

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 county mayor (formally titled county executive) and sheriff are paraphrased in this report. Other officials offered oral responses to certain findings and recommendations; however, we did not include these oral responses in this report.

OFFICE OF COUNTY EXECUTIVE

FINDING 03.01 **THE GENERAL AND SOLID WASTE/SANITATION FUNDS HAD CASH SHORTAGES**

(Material Noncompliance Under Government Auditing Standards)

In the prior year's audit, we reported cash shortages in the General and Solid Waste/Sanitation Funds of \$1,079.50 and \$7,157.62, respectively. During the current year, the General Fund had an additional cash shortage of \$2,053.24, resulting in a total cash shortage of \$10,290.36. On August 7, 2002, the former county executive and Chris Pulley deposited \$1,500 and \$710, respectively, reducing the cash shortage to \$8,080.36. Details of the cash shortage are presented in the Houston County Comprehensive Annual Financial Report for the year ended June 30, 2002. Subsequent to the date of our 2002 audit report, the Houston County Grand Jury indicted the former county executive, Jim Smith, and a former county employee, Chuck Doyle, Jr., on charges of theft, a Class E felony. The Grand Jury also indicted Theresa Pulley, a former employee in the County Executive's Office, on charges of official misconduct, a Class E felony. Each defendant entered into a memorandum of understanding with the District Attorney General's Office. Details of these agreements and an explanation of the status of the \$8,080.36 cash shortage at June 30, 2003, are discussed below:

- A. On September 11, 2003, the former county executive, Jim Smith, and former county employees Chuck Doyle, Jr., and Theresa Pulley each signed a Memorandum of Understanding pursuant to Section 40-15-105, Tennessee Code Annotated. By signing the memoranda, they agreed that their cases would be suspended for a period of time on the stipulation that they meet several conditions. One of the conditions was that Mr. Smith would repay Houston County \$10,425 for the cost of the audit. He met this requirement by depositing \$10,425 with the county trustee from personal funds on September 30, 2003. However, the court did not order Mr. Smith to repay his portion of the cash shortage (\$507.90) at June 30, 2003, and as of the date of this report, this portion of the cash shortage remains unpaid.
- B. Chuck Doyle agreed in his memorandum to make restitution of his portion of the cash shortage (\$3,797.42) to Houston County. As of the date of this report, Mr. Doyle has not paid this amount to Houston County.

C. Theresa Pulley agreed in her memorandum to make restitution of her portion of the cash shortage (\$803.44) to Houston County. As of the date of this report, Ms. Pulley has not paid this amount to Houston County.

D. The remaining cash shortages at June 30, 2003, have not been paid by the following individuals as of the date of this report:

1. Ann Morrison	\$ 73.60
2. Joy Lowe	100.00
3. Lori Schmidt	198.00
4. Freddy Lyle	2,500.00
5. Clarence Marable	<u>100.00</u>
Total	<u>\$2,971.60</u>

The district attorney general did present Freddy Lyle's cash shortage to the Houston County Grand Jury; however, the Grand Jury did not return an indictment. The district attorney general did not present the other remaining shortages to the Grand Jury.

RECOMMENDATION

Officials should continue their efforts to collect the remaining cash shortage of \$8,080.36. If the former county employees do not reimburse the county for their individual amounts of the cash shortage, the county mayor should seek reimbursement for the shortage from the employees' blanket bond.

FINDING 03.02 **A FORMAL PURCHASE ORDER SYSTEM HAD NOT BEEN ESTABLISHED**

(Internal Control – Reportable Condition Under Government Auditing Standards)

The County Executive's Office had not established a formal purchase order system. Purchase orders are necessary to control who has purchasing authority for the county and to document purchasing commitments.

RECOMMENDATION

The office should establish a formal purchase order system to improve internal controls over the purchasing process and to document purchasing commitments.

FINDING 03.03 **THE OFFICE HAD DEFICIENCIES IN BUDGET OPERATIONS**

(Internal Control – Reportable Condition Under Government Auditing Standards)

Our audit revealed the following deficiencies in the office's budget operations:

- A. Budget amendments posted to the accounting records of the General, Solid Waste/Sanitation, and Drug Control Funds did not agree with amendments approved by the County Commission. Also, an approved budget amendment was not posted to the records of the General Debt Service Fund. The financial statements of this report reflect budget amendments and budget amounts as approved by the County Commission.
- B. The General Debt Service Fund's actual fund balance at July 1, 2002, was \$375,289; however, the estimated fund balance reflected in the county's budget for July 1, 2002, was only \$251,822. Therefore, the actual fund balance was \$123,467 more than the estimated fund balance presented to the County Commission.

RECOMMENDATION

The budget and budget amendments posted to the accounting records should agree with amounts approved by the County Commission. Also, the estimate of the beginning fund balance should be made on a more realistic basis to provide county officials with accurate information on which to base funding decisions.

MANAGEMENT'S RESPONSE – COUNTY MAYOR

The mayor stated the following:

- A. We concur. In the future, approved budget amendments will be posted to the accounting records.
- B. In the future, we will budget the estimated fund balance properly.

FINDING 03.04 **THE OFFICE HAD DEFICIENCIES IN ITS ACCOUNTING RECORDS**

(A. Noncompliance Under Government Auditing Standards; B., C. Internal Control – Reportable Condition Under Government Auditing Standards)

Our audit revealed the following accounting deficiencies in the County Executive's Office:

- A. Office personnel did not adequately reconcile the cash balances of the General, Solid Waste/Sanitation, and General Debt Service Funds with the trustee's cash balances. Instead, journal entries were made to each fund's cash balance for the difference needed to agree with the trustee's cash balance without identifying errors and omissions in revenues and expenditures. We have identified and corrected these errors and omissions

and have properly presented revenues and expenditures in the financial statements of this report. Section 9-2-138, Tennessee Code Annotated, requires all administrative officers to reconcile fund accounts with the trustee's balances on a monthly basis.

- B. Several expenditures were misclassified on the accounting records of the General Fund. Because of the number of misclassified expenditures, we did not attempt to properly classify these expenditures. Misclassifying expenditures diminishes the usefulness of the financial records as a management tool and results in a loss of budgetary control. In most instances, we noted that the misclassifications only affected items within major category appropriations. Therefore, we do not believe that the financial statements of the General Fund are materially misstated in this report.
- C. Numerous general journal entries were made to the accounting records of the General, Solid Waste/Sanitation, and General Debt Service Funds without any supporting documentation. In the General Fund, the propriety of some of these journal entries could not be determined and resulted in an unidentified adjustment to expenditures of \$7,714 to balance the payroll liability accounts.

RECOMMENDATION

The office should take the following steps to correct the deficiencies:

- A. The cash balances of the General, Solid Waste/Sanitation, and General Debt Service Funds should be reconciled with the trustee's cash balances monthly, as required by state statute, and posting errors should be corrected promptly.
- B. To ensure effective budgetary control and accountability of funds, the office should classify expenditures in the appropriate accounts.
- C. Documentation should be maintained to explain all journal entries.

MANAGEMENT'S RESPONSE – COUNTY MAYOR

The mayor stated the following:

- A. We concur. We will start reconciling the cash balances of each fund with the trustee's cash balance.
- B. We concur. We will properly classify expenditures.
- C. We concur. Documentation will be maintained for all journal entries.

FINDING 03.05

THE OFFICE HAD PAYROLL DEFICIENCIES

(Internal Control – Material Weaknesses Under Government Auditing Standards)

Our audit revealed the following accounting deficiencies involving payroll:

- A. General ledger payroll deduction accounts were not reconciled with subsidiary payroll records on a monthly basis. Unidentified balances were allowed to accumulate in the withholding accounts for social security, income taxes, and insurance deductions. The failure to reconcile general ledger payroll liability accounts with employee payroll deductions resulted in errors and omissions in reporting and paying employee deductions.
- B. Employees' federal income and social security taxes relating to the county's payroll were not always reported correctly to the Internal Revenue Service (IRS). As a result, on February 10, 2003, and August 5, 2003, the county received refunds in the amounts of \$2,815 and \$5,530, respectively, for the overpayment of taxes reported to the IRS on Form 941 for the quarters ended September 30, 2002, and December 31, 2002.
- C. In some instances, time and attendance records maintained by the County Executive's Office did not have the signatures of the employee and/or county executive.
- D. The office did not maintain records of compensatory and vacation hours that each employee earned and used. Because of the failure to maintain these records, the county had not established leave balances for employees.

RECOMMENDATION

The County Executive's Office should take the following steps to correct the deficiencies:

- A. The office should reconcile general ledger payroll liability accounts with payroll reports, deposits of payroll taxes, and payments of insurance premiums to ensure the accurate reporting of all payroll deductions.
- B. Employees' federal income and social security taxes should be reported correctly to the IRS.
- C. Time and attendance records should be signed by employees and supervisors.
- D. Leave records should be maintained for employees earning compensatory and vacation leave, and these records should include the hours earned and used, and the balances.

MANAGEMENT'S RESPONSE – COUNTY MAYOR

The mayor stated the following:

- A. We concur and will reconcile all payroll records.
- B. We concur and will properly report all employees' withholdings to the IRS.
- C. We concur and will have all employees and supervisors sign time and attendance sheets.
- D. We concur and will maintain all employees' leave records, showing the amounts earned and used, and the balances.

FINDING 03.06 **A DEPUTY SHERIFF WAS REIMBURSED FOR BOTH GAS AND MILEAGE EXPENSE FOR A TRIP TO PICK UP A PRISONER**

(Noncompliance Under Government Auditing Standards)

On September 10, 2002, the county paid a deputy sheriff for both gas (\$186) and mileage (\$597.60) to drive to Duluth, Minnesota, to pick up a prisoner and return to Houston County. The county's travel policy provides only for mileage reimbursement at \$.30 per mile when a county employee uses a personal vehicle for county business.

RECOMMENDATION

The county executive should establish internal controls to ensure county employees are reimbursed travel expenses in accordance with the county's travel policy. The county should seek reimbursement for the overpayment of \$186 to the deputy.

MANAGEMENT'S RESPONSE – COUNTY MAYOR

We concur.

FINDING 03.07 **THE OFFICE DID NOT HAVE FORMAL POLICIES AND PROCEDURES FOR COMPUTER OPERATIONS**

(Internal Control – Reportable Condition Under Government Auditing Standards)

The Office of County Executive did not have written policies and procedures for routine computer operations. Routine operations include system startup/shutdown, application access, system access security, system backup and retention schedules, hardware/software

maintenance, output distribution, and other general data processing functions. Formal policies and procedures are necessary to ensure adequate management control over computer operations.

RECOMMENDATION

Management should prepare a computer policies and procedures manual that defines policies and procedures for operations such as system backups, security measures, and other general data processing functions. Upon completion, the manual should be distributed to all appropriate personnel.

OFFICE OF ROAD SUPERINTENDENT

FINDING 03.08 **PURCHASE ORDERS WERE NOT ISSUED PROPERLY**
(Internal Control – Reportable Condition Under Government Auditing Standards)

Purchase orders were not issued properly. In several instances, descriptions and/or dollar amounts of purchases were not listed on purchase orders until the invoices were received from the vendors. Also, in a few instances, purchase orders were issued after purchases were made. The dollar amounts and descriptions of items on purchase orders are necessary to quantify purchasing commitments and to identify the items purchased. Generating purchase orders after purchases are made defeats the purpose of issuing a purchase order and makes the purchase order approval of payment, rather than approval to make the purchase.

RECOMMENDATION

The office should improve purchasing procedures by listing the dollar amounts and/or descriptions of items on purchase orders and issuing purchase orders before making purchases.

OFFICE OF COUNTY CLERK

FINDING 03.09 **COLLECTIONS WERE NOT DEPOSITED PROPERLY**
(Noncompliance Under Government Auditing Standards)

The county clerk did not deposit collections intact; i.e., funds collected during a specific period of time were not deposited together. Instead, the clerk deposited even amounts of cash, did not maintain a set amount of cash on hand, and deposited checks randomly. Because the clerk used this method of depositing collections, we could not trace all collections to deposits and could not determine if funds were deposited to the office bank account within three days of collection, as required by Section 5-8-207, Tennessee Code Annotated.

RECOMMENDATION

To strengthen internal controls over cash collections and deposits, the county clerk should deposit all funds intact.

OFFICE OF SHERIFF

FINDING 03.10 **DEFICIENCIES WERE NOTED IN THE PURCHASE OF A DOG FOR THE SHERIFF'S OFFICE** (Noncompliance Under Government Auditing Standards)

On March 13, 2001, the county purchased a \$10,000 insurance policy for a dog that was trained in obedience, tracking, and handler protection. The dog was owned by the sheriff's brother, David Barnes, who is a deputy sheriff for Houston County. The insurance premiums for this insurance policy were paid by Houston County, and the county was named as beneficiary. In September 2002, the dog died of unknown causes. The county filed a claim with the insurance agency and received \$7,500 after a \$2,500 deductible was applied against the claim. On October 9, 2002, the sheriff received the \$7,500 from the insurance company. At the November 2002 County Commission meeting, the General Fund's budget was amended to use the \$7,500 to purchase another dog with the stipulation "as long as the county attorney gives a legal opinion that it does not fall under the bidding process." On December 2, 2002, Markley Gill, the county's attorney, issued an opinion that the insurance proceeds were to be used to replace a dog; therefore, competitive bids would not have to be solicited for this purchase. On February 21, 2003, the sheriff, Kenneth Barnes, requested through a purchase requisition that the county purchase a dog from Volunteer Kennels. On February 27, 2003, a county warrant for \$7,500 was issued to T. Glenn Eads of Tennessee Ridge for a Doberman Pinscher. The sheriff informed us that the dog was registered, trained in obedience, trained in handler protection, and partially trained in tracking. However, as of the date of this report, documentation has not been presented to us verifying the dog is actually registered and trained. The county attorney did opine that the county did not have to take competitive bids for the dog; however, the Sheriff's Office did not present any evidence to us that the price the county paid for the dog was a fair price.

RECOMMENDATION

Although the county attorney opined that the county did not have to take competitive bids, the county should have taken steps to ensure paying a fair price for the dog. These steps could include taking competitive bids, requests for proposals, or some other documented measures to ensure paying a fair price. Furthermore, the sheriff should obtain documentation that the dog is actually registered and trained in obedience, tracking, and handler protection.

MANAGEMENT'S RESPONSE – SHERIFF

I disagree with this finding. After the death of the dog, we purchased another one using funds from the insurance company without taking bids, based on the advice of our county attorney. The new dog is registered and certified with the America's Working Dog Advocate as a Patrol Dog Level I, which includes obedience, tracking, and handler protection.

REBUTTAL

The sheriff has not presented us with documentation showing that the dog is registered with the American Kennel Club or any other association. We confirmed with the America's Working Dog Advocate that the dog had attended a seminar from December 2 through December 5, 2003, for testing and certification. They stated they had tested the dog's training skills and issued a certificate for Patrol Dog Level 1. However, they did not actually train the dog and were not aware of the dog's training history. The sheriff was unable to provide any further documentation concerning the dog's background and training.

FINDING 03.11 **BIDS WERE NOT SOLICITED IN COMPLIANCE WITH STATE STATUTES**
(Noncompliance Under Government Auditing Standards)

The sheriff purchased police car video systems (\$11,495) and bulletproof vests (\$5,628) without soliciting competitive bids through public advertisement for these purchases. Sections 5-14-204 through 5-14-206, Tennessee Code Annotated, require that competitive bids be solicited through newspaper advertisement on all purchases estimated to exceed \$5,000. It should be noted that price quotes were obtained prior to the purchases.

RECOMMENDATION

Competitive bids should be solicited through newspaper advertisement for all purchases estimated to exceed \$5,000, as required by state statutes.

MANAGEMENT'S RESPONSE – SHERIFF

I concur and will comply with your recommendations.

FINDING 03.12

THE OFFICE HAD DEFICIENCIES IN ITS INMATE AND COMMISSARY ACCOUNT

(A. Noncompliance Under Government Auditing Standards; B., C. Internal Control – Reportable Condition Under Government Auditing Standards)

Our audit revealed the following deficiencies:

- A. Funds were not deposited to the office bank account within three days of collection, as required by Section 5-8-207, Tennessee Code Annotated. During the period under examination, as many as 15 days lapsed between the date funds were received and the date funds were deposited to the office bank account. Failing to deposit collections within three days not only violates this statute, but also weakens internal controls over funds and increases the potential for loss or theft.
- B. Bank statements were not reconciled with inmate general ledger accounts, and a list of outstanding checks was not prepared during the year. The failure to reconcile bank statements with the general ledger and to prepare outstanding check lists could result in undetected errors.
- C. Disbursements were made by check from the inmate and commissary account for land taxes, child support, and change. However, there was no documentation maintained supporting these disbursements other than receipts signed by the prisoners. We were able to determine through other audit procedures that these funds were expended for the benefit of the prisoners.

RECOMMENDATION

To strengthen internal controls over cash collections and deposits, the sheriff should deposit funds to the office bank account within three days of collection, as required by state statute. The office should reconcile bank statements with general ledger controls and prepare an accurate list of outstanding checks. Also, proper documentation should be maintained to support all disbursements made from the inmate and commissary account.

MANAGEMENT'S RESPONSE – SHERIFF

I concur and will follow your recommendations.

FINDING 03.13

BANK STATEMENTS WERE NOT RECONCILED WITH CASH JOURNAL ACCOUNTS ON A MONTHLY BASIS

(Internal Control – Reportable Condition Under Government Auditing Standards)

Bank statements were not reconciled with cash journal accounts on a monthly basis. The reconciliation of bank statements with cash journal accounts is a necessary procedure to ensure that all cash collections and disbursements are accurately recorded on the accounting records.

RECOMMENDATION

The office should reconcile bank statements with cash journal accounts each month.

MANAGEMENT'S RESPONSE – SHERIFF

I concur and will comply with your recommendations.

OTHER FINDINGS AND RECOMMENDATIONS

FINDING 03.14

RECORDS WERE NOT MAINTAINED FOR GENERAL FIXED ASSETS

(Internal Control – Material Weakness Under Government Auditing Standards)

Houston 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 Houston 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

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

MANAGEMENT'S RESPONSE – COUNTY MAYOR

We will inventory, value, and record the general fixed assets of Houston County.

FINDING 03.15

A SYSTEM OF CENTRAL ACCOUNTING, BUDGETING, AND PURCHASING HAD NOT BEEN ADOPTED

(Internal Control – Reportable Condition Under Government Auditing Standards)

Houston County officials had not adopted a central system of accounting, budgeting, and purchasing. Establishing a central system would significantly improve internal controls over the accounting, budgeting, and purchasing processes.

RECOMMENDATION

Houston County officials should consider adopting the County Financial Management System of 1981 or a private act which would provide for a system of central accounting, budgeting, and purchasing covering all county departments.

FINDING 03.16

DUTIES WERE NOT SEGREGATED ADEQUATELY IN THE OFFICES OF TRUSTEE; COUNTY CLERK; CIRCUIT, GENERAL SESSIONS, AND JUVENILE COURTS CLERK; CLERK AND MASTER; REGISTER; 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; Circuit, General Sessions, and Juvenile Courts Clerk; Clerk and Master; Register; and Sheriff. Officials and employees responsible for maintaining the accounting records in these offices were also involved in receipting, depositing, and 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.

FINDING 03.17

A DEFICIENCY WAS NOTED IN AMBULANCE SERVICE OPERATIONS

(Internal Control – Reportable Condition Under Government Auditing Standards)

The Ambulance Service did not use prenumbered trip tickets. Prenumbered trip tickets are necessary to document sequentially all trips the Ambulance Service makes.

RECOMMENDATION

The Ambulance Service should use prenumbered trip tickets.

MANAGEMENT'S RESPONSE – COUNTY MAYOR

We have now started using prenumbered trip tickets.