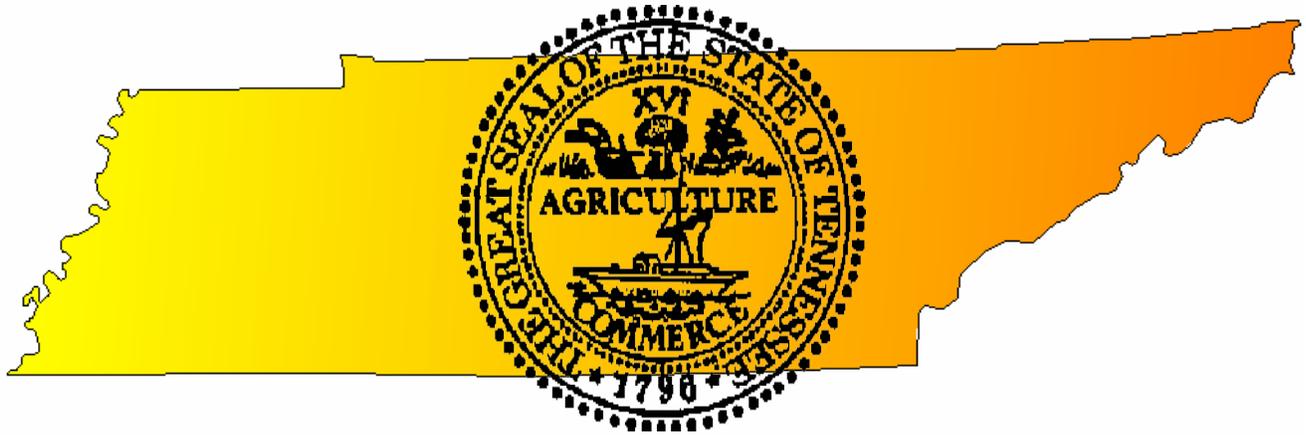


INVESTIGATIVE AUDIT REPORT

CITY OF LAKEWOOD

JULY 1, 2004, THROUGH SEPTEMBER 30, 2005



State of Tennessee



**Comptroller of the Treasury
Department of Audit
Division of Municipal Audit**



STATE OF TENNESSEE

John G. Morgan
Comptroller

C O M P T R O L L E R O F T H E T R E A S U R Y

STATE CAPITOL

NASHVILLE, TENNESSEE 37243-0260

PHONE (615) 741-2501

November 14, 2007

Honorable Mayor and Members of the
Board of Commissioners
City of Lakewood
3401 Hadley Avenue
Old Hickory, TN 37138

Ladies and Gentlemen:

Presented herewith is the report on our investigative audit of selected records of the City of Lakewood for the period July 1 2004, through September 30, 2005. However, when the examination warranted, this scope was expanded.

Section 9-2-102, *Tennessee Code Annotated*, requires that the Comptroller of the Treasury prescribe a uniform system of bookkeeping designating the character of books, reports, receipts and records, and the method of keeping same, in all state, county and municipal offices, including utility districts, which handle public funds. This code section also requires that all officials adopt and use the prescribed system. The Comptroller has prescribed a minimum system of recordkeeping for municipalities, which is detailed in the *Internal Control and Compliance Manual for Tennessee Municipalities* combined with Chapters 1-7 of *Governmental Accounting, Auditing, and Financial Reporting*. The purpose of our audit was to determine the extent of the entity's compliance with certain laws and regulations, including those in the above-mentioned manuals.

The findings and recommendations in this report relate to those conditions that we believe warrant your attention. All responses to each of the findings and recommendations are included in the report.

Honorable Mayor and Members of the
Board of Commissioners
City of Lakewood
November 14, 2006

Copies of this report are being forwarded to Governor Phil Bredesen, the State Attorney General, the District Attorney General, certain state legislators, and various other interested parties. A copy is available for public inspection in our office.

Very truly yours,

A handwritten signature in black ink that reads "John G. Morgan". The signature is written in a cursive style with a long horizontal flourish at the end.

John G. Morgan
Comptroller of the Treasury



**STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF MUNICIPAL AUDIT**

John G. Morgan
Comptroller of the Treasury

SUITE 1600
JAMES K. POLK STATE OFFICE BUILDING
505 DEADERICK STREET
NASHVILLE, TENNESSEE 37243-0271
PHONE (615) 401-7871
FAX (615) 741-1551

Dennis F. Dycus, CPA, CFE, Director
Division of Municipal Audit

November 14, 2006

Mr. John G. Morgan
Comptroller of the Treasury
State Capitol
Nashville, TN 37243-0260

Dear Mr. Morgan:

As part of our ongoing process of examining the records of municipalities, we have completed our investigative audit of selected records of the City of Lakewood. This investigative audit focused on the period July 1, 2004, through September 30, 2005. However, when the examination warranted, this scope was expanded.

Section 9-2-102, *Tennessee Code Annotated*, requires that the Comptroller of the Treasury prescribe a uniform system of bookkeeping designating the character of books, reports, receipts and records, and the method of keeping same, in all state, county and municipal offices, including utility districts, which handle public funds. This code section also requires that all officials adopt and use the prescribed system. The Comptroller has prescribed a minimum system of recordkeeping for municipalities, which is detailed in the *Internal Control and Compliance Manual for Tennessee Municipalities* combined with Chapters 1-7 of *Governmental Accounting, Auditing, and Financial Reporting*. The purpose of our audit was to determine the extent of the entity's compliance with certain laws and regulations, including those in the above-mentioned manuals.

Our examination resulted in findings and recommendations related to the following:

1. Municipal funds apparently used to pay legal fees of the former city manager
2. Shortage of \$484.25
3. Municipal funds used for nonmunicipal purchases
4. Failure to prepare daily collection reports
5. Inadequate separation of duties
6. Utility accounts receivable reconciliation not performed

Mr. John G. Morgan
Comptroller of the Treasury
November 14, 2006

7. Inadequate payroll records
8. Christmas bonuses paid in cash
9. Unauthorized payments for medical expenses
10. Inadequate documentation for disbursements
11. Bid records incomplete
12. Inadequate minutes of meetings

In addition to our findings and recommendations, we are also providing management's response. If after your review, you have any questions, I will be happy to supply any additional information which you may request.

Sincerely,

A handwritten signature in black ink, appearing to read "Dennis F. Dycus", is written over a light gray rectangular background.

Dennis F. Dycus, CPA, CFE, Director
Division of Municipal Audit

**INVESTIGATIVE AUDIT OF SELECTED RECORDS
OF THE CITY OF LAKEWOOD
FOR THE PERIOD JULY 1, 2004, THROUGH SEPTEMBER 30, 2005**

FINDINGS AND RECOMMENDATIONS

1. **FINDING: Municipal funds apparently used to pay legal fees of the former city manager**

Our investigative audit revealed two instances in which it appears that city funds were used to pay the personal legal fees of R. C. White, the former city manager for the City of Lakewood.

Auditors questioned the authenticity of an invoice, approved by Mr. White, supporting a March 18, 2004, \$2,500 payment to the former city attorney, Robert Rutherford. When asked to provide additional documentation for the payment, Mr. Rutherford responded that it was his understanding that the former city manager had reimbursed the city for that payment. He further advised auditors that he did not recognize the invoice located in city files. Auditors and city personnel were unable to locate documentation of reimbursement by Mr. White for these apparent personal legal fees.

Auditors also found that, on May 17, 2005, the former city manager approved a city payment of \$3,246.54 to a Nashville law firm. The city's supporting documentation indicated the services had been performed on behalf of the personal business of the former city manager. After questions were raised about the propriety of that payment, the law firm applied the city's payment to another separate invoice billed to the city for legal work including research involving Metro charter, ouster and recall, and recall of elections.

In a telephone call, Mr. Rutherford told auditors that he limited the description of his legal work performed on behalf of the city at the request of the former city manager, Mr. White.

Section 6-56-112, *Tennessee Code Annotated*, states, "All expenditures of money made by a municipality must be made for a lawful municipal purpose."

The *Internal Control and Compliance Manual for Tennessee Municipalities*, Title 1, Chapter 2, Section 3, states:

Municipal officials should provide constant, close supervision to ensure ... internal controls are working.

Section 3 requires that the related documentation accompany checks presented for approval and signing.

RECOMMENDATION:

To document that each disbursement was for a valid municipal purpose, officials should ensure that adequate supporting documents are maintained in the municipality's files in accordance with the *Internal Control and Compliance Manual for Tennessee Municipalities*. Before signing a check, authorized individuals should review adequate supporting documentation to determine that the disbursement is for a valid municipal purpose and that the charge has not previously been paid.

MANAGEMENT'S RESPONSE:

Honorable Mayor and Members of the Board of Commissioners:

We concur. We are unaware of any services performed by the law firm of Mosely & Mosely for the benefit of the city. The funds in the amount of \$3,246.54 credited by the firm should be fully documented or returned to the city.

2. **FINDING:** **Shortage of \$484.25**

In the course of our examination, we noted that receipts totaling \$484.25 and recorded as being part of an April 22, 2005, deposit into the city's general fund were not deposited into the city's bank account. Although this matter was investigated by the Lakewood Police Department, and one employee subsequently resigned, it was not referred to the Comptroller of the Treasury. Therefore, this office was effectively deprived of its statutory authority to independently investigate this apparent misappropriation of public funds. Section 8-4-109, *Tennessee Code Annotated*, states:

The comptroller of the treasury is hereby authorized to audit any books and records of any governmental entity created under and by virtue of the statutes of the state of Tennessee which handles public funds when such audit is deemed necessary or appropriate by the comptroller of the treasury. The comptroller of the treasury shall have the full cooperation of officials of the governmental entity in the performance of such audit or audits.

Section 9-3-212, *Tennessee Code Annotated*, states:

The comptroller of the treasury, when the comptroller deems it necessary, may require any audit required of any such agency, or any investigative or review work in addition to such audit which, in the exercise of the comptroller's discretion, the comptroller believes necessary to ascertain or correct errors, irregularities, or defaults in the management and disbursement of funds controlled by such agency, to be conducted by the department of audit...

Our investigative audit revealed several weaknesses in the city's collection process that contributed to or could contribute to an undetected misappropriation. Those weaknesses are detailed in Findings 4, 5, and 6.

RECOMMENDATION:

In the future, when management becomes aware of irregularities or possible irregularities, they should immediately contact the Comptroller of the Treasury so that he may exercise his authority to independently investigate the matter.

MANAGEMENT'S RESPONSE:

Honorable Mayor and Members of the Board of Commissioners:

We concur.

3. **FINDING: Municipal funds used for nonmunicipal purchases**

Our investigative audit revealed that in November 2003, municipal funds totaling \$164.20 were apparently used to purchase two tires for a personal automobile registered to the former city recorder. The related invoice appeared to have been signed as approved by the former police chief. In addition, our audit found that on March 8, 2004, the city paid for an alignment for a pickup truck that was not registered to the city and identified by municipal employees as owned by the son of the former city manager. Section 6-56-112, *Tennessee Code Annotated*, states, "All expenditures of money made by a municipality must be made for a lawful municipal purpose."

RECOMMENDATION:

To comply with state law, officials should ensure that all city disbursements are for a lawful municipal purpose.

MANAGEMENT’S RESPONSE:

Honorable Mayor and Members of the Board of Commissioners:

We concur.

4. **FINDING:** Failure to prepare daily collection reports

The recorder did not prepare daily collection reports summarizing the amount and source of cash collected each day. In addition, deposit slips did not list each check included in the deposit. Based on our analysis of deposits, it was apparent that collections were not deposited intact and as recorded in collection records. The *Internal Control and Compliance Manual for Tennessee Municipalities*, Title 3, Chapter 1, Section 6, requires municipal officials to ensure that

... each day the cashier summarizes all cash collections by source on a daily collection report, clearly indicating the amount to be deposited, the amount retained for change, and the amount of cash over or short. Each report should be dated, and the date should be recorded on the corresponding deposit slips. The total on the daily collection report should agree with the total of the corresponding deposit slips as well as the total of all applicable receipts. The cashier should sign the daily collection report....

Section 4 requires that municipal personnel list each check deposited separately on an itemized deposit slip. Section 5 requires that collections be deposited promptly and intact.

RECOMMENDATION:

To better account for collections, each day the cashier should prepare a detailed report of that day’s total collections and the source of those collections. To help document that all collections are deposited intact, the totals of each daily collection report, corresponding prenumbered receipts, and related bank deposit should agree. Municipal personnel should itemize deposit slips and list each check separately.

MANAGEMENT’S RESPONSE:

Honorable Mayor and Members of the Board of Commissioners:

We concur.

5. **FINDING: Inadequate separation of duties**

Three clerks who collected money used the same cash drawer. In addition, one clerk who was responsible for making and recording collections also was responsible for preparing bank deposits. The *Internal Control and Compliance Manual for Tennessee Municipalities*, Title 1, Chapter 2, Section 2, states:

Municipal officials should enforce division of duties to provide a system of checks and balances so that no one person has control over a complete transaction from beginning to end. Work flow should be established so that one employee's work is automatically verified by another employee working independently....

Title 1, Chapter 2, Section 4, of the manual further states:

Municipal officials should ensure that automatic proof techniques are applied whenever possible. These techniques include the use of an employee without prior access to the records to ... reconcile bank accounts ... periodically test ... daily balancing of cash receipts ... open mail and prelist mail receipts ... perform routine duties of other employees ... for at least one vacation period per year.

RECOMMENDATION:

To decrease the risk of undetected errors and irregularities, management should review employees' responsibilities to ensure that no employee has control over a complete transaction. In addition, elected officials should exert increased oversight, where necessary.

MANAGEMENT'S RESPONSE:

Honorable Mayor and Members of the Board of Commissioners:

We concur.

6. **FINDING: Utility accounts receivable reconciliation not performed**

The municipality's records did not include documentation of a monthly reconciliation of utility accounts receivable as reflected in the utility billing register to the general ledger control account. The *Internal Control and Compliance Manual for Tennessee Municipalities*, Title 3, Chapter 3, Section 10, states, "Municipal officials should ensure that ... the total amount of the unpaid individual accounts on the utility billing sheet is

reconciled to the applicable general ledger control account total at the end of each month.”

RECOMMENDATION:

To detect errors or irregularities promptly, municipal officials should ensure that a monthly reconciliation, of the detail listing of accounts receivable in the billing register to the general ledger control account, is performed and documented.

MANAGEMENT’S RESPONSE:

Honorable Mayor and Members of the Board of Commissioners:

We concur.

7. FINDING: Inadequate payroll records

The former recorder, Virginia Moss, received net payroll payments of \$2,497.82 in addition to her regular salary for the calendar year ending December 31, 2004. Documentation in city files indicated that \$1,531.78 of this additional salary was payment for compensatory time. However, city files did not contain evidence of when or if she had earned the compensatory time. There was no documentation to indicate the purpose of the remaining \$966.04 in net payments to Ms. Moss. The *Internal Control and Compliance Manual for Tennessee Municipalities*, Title 2, Chapter 3, sets forth required payroll and personnel documentation and procedures necessary for precise maintenance and centralized control of these records.

RECOMMENDATION:

To decrease the risk of improper payroll payments and to ensure compliance with state and federal regulations, the mayor and members of the board of commissioners should require city personnel to establish and maintain complete payroll and personnel records.

MANAGEMENT’S RESPONSE:

Honorable Mayor and Members of the Board of Commissioners:

We concur.

8. **FINDING: Christmas bonuses paid in cash**

City of Lakewood officials did not require that all applicable city disbursements were made by prenumbered check. Apparently with the knowledge of some city officials, city personnel cashed city checks issued to petty cash totaling \$5,200 and used the cash for 2004 Christmas bonuses to city employees. These payroll-related payments were not subjected to the required federal taxes.

Section 6-56-111, *Tennessee Code Annotated*, states:

- (c) Every municipal official authorized to disburse public funds shall be required to make disbursements of such public funds by consecutively prenumbered checks, warrants or other generally accepted negotiable instruments drawn on the municipality's official bank account or accounts.

The *Internal Control and Compliance Manual for Tennessee Municipalities*, Title 2, Chapter 2, and Chapter 3, provides additional guidance for disbursing municipal funds. Title 2, Chapter 3, Section 11, of the manual states, "Municipal officials should note that local government units are required to report total salaries and make payment of income taxes withheld in the same manner as other employers...."

RECOMMENDATION:

To document that disbursements are for valid municipal purposes, comply with federal tax law, and prevent undetected errors and irregularities, city officials should require the use of consecutively prenumbered checks for all disbursements, including payroll-related payments. Applicable federal taxes should be withheld from all payments to employees for compensation for services.

MANAGEMENT'S RESPONSE:

Honorable Mayor and Members of the Board of Commissioners:

We concur.

9. **FINDING: Unauthorized payments for medical expenses**

We noted numerous payments from city funds, including the Waterworks Fund, to health care providers on behalf of city employees. The "City of Lakewood Personnel Policies and Procedures," adopted November 10, 2003, states, "The City of Lakewood provides basic health coverage. The City pays a percentage depending on single or family coverage." City policies do not further define the responsibility of the city or the

individual in paying for health insurance coverage. We located approval by the mayor and board of commissioners for only a portion of some payments made on behalf of one employee among several employees for which direct payments to health care providers were made. In that approval dated November 21, 2005, it was noted that the city's obligation to pay a portion of the deductible for that employee was implied and never fully defined.

Section 6-54-123, *Tennessee Code Annotated*, requires municipalities to adopt a personnel policy by ordinance, resolution, or other means. The *Internal Control and Compliance Manual for Tennessee Municipalities*, Title 1, Chapter 1, sets forth the required books and records for Tennessee municipalities. Included in those requirements are a complete policies and procedures manual and a complete personnel policy manual.

RECOMMENDATION:

To ensure proper documentation of all payments and that payments made on behalf of employees are according to uniform and established procedures, municipal officials should ensure that all payments made on behalf of employees are made according to properly approved written policies.

MANAGEMENT'S RESPONSE:

Honorable Mayor and Members of the Board of Commissioners:

We concur.

10. **FINDING: Inadequate documentation for disbursements**

The municipality's files did not include adequate supporting documentation for each disbursement. For many disbursements, the files contained either no documentation or only summarized statements. Authorized check-signers apparently did not review and approve adequate supporting documentation before they signed checks.

The *Internal Control and Compliance Manual for Tennessee Municipalities*, Title 2, Chapter 2, Section 4, states:

Municipal officials should ensure ... that supporting documentation is filed alphabetically by vendor or by date paid.... All disbursements, regardless of the accounting procedures, must be supported by invoices, cash tickets or other adequate supporting documentation. (Statements are NOT adequate supporting documentation.)

Section 3 requires that the related documentation accompany checks presented for approval and signing.

RECOMMENDATION:

To document that each disbursement was for a valid municipal purpose, officials should ensure that adequate supporting documents are maintained in the municipality's files in accordance with the *Internal Control and Compliance Manual for Tennessee Municipalities*. Before signing a check, authorized individuals should review adequate supporting documentation to determine that the disbursement is for a valid municipal purpose and that the charge has not previously been paid.

MANAGEMENT'S RESPONSE:

Honorable Mayor and Members of the Board of Commissioners:

We concur.

11. **FINDING: Bid records incomplete**

According to the minutes of the April 8, 2004, meeting of the mayor and commissioners, R.C. White, former city manager, asked commissioners to approve a \$3,640 bid from his son, Steve White, for unspecified repairs for water damage to city hall. The minutes of that meeting mention a second bid of \$7,900 without identifying the bidder. Notes to the meeting mention a third bid from an unidentified bidder for an unspecified amount. We were unable to locate documentation of the two competing bids in city files and we were also unable to locate documentation of the bid specifications and procedures performed in obtaining the bids.

The *Internal Control and Compliance Manual for Tennessee Municipalities*, Title 2, Chapter 1, Section 7, requires that personnel retain sufficient documentation to substantiate that competitive bids were requested when applicable.

RECOMMENDATION:

So that the best price is obtained for work done on behalf of the city, officials should ensure that required bidding procedures are followed for all applicable purchases. Adequate documentation should be maintained to demonstrate compliance with bid policies.

MANAGEMENT’S RESPONSE:

Honorable Mayor and Members of the Board of Commissioners:

We concur.

12. **FINDING:** **Inadequate minutes of meetings**

Members of the planning commission began receiving monthly payments of \$200 beginning in October 2004. Section 13-4-101, *Tennessee Code Annotated*, states that “[t]he chief legislative body may determine whether, and in what amount, to compensate members of the planning commission.” However, auditors were unable to locate any reference to compensation to members of the planning commission in the minutes of the meetings of mayor and members of the board of commissioners of the City of Lakewood.

In addition, auditors found that when the former police chief left Lakewood employment, he took the city’s drug dog with him. The former city manager had apparently made an agreement with the former police chief regarding the purchase of a drug dog. According to that written agreement, the former police chief agreed to raise funds for the purchase of a drug dog through donations and waive the rights to compensation for overtime and training time in exchange for the right to keep the drug dog if and when he left the city’s employment. However, there was no approval of this agreement by the mayor and members of the board of commissioners recorded in the minutes of their meetings.

Section 8-44-104, *Tennessee Code Annotated*, states:

The minutes of a meeting of any such governmental body shall be promptly and fully recorded, shall be open to public inspection, and shall include, but not be limited to, a record of persons present, all motions, proposals and resolutions offered, the results of any votes taken, and a record of individual votes in the event of roll call.

The *Internal Control and Compliance Manual for Tennessee Municipalities*, Title 1, Chapter 1, Section 4, requires that complete minutes of actions taken by the legislative body be maintained and provides a list of items which should be included in the minutes.

RECOMMENDATION:

To document action taken by the governing body, officials should ensure that the recorder maintains complete minutes of all meetings of the governing body. The minutes should be kept at the municipality’s office and be available for public inspection. The mayor and recorder should sign the minutes to document approval.

MANAGEMENT'S RESPONSE:

Honorable Mayor and Members of the Board of Commissioners:

We concur.