

PENNSYLVANIA INTERGOVERNMENTAL COOPERATION AUTHORITY

Minutes of the Meeting of the Board

June 19, 2018

The meeting of the Board of Directors of the Pennsylvania Intergovernmental Cooperation Authority (“PICA”) was held on Tuesday, June 19, 2018 in the PICA board room located at 1500 Walnut Street, 16th Floor, Philadelphia, Pennsylvania.

Attendees

Board: Kevin Vaughan, Tina Byles Williams, Alan Kessler, James Cawley (*via telephone*), Michael Karp (*via telephone*), and Robert A. Dubow (*ex officio*).

Staff: Harvey M. Rice, Gus Tsakos, Dora Ward, Daniel Esposito, and Deidre Morgenstern.

Invited Guests: S. William Richter, Esq., Reed Smith, LLP; Anna Adams, Office of Budget and Program Evaluation; Catherine Paster, Office of the Director of Finance; Jackie Dunn, Office of the Director of Finance; Rasheia Johnson, Office of the City Treasurer.

Call to Order

Mr. Vaughan called the meeting to order at 12:15 p.m.

Approval of Minutes

Mr. Cawley made a motion to approve the minutes from the meeting of May 22, 2018. Mr. Kessler seconded the motion. The motion passed 5-0.

Executive Director’s Report

Mr. Rice stated that PICA staff has issued the following reports since the last Board meeting: the third quarter report on the Quarterly City Managers Report and the May revenue report. Additionally, the City will soon submit the FY2019-2023 Five Year Plan to PICA for review.

PICA staff also executed a new lease, has a drafted a Request for Proposal (RFP) for a study into Police Court Overtime usage, and is formulating a record retention policy. Mr. Kessler asked what the timeframe for the study would be and Mr. Rice responded that he hopes to have all the RFP’s in by July.

Mr. Rice explained that he also provided Board members with investment reports for our Debt Service Reserve Fund which holds low risk investments.

Treasurer's Report

PICA's expenditures are at 87 percent of the budget. Actuals are up, year over year, due to salaries, benefits, and the DROP study.

Resolution 12 – Arbitrage Services

Mr. Rice explained that this is a resolution for the continuation of Parker Bond Consulting's contract for another year. The cost has remained the same. Mr. Kessler made a motion to approve, Mr. Cawley seconded the motion, and the motion passed 5-0 in a roll call vote.

New Business - Report on Financial Statements and Internal Controls of the City of Philadelphia

Mr. Vaughan opened this topic of discussion and requested Mr. Dubow to provide an overview. Mr. Kessler made an initial statement on the topic prior to the City's presentation of its position. Mr. Kessler stated that he is not interested in who was at fault for the deficiencies or how the reconciliation issue arose, as has been discussed in the last few days, but that he is more interested in preventing deficiencies, as well as formulating a plan for the future that would include a combination of personnel and technology as part of the solution. Mr. Kessler referenced the PICA Act in explaining that it is PICA's role, whether or not in connection to the Five Year Plan process, to evaluate the City in terms of "efficient and accountable fiscal practices." He stated that the Task Force involving PICA that was announced this morning by the Mayor is a step in the right direction, but that PICA has other oversight obligations and a role to identify accounting practices and relevant solutions to the issue, including the right to request additional information regarding this topic in the future. He stated that it is fair to wait for a report from the Task Force, but that nonetheless, the Board should keep the reconciliation issue on its agenda for regular discussion at each monthly board meeting in order to get updates from the City. Mr. Kessler closed by saying that identifying best practices in this area and fixing the material weaknesses and significant deficiencies is more important than what is occurring politically within or outside of the PICA Board.

Mr. Dubow explained, in reference to the City Controller's report, that there were 7 accounts that were not reconciled, which accounted for \$40 million. Two of those accounts are not fully reconciled and the City is taking measures, including hiring an outside accounting firm and increasing staff, in order to correct the remaining issues. The outside firm will issue recommendations to the City in November and a full report in December. Mr. Karp asked what were the core causes of these accounting problems. Ms. Johnson replied that there were several retirements of longstanding staff, as well as 4 other vacancies in staff that contributed to the issue. Mr. Kessler asked whether technology has also played a role. Ms. Johnson explained that the City is now cross training other employees in case vacancies occur, reconciliations can continue. She acknowledged that the City could fast track research into reconciliation software, as the City still currently uses Microsoft Excel for these functions.

Ms. Williams asked what the scope of the independent firm's audit will be. Ms. Johnson replied that the firm will be identifying the underlying causes of the accounting problems, will review internal controls, will clear backlog of reconciliations, and will provide recommendations for the future. Ms. Williams also asked how long the vacant positions remained vacant. Ms. Johnson replied that one of them was vacant for 9 to 10 months, while Mr. Dubow added another was vacant for one month. Mr. Cawley asked whether there was other staff available to perform the tasks of the vacant positions in the interim period. Ms. Johnson said that in theory this should occur, and that the City will be cross training employees now with this in mind.

Mr. Dubow went on to discuss the \$924 million in discrepancies that was cited in the Controller's report. He stated that the process leading up to the issuance of the CAFR involves collaboration with the Controller's Office and that the errors prior to its issuance did not affect the General Fund Balance – of the \$924 million in errors, only \$45 million effected the financial statement fund balances in the Aviation, Water, Grants, and Capital funds. He stated the City is engaging an outside firm to help compile the FY2018 CAFR, and will also go through an additional level of review next year of its financial statements before providing them to the Controller. Mr. Kessler asked whether it would be appropriate to have one of the big four accounting firms to conduct this work, rather than the currently selected firm. Ms. Paster replied that the City went through the RFP process and that the Water Department had used this firm in the past. Mr. Rice added that the currently selected firm does municipal audits.

Mr. Kessler asked whether \$900 million discrepancies amounted to a typical level of mistakes for the City. Mr. Dubow said the amount was over \$1 billion last year. He added that \$296 million of this error was due to a budget to actual conversion which did not affect the fund balance.

Presentation by City Controller Rhynhart

Ms. Rhynhart had provided the Board with a two page fact sheet regarding the accounting issues. She stated she wanted to present to the Board to ensure they had all the facts before them. She explained the City Controller issues an annual audit and a related report on internal controls, which is submitted to the federal government for grant money, among other things. She explained there are two types of deficiencies in audits – material weaknesses and significant deficiencies. Material weaknesses occur when a combination of deficiencies serve to increase the risk that errors will be missed in the financial statements. In the private sector, such deficiencies must be cured within one year and are considered very significant. She stated that the City's material weaknesses and significant deficiencies have been present for a long time and that Philadelphia has the worst track record for deficiencies of the top 10 cities, having 8 significant deficiencies and 2 material weaknesses, while other top 10 cities have zero.

Ms. Rhynhart explained low staffing, lack of technology, and insufficient oversight contributed to the \$924 in discrepancies in the financial statements submitted by the City to the Controller's Office. She clarified that the financial statements should be generally accurate when submitted to the Controller, and that their level of inaccuracy reflects a lack of quality controls of accounting practices in the Finance Department. She also referenced a 27 percent reduction in staffing levels.

Ms. Rhynhart acknowledged that most of the errors were rectified and that the Controller's Office issued a clean opinion as a result. However, she explained that the deficiencies point to a heightened risk that the Controller might not be able to issue a clean opinion in the future. She clarified that the deficiencies are longstanding for many years, that they are not uncommon, but that they need to be fixed. She also acknowledged that the plan addressing one of the material weaknesses is detailed and with adequate deadlines, but that this needs to be done for the remaining material weakness and 8 significant deficiencies.

Mr. Rice asked Ms. Rhynhart whether there is a difference between audits conducted for top 10 cities using outside firms versus inside auditors. Ms. Rhynhart explained that there may be a difference in process but that the auditing standards are the same. Mr. Dubow echoed that all of the top 10 cities use outside firms. Mr. Cawley asked Mr. Rice what his underlying suggestion is in asking the question about outside versus inside audits. Mr. Rice elaborated that outside firms "work with the auditee" during the process. He went on to state that PICA uses an outside firm and when questions arise during an audit, if PICA staff produces the appropriate documentation during that process, those items "do not become findings" in the auditor's report. Ms. Rhynhart explained that in her experience and through conversations with the big 4 auditing firms, "the expectation is that the financial statements are much more accurate" when submitted for an audit, whether with an inside or an outside auditor. She stated the goal ought to be to fix and prevent future errors.

Mr. Kessler asked Ms. Rhynhart what the solution to these accounting problems would be, and she reiterated that there needs to be a detailed plan with deadlines regarding all weaknesses and deficiencies, instead of infighting. Mr. Kessler added that everyone is on the same team, and that with two negative outlooks issued by credit rating agencies recently, "all interested parties should work together and not make this something it should not be." Mr. Cawley closed the discussion by stating that these accounting errors are "just bad because they further erode the public's confidence. If we want to change perceptions of public service, we need to make sure these things do not happen in the future."

Public Comment

None.

Adjournment/Recess

Mr. Cawley made a motion to adjourn. Mr. Kessler seconded the motion. The motion passed 5-0.