


A Fraud Case Study: Tarpley Shop Utility District

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2024 CCFO and CMFO Training




TENNESSEE COMPTROLLER OF THE TREASURY

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Fraud in Tennessee

- **What We Do:**
 - The Division of Investigations investigates fraud, waste, and abuse allegations in government and publicly funded entities. The division reports the results of its investigations, including significant internal control and compliance deficiencies noted during the investigations, to the appropriate parties.
- **How We Are Notified:**
 - Hotline Phone Calls, Fraud Reporting Forms, Audits, Contracted Auditors, Other Agencies, Tips



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Division of Investigations
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<https://www.comptroller.tn.gov/office-functions/investigations.html>

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Report Fraud, Waste and Abuse

Session will timeout after 60 minutes
*Indicates a required field
To download a pdf version of the form, please click the button below and mail to address printed on the bottom of the form
PDF

Please provide name of the entity, agency, or department involved *

Entity, Agency, or Department

Please provide the names, job titles, and departments of the individuals involved:

Full Name * Title * Department *

If you don't know, please type "Unknown" If you don't know, please type "Unknown" If you don't know, please type "Unknown"

Add Another

Please select county *

Select County

Please select the type of entity, agency or department *

Select Organization Type

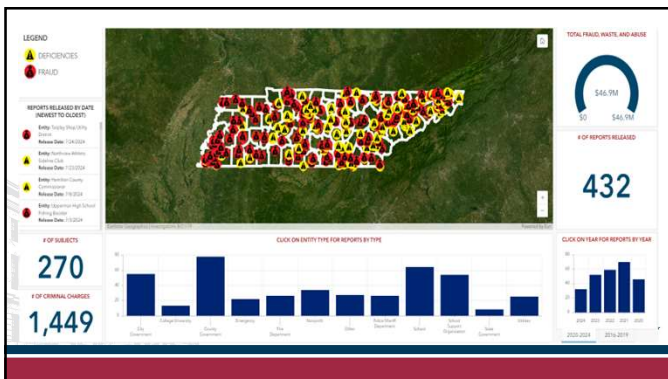
In your own words, please describe the who, what, when, where, how and nature of the fraud, waste or abuse (please provide as much detail as possible, including names and positions of those involved; nature of the fraud, waste or abuse; dates and times; amounts; records involved; how the fraud was discovered; etc.)

Incident Description

Upload supporting documentation including PDF's, Word, Excel and the most common audio and video formats

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Recognize Risk

- Employee theft takes many forms:
 - Theft of collections
 - Theft through disbursements
 - Misuse of assets
 - Payroll schemes




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Theft of Collections

- Voiding receipts; adjusting accounts = stealing cash
- Not documenting receipts and stealing cash
- Intercepting collections through payment platforms




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Theft through Disbursements

- Personal purchases using:
 - Checks
 - Debit/credit cards
 - Payment platforms
- Fabricating invoices; fictitious payees = stealing thru disbursements




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Misuse of Assets & Inventory

- Use of government equipment for personal use
- Theft of inventory
 - Fuel
 - Building materials




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Payroll Schemes

- Overstating hours worked = time theft; "borrowing funds"
- Writing yourself additional paychecks
- Fictitious employees



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Separation of Duties

Review	Reconcile	Approve
Purchase Orders	Dual Signature Checks	

Separation of Duties

- Financial responsibilities should be separated so that no one employee has complete control of a financial transaction.
- When duties cannot be separated, a detailed review of related activities is required as a control activity.




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Objectives


- Follow the investigative process
- Identify opportunities for misappropriation due to internal control issues
- Determine how to improve internal controls



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Tarpley Shop Utility District





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Tarpley Shop Utility District

- Water service provider
- ~1,200 customers
- Located in Giles County

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Background

- The district was governed by a three-person board of directors.
- The district did not have any employees but had a management contract with Byrd Construction, a local company.



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Contract with Byrd Construction

- Original contract signed in 1984
- The original owners of Byrd Construction were the parents of Freddie Byrd.
- When they passed away, Freddie Byrd took over Byrd Construction and, therefore, took over operating the district.
- Freddie Byrd was the general manager, and his wife was the district's office manager.

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Allegation

- Comptroller of the Treasury employee in the Local Government Finance Division submitted an allegation regarding Tarpley Shop Utility District, Byrd Construction, and Freddie Byrd.
- During an investigation conducted by the Utilities Management Review Board, they found multiple instances where the board of directors allowed Byrd Construction to run the district improperly.

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Allegation – Examples of Issues

- District paid for Freddie Byrd’s cell phone – “always on call”
- District bought Freddie Byrd a truck – “always on call”
- The district pays all the gas for the truck.
- Did not properly bid out a project of new water meters for the district.

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Initial Review

- Scope of investigation is not limited to the content of the allegation
 - Understand and consider all areas of risk
- Preliminary interviews conducted with board member, Freddie Byrd, and Byrd’s wife.
- Financial records collected from the district’s office

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Contract with Byrd Construction

- Original contract was executed in 1984
- Contract term of 1 year – never formally renewed

III
TERM OF EMPLOYMENT
 The term of this Agreement shall be from July 1st, 1984, ending June 30th, 1985.

IN WITNESS WHEREOF, the parties have executed this Agreement as of July 1st, 1984.
 TARPLEY SHOP UTILITY DISTRICT

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Terms of the Contract: Compensation

- Byrd Construction received a flat fee of \$8,500 each month for managerial services provided to the district.
- Byrd Construction also billed the district every month for maintenance work on water leaks. The district provided the material, but Byrd Construction would send a bill for labor and use of any machinery needed.

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Terms of the Contract: Bids for Projects

- Any projects costing more than \$5,000 required:
 - Bidding process, OR
 - Board approval for Byrd Construction to perform the project

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Management Responsibilities

- | | |
|---|--|
| <ul style="list-style-type: none"> • General Manager - Freddie Byrd: <ul style="list-style-type: none"> • Reading meters • Pulling water samples • Repairs to water system • Overseeing projects • Billing | <ul style="list-style-type: none"> • Office Manager - Byrd's Wife: <ul style="list-style-type: none"> • Customer adjustments • Collecting customer payments • Bookkeeping • Paying Bills |
|---|--|

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Byrd Construction's Services

- Backhoe Work
- Trenching
- Septic Tanks
- Water and Sewer Lines
- "Meter to house"

STATEMENT IN ACCOUNT WITH
BYRD CONSTRUCTION
 Backhoe Work • Trenching
 Septic Tanks • Water & Sewer Lines
 1901 Columbia Highway • Pulaski, TN 38478
 931.703.6228

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Equipment

- The district owned three trucks.
- All machinery and tools were owned by Byrd Construction, and Byrd Construction would bill the district for the use of those assets.
- The district purchased any materials needed for repairs.

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District-Owned Vehicles

- 1998 Ram 1500 – not in use, unrepairable
- 2001 Ford F150 – Byrd Construction employee drives to read meters for the district
- 2015 Ford F150 – Freddie Byrd drives

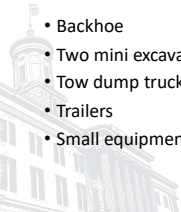
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Byrd Construction's Equipment

- Backhoe
- Two mini excavators
- Tow dump trucks
- Trailers
- Small equipment



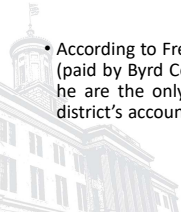
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Disbursement Process: Charge Accounts

- According to Freddie Byrd, his wife (office manager), an office worker (paid by Byrd Construction), his son (paid by Byrd Construction), and he are the only ones allowed to charge goods and services to the district's account for vendors.



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Disbursement Process: Charge Accounts

<ul style="list-style-type: none"> • Materials/inventory <ul style="list-style-type: none"> • C&C Maintenance Supply • General Supply • G&C Supply • Core & Main 	<ul style="list-style-type: none"> • Fuel <ul style="list-style-type: none"> • May Oil • Co-Op
--	--

- Equipment & Vehicle Maintenance
 - Co-Op
 - Eslick Tractor
 - NAPA



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Disbursement Process: Checks

- Checks required two board member signatures.
- Board members would review invoices and sign checks at every monthly meeting.
- The office manager would mail the signed checks to the appropriate vendor.

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Fuel Purchases

- Co-Op
 - Simply tell clerk that the purchase would be charged to the district's account
 - No signatures or documentation of who made the purchases
- May Oil
 - Receipts had to be signed and turned in to May Oil office for each purchase
- Board members reviewed monthly invoices from Co-Op and May Oil
 - Co-Op fuel purchases were not questioned by board members
 - Board members did not review May Oil receipts

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Collections

- Byrd's wife handled the majority of collections and deposits
 - The other office employee would occasionally assist her
- All customers were listed on deposit slips


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Inventory

- Inventory other than pipe was kept at the district's office
 - Materials needed to make repairs (bands, saddles, meters, etc)
- All pipe was kept at Byrd Construction's office
- Byrd typically kept some gravel at Byrd Construction's office



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Identifying Risk Areas


Management Contract

Disbursements

Collections

Equipment

Inventory



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Identifying Risk Areas


Management Contract

Disbursements

Collections

Equipment

Inventory




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Risks: Management Contract

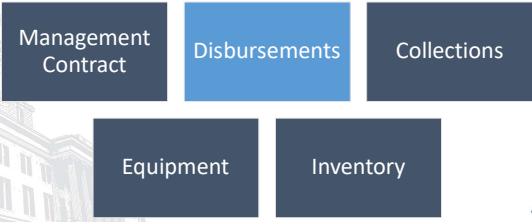
- No updated contract since it ended in 1985
 - Changes made over the years by the Board not included in contract
 - Policies become unclear and unenforceable
- Conflict of interest between the district and Byrd Construction
 - Automatically giving work to Byrd Construction
 - Potentially creating unnecessary work for Byrd Construction
 - Avoiding bids



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Identifying Risk Areas



Management Contract Disbursements Collections

Equipment Inventory




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Risks: Lack of Purchasing Policy

- No defined purchasing policy
- No restrictions on purchases

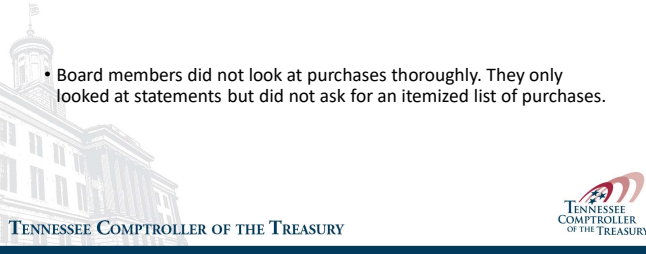


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Risks: Limited Purchasing Oversight

- Board members did not look at purchases thoroughly. They only looked at statements but did not ask for an itemized list of purchases.

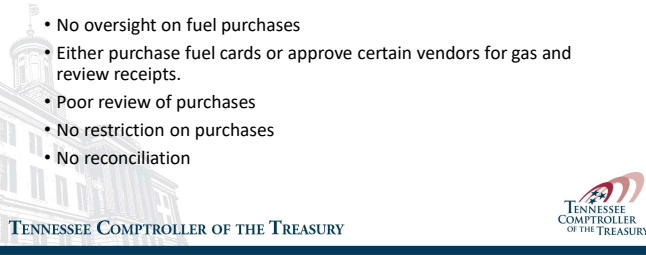


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Risks: Fuel Purchases

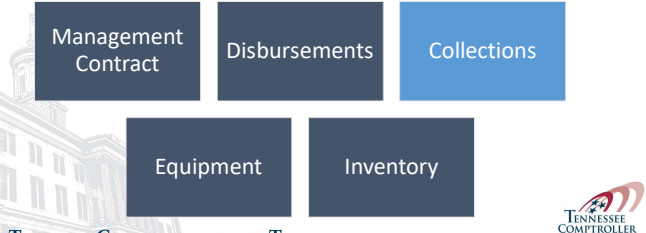
- No oversight on fuel purchases
- Either purchase fuel cards or approve certain vendors for gas and review receipts.
- Poor review of purchases
- No restriction on purchases
- No reconciliation



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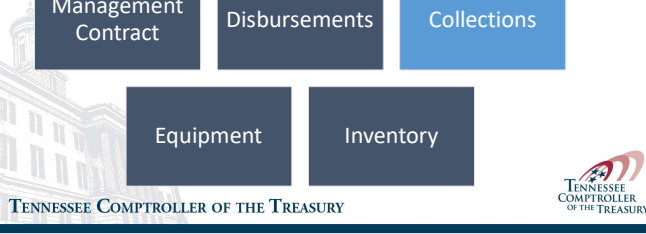
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Identifying Risk Areas



Management Contract Disbursements Collections

Equipment Inventory

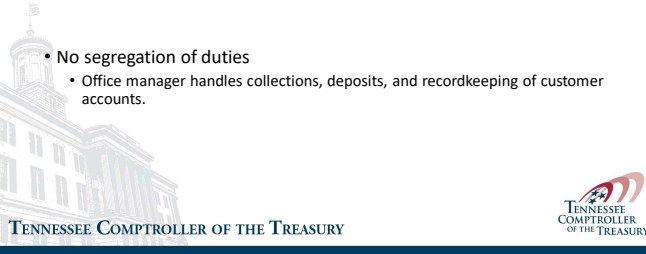


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Risks: Collections

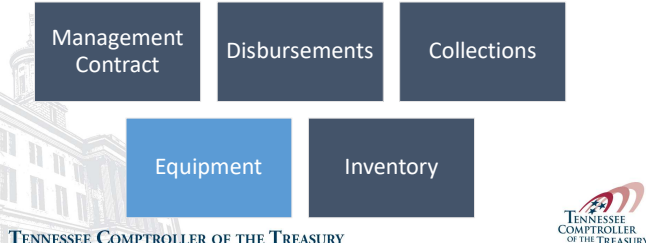
- No segregation of duties
 - Office manager handles collections, deposits, and recordkeeping of customer accounts.



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Identifying Risk Areas

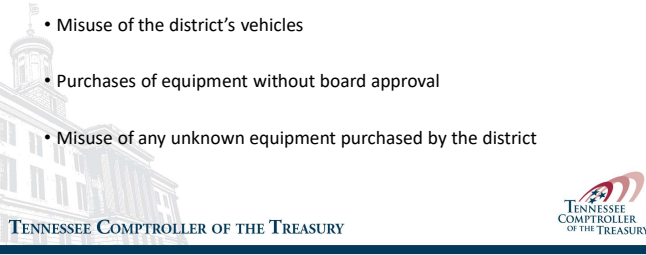


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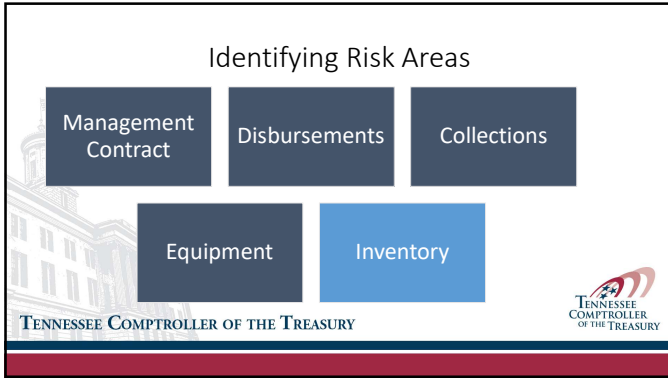
Risks: Equipment

- Misuse of the district's vehicles
- Purchases of equipment without board approval
- Misuse of any unknown equipment purchased by the district



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Risks: Inventory

- Inventory being kept at Byrd Construction's facility
- Potential theft of district inventory for use in Byrd Construction's private projects

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Investigation: Disbursements

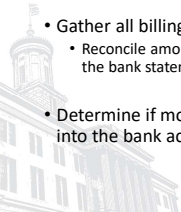
- Gather all invoices and receipts
 - Reconcile invoices to checks to identify missing documentation
 - Obtain any missing invoices from vendors
- Review invoices/receipts and determine the purpose of each purchase
- Determine if each purchase was for the benefit of the district or not

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Investigation: Collections

- Gather all billing registers and bank statements
 - Reconcile amounts recorded in the billing register to amounts deposited into the bank statement
- Determine if money that was collected from customers was deposited into the bank account



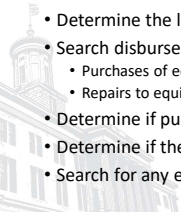
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Investigation: Equipment

- Determine the location of all district equipment
- Search disbursements for anything related to equipment
 - Purchases of equipment
 - Repairs to equipment
- Determine if purchases of equipment were approved by the board
- Determine if the district paid for repairs to non-district equipment
- Search for any evidence of misuse of district equipment




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Investigation: Inventory

- Lack of records would make it difficult to reconcile inventory purchases to use of inventory for repairs
- Invoices were reviewed for any unusual inventory items purchased



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Investigation Result #1

Freddie Byrd made \$7,939.35 in personal purchases.

Byrd's Personal Purchases	
Co-Op	\$ 1,055.09
Core and Main	413.10
Eslick Tractor	1,689.67
G&C Supply	3,433.78
NAPA	1,347.91
Total Personal Purchases	\$ 7,939.55

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Personal Purchases

- Most of these purchases included:
 - Battery-operated tools
 - Small equipment
 - Repairs
 - Vehicle parts that did not fit district-owned vehicles

Byrd's Personal Purchases	
Co-Op	\$ 1,055.09
Core and Main	413.10
Eslick Tractor	1,689.67
G&C Supply	3,433.78
NAPA	1,347.91
Total Personal Purchases	\$ 7,939.55

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Personal Purchases

Apparel	10/09/20	2886987	JDF	21350345	MEN'S MUDS STAY COOL MID BL	2,0000	40,0000	80,00	
<i>Purchase made by Byrd using district funds for boots from the Co-Op</i>									
Exhibit 2									
Apparel	03/06/22	1272247	JDF	1001155	DRYSHOD HAYMAKER HI BROW	1,0000	138,9600	139,96	
								Apparel Total	139,96
<i>Purchase made by Byrd using district funds for boots from the Co-Op</i>									
Exhibit 3									
	02/01/23	1492253	JDF	12622	4X TRAILER BEARING KIT (BT7)	1,0000	65,2000	65,20	
<i>Purchase made by Byrd using district funds for a trailer bearing kit from the Co-Op</i>									

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Investigation Result #2

- Unable to confirm if all purchases were used exclusively for official district purposes.

Questionable Purchases	
C&C Maintenance Supply	\$ 109.90
Co-Op	1,058.78
Core and Main	69.97
Eslick Tractor	4,949.47
G&C Supply	2,259.61
General Supply	137.95
NAPA	86.57
O'Reillys	272.96
Tri-Green	904.43
Total Questionable Purchases	\$ 9,849.64

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Questionable Purchases

Purchase of a new lawn mower for \$4,600 from Eslick.

- The purchase was not recorded or approved in the board minutes
- Invoice not included in the district's documentation.
- Unclear if the mower was used solely for district purposes.

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Discussions with Byrd about Equipment

Byrd was interviewed three times

- First interview: The district has no equipment other than trucks
- Second interview: The district purchased a mower which is kept at Byrd's house under his carport.
- Third interview: The district has a mower, leaf blower, weed eater, chainsaw, and three trucks.


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Investigation Result #3

Tarpley Shop Utility District made questionable fuel purchases totaling at least \$25,035.79.



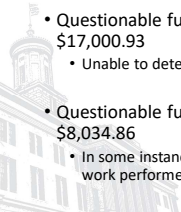
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Investigation Result #3

- Questionable fuel purchases made at the Co-Op totaled at least \$17,000.93
 - Unable to determine who made purchases from Co-Op
- Questionable fuel purchases made at the May Oil totaled at least \$8,034.86
 - In some instances, Byrd allowed relatives to purchase fuel purportedly for work performed for the district.




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Indictment

The Giles County Grand Jury indicted Freddie Byrd on one count of theft over \$2,500 but less than \$10,000, and two counts of official misconduct.




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INTERNAL CONTROL AND COMPLIANCE DEFICIENCIES

Our investigation revealed deficiencies in internal controls and compliance, some of which contributed to Byrd's ability to perpetrate his misappropriation without prompt detection. These deficiencies included:




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Deficiency #1

The district failed to maintain supporting documentation for some disbursements

- There was a period of 18 consecutive months for which investigators could not locate any documentation of disbursements.
- Requiring and maintaining adequate documentation, such as invoices or receipts, allows the board members to verify that all disbursements are proper and for the exclusive benefit of the district, and decreases the risk of errors or misappropriations occurring without prompt detection




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Deficiency #2

The board failed to document internal controls

- Tenn. Code Ann. § 9-18-102(a)(2) requires that utility districts "establish and maintain internal controls, which shall provide reasonable assurance that...funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation."



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Deficiency #3

The board failed to authorize a formal written agreement with Byrd Construction for management services

- Lack of a formal written agreement with Byrd Construction since July 1, 1985.
- The agreement was not updated as the responsibilities and expectations of the district and Byrd Construction changed.
- Without a current formal written agreement, neither the district nor Byrd Construction had accurate guidelines detailing performance responsibilities, obligations, liabilities, or expectations. The lack of an authorized formal written agreement between parties increased the district's liability risks

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Deficiency #4

The board failed to properly oversee district operations, which contributed to multiple purchasing deficiencies

- No formal written purchasing policy
- The board did not solicit competitive bids for a new meter project
- The district paid sales tax in some instances
- No written policies for the use of district credit cards
- The board did not always acquire two board members' approval for purchases
- Invoices or other supporting documentation were not maintained
- Failure to adequately account for fuel usage

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Deficiency #5

The board failed to approve or document adjustments to customer utility bills

- No policy or process to review and approve adjustments to customer utility bills
- The board failed to ensure that personnel maintained a record of all adjustments to customers' utility bills or document that adjustments were approved
- The district's computerized software was not used for adjustments and therefore did not always match what was billed to the customer
- Lack of documentation increased the risk of misappropriation

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Deficiency #6

A conflict of interest existed between the district and Byrd Construction

- Byrd Construction had a contract to manage the district. The district did not receive bids on the repair work but allowed Byrd Construction to perform all leak repairs.
- Managing the district and giving all leak repair work to Byrd Construction created an inherent conflict of interest, or at least an appearance of impropriety in that Byrd was not acting solely in the district's best interest.
- Tenn. Code Ann. § 12-4-101 states, "it is unlawful for any person whose duty is to overlook, or in any manner to superintend any work in [a] utility district... to be directly interested in any such contract."

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Key Takeaways

- Written policies and procedures are important
 - If it isn't written down, it didn't happen!
 - Verbal policies are difficult to enforce
 - Make sure any agreements are updated and renewed
- Establish internal controls and ensure they function properly
 - Preventive, Detective, and Corrective – not just one level!

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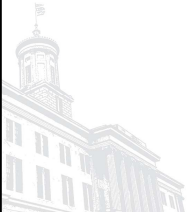
Consider Your Processes

- What processes lack proper controls?
- Is there a higher level of oversight you can add?
- Are controls being performed properly?

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Questions?

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Submit Allegations to the Comptroller's Office

- Fraud Hotline: 1-800-232-5454
- Online Fraud Reporting Form:
<https://apps.cot.tn.gov/ants/submission/submit>

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Thank You!

- Jessica Hannah
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 - Jessica.Hannah@cot.tn.gov
- Forrest Richardson
 - 615-736-6068
 - Forrest.Richardson@cot.tn.gov

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