



The Office of Internal Performance Audit

Internal Audit Report

PPS Automated Clearing House (ACH) Payment Method Audit

January, 2021

**Internal Performance Audit Report
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Table of Contents

Letter of Transmittal3 - 4
ACH Payment Method Audit Report5 - 6
Appendix A – Memo to the Audit Committee7 - 9

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**Internal Performance Audit Report
ACH Audit
PPS Automated Clearing House (ACH) Payment Method Audit**

Letter of Transmittal

January 13, 2021

Portland Public Schools
Audit Committee
501 North Dixon Street
Portland, OR 97227

At the October 9, 2019 meeting of the Audit Committee, Deputy Superintendent Claire Hertz requested the Audit Committee to add the Automated Clearing House (ACH) Payment Method Audit to the 2019-20 Audit Plan. The Audit Committee reviewed, supported the addition to the Audit Plan, and recommended the addition of the ACH Payment Method Audit to the Board of Education for approval. The Board of Education approved this addition on October 29, 2019, via Resolution No. 5988.

The objective of the ACH Payment Method Audit was to determine whether internal controls over the District's ACH payment process, follow best practices in design, and are working efficiently and effectively to mitigate potential fraud and safeguard District funds.

On Friday, August 16, 2019, Portland Public Schools (the District) experienced a fraudulent transaction attempt through its ACH payment method in the amount of approximately \$2.9 million in District funds. The Portland Police, the FBI, and PPS' partners at its banking institution quickly responded and recovered all District funds.

Due to the fraudulent transaction attempt, the District suspended enrolling new vendors in the ACH payment program. The District also suspended making changes in vendor payment account information that participate in the ACH payment program. And, if a change to the vendor account information was requested, the District removed the vendor from the ACH payment program and made subsequent payments to the vendor via check until further notice.

As of the end of our field work (November 2020), the District has not restarted its ACH payment program. As a result, we reviewed internal controls related to the setup of new vendors to the ACH payment program and account information changes for vendors who are enrolled in the ACH payment program; however, testing of these controls was not performed.

The Office of Internal Performance Audit has completed the ACH Payment Method Audit. Based on the results of work performed within the scope of the audit, it is our opinion that, overall, the internal controls over the District's ACH payment program follow best practices in design, and are working efficiently and effectively to mitigate potential fraud and safeguard District funds. Minor items that were not of a magnitude to warrant inclusion in the report were discussed verbally with management.



**Internal Performance Audit Report
ACH Audit
PPS Automated Clearing House (ACH) Payment Method Audit**

Auditing standards require that we obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings, if applicable, and conclusions based on our audit objective.

We extend our appreciation to the staff within Finance Department and the Office of Information Technology for their assistance and cooperation during the course of the audit.

We look forward to discussing the report with you at an upcoming Audit Committee meeting. Thank you for your ongoing support of the Office of Internal Performance Auditing.

Janise Hansen, CIA
Senior Internal Performance Auditor

Mary Catherine Moore
Internal Performance Auditor

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**Internal Performance Audit Report
ACH Audit
PPS Automated Clearing House (ACH) Payment Method Audit**

ACH Payment Method Audit Report

Background Information

The Automated Clearing House (ACH) Network is an electronic funds transfer process between bank accounts. The ACH Network essentially acts as a financial hub and helps people and organizations move money from one bank account to another. ACH transactions consist of direct deposits and direct payments.

The District utilizes the ACH Network to process approximately \$269 million and \$353 million in payments for the 2018-19 and 2019-20 fiscal years respectively.

In August of 2019, the District experienced a fraudulent transaction attempt through its ACH payment method in the amount of approximately \$2.9 million in District funds. In a memo to the Audit Committee, the District detailed actions taken, to address the fraudulent transaction attempt. The full memo is included in Appendix A. Below is a list of some of the actions taken by the District's Finance Department:

- Immediately stopped all ACH payments and verified the accuracy on all accounts that were scheduled to be paid on the week of August 19, 2019 and verified the accuracy on all accounts scheduled for payment this week and any ACH change requests submitted in the past six months.
- Finance Department reviewed existing protocols and procedures related to the process for paying suppliers via ACH and updated their internal controls and approval levels.
- Updated the staff training materials and conducted a mandatory training on Fraud Awareness.
- Removed the ACH Enrollment form from the District's website.

Additionally, Deputy Superintendent Claire Hertz requested the District's Office of Internal Performance Audit perform the ACH Payment Method Audit. The Audit Committee reviewed and supported the addition of the ACH Audit to the District's Office of Internal Performance Audit, and agreed to present it to the Board of Education for approval. The Board of Education approved this addition on October 29, 2019, Resolution No. 5988.

Roles and Responsibilities

District Accounts Payable management has the primary responsibility to establish, implement, and monitor internal controls. Internal Audit's function is to assess and test those controls in order to provide reasonable assurance that the controls are adequate and operating effectively. We conducted this performance audit in accordance with Generally Accepted Government Auditing Standards (GAGAS, aka Yellow Book). 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 objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

Audit Objective(s)

The objective of the ACH Payment Method Audit was to determine whether internal controls over the District's ACH payment process, follow best practices in design, and are working efficiently and effectively to mitigate potential fraud and safeguard District funds.



Internal Performance Audit Report
ACH Audit
PPS Automated Clearing House (ACH) Payment Method Audit

Scope of the Audit

ACH payments made in January 2020 and vendor information changes from January 2020 through May 2020.

Audit Approach and Methodology

To achieve the audit objectives, we performed the following procedures:

- Planned the audit in cooperation with the Finance Department to ensure that we had an understanding of the District's accounts payable processes, policies and procedures.
- Reviewed processes/actions taken by the District (as detailed in the memo to the Audit Committee – see Appendix A) after the attempted ACH fraudulent activity in August 2019.
- Reviewed the reports issued by a global cyber security consultant contracted by the District to perform an investigation after the attempted ACH fraudulent activity.
- Reviewed any internal investigations that were performed.
- Inquired with PPS' Office of Technology and Information Services (OTIS) to determine if any security improvements were implemented or tested to prevent future malicious attempts.
- Analyzed available data to corroborate the information obtained during our walkthroughs.
- Reviewed applicable PPS Accounts Payable Internal Control Narrative and PPS Purchases and Accounts Payable Policy and Procedure.
- Drew on criteria from suggestions made by the District's financial institution.
- Gathered information on ACH payment processing best practices and how to combat fraud from external sources.
- Verified that all Finance staff members completed the mandatory Fraud Awareness training.
- Reviewed segregation of duties in the Finance Department.
- Reviewed appropriateness of Finance staff's access to the District's financial system.
- Utilized a sampling methodology with 95 percent confidence level to select 42 ACH transactions that occurred in January 2020 for testing of ACH payment transactions, and 20 vendor information changes from January 2020 through May 2020.
- Performed tests and analysis of the objective areas to support our conclusions.

Conclusion

Based on the results of the audit, overall we found the District's internal controls over ACH payments follow best practices in design and appear to be working efficiently and effectively to mitigate potential fraud and safeguard District funds. Testing of the District's internal controls for setting up new vendors to the ACH payment program and updating ACH payment information was not completed. When the District has resumed the process for setting up new and updated ACH payments, the Office of Internal Performance Audit will test these internal controls and issue an updated audit report.



Internal Performance Audit Report
ACH Audit
PPS Automated Clearing House (ACH) Payment Method Audit

Appendix A: Memo to the Audit Committee



PORTLAND PUBLIC SCHOOLS
OFFICE OF DEPUTY SUPERINTENDENT
Business and Operations
501 North Dixon Street / Portland, OR 97227
Telephone: (503) 916-3380 / Fax: (503) 916-

Date: August 23, 2019
To: Audit Committee Members
From: Deputy Superintendent, Claire Hertz
Subject: Update on recent fraudulent ACH transaction

This is an update regarding the recent fraudulent ACH transaction that occurred last Friday at PPS. Some of you may have spoken directly with the staff regarding this over the past week. The most important news to note - we received all funds back into our account on Tuesday morning thanks to a lot of support from FBI investigators and the two banking institutions involved in the transaction. Below is a list of actions that we have taken and/or are in progress.

You will also see a message from the Superintendent that we sent out to staff and school communities that was translated into our key languages for families.

Please do not hesitate to reach out to me if you have any questions.

ACTIONS TAKEN/IN PROGRESS/PLANNED:

Finance Department:

- Immediately stopped all ACH payments scheduled to be paid on August 19 and verified the accuracy on all accounts scheduled for payment this week and any ACH change orders submitted in the past six months
- Reviewed existing protocols and procedures related to the process for paying vendors via ACH and added additional internal controls and approval levels
- Updated staff training materials and conducted mandatory training for all finance department staff on Tuesday, Aug. 20
- All new finance staff will be required to complete fraud prevention training before accessing the district's finance information system
- Requested PPS auditors of record, TKW, to immediately launch an investigation of all vendor payment processes, protocols and internal controls; TKW meeting occurred on August 19 to begin this work
- District finance department leaders met with top Wells Fargo executive on Monday to review event and update incident and contact information
- Conferred with Carol Samuels, PPS bond financial advisor, on Monday to confirm disclosure to bondholders is not necessary



Internal Performance Audit Report
ACH Audit
PPS Automated Clearing House (ACH) Payment Method Audit

- Removed contracts from our website and will allow access to PPS contract information through our public records request process Removed ACH Enrollment form from district website - vendors will need to request form from finance staff, which will include a verification process confirmed with vendor information already on file with the district

Human Resources:

- Worked in conjunction with IT and Security Services to suspend two employees' access to all PPS systems and buildings August 19
- Both employees placed on paid administrative leave pending investigation
- Providing support to Legal and external investigator on workplace investigation

Law Enforcement/Security:

- Immediately contacted Portland Police Bureau
- Filed Internet Fraud Claim paperwork with FBI
- FBI recovered all funds from fraud incident
- PPS Security Services continues to assist and support law enforcement investigations and inquiries

Legal and Risk Management:

- Consulted outside legal counsel to, among other things, establish priority, direct line of communication with FBI
- Filed claims under relevant district's insurance policy to pay for breach response investigation; assessing whether current coverage limits are sufficient Secured consultant to perform security breach investigation and workplace misconduct investigation
- Along with Finance and IT teams, interfacing with FBI to provide information for criminal investigation

Office of Technology and Information Systems:

- Immediately disabled two employees' email and online access to all PPS systems
- Lead contact on security breach investigation and system assessment

Other notes:

- PPS has secured three external investigations regarding the incident:
 - Forensic cybersecurity review
 - Financial systems and control
 - Workplace process and employee conduct



**Internal Performance Audit Report
ACH Audit
PPS Automated Clearing House (ACH) Payment Method Audit**

SUPERINTENDENT'S MESSAGE TO STAFF AND SCHOOL COMMUNITIES

Dear PPS Staff and School Communities,

We want to let you know that Portland Public Schools has been working since Friday with law enforcement and financial institutions in response to a banking crime involving the district. Fortunately, we have confirmed that the banking institutions involved have frozen the approximately \$2.9 million in district funds that were transferred to a fraudulent account disguised as the account of a legitimate PPS construction contractor. PPS has already begun the process to recover and fully return the funds back to the district, likely within the next several days.

Once we were made aware of this fraudulent transaction on Friday, we immediately notified law enforcement, including the FBI and Portland Police Bureau, as well as the Board of Education. We also began an internal investigation to determine the origin of this transaction and how and why the transaction was processed by PPS.

Following standard procedure, two district employees involved with processing the transaction were placed on paid administrative leave, pending a full investigation. Initial information indicates that the fraud was perpetrated externally and no district employee engaged in criminal activity; however, the district is implementing best practices to investigate this case thoroughly.

All district payment procedures and internal controls are being reviewed, additional protocols and actions have already been identified, and all district finance staff will receive mandatory, updated training this week to reinforce protocols and to ensure updated procedures are in place to prevent incidents like this from occurring. We have conducted an initial review of previous transactions, as well as a review of vendor account management and fund transfer protocols. In addition, we have updated our fraud awareness training materials.

All of this is being followed by a full, independent, external investigation involving outside experts from the fields of online security, financial processes and controls, and workplace fraud. Additionally, the district's external auditor will independently review our financial controls and vendor management protocols.

We are treating this incident with the utmost seriousness. We will continue to cooperate fully with law enforcement to protect school district funds and to apprehend the perpetrators. We thank Portland Police, the FBI, and our partners at Wells Fargo for their quick response and assistance they have extended to PPS over the last four days. Unfortunately, school districts and educational entities around the country have increasingly become targets of financial fraud and cyber security threats. We will use this instance to further strengthen our financial controls and plan to share our experience with other school districts.

Sincerely,

Guadalupe Guerrero
Superintendent

