



**Johnson County Auditor**  
Johnson County, Kansas  
**PERFORMANCE AUDIT**

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**January 11, 2007**

**Library Special Use Fund  
Management and Financial Review**

*“The Library needs policies for Special Use Fund expenditures”*



## Johnson County Audit Services

January 11, 2006

To: The Johnson County Board of County Commissioners  
Michael Press, County Manager  
Mona Carmack, County Librarian

In accordance with the approved audit plan, we performed an audit of the Library's Special Use Fund. The audit objective was to determine if the Johnson County Library is managing the Library Special Use Fund according to Kansas statutes and if expenditures made from this fund were appropriate.

We concluded the Special Use Fund could be discontinued as a separate fund. As an alternative, the Library needed to establish appropriate policies for identifying specific expenditures that would be allowable from the fund. Also, improvements in quality control to ensure compliance with existing purchasing policies and procedures were needed.

The audit was conducted according to applicable standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, except that Peer Review has not been performed, and included such tests of the procedures and records as considered appropriate.

I appreciate the cooperation received from the County Librarian and the Library staff during this audit.

William D. Miller, CIA, CGFM  
County Auditor

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# Library Special Use Fund

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## **RESULTS AND RECOMMENDATIONS**

### **1. The Library Special Use Fund Causes Inflexibility and Undue Complexity**

The Johnson County Library Special Use Fund has no financial or operational purpose because of changes in Kansas law and accounting principles since the fund was established in 1984. Generally accepted accounting principles mandate that the county establish the minimum number of funds. The Special Use Fund was established by the Board of County Commissioners in 1984 to provide additional funds for expansion of Library facilities at a time when operating funds for Libraries were restricted by mill levy caps. The mill levy caps have been repealed by the Kansas Legislature. The Special Use Fund has remained in use and, over time, its use has broadened until Library staff is unable to differentiate the expenditures to be paid from this fund from the expenditures to be paid from the Library Operating Fund. The use of this additional fund restricts the use of the money in this fund; increases the complexity of budgeting, accounting, and financial management; and, reduces efficient and economical financial administration.

#### **Recommendations**

We recommend the Director, Office of Financial Management:

1. Work with the Library staff and the Director of Budget and Financial Planning to eliminate the Special Use Fund by the end of 2007 in compliance with generally accepted accounting principles. The mill levy associated with the Special Use Fund should be combined with the Library General mill levy and the operations currently accounted for in the Special Use Fund should be accounted for in the Library Operations Fund.

#### **Management Comments**

*Director, Office of Financial Management: In complying with the County's approved financial policies, OFM follows Generally, Accepted Accounting Principles (GAAP). The auditor references the GAAP general rule found in GAFRS 1300.118 to "...establish the minimum number of separate funds..."*

*The underlying premise of GAFRS 1300.118 is that a minimal number of funds is better because "Using too many funds causes inflexibility and undue complexity in budgeting, accounting and other phases of financial management..." OFM does not believe that the Library's current use of the Special Use Fund causes inflexibility and undue complexity. Establishing proper guidelines for use of the fund will allow the Library to have flexibility, efficient use of resources, and clarity on when the fund should be used.*

*The Library Special Use Fund was established by a Board of County Commission resolution. That being the case, Chief Legal Counsel advises that it will take formal Board action to eliminate it. OFM is not in a position to arbitrarily close the fund.*

*County Librarian: The Library board and staff do not support the recommendation to combine the library operating and special use funds. Procedures will be established to specifically identify which expenditures will be budgeted and expended from the special use fund.*

### **Auditor's Response**

We believe that the key here is establishing appropriate guidelines for the use of this special fund. The guidelines should make a clear distinction between the types of expenditures allowed in the Special Use Fund and those allowed in the Library Operating Fund. The distinction should be incorporated in a policy which does not allow case by case or *ad hoc* decisions based on the exigencies of the moment. The policy should also ensure that transactions that can be handled in the Library Operating Fund through the use of Oracle accounting are handled that way rather than using the Special Use Fund as a substitute.

### **Discussion**

The Special Use Fund was established by the Board of County Commissioners (BOCC) on May 3, 1984, for the purpose of issuing bonds for the construction of libraries in Lenexa and Shawnee. The BOCC used the authority provided them by K.S.A. 12-1257. The description of the purpose of the SUF was very broad and included "to equip, repair, maintain, remodel, and furnish furniture and equipment, including books, computers, shelving, tables and chairs, at the new library branch and any other library location in the Johnson County Library system, as determined by the Board of County Commissioners." All of these uses are also allowed uses in the Library Operating Fund. In fact, there is no use of the money in the Special Use Fund which is not allowed in the Library Operating Fund.

During the course of the audit, we consulted with a wide range of individuals including the Library staff, the Library attorney, County counsel, and the staff at the Office of Financial Management, and the County Budget staff. We asked all of them to define what makes the Special Use Fund special. We tried to determine what particular expenditures were required to be made from the Special Use Fund. No one was able to provide a distinction between the two funds. No one could state any specific expenditure that would be allowed in the SUF and not be allowed in the Library Operating Fund.

Library staff agreed that there were certain maintenance expenditures that seemed unlikely to be allowable in the Special Use Fund. The Library attorney stated that "general personnel expenditures" would not be allowed but continued by saying that personnel expenditures would be allowable in some circumstances.

In written comments, the Library staff stated:

Library board had been encouraging the establishment of a flexible facilities maintenance fund and a technology fund, so it was established with a request for more funding in the SUF.

The “maintenance fund” and “technology fund” as used here are not funds in the accounting sense but rather designations of budget money to pre-determined uses or projects.

The Oracle accounting system used by the County has excellent facilities for maintaining project accounting for the activities described. The projects described would be better maintained within the Library Operating Fund where the Library Board has greater flexibility in redirecting the use of the money to meet its changing needs. If the only use of the SUF is management reporting and control, there are simpler and more direct methods established with the Oracle accounting system.

### **Generally Accepted Accounting Principles**

*The Codification of Governmental Accounting and Reporting Standards (GAFRS)* is the source of generally accepted accounting principles for governments and has been adopted by Johnson County as the standard of accounting and reporting. The first chapter of the standards relates to fund accounting and requirements for establishing funds.

GAFRS 1300.118 states:

The general rule is to establish the minimum number of separate funds consistent with legal requirements, operational requirements, and the principles of fund classification.... Using too many funds causes inflexibility and undue complexity in budgeting, accounting and other phases of financial management, and is best avoided in the interest of efficient and economical financial administration.

GAFRS 1300.105 states that Special Revenue funds are:

...to account for the proceeds of specific revenue sources... that are legally restricted to expenditures for specific purposes....and use of special revenue funds is not required unless they are legally mandated.

Both the Library Operating Fund and the SUF are Special Revenue Funds because their use is limited to Library functions. The SUF is not mandated by statute. K.S.A. 12-1257 says that the BOCC may establish a fund but is not required to do so if it does not levy a special tax under the statute.

Since there is no legal requirement for a separate SUF, only a clear operational requirement would support the maintenance of the additional fund. Library officials have been unable to show that the fund is required for operations. In fact, they have not made any specific distinction between the use of the Library Operating Budget and the Special Use Fund Budget. Library staff stated that the choice of which fund to charge with an expense is often dictated by which fund has a remaining budget balance.

In the interest of greater flexibility for Library financing, reduced budget analysis, and improved efficiency and economy in financial management, we believe the SUF should be eliminated and the related mill levy combined with the Library general mill levy.

## **2. The Library Does Not Have Adequate Internal Controls for Purchasing**

The Library's internal control system for purchasing was flawed because managers did not provide adequate implementing procedures to guide staff in decision-making. Also, staff did not follow appropriate procedures in processing purchases. Audit tests showed a lack of appropriate approval signatures for purchases, lack of dating of approvals, failure to include contract information with the invoice when it was applicable, and several of the purchase orders in the sample were dated after the date of purchase. Library management said internal procedures were in transition and had not been updated in over 5 years. However, they were following County purchasing policies in the interim which they believed were sufficient. County policy cannot substitute for implementing procedures which give staff step-by step guidance on processing purchase requests. As a result, the Library is at risk of making purchases that are not allowed.

### **Recommendations**

We recommend the County Librarian:

- 2.1 Update Library purchasing Administrative Regulations and procedures to ensure adequate internal control over purchasing.
- 2.2 Develop a quality control process to ensure compliance with existing Administrative Regulations and procedures.

### **Management Comments**

- 2.1 *Administrative Regulation 50-30-25 Contracts has been updated by the Library Board. Library staff will update internal procedures to comply with county purchasing policies and Library Administrative Regulation 50-30-25 by December 31, 2006.*
- 2.2 *The updated procedures will include an internal process whereby the County Librarian or designee will spot check ten invoices each quarter for compliance with the Administrative Regulations and internal procedures.*

### **Discussion**

To test the Library's internal controls over purchasing made from the Special Use Fund, we selected a random sample of 185 transactions from a population of 335 paid transactions. We tested the internal controls based on the Library's existing procedures provided to us.

Administrative Regulation Manual (ARM) 50-30-25 provides procedures for purchases of \$10,000 or more, which include: following County Purchasing Procedures for purchases of \$10,000 or more, informal bidding for purchases of \$10,000 to \$49,999, approval from the

County Librarian, and formal bidding procedures for purchases of \$50,000 or more. In addition, any expenditure of \$100,000 or more requires Library Board approval.

Procedures for purchases of less than \$10,000 are defined in Library Procedures SU 60-50-70, which includes attaching the related Purchase Order (PO) to each invoice, ensuring that the invoice matches the PO, ensuring the invoice is approved by a manager and initialed, and marked okay to pay. We also tested the expenditures to ensure that the PO was dated prior to the invoice date for the purposes of our review.

Library procedures for purchases made with the purchasing card are contained in Library Procedures SU 60-50-65. The Library purchasing card procedures require library staff to follow county purchasing card procedures and the Library Procedures SU 60-50-70 for purchases under \$10,000. Based on the Library purchasing card procedures we tested all of the attributes for purchases under \$10,000 plus the following:

- The purchasing card log was completed and signed by an approver
- The original receipt was maintained
- Third party reconciliation was performed
- Transactions were not split to circumvent the purchasing policies.

Our review took into account the procedures required for the dollar amount of the purchases and additional attributes as explained above.

### **Documentation and authentication of purchases were not properly executed**

Based on the County policy, Library Administrative Regulations and procedure requirements for the purchases, we found the following issues:

- For purchases of \$10,000 or more, 67 percent (8 out of 12) of the expenditures from the SUF did not fully comply with policy or procedural requirements.
- Of the 142 purchases under \$10,000, 69 were not in full compliance<sup>1</sup> with the library's existing Administrative Regulations and procedures for these purchases.
- Of the 31 purchases made with the P-Card, 26 were not in full compliance with the library's existing Administrative Regulations and procedures for these purchases<sup>2</sup>.

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<sup>1</sup> We reviewed 8 different attributes and procedural requirements for purchases under \$10,000. "Full compliance" would indicate that all procedural requirements were met. Not all attributes were applicable to all expenditures. This was taken into account when reviewing each expenditure and its supporting documentation. For each attribute, the compliance rate ranged from 51 to 98 percent. Only 51% of the expenditures met all of the applicable procedural requirements for compliance with the Library's own policy.

<sup>2</sup> The majority of purchases that were not in full compliance with the Library policies and procedures were in compliance with County P-Card Guidelines. County P-Card Guidelines are sufficient for the Library to follow when incorporating its own procedures and Library procedures could be updated accordingly.

The most prevalent departures from procedure were: (1) lack of appropriate approval signatures for the purchases, (2) no dating of approvals, and (3) failure to include contract information with the invoice when it was applicable. Several of the purchase orders in the sample were dated after the date of the purchase and 50 of the purchases did not include internal purchase orders with the invoice.

Purchases were made before being approved

Library management staff said many of these procedures were outdated so personnel were not instructed to follow them and Library management did not enforce them. Staff said the implementation of Oracle in 2001 and subsequent time constraints prevented a comprehensive review and update of the Library Administrative Regulations and procedures.

Our review of transactions found that while some of the procedures were followed, many of the procedures were not followed or were followed only occasionally. The mixture of compliant and non-compliant transactions indicates that the internal control system was not adequate within the transactions we reviewed. This mixture also indicated that no effective quality control system was in place to ensure the consistent use of any particular procedure old or new.

Library staff said when the procedures are updated, they expect to include many of the current procedures that the audit determined were not followed by staff. The updated procedures will still include requirements for internal purchase orders prior to purchase and approving managers' signatures on the invoices.

Library staff said they relied on County Purchasing Policy to replace the Library procedures and provide their internal controls. However, County Purchasing Policy is specifically designed to require competitive procurement and to establish the approval process for purchases and does not include any specific internal control procedures. County policy cannot substitute for day-to-day operating procedures at the department or agency level.

As an example of the failure of an internal control procedure, the eight transactions over \$10,000 mentioned above were computer purchases included on two purchase orders, one in 2004 and one in 2005, totaling \$476,549. Library staff stated they relied on the Board's approval of the annual budgets rather than obtaining the Board's approval for these transactions over \$100,000. ARM 50-30-25(i) limits the County Librarian's transaction approval authority to \$99,999.99 and requires the approval of purchases of \$100,000 or more by the Library Board. The approval of an overall budget does not substitute for the specific internal control related to review of transactions above the threshold level and the supporting documentation.

In response to the Library staff's assertion that these transactions were approved by County purchasing based on the Library Board approval, we extended our review of the transactions and interviewed County purchasing staff. We found an additional transaction in 2006 which failed to meet the Library or County purchasing policies. Purchasing staff stated that all three transactions had already been completed prior to their entry in the Oracle system for purchasing review. Purchasing accepted the transactions in 2004 because County policy at that time allowed the transaction although Library policy did not.

In 2005, County purchasing staff accepted the transaction but told the Library staff that the transaction was in violation of County policy. The transaction was approved only because the order had been received from the vendor. In 2006, the Library staff again purchased materials without following Library and County purchasing policy and, again, failed to enter the transactions in Oracle until the purchases had been made.

These actions emphasize the need for improved internal controls and management accountability to ensure purchases are made in accordance with County and the Library's purchasing policies.

**OBJECTIVES, SCOPE AND METHODOLOGY**

**Objectives**

The audit objective was to determine if the Johnson County Library is managing the Library Special Use Fund according to Kansas statutes and if expenditures made from this fund were appropriate. The audit included these objectives:

- Financial review of the Library Special Use Fund
- Testing of expenditures for compliance with the policies, procedures, and internal controls applicable to the Library Special Use Fund
- Review of the Library Special Use Fund management systems

**Scope and Methodology**

Our period of audit included transactions from January 1, 2004, through December 31, 2005. We reviewed the following:

- Policies and procedures for compliance with County policies and applicable laws, rules and regulations,
- Procedures for the Library purchasing,
- A random sample of expenditures made from the SUF which included P-Card purchases, as well as purchases over and under \$10,000,
- Kansas statutes, and
- Board of County Commissioners minutes and resolutions.

We interviewed management and staff members to obtain an understanding of management and internal controls. We had staff members explain how they performed tasks relating to purchasing and accounting with the SUF.

We also consulted with Library staff, Library counsel, County counsel, the Office of Financial Management, and the Department of Budget and Financial Planning to obtain an understanding of the use and functionality of the SUF.