



Office of the Washington State Auditor
Pat McCarthy

Fraud Investigation Report

Town of Hatton

For the Investigation Period January 1, 2016 through July 31, 2018

Published July 25, 2019

Report No. 1023959





**Office of the Washington State Auditor
Pat McCarthy**

July 25, 2019

Mayor and Town Council
Town of Hatton
Hatton, Washington

Report on Fraud Investigation

Attached is the official report on a misappropriation at the Town of Hatton. On July 30, 2018, the Town notified the State Auditor's Office of a potential loss of public funds. This notification was submitted to us under the provisions of state law (RCW 43.09.185).

This report contains the results of our investigation of the former clerk/treasurer's unallowable activities at the Town from January 29, 2016, through July 6, 2018. The purpose of our investigation was to determine if a misappropriation had occurred.

Our investigation was performed under the authority of state law (RCW 43.09.260) and included procedures we considered necessary under the circumstances.

If you are a member of the media and have questions about this report, please contact Director of Communications Kathleen Cooper at (360) 902-0470. Otherwise, please contact Fraud Manager Sarah Walker at (509) 454-3621.

Pat McCarthy
State Auditor
Olympia, WA

cc: Valerie Phillips, Clerk-Treasurer

FRAUD INVESTIGATION REPORT

Investigation Summary

On July 30, 2018, the Mayor of the Town of Hatton notified our Office regarding a potential loss of public funds as required by state law.

We initiated an investigation and determined a payment misappropriation totaling \$6,289 and questionable expenditures totaling \$15,783 occurred at the Town between January 29, 2016, and July 6, 2018. We also identified penalties and fines related to overdue payroll tax totaling \$455 that have been assessed to the Town. The table below shows the misappropriation and questionable amounts by category.

The Town filed a report with Adams County Sheriff's Office on July 14, 2018. We will refer this report to the Adams County Prosecuting Attorney's Office.

Summary of results		
Area of investigation	Misappropriation	Questionable
Payroll	\$5,301	\$14,032
Travel reimbursements	\$0	\$145
Debit card	\$988	\$1,526
Cash receipts	\$0	\$80
TOTAL	\$6,289	\$15,783

Background and Investigation Results

The Town, located in Adams County, operates on an annual budget of approximately \$116,000. The Town provides water and garbage services to about 100 citizens. The Town operates under a mayor-council form of government. The elected five-member Council is the Town's oversight body that sets and approves all Town policies. The Town currently has two part-time employees who handle the day-to-day operations. The Clerk/Treasurer position is responsible for monitoring the day-to-day operations, and preparing and processing all disbursement transactions.

Our investigation focused on utility billing, general disbursements, payroll disbursements, and bank account debit card activity. The former Mayor resigned July 2018, and the City appointed

the new Mayor in August 2018. The Clerk/Treasurer was hired in 2014, and her employment ended in July 2018. Our investigation found the following:

Payroll

The Clerk/Treasurer was responsible for preparing and recording the payroll within the accounting system, calculating payroll withholding taxes and authorizing Town payroll checks, including her own. The Mayor was responsible for reviewing and approving payroll. During our review of payroll, we identified the following:

- 909.2 questionable hours worked by the Clerk/Treasurer, totaling \$14,032. Those hours include working from home and going to training/conferences without pre-approval.
- On June 15, 2017, a check for \$1,000 was issued to the Clerk/Treasurer as a personal loan. In the July 10, 2017, council meeting, she requested a \$1,000 loan from the Town Council to assist her with a down payment for the purchase of a van. The request was not approved. We determined this to be a misappropriation of public funds.
- On July 9, 2018 a check totaling \$4,301 was improperly issued to the Clerk/Treasurer. The notes left by the Clerk/Treasurer noted this was to reimburse her for the federal income tax withholdings held from her paychecks over years 2015 to 2018. Calculation notes show tax withholdings amounted to \$5,151 but she reduced \$850 related to the repayment of the personal loan taken in June 2017. We identified \$4,301 to be misappropriated disbursements.

General disbursements/travel reimbursements

The Clerk/Treasurer was responsible for traveling to a nearby Town to deposit funds and purchase office supplies for the Town Hall. During our review of Town's disbursements, we noted the Clerk/Treasurer requested reimbursement for mileage driven while traveling for Town business. We reviewed all travel reimbursement requests made by the Clerk/Treasurer between January 2016 and July 2018. We identified \$145 in disbursements to the Clerk/Treasurer that lacked support, making that amount questionable.

Debit card

The Clerk/Treasurer was issued a Town debit card for Town purchases. The Town has a debit card policy, which states the card can be used for office supply purchases and requires any other purchase over \$50 to have prior authorization by the Council. We reviewed all debit card transactions between January 2016 and July 2018. We identified \$988 of misappropriated funds related to purchases of fuel and food using the Town's debit card. In addition, we identified \$3,810 of unallowable debit card transactions, each of which exceeded \$50 but lacked prior authorization, and \$1,526 of questionable debit card transactions. Some were not supported by receipts and we could not determine if others were for a valid business purpose.

Cash receipts

The Clerk/Treasurer was responsible for receipting utility payments, recording utility payments on utility accounts, and depositing funds at the bank. During our review of the Town's bank statement and utility account note cards, we identified a utility payment of \$80 in February 2017 that we could not match to Town bank deposit records.

Utility billing

The Clerk/Treasurer was responsible for preparing utility bills and applying fees and fines to utility accounts when applicable. Based on our review, late fees totaling \$393 were not properly applied to the Clerk/Treasurer's personal account. We also found the Mayor had \$363 in late fees not applied to his personal account.

Penalties/fines

The Clerk/Treasurer was responsible for making sure the Town paid its quarterly payroll income tax withholding to IRS regularly. According to the Town's new Clerk/Treasurer, the Town has not paid payroll taxes since 2015. As of April 8, 2019, the IRS has assessed penalties and interest related to overdue payroll taxes from the first quarter of 2015, totaling \$455.

On April 9, 2019, we interviewed the former Clerk/Treasurer, who said that in June 2017 she discussed the \$1,000 loan with the Mayor and various Council members. She said the Mayor approved it, and she paid it back. She further said that she never understood how to report payroll withholding to the Internal Revenue Service (IRS) and did prepare a check to herself for reimbursement of her 2015 to 2018 federal tax withholdings.

Control Weaknesses

Internal controls at the Town were not adequate to safeguard public resources. We found the following weaknesses allowed the misappropriation to occur:

- Disbursement controls, including controls over payroll, were not adequate to ensure payments were allowed, supported by receipts or timesheets, and for a Town purpose.
- The Council did not perform a secondary review of the Clerk/Treasurer's debit card transactions and did not make sure the Clerk/Treasurer submitted quarterly income tax reports to the IRS.
- Cash receipting controls were not adequate to ensure funds receipted were deposited to the Town's bank account.
- The Town lacked adequate oversight over utility billing to make sure the Clerk/Treasurer consistently applied late fees to accounts in accordance with Town policy.

Recommendations

We recommend the Town strengthen internal controls over disbursements, cash receipting and utility billing, including oversight and monitoring in order to safeguard public resources and comply with Town policies. We also recommend the Town strengthen monitoring over the Clerk/Treasurer position to ensure timely submission of quarterly income tax report to IRS.

We further recommend the Town seek recovery of the misappropriated \$6,289 and related investigation costs of \$14,878 from the former Clerk/Treasurer and/or its insurance bonding company, as appropriate. Any compromise or settlement of this claim by the Town must be approved in writing by the Attorney General and State Auditor as directed by state law (RCW 43.09.260). Assistant Attorney General Matt Kernutt is the contact person for the Attorney General's Office and can be reached at (360) 586-0740 or mattk1@atg.wa.gov. The contact for the State Auditor's Office is Brandi Pritchard, Assistant Director of Local Audit, who can be reached at (360) 489-4591 or Brandi.Pritchard@sao.wa.gov.

Town's Response

The Town of Hatton would like to thank the Washington State auditor's team for helping us execute this audit. We are very happy to see this concluded and move forward. We, with the recommendations from the audit team have placed some internal controls that will prevent the town from being in this position from here on out. We have made available to the clerk Quick Books and sufficient training on how to best utilize this software. We have ensured the clerk has the proper training and resources to complete the day-to-day tasks as well as any and all financial reporting. We plan on moving forward and staying in compliance. Thank you very much.

State Auditor's Office Remarks

We thank Town officials and personnel for their assistance and cooperation during the investigation.

ABOUT THE STATE AUDITOR'S OFFICE

The State Auditor's Office is established in the state's Constitution and is part of the executive branch of state government. The State Auditor is elected by the citizens of Washington and serves four-year terms.

We work with our audit clients and citizens to achieve our vision of government that works for citizens, by helping governments work better, cost less, deliver higher value, and earn greater public trust.

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We take our role as partners in accountability seriously, and provide training and technical assistance to governments, and have an extensive quality assurance program.

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