

To: Nicole Galloway - Missouri State Auditor
Mary Johnson - Chief Investigator, State Auditor's Office
Mayor and City Council, City of St. Joseph, MO

From: Beau Musser, CPA
Assistant Director of Administrative Services (Controller)
City of St. Joseph, MO

Subject: Financial Concerns - City of St. Joseph

Date: 1-14-2020

The purpose of this memo is to formally notify the Missouri State Auditor of numerous material accounting deficiencies and irregularities with the financial systems of the City of St Joseph, Missouri. This memo is necessary because of the lack of an appropriate response by senior city administrators and elected officials.

In August of 2019, after 12 frustrating months of trying to convince senior city administrators to address and fix a multitude of internal control issues and financial concerns at the City of St. Joseph, MO, I emailed the City Manager and Mayor a 12 page memo detailing those concerns and I asked them for help in addressing my concerns. After nearly 4 months, nothing meaningful has transpired to fix these problems and worse yet, I was removed from supervising the activities on which I blew the whistle. In fact, neither the City Manager or the Mayor even asked me a follow up question to my well documented concerns. It was my expectation that my concerns would be communicated to the entirety of city council and the city's "blue ribbon audit committee," however, that was not the case. As a CPA, I have a professional obligation to document the issues that I encounter and issues that have been reported to me. Those detailed concerns can be found below.

Sewer Billing Issues

- Weekly Exception Report, which is the most important step in weekly invoicing process, was not being reviewed and addressed each week prior to my work at the city.
 - Annual lost revenue is estimated to be at least **\$250,000** (Millions of \$'s lost over time)
 - The customer service manager who oversees sewer billing was never properly trained for the job. She has had the job for approximately 3 years, and to this day (12 months after I blew the whistle), no detailed written procedures exist for her and her staff to follow
- Certificate of Occupancy Permits not reviewed by the sewer billing department to ensure new businesses are being billed for sewer (No report even existed when I first started looking into this. Permits were issued using power-point files.)
 - Brand new Brewery in town operated without receiving a sewer bill. The other new brewery was receiving a sewer bill but being billed incorrectly as a residential customer
- Sewer Tap Connection Report not reviewed by the sewer billing department (No said report even existed)
 - Approximately 60 new customers never received bills, an annual cost of approx **\$50,000** to the city. The city even paid a contractor over \$45,000 to join our sewer system and then went years without ever receiving a sewer bill. An audit of all sewer tap connections

revealed that nearly 25% of all new sewer tap connections did NOT receive a sewer bill. The City Manager misled the City's audit committee by pretending this was an isolated issue related to "not checking a box" when in fact the problem is due to a complete lack of internal controls

- Customers on Autopay not receiving sewer bills. My own personal sewer bill was either not billed or billed incorrectly (zero usage) wrong twice within a 12 month period
- Only Customers with current monthly activity were mailed statements indicating a balance due
- A City Council Member's new business went years without ever receiving a sewer bill. After I learned of this and communicated to staff to start billing the customer, the account still wasn't billed for 3 months after I was assured they were being billed.
- Old accounts receivable balances not reviewed and followed up on by the sewer billing department. Statements weren't even mailed to the customer
- For years, the Director of Revenue and Sewer billing staff have violated the city's own policy by reducing customer's sewer bills without the proper authority to do so. This can be confirmed by the public works director
- Annual Sewer Revenue continues to fall \$1,000,000 short of the annual amount we should be receiving based on the city's own Annual Sewer Rate Study. This study is prepared by outside consulting firms (Historically, Craig Brown with Black and Veatch). For years, our consultants have highlighted significant lost revenue from commercial customers - a problem ignored by the City Manager and CFO (This can be confirmed by the Director of Public Works). A reconciliation of actual sewer usage revenue to our annual sewer rate reports shows potential lost revenue of more than **\$2.5 million** from FY 17 to FY 19. More details of lost commercial revenue is noted below
- Internal Audit review of the City's permitting process produced countless inconsistencies, including numerous instances of permits issued without being invoiced. According to the Director of Technology, a current city council member was able to get permits without being invoiced the fee
 - Chamber of Commerce Employee allowed to install a septic tank when he did not have 3 acres of land required by city law. Ironically, the address was issued a sewer connection permit (although never billed for sewer services)
 - According to the Director of Revenue, the City Manager, CFO and Director of Planning and Development turned a blind eye while an elected official illegally tapped the City's sewer system without pulling Permits (\$500 permit fee). This is significant because not only does it provide the plumber an unfair advantage, but the city loses out on sewer revenue because it has no way of knowing the customer is on our sewer system.
- According to multiple Public Works employees, the following commercial sewer billing issues (Which cost sewer users millions of dollars) were noted PRIOR to my arrival at the City of St. Joseph. Please keep in mind that these issues were known by the City Manager and the City's CFO (Director of Admin Services) and he still directed me to NOT review the city's sewer billing issues
 - "The Director of Revenue, because of her failure to understand Excel failed to average billing for several industries resulting in them only being billed for 2 or 3 days a month instead of the full month. The result was a loss in income to the city of over **2 million dollars**. The actual net result was that the **residents were paying a higher rate than they should have**, this burden should have been on the wholesale customers. I have an email to Bruce on this subject. He was informed on 01/08/18, he decided not to correct the issue until 07/01/18."

- “There was an industry in St. Joseph called Oak Mill, they were operating without a business license and no one was aware they existed. After we became aware of them they ran up a sewer bill of approximately **\$250,000**. During this period I kept wanting to shut them down. City Hall wouldn't allow it. (City Manager & Legal). In summary they folded up shop and never paid their bill.”
- “Blue Sun (Commercial Customer), KQTV filed a FOIA on the city requesting billing information related to Blue Sun. I supplied a spreadsheet that showed that Blue Sun was allowed to not pay from Apr 2013 - Jan 2014 a total of **\$771,705.39**. Bruce stated in an interview on KQTV that it was \$410,000.00.”
 - According to the Director of Public Works, when this information was “sunshined” (Freedom of Information Act), the City Manager/Legal Department withheld pertinent information and misled the public on the extent of the problem (Lost revenue which ultimately increased the sewer bill that everyone else had to pay).

Misappropriation of Sales Tax Revenue

- A 1% sales tax passed in 1979 was approved by voters with 70% of those funds to be spent on capital improvements for streets. For Fiscal Years 2019 and 2020, \$0 was allocated to large street improvement projects (The tax brings in approximately \$12,000,000 annually). Ultimately, the sales tax revenue (70% of \$12,000,000) is being diverted to the general fund to help cover the City's deficit spending that has taken place the last 3 or 4 fiscal years.

Misrepresentation of General Fund Balance

- For the FY 2019 City Budget presented to City Council, the general fund unassigned fund balance was wildly overstated. \$9,164,438 was reported to City Council when adopting the budget, when the city's own audited report showed a balance of only \$4,906,522. This false presentation was hiding the fact that the city's General Fund Balance was/is in peril. To verify this information, I am providing the following links:
 - <https://www.stjoemo.info/ArchiveCenter/ViewFile/Item/565> (Page 37 of 362)
 - <https://www.stjoemo.info/ArchiveCenter/ViewFile/Item/591> (Page 151)

Misrepresentation of Financials

- The City Manager continues to misrepresent the finances of the Municipal golf course. In the FY 2020 Budget book, the City manager stated the golf fund barely meets it's revenue needs, when in fact, the Golf course loses approximately \$200,0000+ annually
- FY 20 City Manager budget memo states that there is a balanced general fund budget when in fact the city has a significant budget deficit. And this deficit should be more as the city manager has diverted Sales tax revenue to the general fund when voters approved it to be spent on capital street improvements (70% of \$12 million is going to the general fund instead of the streets department)

Police Pension Fund - Potential Out of Compliance with Federal Tax Laws

- Just before my first day at the city (August 2018), the city police pension fund went from self managed to LAGERS for existing employees while retired employees stayed on the existing plan. During that process, the plan went out of compliance with the IRS (according to a third party

attorney), and as a result, it's possible the retiree benefits would become taxable to the retirees. The police pension fund has hired a new attorney to fix this problem.

Prevention of Critical Information Reporting to City Council

- Negative Unreserved Landfill Fund Balance (Multi-Million \$ Deficit) while continuing to use landfill profits on general fund expenses. Landfill funds being used for non-landfill purposes without even asking the Landfill director, who had expressed concerns about the negative unreserved fund balance
- \$6 million Street Department equipment needs
 - According to the Director of Public Works, the City Manager will not allow the public works department to communicate this information to city council (Keep in mind that the 1% sales tax revenue is already being diverted to the general fund)
- Refusal to allow the Annual Financial Audit to be presented by the city's auditor to city council (Auditor told me and City Manager that the city was in a financial emergency as of 6/30/18. This info was never communicated to City council). The City went 3 fiscal years without bringing the auditor in to present this information. During this timeframe, the City's general fund unassigned balance went from nearly \$13,218,788 to \$4,906,522. Ideal reserves for the city would be closer to \$20 or \$25 million
- Refusal to provide detailed Capital project information to city council
- Refusal to provide detailed financial information at the g/l account and program level to City Council
- Massive discrepancies in actual sewer user revenue vs. expected revenue based on actual water usage (See the detailed section documenting sewer billing issues above)

Misappropriation of CIP Funds

- CIP Funds misappropriated - Should have used Sewer (Enterprise) Fund for Bike Trail Land Expenditures. The director of Public Works can confirm that these expense reclasses were proposed by myself and him, but not booked by the CFO

Potential Payroll/Pension Misappropriation of Assets

- It's been reported to me by a Director at the city that the City may have misappropriated pension funds when it terminated it's former HR Director. The former HR director was terminated prior to the city's pension enhancement date (7/1/17), however, she was paid thru 11/16/17 setting up the possibility she is receiving the pension enhancement that she did not earn.
- It's been reported to me that the City's former CFO reported other payroll misappropriations by the city's one and only payroll accountant. The former CFO went to discipline the payroll employee but was prevented from doing so by the City Manager/City Attorney. Ultimately, it was the former CFO who was terminated (or forced to resign)

Other Issues related to Elected Officials

- City Council Member "A" racked up a \$500 cell phone bill and did not reimburse the city. The Assistant City Manager attempted to misappropriate funds to the public works department. This can be confirmed by city employees in the IT Department.

- City Council Member “B” was issued a permit without being billed the permit fee (This can be confirmed by the director or IT)
- The Director of Revenue claims that a former elected official was notorious for tapping the city's sewer without pulling the required \$500 permit fee.
- As part of my internal audit procedures (Reviewing permits to ensure the company/individual was receiving a sewer bill), it was noted that NUMEROUS instances could be found where companies/individuals received permits without paying the relevant fee. Many years have gone by without anyone providing oversight of the city's permitting process. A detailed review of the city's permitting process (by an independent/external auditor) is desperately needed. For more information, please contact the Director of IT.
- City Council Member “A” has not recused himself from voting on their employers construction contracts with the City (This is was reported to me by the Director of Public Works and known by the City Manager)
- Director of Admin Services attempted to gain private/sensitive sales tax information on a furniture company that is a competitor of his sister's employer
- The Current Mayor defamed me during a public meeting. Claimed I "Plugged #s" in the financial reports I provided to city council.

Information Technology Concerns

- 1 digit passwords allowed - In a world where most companies require 10 digit passwords that include numbers/letters/symbols and capitalization, the City of St. Joe allows for employees to have 1 digit passwords. This is a massive security risk.
- No requirement to change password after a new employee starts working
- No “Lock screen” feature (If an employee walks away from the computer for a short period of time, the PC should revert to a locked screen in order to prevent someone else from accessing sensitive data)
- Multiple Directors falling for “phishing schemes”, including \$800 worth of Google Play gift cards purchased for the City Manager by the HR Director. The Director of the Parks Department was on his way to buy \$800 of Google Play cards before the IT Department called him to inform him it was a scam
- No required IT Security Training - even after the Director of HR fell for a “phishing email scam”

General Accounting Concerns

- Numerous cash accounts not reconciled on a monthly basis
 - The Civic Arena Bank Account went unreconciled for 12 straight months in FY 18. When I instructed Accountant “A” to reconcile the account, she was unable to do so properly
 - The Civic Arena Concession stand had over \$100,000 in cash sales each fiscal year with no inventory system or point of sale system. I expressed my concern to the CFO that cash sales would “make a thief out of an honest person,” but he didn't share my same concern and told me to ignore this problem (Every problem I encountered, including Millions of lost sewer revenue, I was told to ignore)
 - In FY 19, I realized that not only had “Accountant A” not reconciled the Police Pension Investment account for 4 months, she hadn't even recorded the monthly pension disbursements which totaled more than \$200,000 each month. This is a complete

breakdown of the City's fiduciary duty to provide proper accounting and controls for this fund.

- For all other investment accounts, the city did not account for investments at Market Value and the CFO couldn't understand why this is necessary (The balance sheet, which is never provided to city council, would be incorrect. Accounting 101 tells us that if the Balance Sheet is incorrect, then by default so is the Income Statement)
- Cash balances by city program not accounted for properly each month
- Inability of city staff accountants to produce proper monthly financial statements including Balance Sheet reports (In fact, only with the help of the external auditor is city staff able to produce Annual Financial Statements. Unfortunately, those annual financial statements were not presented to City Council for 3 years (from FY 16 to FY 18). A period in which the City's unassigned Fund Balance went from \$13,218,788 to \$4,906,522). Obviously this decrease in Fund Balance was due to deficit spending. In FY 19 and 20, in an attempt to address these deficits, the entirety of the 1% sales tax passed in 1979 by voters was diverted to the general fund)
- Inability to properly calculate fund balances
- The city's Balance Sheet reports (If ever produced) excluded the City's \$30+ million unfunded pension liability (I'm not sure how it's a balance sheet report if balance sheet accounts are excluded)
 - The City's CFO told me that I was spending too much time on the balance sheet
- Accounts Receivable subledger balances not reconciled to the general ledger balance
 - For the FY 18 audit, which began right after I started, the unreconciled balance of sewer fund receivables was approximately \$500,000
- Accounts Receivable Aging reports not reviewed and followed up on (no collection efforts made)
- TIF Accounting - No one in the accounting department, including the CFO, understands the accounting necessary for the Special Allocation Fund (Tax Increment Financing Fund). After the CFO got caught budgeting the exact same amount for FY 20 that he did for FY 19 (FY 19 was wildly inaccurate), he held an impromptu meeting 15 minutes before a city council meeting in an effort to understand the \$10,000,000+ fund balance sitting in this fund. After communicating to the CFO that neither the revenue accountant nor the TIF accountant understood the process, I repeatedly asked for training myself that never materialized. In my attempt to clean up this accounting on a monthly basis, I quickly realized that the city was advancing developers money before it was ever received by the city, resulting in 'negative cash positions' for the city. When I questioned the TIF accountant about this, he admitted that he didn't understand (accounting) accruals. This same accountant, who has the title of budget accountant, told city staff that he had zero budget experience when they hired him for the job.
- Payroll Liability Accounts went unreconciled for nearly 2 years (Since the previous CFO was terminated). I had to make a \$100,000+ adjustment to these liability accounts, which of course meant that reported fund balance was incorrect prior to these adjustments. The lack of oversight of the payroll process was astonishing, especially since the city only has 1 payroll accountant (Which is an internal control issue itself). The lack of oversight of the payroll liability accounts is also concerning considering the potential misappropriation of payroll funds documented above.
- At the time of my last financial review, the city's worker's compensation fund was on the verge of being "upside down" (Negative Fund Balance). I informed the CFO that the general fund would need to fund the Worker's Compensation Fund in order to make up for the difference, otherwise, our general fund balance calculations would be incorrect. I was prevented from making this journal entry. The financial impact of the w/c fund is not insignificant. The city will need to increase the % charged to programs to cover the cost of the self insurance plan, which in turn will exacerbate the city's deficit spending problem.

- Other pressing financial concerns that will impact the general fund in the next fiscal year or 2 is the state of the public safety fund. The public safety fund balance reserves will be depleted (Down to \$0) very soon, and when that happens, the annual transfer to the general fund (which is used to pay for public safety salaries) will have to be reduced. This will exacerbate the current general fund budget deficit. Unfortunately, the general fund reserves are already woefully inadequate, and this “shock to the system” will be difficult to absorb. The financial emergency that was communicated to the City Manager by the external auditor over a year ago is only going to get worse, especially if the city’s pension plan and workers compensation expense burden continue to grow.