

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 are included 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 04.01 **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 (Direct Quote)

Carter County along with several other counties in the State of Tennessee has not fully implemented GASB 34. The county has approved fixed asset policies and procedures and is close to wrapping up our initial valuations and depreciation schedules.

OFFICE OF FINANCE DIRECTOR

FINDING 04.02 **DEFICIENCIES WERE NOTED IN THE ISSUANCE OF CAPITAL OUTLAY NOTES (Material Noncompliance Under Government Auditing Standards)**

The county authorized two capital outlay notes totaling \$1,300,000 to provide funding for the jail project. The County Commission's resolution authorizing these notes required that the county mayor and county clerk sign the notes. However, the first note was signed by the county mayor and the finance director, and the second note was signed by the finance director.

RECOMMENDATION

The county mayor and county clerk should sign notes, as provided in the County Commission resolution.

MANAGEMENT'S RESPONSE – FINANCE DIRECTOR (Direct Quote)

The resolutions were reviewed and accepted by the Office of Local Finance. This issue only involved the required signatures on promissory notes. While the Director of Finance can execute notes, the resolution as approved by County Commission required multiple signatures. The notes in question were amended to accurately reflect this.

FINDING 04.03 **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 some collections, in violation of 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 (Direct Quote)

Our primary goal is for the landfill to be self-supporting. These fees will help in the achievement of that goal. However, receipt collection has historically been a problem area. With that said, a corrective solution was presented for review with the Division of County Audit whereby cash handling responsibilities would be removed from convenience center

employees and potentially transferred to independent vendors. This proposed plan of corrective action wasn't as promising as initially thought and other alternatives are being reviewed for cost effectiveness.

FINDING 04.04 **THE OFFICE HAD BUDGET DEFICIENCIES**
(Internal Control – Material Weakness Under Government Auditing Standards)

During the year, the following budget deficiencies were noted:

- A. Expenditures exceeded appropriations approved by the County Commission in various major categories (the legal level of control) of the General Fund, General Debt Service Fund, Courthouse and Jail Maintenance Fund, Solid Waste/Sanitation Fund, Health Department Fund, and Drug Control Fund, by amounts up to \$37,000. Such overexpenditures are a violation of state statutes.
- B. The original estimate of the beginning fund balance in the General Fund was \$308,130. This estimate was increased during the year to \$1,451,625. However, the actual beginning fund balance was \$686,105. Therefore, the estimate of the beginning fund balance was increased to \$765,520 more than the actual fund balance.
- C. The school department underestimated the beginning fund balance of the Central Cafeteria fund (a major fund of the school department) by \$672,458.

RECOMMENDATION

Expenditures should be held within appropriations approved by the County Commission. Reasonable estimates should be used when budgeting the beginning fund balance.

MANAGEMENT'S RESPONSE – FINANCE DIRECTOR (Paraphrase)

Carter County uses fiscally conservative budgeting practices of over-estimating expenses and under-estimating revenue.

- A. The amount of \$37,000 was primarily due to one item, the purchase of playground equipment for Parks and Recreation. Near the year-end a purchase order was issued, that required the full amount to be encumbered even though no bill had been received and cash was not disbursed. In the future, we will be more conscious of potential encumbrances, as well as actual cash flow and balances.
- B. Carter County was faced with some extreme challenges in relation to our jail. The county was facing unbudgeted costs associated with the liability of multiple lawsuits, higher than average medical costs, and the purchase of modular units. This required fund balances to be used for such emergency situations. In doing so, the county adopted budget amendments to appropriate funding from fund balance

until a revenue source could be identified. Financing sources were secured through the issuance of a capital outlay note, and a tax rate for the subsequent fiscal year was approved to fund these necessary additional expenses. The under-estimation of Cafeteria Fund resulted from the conservative practice of under-estimating cafeteria balances. Going forward, we will work to more accurately reflect this balance.

FINDING 04.05 THE GENERAL FUND AND THE SCHOOL FEDERAL PROJECTS FUND HAD FUND DEFICITS

(Internal Control – Reportable Condition Under Government Auditing Standards)

The General Fund had an undesignated fund deficit of \$189,180 at June 30, 2004. This fund deficit resulted primarily from overestimating available fund balance in the General Fund's budget for the 2003-04 year. Also, the School Federal Projects Fund had a fund deficit of \$28,201 at June 30, 2004. This fund deficit occurred because reimbursements for grant expenditures were not requested in a timely manner.

RECOMMENDATION

County officials should take steps to liquidate these fund deficits. Available fund balances should be reasonably estimated in the budget, and reimbursements for grant expenditures should be submitted in a timely manner.

MANAGEMENT'S RESPONSE – FINANCE DIRECTOR (Direct Quote)

Fiscal Year 2003-04 for the General Fund proved challenging as the county was faced with multiple jail related lawsuits, higher than average medical costs and the purchase of jail modular units. While there was an adequate fund balance at the end of the fiscal year, the amount of undesignated funds was low due to a sizable encumbrance and designated fund balance (reserve account) for the purchase of the jail modular units. Interim financing was secured through the issuance of capital outlay notes until a property tax rate could be set to provide a matching revenue source in the subsequent fiscal year.

FINDING 04.06

THE OFFICE HAD INTERNAL CONTROL WEAKNESSES IN THE MAINTENANCE OF ACCOUNTING RECORDS

(Internal Control – Reportable Condition Under Government Auditing Standards)

During our review of controls we noted that the finance director had not adequately reviewed various reconciliations and journal entries. This lack of oversight resulted in the following deficiencies:

- A. Some prior-year receivables and payables were incorrectly posted to current-year operations. Also, several payroll liability accounts in the General Fund reflected debit balances at June 30, 2004.
- B. During the year, revenues received from a reimbursable grant totaling \$64,860 were erroneously posted to the Health Department Fund when the funds actually should have gone to the General Purpose School Fund. This error was not detected until December 2004.
- C. Reserve amounts were not reflected in the General Fund as of June 30, 2004, and an analysis of reserves had not been prepared. An analysis of is necessary to document the unexpended amount of legally restricted revenues.
- D. Formal documentation was not maintained to support many of the general journal entries posted to the accounting records. In some instances, the computer-generated general journal could not be located. Also, the “extract” software function was used extensively for the School Department funds to make changes to previously posted entries. However, logs of the entries deleted or changed through this function had not been printed and reviewed by the finance director.

We presented audit adjustments to the director of finance to correct the misstatements we detected. The finance director reviewed and posted these adjustments in order to properly reflect these amounts in the financial statements.

RECOMMENDATION

The finance director should provide closer oversight of the accounting function to ensure that the records are accurately maintained and that errors are detected and corrected in a timely manner. An analysis of reserves should be prepared, documenting beginning balances, revenues, expenditures, and ending balances for all legally restricted revenue sources. Formal documentation should be maintained for all journal entries made to the accounting records. In addition, the finance director should limit the use of the “extract” function, and the “extract” log should be periodically printed and reviewed by the finance director to ensure that it has been used only for approved purposes.

MANAGEMENT'S RESPONSE – FINANCE DIRECTOR (Direct Quote)

The finance director stated the following:

- A. Posting of receivables will require the sign-off of the Director of Finance as we close out the fiscal year.
- B. The Health Department had a similar grant during the same time period and based on the remittance advice the funds were deposited by the Trustee into the Health Department unknowingly. This was an honest mistake that was easily corrected. In the future, we should try to reference grant contract numbers provided on the remittance as a cross-reference.
- C. The auditor has historically [assisted in preparing] a reserve account analysis. However, due to the segregation of responsibilities it is beneficial for the finance department to take on this task in the future.
- D. System access to accounting records will be evaluated and reviewed for appropriateness. All journal entry postings will require sign-off by Finance Director or Deputy Director in the future.

OFFICE OF TRUSTEE

FINDING 04.07 **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 5-8-210, 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 04.08 **CONTROLS OVER FILING TITLE APPLICATION FORMS WERE INADEQUATE**
(Internal Control –Reportable Condition Under Government Auditing Standards)

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 title application forms.

RECOMMENDATION

Title application forms should be filed in a manner that corresponds to the daily reports filed with the state.

OFFICE OF SHERIFF

FINDING 04.09 **INTERNAL CONTROLS OVER THE HANDLING OF INMATE FUNDS WERE INADEQUATE**
(Internal Control –Reportable Condition Under Government Auditing Standards)

Our audit revealed the following internal control weaknesses over accounting for funds channeled through the Sheriff's Department for the benefit of inmates:

- A. The receipts issued by the Sheriff's Department employees were not official, prenumbered receipts, as required by Section 9-2-104, Tennessee Code Annotated. Instead, receipt numbers were handwritten on the receipt.
- B. Inmates were required to sign a log indicating the amount of funds they received; however, amounts on this log were not reconciled with amounts received by the Sheriff's Department.

RECOMMENDATION

Official, prenumbered receipts should be written for all monies received. Controls should be developed that include a reconciliation of the monies receipted by the Sheriff's Department employees with the amount remitted to the inmates. This reconciliation should be performed by someone not involved in the handling inmate funds.

OTHER FINDING AND RECOMMENDATION

FINDING 04.10 **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.