Although petty cash issuances are reportedly limited to \$100 for each employee, the City did not enforce this policy, and these two former employees easily obtained cash beyond the allowable amount on several occasions. Further, these overpayments went undetected because the petty cash and travel forms were not properly reconciled.

Controls over credit card use—The City should establish and distribute a credit card policy providing guidelines as to allowable purchases, spending limitations, required documentation, and proper reconciliation processes. However, as of August 2002,

54 employees had been issued city credit cards, but no credit card policy had been published to guide their use. Furthermore, credit card statements were only reconciled to available receipts for completeness. The credit card statements were not reconciled to ensure the purchase was for a specific city purpose or to determine if the purchase was already paid through a travel form, which would have resulted in a duplicate payment.

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RECOMMENDATIONS

To help ensure proper control over and use of public monies, city management should establish effective internal controls over travel, petty cash, and credit card activities including policies, procedures, and monitoring activities. Specifically, management should ensure that:

1. No city employee has the ability to carry out all steps in the travel expense process. Accordingly, the City should properly separate among employees the following travel expense activities:
 - Recording travel expenditures
 - Approving department, budget, and accounting levels of travel expenditures
 - Reconciling petty cash issuances and original receipts to travel forms
2. All changes made to travel expenses and payment requests receive unrelated supervisory approval once initial approvals are obtained.
3. No city employee has the ability to carry out all steps in the credit card process. Accordingly, the City should properly separate among employees the following credit card functions:
 - Authorizing credit card issuance
 - Receiving credit card statements
 - Reconciling credit card statements to receipts and invoices
 - Reviewing credit card usage to ensure it is for appropriate city purposes
 - Authorizing payment
4. Policies are updated, clarified, and implemented for petty cash and travel activities. These policies should include clear guidelines for reconciling petty

cash issuances with travel forms and receipts, as well as determining the appropriateness of the travel.

5. Policies are established and implemented for proper credit card use. These policies should include a requirement that the public purpose of purchases made with the credit card are appropriately documented and approved.
6. Periodic monitoring is performed to ensure that all policies and procedures are being followed.

CONCLUSION

On January 13, 2005, the Arizona Attorney General's Office took criminal action against Mr. Gary McPherran and Mr. Gary Murray through the Superior Court Grand Jury. This action resulted in the indictment of both individuals on two counts each of theft and fraudulent schemes.

