

INVESTIGATIVE AUDIT REPORT

**TOWN OF SURGOINSVILLE
JULY 1, 2006, THROUGH JUNE 30, 2007**



State of Tennessee



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



STATE OF TENNESSEE

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

John G. Morgan

Comptroller

STATE CAPITOL

NASHVILLE, TENNESSEE 37243-0260

PHONE (615) 741-2501

October 9, 2008

Honorable Mayor and Members of the
Board of Aldermen
Town of Surgoinsville
P. O. Box 67
Surgoinsville, TN 37873-0067

Gentlemen:

Presented herewith is the report on our investigative audit of selected records of the Town of Surgoinsville. This investigative audit focused on the period July 1, 2006, through June 30, 2007. 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 former vice-mayor, Otis Lawson, had an apparent unlawful conflict of interest between his official duties and his personal interest and also apparently required and received a kickback on a town check payable to Randy's Fabricating. Additionally, Mr. Lawson apparently misappropriated an engine analyzer and a truck hitch acquired by the town through a military surplus program in which the town participated. Finally, it appears that Mr. Lawson instructed public works employees to remove signs that had been placed around town advising the public of a recently passed trucking ordinance.

Each of these matters has been referred to the local district attorney general for his consideration. However, regarding the removal of the trucking ordinance signs, we are aware that the statute of limitations appears to have lapsed.

Honorable Mayor and Members of the
Board of Aldermen
Town of Surgoinsville
October 9, 2008

The findings and recommendations in this report also relate to those conditions that we believe warrant your attention.

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

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

October 9, 2008

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 Town of Surgoinsville. This investigative audit focused on the period July 1, 2006, through June 30, 2007. 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 former vice-mayor, Otis Lawson, had an apparent unlawful conflict of interest between his official duties and his personal interest and also apparently required and received a kickback on a town check payable to Randy's Fabricating. Additionally, Mr. Lawson apparently misappropriated an engine analyzer and a truck hitch acquired by the town through a military surplus program in which the town participated. Finally, it appears that Mr. Lawson instructed public works employees to remove signs that had been placed around town advising the public of a recently passed trucking ordinance.

Each of these matters has been referred to the local district attorney general for his consideration. However, regarding the removal of the trucking ordinance signs, we are aware that the statute of limitations appears to have lapsed.

Mr. John G. Morgan
Comptroller of the Treasury
October 9, 2008

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

1. Military surplus property totaling at least \$137,104 missing
2. Military surplus property used for purposes other than law enforcement and by governmental entities other than the town
3. Oil-burning furnace gifted to vice-mayor without being declared surplus by the board or being sold at auction
4. Contract with former town attorney apparently backdated and entered into without board approval
5. Contract with Brothers Repair apparently backdated and entered into without board approval
6. Deliberate circumvention of bid process by former mayor

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". The signature is fluid and cursive, with a large initial "D" and "F".

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

**INVESTIGATIVE AUDIT OF SELECTED RECORDS OF THE
TOWN OF SURGOINSVILLE
FOR THE PERIOD JULY 1, 2006, THROUGH JUNE 30, 2007**

LEGAL ISSUES

1. **ISSUE: Unlawful conflict of interest of former vice-mayor Otis Lawson**

The former vice-mayor, Otis Lawson, had an apparent unlawful conflict of interest between his official duties and his personal interest. During a board meeting on August 9, 2004, Mr. Lawson asked the town attorney whether it would be a conflict of interest for him to service town vehicles. The town attorney advised Mr. Lawson that it would be a conflict of interest. However, subsequent to receiving that legal advice, during the period January 11, 2006, through August 3, 2006, the Town of Surgoinsville paid A & L Contractors \$4,590 for work on town vehicles. Mr. Lawson was part-owner of the company. Several current and former town officials advised auditors that, when they raised concerns about the town doing business with A & L Contractors, Mr. Lawson denied having any ownership interest in the company and stated that there was no conflict of interest. It also appears that Mr. Lawson used his position as vice-mayor to direct public works employees to take town vehicles to A & L Contractors for needed repairs and maintenance.

2. **ISSUE: Kickback required and received by former vice-mayor Otis Lawson**

Former vice-mayor Otis Lawson apparently required and received a kickback on a town check payable to Randy's Fabricating. On April 6, 2006, town check no. 6181 for \$170.62 was issued to Randy's Fabricating for work performed on a town vehicle. The back of the check was second endorsed by Mr. Lawson. In an interview of the purported owner of Randy's Fabricating, he stated that it was Mr. Lawson's idea to create the fictional company and have him submit the invoice, since it would be a conflict of interest for Mr. Lawson to submit an invoice for the work. Mr. Lawson apparently transacted the check and paid the purported owner of Randy's Fabricating not more than \$20, keeping the remainder for himself.

3. **ISSUE: Engine analyzer and truck hitch acquired through military surplus program apparently misappropriated by former vice-mayor Otis Lawson**

The former vice-mayor, Otis Lawson, apparently misappropriated an engine analyzer and a truck hitch acquired by the town through a military surplus program in which the town participated. The military valued the items at \$7,248 and \$300, respectively.¹ In an interview with Mr. Lawson, when asked about the engine analyzer and truck hitch, he admitted being in possession of both items, claiming that employees of the public works department had simply dumped them at his home, in his yard, without his permission. Auditors observed both the engine analyzer and the truck hitch located in the side yard of Mr. Lawson's home. However, public works employees denied that they had dumped the items in Mr. Lawson's yard. Available documentation indicated that both items were picked up on the town's behalf by Mr. Lawson and former police chief Dale Scalf during a trip to Jacksonville, Florida. In an interview with Mr. Scalf, he stated that he had personally observed both items to be located at A & L Contractors,² the business Mr. Lawson co-owned. In addition to A & L Contractors, Mr. Lawson owned a trucking business and would, therefore, have an obvious use for both items.

4. **ISSUE: Former vice-mayor Otis Lawson instructed public works employees to remove traffic signs in apparent furtherance of his own interests**

Former vice-mayor Otis Lawson instructed employees of the public works department to remove signs that had been placed around town advising the public of a recently passed trucking ordinance that limited the size of trucks allowed to use most town streets. In an interview with Mr. Lawson, he acknowledged that he instructed the employees to remove the signs, but stated that he did so because the ordinance had not passed on second reading. According to Mr. Lawson, the ordinance was enacted before he was elected to the board. However, minutes of board meetings clearly indicate that ordinance 32-2003, restricting vehicles with a gross vehicle weight rating of over 35,000 pounds to travel only on Phipps Bend Road and Highways 346 and 11W, passed on second reading on August 11, 2003. Mr. Lawson was present and voted against the ordinance on both its first and second readings.³ As an independent truck company owner and operator that

¹ All subsequent values for military surplus items are also per the military, the only objective valuation available.

² A & L Contractors was located at 200 Glass Plant Road. Mr. Lawson's personal residence was located on Main Street, several miles away. It appears that Mr. Lawson moved the items from his business address to his personal residence prior to speaking with auditors.

³ The ordinance in question, Ordinance 32-2003, was allegedly removed from the ordinance book while the recorder was on vacation during Christmas 2004. In the recorder's absence, the ordinance book was apparently left in the possession of former mayor Hanes Cooper, who also voted against the ordinance, and former vice-mayor Otis Lawson. Mr. Cooper and Mr. Lawson were the only board members to vote against the ordinance. Upon her return from vacation, the recorder noticed the ordinance missing and reprinted and replaced it, over the alleged objections of the former mayor.

operated out of the town, and as evidenced by his steadfast opposition to the ordinance, Mr. Lawson had an obvious interest in the ordinance.

Each of these matters has been referred to the local district attorney general for his consideration. However, regarding the removal of the trucking ordinance signs, we are aware that the statute of limitations appears to have lapsed.

FINDINGS AND RECOMMENDATIONS

1. **FINDING: Military surplus property totaling at least \$137,104 missing**

As mentioned previously, the Town of Surgoinsville participated in a military surplus program. During the period January 1, 2006, through June 30, 2007, the town obtained military surplus property valued at \$872,580, per the military. Auditors from our office and representatives of the Law Enforcement Support Office (LESO) performed simultaneous inventories of the military surplus property in possession of the town. Although many items were located, military surplus property totaling at least \$137,104 in value was missing.⁴

Among the missing items were a sandblaster, a plasma cutter, a welder, and a pressure washer. Each was located at A & L Contractors, ostensibly being stored in accordance with an agreement between former mayor Hanes Cooper and former vice-mayor Otis Lawson. The aggregate value of the four items was \$13,682. Subsequent to the performance of the inventory, Mr. Lawson returned the items to the town. Also missing were a 24-volt winch kit valued at \$1,490 and a wheel or tire mounter/demounter valued at \$2,052. A town employee informed auditors that Mr. Lawson had admitted being in possession of the 24-volt winch kit and a former town employee and a former town official stated that Mr. Lawson was in possession of the mounter/demounter and that it was located at A & L Contractors.

In addition to those items that Mr. Lawson either misappropriated or was apparently otherwise in possession of, missing military surplus items included nine central processing units with an aggregate value of \$21,586, a cutting machine valued at \$17,520, and a vertical floor compressor valued at \$8,000, among numerous other items. In addition to those items identified as missing, auditors and LESO representatives could not locate or identify numerous other items of lesser value, including items which appeared to be interchangeable or otherwise difficult to identify, or items that appeared to have no discernable personal or business purpose.

⁴ This amount includes the engine analyzer and truck hitch apparently misappropriated by Mr. Lawson and addressed in Legal Issue 3.

RECOMMENDATION:

To help prevent loss of valuable municipal property, by either misappropriation or other means, town officials should require that property be stored in secure locations and inventoried regularly. Under no circumstances should town officials or employees be allowed to maintain or store town equipment or other property at their homes or places of business, with the obvious exception of equipment which may be needed to carry out their official municipal duties.

2. **FINDING: Military surplus property used for purposes other than law enforcement and by governmental entities other than the town**

Military surplus property totaling at least \$272,643 was being used in direct violation of allowable uses under conditions of the program. When the town began participating in the military surplus program, its representative, former police chief Dale Scalf, was required to sign an agreement detailing the obligations and responsibilities assumed by the town for participating in the program. The first condition cited in the agreement is that the town agrees to maintain the “property for use as intended for law enforcement activities only.”

However, auditors and LESO representatives identified numerous items located in departments other than the police department and apparently being used for purposes other than law enforcement activities. Among the military surplus items being used in violation of allowable use were several items that were no longer even in the possession of the Town of Surgoinsville, including a power saw, diesel generator, and safe located at the Surgoinsville Utility District⁵ and a GPS device and night vision capable video camera in the possession of the local sheriff’s department.

In addition to those items which were not being used in the town’s law enforcement efforts, we noted numerous small items, which may have a discernable law enforcement purpose, but which were acquired in such quantities as to defy reason. For instance, from January 1, 2006, through March 31, 2007, through the efforts of Mr. Scalf, the town acquired 31 bayonets and combat knives with an aggregate value of \$1,573, despite having a relatively small police force.⁶ On the town’s behalf, Mr. Scalf also acquired 22 digital cameras and camcorders with an aggregate value of \$33,070, 50 jackets with an aggregate value of \$6,585, and 52 pairs of pants and trousers with an aggregate value of \$2,900 during the same 15-month period.

⁵ One of the commissioners of the utility district, Hanes Cooper, was also the town mayor at the time the items located at the utility district were acquired.

⁶ At the inception of our investigative audit, the town employed five part-time and two full-time police officers, including the police chief.

RECOMMENDATION:

To demonstrate good faith and avoid sanctions, including possible expulsion from state and federal programs, town officials should ensure compliance with all provisions of any government programs in which the town may be enrolled. Particularly regarding the military surplus program, since the only cost incurred is the cost of shipping or travel, it is important that town officials realize that, just because items can be acquired does not mean that they should be acquired. Once acquired, all military surplus should be used in strict accordance with the town's agreement with LESO.

3. **FINDING: Oil-burning furnace gifted to vice-mayor without being declared surplus by board or being sold at auction**

Former vice-mayor Otis Lawson was apparently given an oil-burning furnace previously used by the public works department. When former mayor Hanes Cooper decided to replace the furnace, Mr. Lawson obtained possession of it. In an interview with Mr. Lawson, he indicated that Mr. Cooper gave him the furnace when the town obtained a grant to replace it. However, there is no provision in state law authorizing municipal officials to simply give away public property, particularly to other municipal officials or employees. The *Internal Control and Compliance Manual for Tennessee Municipalities*, Title 1, Chapter 4, addresses aspects of safeguarding assets. Any responsible system of asset safeguards would include development of a policy regarding the disposal of public property and prevent the appearance of any impropriety in the disposal of such property.

RECOMMENDATION:

To fulfill their fiduciary duty to the town and avoid the appearance of impropriety, town officials should prohibit the gifting of town property, particularly to town employees and officials. Surplus town property should be declared as such and disposed of at auction.

4. **FINDING: Contract with former town attorney apparently backdated and entered into without board approval**

Former mayor Hanes Cooper apparently entered into a backdated contract with a local attorney, Crystal Goan-Klumb, to provide legal representation to the Town of Surgoinsville. The board of mayor and aldermen was apparently unaware of the existence of the contract, believing the town was still represented by Foster Law Office, for whom Ms. Goan-Klumb had previously worked. The contract was clearly initially dated November 1, 2007, but the year was apparently subsequently changed to 2006. Ms. Goan-Klumb was paid \$1,203 pursuant to the backdated contract.

In an interview with Mr. Cooper, he stated that Ms. Goan-Klumb was no longer employed by Foster Law Office when the contract was signed. However, Ms. Goan-Klumb did not leave Foster Law Office until March 2007, indicating the contract was not entered into until sometime after March 1, 2007. This conclusion is bolstered by the fact that the town recorder was not provided a copy of the contract until May 10, 2007, by which time Mr. Cooper had been out of office for more than four months and had no authority to conduct town business. When asked about the timing of the contract, Ms. Goan-Klumb claimed that the contract was entered into while she was still working for Foster Law Office. However, the contract clearly referred to Foster Law Office as “past employer” and “previous employer” and stated that Ms. Goan-Klumb “has severed all ties with the Foster Law Office.” Additionally, the managing partner of the firm has asserted that he would not have allowed Ms. Goan-Klumb to personally enter into such a contract while still employed by his firm.

RECOMMENDATION:

To fulfill their fiduciary duty to the town, town officials should ensure that former officials do not enter into contracts for any services on behalf of the town and should consider possible legal recourse to recover fees paid to Ms. Goan-Klumb under the backdated contract.

5. **FINDING: Contract with Brothers Repair apparently backdated and entered into without board approval**

Former vice-mayor Otis Lawson apparently entered into a back-dated contract with Brothers Repair for the service and repair of town vehicles. In interviews with Mr. Lawson and the co-owner of Brothers Repair, Erik Logan, both stated that the town awarded the contract to Brothers Repair based on work the company did on a town truck used for the removal of leaves. Mr. Logan stated that the work included repair of a turn signal and Mr. Lawson stated that the work had to be performed over the weekend. Mr. Lawson further stated that former mayor Hanes Cooper consented to the arrangement. Section 1-202 of the town’s municipal code states, “The mayor shall execute all contracts as authorized by the board of mayor and aldermen.” No board authorization of the contract could be located in minutes of meetings of the board.

The contract with Brothers Repair was dated October 16, 2006. The first invoice paid by the town was dated November 18, 2006, for work on a town truck. Included on the invoice were the notations “Replace turn signal switch” and “Labor working on Sat. & Sunday to have this ready by Monday,” closely matching the memories of Mr. Logan and Mr. Lawson regarding the nature and urgency of the work performed. However, both Mr. Logan and Mr. Lawson cited the work performed on the truck as the reason for entering into the contract. If so, the contract clearly would have been entered into at some point after November 18, 2006, not in the preceding month. On November 17, 2006, one day prior to the date of the invoice, the Town of Surgoinsville was officially notified that

Hanes Cooper and Otis Lawson both lost their bids for re-election. Therefore, it appears that not only was the contract backdated, but also that Mr. Cooper and Mr. Lawson were both aware at the time the contract was entered into that they would no longer be serving on the board of mayor and aldermen.

RECOMMENDATION:

To fulfill their fiduciary duty to the town, officials should ensure that all contracts are brought before the full board of mayor and aldermen for a vote. Any contracts not approved by vote of the board should not be recognized.

6. **FINDING: Deliberate circumvention of bid process by former mayor**

During the calendar year 2006, former mayor Hanes Cooper apparently deliberately circumvented the town's purchasing policy, requiring at least three checks totaling \$7,485 to be issued to L & W Paving for the paving of town streets. Each of the checks was issued in the amount of \$2,495, only \$5 below the town's threshold for required bids. Even though the three payments were each for work performed on the same paving project, the work and payments were apparently broken up to avoid the necessity for bids. The town's unwritten purchasing policy provided that expenditures over \$2,500 be let out for bid and Sections 6-56-304 and 6-56-306, *Tennessee Code Annotated*, require that expenditures of \$2,500 or more be let out for bid unless the municipal governing body adopts an ordinance increasing the bid limit.

RECOMMENDATION:

To obtain the best price, comply with the town's purchasing policy and state law, and avoid the appearance of impropriety, town officials should ensure that all expenditures exceeding the town's bid limit are properly let out for bid.