

STATE OF DELAWARE

OFFICE OF AUDITOR OF ACCOUNTS

TOWN OF KENTON

MISAPPROPRIATION OF TOWN FUNDS

SPECIAL INVESTIGATION

FIELDWORK END DATE: AUGUST 26, 2010

ISSUANCE DATE: SEPTEMBER 13, 2010

REISSUANCE DATE: NOVEMBER 5, 2010¹

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¹ Report was revised to include the Town's response to the findings and recommendations.



State of Delaware
Office of Auditor of Accounts
R. Thomas Wagner, Jr. – CFE, CGFM, CICA
At a Glance

Working Hard to Protect YOUR Tax Dollars

Why We Did This Review

The Office of Auditor of Accounts (AOA) received a hotline allegation regarding the Town of Kenton from members of the current Town Council: *"The former Treasurer of the Town of Kenton is alleged to have stolen approximately \$100,000. She was removed from the position by unanimous council vote in April 2010."*

Background

The Town of Kenton is located in Kent County, Delaware, and is part of the Dover Metropolitan Statistical Area. A Town Council governs the town and is composed of five members, all of whom are elected at large by the citizens of the Town of Kenton. The positions of Mayor, Vice Mayor, and Secretary are then filled from the elected Council members by Council vote. The Treasurer, per Town Charter, is also to be elected by the citizens of the Town of Kenton. The population as of the 2000 census was 237.

Town of Kenton, Misappropriation of Town Funds

What We Found

After review of the Town's records, the AOA has determined that the former Treasurer, who is also the former Mayor's wife, misappropriated funds in the amount of \$198,013. (Note: Amount is subject to change pending further investigation.) In addition, evidence obtained indicates the former Treasurer allegedly fabricated and forged documents in order to grant herself the authority to sell an easement owned by the Town for net proceeds of \$134,116.40. Of this amount, \$77,000 was used to replenish the Town's bank accounts (\$50,000 to the General fund and \$27,000 to the Municipal Street Aid fund). The remaining funds that were misappropriated included \$15,427.86 for restitution payments resulting from the former Treasurer's prior felony theft convictions.

We have concluded that there was a lack of segregation of duties with the Treasurer's position and a lack of oversight by the previous Town Council regarding the financial management of Town funds. Furthermore, the loss to the Town of Kenton could have been mitigated if the Town Council had required the Treasurer to be bonded, as is required by the Town of Kenton Charter.

What We Recommend

The potential criminal matters uncovered have been referred to the State of Delaware Office of the Attorney General. The Town of Kenton Town Council should immediately develop written internal control policies that describe the specific responsibilities of the Treasurer and of the Town Council; this should include proper segregation of duties for both the Town Council and the Treasurer. As a condition of the appointment of the next Town Treasurer, we recommend that the Town Council ensure that the Treasurer be bonded in the amount that is acceptable to the Town Council as required by the Town of Kenton Charter.

Please read the complete report for a full list of findings/recommendations.

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AUDIT AUTHORITY

Title 29, Del. C. c. 29 authorizes the Auditor of Accounts to file written reports containing:

1. Whether all expenditures have been for the purpose authorized in the appropriations;
2. Whether all receipts have been accounted for and paid into the State Treasury as required by law;
3. All illegal and un-businesslike practices;
4. Recommendations for greater simplicity, accuracy, efficiency, and economy; and
5. Such data, information, and recommendations as the Auditor of Accounts may deem advisable and necessary.

ALLEGATION AND BACKGROUND

ALLEGATION

The Office of Auditor of Accounts (AOA) received the following hotline allegation regarding the Town of Kenton from members of the current Town Council: *"The former Treasurer of the Town of Kenton is alleged to have stolen approximately \$100,000. She was removed from the position by unanimous Council vote just before Easter. She is the Mayor's wife and has also forged his signature on 2 checks to herself. At first, the checkbooks were not turned over because she said the bank had them for an audit. When the signature cards for the accounts were changed, the bank pointed out another account existed with an \$8 balance. This was the Town's Activities Account, which should have been closed (NOTE: The complainant provided account statements for the Activities Account for the period from January through April 2010). In January, the Town received a wire deposit in this account from an unknown source for approximately \$134,000. \$50,000 was transferred to the general checking account and the former Treasurer spent the rest through April."*

BACKGROUND

The Town of Kenton is located in Kent County, Delaware and is part of the Dover Metropolitan Statistical Area. The population as of the 2000 census was 237. A Town Council governs the town and is composed of five members, which are elected at large by the citizens of the Town of Kenton and are not compensated. The positions of Mayor, Vice Mayor, and Secretary are then filled from the elected Council members by Council vote. The Treasurer, per Town Charter, is also to be elected by the citizens of the Town of Kenton. The following are excerpts from the Town Charter:

- The Mayor presides at all meetings of Council; serves as the head of the Town government for all ceremonial purposes, appoints all committees, subject to Council confirmation, receives complaints of nuisances and all complaints of violations of law or ordinances and presents those complaints to the Council for appropriate action by the Council. The Mayor also signs any warrants on the Treasury for the payment of any Town money.
- The Vice-Mayor, during the temporary absence or inability of the Mayor, acts as the Mayor, and while so acting is vested with all the powers, duties, and authority of the Mayor.
- The Secretary shall keep a true and faithful record of all the proceedings of Council at all meetings and to do and perform such other matters and things as may be prescribed by this Act, or law or which Council may from time to time prescribe by resolution and ordinance.
- The Town Treasurer, to be elected, shall be nominated in the same manner and be elected by the same qualified voters, at the same Town elections and by the same regulations as the nomination and election of members of Council. The Treasurer is responsible for the collection of Town taxes and other revenue accruing to the Town and payment of all orders drawn on him by order of the Council and signed by the Mayor and Secretary. The term of the Town Treasurer is two years from the day following his election, or until his successor has been duly elected and qualified. The Town Treasurer is sworn or affirmed to faithfully and honestly perform the duties of his office by any member of the Council, Mayor, or Vice-Mayor. The Town Treasurer is to be bonded by the Town with sufficient surety to be approved by Council, in the sum as determined by Council, conditioned on the faithful discharge of the duties of his office and for the payment to his successors in office all sums of money belonging to the Town.

ALLEGATION AND BACKGROUND

- Use Of Town Money: Town funds are to be used at the discretion of the Town Council for the improvement, benefit, protection, ornament and best interests of the Town, as Council may deem proper, and to use Town money to accomplish and carry into effect all acts and things which it has power to do by virtue of the Laws of Delaware, this Act and all lawful ordinances and resolutions of Council.

An audit was previously conducted by the AOA in November 2007 relating to the Municipal Street Aid (MSA) fund. The following findings were noted:

- The Treasurer was not bonded.
- Real estate bills were not prepared for 2005, 2006, and 2007, resulting in lost income of approximately \$11,500.
- Deposits totaling \$103,422.76 were not made timely. Some checks were held as long as five months before being deposited. This decreased the amount of interest income that could have been earned.
- Bills totaling \$59,738.11 were not paid timely, resulting in late fees of \$309.14.
- The Town did not maintain support for transactions totaling \$11,020.42.
- The Town did not update the authorized signer list when a Council member resigned.
- Municipal Street Aid reports were incorrect.
- Bank reconciliations were not prepared.
- The Town does not have written policies and procedures.

OBJECTIVE, SCOPE, AND METHODOLOGY

OBJECTIVE

The objective of the investigation was to determine if any funds were misappropriated and the extent (dollar amount) of the misappropriation. AOA will assist the Office of the Attorney General in their investigation if this matter is referred for prosecution.

SCOPE

The scope of the investigation is July 1, 2008 through April 30, 2010. The investigation was performed in accordance with the President's Council on Integrity and Efficiency, Quality Standards for Investigations.

METHODOLOGY

The investigation approach includes:

- Inquiry of Town Officials
- Review of source documentation (including bank records)
- Assistance from Office of the Attorney General to determine the existence of additional bank and credit card accounts

The conclusion of the allegation(s) is defined as follows:

Substantiated:	The allegation has been verified by competent evidence.
Partially Substantiated:	A portion of the allegation has been verified by competent evidence; however, competent evidence to verify the entire allegation could not be provided by the agency or obtained by AOA.
Unsubstantiated:	Competent evidence was found to dispute the allegation.
Unable to Conclude:	Competent evidence to verify the allegation could not be provided by the agency or obtained by AOA.

CONCLUSIONS

OBJECTIVE

Determine if any funds were misappropriated and the extent (dollar amount) of the misappropriation.

Results of Testing

After review of the Town's records, the AOA has determined that the former Treasurer, who is also the former Mayor's wife, misappropriated funds in the amount of \$198,013. (Note: Amount is subject to change pending further investigation.) In addition, evidence obtained indicates the former Treasurer allegedly fabricated and forged documents granting her authority to sell an easement owned by the Town for net proceeds of \$134,116.40. Of this amount, \$77,000 was used to replenish the Town's bank accounts (\$50,000 to the General fund and \$27,000 to the Municipal Street Aid fund). The remaining funds that were misappropriated included \$15,427.86 for restitution payments resulting from the former Treasurer's prior felony theft convictions.

Misappropriation of Town Funds

As of the issuance date of this report, the AOA found that transactions totaling \$198,013 were misappropriated and did not have proper authorization from the Town Council, did not benefit the Town of Kenton, and did not have proper supporting documentation. This amount includes \$188,933 that was misappropriated from the bank accounts in the name of the Town of Kenton, \$2,700 of un-deposited revenue including rental income and income from Town events, and \$6,380 in outstanding credit card balances that were opened in the name of the Town of Kenton without approval or knowledge of the Town Council. *Exhibit 1* below shows the major categories of expenditures that were misappropriated by the former Treasurer during her appointment as Treasurer.

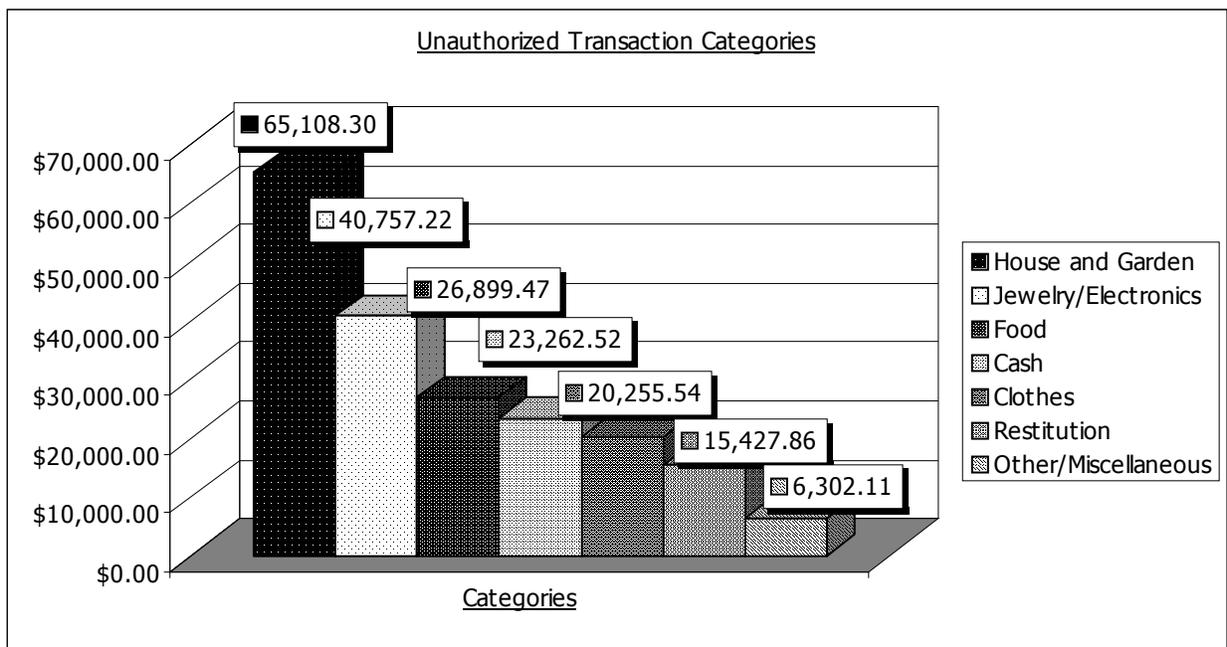


Exhibit 1

CONCLUSIONS

Restitution for Previous Convictions Paid with Town Funds

According to information provided by the Office of the Attorney General, the former Treasurer for the Town of Kenton has a criminal record consisting of 44 felony charges, 12 felony convictions, 62 misdemeanor charges, and 3 misdemeanor convictions, which resulted in Court ordered restitution payments and wage garnishment. The convictions include unlawful use of credit cards, forgery, and identity theft of someone 62 years or older. After failure to pay those obligations, she was issued a subpoena from the New Castle County Superior Court in January 2010 for a Contempt of Court hearing for non-payment. On February 1, 2010, the former Treasurer called the Office of State Court Collections Enforcement and paid four separate payments by phone using the Town of Kenton's bank account totaling \$15,427.86. The Town Council had no knowledge of these transactions and did not authorize them nor would they have authorized them if they had been properly presented for approval. This amount is shown in *Exhibit 1*.

Theft of Town Asset

Through our review of the bank account statements, we noted a deposit on January 26, 2010, in the amount of \$134,116.40 from an unknown source. The AOA investigated this transaction to determine what transpired. From documentation provided by the current Town Council of the Town of Kenton, the AOA found that the former Treasurer appears to have used her position to fraudulently sell an easement owned by the Town of Kenton without the Town Council's approval or knowledge. The Town of Kenton owns a parcel of land where a wireless communications tower (cell tower) is constructed. In exchange for using the land for the tower, the tower owner agreed to pay the Town of Kenton \$1,650 per month indefinitely. In June 2008, a different company made an offer to the Town to purchase a 30-year easement for the property for \$187,000. The Town discussed and rejected this offer as noted in the August 2008 Council minutes. In January 2010, evidence obtained indicates the former Treasurer appears to have fabricated two sets of Town Council meeting minutes: (1) stating she was the "Town Manager" and had authority to sell the easement and (2) that the sale of the easement, with a price of \$143,550, was approved by a unanimous vote of the Town Council on December 23, 2009. The alleged fabricated and forged meeting minutes were submitted to the buyer of the easement and the sale was approved. The settlement documents, dated January 22, 2010, bore the signature of the previous Treasurer and included the false title of "Town Manager." As a result of the sale, the Town received a net lump sum payment of \$134,116.40 on January 26, 2010, and the buyer of the easement now receives the monthly payment of \$1,650 and has control over the property for future rent negotiations. The AOA confirmed that no authorization was given to the former Treasurer for the sale of the easement and that the Council minutes given to the buyer of the easement contained the forged signature of one of the Council members. Since this agreement is perpetual with no stated term, the loss to the Town increases each month they do not receive the lease payments from the tower owner.

CONCLUSIONS

Timeline of Events

Date	Event
May 24, 2008	The bank reported that the former Mayor and the former Treasurer became signatories on the Activities Account owned by the Town of Kenton.
May 28, 2008	The first unauthorized check cleared the bank.
May 30, 2008	Ending balance for the General Fund was \$12,500.98, Activities Account \$6,516.61, Municipal Street Aid \$15,140.09, and Money Market Fund \$78,964.49. Total for all accounts: \$113,122.17.
June 2, 2008	The Mayor reported to the Council in the Town Council meeting that the Activities Account was to be closed. However, the account was not closed and unauthorized transactions continued through April 2010.
September 8, 2008	The previous Treasurer was appointed into her position for the Town of Kenton via a vote of the Town Council. The vote to appoint her as Treasurer was unanimously approved by the members of the Town Council, which included her husband who was Mayor at the time of her appointment and fully aware of her prior felony convictions.
November 24, 2008	A debit card is issued to the former Treasurer for the Activities Account.
December 1, 2008	The former Treasurer began using the debit card for unauthorized transactions with total spending over \$1,000 on this date. A total of 114 debit card transactions were made in the month of December.
December 31, 2009	Ending Balance for the General Fund was \$67.66, Activities Account, \$75.16, Municipal Street Aid \$2,421.98, and Money Market fund \$0. Total for all accounts: \$2,564.80. Since the Treasurer had exhausted the Town's cash reserves, the fraudulent activity stopped until after settlement of the sale of the easement.
January 22, 2010	The former Treasurer signs settlement documents finalizing the sale of the Town's cell tower easement. The former Treasurer presented alleged fabricated and forged documents that indicated her appointment to the position of "Town Manager" and authorized her to make the sale.
January 26, 2010	A wire deposit for \$134,116.40 was made into the Activities Account for the sale proceeds of the cell tower easement. \$50,000 was then transferred to the General Fund.
January 29, 2010	A check was written for \$27,000 from the Activities Account and deposited in the Municipal Street Aid account. Unauthorized transactions also resumed on this date.
February 1, 2010	The former Treasurer made four unauthorized transactions totaling \$15,427.86 to the Delaware Office of State Court Collections for payment of restitution resulting from her previous felony convictions of forgery and theft. The former Treasurer also spent over \$7,500 at various retailers on this date.
April 6, 2010	Town Council removes the former Treasurer from her position as Town Treasurer.
April 30, 2010	Ending Balance for the General Fund was \$51,876.66, Activities Account \$0, Municipal Street Aid \$24,802.36, and Money Market fund \$13.44. Total for all accounts: \$76,692.46.

CONCLUSIONS

The above issues that are considered criminal in nature have been referred to the Office of the Attorney General for prosecution. The AOA will continue to work jointly with the Office of the Attorney General to help with the investigation.

Conclusion

The allegation is *substantiated*.

FINDINGS AND RECOMMENDATIONS

Finding #1 – Misappropriation of Town Funds, Alleged Fraudulent sale of a Town Asset, Restitution for prior convictions paid with Town funds

Criteria

The Town of Kenton Charter, Section 4, Organization of Council, (g) Powers of Council; Manner of Acting states the following: "All powers of the Town shall be vested in the Town Council, except as otherwise provided by law, and the Council shall provide for the exercise thereof and for performance of all duties and obligations imposed on the Town by law. All powers of Council, whether express or implied, shall be exercised in the manner provided by ordinance or resolution of Council." The Town of Kenton Charter, Section 10, Finances, (b) Use of Town Money also states "The Town Council of said Town shall have full power and authority to use the money in the Treasury of said Town, or any portion thereof, from time to time, for the improvement, benefit, protection, ornament and best interests of the said Town, as Council may deem proper, and to use Town money to accomplish and carry into effect all acts and things which it has power to do by virtue of the Laws of Delaware, this Act and all lawful ordinances and resolutions of Council."

Condition

The former Treasurer of the Town of Kenton, in her sworn position of Town Treasurer, used that position to make unauthorized purchases (via the Town owned bank accounts and through credit cards improperly opened by the previous Treasurer), write unauthorized checks and make unauthorized ATM withdrawals in the amount totaling \$198,013. Included in this amount is \$15,427.86 paid to the State of Delaware Office of State Courts Collections for restitution resulting from the former Treasurer's prior criminal convictions. The Town Council had no knowledge of these transactions and did not authorize them, nor would they have authorized them if they had been properly presented for approval. The previous Town Treasurer maliciously paid these items for her personal benefit thus resulting in likely theft of Town funds.

In addition, the former Treasurer of the Town of Kenton used her position to sell an asset owned by the Town of Kenton without the Town Council's knowledge or approval and allegedly forged the signature of a current member of the Town Council. As a result of the sale, the Town received a net lump sum payment of \$134,116.40 on January 26, 2010, and the buyer of the easement now receives the monthly payment of \$1,650 and has control over the property for future rent negotiations. From our review of the bank account detail, the former Treasurer then misappropriated the majority of the proceeds from the sale for her personal gain.

Cause

These fraudulent acts by the former Treasurer were caused by a lack of financial oversight by the previous Town of Kenton Town Council. The former Treasurer intentionally withheld bank account information from the Town Council in order to carry out these unauthorized transactions. She willfully used the Town's bank account to initiate personal transactions for her benefit, not for the benefit and best interests of the Town of Kenton.

FINDINGS AND RECOMMENDATIONS

Effect

The Town of Kenton has been deprived of \$198,013 and the monthly payment for the easement, which will have an impact on future cash flow. These assets could have been used to benefit the residents of the Town of Kenton.

Recommendation

This matter has been referred to the State of Delaware Office of the Attorney General.

Finding #2 – Segregation of Duties, Lack of Oversight by the Town Council

Criteria

The Committee of Sponsoring Organizations of the Treadway Commission (COSO), Internal Control Integrated Framework, Chapter 4, Control Activities, Segregation of Duties states, "Duties are divided, or segregated, among different people to reduce the risk of error or inappropriate actions. For instance, responsibilities for authorizing transactions, recording them and handling the related asset are divided." The COSO, Internal Control Integrated Framework, Chapter 6, Monitoring states "Internal control systems need to be monitored—a process that assesses the quality of the system's performance over time. This is accomplished through ongoing monitoring activities, separate evaluations or a combination of the two. Ongoing monitoring occurs in the course of operations. It includes regular management and supervisory activities, and other actions personnel take in performing their duties. The scope and frequency of separate evaluations will depend primarily on an assessment of risks and the effectiveness of ongoing monitoring procedures. Internal control deficiencies should be reported upstream, with serious matters reported to top management and the board."

Condition

Through interviews with the Town of Kenton Town Council and a review of the Town Council Meeting Minutes, it was concluded that there was insufficient oversight by the previous Town Council and a lack of segregation of duties with regards to the activities of the former Treasurer.

Cause

The Town has insufficient written policies and procedures describing what the Treasurer's responsibilities are and how financial transactions are reported and approved by the Town Council. High turnover of Town Council members due to the volunteer nature of the positions and difficulty in getting new volunteers to serve on the Council are also factors.

Effect

The lack of oversight by the Town Council and the lack of segregation of duties for the Treasurer position contributed to the alleged acts of fraud that were perpetrated by the former Treasurer and led to Town assets being lost or misappropriated.

FINDINGS AND RECOMMENDATIONS

Recommendation

The Town of Kenton Town Council should immediately develop a written financial policy that discusses the duties of the Treasurer and the duties of the Town Council with regards to every type of financial transaction that the Town of Kenton enters into. This should include proper segregation of duties for both the Town Council and the Treasurer.

Finding #3– Treasurer not bonded

Criteria

Town of Kenton Town Charter, Section 5, Other Elected Officials, (a). Town Treasurer part (4) states, "The Town Treasurer, before entering upon the duties of his office, shall be bonded by the Town with sufficient surety to be approved by Council, in the sum as determined by Council, conditioned on the faithful discharge of the duties of his office and for the payment to his successors in office all sums of money belonging to said Town which may remain in his hands upon the settlement of his accounts to which bond and condition shall be annexed a warrant of attorney for the confession of judgment for said penalty." Delaware Code, Title 30, § 5165 (b) (1) states, "Each Municipality shall furnish evidence annually to the State Treasurer that the municipality employee authorized to expend municipal street aid funds are bonded in an amount as may be required by the charter of the municipality."

Condition

The former Treasurer of the Town of Kenton was never bonded as required by the Town of Kenton Charter. Also, a previous audit issued by the Office of the Auditor of Accounts dated November 6, 2007, recommended that the Treasurer be bonded per Delaware Code, Title 30, § 5165. Had the Town applied for bonding for the former Treasurer, the Town would have been notified of her prior felony convictions and, presumably, would not have appointed her to the position, which resulted in alleged fraud.

Cause

The Town of Kenton, Town Council did not act on the AOA's recommendation to have bonding in place for the Treasurer as recommended in our audit report dated November 26, 2007.

Effect

As a result, the Town of Kenton will not have the opportunity to make a claim against the bond, which would have mitigated the loss the Town has suffered as a result of the alleged fraud perpetrated by the previous Treasurer.

Recommendation

As a condition of the appointment of the next Town Treasurer, we recommend that the Town Council ensure that the Treasurer be bonded in the amount that is acceptable to the Town of Kenton Town Council as required by the Town of Kenton Charter.

FINDINGS AND RECOMMENDATIONS

Town of Kenton Response to Findings and Recommendations

We received the following response from the Town:

The Town of Kenton, in its ongoing pursuit to ensure its financial integrity going into the future, has put into place policies and procedures that will limit the Treasurer's control of money and hold the Treasurer accountable to the Mayor and the whole council. On August 14, 2010, the Treasurer and the Mayor were both bonded in the amount of \$25,000.00. Step two, the Treasurer has been removed as a signer on all accounts. The Mayor is the only signer on all accounts, and, as the charter instructs, the Treasurer will prepare the checks for the Mayor to sign. This should ensure that no one person is handling the finances for the Town. Step three, all debit cards have been destroyed.

All bills will be presented at monthly council meetings to be paid by motion of council, and all bank statements for the previous month's activity are to be presented with the financial report to verify what is on the financial report is on the bank statements, so the whole council is aware of the financial activity and approves of the activity. Both the financial report and the bank statement must be approved by consent or motion of the council. The policy and procedures for the Treasurer have been discussed with council and the Treasurer and have been approved by council.

It is my intent as the Mayor of the Town of Kenton that the financial activity and all that this council does is on the table for all to see. Our policies shall be posted on bulletin boards in the council building for any one attending meetings to review. Anyone wanting to be on council will have to consent to a background check. All our council members have passed the background check at this time including the Secretary.

The council will consist of the Mayor, Vice Mayor, and Council Person At Large. These three are the only decision makers. The Treasurer and the Secretary do not vote on issues as council members. This further segregates their duties.

My definition of integrity is to do the right thing even though nobody is watching.

Paul Caple
Mayor

DISTRIBUTION OF REPORT

Copies of this report have been distributed to the following public officials:

The Honorable Jack A. Markell, Governor, State of Delaware
The Honorable Russell T. Larson, Controller General, Office of the Controller General
The Honorable Joseph R. Biden, III, Attorney General, Office of the Attorney General
The Honorable Velda Jones-Potter, Treasurer, Office of the State Treasurer

Officials of Audited Entity

Mr. Paul Caple, Mayor, Town of Kenton
Mr. Jacob Tice, Treasurer, Town of Kenton
Mr. David Finnachairo, Town Solicitor, Town of Kenton