

# STATE OF NORTH CAROLINA

OFFICE OF THE STATE AUDITOR

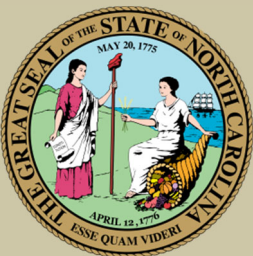
BETH A. WOOD, CPA



## TOWN OF ELIZABETHTOWN

ELIZABETHTOWN, NORTH CAROLINA

INVESTIGATIVE AUDIT REPORT  
JULY 2023



**NC OSA**  
The Taxpayers' Watchdog

# EXECUTIVE SUMMARY

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## **PURPOSE**

The North Carolina Office of the State Auditor initiated an investigative audit in response to four allegations received regarding the Town of Elizabethtown (Town). An allegation related to payroll taxes not being withheld for the former Town Manager<sup>1</sup> was substantiated.

While investigating the initial allegations received, investigators discovered that the Town was unable to provide supporting documentation<sup>2</sup> for a significant number of charges made to the Town credit card assigned to the former Town Manager.

## **BACKGROUND**

The Town is in Bladen County, North Carolina. According to the Town's website, approximately 3,500 residents live in the Town.

For the year ended June 30, 2022, the Town had a budget of \$6.6 million for its General Fund and Utility Fund.

## **KEY FINDING**

- The Town did not withhold the required amount of payroll taxes for the former Town Manager in accordance with federal and state requirements.
- The Town was unable to provide supporting documentation for charges made to the Town's credit card that was assigned to the former Town Manager.

## **KEY RECOMMENDATIONS**

- The Town Council should ensure that the Town has procedures in place to accurately withhold payroll taxes for all employees.
- The Town Council should ensure that no financial obligation of the Town is being paid without supporting documentation that ensures the obligation was included in the budget and is for valid a Town purpose.

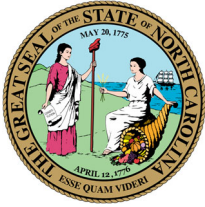
*Key findings and recommendations are not inclusive of all findings and recommendations in the report.*

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<sup>1</sup> The former Town Manager was employed with the Town from February 2008 through March 2021.

<sup>2</sup> Supporting documentation could include purchase orders, invoices, receipts, or other records to support an expenditure's valid business purpose.

STATE OF NORTH CAROLINA  
**Office of the State Auditor**



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## **AUDITOR'S TRANSMITTAL**

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The Honorable Roy Cooper, Governor  
Members of the North Carolina General Assembly  
Town Council, Town of Elizabethtown

Ladies and Gentlemen:

Pursuant to North Carolina General Statutes § 147-64.6(c)(16) and § 147-64.6B, we have completed an investigative audit of allegations concerning the Town of Elizabethtown. The results of our investigative audit, along with recommendations for corrective action, are contained in this report.

Copies of this report have been provided to the Governor, the Attorney General, and other appropriate officials in accordance with N.C.G.S. § 147-64.6(c)(12). We appreciate the cooperation received from the management and employees of the Town of Elizabethtown during our investigative audit.

Respectfully submitted,

A handwritten signature in cursive script that reads "Beth A. Wood".

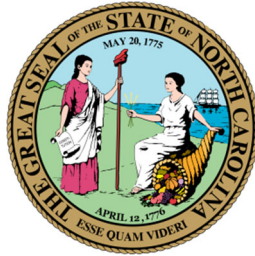
Beth A. Wood, CPA  
State Auditor



**Beth A. Wood, CPA**  
**State Auditor**

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# BACKGROUND

The North Carolina Office of the State Auditor initiated an investigative audit in response to four allegations received regarding the Town of Elizabethtown (Town). An allegation related to payroll taxes not being withheld for the former Town Manager<sup>3</sup> was substantiated.

While investigating the initial allegations received, investigators discovered that the Town was unable to provide supporting documentation<sup>4</sup> for a significant number of charges made to the Town credit card assigned to the former Town Manager.

Our investigative audit procedures included the following:

- Review of applicable policies and procedures.
- Examination and analysis of available documentation related to the allegations.
- Interviews with current and former personnel from the Town.

This report presents the results of the investigative audit. The investigative audit was conducted pursuant to North Carolina General Statutes § 147-64.6(c)(16) and § 147-64.6B. This report does not constitute an audit or attestation engagement conducted in accordance with generally accepted government auditing standards.

The Town is in Bladen County, North Carolina. According to the Town's website, approximately 3,500 residents live in the Town.

For the year ended June 30, 2022, the Town had a budget of \$6.6 million for its General Fund and Utility Fund.

The Town operates under a council-manager form of government, whereby the Town Council, which includes the mayor, serves as the legislative body of the Town in establishing policy and law.

The Town Manager is appointed by the Town Council to carry out the day-to-day administrative operations of the Town.

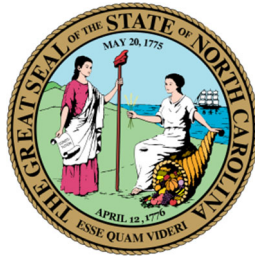
The former Finance Director<sup>5</sup> reported to the former Town Manager. The former Finance Director was responsible for the Finance Department, which included the Town Accountant.

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<sup>3</sup> The former Town Manager was employed in that position from February 2008 through March 2021.

<sup>4</sup> Supporting documentation could include purchase orders, invoices, receipts, or other records to support an expenditure's valid business purpose.

<sup>5</sup> The former Finance Director was employed with the Town from February 2015 through June 2020.



# **FINDINGS AND RECOMMENDATIONS**

## **1. TOWN DID NOT WITHHOLD THE REQUIRED AMOUNT OF PAYROLL TAXES FOR FORMER TOWN MANAGER**

The Town of Elizabethtown (Town) did not withhold the required amount of payroll taxes for the former Town Manager<sup>6</sup> in accordance with federal and state requirements.<sup>7</sup> As a result, the Town is liable for the amount that was required to be withheld.<sup>8</sup>

Changes to the former Town Manager's withholdings were made in the Town's payroll system. However, employees with access to make changes in the payroll system denied making any changes that would have impacted the former Town Manager's withholdings.

Federal and state requirements<sup>9</sup> require employers to withhold a required amount of taxes from employee paychecks.

### **Required Amount of Payroll Tax Not Withheld**

The Town did not withhold the required amount of payroll taxes for the former Town Manager in accordance with federal and state requirements.

Employers are required to withhold employment taxes, such as federal and state income taxes, Social Security, and Medicare, from employees' paychecks based on the number of withholding allowances<sup>10</sup> that the employee claims. The Town remits the taxes to federal and state agencies.

Investigators reviewed the tax withholdings for the former Town Manager for tax years 2018 through 2020.<sup>11</sup> The withholdings were compared to the required withholding amounts<sup>12</sup> and investigators found the following:<sup>13</sup>

- Federal Income Tax withheld was deficient by \$28,892 (98% of what was required).
- North Carolina Income Tax withheld was deficient by \$1,384 (9% of what was required).
- Social Security Tax withheld was deficient by \$1,200 (5% of what was required).
- Medicare Tax withheld was deficient by \$129 (2% of what was required).

### **Resulted in Liability for the Town**

As a result of the Town not withholding the correct amount of payroll taxes, the Town is liable for the amount that was required to be withheld.

<sup>6</sup> The former Town Manager was employed in that position from February 2008 through March 2021.

<sup>7</sup> Federal – 26 U.S. Code § 3402(c)  
State – N.C.G.S. § 105-163.2

<sup>8</sup> Federal – 26 CFR 31.3403-1  
State – N.C.G.S. § 105-163.8

<sup>9</sup> Federal – 26 U.S. Code § 3402(c)  
State – N.C.G.S. § 105-163.2

<sup>10</sup> A withholding allowance is an exemption that lowers the amount of income tax you must deduct from an employee's paycheck. A larger number of withholding allowances means smaller income tax deductions, and a smaller number of allowances means larger income tax deductions.

<sup>11</sup> The former Town Manager separated from his employment with Elizabethtown in March 2021.

<sup>12</sup> 26 U.S. Code § 3402(c) is the requirements for federal withholdings. N.C.G.S. 105-163.2(b) is the requirement for state withholdings.

<sup>13</sup> The percentages below represent the percent of the total amount that was required to be withheld. For example, in the first bullet, \$28,892 is 98% of what was required to be withheld.



Specifically, federal and state regulations<sup>14</sup> state that the Town is liable for the required withholdings whether or not the withholdings were collected from the employee.

### **Caused by Unauthorized Change to Payroll System**

The required amount of payroll taxes were not withheld in accordance with state and federal regulations because of two changes made in the Town's payroll system that impacted the amount of the withholdings. According to the former Town Manager, he **did not** authorize the changes.

In December 2015, the former Town Manager's federal income tax withholding was changed in the payroll system from \$236.32 per pay period to \$0.00 per pay period. Then, in April 2016, the federal income tax withholding was changed from \$0.00 per pay period to \$8.30 per pay period.

According to the former Finance Director,<sup>15</sup> the **only** two employees who had access to make changes in the payroll system were the former Finance Director himself and the former Town Accountant.

Both the former Finance Director and the former Town Accountant denied making the changes to the system.

Additionally, the payroll system did not capture the identification of who made the changes in the system. Investigators reviewed a report from the payroll system that listed changes made to the former Town Manager's payroll profile. There were no initials or other identifying information on the report which would indicate who made the changes.

### **Federal and State Law Specify the Amount of Taxes to Be Withheld**

Federal and state requirements state that employers must withhold taxes from employee paychecks based on the number of withholding allowances claimed by the employee.

Specifically, the United States Code of Regulations<sup>16</sup> requires employers to deduct and withhold taxes in accordance with tables or procedures described by the Secretary of the Internal Revenue Service (IRS). The IRS provides instructions on how to calculate the amount of taxes to withhold in the annual Publication 15 and 15-T.

Additionally, North Carolina General Statutes<sup>17</sup> require employers to deduct and withhold state income taxes and provides instructions on how to calculate the amount of taxes withheld.

### **Recommendations**

The Finance Director should ensure that no changes are made to the payroll system without proper authorization.

Town Management should upgrade the payroll system to ensure that there is an audit trail that identifies everyone who makes changes to the payroll system.

The Town Council should ensure that the Town has procedures in place to accurately withhold payroll taxes for all employees.

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<sup>14</sup> Federal – 26 CFR 31.3403-1  
State – N.C.G.S. § 105-163.8

<sup>15</sup> The former Finance Director was employed with the Town from February 2015 through June 2020.

<sup>16</sup> 26 U.S. Code § 3402

<sup>17</sup> N.C.G.S. § 105-163.2

## **2. NO SUPPORT FOR CREDIT CARD CHARGES**

While investigating the initial allegations received, investigators discovered that the Town of Elizabethtown (Town) was unable to provide supporting documentation<sup>18</sup> for charges made to the Town's credit card assigned to the former Town Manager.<sup>19</sup> As a result, the Town potentially paid for purchases that did not have a valid Town purpose.

The Town did not have adequate processes in place, including written policies and procedures, regarding the use of credit cards.

To comply with state law,<sup>20</sup> receipts and a documented business purpose must accompany all credit card expenditures.

### **Credit Card Charges Without Supporting Documentation**

The Town was unable to provide supporting documentation for credit card charges made to the Town's credit card assigned to the former Town Manager. The Town was unable to provide documentation to show that the charges/purchases had been included in the budget and were made for a valid Town purpose.

From January 2019 to April 2021, the Town Manager's Town-issued credit card was used to make 137 purchases totaling \$14,117. Investigators reviewed all purchases and found that the Town was unable to provide supporting documentation for 119 purchases (87%) totaling \$8,448.

Specifically,

- 64 purchases totaling \$5,173 had an itemized receipt but lacked documentation to support a valid Town purpose.
- 55 purchases totaling \$3,275 had neither an itemized receipt nor documentation to support a valid Town purpose.

### **Resulted in Funds Potentially Misused**

As a result of the lack of documentation for the credit card charges, the Town potentially paid for purchases that did not have a valid Town purpose.

### **Caused by Inadequate Processes for Issuing Payments**

The Town did not have any written policies and procedures regarding the use of the Town credit card. Therefore, there was no Town policy that required that supporting documentation be submitted for credit card charges.

Additionally, the Town was unable to provide documentation to support that the card charges were for purchases that had been included in the budget and were for a valid Town purpose before the credit card bill was paid.

### **State Law Required Expenses Be Supported and Reviewed**

To comply with state law, receipts and a documented business purpose should accompany all credit card expenditures.

<sup>18</sup> Supporting documentation could include purchase orders, invoices, receipts, or other records to support an expenditure's valid business purpose

<sup>19</sup> The former Town Manager was employed with the Town from February 2008 through March 2021.

<sup>20</sup> N.C.G.S. § 159-28

First, North Carolina General Statute<sup>21</sup> states that no obligation can be incurred unless the budget ordinance includes an appropriation for the obligation and funds are available to pay the obligation.

Further, North Carolina General Statute<sup>22</sup> requires payments made by the Town to be preaudited before the payment is made to ensure that the expenditure was included in the budget ordinance and there are funds available to pay the expenditure.

Without reviewing documentation to support the amount and the business purpose for the expenditure, the Finance Director would not be able to ensure that the credit card purchases were for items included in the Town's budget ordinance and that funds were available to cover the expense.

The University of North Carolina at Chapel Hill School of Government<sup>23</sup> specifically states that the preaudit process applies to electronic payments, such as credit cards, and "that all ... credit card ... transactions must be preaudited on a transaction-by-transaction basis."<sup>24</sup>

Second, the North Carolina State Constitution requires expenses to be incurred only for a public purpose. Specifically, the Constitution states:

The General Assembly may enact laws whereby the State, any county, city or town, and any other public corporation may contract with and appropriate money to any person, association, or corporation for the accomplishment of public purposes only.

Without supporting documentation, it is unclear if these credit card charges were for the accomplishment of public purposes only.

### **Recommendations**

The Town Council should establish a comprehensive policy for credit card usage that includes, **but is not limited to**, requirements such as:

- Itemized receipts for purchases.
- A documented Town purpose for purchases.
- Validation that the purchases were included in the Town's budget.
- Review of all credit card documentation (including receipts and the documented business purpose) before approval of the payment of a credit card bill.

The Town Council should ensure the Finance Director and Town employees are following the comprehensive policy for credit card usage.

The Town Council should ensure that no financial obligation of the Town is being paid without supporting documentation that ensures the obligation was budgeted for and is for a valid Town purpose.

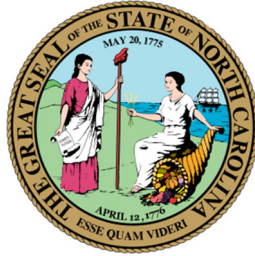
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<sup>21</sup> N.C.G.S. § 159-28(a)

<sup>22</sup> N.C.G.S. § 159-28(a1)

<sup>23</sup> Coates' Canons NC Local Government Law, Preauditing Electronic Transactions Just Got (A Little) Easier, published 03/23/2018, by Kara Millonzi.

<sup>24</sup> The North Carolina Local Government Commission Memorandum 2018-05 addressed the preaudit process for electronic payments, including credit cards. It states that units of government can be exempt from the preaudit certificate requirements on electronic transactions if the unit has (1) adopted a resolution authorizing the unit to engage in electronic payments, (2) adopted policies and procedures for electronic obligations, and (3) included in the policy the basic procedures for preauditing obligations incurred by electronic transactions. The Town has not met these requirements, and therefore is not exempt from the preaudit process for credit cards.



# **STATE AUDITOR'S RESPONSE**

The Office of the State Auditor (OSA) strives to provide reports with complete and accurate information to the Governor, the General Assembly, the citizens of North Carolina, and the stakeholders of the Town. When the response of an auditee potentially **obscures** an issue, **misleads** the reader, or **minimizes** the importance of auditor findings and recommendations, OSA provides clarifications regarding the auditee's response.

In their response to this investigative report, the Town of Elizabethtown (Town) made statements that may mislead the reader.

To ensure complete and accurate information, OSA offers the following clarifications.

**No Support for Credit Card Charges**

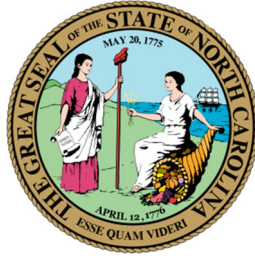
In the response from the Town of Elizabethtown (Town), the Town stated,

The Town was able to verify through records provided by the credit card company all charges made by the Town Manager during this time period as authorized and approved purchases.

**This is misleading.**

The records provided by the credit card company would not include the business purpose for the credit card charges. Therefore, the Town would not have documentation to ensure that the charges were for valid business purposes.

Again, OSA provides this clarifying information to ensure that this report provides complete and accurate information to the Governor, the General Assembly, the citizens of North Carolina, and the stakeholders of the Town.



# **RESPONSE FROM THE TOWN OF ELIZABETHTOWN**

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TOWN OF  
**ELIZABETHTOWN**  
TOWN MANAGER

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June 23, 2023

The Honorable Beth Wood, CPA  
State of North Carolina  
Office of the State Auditor  
20601 Mail Service Center  
Raleigh, North Carolina 27699-0600

Reference: Response to Draft of Investigative Audit Report June 2023

Dear Ms. Wood:

This letter is in response to the draft of an investigative audit report which was provided to the Town of Elizabethtown Town Council on June 22, 2023. Representatives from the Office of the State Auditor presented and explained the findings to two members of the Council along with the Town Manager, Finance Director, Town Clerk and Town Attorney.

The Town of Elizabethtown Town Council has reviewed and acknowledged the findings listed in the draft investigative audit report. The findings reported occurred under a former Town Manager and Finance Director. The current Town Manager and Finance Director have implemented internal controls to address the findings detailed in the draft investigative audit report.

**FINDING #1 – TOWN DID NOT WITHHOLD THE REQUIRED AMOUNT OF PAYROLL TAXES FOR THE FORMER TOWN MANAGER**

The Town of Elizabethtown did not withhold the required amount of payroll taxes for the former Town Manager in accordance with federal and state requirements.

**RECOMMENDATIONS –**

- The Finance Director should ensure that no changes are made to the payroll system without the proper authorization.
- Town Management should upgrade the payroll system to ensure that there is an audit trail that identifies everyone who makes changes to the payroll system.
- The Town Council should ensure that the Town has procedures in place to accurately withhold payroll taxes for all employees.

*“The mission of the Town of Elizabethtown is to deliver cost effective services that promote public health and safety and enhance the quality of life of all citizens.”*



RESPONSE –

- The Town and former Town Manager have corrected all payroll taxes in accordance with federal and state requirements.
- As of April of 2021, no changes have been made to any employee's withholding in the payroll system without written authorization from the employee.
- Town Management is in the process of replacing the Town's financial software. The new software will ensure there is an audit trail of all changes made and who makes them in the payroll system.
- All taxes were paid by the employee prior to the completion of the audit or issuance of the draft report.

FINDING #2 – NO SUPPORT FOR CREDIT CARD CHARGES

The Town of Elizabethtown (Town) was unable to provide supporting documentation for charges made to the Town's credit card assigned to the former Town Manager.

RECOMMENDATIONS –

- The Town Council should establish a comprehensive policy for credit card usage that includes, but is not limited to, requirements such as:
  - Itemized receipts for purchases.
  - A documented Town purpose for purchases.
  - Validation that the purchases were included in the Town's budget.
  - Review of all credit card documentation (including receipts and the documented business purpose) before approval of payment of credit card bill.
- The Town Council should ensure the Finance Director and Town employees are following the comprehensive policy for credit card usage.
- The Town Council should ensure that no financial obligation of the Town is being paid without supporting documentation that ensures the obligation was budgeted for and is for a valid Town purpose.

RESPONSE –

- The Town is confident that the former Town Manager provided the proper documentation to the Finance Director during his tenure. The Town was unable to produce all the receipts for the credit card charges during the audited period, however, there was nothing on the credit card statements that caused Town management to question the legitimacy of the purchases by the former Town Manager. The Town was able to verify through records provided by the credit card company all charges made by the Town Manager during this time period as authorized and approved purchases.

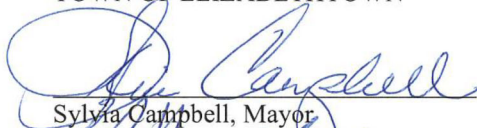


- The Town has established a policy that no charges to the Town's credit card are to be paid without an itemized receipt detailing the purchases. If the employee has lost the receipt, they must sign a statement to that effect with a detailed list of what was purchased.
- The Town is in the process of preparing a Fiscal Policies and Procedures Manual for the Town of Elizabethtown which will include policies and procedures for the use of the Town's credit card. Once the Fiscal Policies and Procedures Manual has been adopted by the Town of Elizabethtown Town Council, the Town Manager and Finance Director will review it periodically to ensure the relevance and compliance with governing North Carolina General Statutes and Generally Accepted Accounting Principles. The Town Manager will report, advise, and recommend revisions to the manual to the Town of Elizabethtown Town Council as appropriate.

Based on the implemented procedures, the Town of Elizabethtown Town Council states, with a high degree of confidence, that there is minimal risk of similar findings occurring in the future. The Town of Elizabethtown Town Council appreciates the efforts made by the Office of the State Auditor.

Respectfully Submitted,

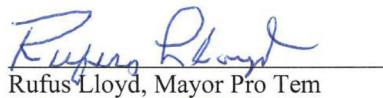
TOWN OF ELIZABETHTOWN

  
Sylvia Campbell, Mayor

  
Howell Clark, Council Member

  
Paula Greene, Council Member

  
Herman Lewis, Council Member

  
Rufus Lloyd, Mayor Pro Tem

  
Rich Glenn, Council Member

  
Ricky Leinwand, Council Member

# ORDERING INFORMATION

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For additional information contact the  
North Carolina Office of the State Auditor at:  
**919-807-7666**



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This investigation required 1,082 hours at an approximate cost of \$123,860.