

PART II, FINDINGS RELATING TO THE FINANCIAL STATEMENTS

Findings and recommendations as a result of our examination are presented below. We reviewed these findings and recommendations with management to provide an opportunity for their response. The written responses of the director of finance and sheriff are paraphrased in this report. Other officials offered oral responses to certain findings and recommendations; however, these oral responses have not been included in this report.

OFFICE OF FINANCE DIRECTOR

FINDING 02.01 PURCHASE ORDERS WERE NOT ISSUED

(Internal Control – Reportable Condition Under Government Auditing Standards)

The office did not issue purchase orders for all applicable purchases. Purchase orders are necessary to control who has purchasing authority and to document purchasing commitments.

RECOMMENDATION

The office should issue purchase orders for all applicable purchases.

MANAGEMENT'S RESPONSE — DIRECTOR OF FINANCE

Effective July 1, 2002, all departments are required to issue purchase orders for all purchases.

FINDING 02.02 THE OFFICE DID NOT SOLICIT COMPETITIVE BIDS FOR ROAD DEPARTMENT PURCHASES

(Noncompliance Under Government Auditing Standards)

Competitive bids were not solicited for purchases of culverts and tires for the Road Department. The Uniform Road Law, Section 54-7-113, Tennessee Code Annotated, requires competitive bids on all Road Department purchases estimated to exceed \$5,000.

RECOMMENDATION

Competitive bids should be solicited for all purchases estimated to exceed \$5,000 in the Road Department.

FINDING 02.03 GENERAL LEDGER PAYROLL DEDUCTION ACCOUNTS WERE NOT RECONCILED WITH SUBSIDIARY PAYROLL RECORDS
(Internal Control — Reportable Condition Under Government Auditing Standards)

General ledger payroll deduction accounts for the General Fund and Solid Waste/Sanitation Fund were not reconciled with subsidiary payroll records on a monthly basis. Unidentified balances had accumulated in the following withholding accounts: Federal Income Tax, Social Security, Medicare, Retirement, Insurance, Garnishments, and Deferred Compensation. The failure to reconcile general ledger payroll deduction accounts with employee payroll deductions resulted in errors and omissions in the reporting and paying of employee deductions.

RECOMMENDATION

All general ledger payroll deduction accounts should be reconciled monthly with subsidiary payroll records to ensure that amounts withheld from employees' wages are properly accounted for and remitted to the appropriate agency.

MANAGEMENT'S RESPONSE — DIRECTOR OF FINANCE

In the future, all general ledger payroll deductions will be reconciled monthly with subsidiary payroll records.

FINDING 02.04 THE OFFICE HAD DEFICIENCIES IN PAYROLL PROCEDURES
(A. and F. Internal Control — Reportable Condition Under Government Auditing Standards; B., C., D., and E — Noncompliance Under Government Auditing Standards)

A review of payroll procedures for the General Fund disclosed the following deficiencies:

- A. In numerous instances throughout the year, payroll checks for employees and county officials were processed and distributed to these individuals before the end of the pay period. In some instances, these checks were processed up to 25 days in advance. As a result of this procedure, these employees and county officials were paid for work that had not yet been performed.
- B. Income tax was not withheld from the paychecks of two county employees who were paid from the General Fund. Written authorization forms (W-4s) were on file reflecting that withholding taxes should have been withheld from their paychecks.
- C. On June 20, 2002, an employee of the County Executive's Office was improperly paid \$6,000.96 for 41 days of unused sick leave and 15 days of unused vacation leave. Although the county executive approved this payment, it was made in violation of

the office's personnel policies since there are no provisions for employees to receive payment for unused sick leave. Also, unused vacation leave can only be paid upon separation from service. It should also be noted that prior to receiving this payment this employee's leave records reflected 91 days of sick leave and 25 days of vacation leave. The personnel policies of the County Executive's Office provide for employees to accumulate a maximum of 50 sick days and 25 vacation days. Therefore, this employee was also allowed to accumulate sick days over the maximum allowed by the personnel policy. We have reflected this improper payment as an accounts receivable in the financial statements of this report. On November 8, 2002 this employee signed an agreement to refund \$5,541.89 to the county which represents the net amount of the \$6,000.96 she was paid. The employee agreed to pay the \$5,541.89 in three installments beginning with \$541.89 on December 6, 2002, \$2,500.00 on June 6, 2003, and \$2,500.00 on June 6, 2004.

- D. On December 14, 2001, an employee of the General Sessions Judge's Office was improperly paid \$959.16 for ten vacation days and two personal days. This office's leave policy does not provide for employees to be reimbursed for unused vacation and personal days. This improper payment has been reflected as an accounts receivable in the financial statements of this report. On November 6, 2002 the General Sessions Judge refunded \$885.78 to the county which represents the net amount of the \$959.16 paid to the employee.
- E. On August 23, 2002, an employee of the County Clerk's Office was improperly paid \$1,571.30 for 19 days of unused sick leave when she resigned her position with the clerk's office. This office's leave policy does not provide for employees to be reimbursed for any unused sick leave upon leaving employment. On November 6, 2002 this former employee signed an agreement to refund \$1,428.32 to the county which represents the net amount of the \$1,571.30 she was paid. This former employee will reimburse the county through 36 monthly installments with the first installment beginning December 5, 2002.
- F. Duties were not segregated adequately among employees in the Finance Department for payroll functions. One employee was responsible for all payroll functions, including the signing of payroll warrants.

RECOMMENDATION

The office should not issue payroll checks prior to the end of the payroll period. Federal income tax should be withheld in every instance. Sick and vacation leave should be maintained in accordance with the office's personnel policies. County officials should adhere to their personnel policies. To strengthen internal controls over payroll operations, the office should segregate payroll duties among employees.

MANAGEMENT'S RESPONSE — DIRECTOR OF FINANCE

- A. Steps will be taken immediately to stop paying officials and employees in advance of work performed.

- B. In the future, proper withholdings will be withheld from employees' salaries.
- F. Duties will be segregated among employees in the Finance Department. In future, the finance director and official of each department will sign payroll warrants.

OFFICE OF ROAD SUPERVISOR

FINDING 02.05 THE ROAD DEPARTMENT DID NOT MAINTAIN A SYSTEM TO ACCOUNT FOR THE USE OF SOME MATERIALS
(Internal Control — Reportable Condition Under Government Auditing Standards)

The Road Department had a system to account for materials, such as rock and asphalt, used on state-aid road projects. However, the department did not have a system to account for materials used on other types of road projects. The failure to maintain a system to document the use of road materials results in a loss of control over the assets and increases the risk of inventory loss.

RECOMMENDATION

The Road Department should develop and implement a system to account for materials used on all types of road projects.

FINDING 02.06 THE ROAD DEPARTMENT HAD INADEQUATE CONTROLS OVER INVENTORY
(Internal Control – Reportable Condition Under Government Auditing Standards)

The Road Department did not maintain adequate controls over inventory. Our audit revealed the following deficiencies:

- A. Some assets were not tagged or clearly marked as property of the Road Department, and some assets were not listed on the department's inventory.
- B. Procedures were not in place to ensure that newly acquired assets were added to the inventory list and that personnel independent of maintaining inventory records verified the list periodically.

Generally accepted accounting principles require accountability for county-owned assets.

RECOMMENDATION

To improve controls over inventory, the Road Department should tag all assets, ensure that the inventory lists include property tag numbers, implement procedures for adding assets to inventory records, and ensure that personnel independent of the record-keeping process periodically verify inventory records.

FINDING 02.07 **THE ROAD DEPARTMENT PERFORMED WORK ON PRIVATE PROPERTY**
(Noncompliance Under Government Auditing Standards)

The road supervisor used county equipment, manpower, and gravel to construct a parking lot for a local church. He stated that he did this work believing the Road Department could perform work for a nonprofit organization. Section 54-7-202, Tennessee Code Annotated, prohibits road departments from doing work on private property.

RECOMMENDATION

The Road Department should not perform work on private property.

OFFICE OF DIRECTOR OF SCHOOLS

FINDING 02.08 **THE OFFICE PROCESSED AND DISTRIBUTED PAYROLL CHECKS INAPPROPRIATELY**
(Internal Control – Reportable Condition Under Government Auditing Standards)

The School Department processed and distributed payroll checks to some employees in the Central Office on the tenth day of each month for that month's salary, in effect paying these employees for work that had not yet been performed.

RECOMMENDATION

School officials should not issue payroll checks to employees before they earn the compensation.

OFFICE OF TRUSTEE

FINDING 02.09 **THE TRUSTEE DID NOT FOLLOW HIS OFFICE PERSONNEL POLICY
(Noncompliance Under Government Auditing Standards)**

The trustee placed one of his employees on administrative leave with pay after being injured in an accident during working hours. This employee was paid \$7,573.13 while on administrative leave. However, the office personnel policy does not provide for paid administrative leave. On November 6, 2002 this employee refunded \$6,118.36 to the county which represents the net amount of \$7,573.13 she was paid.

RECOMMENDATION

The trustee should make payroll payments in accordance with the office personnel policy.

OFFICE OF CIRCUIT, GENERAL SESSIONS, AND JUVENILE COURTS CLERK

FINDING 02.10 **EXECUTION DOCKET TRIAL BALANCES DID NOT RECONCILE WITH CASH JOURNAL ACCOUNTS
(Noncompliance Under Government Auditing Standards)**

At June 30, 2002, the circuit and general sessions courts clerk had prepared trial balances of execution docket cause balances, as required by Section 18-2-103, Tennessee Code Annotated (TCA). However, these trial balances did not reconcile with cash journal accounts by substantial amounts, and we were unable to trace amounts from the docket trial balance to the dockets. Therefore, we were unable to determine if the clerk had complied with provisions of the Unclaimed Property Act, Section 66-29-110, TCA. This statute provides that any funds held by the court for one year and unclaimed by the owner are considered abandoned. Section 66-29-113, TCA, further requires these funds to be reported and paid to the state Treasurer's Office.

RECOMMENDATION

The execution docket trial balances should be reconciled with cash journal accounts. Any funds held by the court for one year and unclaimed by the owner are considered abandoned and should be reported and paid to the state Treasurer's Office in compliance with state statute.

FINDING 02.11 EXCESS FEES WERE NOT REPORTED AND PAID TO THE COUNTY IN COMPLIANCE WITH STATE STATUTE
(Noncompliance Under Government Auditing Standards)

The circuit and general sessions courts clerk did not report and pay excess fees to the county in compliance with Section 8-22-104, Tennessee Code Annotated. This statute requires excess fees to be reported and paid to the county quarterly and requires the clerk to retain sufficient fees to operate the office for three months. Excess fees exceeded statutory limits for each quarter during the year.

RECOMMENDATION

The clerk should report and pay excess fees to the county in compliance with state statute.

FINDING 02.12 THE OFFICE HAD DEFICIENCIES IN COMPUTER SYSTEM BACK-UP PROCEDURES
(Internal Control — Reportable Condition Under Government Auditing Standards)

The following weaknesses regarding computer system back-up procedures in the Offices of Circuit, General Sessions, and Juvenile Courts Clerk were identified:

- A. System backups were not stored off site. In the event of a disaster, all back-up data could be destroyed, resulting in costly delays in generating and recording information accounted for through the automated process.
- B. A back-up log was not maintained. If system backups are not labeled and inventoried systematically, discrepancies may occur and affect the integrity of system backups in the event of a hardware or software failure.

RECOMMENDATION

Weekly backups should be rotated off site on a weekly basis. Year-end backups should be stored off site and retained indefinitely. Some possibilities for an off-site storage location would be another county office building with a fireproof vault or a safe deposit box at a local bank. Furthermore, a current log of all backups that includes label descriptions, date of creation, contents, and storage location should be maintained.

FINDING 02.13 SUFFICIENT USER DOCUMENTATION WAS NOT MAINTAINED
(Internal Control – Reportable Condition Under Government Auditing Standards)

The circuit, general sessions, and juvenile courts clerk did not maintain formal user documentation pertaining to the court software. This documentation is necessary to provide users with information system inputs, application processing requirements, output definitions, and system recovery. Inadequate documentation may result in inaccurate and inefficient processing of applications.

RECOMMENDATION

The office should maintain user documentation pertaining to all software applications. Management should contact their vendor and obtain current user documentation for all components of their computer system.

FINDING 02.14 THE OFFICE DID NOT DEVELOP A DISASTER RECOVERY PLAN
(Internal Control – Reportable Condition Under Government Auditing Standards)

The circuit, general sessions, and juvenile courts clerk did not develop a disaster recovery plan to assist in re-creating its data processing environment in the event of a disaster. Without a formal, written plan, critical computerized applications could be disrupted indefinitely until the system could be repaired or a back-up facility could be found and made operational.

RECOMMENDATION

Management should develop and regularly update a disaster recovery plan defining procedures for personnel to follow in the event of a major hardware or software failure, or temporary or permanent destruction of facilities. The plan should contain provisions for a contingency operations site, as well as the adequate backup of data files, system programs, user documentation, supplies, and computer hardware so that operations could continue as normally as possible. A copy of the plan should be kept in a secure area within the office, as well as at a secure, off-site location.

OFFICE OF CLERK AND MASTER

FINDING 02.15 **EXCESS FEES WERE NOT REPORTED AND PAID TO THE COUNTY IN COMPLIANCE WITH STATE STATUTE
(Noncompliance Under Government Auditing Standards)**

The clerk and master did not report and pay excess fees to the county in compliance with Section 8-22-104, Tennessee Code Annotated. This statute requires excess fees to be reported and paid to the county quarterly and requires the clerk and master to retain sufficient fees to operate the office for three months. Excess fees exceeded statutory limits for each quarter during the year.

RECOMMENDATION

The clerk and master should report and pay excess fees to the county in compliance with state statute.

OTHER FINDINGS AND RECOMMENDATIONS

FINDING 02.16 **RECORDS WERE NOT MAINTAINED FOR GENERAL FIXED ASSETS
(Internal Control — Material Weakness Under Government Auditing Standards)**

Henderson County did not inventory, value, and record its general fixed assets (buildings, equipment, etc.), as required by generally accepted accounting principles. The Governmental Accounting Standards Board has adopted Statement 34, which will become effective in Henderson County for the year ending June 30, 2004. Statement 34 places an even greater emphasis on the need to maintain general fixed asset records.

RECOMMENDATION

Henderson County should inventory, value, and record its general fixed assets in accordance with generally accepted accounting principles.

MANAGEMENT'S RESPONSE — DIRECTOR OF FINANCE

We are in the process of establishing records for all general fixed assets in Henderson County.

FINDING 02.17 DESIGNATED SITUS-BASED TAXES WERE INADEQUATE TO FUND RURAL FIRE PROTECTION
(Material Noncompliance Under Government Auditing Standards)

During the year, Henderson County expended \$322,509 from the General Fund to provide fire protection service to rural areas of the county. The County Commission has designated certain situs-based taxes in the General Fund to be used to fund rural fire protection. However, these situs-based taxes amounted to \$187,036 during the year and were not enough to cover operating expenditures of \$322,509 for rural fire protection. Therefore, the property taxes of all county citizens, living both inside and outside Lexington city limits, helped to fund this service, and citizens living within the City of Lexington paid for fire protection service in both the city and rural areas.

RECOMMENDATION

In addition to the designated situs-based taxes, Henderson County should consider establishing fire districts and taxing annually the property owners of each district to pay that district's share of the total budget of the countywide departments.

FINDING 02.18 DUTIES WERE NOT SEGREGATED ADEQUATELY IN THE OFFICES OF TRUSTEE, COUNTY CLERK, JUVENILE COURT CLERK, CLERK AND MASTER, AND SHERIFF
(Internal Control – Reportable Condition Under Government Auditing Standards)

Duties were not segregated adequately among the officials and employees in the Offices of Trustee, County Clerk, Juvenile Court Clerk, Clerk and Master, and Sheriff. Employees responsible for maintaining accounting records were also involved in receipting, depositing, and disbursing funds, and/or reconciling bank statements. We realize that due to limited resources and personnel, management may not be able to properly segregate duties among employees. However, our professional standards require that we bring this matter to the reader's attention in this report.

MANAGEMENT'S RESPONSE – SHERIFF

I will address this problem immediately.