



**SUBJECT: Fraudulent Vendor Payment Update**

**TO: Audit Committee**

**FROM: Legal Department**

Report Number: L-20-19

Wards Affected: Not Applicable

File Numbers: 155-03-16

Date to Committee: September 11, 2019

Date to Council: September 23, 2019

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**Closed Session:**

Subject matter relates to the following provision under the Municipal Act:

"the security of the property of the municipality or local board" – Confidential Appendices A & B

"litigation or potential litigation, including matters before administrative tribunals, affecting the municipality or local board" - Confidential Appendix A

"advice that is subject to solicitor-client privilege, including communications necessary for that purpose" - Questions Committee may have of external legal counsel dealing with the civil proceedings taken/to be taken to recover the funds or the on-going insurance claims.

**Recommendation:**

Receive and file legal department report L-20-19 Fraudulent Vendor payment update.

**Purpose:**

An Engaging City

- Good Governance
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## **Background and Discussion:**

On May 27, 2019, senior management verbally advised Council the City was the victim of a fraudulent vendor payment scheme. Subsequently, on June 5, 2019, senior management verbally advised the Audit Committee of the incident and committed to reporting back to both the Audit Committee and Council in September.

In a media release on June 13, 2019, the City disclosed it had discovered it was a victim of fraud on May 23, 2019. A single transaction was made to a falsified bank account because of a complex phishing email to City staff requesting to change banking information for an established City vendor. The transaction was in the form of an electronic transfer of funds made to the vendor in the amount of approximately \$503,000 and was processed on May 16, 2019.

## **Strategy/Process**

Upon learning of the fraudulent payment, the City took immediate steps of:

- reporting the unauthorized payment to our financial institution;
- filing a police report with the Halton Regional Police Service (HRPS);
- notifying our insurers;
- initiating an independent external investigation.

Since identifying and reporting the incident, the HRPS are pursuing their criminal investigation, the City continues to work with its insurer to determine claim coverage, and the City has commenced legal action to obtain information to aid in the recovery of funds.

## ***Independent Investigation***

The City engaged Haywood Hunt & Associates Inc. as a fully independent and objective resource to conduct the external investigation. Their investigator interviewed City staff and vendor staff; all of whom have been fully cooperative. Their investigator also connected with HRPS. The results of the internal investigation outline the scheme and how it was perpetrated; detailed information is contained in confidential Appendix A.

## ***The Scheme***

The scheme, perpetrated entirely through email, involved a person posing as an employee of a vendor performing work for the City and requesting changes to the vendor's banking information. The sophistication of the scheme is marked by the

establishment of web domains with close likeness to the vendor's real name and the City's accounts payable unit. The emails initiated by the perpetrator included the use of the real vendor's logo and address information, as well as the City's logo and accounts payable contact information. The purpose of the emails was to deceive the recipients, making them believe the email was from the vendor and the City. Once contact with the City was established, several emails were exchanged by the perpetrator; all with the intent of deceiving the City. This set of circumstances is consistent with a "Phishing Scheme" where an individual with malicious intentions attempts to obtain sensitive information by deceptive means such as representing a legitimate person or entity. The individual then uses the sensitive information to achieve a goal which in this instance was to obtain funds from the City.

### ***Vendor Impact***

The City has honoured its payment commitment to the vendor.

### ***Internal Operations***

In this case, the criminals used social engineering, knowledge of City processes, as well as an apparent understanding of municipal payment systems, to facilitate the fraud. Internally, management has identified and implemented additional internal controls to minimize the opportunity for re-occurrence. Key among these controls is a heightened awareness campaign as these types of targeted attacks are all too common and can take many forms affecting governments, businesses, and individuals. Details of control enhancements are contained in confidential Appendix B.

### ***Recovery***

The City is working through its insurers and the legal system to effect recovery of funds.

Civil litigation is underway to effect recovery of bank account holdings. A Statement of Claim was commenced in the Superior Court of Justice to freeze the bank account and related bank accounts into which the City funds were deposited or subsequently transferred to, and for production of documents and information from the Royal Bank. An order of the court was obtained effecting the relief sought. The City will be pursuing additional legal proceedings in order to recover the funds. The City is represented in the civil proceedings by Mr. James Riewald of Gowlings WLG (Canada) LLP who will be in attendance to answer any questions in this respect that members of Committee may

have. Because the legal proceedings are on-going, these questions will have to be responded to during the in-camera portion of the meeting.

From an insurance perspective, the City immediately put its insurer Jardine Lloyd Thompson Canada Inc. on notice of the loss. The City does have policies of insurance both for crime (Aviva) and cyber (CFC) loss. The adjusters for the insurers are doing their due diligence in investigating the incident. At the time of preparing this report, a determination has not been made with respect to coverage for the City's loss.

### **Financial Matters:**

As stated, the fraudulent vendor payment was approximately \$503,000.

The total financial impact of the incident cannot be determined until the outcome of the insurance claim and recovery of funds process is complete.

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### **Connections:**

N/A

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### **Public Engagement Matters:**

N/A

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### **Conclusion:**

This incident was the result of online fraud with falsified documents at a level of sophistication not typically seen. The City is confident it has internal controls in place to minimize the opportunity for this type of fraud to occur. These types of targeted attacks are all too common and can take many forms against governments, businesses, and individuals.

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Respectfully submitted,

Nancy Shea Nicol

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**Appendices:**

- a. Confidential: L-20-19 Appendix A – Final Investigation Report (Haywood Hunt & Associates Inc.)
- b. Confidential: L-20-19 Appendix B – Internal Controls Update

**Approved by:**

N/A

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Department Head      Director of Finance      City Solicitor      City Manager

**Distribution Information:**

No distribution of this confidential information those with a pecuniary interest

- Not Applicable
- Applicable (specify names)

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- City Manager       City Clerk       City Solicitor and Director of Legal
- Director of Finance       City Auditor       Mayor’s Chief of Staff
- Mayor and Members of Council

**Disposition and Comments:** (completed by the Clerks Department)

Committee:

01-Approved 02-Not Approved 03-Amended 04-Referred 05-Received & Filed  
06-Withdrawn

Council:

01-Approved 02-Not Approved 03-Amended 04-Referred 05-Received & Filed  
06-Withdrawn