



May 9, 2001

Honorable Members of the Board of County Commissioners:

The Johnson County Audit Services Department has completed a progress report on the resolution of a reportable condition, within the Treasurer's Department, cited in the fiscal 1999 Management Letter. Our examination was conducted in accordance with generally accepted government auditing standards, with the exception of a peer review.

Our review was performed to provide the Board of County Commission, the County Administrator, and the Treasurer with an objective evaluation of the progress made in the Treasurer's Department toward resolving identified cash reconciliation weaknesses.

In our opinion, significant opportunities exist for the Treasurer's Department to improve the managerial controls over the cash reconciliation procedures, as noted in the Findings section of this report.

Audit findings were discussed in detail with the Treasurer's representatives. The Treasurer and his representatives' responses are included in the Findings section of this report, under *Treasurer's Representatives Comments*. We appreciate the assistance, courtesy, and cooperation extended to us by the Treasurer's Department.

Martin J. Kolkin
County Auditor

**Progress Report on Cash Weaknesses Identified
Within the Treasurer's Department
Report Number 2001-03
Executive Summary**

The Johnson County Audit Services Department has completed a progress report on the resolution of a reportable condition, within the Treasurer's Department, cited in the fiscal 1999 Management Letter.

Our review identified the following significant opportunities for increasing managerial controls and oversight over the cash reconciliation process in the Treasurer's Department:

Establish written policies and procedures to clearly delineate responsibilities for monthly bank reconciliations. (refer to page 2).

Creation of a monthly report that reconciles the bank statement balances, the Treasurer's records balances, and the outstanding checks balances listed on the County's financial system (refer to page 3)

The County Auditor recommends that the Treasurer's representatives prepare a monthly reconciliation of the bank statement balances, the Treasurer's records balances, and the County's financial system outstanding balances

Treasurer's officials concurred and prepared December 2000 reconciliations.

Correction of identified adjustments noted on the monthly reconciliation statement. Our examination noted the following required corrections (refer to page 4):

Bank Statement Balances

- Over \$17.3 million of voided and cancelled checks were incorrectly listed as outstanding;
- Approximately \$453 thousand of checks attributable to other County bank accounts were incorrectly listed as outstanding on the County's accounts payable account;

Treasurer's Records

- Manual checks in excess of \$178 thousand, that do not belong in the AP account, need to be removed from the AP outstanding check listing;

County Financial System

- Approximately \$45 thousand of paid checks need to be removed from the County's financial system records of outstanding checks.

The County Auditor notes that the Treasurer's representatives have begun action to resolve all items noted above.

**Progress Report on Cash Weaknesses Identified
Within the Treasurer's Department
Report Number 2001-03
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**Progress Report on Cash Weaknesses Identified
Within the Treasurer's Department
Report Number 2001-03
Preliminary Section**

INTRODUCTION

In accordance with the duties assigned to the County Auditor, I have examined the reportable condition and material weakness of the Treasurer's department cited in the fiscal 1999 management letter prepared by Johnson County's external certified public accountants, Cochran, Head, and Company, CPAs.

OBJECTIVES

The Audit Services Department worked with the Treasurer's Department, the Office of Financial Management ("OFM"), and the County Administrator ("CA") to provide recommendations to strengthen managerial controls over the accounts payable ("AP") and payroll ("PR") bank accounts.

BACKGROUND

The fiscal 1999 management letter, issued by Cochran, Head, and Company, CPAs, cited a reportable condition and material weakness for the Treasurer's bank reconciliation processes. The management letter noted that the Treasurer did not perform accurate and timely reconciliations or maintain an accurate listing of outstanding checks

Reportable Condition Defined¹

A reportable condition is a significant deficiency in the design or operation of the internal control that could adversely affect the County's ability to record, process, summarize, and report financial data consistent with the assertions of management in the general-purpose financial statements.

Material Weakness Defined¹

A material weakness is a reportable condition in which a specific control procedure does not reduce, to a relatively low level, the risk that errors or irregularities in amounts that would be material in relation to the general-purpose financial statements.

PREVIOUS INTERNAL AUDIT

An Audit Services' *Payroll Report*, dated 5/31/97, noted that the AP and PR bank accounts were not reconciled to a detailed listing of outstanding checks. The report recommended that any differences between the bank reconciliation and the outstanding checklist be researched and resolved. The audit report stated that this deficiency was a high-risk item.

AUDIT SCOPE & METHODOLOGY

In order to address deficiencies noted in an Audit Services' *Payroll Report*, dated 5/31/97, new bank accounts were established for the AP, during October 1998, and the PR, during March 1998. The scope of our review for Treasurer examined the new accounts for AP and PR accounts from October 1998 & March 1998, respectively, through December 2000.

Our review included, but was not limited to the following:

- An examination of bank account statements for all accounts;
- Analytical examination of Johnson County financial data;
- Review of the Treasurer's bank reconciliation records; and
- Discussions with the Treasurer's office, the Office of Financial Management, and Information Technology Services.

¹ Codification of Statements on Auditing Standards AU Section 325.02

**Progress Report on Cash Weaknesses Identified
Within the Treasurer's Department
Report Number 2001-03
Findings**

OVERVIEW

Treasury representatives acknowledged that the bank reconciliations performed by their department did not fulfill the required management control objectives regarding the existence, accuracy, and validity of outstanding checks noted in the AP and PR bank accounts.

Additionally, Treasurer's officials requested general guidance, in the form of recommendations, from the Audit Services Department for preparing account reconciliations that would meet the Treasurer's management control objectives.

1. POLICIES & PROCEDURES

Written policies and procedures for the monthly reconciliations of the Treasurer's cash accounts did not exist.

RECOMMENDATIONS

The County Auditor recommends that the Treasurer's department establish written policies and procedures that clearly delineate responsibilities and practices for monthly bank reconciliations.

Treasurer's Representatives Comments

Treasurer's representatives concurred.

EXISTING PRACTICES

In an attempt to resolve reconciliation problems noted in the Audit Services Report, dated 5/31/97, the Treasurer's Department began using a positive pay, check clearing process ("positive pay process") for the AP and PR bank accounts during fiscal 1998. The "positive pay practices" involved:

1. The County's Information Technology Service ("ITS") providing the bank a complete record of checks, obtained from LGFS and Genesys (the payroll system), to be issued from the United Missouri Bank NA ("UMB") AP and PR bank accounts.
2. UMB then compares every check presented to the bank against the record of checks provided by ITS.
3. The UMB positive pay accounts always carry a zero balance at the end of the business day.
4. Only the amounts of the checks tendered for payment are to be "swept" from another of the County's bank accounts, account number "1058", into the positive pay AP and PR accounts.
5. UMB then sends a monthly statement on compact disc ("CD"), and later in a hard copy form, to the Treasurer's department. The monthly information includes a detailed listing of all checks that remain outstanding.
6. The Treasurer's representatives then prepare a running total of all outstanding checks, adjusted for monthly receipts, monthly disbursements, and reconciling items. This total simply represented the Treasurer's running total of outstanding items. This total was not intended to be reconciled to UMB's or the LGFS' outstanding checks totals.

County Auditor's Comments

Our review identified numerous flaws in the existing practices for management controls within the current reconciliation processes for the AP and PR accounts. The following material areas were noted for improvements within the Treasurer's practices for reconciling the AP and PR accounts:

2. RECONCILIATION OF BANK REPORTS, THE TREASURER’S RECORDS, AND THE COUNTY’S FINANCIAL REPORTING SYSTEM

A report that reconciles the monthly bank statement balances, the Treasurer’s records balances, and LGFS outstanding balances did not exist.

As an alternative, the Treasurer’s personnel employed a “running balance system” for the AP and PR accounts, which effectively adds or subtracts receipts, disbursements, or outstanding items from the Treasurer’s month-end balance. However, the “running balance system” monthly total did not agree with either the bank statement report or LGFS monthly totals or provide management control objectives regarding the existence, accuracy, and validity of outstanding checks noted in these accounts.

RECOMMENDATIONS

The County Auditor recommends that the Treasurer’s representatives prepare a monthly reconciliation of the bank statement balances, the Treasurer’s records balances, and LGFS outstanding balances.

Treasurer’s officials concurred and prepared a December 2000 reconciliation that agreed with the bank statement balance, the Treasurer’s records, and LGFS balances.

**Exhibit One
Recommended Reconciliation of the Bank Reports
Treasurer’s Records, the LGFS Balances**

	Bank Balance	Treasurer’s Balance	LGFS Balance
Source of Records	UMB	Treasurer’s Representatives	OFM’s Representatives
Beginning Balance	Outstanding Checks listed on the Month Bank Statement, on CD	Treasurer’s Current Month Outstanding Check Listing	Outstanding Warrant Listing
<u>Adjustments</u>			
Add		LGFS Checks not Yet Recorded in the Treasurer’s Records and Cancelled Checks	
Subtract	Void and Cleared Checks	Checks Cleared from the Wrong Account & Payroll Corrections	Cleared Checks and Posting Errors
Adjusted Balance	Adjusted Outstanding Check Listing	Treasurer’s Current Month Outstanding Check Listing	Adjusted Outstanding Warrant Listing

Auditor’s Note: Adjusted Balance per the Bank, Treasurer, and LGFS must agree at the end of the reconciliation process.

County Auditor’s Comments

The County Auditor notes that adjustments, except for simple timing differences², require action to resolve adjustments prior to the following month’s reconciliation. The County Auditor’s examination confirmed a number of areas identified by the Treasurer’s representatives, as of December 2000, within the Bank Balances, the Treasurer’s Balances, and the LGFS account balances that require action to resolve long-standing unresolved adjustments.

Treasurer’s Representatives Comments

Treasurer’s representatives concurred.

² Such as checks recorded on LGFS, but not received by the bank on the last workday of the month.

3. BANK BALANCES

UMB provided monthly CDs that contain exportable data of checking activity, including monthly cleared checks and a history of all outstanding checks. Based upon the outstanding check data contained within the December 2000 CD statement, the County Auditor noted:

- Approximately \$17.3 million of voided AP checks and approximately \$17 thousand of PR checks inaccurately remained on UMB's monthly outstanding check listing.
- Additionally, \$453 thousand of checks attributable to a different County bank account were incorrectly listed as outstanding by UMB for the previous AP³ account.
- Our review also noted that the UMB's outstanding check listing totals and outstanding item count did not agree to our totals and item count of the same information. UMB needs to be contacted to determine the cause of this situation.

RECOMMENDATIONS

The County Auditor recommends that the Treasurer's representatives ensure that appropriate County personnel provide void check listings monthly to UMB. Additionally, the County Auditor recommends promptly contacting bank representatives when checks are posted to the wrong County bank account. The County Auditor also recommends that the Treasurer's department ensure that the data received from the bank is received in usable format.

Treasurer's Representatives Comments

The Treasurer's department acknowledged primary liaison responsibility with the bank and stated that UMB had been contacted regarding posting errors within County accounts. Additionally, OFM and Treasurer's representatives agreed to work together to provide monthly void check listings to the bank. The Treasurer's officials further agreed to consult with UMB to ensure that all information needs of the County were addressed.

4. TREASURER'S RECORDS

Status of Outstanding Checks

Our review noted that the Treasurer's outstanding check listings required approximately \$178 thousand of corrections to accurately state the AP outstanding check totals. These corrections consisted primarily of the following:

- Manual checks in excess of \$178 thousand, that do not belong in the AP account, needed to be removed from the AP outstanding check listing;

RECOMMENDATIONS

The County Auditor recommends that the Treasurer or his representatives take all necessary action to accurately state the AP account's outstanding checks.

Treasurer's Representatives Comments

The Treasurer's representatives have taken corrective action to accurately state the AP outstanding check listing.

5. LGFS RECORDS

The County Auditor noted \$45,410 of checks that had been paid, listed as outstanding checks on LGFS.

RECOMMENDATIONS

The County Auditor recommends that OFM officials correct the outstanding warrants listing to reflect the \$45,410 of warrants that cleared the AP account.

³ As noted in the Audit Scope & Methodology section of this report, the use of the previous AP account was discontinued when the new AP account was established in October of fiscal 1998.

OTHER COMMENTS

The County Auditor additionally recommends that all reconciliations be completed in a timely manner, the following month. Our examination noted that reconciliations were sometimes performed several months after the month-end close.

Treasurer's Representatives Comments

The Treasurer's representatives stated that the Treasurer's department would strive to reconcile the bank statements in a timely manner. The representatives further noted that during the previous two tax collection seasons, the individual responsible for reconciliations had focused on collecting taxes and providing customer service to the tax-paying public, rather than preparing reconciliations. The Treasurer's representatives speculated that, based on their current resources, the reconciliations may not be finished the following month during the tax collection season.

The Treasurer's representatives explained that they had looked into managing their current workload differently, to minimize the impact of tax seasons on the reconciliation process. However, the representatives concluded that the current workload during tax season exceeds the available resources.

Additionally, the Treasurer officials noted that the Treasurer had requested an additional FTE, through the budget process, to help remedy this situation.