

## **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 finance director and director of schools 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.

### **CARTER COUNTY AND CARTER COUNTY SCHOOL DEPARTMENT**

#### **FINDING 03.01      **GOVERNMENT-WIDE FINANCIAL STATEMENTS WERE NOT PRESENTED IN ACCORDANCE WITH GENERALLY ACCEPTED ACCOUNTING PRINCIPLES****

(Material Noncompliance Under Government Auditing Standards)

Carter County and the Carter County School Department did not identify and determine the historical value of their capital assets and the related depreciation amounts of these assets. Therefore, Carter County and the Carter County School Department were unable to provide the information necessary to prepare government-wide financial statements for all of their activities, as required by Governmental Accounting Standards Board (GASB) Statement No. 34, Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments. GASB is the standard-setting body for accounting principles that state and local governments are required to follow. As a result of this omission, Carter County’s and the Carter County School Department’s financial statements are not presented in accordance with generally accepted accounting principles; thus, we have issued an adverse opinion on their financial statements.

The Office of the Comptroller of the Treasury, State of Tennessee, requires governments that do not implement GASB Statement 34 to issue a financial report in compliance with Financial Reporting Standards for County Governments, Component Units of County Governments, and Special School Districts That Do Not Implement Governmental Accounting Standards Board Statement 34, established by the Comptroller of the Treasury. Carter County’s and the Carter County School Department’s financial statements are presented in compliance with these requirements.

#### **RECOMMENDATION**

Carter County and the Carter County School Department should present government-wide financial statements in conformity with generally accepted accounting principles, and should compile and maintain records that properly account for their capital assets. These records should document the historical cost of their capital assets and the related depreciation amounts of these assets. This information is necessary to present the financial statements in accordance with generally accepted accounting principles.

#### **MANAGEMENT’S RESPONSE – FINANCE DIRECTOR**

I believe it would be easier to implement GASB 34 after the county’s accounting functions are centralized. Furthermore, we can gain valuable insight from the counties that just recently implemented GASB 34 in the East Tennessee region. The director of finance is in

the process of drafting an implementation plan and is researching the option of contracting with a private vendor for initial infrastructure asset valuations.

---

## **OFFICE OF FINANCE DIRECTOR**

### **FINDING 03.02      **DEFICIENCIES WERE NOTED IN THE IMPLEMENTATION OF THE COUNTY FINANCIAL MANAGEMENT SYSTEM OF 1981****

(Material Noncompliance Under Government Auditing Standards)

The county did not fully implement the provisions of the Financial Management System of 1981 by August 1, 2003, as required by state statute. During the 2001-02 fiscal year, Carter County adopted the provisions of the County Financial Management System of 1981 – Section 5-21-101, et seq., Tennessee Code Annotated (TCA). This act establishes a central system to include budgeting, accounting, purchasing, payroll, and cash management covering all county departments. Section 5-21-127, TCA, requires that the system be fully implemented by August 1 of the second fiscal year following adoption of the system. During the current fiscal year, the finances of the county and the Highway Department were consolidated into one central finance department. Subsequent to June 30, 2003, most financial operations of the Carter County School Department were also included. However, the following deficiencies were noted in the implementation of the provisions of the act:

- A. The minutes of meetings of the Financial Management Committee did not reflect the approval of any formal policies and procedures relating to the budgeting, accounting, purchasing, payroll, and cash management functions of the Finance Office until December 2003.
- B. The minutes of meetings of the Financial Management Committee did not reflect that a deputy director had been recommended and approved. Section 5-21-108, TCA, requires that the finance director recommend an employee of the Finance Office to serve as deputy director upon approval of the committee.
- C. Disbursement warrants were not signed in compliance with state statute. In most instances during the year, only the finance director's signature was present on disbursement warrants for funds administered by the county executive and highway superintendent. Section 5-21-116, TCA, requires the department head's signature on all disbursement warrants. The department should keep a copy of each disbursement warrant with the original being returned to the finance director for signature as cosigner and for filing and mailing. In lieu of each department head's signature on disbursement warrants, the departments may authorize the use of a signature plate in accordance with general law and approval by the Office of the Comptroller of the Treasury.

- D. Subsequent to June 30, 2003, the accounting functions of the School Department were transferred to the Finance Office under the control of the finance director. However, upon inquiry, we noted that the finances relating to the Head Start Program were still maintained by the School Department. In addition, disbursement warrants issued for school funds, except for food service, were not cosigned by the finance director, as required by Section 5-21-116, TCA. Also, salaries and benefits of the former School Department accounting personnel who were moved to the Finance Office were not paid under the Finance Office's major category, as required by Section 5-21-103, TCA. Instead, those employees were still paid through School Department funds.

### RECOMMENDATION

The county should take steps to fully implement and comply with all provisions of the County Financial Management System of 1981.

### MANAGEMENT'S RESPONSE – FINANCE DIRECTOR

The finance director stated the following:

- A. The Carter County Financial Policies and Procedures Manual was formally approved during the December 2003 meeting. However, individual policies (budgeting, purchasing, and travel) had been presented and received approval in principle prior to the December meeting. The main objective of the December meeting was to approve the Policies and Procedures Manual in more of its entirety rather than in a piece-meal fashion. A meeting of the Financial Management Committee is scheduled for February 4, 2004. At that meeting, I anticipate that all committee members will agree to the statement of facts presented above and that prior meeting notes will be revised.
- B. A deputy director was approved by the Financial Management Committee during the meeting on February 4, 2003. A meeting of the Financial Management Committee is scheduled for February 4, 2004. At that meeting, I anticipate that all committee members will agree to the statement of facts presented above and that prior meeting notes will be revised.

Items A. and B. simply reflect poor notetaking. The director of finance will do the following to ensure the accuracy of the Financial Management Committee notes: designate a recorder (deputy director or secretary) and potentially tape-record meetings.

- C. This was a timing issue in the implementation process due to the transition from one system to another. We have an automatic check signature machine, and we recently received the necessary approval from the Comptroller's Office in regard to appropriate controls. Warrant signature plates will be revised to reflect the changes with the Financial Management Act of 1981.

- D. The integration of Head Start was approved in the Implementation Plan that was presented to the Financial Management Committee. Head Start wasn't brought over with the existing school function due to the planning consideration that this work would have to be absorbed through the existing personnel transferring from the School Department. The Head Start Program will be incorporated with the centralization of all county payrolls and payment processing.
- 

**FINDING 03.03**      **DEFICIENCIES WERE NOTED IN THE ISSUANCE OF A REFUNDING CAPITAL OUTLAY NOTE**  
(Material Noncompliance Under Government Auditing Standards)

We noted the following deficiencies regarding the issuance of a refunding capital outlay note:

- A. The county improperly approved the note. On April 21, 2003, the County Commission, by motion, authorized the finance director to refinance certain capital outlay notes to obtain interest savings. A refunding plan was then submitted to the state director of Local Finance on May 27, 2003. Section 9-21-612, Tennessee Code Annotated (TCA), and Section 9-21-903, TCA, provide that the County Commission may only take action regarding the refunding after receiving the state director of Local Finance's report on the refunding plan or after the passage of 15 days from the date the plan was received by the state director.
- B. The finance director issued the refunding note on May 30, 2003, only three days after submitting the plan and before the state director of Local Finance's report on the plan, which was dated June 6, 2003, and before the County Commission's detailed resolution authorizing the note, which was not approved until June 23, 2003.
- C. The note was signed only by the finance director. The County Commission's resolution authorizing the note required that the county executive and county clerk sign the note.

**RECOMMENDATION**

Carter County officials should follow the requirements set out in state statutes for the issuance of notes. In addition, the county executive and county clerk should sign notes, as provided in the commission resolution.

**MANAGEMENT'S RESPONSE – FINANCE DIRECTOR**

This finding involves a learning curve. The original resolution was presented to the County Commission during the April meeting; however, it was determined at a later time to have been passed in a motion form rather than as a resolution.

I worked with the director of Local Finance and corrected this issue by presenting the refunding for approval as a resolution during the next County Commission meeting (June 23, 2003). The director of Local Finance accepted the resolution dated June 23. Ultimately, the Office of Local Finance approved the refunding plan and issue. All necessary statutory steps were completed except for a minor timing issue. The refunding saved the county approximately \$24,000, as we were able to effectively lower our interest rate from 5.2 to 3.45 percent. In the future, we will be more knowledgeable of issues that must be passed as resolutions rather than motions.

---

**FINDING 03.04      COMPETITIVE BIDS WERE NOT SOLICITED IN ACCORDANCE WITH PRIVATE ACT**  
(Noncompliance Under Government Auditing Standards)

Pending implementation of the Financial Management System of 1981, purchasing procedures for the Office of County Executive were governed by provisions of Chapter 238, Private Acts of 1951, as amended, which require all purchases exceeding \$2,000 to be based on competitive bids. During the period under audit, the following items were purchased without solicitation of competitive bids:

- A.     Food supplies for the Carter County jail facility
- B.     Three laptop computers costing a total of \$5,999
- C.     Three projectors costing a total of \$7,485
- D.     An imaging system, including peripherals and supplies, costing \$7,154
- E.     A trailer costing \$6,500
- F.     Eight bullet-proof vests costing a total of \$6,595

**RECOMMENDATION**

Competitive bids should be solicited in all applicable instances.

**MANAGEMENT'S RESPONSE – FINANCE DIRECTOR**

The finance director stated the following:

- A.     This occurred prior to my tenure. However, it appears that there was a misunderstanding in that county personnel thought that food supplies could be “piggy-backed” from existing contracts through our school system (same vendor) that had been competitively bid. Food supplies for the jail have now been competitively bid, and a contract has been awarded.

B.&C. This occurred prior to my tenure. However, it appears there was a misconception that if the individual item prices were below the bid threshold (\$2,000 in this case) that they were not required to be bid.

D., E.,

& F. These items were purchased in relation to an Emergency Management Agency (EMA) grant. EMA grants typically involve specialized equipment for which there are a limited number of providers. However, other potential suppliers could have provided these items. These items were reviewed with the EMA department, and in future grant processes, the Finance Office will work more closely with EMA on reviewing items requiring bids.

---

**FINDING 03.05      RECEIPTS WERE NOT ALWAYS WRITTEN FOR  
COLLECTIONS AT THE CONVENIENCE CENTERS**  
(Internal Control – Material Weakness Under Government Auditing  
Standards)

At the two county-operated convenience centers, receipts were not always issued for collections, as required by Section 9-2-103, Tennessee Code Annotated (TCA). The convenience centers only issued receipts at customers' requests. Without receipts, we were unable to determine if all the centers' collections had been accounted for and if all funds had been deposited within three days of collection, as required by Section 5-8-207, TCA.

**RECOMMENDATION**

The convenience centers should issue receipts for all collections and should deposit funds within three days of collection, as required by state statutes.

**MANAGEMENT'S RESPONSE – FINANCE DIRECTOR**

Our primary goal is for the landfill to be self-supporting. These fees help in the achievement of that goal. However, receipt collection has historically been a problem area. A corrective solution will be explored.

---

**FINDING 03.06      DUTIES WERE NOT SEGREGATED ADEQUATELY IN THE  
FINANCE OFFICE**  
(Internal Control – Reportable Condition Under Government Auditing  
Standards)

Duties were not segregated adequately in the Finance Office. During the year, the office consisted of the finance director, one accounting clerk responsible for all funds administered by the county executive, and one accounting clerk responsible for the Highway Fund. Each

accounting clerk's duties included preparing purchase orders, signing purchase orders in the director's absence, processing invoices for payment, signing disbursement warrants in the director's absence, entering and processing payroll, posting cash receipts, performing monthly reconciliations, preparing and entering general journal entries, and maintaining the accounting records.

### RECOMMENDATION

Management should take steps to segregate duties adequately in the Finance Office.

### MANAGEMENT'S RESPONSE – FINANCE DIRECTOR

Responsibilities of current employees will change with the centralization of finance functions for the county to ensure proper segregation of duties. Proposed segregation of duties is highlighted in the Implementation Plan of the 1981 Act (Organization Structure). However, this is a transitional period when it is critical to transition employees into one site and allow an adequate settlement period before changing job responsibilities. In addition, this settlement period is necessary so that employees can be cross-trained on different accounting functions to which they may not have been previously exposed (payroll, purchasing, budgeting, etc.).

---

## **OFFICE OF DIRECTOR OF SCHOOLS**

### FINDING 03.07

### **TIME RECORDS WERE FALSIFIED**

(Material Noncompliance Under Government Auditing Standards)

Carter County school officials informed us of an internal investigation they had conducted regarding a transportation department employee who was paid for hours she did not work. Based on their investigation, school officials concluded that an employee was paid for 86 work days between August 2002 and January 2003 when she was actually absent from work due to an illness. The employee's time sheets submitted to the payroll clerk for this period falsely reflected the employee had worked days on which she was absent. These time sheets were signed by the transportation supervisor, and the employee's name was signed by another transportation department employee, along with that employee's initials. Section 39-16-504, Tennessee Code Annotated (TCA), states that it is unlawful to "knowingly make a false entry in, or false alteration of, a governmental record."

Once these falsified time sheets were discovered, school officials determined that this employee only had ten days of leave and therefore was paid for 76 days (86 days – 10 days of vacation and sick leave) that she did not work. The employee resigned January 31, 2003, due to her illness. After the investigation was complete, the School Department approved a request from nine employees to transfer a portion of their accumulated sick leave days to this employee to make up for the days this employee was paid for but did not work. That request was made based on an existing sick leave policy of the School Department. If it was the employees' intent to transfer leave to the absent employee, this transfer should have been requested before the employee was paid, and time sheets should not have been

falsified. To maintain the integrity of the time reporting system, it is imperative that time records reflect the actual time worked for each employee.

### RECOMMENDATION

Carter County school officials should establish internal controls over payroll procedures to ensure that time sheets reflect actual hours worked and that employees are not paid for hours not worked unless they are on approved leave with sufficient balances to cover the absences. School officials should monitor these procedures to ensure compliance. Furthermore, school officials should ensure that employees are aware of the provisions of Section 39-16-504, TCA.

### MANAGEMENT'S RESPONSE – DIRECTOR OF SCHOOLS

Upon discovery that an employee was being paid during unpaid medical leave, we contacted the Comptroller's Office and conducted an internal investigation. No criminal intent was evident, and we noted that the current leave policy, if it had been correctly applied, would have solved the employee's leave deficit. We implemented additional controls to ensure that time sheets reflect the actual time worked. Time sheets are inspected for a valid employee signature, with payroll warrants not to be released without signed time sheets in hand. Leave time policies have been reviewed with transportation employees and the supervisor. A written reprimand has been issued and documented.

---

### FINDING 03.08

### **DEFICIENCIES WERE NOTED IN CONTROLS RELATING TO COMPLIANCE WITH FEDERAL GRANT REQUIREMENTS**

(Internal Control – Material Weakness Under OMB Circular A-133)

The School Department did not have controls in place to ensure compliance with the Davis-Bacon Act and federal procurement, suspension, and debarment requirements for the School Renovation Grant. Federal regulations require that contractors and subcontractors pay prevailing wages on any construction contract that exceeds \$2,000 and that contractors and subcontractors receiving individual awards for \$100,000 or more certify that the organization and its principals are not suspended or debarred when the project is financed either wholly or in part by federal funds. The School Department paid \$450,000 from a federally funded School Renovation Grant for labor and materials to renovate schools without documenting compliance with these requirements until after the projects were completed.

Subsequent to the completion of the School Renovation Grant, School Department personnel obtained documentation from the construction contractors to support the compliance with the Davis Bacon Act (payment of prevailing wages) and the procurement, suspension, and debarment requirements. By not performing the verification in a timely manner, the School Department risked noncompliance with the requirements.

## RECOMMENDATION

School Department officials should implement controls to ensure compliance with federal grant requirements. These controls should include procedures for identifying, reviewing, and monitoring compliance requirements on a timely basis for each individual grant awarded. In addition, the School Department should ensure that all employees involved in the expenditure of grant funds are aware of all applicable requirements and regulations governing the use of these funds.

---

## FINDING 03.09      **DEFICIENCIES WERE NOTED IN PURCHASING PROCEDURES RELATING TO BIDS** (Noncompliance Under Government Auditing Standards)

Pending implementation of the Financial Management System of 1981, purchasing procedures for the School Department were governed by Section 49-2-203, Tennessee Code Annotated, which provides for the county Board of Education through its executive committee to make all purchases. This statute also requires that competitive bids be solicited through newspaper advertisement on all purchases estimated to exceed \$5,000. The following deficiencies were noted in the department's purchasing procedures:

- A. Propane purchased for various schools was not competitively bid.
- B. Window blinds costing \$21,834 were purchased without obtaining competitive bids. Instead, the vendor was selected based on prior work performed and on prior bids.
- C. A used pick-up truck was purchased without obtaining competitive bids. It should be noted that price quotes were obtained from various vendors.

## RECOMMENDATION

Competitive bids should be solicited through newspaper advertisement for all applicable purchases.

---

FINDING 03.10      **THE SCHOOL FEDERAL PROJECTS FUND HAD A CASH OVERDRAFT AT JUNE 30, 2003**  
(Internal Control – Reportable Condition Under Government Auditing Standards)

The School Federal Projects Fund had a cash overdraft of \$101,411 at June 30, 2003. The cash overdraft resulted from disbursing funds that exceeded cash on deposit with the county trustee. The overdraft was liquidated subsequent to June 30, 2003, through funds received from the state Department of Education.

RECOMMENDATION

The office should not make disbursements that exceed available cash balances on deposit with the county trustee.

---

FINDING 03.11      **EXPENDITURES EXCEEDED APPROPRIATIONS**  
(Noncompliance Under Government Auditing Standards)

Expenditures exceeded appropriations approved by the County Commission in the Central Cafeteria Fund by \$10,499. Section 5-9-401, Tennessee Code Annotated, states that “ all funds ... including, but not limited to ... taxes, county aid funds, federal funds, and fines, which are to be used in the operation and respective programs of the various departments, commissions, institutions, boards, offices, and agencies of county government shall be appropriated to such use by the county legislative bodies.”

RECOMMENDATION

Expenditures should be held within the amounts appropriated by the County Commission.

---

**OFFICE OF TRUSTEE**

FINDING 03.12      **THE TRUSTEE'S DEPOSITORY USED AN UNAUTHORIZED METHOD OF PAYING COUNTY WARRANTS**  
(Noncompliance Under Government Auditing Standards)

The office's depository deducted warrants from the office's bank account before the bank presented the warrants to the trustee for payment. Section 8-11-104(7), Tennessee Code Annotated (TCA), states that the trustee should “pay all just claims against the trustee's county as they are presented, if the trustee has a sufficient sum of money ... not otherwise appropriated.” The depository's practice did not provide a method for the trustee to verify the availability of funds for paying warrants.

Section 58-210, TCA, provides an alternate method for the trustee to determine that adequate funds are available and for the bank to charge the trustee's account directly. This section authorizes county trustees to implement a checking system instead of a warrant system for disbursing funds. However, as of the date of this report, the trustee had not elected to implement a checking system.

#### RECOMMENDATION

The office's depository should not deduct warrants from the office's bank account until the warrants have been presented to the trustee for payment. As an alternative to this practice, the trustee should consider implementing a checking system for disbursing county funds, as authorized by state statute.

---

#### **OFFICE OF COUNTY CLERK**

**FINDING 03.13      **CONTROLS OVER CASH COLLECTIONS WERE INADEQUATE****  
(Internal Control – Material Weakness Under Government Auditing Standards)

Our audit revealed numerous material internal control deficiencies in the office's cash collections and deposits. Some of these deficiencies were reported in prior fiscal years and have not been corrected or have been only partially corrected. We noted the following internal control deficiencies:

- A. The daily cash book did not reference the receipt numbers for miscellaneous collections, which included hotel/motel tax, mineral severance tax, beer tax, boat tax, and miscellaneous clerk fees.
- B. Receipts for miscellaneous collections did not reflect the method of payment (i.e., cash or check).
- C. The daily renewals and title application forms were not filed in a manner that corresponded to the daily reports made to the state. As a result, amounts reported on the various daily motor vehicle reports could not be easily reconciled with the corresponding renewal and title application forms.
- D. Official, prenumbered receipts were not issued for marriage licenses, copy fees, interest earned on checking and trust accounts, and in several instances, probate collections. Section 92-104, Tennessee Code Annotated (TCA), requires that official, prenumbered receipts be issued for all collections.
- E. Controls were not adequate over business tax collections. Receipts were issued out of sequence, and numerous differences were noted between the

receipts issued and the collections reported on the daily cash book. We were informed that one reason for these differences was that receipts were issued by the office after calculating amounts due, regardless of when the funds were actually collected. This practice undermines all the internal controls over the receipting and accounting process. Other business tax deficiencies include differences between names printed on the receipts compared to names printed on the computerized business tax report, differences in dollar amounts for receipts recorded on the daily cash book compared to actual receipt documents, and in some instances, the same business license number was used for more than one business.

- F. In one instance, probate court receipted the same money twice. Also, probate receipts and disbursements were not posted to the official execution docket. Section 18-1-105, TCA, requires all funds paid into and out of the office to be entered on the execution docket.

Because of the number and severity of these internal control deficiencies, we were unable to determine if all funds collected had been receipted and properly accounted for. Additionally, we were unable to determine if the clerk had complied with Section 5-8-207, TCA. This statute requires that officials deposit all funds within three days of collection.

#### RECOMMENDATION

The daily cash book should reference the receipt numbers for miscellaneous collections, and receipts for miscellaneous collections should reflect the method of payment. Official, prenumbered receipts should be issued for all collections and should be properly accounted for. Controls over daily renewal and title application forms should be improved. Daily renewal and title application forms should be filed in a manner that corresponds to daily reports filed with the state. Control totals of renewal and title application forms should be prepared and reviewed with amounts reported on the daily cash book. Controls over business licenses should be improved. Receipts should be issued only when funds are actually collected. Care should be taken to ensure that information on actual business license forms agrees with the daily business tax report information and with amounts reported on the daily cash book. Finally, the clerk should post all receipts and disbursements relating to probate cases in the execution docket, as required by state statute.

---

FINDING 03.14      **DEFICIENCIES WERE NOTED IN THE COLLECTION OF DELINQUENT BUSINESS TAXES**  
(Noncompliance Under Government Auditing Standards)

Our examination disclosed that although the clerk had procedures to notify delinquent businesses of their need to file a business tax return, no follow-up procedures were performed to determine that delinquent businesses filed returns after these notices were sent. Also, the clerk did not issue distress warrants to the delinquent businesses, as required by Section 67-4-719, Tennessee Code Annotated. The clerk's failure to perform

follow-up procedures or to issue distress warrants could result in a loss of revenue for the county.

### RECOMMENDATION

The county clerk should implement follow-up procedures to determine if delinquent businesses filed business tax returns, and when necessary, the clerk should issue distress warrants to collect taxes from delinquent businesses, as required by state statute.

---

### **OTHER FINDING AND RECOMMENDATION**

#### FINDING 03.15

#### **DUTIES WERE NOT SEGREGATED ADEQUATELY IN THE OFFICES OF CLERK AND MASTER, REGISTER, AND SHERIFF**

(Internal Control – Reportable Condition Under Government Auditing Standards)

Duties were not segregated adequately among officials and employees in the Offices of Clerk and Master, Register, and Sheriff. Officials and employees responsible for maintaining the accounting records were also involved in receipting, depositing, and/or disbursing funds. 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.