

PART II, FINDINGS RELATING TO THE FINANCIAL STATEMENTS

Findings and recommendations as a result of our examination are presented below. We have reviewed these findings and recommendations with management to provide an opportunity for their response. The written responses of the sheriff and chief deputy 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.

CAMPBELL COUNTY AND CAMPBELL COUNTY SCHOOL DEPARTMENT

FINDING 04.01 **GOVERNMENT-WIDE FINANCIAL STATEMENTS WERE NOT PRESENTED IN ACCORDANCE WITH GENERALLY ACCEPTED ACCOUNTING PRINCIPLES**
(Material Noncompliance Under Government Auditing Standards)

Campbell County and the Campbell County School Department did not identify and determine the historical value of their capital assets and the related depreciation amounts of their assets. Therefore, Campbell County and the Campbell County School Department were unable to provide 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, Campbell County’s and the Campbell County School Department’s financial statements are not presented in accordance with generally accepted accounting principles; thus, we have issued adverse opinions 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. Campbell County’s and the Campbell County School Department’s financial statements are presented in compliance with these requirements.

RECOMMENDATION

Campbell County and the Campbell 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.

OFFICE OF HIGHWAY SUPERINTENDENT

FINDING 04.02 **THE HIGHWAY SUPERINTENDENT FALSIFIED INVOICE DATES TO CIRCUMVENT BUDGETARY CONTROLS OVER ASPHALT PURCHASES**

(Material Noncompliance Under Government Auditing Standards)

In early September 2004, the finance director notified us of improprieties involving the falsification of the dates on invoices for asphalt purchases during the tenure of Michael Leach as highway superintendent (September 1, 1996, through August 31, 2004). The finance director also notified the county attorney and the district attorney general of these improprieties. The finance director then reviewed all asphalt purchases made since August 1995 with us and the asphalt vendor to determine the extent to which invoice dates had been falsified in prior years and to determine the correct amount of liability for unpaid asphalt purchases at June 30, 2004, and August 31, 2004. In addition, the finance director confirmed liabilities at August 31, 2004, with all vendors used by the Highway Department to determine if improprieties occurred with other invoices.

From this review, it was determined that Mr. Leach had made changes to the dates on numerous invoices for asphalt to conceal the fact that he had overspent the budget for the current fiscal year and to charge the expenditures to the budget for the following year. Section 54-7-113, Tennessee Code Annotated (TCA), provides that “expenditure of funds for the operation of the county road department shall be made within the limits of the approved budget and the appropriations made for the department.” Also, Section 39-16-504, TCA, states that is unlawful to “knowingly make a false entry in, or false alteration of, a governmental record.”

The earliest invoice detected with a falsified date was for asphalt purchases of approximately \$225,000 made in June of 2000. The highway superintendent changed the dates on this invoice to the following fiscal year before submitting the invoice to the Finance Department for payment. Over the next four fiscal years, a total of 13 invoices were falsified for the purpose of recording the purchase in a fiscal year subsequent to the fiscal year the purchase was made in. In some instances, the highway superintendent changed information on the actual invoices before submitting them to the Finance Department for payment. In other instances, the highway superintendent created bogus replacement invoices on a computer and submitted those for payment. The bogus invoices reflected dates different from the actual invoices.

The falsification of these invoice dates and their recording in the wrong fiscal year have caused the financial statements of the Highway/Public Works to be materially misstated for fiscal years 2000 through 2003. The budgetary and financial impact of these falsified invoices is discussed further in Finding 04.03.

The highway superintendent was able to carry out these improper acts because of deficiencies in purchasing and invoice processing procedures disclosed in Finding 04.04.

RECOMMENDATION

Official records of the office should not be altered or falsified, and expenditures should not exceed appropriations adopted by the County Commission.

FINDING 04.03 **BUDGET OPERATIONS OF THE HIGHWAY/PUBLIC WORKS FUND HAVE BEEN SIGNIFICANTLY AFFECTED BY THE IMPROPRIETIES IN ASPHALT PURCHASES**
(Internal Control – Reportable Condition Under Government Auditing Standards)

Our audit revealed the following budgetary improprieties for the Highway/Public Works Fund:

- A. From our discussions with the asphalt vendor, it has been determined that the asphalt vendor was owed a balance of \$444,268 on June 30, 2003. However, the accounting records of the Highway/Public Works Fund did not reflect any liability to the asphalt vendor at June 30, 2003. Instead, these amounts were inappropriately charged to the subsequent fiscal year's budget (2004 year) because the highway superintendent had altered the dates reflected for those purchases. We have reflected a prior-period adjustment (\$444,268) that management has approved and posted to beginning equity of the Highway/Public Works Fund in the financial statements of this report to properly establish the actual beginning fund balance.
- B. The actual balance owed to the asphalt vendor on June 30, 2004, was \$279,404. Management has made adjustments to the financial records to properly present this amount in the financial statements of this report.
- C. The balance owed to the asphalt vendor as of August 31, 2004, was \$645,348. This was primarily attributable to several large asphalt purchases amounting to \$501,173 between July 1, 2004, and August 2004. The entire appropriation for asphalt for the 2004-05 year was \$410,607. Therefore, in the first two months of the fiscal year, the Highway Department had already exceeded its appropriation for asphalt for the entire year by \$90,566. Also, if asphalt purchases had been properly recorded in prior years' records, appropriations would have been overspent in two of the years between fiscal year 1999-2000 and fiscal year 2002-03.
- D. The financial statements of the Highway/Public Works Fund reflect an undesignated fund deficit of \$54,867 as of June 30, 2004. This includes a reduction in undesignated fund balance for encumbrances recognized for the uncompleted portion of bridge construction contracts of \$344,951. However, those bridge contracts are funded primarily from state funds that will be received and recognized as revenues subsequent to June 30, 2004. The

following statement represents the financial condition of the Highway/Public Works Fund at June 30, 2004, if the reimbursable portion (\$327,027) of the construction contracts had not been reflected as a reservation of fund balance:

Highway/Public Works Fund
 Fund Equity – Restated
 June 30, 2004

Fund Balance	
Unreserved:	
Undesignated	<u>\$ 272,160</u>
Fund Balance, June 30, 2004 – Restated	<u>\$ 272,160</u>

- E. The budget document presented to the County Commission reflected an estimated beginning fund balance for the 2004-05 year of \$624,197. However, the actual fund balance (before the reduction for encumbrances for reimbursable bridge contracts) was only \$272,160. Because the fund balance was so much lower than estimated, and the fact that expenditures for appropriations for asphalt have already exceeded appropriations, the county needs to closely monitor operations of the Highway/Public Works Fund to ensure that the fund ends the year in sound financial condition.

RECOMMENDATION

The financial management committee should closely monitor the operations of the Highway/Public Works Fund and take steps, including budgetary adjustments, necessary to ensure that the fund ends the year in sound condition.

FINANCIAL MANAGEMENT COMMITTEE

FINDING 04.04 PURCHASING PROCEDURES CURRENTLY IN PRACTICE VIOLATE PROVISIONS OF THE FINANCIAL MANAGEMENT SYSTEM OF 1981 AND WEAKEN CONTROLS OVER PURCHASING
 (Material Noncompliance Under Government Auditing Standards)

Campbell County, including the discretely presented Campbell County School Department, operates under the 1981 Financial Management System. This act provides, among other things, for all purchases to be made by the director of finance or a deputy appointed by the director, unless a separate purchasing department is established and a separate purchasing agent is hired. Campbell County has not established a separate purchasing department; therefore, the director is statutorily charged with making all purchases of any kind for all

county departments. As detailed below, numerous purchases were not made by the finance director, and/or internal controls over purchases were inadequate:

- A. Some county departments obtained blank purchase orders from the Finance Office and issued the purchase orders to vendors before they were approved by the finance director to ensure that appropriations were available.
- B. The highway superintendent made many purchases before purchase orders were issued. The superintendent often waited until the invoice was received before completing a purchase order to accompany the invoice to the Finance Office for payment.
- C. Several county departments received invoices directly from vendors rather than the Finance Office. This causes delays in invoice processing and provides the opportunity for the invoices to be held by the departments or altered, as occurred in the Highway Department.
- D. In numerous instances, many departments completed purchase orders after purchases were made. This defeats the purpose of a purchase order and increases the risk of overspending appropriations and of violating other purchasing policies.

RECOMMENDATION

The finance director should make all purchases for all departments of county government, as required by the 1981 Financial Management System. The financial management committee should develop and adopt new purchasing policies and procedures to correct the deficiencies noted in this finding. Specifically, all vendors should be required to have a valid purchase order signed by the finance director before providing goods or services to county departments, all purchase orders should be issued by the Finance Department, and all purchase orders should be issued before the actual purchase and after the finance director has signed them indicating available appropriation. Furthermore, individual departments should not have access to blank purchase orders, and all vendors should be instructed to mail payment requests directly to the Finance Department.

OFFICE OF SHERIFF

FINDING 04.05 **THE OFFICE HAD A CASH SHORTAGE OF \$5,000 AS OF JUNE 30, 2004**
(Material Weakness – Internal Control Under Government Auditing Standards)

The Sheriff's Office had a cash shortage of \$5,000 on June 30, 2004. This cash shortage occurred because collections totaling \$1,000 were not deposited or otherwise accounted for, and disbursements of \$4,000 from confidential drug funds were not documented. Findings 04.06 and 04.07 contain additional details concerning this matter. The sheriff liquidated

the cash shortage with personal funds, and we have reviewed this shortage with the district attorney general.

FINDING 04.06 THE OFFICE WAS UNABLE TO ACCOUNT FOR A COLLECTION OF \$1,000 BECAUSE OF INADEQUATE ACCOUNTING RECORDS AND PROCEDURES
(Material Weakness – Internal Control Under Government Auditing Standards)

The Sheriff's Office could not account for all receipts the office issued. In August 2003, office receipts exceeded deposits by \$1,000. This amount is included in the cash shortage reported in Finding 04.05.

We were not able to determine which individual receipt(s) was not deposited, since more than one receipt was issued for \$1,000 and office records often did not itemize the receipts on the deposit slips. The undeposited collections went undetected because of inadequate accounting procedures and records, as detailed in Finding 04.08.

RECOMMENDATION

All funds the office receipts should be deposited into the office bank account and should be posted in the cash journal.

MANAGEMENT'S RESPONSE – SHERIFF AND CHIEF DEPUTY (PARAPHRASE)

Sheriff McClellan has written a check from his personal account to the Campbell County Sheriff's Department account in the amount of \$1,000 to replace this shortage.

FINDING 04.07 DRUG FUND EXPENDITURES WERE NOT ADEQUATELY DOCUMENTED
(Material Weakness – Internal Control Under Government Auditing Standards)

Our audit revealed the following deficiencies in the use of drug funds:

- A. During the year, a check for \$4,000 was written to a drug agent for confidential drug investigation activities. This agent was subsequently fired and never submitted any documentation to support the use of these funds. Due to the lack of documentation to support this disbursement, this \$4,000 has been included in the cash shortage reported in Finding 04.05.

- B. Witness signatures often were not obtained to document payments made to informants. Witness signatures are necessary to adequately document such payments.

RECOMMENDATION

All checks written from the confidential drug fund should be supported by adequate documentation. Drug agents should maintain documentation of funds received and used. Officials of the Sheriff's Office should periodically obtain, review, and approve the agents' documentation. The office, rather than individual agents, should maintain original documentation of the use of drug funds. Witness signatures should be obtained to document all payments to informants from confidential drug control funds.

MANAGEMENT'S RESPONSE – SHERIFF AND CHIEF DEPUTY (PARAPHRASE)

Sheriff McClellan has written a check from his personal account in the amount of \$4,000 to the Campbell County confidential drug account. This office is of the opinion that the former drug agent had not properly tried to explain these expenditures, and a request for an official investigation by the TBI into these missing funds has been made by this department. I have now ordered the new drug agent to complete documentation daily and to provide to me copies of all documents for my review on a weekly basis. I will keep these documents independently from his records in my office. He has been informed to have a witness to all transactions if at all possible.

FINDING 04.08 **THE OFFICE HAD WEAKNESSES IN INTERNAL CONTROLS OVER DEPOSITS, AND ACCOUNTING RECORDS WERE NOT MAINTAINED PROPERLY**
(Material Weakness – Internal Control Under Government Auditing Standards)

Our audit revealed the following deficiencies over deposits and accounting records:

- A. Receipts were not deposited intact and were not deposited within three business days, as required by Section 5-8-207, Tennessee Code Annotated.
- B. All receipts and disbursements were not posted to the office cash journal.
- C. The office cash journal was not balanced and reconciled with monthly bank statements.

Because of the deficiencies and inadequate controls described above, the scope of our audit was not sufficient to enable us to determine the propriety of financial operations of the Sheriff's Office.

RECOMMENDATION

All collections should be deposited intact and within three business days, as required by state statute. All receipts and disbursements should be posted to the office cash journal on a timely basis and should be balanced at the end of each month. In addition, the cash journal should be reconciled with bank statements on a monthly basis.

MANAGEMENT'S RESPONSE – SHERIFF AND CHIEF DEPUTY (PARAPHRASE)

Adequate accounting procedures are now in effect. The person who was charged with performing these procedures failed to do so and was terminated from employment for this and other reasons. We now maintain the daily cash journal and balance it daily. We also make bank deposits on a near-daily basis rather than using the three-day rule.

OFFICE OF TRUSTEE

FINDING 04.09 **THE OFFICE DID NOT FULLY USE ITS AUTOMATED ACCOUNTING SYSTEM**

(Internal Control – Reportable Condition Under Government Auditing Standards)

The Office of Trustee did not fully use its automated accounting system to maintain financial information. Although the office used the automated system to perform all receipting and warrant reconciliation functions, the system was not used to maintain the cash journal or generate financial statements for the office. The automated cash journal capabilities were installed, and the office paid a maintenance charge for these capabilities.

RECOMMENDATION

Management should use the automated cash journal functions to generate the office's financial statements.

OFFICE OF CIRCUIT AND GENERAL SESSIONS COURTS CLERK

FINDING 04.10 **ACCOUNTING RECORDS WERE NOT RECONCILED WITH THE BANK STATEMENTS IN THE OFFICE OF CIRCUIT AND GENERAL SESSIONS COURTS CLERK**

(Internal Control – Reportable Condition Under Government Auditing Standards)

The general ledgers maintained for the Office of Circuit and General Sessions Courts Clerk were not reconciled on a current basis. Bank statements for May 2004 through October

2004 were not reconciled with general ledger balances until November 2004. As a result, two deposits that were posted twice went undetected in the Office of General Sessions Court Clerk. Reconciling the general ledger with bank statements on a monthly basis is critical to detecting posting errors.

RECOMMENDATION

The general ledger should be reconciled with bank statements on a monthly basis.

FINDING 04.11 **ACCOUNTING RECORDS FOR SHORT-TERM ACCOUNTS WERE NOT MAINTAINED PROPERLY IN THE OFFICE OF CIRCUIT AND GENERAL SESSIONS COURTS CLERK**
(Internal Control – Reportable Condition Under Government Auditing Standards)

Our audit revealed the following deficiencies over accounting records for short-term accounts:

- A. Some interest on short-term accounts was not posted to the clerk’s subsidiary records and/or to the clerk’s general ledger.
- B. Subsidiary records for short-term accounts were not reconciled with general ledger accounts.

The clerk’s subsidiary records and general ledger should accurately reflect all short-term account transactions. Reconciling the subsidiary records with the general ledger, along with reconciling the general ledger with the bank, as noted in Finding 04.10, helps detect transactions that have not been posted. It is important to maintain accurate and timely accounting records to ensure that all of the office’s funds are accounted for by the clerk.

RECOMMENDATION

All short-term account transactions should be posted to the subsidiary records and to the general ledger on a timely basis, and the subsidiary records should be reconciled with the general ledger monthly.

OTHER FINDING

FINDING 04.12

DUTIES WERE NOT SEGREGATED ADEQUATELY IN THE OFFICES OF TRUSTEE, COUNTY CLERK, CIRCUIT AND GENERAL SESSIONS COURTS CLERK, CLERK AND MASTER, AND REGISTER

(Internal Control – Reportable Condition Under Government Auditing Standards)

Duties were not segregated adequately among officials and employees in the Offices of Trustee, County Clerk, Circuit and General Sessions Courts Clerk, Clerk and Master, and Register. Officials and employees responsible for maintaining the accounting records in these offices 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.