

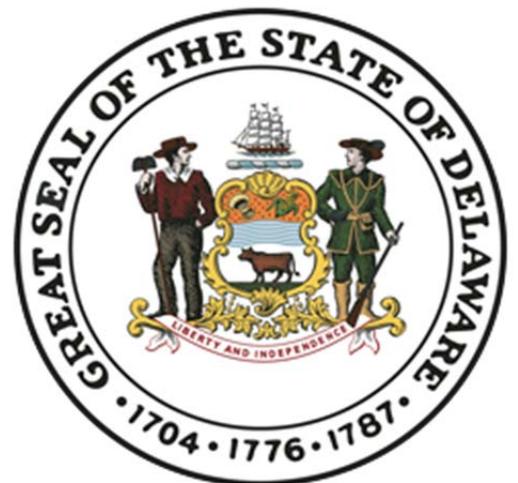
**State of Delaware
Office of Auditor of Accounts**

**Tappahanna Tax Ditch Treasurer
Embezzles Funds**

Special Investigation

**Fieldwork End Date: June 3, 2014
Issuance Date: June 11, 2014**

R. Thomas Wagner, Jr., CFE, CGFM, CICA
Auditor of Accounts





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!

Report Fraud, Waste, and Abuse

Citizens have the right to demand that their tax dollars are properly spent. Fight fraud, waste, and abuse in State government by contacting our confidential Fraud Hotline with supporting evidence.

1-800-55-FRAUD
or
auditor.delaware.gov

This investigation was performed in accordance with the Council of the Inspectors General on Integrity and Efficiency, *Quality Standards for Investigations*.

For further information on this release, please contact:

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Tappahanna Tax Ditch Treasurer Embezzles Funds

The Department of Natural Resources and Environmental Control (DNREC) contacted the Office of Auditor of Accounts (AOA) after performing a review of an anonymous tip that funds belonging to the Tappahanna Tax Ditch in Kent County had been misspent. According to the last annual report submitted to DNREC, the Tappahanna Tax Ditch had \$49,816 at December 31, 2012. One year later, the ending balance per the bank statement as of December 31, 2013, was \$14.07.

AOA substantiated that the Tappahanna Tax Ditch Treasurer (Treasurer Cox¹) embezzled² \$124,654.98 of comingled funds. Although the embezzlement began in 2009 with unauthorized cash withdrawals, the majority, \$78,870.80, occurred after Treasurer Cox obtained a debit card for the account in August 2013. Treasurer Cox abused the authority entrusted in him by making unauthorized purchases and drawing thousands of dollars via bank branch, check, and ATM withdrawals.

From 2009 through 2013, Treasurer Cox withdrew over \$90,000 in cash and made over \$30,000 in purchases and payments. His expenditures consisted of numerous trips and lavish purchases including a boat and electronics. He also squandered the funds on frivolous items such as Apple iTunes, cigars, and a tattoo.

Since there were insufficient controls surrounding the Tappahanna Tax Ditch funds, the Ditch Managers and other landowners were unaware of Treasurer Cox's embezzlement activities. According to the bank, Treasurer Cox was the only authorized signer on the account and the bank statements were mailed to his address. Treasurer Cox hid his unauthorized activity by not providing bank statements with the financial reports presented at the annual tax ditch meetings.

Historically, with assistance from DNREC, volunteers that run these organizations have been very successful. They are dedicated individuals and should be commended for their efforts and stewardship.

AOA communicated with the Attorney General's Special Investigations Unit for the duration of this investigation and provided the results for determination of any criminal activity.

¹ Mr. Jeffrey Cox of Hartly, Delaware, served as the Treasurer of the Tappahanna Tax Ditch from March 2006 until January 2014 when his account access was terminated.

² As defined by the Association of Certified Fraud Examiners *2014 Fraud Examiners Manual*, embezzlement is the wrongful taking or conversion of the property of another by a person to whom it has been lawfully entrusted (or to whom lawful possession was given).

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The conclusion of the allegation 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, or competent evidence was found to dispute a portion of the allegation.
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.

Background

Tax ditches provide drainage and flood control in both agricultural and urban areas throughout the State of Delaware. The Delaware General Assembly enacted the 1951 Drainage Law³ to establish, finance, and maintain drainage organizations (tax ditches). Formation of a tax ditch can only be initiated by landowners who petition Superior Court to resolve drainage or flooding concerns. Following the outcome of the final hearing, and if deemed appropriate, the Superior Court judge issues a Court Order establishing the tax ditch organization. The Court Order establishes permanent rights-of-way for the tax ditch organization for construction and maintenance operations, empowers the organization with taxation authority to collect funds from all affected landowners within the watershed to perform this construction and maintenance, and establishes the taxation amount for individual properties.⁴ The ditch tax is then administered by the respective county government and included in the landowners' annual property tax bills. The county then distributes the collected tax revenue to the respective tax ditches. In 2013, statewide ditch tax revenue was \$677,677.

A tax ditch is a governmental subdivision of the State. The organization is comprised of all landowners (also referred to as taxables) of a particular watershed or sub-watershed. The operations of a tax ditch are overseen by ditch managers and a secretary/treasurer. These officers are landowners within the watershed and are elected at an annual meeting by the taxables. Tax ditch managers and the secretary/treasurer may be entitled to receive compensation at a rate determined by the taxables⁵; however, the majority of ditch managers and secretary/treasurers are volunteers. Typical tax ditch expenditures include mowing or targeted herbicide applications to control vegetation and maintain water flow, meeting expenses (advertising, postage for notices, location fees), and other expenses needed to maintain the ditch and allow for proper drainage. Every 15 to 20 years, the ditch may need to be "dipped out" to remove accumulated sediments and restore the ditch to its original design.⁶

The Department of Natural Resources and Environmental Control (DNREC), Division of Watershed Stewardship, Drainage & Tax Ditches Program provides technical assistance and administrative support to tax ditch organizations from the legal formation process through the maintenance of the State's 2,000 miles of tax ditches. Delaware has 234 individual tax ditch organizations⁷, ranging in size from 56,000 acres as in the Marshyhope Creek Tax Ditch in southern Delaware, to a two-acre system in Wilmington. Tax ditch channels range in size from six to 80 feet wide and two to 14 feet deep. A collaboration of the Board of Ditch Commissioners, the county conservation district, and the DNREC Division of Watershed Stewardship determines the location and size of the ditch. The dimensions depend on the acreage being drained and the topography.

The Tappahanna Tax Ditch, established in 1972, is located west of Dover and basically parallels the south side of Route 8 for 6.6 miles. The Tappahanna Tax Ditch is a large watershed area that receives water from four other tax ditches. (*See Illustrations 1 and 2.*) The taxables living within the four contributing tax ditches also pay an additional ditch tax for the Tappahanna Tax Ditch. The Tappahanna watershed area consists of 1,805 land parcels totaling approximately 13,800 acres. Tappahanna's average annual tax revenue is approximately \$5,600.

³ 7 Del. C., c. 41

⁴ <http://www.dnrec.delaware.gov/swc/Drainage/Pages/TaxDitches.aspx>

⁵ 7 Del. C., §4158

⁶ Per DNREC Drainage Brochure

⁷ Confirmed by DNREC as of January 13, 2014

Illustration 1 – Tappahanna Tax Ditch

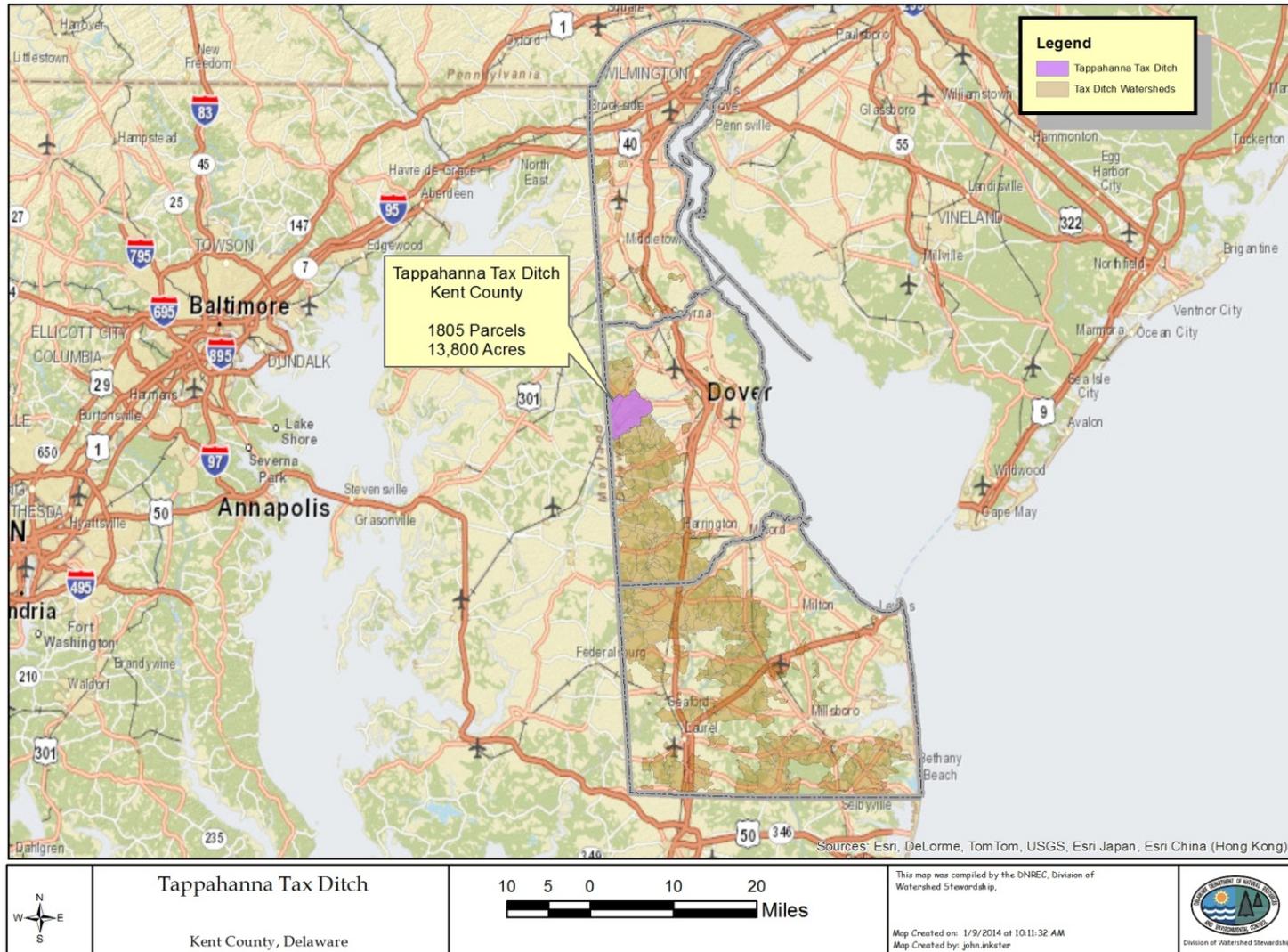
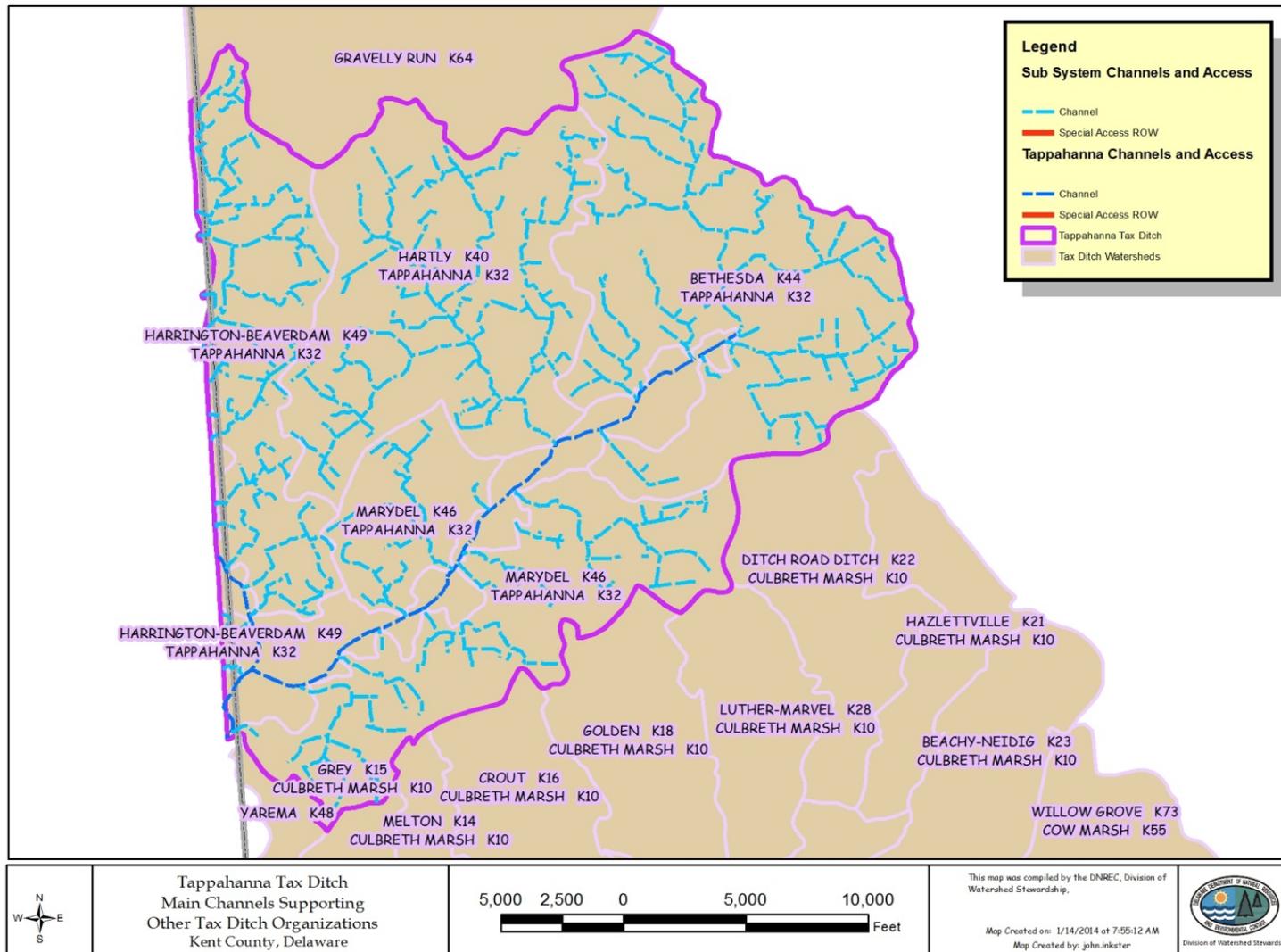


Illustration 2 – Tappahanna Tax Ditch Watershed Area



Maps courtesy of DNREC.

Allegation and Results

Allegation – Substantiated

DNREC contacted AOA in December 2013 after reviewing an anonymous tip that funds belonging to the Tappahanna Tax Ditch in Kent County had been misspent. According to the last annual report submitted to DNREC in June 2013, the Tappahanna Tax Ditch had \$49,816 at December 31, 2012. The ending balance per the bank statement as of December 31, 2013 was \$14.07.

Results of Our Review

The Tappahanna Tax Ditch Treasurer (Treasurer Cox⁷) embezzled⁸ \$124,654.98 from the Tappahanna Tax Ditch bank account. Although the embezzlement began in 2009 with unauthorized cash withdrawals, the majority, \$78,870.80, occurred after Treasurer Cox obtained a debit card for the account in August 2013. Treasurer Cox commingled his personal funds with the tax ditch funds as discussed in further detail on page 9 of this report. However, Treasurer Cox used those funds and the tax ditch funds for personal endeavors, leaving the Tappahanna Tax Ditch with only \$14.07 before his account access was terminated. Treasurer Cox abused the authority entrusted in him by making unauthorized purchases and drawing thousands of dollars via bank branch, check, and ATM withdrawals.

Since there were insufficient controls surrounding the Tappahanna Tax Ditch funds, the Ditch Managers and other taxables were unaware of Treasurer Cox's embezzlement activities. According to the bank, Treasurer Cox was the only authorized signer on the account, and the bank statements were mailed to his address. Treasurer Cox hid his unauthorized activity by falsifying financial reports and not providing bank statements at the annual tax ditch meetings. For example, the December 31, 2012 balance of \$49,816.26 reported by Treasurer Cox at the annual meeting did not agree to the \$35,794.39 bank balance⁹.

The Drainage Law¹⁰ states "...the records of the secretary-treasurer shall be audited annually by 2 qualified persons..." While the magnitude of such an audit is not defined, AOA does not believe the intent of the law is to have a financial statement audit in accordance with standards established by the American Institute of Certified Public Accountants and the U.S. Government Accountability Office's *Government Auditing Standards*. However, at a minimum, the two individuals chosen to perform the "audit" should verify the balance reported on the treasurer's report to the bank statement and review disbursements for appropriateness. Further, the tax ditch organizations are encouraged to utilize the services provided by DNREC and their respective county conservation district for an "arms-length" review of their financial records.

On January 6, 2014, DNREC sent a certified letter to Treasurer Cox, which he signed for, requesting all Tappahanna Tax Ditch records in his possession be turned in to AOA for audit. When nothing was turned in, AOA initiated a subpoena that was issued to him on February 12, 2014, for the documents. Treasurer

⁷ Mr. Jeffrey Cox of Hartly, Delaware, served as the Treasurer of the Tappahanna Tax Ditch from March 2006 until January 2014 when his account access was terminated.

⁸ As defined by the Association of Certified Fraud Examiners *2014 Fraud Examiners Manual*, embezzlement is the wrongful taking or conversion of the property of another by a person to whom it has been lawfully entrusted (or to whom lawful possession was given).

⁹ Bank balance consists of \$5,794.39 checking account balance as of December 31, 2012 and a \$30,000 Certificate of Deposit (CD), not including any interest earned. Total interest earned over the life of the CD was \$797 upon closure on August 6, 2013.

¹⁰ 7 Del. C. §4163 (2)

Cox finally turned in a few documents, including three overdraft notices and just three months of bank statements. Treasurer Cox did not provide any invoices, receipts, checkbook ledger, or other information regarding his spending sprees. He later claimed the missing records were thrown out because of water damage. Through subpoenas and with the cooperation and assistance of PNC Bank, Kent County, the Kent Conservation District, DNREC, and various vendors, AOA was able to obtain the needed documents and information to perform the investigation.

AOA reviewed the January 2007¹¹ through January 2014 bank statements for the Tappahanna Tax Ditch and discovered the embezzlement began on March 18, 2009. On this date, Treasurer Cox purchased a Certificate of Deposit (CD) for the Tappahanna Tax Ditch and, due to his sole authority over the tax ditch funds, withdrew \$300 in cash the same day. See Exhibit 1. Within the next two weeks, Treasurer Cox had already embezzled \$12,000 from the Tappahanna Tax Ditch operating account. Through review of the detailed transactions, AOA found no evidence that these funds were used for legitimate tax ditch expenses.

Exhibit 1 – First Unauthorized Cash Withdrawal

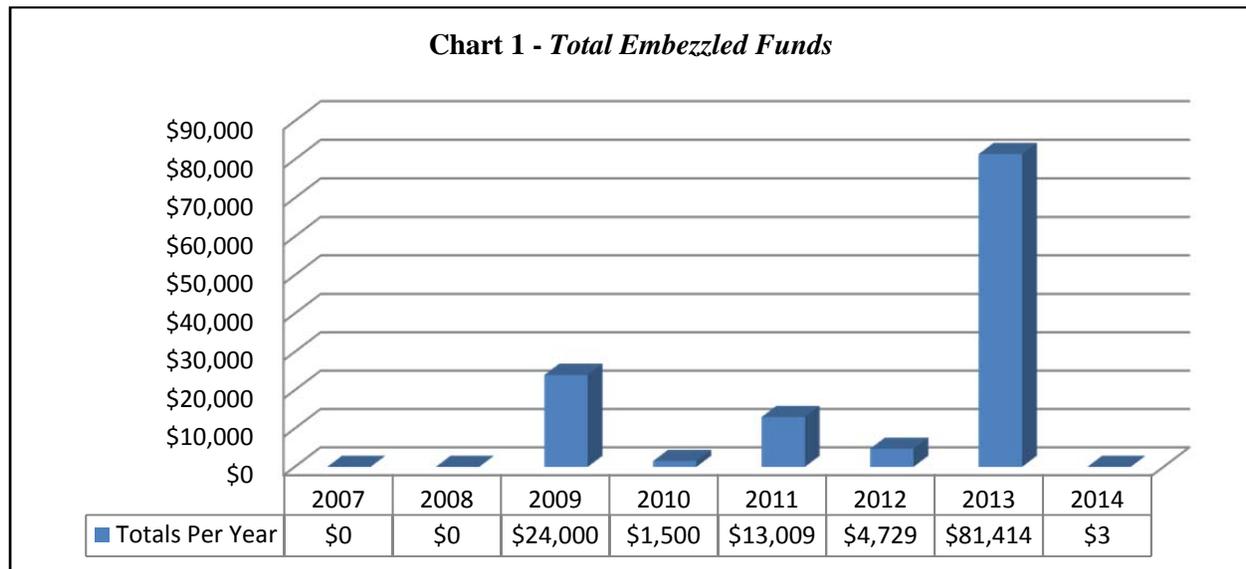
The image shows the front and back of a PNC check. The front of the check is dated 3-18-09 and is payable to CASH for the amount of \$300.00. The check is issued by TAPPAHANNA TAX DITCH. The routing number is 00359. The memo field is blank. The MICR line at the bottom of the front of the check is: @0000 @ 054000030 @ [redacted] @000030000@. The back of the check shows a stamp from PNC Bank, Delaware, dated 3/18/09, and a signature strip with a signature that is mostly obscured by a redaction box. The stamp includes the text: PNC BANK, DELAWARE, CENTRAL PA, MIDDLETOWN, PA, 19709. The signature strip includes the text: DO NOT WRITE, STAMP OR SIGN BELOW THIS LINE, RESERVED FOR FINANCIAL INSTITUTION USE.

¹¹ Although Treasurer Cox was elected in March 2006, bank records prior to 2007 are no longer available from the bank.

From 2009 through 2013, Treasurer Cox withdrew over \$90,000 in cash and made over \$30,000 in purchases and payments. His expenditures consisted of numerous trips and lavish purchases including a boat and electronics. He also squandered the funds on frivolous items such as Apple iTunes, \$400 on cigars, and over \$350 in overdraft fees and service charges.

Checks and Withdrawals	\$91,090.00
Purchases and Payments	\$33,166.23
Bank Fees	\$367.98
CD Early Withdrawal Penalty	\$30.77
Total Embezzled	\$124,654.98

The graph below shows the total dollar amounts Treasurer Cox spent on unauthorized transactions per year.



During the period from January 1, 2007 through January 14, 2014, legitimate transactions incurred by the Tappahanna Tax Ditch consisted of tax receipts of \$44,542.89 and ditch maintenance expenditures totaling \$13,528.75.

Treasurer Cox obtained a debit card for the account on August 1, 2013, just before embarking on a series of trips. His first excursion was to Key West, Florida, where he used the taxables’ money to purchase a \$200 tattoo and other shopping and tourist excursions costing approximately \$1,200. Along with swiping the debit card at multiple locations, Treasurer Cox withdrew \$2,600 in cash from ATMs in Key West. Three same day ATM withdrawals totaling \$875 came from a machine located at 1221 Duval Street. Further research indicated this address is an “Adult Entertainment Club”, which advertises that an ATM is located inside along with “live nude entertainment” and one-on-one private rooms.

While on his Key West trip, Treasurer Cox cashed in Tappahanna’s \$30,000 CD by making a call to the bank. Since the CD was still seven months away from maturity, the bank assessed an early withdrawal

penalty of \$30.77. He returned home for a few days, long enough to purchase a 1997 Boston Whaler Boat and a 2000 Johnson 150 horse power motor for \$11,126. Per the vendor invoice at Exhibit 2, Treasurer Cox paid for this boat and motor in split payments of \$5,000 in cash and \$6,126 on the tax ditch's debit card. Conveniently, on the same day as this unauthorized purchase, Treasurer Cox withdrew \$10,000 in cash from a bank branch in Kent Island, MD. See Exhibit 3.

Exhibit 2 – Boat Purchase

INVOICE



Chesapeake Whalertowne

108 Hess Frontage Road • Grasonville, MD 21638
Phone: (410) 827-8080 • Fax: (410) 827-3888






Jeffrey Howard Cox
[REDACTED]

DATE: August 10, 2013
TERMS:
FED. I.D. #52-0797657

1 1997 Boston Whaler 170 Outrage	+	\$5,800.00
1 2000 Johnson 150 HP	+	<u>\$4,700.00</u>
Balance		\$10,500.00
DNR Registration/Office Fees		\$101.00
DNR Tax	+	\$525.00
Balance		\$11,126.00
Cash Deposit 8/10/13	-	\$5,000.00
Visa Deposit 8/10/13	-	\$6,126.00
Balance		\$0.00

Boat Hull # [REDACTED]
Engine Serial # [REDACTED]

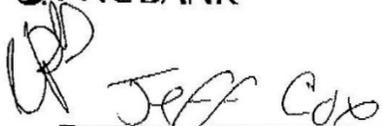
Exhibit 3 – Cash Withdrawal for Boat Purchase

Jan. 22. 2014 2:27PM PNC Bank No. 1462 P. 1



Checking/Savings Withdrawal Ticket

Date 8/10/13


 Hereby Acknowledges \$ 10,000⁰⁰

The Undersigned

Receipt Of Ten Thousand Dollars

Account Number [REDACTED]

Region [REDACTED]

* 265 Withdrawal BS \$10,000.00 PD

⑆7409⑉9909⑆

Just as he was re-opening his equipment sales and repair business in October 2013, Treasurer Cox purchased a Gateway desktop computer and monitor and two wireless printers from Best Buy for \$666.92. He also purchased many hand held tools, a five drawer tool chest, compressor, a 4x8 foot utility trailer, and a motorcycle lift from Harbor Freight. Treasurer Cox spent almost \$2,600 at Harbor Freight despite the debit card being declined two times during one of the purchases.

When AOA interviewed Treasurer Cox in April 2014, he stated he put his own money in the account and took money out without the Tax Ditch Managers' knowledge or authorization. He stated, "I comingled funds and used that checking account to purchase things on my own." However, Treasurer Cox did not make his first deposit of his own money until March 9, 2012; three years after the embezzlement began. At this point, he had withdrawn \$38,918 from Tappahanna's account, dwindling the account balance to less than \$200. Less than four months later, on June 28, 2012, the bank closed Tappahanna's account since it had been overdrawn for more than thirty days. On July 23, 2012, Treasurer Cox paid the balance due to the bank and had the account re-opened only one week prior to receiving the Kent County tax deposit.

Aside from the tax revenue deposits made directly by Kent County, Treasurer Cox deposited \$46,640.72 into Tappahanna's account during his tenure. This amount includes a retirement fund disbursement of \$32,466.70 from his previous employer after termination in September 2013. If these deposits were made to replenish the account, it did not deter him from continuing to spend the taxables' money. Two days after he deposited his retirement money, he withdrew \$25,000 (see Exhibit 5). He continued his discretionary spending through December 31, 2013, when his access to the account was terminated.

Exhibit 5 – \$25,000 Cash Withdrawal

PNC BANK ACCOUNT NUMBER REGIONAL ID Date 10/7/13

Checking/Savings Withdrawal Ticket

NON-NEGOTIABLE FORM 162753 \$ 25,000 .00

FORM 162753 Jeffrey H. Cox Hereby Acknowledges
The Undersigned

Receipt Of 25,000 Twenty Five Thousand Dollars

Signature

⑆7409⑆9909⑆

AOA communicated with the Attorney General's Special Investigations Unit for the duration of this investigation and provided the results for determination of any criminal activity.

AOA commends the volunteers that manage tax ditch organizations for their efforts and stewardship and encourages them to seek appropriate resources to ensure proper controls are in place over taxpayer funds. According to the Drainage Law¹², it is the secretary-treasurer's duty to provide for the safekeeping of any funds of the tax ditch which are placed in his or her custody. AOA reviewed DNREC's financial controls advice document and financial reporting template and made suggestions to improve internal controls surrounding tax ditch funds.

¹² 7 Del. C. §4163 (3)