



August 30, 2001

Honorable Members of the Board of County Commissioners:

The Johnson County Audit Services Department has completed a limited scope audit of the Register of Deeds' internal control system. Our examination was conducted in accordance with generally accepted auditing standards and the responsibilities of the County Auditor, Resolution 80-94.

The County Auditor undertook this audit in response to concerns expressed by the Register of Deeds regarding the adequacy of her department's policies and practices. Our audit was performed to provide the Board of County Commissioners, the Register of Deeds, and the County Administrator with an objective evaluation of the adequacy of existing managerial controls, policies, and practices within the Register of Deeds department.

In my opinion, the Register of Deeds' internal control system failed to provide reasonable assurance regarding: 1) the reliability of financial reporting; 2) the effectiveness and efficiency of Register of Deeds operations; and 3) adherence with applicable laws and regulations, as noted in the Conclusions section of this report.

The audit conclusions were discussed in detail with the Register of Deeds. The Register of Deeds' written response is included in the Appendix of this report. We appreciate the assistance, courtesy, and cooperation extended to us by the Register of Deeds and her representatives.

Martin J. Kolkin
County Auditor

**Register of Deeds Internal Control Audit
Report Number 2001-05
Executive Summary**

The Audit Services department undertook this audit in response to concerns expressed by the Register of Deeds regarding the adequacy of her department's internal control policies and practices. The County Auditor's audit noted the need for establishing and improving fundamental internal control policies and practices of the Register of Deeds in the following areas:

Segregation of Duties

The Register of Deeds' representatives were permitted to authorize transactions, record the same transactions, and maintaining the custody of assets, which are functions that are conventionally separated in order to reduce opportunities for employees to both perpetrate and conceal errors or irregularities in the normal course of their duties (refer to page 3).

Physical Controls

The Register of Deeds' physical controls failed to provide sufficient protection over the security of assets and access to the data files. These physical controls also did not provide periodic comparisons of subsidiary ledgers with the prevailing books of record (refer to page 4).

Information Processing

The Register of Deeds' department has used three different data information systems over the last several years, Phoenix (currently in use), ARMIS (in use from 1/2000 - 3/2001), and COTT (used prior to 1/2000). The County Auditor's review located serious control deficiencies within all three data information systems employed by the ROD's department (refer to page 5).

The COTT system was neither Y2K compliant nor supported by the County's Information Systems department. During our review, the COTT system became inoperative. The ARMIS database was unable to produce the same results as printed daily revenue reports generated by the same ARMIS system approximately 37% of the time. Historic revenue information within the ARMIS database system could be changed by modifying the date field. The ARMIS system also was not supported by the County's Information Technology Services department. The Phoenix system, created to correct programming flaws within the ARMIS system, still allowed ROD representatives to revise transaction dates and thus change daily revenue results.

RECOMMENDATIONS

The County Auditor recommends that the Register of Deeds:

1. Restructure her department to provide sufficient separation of duties in order to reduce the opportunity of any person to be in a position to both perpetrate and conceal errors or irregularities in the normal course of that individual's duties.
2. Establish and maintain formal policies and procedures that are designed to provide accurate financial reporting, effective and efficient operations, and clearly demonstrate compliance with applicable statutes, laws, regulations, and County policies.
3. Modify the Phoenix system application to retain historic data and to sufficiently document any changes, corrections or adjustments.

**Register of Deeds' Internal Control Audit
Report Number 2001-05
Table of Contents**

PRELIMINARY SECTION

Introduction	1
Objective	1
Audit Scope & Methodology	1
Revenue History	1

CONCLUSIONS

Background	2
Management Responsibilities	2
Internal Control Defined	2
Control Activities Defined	2
Policies and Procedures	2
Written Policies & Procedures	2
Recommendations	2
ROD Comments	3
Internal Control Practices	3
Segregation of Duties	3
Defined	3
Purpose	3
Practices	3
Recommendations	2
ROD Comments	4
Physical Controls	4
Defined	4
Purpose	4
Practices	4
Recommendations	4
ROD Comments	4
Information Processing	4
Defined	4
Purpose	5
Practices	5
COTT	5
ARMIS	5
Phoenix	5
Recommendations	5
ROD Comments	5
Appendix – Register of Deeds Comments	6

**Register of Deeds Internal Control Audit
Report Number 2001-05
Preliminary Section**

INTRODUCTION

The Audit Services Department, at the direction of the Board of County Commissioners (“BOCC”), performed a limited scope examination of the department of the Register of Deeds (“ROD”). The County Auditor notes that shortly after assuming the duties and responsibilities of the ROD, on January 8, 2001, Mrs. Rebecca Davis, requested that the BOCC authorize a detailed internal audit of her department’s policies and practices. ROD Davis expressed a strong desire to improve and strengthen existing controls in her department.

OBJECTIVE

This report provides the BOCC, the ROD, and the County Administrator (“CA”) with an objective evaluation of the adequacy of existing managerial controls, policies and practices, within the ROD’s department, and provides recommendations for strengthening controls.

AUDIT SCOPE & METHODOLOGY

The scope of our review focused on policies and procedures in place at the time of our examination. Our audit included, but was not limited to the following:

- Physical observations of ROD operations;
- Analytical examination of Johnson County budget data and financial information;
- Examination and verification of ROD computer generated data; and
- Interviews and discussions with personnel from the following departments: ROD, Information Technology Services (“ITS”), Office of Financial Management, and County Administration.

REVENUE HISTORY

**Table One
Annual ROD Revenues**

Fiscal Year	1996	1997	1998	1999	2000	Revenue Totals
Mortgage Registration	\$8,807,449	\$9,368,188	\$13,977,087	\$13,768,630	\$11,577,685	\$57,499,039
Recording Fees Revenue	1,059,820	1,112,069	1,556, 717	1,402,351	1,167,199	6,298,156
Heritage Trust Fund	352,297	374,769	559,083	550,777	464,003	2,300,929
Copying Revenues	101,389	97,086	127,966	133,608	107,896	567,945
Totals	\$10,320,955	\$10,952,112	\$16,220,853	\$15,855,366	\$13,316,783	\$66,666,069

Source: The Johnson County Local Governmental Financial System (“LGFS”).

**Register of Deeds Internal Control Audit
Report Number 2001-05
Conclusions**

The County Auditor’s review determined that the ROD’s internal control system failed to provide reasonable assurance regarding: 1) the reliability of financial reporting; 2) the effectiveness and efficiency of ROD operations; and 3) adherence with applicable laws and regulations.

This examination disclosed significant deficiencies that could adversely affect the ROD’s ability to record, process, summarize, and report financial data consistent with the assertions of management.¹

BACKGROUND

Codification of Statement on Auditing Standards (“SAS”) sets forth the responsibility of management to establish and maintain adequate systems of internal control.

Management Responsibilities

SAS section AU 110.03, *Distinction Between Responsibilities of Auditor and Management*, states:

Management is responsible for adopting sound accounting policies and for establishing and maintaining internal control that will, among other things, record, process, summarize, and report transactions, consistent with management’s assertions...

Internal Control Defined

SAS section AU 319.06 defines internal controls in the following manner:

Internal control is a process---effected by an entity’s board of directors, management, and other personnel---designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- (a) reliability of financial reporting,*
- (b) effectiveness and efficiency of operations, and*
- (c) compliance with applicable laws and regulations.*

Control Activities Defined

SAS section AU 319.32 defines control activities as:

The policies and procedures that help ensure that management directives are carried out...and may be categorized as policies and procedures that pertain to the following:...

- Segregation of Duties;*
- Information processing; and*
- Physical controls.*

POLICIES & PROCEDURES

WRITTEN POLICIES & PROCEDURES

Our review determined that the ROD’s department does not maintain written policies or procedures. The County Auditor located an outdated fiscal 1994 office manual, no longer in used.

Recommendations

The County Auditor recommends that the ROD establish and maintain formal policies and procedures that are designed to provide accurate financial reporting, effective and efficient operations, and clearly demonstrate compliance with applicable statutes, laws, regulations, and County policies.

¹ Codification of Statements on Auditing Standards AU Section 325.21, “*Example of Possible Reportable Conditions.*”

ROD Comments

The ROD concurred with the need for written policies and procedures for the operation of her department. The ROD stated that the process for creating written policies and procedures had already begun.

INTERNAL CONTROL PRACTICES

Our audit noted numerous opportunities for improving fundamental ROD internal control practices related to:

- 1. Segregation of Duties;**
- 2. Physical controls, and**
- 3. Information processing.**

SEGREGATION OF DUTIES

Defined

Segregation of duties is the managerial control of assigning different people the responsibilities of authorizing transactions, recording transactions, and safeguarding assets.

Purpose

This control reduces the opportunity of any person to be in a position to both perpetrate and conceal errors or irregularities in the normal course of an individual's duties.

Practices

The County Auditor's review determined that inadequate separation of duties at the ROD's department existed for the following key responsibilities:

1. The daily reconciliation of receipts and the ROD's financial database system are performed by the same individual who counts the daily receipts;
2. The individual performing the daily reconciliation also has the ability to modify historical information within the ROD's financial database system²;
3. The individual preparing the daily reconciliations of receipts also performs the ROD's monthly bank reconciliations. Prepaid fees by title companies are received, recorded in a prepaid fees spreadsheet, charged fees as expenses occur, and recorded on the deposit slip by one individual. Additionally, no procedures exist to reconcile the prepaid fees spreadsheet to the daily deposit slips;
4. Batches of title company documents are delivered to the ROD's "Drop-Off" window for recording and billing. The fees for these documents are determined, recorded, and "expensed" or billed by one individual;
5. The individual that records the fees for "drop-off" charges also performs the daily reconciliations;
6. Our review noted that one ROD representative could both request and approve vendor payments; and,
7. Complaints regarding customer-billing accounts are performed by the individual responsible for billing customer accounts.

Recommendations

The County Auditor recommends that the ROD restructure her department to provide sufficient separation of duties to reduce the opportunity of any person to be in a position to both perpetrate and conceal errors or irregularities in the normal course of that individual's duties.

Additionally, the County Auditor recommends that the ROD develop a management action plan indicating the timeframes for resolving the inadequate separation of duties key responsibilities noted in this report.

² Discussed in greater detail in this report, see sections titled ARMIS and Phoenix

ROD Comments

The ROD concurred with the need to separate incompatible duties in her department. The ROD stated that she was in the process of restructuring her department.

PHYSICAL CONTROLS

Defined

Physical controls encompass the physical security of assets, including: adequate safeguards, secured facilities, authorization for access to computer programs and data files, and periodic accounting and comparison with amounts shown on control records.

Purpose

The purpose of physical controls is to prevent misappropriation of assets.

Practices

Our examination noted the following inadequate physical controls over ROD assets:

1. Checks are not restrictively endorsed upon receipt;
2. Customer payments are attached to "mail-in" documents and stored in boxes prior to recording in the ROD's database. During this audit, the County Auditor observed that documents and their accompanying payment remained unprocessed for six calendar days;
3. Unprocessed "mail-in" documents and payments were stored in an unlocked file cabinet in the ROD safe room. The County Auditor observed instances where unprocessed "mail-in" documents and payments were stored on the safe room floor, due to storage limitations;
4. Daily receipts, averaging approximately \$53,000, remained in the ROD's safes for an average of six calendar days before being submitted for deposit;
5. Safes remain unlocked in an unlocked room during business hours;
6. Safes were sometimes left unlocked in the evenings to allow ROD personnel to work after hours;
7. ROD personnel stated that the combinations to the safes had never been changed;
8. Keys to locked daily cash drawers, which hold the prior day's receipts, were stored above the ROD safes, as previously noted, the safes and safe room remained unlocked during business hours;
9. The daily cash drawer receipts are not counted for verification of amounts at the end of each day;
10. At the beginning of each business day, a ROD deputy removes the prior day's cash drawer and places the daily receipts in a zippered bank bag. The zippered bank bag, which is not locked, is left unattended in the Accounting Manager's cubicle to prepare the daily deposit slip.
11. No bank reconciliations or outstanding check list were maintained by ROD representatives. The monthly bank reconciliation is performed on an electronic spreadsheet that saves the current month's reconciliation on top of the previous month's data. Monthly reconciliations are not printed; and,
12. Our review located a microfilm scanner, purchased in fiscal 1996 for \$97,625, that was not recorded on the ROD's or the County's fixed asset listing.

Recommendations

The County Auditor recommends that the ROD create and maintain appropriate physical controls to prevent the misappropriation of ROD assets. Additionally, the County Auditor recommends that the ROD develop a management action plan indicating the timeframes for resolving the physical control deficiencies noted in this report.

ROD Comments

The ROD concurred and agreed to create and maintain appropriate physical controls during her department's upcoming restructure.

INFORMATION PROCESSING

Defined

Information processing activities are a variety of controls performed to check the accuracy, completeness, and authorization of transactions.

Purpose

Information processing controls include system acquisition, maintenance, and access security. Information processing controls help ensure that transactions are valid, properly authorized, and completely and accurately processed.

Practices

The ROD's department maintains its revenue and cash collection information on a data indexing system that stores information in a database format. The ROD's department has used three different data information systems over the last several years, Phoenix (currently in use), ARMIS (in use from 1/2000 - 3/2001), and COTT (used prior to 1/2000).

The County Auditor's review located serious control deficiencies within all three data information systems employed by the ROD's department.

COTT

The County Auditor's review noted that the COTT system was neither Y2K compliant nor supported by the County's ITS department. During our review, the COTT became inoperative and the data was migrated to the Phoenix system.

ARMIS

Our review concluded that the daily revenues maintained within the ARMIS system (database) failed to match the printed daily revenue report generated by the same ARMIS system approximately 37% of the time.

The County Auditor attempted to match the daily revenue reports printed at the end of business from the ARMIS system to the daily revenues maintained within the ARMIS database for the period January 3, 2000 through December 29, 2000 or 254 business days. The dollar variance between the ARMIS system's database and the ARMIS system's printed daily records ranged from an underage of \$595 to an overage of \$4,793. The information from the ARMIS database should have shown no variances from the information on the ARMIS system's printed daily records, given that the information was drawn from the same system and data source.

ROD representatives were unable to explain specific variances between the ARMIS database and the printed ARMIS report. In general terms, the ROD representatives attributed the unexplained variances between the information to two principle problems: internal flaws within the ARMIS database that misread historical data and the system permits any ROD representative to revise transaction dates and thus change daily revenue results.

Additionally, the ARMIS system application is not supported by the County's Information Technology Services department ("ITS").

Phoenix

According to the ROD, the Phoenix system was created to correct programming flaws within ARMIS and to provide an information system supported by the County's ITS department. However, under the Phoenix system, ROD representatives retained the ability to revise transaction dates and thus change daily revenue results.

ROD representatives stated a need to revise transaction dates to correct prior errors. However, prudent business practices dictate that historical financial data remain intact and any changes, corrections, or adjustments be adequately documented.

Recommendations

The County Auditor strongly recommends that the ROD modify the Phoenix system application to retain historic data and to sufficiently document any changes, corrections or adjustments.

ROD Comments

The ROD agreed to work with ITS to correct identified weaknesses within the Phoenix system.

APPENDIX

August 28, 2001

To: Martin Kolkin, County Auditor

From: Rebecca L. Davis, Register of Deeds

I would like to express the gratitude of the Register of Deeds department for your help in sorting out our accounting issues. Ever since requesting the audit in January of 2001, we have been preparing to implement the recommendations of the county in order to correct the existing problems.

At this time, we are in the process of separating duties and establishing the physical controls suggested. We feel that within the next three months, these practices will be in place. We anticipate that it will take at least until May 2002, to create and maintain the written policies and procedures.

Again, thank you for your help, and if there are any further questions please feel free to contact me at 715-2300.

Sincerely,

A handwritten signature in black ink that reads "Rebecca L. Davis". The signature is written in a cursive style with a large, prominent "R" and "D".

Rebecca L. Davis
Register of Deeds