



Johnson County Auditor
Johnson County, Kansas
PERFORMANCE AUDIT

February 19, 2009

Airport Management Audit

Management needs to document procedures and internal controls.



Johnson County Audit Services

February 19, 2009

To: The Johnson County Board of County Commissioners
Lee Metcalfe, Executive Director, Johnson County Airport Commission

In accordance with the approved audit plan, we performed an audit of the Johnson County Airport Commission (Airport). This audit reviewed the overall management practices of the Johnson County Airport. The audit reviewed agency-wide practices and procedures for compliance with laws, rules, and regulations as well as County policy. We reviewed transactions for the period 2006-2008.

The Airport was organized and generally well managed. We did not find any major issues in our review of purchasing, travel and meal expenditures, or contracts.

We found the Airport lacked written internal policies and procedures to ensure internal controls were documented and maintained. The lack of internal procedures led to non-compliance with County policy and Federal requirements.

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 Department's staff during this audit.

William D. Miller, CIA, CGFM
County Auditor

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AIRPORT MANAGEMENT AUDIT

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RESULTS AND RECOMMENDATIONS

1. Airport Management Has Not Established Internal Policies and Procedures

The Johnson County Airport Commission (Airport) does not have written policies and procedures documenting the Airport's business processes. The lack of documented policy and procedures led to the following:

- Poor cash receipt controls with a lack of segregation of duties
- Non-compliance with A-133 grant requirements
- No physical inventory performed of fixed assets, computer, or equipment inventories
- Non-compliance with County requirements for use and reporting of County owned cellular phones

Airport Management did not see the need for documentation of internal controls and business processes prior to our audit because, as a small organization with low staff turnover, employees were aware of their responsibilities and duties. Management believed following County policies and procedures was sufficient. However, the lack of written internal policies and procedures led to variances from County policies and procedures, weakened internal controls, and put cash and other assets at risk for fraud, misuse, and abuse. Written policies and procedures are also important for the orderly transition and orientation of new staff during staff transitions.

Recommendations

We recommend the Executive Director, Johnson County Airport Commission:

- 1.1 Develop and implement written policies and procedures documenting the internal controls specifically for the business processes of the following areas:
 - Billing and cash receipt
 - Accounts receivable
 - Grant management, receivables, and inventory of assets purchased with grant funds
 - Fixed assets inventory
 - Assignment, use and reporting of Airport owned cellular phones and mobile communications devices
- 1.2 Improve segregation of duties by working with the Johnson County Treasurer to establish a process of receiving cash payments directly through the Treasurer's cash receipt functions.

Management Comments

While Airport Management has in fact established internal procedures, we were not aware of the GAAP requirement to document such internal policies and procedures beyond those addressed in the County's published policies and procedures. Staff are in the process of documenting internal policies and procedures per the Auditor's recommendations.

With regard to segregation of duties, Staff will continue discussions with the Treasurer's Office and Oracle support staff with the objective of transferring cash receipts processing responsibility to the Treasurer's Office.

Discussion

Airport Business Processes

The Airport Commission manages and operates two airports, a business park, a railroad, and a water plant. The Airport generates revenue from leasing land and buildings for business and manufacturing operations, leasing land for agricultural purposes, and renting hangars for airplane storage as well as additional services such as rail car management and sales of water. The total revenue generated from these operations was \$4.4 million in 2006 and \$4.6 million in 2007.

The Airport receives additional funds from Federal Aviation Administration (FAA) grants. The Airport received a total of \$4.9 million in FAA grants between March 2004 and June 2008. FAA grants are subject to Office of Management and Budget (OMB) A-133 circular federal grant requirements.

The Airport maintains an inventory of 20 computers and 60 heavy equipment items such as, tractors, industrial mowers, road graders, trucks and SUV's. None of the items in the inventory were purchased with grant funds since all of the grants are either for planning or construction.

County financial policies and internal controls

Johnson County Financial Policy 100.3 requires County departments to follow generally accepted accounting principles (GAAP) and submit to annual audit of the County's financial statements. The Office of Financial Management (OFM) requires County departments to establish and document internal controls in order to comply with GAAP and in preparation for the County's annual audit.

Written policies and procedures were needed

Internal controls are processes set up within an organization to minimize fraud. The management of each County department is responsible for defining, implementing, and enforcing internal controls for the processes within its department. Internal controls include, but are not limited to, segregation of duties, security of assets, and reconciliation of county records.

Airport needs to segregate duties for billing and cash receipts

Airport management did not maintain adequate internal controls over billing and cash receipts. The Airport has two administrative staff performing billing, cash receipts, and recording accounts receivables (AR). One staff member's primary duty is billing and the other's primary duty is cash receipts and recording. However, the billing staff acts as the back up for the cash receipts staff and vice versa.

County departments are required to maintain a segregation of duties. Segregation of duties means ensuring one employee does not handle an entire process, such as ordering, approving and receiving, where fraud can be hidden more easily.

The Airport has limited staff to ensure a segregation of duties is maintained. Both staff members have access to billing, receipt, recording and deposit functions to provide backup when one is absent.

The County Treasurer's Office handles collection and receipt recording for departments such as the County Assessor's Office and Wastewater. Airport management should consider working with the County Treasurer's Office to perform receipt collection and recording functions in order to ensure segregation of duties are maintained. Airport management should also document and enforce internal control processes for billing and cash receipts in order to comply with County financial policies and requirements.

Airport needs to maintain internal controls for federal grant requirements

Airport management did not have any written internal policy or procedures for grant management. Written policy and procedures document the agency's processes and internal controls for grant expenditures and for compliance with grant requirements.

The Airport is required to document these controls to comply with OMB Circular A-133¹ grant audit requirements and the County's policy to follow GAAP. OMB A-133 subpart C requires auditees (grant recipients) to maintain internal control over Federal programs that provides reasonable assurance that the auditee is managing Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a material effect on each of its Federal programs.

Airport staff was not aware of the OMB A-133 requirement to maintain written internal control policies and procedures.

The Airport has multiple fraud risks, including contract fraud, when it does not have sufficient and documented internal controls. It is Airport management's responsibility to ensure sufficient internal controls are in place and documented to protect the Airport, monitor the contractors who provide the planning and construction on these projects, and ensure the appropriate use of federal funds.

Airport needs to perform physical inventory of assets

Airport staff maintained a detailed listing of equipment, capital assets, and computers but did not perform a periodic physical inventory of the equipment to ensure all assets were accounted for. We found one John Deere skid loader, worth \$43,000, that was not included on the equipment or capital assets listing. The skid loader had been reported to OFM as a capital asset but was not added to the internal inventory list.

¹ Federal Office of Management and Budget (OMB) grant requirements for the audits of state and local governments receiving federal grants are cited in the A-133 circular.

County Financial Policy 160.2 requires all assets with a value over \$1,000 be recorded and periodic physical inventories be performed. Items worth less than \$1,000 should be inventoried as needed for prudent care of County funds and property.

Airport staff did not perform any periodic physical inventories of the assets because they felt most of the equipment was large enough they would know if it was missing. If Airport staff had performed a physical inventory of the equipment, they would have known the skid loader had not been added to the inventory listing.

Physical inventories are required

Airport staff did not have any written procedures or internal controls to follow for documenting and testing of Airport equipment, capital assets or computers. Airport management should establish internal procedures documenting internal controls to ensure that assets are protected and accounted for.

Airport needs sufficient internal controls over County owned phones and to report fringe benefits

The Airport management did not document procedures or internal controls for use of its cellular phones assigned to employees. In addition, the Airport did not report the value of the phones to OFM as fringe benefits for employees they were assigned to. The Airport paid a total of \$12,765 in cellular phone charges for five County owned phones between July 1, 2006 and June 30, 2008.

Johnson County Human Resources Policy 515 requires agencies to report taxable fringe benefits according to federal and state laws. Procedure 515.2 requires agencies report monthly cellular phone billing amounts to OFM. The County will include the total amount of individual plans and allocate amounts of the pooled plans on employee's W-2's as taxable fringe benefits.

Procedure 515.2 also requires agencies to develop guidelines to ensure employees use assigned cellular phones according to County policy. County agencies are responsible for reviewing monthly bills to ensure employees:

- Use the most efficient and cost effective usage plans
- Use the phones in the most efficient and economical manner
- Use the phones for personal use reasonably and within the agency's guidelines

Airport management was aware of the policy but did not to pursue or enforce it. The Deputy Director said he reviewed the cellular phone bills for reasonableness but had not developed written guidelines to hold employees accountable. Airport management said they would start complying with the County policy and submit monthly phone charges to OFM as required.

Airport management needs to develop procedures and guidelines to document internal controls and ensure County policy is followed. The Airport is at risk for abuse of the cellular phones without specific procedures or guidelines for holding employees accountable. Also, documented policies and procedures are critical elements for succession planning to smooth employee

transition during turnovers. This is especially important when the staff sizes are small and many responsibilities are vested with a single employee.

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2. Staff Did Not Reconcile and Report All Accounts Receivables

Airport staff did not report all accounts receivables (AR) at year end. Staff did not perform a reconciliation of the AR because the software program used for billing and recording AR did not have sufficient reporting capabilities. Staff did not fully understand the year end reporting requirements and only reported those accounts with balances over \$2,000. As a result, the Airport underreported accounts receivable by \$222,700 in 2006 and \$327,527 in 2007.

In addition, Airport staff delayed billing the FAA until 2008 for reimbursable grant funds for two projects that were completed in 2007. Staff waited until the projects were signed off by the FAA before the final billing. Because staff believed the issuance of a bill was needed to recognize a receivable, \$11,002 in grants receivable was not recorded in 2007. This additional receivable was not reported to OFM at year end.

Recommendations

We recommend the Executive Director, Johnson County Airport Commission:

- 2.1 Ensure staff performs a reconciliation of the AR by account and reports all AR to the Office of Financial Management at year end.
- 2.2 Ensure staff reports receivables from federal grants to the Office of Financial Management at year end along with other accounts receivables.

Management Comments

Staff reported Accounts Receivable precisely as instructed by the Office of Financial Management. We did not learn until the audit that the written instructions issued by OFM were not worded to reflect what OFM really intended.

Discussion

County Policy and Financial Guidelines

County Financial Policy 100.3 states all agencies, departments, elected officials, boards, commissions, representatives, and authorized agents:

...will follow accounting principles generally accepted in the United States of America applicable to government units (GAAP), as promulgated by the Governmental Accounting Standards Board (GASB), in the preparation of the County's annual audited financial statements.

The Office of Financial Management (OFM) has developed Accounts Receivable guidelines and Year End Closing guidelines to ensure County agencies and departments are following generally accepted accounting principles for reporting financial information. These guidelines require departments or agencies that bill for services to report all accounts receivable in aggregate over

\$2,000 and all amounts written off. County financial data is reported in the Comprehensive Annual Financial Report, and the Schedule of Federal Expenditures of Federal Awards (Single Audit).

Aggregate Accounts Receivable amounts were not reported

Airport staff did not report the total AR amounts due to the Airport in 2006 or 2007. The table below shows the underreported amounts:

Table 2.1: Accounts Receivable Underreported

Year End	Actual AR	Reported AR	Unreported AR
2006	\$ 348,354.93	\$ 125,654.58	\$ 222,700.35
2007	\$ 357,486.61	\$ 29,959.77	\$ 327,526.84

Source: Audit Services analysis of accounts receivable records 2005 -2007

Airport staff did not understand year end guidelines for reporting AR. OFM intended to receive reports on AR from any department with more than \$2,000 in total AR. Airport staff only reported those accounts with a balance exceeding \$2,000. Once the \$2,000 threshold is met, all AR balances, regardless of balance, should be reported.

Airport staff did not use GAAP when preparing AR amounts to report. Staff did not perform an appropriate reconciliation by account to ensure that AR amounts were accurate because the AR software used prior to 2008 only produced basic reports for billing purposes. Staff did not take into account year end balances from prior years when calculating the total AR amount owed and therefore underreported total amount owed by account.

Airport staff did not bill the FAA for some work completed in 2007. These amounts should have been reported to OFM as grant receivables. Table 2.2 shows the federal projects with unbilled amounts at year end 2007.

Table 2.2: Unbilled Federal Contract Amounts

Project	Award Amount	Unbilled at 2007 year end
New Century Master Plan	\$146,229	\$ 7,891
Taxiway Lighting	533,519	3,111
Total	\$679,748	\$11,002

Source: Audit Services analysis of grants receivable records 2005 -2007

The Airport made these payments to the contractors for both grants for work completed in July 2007. Airport staff delayed billing the FAA for reimbursement in both cases because the FAA was required to sign off on the master plan and taxiway lighting prior to the final billings being approved for reimbursement. Airport staff should have reported grants due from the FAA totaling \$11,002 to OFM at 2007 year end.

Airport staff should reconcile and report all accounts receivable and federal awards due to the Airport during year end reporting to ensure the Airport is in compliance with County policies and procedures which require departments and agencies to follow GAAP requirements.

3. Executive Director's Purchasing Card Transactions Were Not Appropriately Reviewed

The Airport's Executive Director's purchasing card (P-Card) transactions were not reviewed by anyone with a position of authority to question purchases. A subordinate reviewed and approved the Executive Director's transactions. Airport management was not aware P-Card guidelines require a cardholder's transactions to be approved by someone with authority over the cardholder. Airport management creates an inherent risk in the internal controls of approval hierarchy by allowing subordinates to approve P-Card transactions. The Airport is at risk for fraud, misuse or abuse of funds without an appropriate separation of duties and hierarchal approval system.

Recommendation

We recommend the Director, Johnson County Airport Commission:

- 3.1 Ensure all the Executive Director's P-Card transactions are reviewed by a member of the Airport Commission, supervisory to the Executive Director and the Transaction Approval Report is signed by the reviewer.

Management Comments

While we believe the Deputy Director is in a better position than the volunteer chairman or treasurer of the Airport Commission to judge what charges are appropriate and in keeping with County policy, procedures will be modified to include the chairman or treasurer in the approval process. This may delay the submission of P-Card reconciliations, as the Airport Commission only meets on the fourth Wednesday of each month.

Discussion

The County's P-Card is a purchasing tool used to save costs in processing daily purchases under \$10,000 needed to carry out business. The Airport has 11 employees assigned active P-Cards. P-Cards can be a safe and cost efficient way for the employees to make purchases, but the Airport needs to ensure the County P-Card Guidelines containing proper internal controls are followed.

Airport management has designed specific procedures for the use of purchasing cards for Airport employees. These procedures include documented internal controls. However, not all of the County's P-Card guidelines are included in the procedures.

County P-Card Guidelines

The County P-Card guidelines define the Card Approving Official as:

The person who will review and approve the Transaction Approval Report, ensuring that they are complete, accurate, and reflect only authorized purchases....

Approving officials' responsibilities include signing the Transaction Approval Report. The guidelines require the approving official be someone in position of authority over the cardholder. Subordinates or peers are not allowed to sign and approve the report.

Airport Executive Director's transactions were approved by a subordinate

The Deputy Director reviewed and signed the Executive Director's P-Card transaction reports. From January 2006 through December 2007, the Executive Director charged \$3,711 on his P-Card. The Airport Commission did not review any of his individual P-Card purchases.

Airport management was not aware P-Card guidelines were changed in 2005, requiring all cardholders' purchases to be approved by someone in a position of authority over the cardholder.

P-Card guidelines
require supervisory
approval

The Executive Director's purchase limit was \$3,000 per transaction and \$10,000 monthly. The cardholder's transaction and monthly purchasing limits determine monetary risk for the department. The Executive Director's maximum purchase was \$525 during our audit period, but his purchasing limit presents the maximum risk to the department.

The Airport management puts the subordinate in an awkward position if any of his superior's transactions should be questioned. The Airport should have someone in a position of authority reviewing the Executive Director's purchases and reduce the risks of fraud, misuse and abuse.

OBJECTIVES, SCOPE AND METHODOLOGY

Objectives

This audit reviewed the overall management practices of Johnson County Airport Commission (Airport). The audit reviewed agency-wide practices and procedures for compliance with laws, rules, and regulations as well as County policy. The audit tested programs for efficiency and effectiveness.

Specific objectives for this audit included:

- Review Accounts Payable and P-Card expenditures to determine if savings can be achieved by eliminating waste and determine if internal controls are in place to reduce risk in purchasing.
- Review purchasing practices to ensure compliance with applicable County policies and procedures including the utilization of purchasing within County established contracts.
- Review employee meal and travel expenses to determine if the department is in compliance with applicable County policy and procedure and if effective management controls are in place over such expenses.
- Review contract and grant management to determine if contracts are managed effectively and efficiently.
- Review Accounts Receivable, and billing procedures to determine effectiveness and efficiency in billing and collections.
- Perform an asset inventory review to determine compliance with applicable County policies and procedures.
- Review any “shadow” system software in use.

Background

Johnson County Airport Commission manages two airports, New Century Air Center and JOCO Executive Airport. The Airport Commission is appointed by the BOCC and serves as the Board of Directors for the airports. The Airport Commission appoints an executive director to manage day to day operations. The airport is a vital county service for small aircraft operators. The functions of the Airport are varied and include rental services for some aspects of operations.

The BOCC has adopted a policy requiring the Airport Commission to attain self-sufficiency.

Scope and Methodology

In order to accomplish the objectives we reviewed:

- County wide financial and purchasing policies and procedures
- Billing and Accounts Receivable processes
- Accounts Payable invoices from July 2006 through June 2008
- P-Card transactions from July 2006 through June 2008
- Accounts Receivable data from January 2006 through December 2007
- Capital Asset, Equipment, and computer inventory
- Grant management practices

Computer Data

We used data from various computer systems in performing this audit including, but not limited to: The County's Oracle financial and human resources system (Oracle) and the Airport's billing and AR software.

The Oracle system data has been validated by others as part of the annual audit process. We did not rely on any other systems other than to make selections for testing purposes.

Statistical Sampling

We used statistical and judgment sampling to select items for review. We used statistical sampling to select testing samples in a number of audit steps. Where statistical sampling was used, we designed our samples to provide 90 percent assurance with a 5 percent margin of error. Both sample sizes and items to be reviewed were generated by commercial statistical software. Judgment sampling was used primarily for attribute testing – procedural compliance.