



County Technical Assistance Service
INSTITUTE FOR PUBLIC SERVICE

INTERNAL CONTROLS

HIGHWAY DEPARTMENT

2016

CTAS.TENNESSEE.EDU

INTERNAL CONTROLS

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Table of Contents

1.Introduction.....	2
2.Internal Controls Questionnaire	4
3.Internal Controls Assessment	10
4.Internal Controls Checklist.....	19
5. Appendix	
a)Public Chapter 112	30
b)Sample Risk Assessment	32
c)Article: What CPAs Can Learn from Dixon, Illinois	34

INTRODUCTION

As governmental entities across the county have seen an increase with waste, fraud and abuse the Tennessee General Assembly took proactive steps this legislative session by passing Public Chapter 112 which amended T.C.A. 9-18-102(a). The amendment provides the following:

Whether obligations and costs of the operation are in compliance with applicable law; (II) Whether county funds, property and other assets that are designated/assigned to the highway department are safeguarded against waste, loss, unauthorized use or misappropriation and (III) Whether revenues and expenditures in the highway department's fee account and county general fund (as it relates to the highway department) are properly recorded and accounted for to permit the preparation of accurate and reliable financial and statistical reports and to maintain accountability over the assets.

To assist TN counties with compliance CTAS has worked diligently to prepare an Internal Controls toolbox. The toolbox consists of the following tools: (1) internal controls questionnaire, (2) internal controls assessment, (3) segregation of duties checklist, and 4) sample internal controls risk assessment. In addition to the tool box CTAS has prepared a 4-hour internal control class. Beginning January 7, 2016, CTAS will begin the internal controls training on a statewide basis and concluding in March.

We at CTAS hope each elected official and their staff take advantage of our training and our tool box to prepare their internal controls that will allow them to comply with PC 112 and to provide a better system of financial management.

HIGHWAY DEPARTMENT
SAMPLE INTERNAL CONTROLS QUESTIONNAIRE
January 2016

Sample Internal Control Assessment Questions

Highway Department

Summary: The following assessment questions are divided into three parts to address the changes in T.C.A. 9-18-102(a): (I) Whether obligations and costs of the operation are in compliance with applicable law; (II) Whether county funds, property and other assets that are designated/assigned to the highway department are safeguarded against waste, loss, unauthorized use or misappropriation and (III) Whether revenues and expenditures in the county highway fund are properly recorded and accounted for to permit the preparation of accurate and reliable financial and statistical reports and to maintain accountability over the assets.

I. Whether obligations and costs of the operation are in compliance with applicable laws

Purchase orders:

- a) What is the county purchasing policy?
- b) Who originates purchases?
- c) Who makes sure funding is available?
- d) Who authorizes the purchase?
- e) Who places the order?
- f) Who verifies the goods received?
- g) Is there a different protocol for items ordered online? If so, what is it?
- h) What is the protocol for large items?
- i) What is done with the invoice?
- j) What is the protocol for blanket purchase orders?
- k) Who reviews the shipping tickets?

Store cards:

- a) Where are store cards (e.g. Walmart, Lowe's) kept?
- b) Who is authorized to go to the stores?
- c) Can blanket purchase orders be made on the store cards?
- d) Who approves the purchases?
- e) Who reviews the invoices?
- f) What records are sent to the county finance department?

Credit cards:

- a) Credit cards are not utilized (if credit cards are used, recommend a written policy and then review actual operations to ensure compliance with policy).

Contracts:

- a) Who signs contracts dealing with purchasing?
- b) How are contracts chosen?
- c) How are contracts over one year in length approved?

- d) Who reviews the contracts?
- e) Who ensures contract compliance within the county purchasing policy?

Emergency purchases:

- a) Who is in charge of coordinating with the county finance department in the case of emergency purchases?
- b) Where can one find protocol for emergency purchases?

Payroll:

- a) How is payroll authorized?
- b) Who prepares it?
- c) Who manages the budget throughout the year?
- d) Who is responsible for foreseeable budget overages?
- e) What type of account is used for payroll and why?

II. Whether county funds, property and other assets that are designated/assigned to the highway department are safeguarded against waste, loss, unauthorized use or misappropriation

Receipting:

- a) Who receipts checks?
- b) Are all individuals that are authorized to receipt and/or have access to county funds covered by the county blanket liability bond/insurance? This would include interns, temporary and seasonal employees, part time workers from a human resource agency.
- c) How are funds receipted?
- d) Where are receipted funds stored?
- e) Who takes the receipted checks to the trustee's office?
- f) How often are they taken?
- g) How is proof provided that the checks were taken to the Trustee office?
- h) How does the highway department ensure their records match up with the trustee's balance?
- i) Who receipts the check if the office manager is absent?

Bulk fuel pumps:

- a) Where are bulk fuel pumps maintained?
- b) How is fuel bid out?
- c) Who delivers it?
- d) Can other county departments/non-profits purchase gasoline from the Highway Dept?
- e) How do employees/other county departments document their fuel usage?
- f) Who collects the fuel tickets (if these are used)?
- g) Who sends out the fuel bills to county departments?
- h) Who places fuel orders?
- i) Who turns the fuel pumps on and off?
- j) How is the switch pad secured?
- k) How does the highway department secure the fuel pumps after regular work hours?

Payroll (with a centralized financial system, 1981, 1957 or some private acts)

- a) How does the department protect itself against fraud from employees?
- b) How do employees log their hours?
- c) How does the superintendent disperse duties to ensure everyone is working?
- d) Who collects and compiles payroll hours?
- e) How is vacation, sick and personal leave managed during the year?
- f) Are all employees paid the same way?
- g) Who reviews the checks?
- h) What is the cap for vacation, sick and personal time accrual?
- i) Does sick time roll over? If not, what happens to it?
- j) What happens when someone exceeds their maximum vacation/personal time?
- k) Who maintains and calculates the annual leave accrual for highway department employees?
- l) How are the expenditures ensured to be in line with the approved budget?
- m) Who does it?

Inventory of crushed rock:

- a) Where is crushed rock kept?
- b) How is it secured?
- c) How is the inventory kept up-to-date?
- d) How is it tracked?

Inventory of metal culvert:

- a) Where is metal culvert kept?
- b) How is it secured?
- c) How is the inventory kept up-to-date?
- d) How is it tracked?

Inventory of cold mix:

- a) Where is it stored?
- b) How is it secured?
- c) How is it tracked?
- d) How is the inventory kept up-to-date?

Inventory of vehicles and large equipment:

- a) How are vehicles inventoried?
- b) Who does the physical inventory?
- c) How are vehicles that meet depreciation thresholds logged?
- d) Who does this data entry into a computer system?
- e) How are all vehicles and large equipment identified as being county highway property?
- f) Who registers new purchases of vehicles and equipment in the department?
- g) How are the registrations logged?

- h) How are surplus sales taken out of the system?
- i) Who is responsible for removing the surplus equipment of the software system?
- j) Who is in charge of communicating what type of work vehicles and materials are to be used for?

Inventory of small equipment and tools:

- a) Who maintains an inventory of small equipment and tools?
- b) To whom are missing items reported?
- c) Where are tools kept that aren't assigned to a vehicle?

Liquid asphalt:

- a) How is the amount of asphalt needed by the department determined?
- b) Who orders the asphalt?
- c) Who records the amount used on each road project?
- d) What is done with leftover asphalt?

Hot mix asphalt:

- a) How is hot mix bid out?
- b) Who hauls it to the job site?
- c) Who performs the actual paving?
- d) Who verifies the contractor's billing with the bid price and the amount of asphalt received?
- e) Is anyone present to verify the load is delivered?
- f) How is proof shown that the loads were delivered?

Highway construction:

- a) How are the contractor and engineer bid?
- b) How is state-aid road construction tracked?
- c) Who is responsible for coordinating with TDOT to ensure all requirements are met?

Bridge construction:

- a) How are the contractor and engineer bid?
- b) How is the work being done by third parties and the department coordinated?
- c) How does the department keep record of the final cost?

III Whether revenues and expenditures in the county highway fund are properly recorded and accounted for to permit the preparation of accurate and reliable financial and statistical reports and to maintain accountability over the assets

- a) How does the department ensure receipted funds are coded to the correct revenue line item with the trustee?
- b) Who coordinates with the county finance department to ensure all purchase orders for non-payroll items are coded to the correct object code and expenditure budget?

- c) Who coordinates with the county finance department to ensure capital assets are up to date and in compliance with county asset policies?
- d) Who ensures the original highway fund budget was posted by county finance correctly?
- e) How does the department make sure revenues are coded correctly and are tracking in line with the budget revenues?
- f) How can the department be sure expenditures are in line with the budget?
- g) Who reports anticipated overages?
- h) Who reviews the year-end closing entries?
- i) Who reviews the capital asset listings?
- j) Who reviews and corrects audit findings?

HIGHWAY DEPARTMENT
SAMPLE INTERNAL CONTROLS ASSESSMENT
January 2016

Internal Control Assessment of Sample County Highway Department

Purpose: To document an understanding and assess the internal controls of the Sample County Highway Department as it pertains to the following:

- I. Whether the obligations and costs of the operation are in compliance with applicable law
- II. Whether county funds, property and other assets that are designated/assigned to the highway department are safeguarded against waste, loss, unauthorized use, or misappropriation
- III. Whether revenues and expenditures in the county highway fund are properly recorded and accounted for to permit the preparation of accurate and reliable financial and statistical reports and to maintain accountability over the assets

Overview: An in-depth analysis of the internal control environment for the operations of the Sample County Highway Department was performed over a two and a half day period by multiple county highway and finance department employees, as well as Pedro Gonzales, county road superintendent, and Rico Suave, the CTAS field consultant

Highway Department

- I. Obligations and costs of the operation are in compliance with applicable law

Ensure that contracts are in place for goods and services that are required by law, review purchasing procedures for non-payroll costs to ensure compliance with law, review payroll procedures to ensure that payroll is for legitimate and authorized employee costs only, review emergency purchase procedures for compliance with law, ensure any store cards and credit cards used by the department are in compliance with purchasing policy and law and are safeguarded. Review the above procedures for efficiency.

Purchasing: The Highway Department complies with the adopted county purchasing policy under the Financial Management System of 1981 that is in effect for Sample County Government.

Purchase Orders: Pedro Gonzales (Road Superintendent) will originate a purchase order requisition with the county finance department and Pedro or Ursula Winters (office manager)

coordinates with the finance department to ensure there is funding available in the line item for the purchase and that the vendor is on the approved vendor list. The county finance department issues the purchase order which authorizes the purchase to be made. Pedro, Ursula or a county highway employee will then place the order with the vendor and when the goods arrive (if the highway employee does not pick up purchase at a local store) the same people verify that the goods received are the goods itemized on the invoice. If goods are ordered online or over the phone and shipped to the highway department, Ursula will verify that the goods received are on the shipping list and invoice when delivered. If it is a large item (engine, heavy tractor part, etc.) that is shipped directly to the highway shop area, Ursula verifies with the shop employees that the goods received are the goods on the shipping list/invoice. The invoice is then initialed as goods received by Pedro and forwarded to county finance, along with the copy of PO requisition and gold copy of purchase order for payment by accounts payable. The highway department can utilize blanket purchase orders with numerous vendors (hardware store, auto parts store) and the vendor will send a monthly invoice, which Ursula reviews against the individual shipping tickets to verify they are legitimate county purchases of goods and that the person that picked up the goods at the store is a highway employee.

Store cards: Walmart and Lowes cards are kept locked up when not in use in Ursula's office in a filing cabinet. Ursula will go to these stores for needed purchases after a purchase order is originated for the purchase and approved by Pedro and the county finance department. Blanket purchase orders are not utilized for the store cards so every individual purchase with the cards is approved by the road superintendent prior to purchase. Ursula and Pedro will review the monthly invoices from these store card purchases together at the end of the month and then send the invoice over to the finance department with the purchase requisition and gold copy of the approved purchase order for payment.

Credit Card: The Sample Highway Department does not utilize credit cards.

Contracts: Per Sample County purchasing policy, the county finance director signs all county contracts dealing with purchasing. Once competitive bids are opened by the county finance office, the county road board reviews and awards the bids based on best and lowest price. All contracts that are over one year in length are approved by the county commission after the county attorney

reviews them. Ursula and Pedro coordinates with the county finance department to ensure contract compliance per county purchasing policy.

Emergency purchases: The road superintendent (Pedro) will coordinate with the county finance department in the case of emergency purchases that arise from unforeseen events that will require normal bidding procedures to be circumvented because of the nature of the emergency at hand. The county purchasing policy addresses emergency purchases and the highway department complies with these policies.

Payroll: Payroll is authorized each fiscal year through the annual county budget appropriation for the highway fund that is prepared by Pedro and then sent to the county commission for approval in compliance with the county uniform highway law. Ursula receives a copy of the adopted budget and then receives a monthly year-to-date expenditure vs. budget report from county finance each month. Ursula and Pedro will bring any anticipated, foreseeable budget overages to the attention of county finance in order that a budget amendment can be prepared timely. All payments to employees are paid thorough payroll accounts (not vendor accounts) in order to comply with IRS tax code for payroll taxes and state unemployment compensation and worker comp laws.

II. Whether county funds, property and other assets that are designated/assigned to the highway department are safeguarded against waste, loss, unauthorized use or misappropriation

Overview: The audited financial report detailed expenditure statements was reviewed to identify expenditures of material amounts and then internal controls over these items were scrutinized. In the highway department, material expenditure amounts were: payroll, liquid asphalt, crushed stone, diesel fuel, highway equipment, equipment and machine parts, and highway construction. Assets of the highway department that were identified through interview of staff and capital asset records and that are at risk for waste, loss, unauthorized use or misappropriation are cash receipts on hand, bulk fuel pumps at highway garage, vehicles, new metal tile inventory, scrap/recycle metal disposal, and surplus of highway equipment. Internal controls over these material assets/costs were scrutinized in-depth.

Receipt/disburse/deposit/reconcile/segregation of duties over cash:

The following procedure will be in place to help satisfy and insure compliance with internal controls over receipting at the highway department. The highway department does not maintain a bank account since all accounting for the department, except receipting, is handled by the county finance office. The highway department does not disburse checks as this is a duty of the county finance department as well. The highway department receives checks from the local library, property assessor, county agriculture center, county veterans' office, county finance office and the county solid waste department for gas reimbursement, scrap metal sales from the local scrap yard or from government deals for surplus property sales. The county highway department does not receipt cash.

1. Ursula Winters (office manager) will receipt checks into an official, pre-numbered receipt book and lock the receipted checks into a locked filing cabinet in her office.
2. Ursula will carry the receipted checks within three business days over to the county trustee's office and deposit these funds with the county trustee. The county trustee will issue a trustee receipt that Ursula will take back to the highway department office and keep on file. The trustee receipts are capable of being reconciled back to the individual highway department receipts that make up the total deposit that was made at the highway department. Pedro and Ursula keep a notebook at the highway department and enters into it an up-to-date cash with trustee balance of the highway fund by coordinating with the county trustee and finance office as an additional "check" to ensure that the cash with trustee balance is correct on the financial records of the county finance department.

Note: In the event of absence (extended sickness, vacation, etc.) Pedro would receipt the checks and make the deposit with the county trustee.

Bulk fuel pumps: The county highway department maintains bulk fuel pumps at the highway garage for diesel and gas needs. Fuel is competitively bid by the county finance department and is delivered to the bulk tanks by the vendor. Gasoline is purchased by the highway department and used for official highway business and sold to other county departments (see above) as well for county business. Tickets are completed by the county employees getting the fuel when vehicles are filled at the county pumps, which are located right outside the highway department office's window. These tickets are summarized by Ursula (office manager) and expensed/billed to the

various county departments monthly. The highway department has never had a problem with the other county departments paying their fuel bills timely. When the bulk fuel tanks get low, Ursula will place an order with the fuel vendor (who has an open PO) for additional fuel. The fuel pumps are powered off the highway office building's electric and are turned off from inside the shop each night and the switch box is padlocked (Highway superintendent, office manager, shop foreman and assistant superintendent have keys). The main gate to the highway department is padlocked at closing time as well.

Payroll: To protect against fraud (ghost employees, unauthorized bonus payments, etc.) all highway department employees have a personnel file maintained in the highway department office by Pedro and Ursula. All employees utilize a punch time clock in the county highway garage when they report for duty in the morning and when they end their shift. The road superintendent is present in the highway garage every workday at the beginning of the work shift to hand out daily assignments and to ensure all employees are at work. At the end of pay period, Ursula (office manager) collects the time cards and compiles the payroll hours for each employee for the pay period, notes any vacation and sick time taken and then submits this summary report to the county finance office for payroll processing. Ursula keeps a detailed balance per employee of accumulated sick, vacation and personal leave on file. Some employees are on direct deposit, others receive paper checks from Ursula after Pedro reviews the checks (and stubs for direct deposit). Personnel policy for the highway department caps the vacation accrual per employee at 3 weeks, sick time is capped at 96 hours and personal time at 160 hours. Any sick time not used at calendar year-end is paid out and the employee starts over accruing 8 hours per month. When/if an employee exceeds the maximum vacation/personal time cap (which is rare) then they are sent home for a day off as these overages are not paid out. An annual leave accrual summary is calculated by Ursula for external financial reporting purposes at the end of the fiscal year and forwarded to the county finance office. Ursula and Pedro review the monthly budget to actual expenditure reports to ensure the actual expenditures are in line with the approved budget.

Inventory of crushed rock, metal culvert and cold mix:

Crushed rock is kept on the back lot behind the maintenance shop and is secured behind a locked gate after hours. When rock is taken off the inventory pile, the drivers prepare a trip ticket that Ursula and Pedro use to reconcile the tonnage to the last large delivery runs. The rock is tracked

to each job site (road, bridge, right-of-way easements) by the road and bridge computer capitalization software system.

Metal culvert is kept on the back lot behind the maintenance shop and is secured behind a locked gate after hours. When culvert is taken off to a job site, the drivers prepare a trip ticket that Ursula and Pedro use to reconcile the culvert taken to the inventory on hand. The culvert is tracked to each job site (road) by the road and bridge computer capitalization software system.

A small load of cold mix (20 tons) is kept on hand for filling potholes. The pile is secured after hours. Since this is a small amount of material and the cold mix is used to fill holes of various sizes, the material is not tracked to individual job sites. Pedro keeps an eye on the quantity on hand and based on his numerous years of experience, would know if there was abnormal shrinkage of the cold mix.

Inventory of vehicles and large equipment: Ursula maintains an inventory of assigned vehicles on the highway capital asset software system. The inventory software records vehicle make, model, year, description, year purchased, purchase price, and VIN. Ursula coordinates with the county finance department to be sure that any vehicle or equipment that meets depreciation thresholds is on the county finance depreciation software. All vehicles and large equipment are marked as county highway property and numbered. Pedro will enter in any new purchases of vehicles and equipment into the highway department capital asset software and delete any surplus sales of equipment after these assets are no longer in use and declared surplus and sold. Pedro and his assistant road superintendent communicate to the county highway employees that no work or material is to be used for anything except county roads and jobsites.

Inventory of small equipment and tools: An inventory of small equipment, furniture and tools assigned to the county highway department is maintained and updated annually by Donald Duck, highway shop employee. Any missing items when the inventory is done are reported to Pedro. All tools that are not assigned to vehicles are kept in the highway department maintenance shop.

Liquid asphalt: Each road that is to be resurfaced, after the road is confirmed to be a county-owned road, is measured for distance and the needed quantity of liquid asphalt is determined. Liquid asphalt is then ordered by Pedro and a bulk carrier is dispatched from the vendor to spot load the liquid asphalt into the county-owned distributor. The amount used on each road project is recorded

and tracked by Ursula and Pedro in the road capitalization software system as well as reconciled back to the bulk load invoice. If there is a small amount of leftover liquid asphalt then the highway department will maintain this material in the 1500 gallon distributor truck for use in the county owned Dura-patch machine to be used for small patch jobs (road cuts, shoulder work, etc.) around the county. In the rare instance that there is a large quantity of liquid asphalt remaining in the vendor's delivery truck, the material is returned for a vendor credit.

Hot mix asphalt: Hot mix is competitively bid out in compliance with county purchasing policy. A third party is contracted to haul hot mix to the job site and to do the actual paving for large jobs. Pedro will verify that the billing from the paving contractor agrees with the bid price and that the tons of material charged for is what was received from the asphalt plant prior to approval of payment. A county highway employee is assigned to be physically present at each contracted paving site during construction to verify loads delivered and to sign trip tickets and take a copy of the tickets to Ursula.

Highway Construction: This expenditure line item is to track and separate all state-aid road construction in the financial records as requested by TDOT and the state comptroller's office. Road paving, striping, engineering, road signs and traffic control costs that are associated with state-aid roads are posted to this line item. The same internal controls for tracking the individual costs and assets (hot-mix, crushed stone, signs) are utilized for state-aid roads as well as TDOT required forms. TDOT reviews all state-aid expenditures to verify that funds were utilized in accordance with grant requirements. Pedro works closely with TDOT to ensure that grant requirements are met. All state-aid paving is capitalized and tracked on the highway capital asset software system.

Bridge construction: Bridge construction/replacement is bid out to a third party contractor and engineer in compliance with county purchasing policy and grant requirements. Pedro coordinates with the contractor and engineer to ensure that the bridge is placed as specified and that work is done prior to contractor draws as determined by the project contract. Pedro enters the cost of the bridge construction/replacement into the highway capital asset tracking software when the final cost is determined.

- III. Whether revenues and expenditures in the county highway fund are properly recorded and accounted for to permit the preparation of accurate and reliable financial and statistical reports and to maintain accountability over the assets

Ursula is responsible for coordinating with the county trustee's office to ensure that all receipted funds are coded to the correct revenue line item when she carries over the deposit. Ursula and Pedro coordinate with the county finance department to ensure purchase orders for non-payroll items are coded to the correct object code and expenditure budget. Ursula coordinates with the county finance office to ensure that capital asset records for external reporting purposes are up to date and in compliance with county capital asset policies.

Ursula and Pedro review the expenditure and revenue budget-to-actual report monthly for the highway fund to determine:

1. The original, approved highway fund budget was posted by the county finance office correctly.
2. Revenues were coded correctly and are tracking in line with the budgeted revenues
3. Expenditures are in line with the budget and if an overage is anticipated, that the county finance office is notified that a budget amendment will be requested.

The county finance office will post year-end property taxes receivable, any grant receivables, accounts payables and any encumbrances to the highway fund when they close the books. Ursula and Pedro will review these year-end closing entries. Pedro will review capital asset listings for external financial reporting and depreciation schedules with the county finance department to ensure accurate reporting and accountability of capital assets assigned to the county highway department.

Corrective action of any identified internal control deficiencies from independent audit: Pedro would review any audit findings that noted internal control deficiencies in the highway department operations and would seek to correct these weaknesses. As noted in Sample County's prior year audit, the highway department has no audit findings.

HIGHWAY DEPARTMENT
SAMPLE SEGREGATION OF DUTIES CHECKLIST
January 2016

County Highway Department
Internal Control Checklist
Receipts

See Column Instructions Below

Checks Received in the Mail		Daily Receipting and Depositing					
Open Mail Stamp All Checks for "Deposit Only" When Received	Issue Receipts for Mail-in Checks	Maintain Separate Cash Drawers	*** Issue Receipts for Over-the- Counter Checks	Stamp All Over-the- Counter Checks for "Deposit Only" When Received	Deposit Intact Check Out and Make Up Daily Deposit	Deposit all checks in the Trustee's Office	Verify Trustee's receipt with Check-out Sheet
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)

Seven-Person Office:

Highway Official	
Deputy Director Employee #1	
AP/Admin Employee #2	
AP/Admin Employee #3	
AP Employee #4	
AP/Payroll Employee #5	
Payroll Employee #6	
Payroll Employee #7	

					X		XX
X					XX		X
XX	XX	XX	XX	X		X	
XX	X	X	X	XX		XX	
							X

Column Instructions:

- XX** The Person indicated by the XX is the preferred person to perform the procedure.
- (1)** Two employees are assigned to open mail, stamp checks " For Deposit Only Acct# XXXXXX0954" immediately upon receipt. The acct. # on the stamp is the Trustee's Bank Account Number.
- (2)** Issue receipts for the mail-in checks in preprinted receipt book.
- (3)** A locked bank bag is issued to the employee responsible for receipting funds for that day
- (4)** Manually issue Receipts for Over-the-Counter Checks in the preprinted finance dept. receipt book.
- (5)** Stamp All Checks for "Deposit Only Acct# XXXXXX0954" immediately upon receipt.
- (6)** Combine the checks & money order receipts from the locked bank bag. Make an itemized list of all checks and money orders and total the list (Excel File). The deposit is made intact for each day or period. We aim to make deposits with the trustee daily. Keep all collections in a locked safe or file drawer until the deposit is made if deposits are not daily.
- (7)** Carry the deposit to the trustee's office and obtain a receipt from the trustee for the amount of the deposit.
- (8)** Verify that the amount on the trustee's receipt agrees with the check-out list from Column 6. Initial and date the trustee's receipt to indicate the review. Attach the trustee's receipt to check-out list and file for audit.

County Highway Official
Internal Control Checklist
Issuing Non-Payroll Checks

See Column Instructions Below

Issuing Non-Payroll Checks				
Non-Payroll Checks		Signature Authority		
Enter Invoices	Print & Attach Invoices Checks	Verify Amt. and Sign	Process & Mail Checks	Reconcile Acct Pay. Bank State.
(1)	(2)	(3)	(4)	(5)

Seven-Person Office:

Highway Official		XX		
Deputy Director Employee #1		X ~~		X
AP/Admin Employee #2	XX	XX	X	
AP/Admin Employee #3	XX		XX	
AP Employee #4	XX	X	X	
AP/Payroll Employee #5				
Payroll Employee #6				
Payroll Employee #7				XX

Column Instructions:

XX	The person indicated by the XX is the preferred person to perform the procedure.
~~	This person should only sign checks when the Highway Official is absent. See Column 2 Instructions.

Issuing Checks -

- | | |
|-----|---|
| (1) | Physically enter invoices and prepare for issuance of check. |
| (2) | Physically print checks & prepare the checks for signature. |
| (3) | Determines the reason and examine documentation for the issuance of the check. Sign the checks.
Sample County non-payroll checks require two signatures and are signed by the following: County Funds- County Mayor & Highway Official; Highway Fund- Highway Superintendent & Highway Official; School Funds- School Board Director & Highway Official. Backup signers for the Highway Official is the Finance Deputy Director, and the chairman for the other departments serve as backup signers. |
| (4) | Process the signed checks and invoices, stubs & check copies and mail. |
| (5) | Reconcile the accounts payable bank statements with the trustee and finance software |

County Highway Official
Internal Control Checklist
Payroll Checks

See Column Instructions Below

Issuing Payroll Checks								
Obtain Time-sheets. from Department Heads	Approve or Determine that Leave Balances/ Time-sheets have been Approved	Process Payroll Post to Gen Ledger & Online Check Stubs	Process Payroll ACH Direct Deposit	Determine that Payroll Deduction Accounts Clear out for each Payroll	Determine Amount of Payroll Tax Deposit	Approve Payroll Tax Deposit Sign Acct Pay Checks	Make the Necessary Deposits Net Pay & Taxes	Review Payroll Ledger / Register for Reasonableness
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)

Seven-Person Office:

Highway Official						XX		X
Deputy Director - Employee #1						X		X
AP/Admin - Employee #2							X	
AP/Admin - Employee #3							XX	
Acct Payable - Employee #4								
AP/Payroll - Employee # 5	X	X	XX	X				
Payroll - Employee # 6	XX	XX	X	XX	XX	X		XX
Payroll Employee #7		X			X	XX		

Column Instructions:

XX The Person indicated by the XX is the preferred person to perform the procedure.

Issuing Payroll Checks -

(1) Collect the time sheets from each department head.

(2) Sign the time sheets indicating approval of the hours presented and leave calculations, as applicable. Calculate salaries and deductions in software and proof with co-worker. All time sheets/cards are recalculated, signed by the employee, and signed as approved by the employee's supervisor. The Highway Official should ensure this has been done in every case. Each employee, even salaried employees, should complete some form of time and attendance record. Time and Attendance records should indicate leave taken and leave balances as well as time worked.

(3) Process payroll and post to general ledger. Upload check stubs into eStub software. Sample County doesn't issue physical payroll checks except in case of emergency, then checks are signed manually by the Highway Official or deputy Highway Official.

(4) Determine ACH accuracy and upload to bank online treasury management, build and release file for the necessary date(s).

(5) Determine that all payroll deductions are paid to proper payee and that payroll deductions clear out for each payroll period.

(6) Utilize payroll records to calculate the amount of the Payroll Tax Deposit.

(7) Approve the amount of the payroll tax deposit. Then electronically make the payroll tax deposit or supervise the performance of this procedure. Verify the amounts, sign the payroll or other payroll deduction checks.

(8) Mail or deliver, or deposit checks as applicable.

(9) The bookkeeper scans/reviews the payroll ledgers /registers for obvious errors or miscalculations and notes the total payroll amount and department totals. Scans the ledgers for new employees, employees that have no payroll deductions, look at overtime, compensatory time, look for persons who are paid from more than one account code, and similar unique items. Considers whether or not the amounts appear reasonable.

County Highway Official
Internal Control Checklist
Cash Reconciliations

See Column Instructions Below

Cash with Trustee - All Funds						Cash in Bank - All Funds			
Obtain the Trustee's Monthly Report	Obtain a list from the Trustee or prepare a list of outstanding checks.	Reconcile the Trustee's Cash Balance to Fund Cash	Investigate Old Outstanding Checks or Unusual Items	**	Receive, Open, and Review Bank Statements and Cancelled Checks	Perform Bank Reconciliation	Review Bank Reconciliation and Trace Reconciling Items and Balance to Acct. Records	**	
				Prepare any Necessary Adjusting Journal Entries				Prepare any Necessary Adjusting Journal Entries	
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	

Seven-Person Office:

Highway Official	XX		XX		XX			XX	XX
Deputy Director - Employee #1	X	X	X		X		XX	X	X
AP/Admin - Employee #2									
AP/Admin - Employee #3									
Acct Payable - Employee #4									
AP/Payroll - Employee # 5				X					
Payroll - Employee # 6									
Payroll Employee #7		XX		XX		X	XX		

Column Instructions:

XX	The Person indicated by the XX is the preferred person to perform the procedure.
**	See additional instructions for Journal Entries under the Journal Entries Tab.

Cash with Trustee Reconciliation

- (1) The trustee provides a report of receipts, disbursements, and cash balances during the month or shortly after the end of each month.
- (2) Determines which checks are outstanding and, therefore, not yet deducted from the trustee's cash balance. Makes a list of outstanding checks. Includes the date of issuance, the payee, and the amount for each outstanding check.
- (3) Reconciles the general ledger account - "Cash with Trustee" - to the cash balance shown on the trustee's report for each fund under the authority of the financial act of 1981.
- (4) Finds out why old outstanding checks have not cleared. Investigates any other unusual items from the trustee's report.
- (5) Often there are differences between the trustee's cash balance and the general ledger account - "Cash with Trustee" other than outstanding checks. For example, the bank paid a check for an amount different from the amount it was written for fund transfers, and receipts or disbursements posted to the wrong fund via manual checks, etc. These types of differences may require a journal entry to bring the Trustee's cash balance into agreement with the General Ledger Account - "Cash with Trustee". Differences should be investigated and corrected each month. The Highway Official and Deputy Director have this duty and back each other up.

Monthly Bank Reconciliation - Use only if the Finance Office maintains any bank accounts outside the Trustee's Office.

- (6) A person who is **not** responsible for reconciling the bank should open the bank statement and review it for unusual transactions, bank transfers, bad checks, and if possible, cancelled checks. Trace deposits-in-transit, bad checks, outstanding debits or credits, outstanding checks, etc. from the **previous bank reconciliation** to the current bank statement. Ensure that interest earned was posted to accounting records if applicable. Initial and date the statement indicating that you opened and reviewed the statement. (If possible, get copies of cancelled checks, front and back, in your bank statements.)
- (7) Obtain the bank statement after it has been initialed and reviewed as directed in Step 6. Perform the bank reconciliation. This is done monthly.
- (8) A person who is **not** responsible for reconciling the bank should review the bank reconciliation. Trace the balance on the bank reconciliation to the general ledger. Make sufficient inquires to understand reconciling items (i.e. Deposits-in-transit, bad checks, outstanding debits or credits, interest earned, large or unusual outstanding checks, etc.). Trace at least some of the reconciling items to underlying accounting records. Initial and date the reconciliation to indicate the review.

County Highway Official
Internal Control Checklist
Trade Accounts Receivable
Reconciliations

The Finance Office does not have active trade accounts. We collect misc. receipts only.

See Column Instructions Below

Trade Accounts Receivable (A/R) - All Funds

	Add:	Subtract:		The	The		**
Obtain Beginning Receivable Balance	Amounts Billed to Customers Current Month	Collections, Adjustments, Write-Offs	Ending Receivable Balance Equals Column 1+2-3	Balance from Column 4 should agree with the total of all Individual Accounts	Balance from Columns 4&5 should agree with the General Ledger	Locate and Explain any difference between Columns 4, 5, & 6	Prepare Necessary Correcting Journal or Other Entries
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)

Seven-Person Office:

Highway Official
Deputy Director - Employee #1
AP/Admin - Employee #2
AP/Admin - Employee #3
Acct Payable - Employee #4
AP/Payroll - Employee # 5
Payroll - Employee # 6
Payroll Employee #7

XX	XX	XX	XX	XX	XX	XX	XX
X	X	X	X	X	X	X	X

Column Instructions:

XX	The Person indicated by the XX is the preferred person to perform the procedure.
**	See additional instructions for Journal Entries under the Journal Entries Tab.

Trade Accounts Receivable (examples are ambulance, landfill, and utility receivables)

- (1) Obtain the beginning balance of trade accounts receivable. This balance should exist in the accounting records. If a record of the beginning balance (i.e. accounts receivable control record) does not exist, this is an indicator that internal controls either do not exist or are not working.
- (2) This amount should be the total amount billed to customers during the current month.
- (3) This amount should be the total of all collections, adjustments, and write-offs that reduce the accounts receivable balance. **(Important: No accounts receivable balance should be written-off without a write-off policy and approval of the county commission or its designee.)**
- (4) The sum of columns 1+2-3 should equal ending accounts receivable. This is separated in three steps for illustration purposes. In an automated system, this is essentially one step with the system printing a report. However, the bookkeeper and **someone not associated with the accounts receivable records** should be reviewing the totals of billings, collections, and write-offs for reasonableness each month.
- (5) The accounts receivable records should have a summary (control record) and a detailed list of accounts receivable by individual customer. The summary (control record) accounts receivable total should agree with the total of all the individual customer receivable balances. This should be verified every month.
- (6) The summary (control record) and the individual customer balances total should agree with the general ledger accounts receivable balance. This should be verified every month.
- (7) Any difference between the accounts receivable balances on the control record, the detailed list and the general ledger should be investigated and corrected each month. Any consistent or significant differences should be reported directly to the Highway Official
- (8) Prepare the adjusting journal entries to correct the differences.

County Highway Official
Internal Control Checklist
Purchasing

See Column Instructions Below										
Purchasing										
Obtain Requisition From Department Heads For Encumbrance	Issue Detailed Purchase Order for which records Against Budgets	Approve the Purchase Order	Order Goods/Services Based on Approved Purchase Order	Receive Ordered Goods/Services	Sign Invoice or shipping Documents Indicating the Goods/Services Were Received	Match Shipping Documents, Purchase Order, and Prepare for Check Issuance	Print Checks attach to Invoice, Etc.	Sign & Approve Check for Payment	Process Payment check stubs, etc. Mail	Determine the Disposition of any Unused Purchase Orders
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)

Seven-Person Office:

Highway Official	X	X	XX	XX	X	X			XX		X
Deputy Director - Employee #1	XX (Schools)		X	X	X			X			X
AP/Admin - Employee #2		XX				XX	X	XX		X	
AP/Admin - Employee #3										XX	
Acct Payable - Employee #4		X				XX	X				XX
AP/Payroll - Employee # 5	XX (Co/Hwy)			XX	XX	X					
Payroll - Employee # 6											
Payroll Employee #7											

Column Instructions:

XX The Person indicated by the XX is the preferred person to perform the procedure.

Purchasing

- (1) The finance office obtains a requisition or obtains purchase information based on the current county purchasing policy. The name of the person making the request, the method of the request (e.g. by telephone) and the date is documented. The request is detailed. The brand, quantity, product order number, price and total purchase amount is documented. Requests for purchase orders that do not include complete information are not accepted. The request normally comes from a department head or the department head's designee. Departments don't generally have multiple employees who make requests for purchase orders except in few circumstances as designated by the elected official or department head.
- (2) Issue the purchase order for approval. A yellow copy of the purchase order goes to the department that ordered the goods/services. The original green document goes to finance accounts payable personnel to match with the supporting documentation for payment purposes, then attached to check. This data entry of the purchase orders automatically record against the individual budgets.
- (3) The Highway Official or designee determines whether bid laws and local purchasing policy have been followed and ensures the purchase order is completed in detail and ready for approval. The purchase order is approved by two signatures for county and highway and one signature for schools. The Highway Official and deputy director sign for approval, and then the county mayor, highway superintendent or chairman of the county commission or highway commission sign for approval. The school director has opted to sign the requisition only. The school purchase orders require only one signature; the Highway Official or deputy director.
- (4) Physically order the goods/services as listed on the purchase order. Sometimes this will be completed in the finance office, and sometimes this will be done by the department head or a specific department designee. Local vendors of goods/services are advised of the persons who are authorized to make purchases on behalf of the government. Local vendors are also advised that no goods or services can be purchased without an approved purchase order for items over \$25.
- (5) The finance office, the department head, or a specific department designee receives the order.
- (6) Once the goods have been shipped and received or the service rendered, the finance office, the department head, or a specific designee checks the order and signs/dates the purchase order, the invoice, or the shipping documentation indicating that the goods/services have been received as ordered. The documents then go to finance accounts payable personnel.
- (7) Once the goods have been shipped and received or the service performed, the Finance Office accounts payable personnel receives the shipping documents, invoices and then matches e Purchase Requisition, Purchase Order, Shipping Documents, Invoice, etc. and prepares the invoices for payment. This will be the documentation used to approve the checks.
- (8) A different accounts payable clerk then selects the previous accounts payable clerks items that are ready for check issuance, prints the corresponding check and attaches it together for signature & approval.
- (9) The Highway Official or deputy director approve the check for payment. All non-payroll checks require two signatures for approval. The county mayor, highway superintendent and director of schools sign for the funds for which they are responsible. If they are not available, the chairman from each of their boards is the second approving signature.
- (10) A third admin/accounts payable clerk processes the payments and mails the checks.
- (11) Purchase orders are reviewed and maintained on a monthly basis by an accounts payable clerk to determine if the services/goods have been cancelled or postponed. A determination is made as to whether the outstanding purchase orders should be liquidated or amended. The Highway Official and deputy Highway Official review the outstanding purchase orders as well in maintaining the budgets, amendments and reports to the department heads and commission/boards.

County Highway Official
Internal Control Checklist
Grants

See Column Instructions Below					
Grant Performance and Documentation					
Obtain Co. Commission's Approval to Apply for the Grant	Read the Grant Contract. Also Obtain and Read OMB's Uniform Grant Guidance	Maintain Central Grant Documentation Files	Maintain Separate General Ledger Revenue and Expenditure Accounts for Each Grant	Mark or Tag Grant Equipment and make an Inventory listing by Grant	Physically Observe the Equipment on the Inventory Listing
(1)	(2)	(3)	(4)	(5)	(6)

Seven-Person Office:

Highway Official	XX	XX	XX	XX	XX	XX
Deputy Director - Employee #1	X	X	X	X	X	X
AP/Admin - Employee #2						
AP/Admin - Employee #3						
Acct Payable - Employee #4						
AP/Payroll - Employee # 5						
Payroll - Employee # 6						
Payroll Employee #7						

Column Instructions:

XX The Person indicated by the XX is the preferred person to perform the procedure.

Grants Performance and Documentation

- (1) The Highway Official or deputy director works with all county personnel to ensure the grant procedures are followed as approved in the county policy. The finance committee will receive a pre-grant application form or application/approving resolution for federal, state, or other grants. The finance committee approves and sends the application to the county commission for approval. When it is approved, the grant is included in the county, highway or school budget as appropriate. The authorized persons to sign a grant on behalf of Sample County are as follows: the county mayor, the highway superintendent, and the director of schools. The grant pre-application form is a summary form showing the particulars of the grant.
- (2) The most recent version of the U.S. Office of Management and Budget's uniform administrative requirements, cost principles and audit requirements for federal awards are on file at the finance office and available by internet at any time. This document is downloaded from the Internet and on file. The Highway Official is responsible for knowing the contents of the OMB document and the grant contract and seeks any clarification from federal, state or other grant program management personnel.
- (3) All grant documents related to Sample County government, highway and schools, regardless of the department that applies for and receives a grant, are maintained in a central file in the finance office. Each grant is kept in a separate file by fiscal year. The file contains the grant application, grant reports, budget and budget amendments, correspondence from the State of Tennessee and the federal agency, monitoring reports, information specific to the grant (such as CFDA Number and Exact Grant Title, DUNS Number and Exact Entity Title for the DUNS Number), key dates, total amount of federal award, federal and state award agencies, and indirect cost calculations if applicable, etc. The required documentation is presented throughout OMB's uniform guidance as mentioned in (1) above. Internal control and procurement policies are on file in the finance office.
- (4) Revenues and expenditures for each federal or state grant are maintained in separate revenue or expenditure accounts or are cost centered so that each grant can be easily recognized and accounted for in the county's accounting records. The Highway Official is responsible for maintaining the county and highway grants, whereas the deputy Highway Official maintains the school grants. Both positions are a backup for each other.
- (5) Equipment purchased with federal and state grants is permanently marked or tagged as equipment purchased with specific grant funds. An inventory listing is made of equipment purchased with grants funds. Equipment is listed separately for each state or federal grant. Equipment on the inventory listing is physically inspected on a periodic basis by someone not associated with preparing and maintaining the inventory list. The department responsible for the equipment has the responsibility of marking the equipment and annually submits an inventory list to the county mayor's office for audit purposes. County, insurance policy & inventory policies are regarded by the responsible department head. The fixed assets are maintained by the Highway Official and deputy Highway Official.
- (6) The equipment is physically observed by the responsible parties of each department on an annual basis. The inventory list is maintained and is updated with the finance office for insurance and fixed asset maintenance.

County Highway Official
Internal Control Checklist
Budget

See Column Instructions Below			
Budget Operations			
Prepare the Annual Budget for County Commission Approval	Review the Budget Monthly	Prepare Budget Amendments and Post to Accounting Records	Major Appropriation Category Budgets should not be Exceeded.
(1)	(2)	(3)	(4)

Seven-Person Office:

Highway Official	XX	XX	XX	XX
Deputy Director - Employee #1	X	X	X	X
AP/Admin - Employee #2				
AP/Admin - Employee #3				
Acct Payable - Employee #4				
AP/Payroll - Employee # 5				
Payroll - Employee # 6				
Payroll Employee #7				

Column Instructions:

☐ XX The Person indicated by the XX is the preferred person to perform the procedure.

Budgeting

- (1) Sample County operates under the Financial Act of 1981. In November of each year, the finance committee approves a budget calendar for the new fiscal year budget cycle. By March 1st of each year, the finance committee reviews and approves the budget packet template distributed to the county and highway departments. The school departments have their own budget calendar that coincides with the main calendar. The Highway Official receives the county general budget request annually by mid April. The school and highway budgets are a combined effort of the finance office staff, the director of schools, school board and highway superintendent, and highway commission. Generally, the school board and the highway commission have an approved budget by mid May each year and are then added to the other fund budgets. The budget is then consolidated by the Highway Official and presented to the finance committee in mid May. In June, the finance committee reviews all pertinent information in regard to the budget as per TCA. The goal is have an approved consolidated budget with tax rate recommendation to send to the July county commission meeting. This process is described in TCA 5-21-110 & 5-21-111.
- (2) The budgets are reviewed on a monthly basis by the Highway Official (county & highway) and the deputy finance irector (schools). Monthly reports are distributed to the departments, including but not limited to the statement of revenue, statement of expenditures, account analysis, outstanding purchase order report and cost center reports, if applicable. The Highway Official submits a monthly report to the county commission in the form described in TCA 5-21-114.
- (3) Inter-category amendments can be approved by the Highway Official and the county mayor in regard to the county funds, the Highway Official and the highway superintendent for highway funds and the Highway Official and the director of schools for the school funds. This is a procedure used when funds are not added to a category, but an allocation is decreased to increase another allocation when funds are needed for procurement.
- (4) Amendments that are needed to decrease/increase revenues and expenditure categories are prepared by the Highway Official (county & highway) and the deputy Highway Official (schools). The highway commission and school board approve these amendments prior to presenting them to the finance committee. The finance committee then approves and sends the amendments to the next county commission meeting for approval. When the commission approves the amendments, they are then entered and posted by the Highway Official and deputy Highway Official.

County Highway Official
Internal Control Checklist
Journal Entries

See Column Instructions Below

Entering Journal Entries and Transfers			
Prepare and Document the Journal Entry	Approve Journal Entries	Post Journal Entries to Accounting Records	Review Accounting Records for Proper Posting
(1)	(2)	(3)	(4)

Seven-Person Office:

Highway Official	XX	XX		XX
Deputy Director - Employee #1	X	X		X
AP/Admin - Employee #2			X	
AP/Admin - Employee #3				
Acct Payable - Employee #4			XX	
AP/Payroll - Employee # 5				
Payroll - Employee # 6				
Payroll Employee #7				

Column Instructions:

XX The Person indicated by the XX is the preferred person to perform the procedure.

Entering Journal Entries

- (1) Finance staff may bring corrections to the attention of the Director and Deputy Director that need to be made, or the director may find the errors in the monthly budget reviews. A standard journal entry form is utilized. The form records debits and credits and explains the transaction in detail for each journal entry. Documentation is attached as necessary.
- (2) The Highway Official approves all journal entries. The deputy director is the designee in the director's absence.
- (3) Accounts payable and administrative personnel are utilized to perform the data entry.
- (4) Prior to posting the journal entries, the director of finance & the deputy director review the pre-

County Highway Official
Internal Control Checklist
Payroll & Employee Maintenance

See Column Instructions Below

Maintaining Employee Payroll Records

Obtain Payroll Change Notice from Department Heads	Approve or Determine that Funds are Budgeted for New Hire or Changes for Employees	Process Data Entry for Employee Changes in Payroll Software	Check Data Entry for Employee Changes/Additions in payroll software
(1)	(2)	(3)	(4)

Seven-Person Office:

Highway Official	X	XX		X
Deputy Director - Employee #1		X		
AP/Admin - Employee #2				
AP/Admin - Employee #3				
Acct Payable - Employee #4				
AP/Payroll - Employee # 5	XX		X	XX
Payroll - Employee # 6			XX	
Payroll Employee #7			X	X

Column Instructions:

XX The Person indicated by the XX is the preferred person to perform the procedure.

Issuing Payroll Checks -

(1) Collect the Payroll Change Notices from Department Head/Elected Officials.

(2) Check employee database and current fiscal year budget for availability of funds for the changes being requested in regard to payroll/staff.

(3) Perform New Hire Orientation, and/or process the approved changes in the Payroll Software. These changes include: additions of new employees, pay expense lines, pay adjustment lines and leave balances.

(4) Check data entry for Employee additions or changes in the payroll software to assure accuracy.

APPENDIX



State of Tennessee

PUBLIC CHAPTER NO. 112

SENATE BILL NO. 413

By Haile

Substituted for: House Bill No. 187

By Hawk

AN ACT to amend Tennessee Code Annotated, Section 9-18-102, relative to internal controls for local governments.

BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF TENNESSEE:

SECTION 1. Tennessee Code Annotated, Section 9-18-102(a), is amended by deleting the subsection in its entirety and by substituting instead the following language:

(a) Each agency of state government and institution of higher education along with each county, municipal, and metropolitan government shall establish and maintain internal controls, which shall provide reasonable assurance that:

- (1) Obligations and costs are in compliance with applicable law;
- (2) Funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and
- (3) Revenues and expenditures are properly recorded and accounted for to permit the preparation of accurate and reliable financial and statistical reports and to maintain accountability over the assets.

SECTION 2. This act shall take effect June 30, 2016, the public welfare requiring it.

SENATE BILL NO. 413

PASSED: March 30, 2015



RON RAMSEY
SPEAKER OF THE SENATE



BETH HARWELL, SPEAKER
HOUSE OF REPRESENTATIVES

APPROVED this 10th day of April 2015



BILL HASLAM, GOVERNOR

Sample Risk Assessment for TN County Office and/or Department

Review, gain an understanding of, and document the internal control procedures that your office already has in place and is currently practicing. Internal control is defined as a process affected by an organization's structure, work and authority flows, people and management information systems, designed to help the organization accomplish specific goals or objectives. Internal controls should address specific risks associated with the day-to-day operations and transactions in the county offices that will be utilizing or accounting for public funds and assets. The objectives of your internal controls should be to provide reasonable assurance that your office can document and demonstrate the following:

- I The obligations and costs of the operation are in compliance with applicable law
- II To ascertain if county funds, property and other assets that are designated/assigned to the office/department are safeguarded against waste, loss, unauthorized use, or misappropriation
- III Revenues and expenditures are properly recorded and accounted for to permit the preparation of accurate and reliable financial and statistical reports and to maintain accountability over the assets

Hold a formal meeting with key employees of the county office, if a larger office. Consider including the county finance and/or county trustee office in the sections that deal with financial reporting issues that have an impact on their offices as well.

- Obtain the county's most recent annual financial and compliance audit and review applicable audit findings that identified significant or material weaknesses in internal controls of the county office. Have these identified internal control weaknesses been corrected or has compensating internal controls been put into place to offset these identified weaknesses?
- Ask yourself (and the group if appropriate) their thoughts on how assets and funding assigned to the county office could possibly be misappropriated, wasted or abused. You, or the group, should brainstorm about the possibility of circumvention of the internal controls that are in place and discuss any needed changes to policies and procedures to eliminate/reduce significant internal control weaknesses that have been identified by the internal control assessment that was performed in-house.
- If delegating authority to make changes, determine who will be the senior level employee in your office designated for addressing internal control weaknesses identified by the external audit as well as issues that were identified by the internal control assessment that was performed in-house. Be sure to involve legal counsel to

review any updates to office written policies (personnel, purchasing, etc.) prior to any official policy change.

- Based on any corrective actions and updates to policies and procedures effecting internal controls of the office, update your written internal control assessment to reflect these changes made.
- Assign senior level staff (if not yourself) to continue to monitor the updated internal control procedures to help ensure compliance with adopted policies and procedures

The group should have at least one formal 'follow up' meeting in the near future to determine if all the material identified internal control risks that were identified in the first meeting have been mitigated. The group should also consider having at least an annual management meeting to ensure that any concerns that arise dealing with internal control issues are addressed, objectives of the office are being met, and proper accounting and reporting requirements are being achieved. If the office is currently receiving federal grant funding, it is recommended that the senior accounting official consult with the State or Federal department, which the grant funding is being received from, prior to each meeting to identify any new internal control or reporting issues that need to be addressed by county management at this time.

The \$54 million fraud

What CPAs can learn from the fleecing of Dixon, Ill.

July 31, 2013

by Kelly Richmond Pope, CPA, Ph.D.

In the wake of the largest municipal fraud in U.S. history, the questions still swirl. How could the treasurer of an Illinois town with an annual budget of \$6 million to \$8 million embezzle nearly \$54 million over two decades? How could such a scam go undetected in annual audits by two independent accounting firms and in annual audit reviews by state regulators?

What can the accounting profession learn to prevent or catch similar schemes in the future?

This article looks at how a quarter horse enthusiast named Rita Crundwell drained the coffers of Dixon, Ill. It examines the circumstances that laid the foundation for the fraud, the strategies she used to perpetrate it, and the red flags that should have signaled something was amiss.

The Crundwell chronicle

Crundwell was a longtime employee of the city of Dixon, her hometown, before she started stealing from its coffers. She began working for the town in 1970, while she was still in high school, and quickly moved into a finance role. In 1983, she was named treasurer and comptroller.

She launched the fraud scheme on Dec. 18, 1990, when she opened a secret bank account in the name of the City of Dixon. Crundwell was the only signatory on the account, which was called the RSCDA - Reserve Fund. The initials stood for Reserve Sewer Capital Development Account, and Crundwell was the only person who knew it existed.

She began transferring funds from city accounts into the RSCDA account in 1991. That year, Crundwell transferred more than \$181,000 into the RSCDA account.

The rate of theft escalated over the 21 years she pilfered money from the town.

Trust is not an internal control

The city of Dixon placed a great deal of trust in Crundwell—too much, as it turned out. The city, which does not have a city manager, gave Crundwell wide rein over its finances and set the stage for her massive fraud.

Occasionally, Dixon employees or leaders would question Crundwell about financial shortfalls. She would respond that the state of Illinois was late with payments to the city. The excuse was believable because the state sometimes was as much as a year late with payments. The problem was that no one independently verified Crundwell's story. City officials relied on annual audits by independent audit firms as well as annual reviews by the state of Illinois. The town's finances were given the OK in those reviews, and Crundwell continued to move city money into her accounts.

“Raising questions is a start, but making sure these questions are answered appropriately is key,” said Kelly Paxton, a licensed private investigator for Denver-based Financial CaseWorks LLC.

Crundwell built trust with the community by building a large quarter horse breeding operation that employed many residents and through her interactions with her neighbors and co-workers. People asked to describe Crundwell often said things such as:

- She was sweet as pie;
- You couldn't find a nicer person on the face of the planet to talk to;
- She was the nicest person in the world to work for;
- If you needed something, she'd give it to you; and
- If you thought something needed to be done, she did it.

The lesson painfully learned by Dixon was that trust without verification is a recipe for disaster. CPAs can learn from that mistake as well as a couple of fraud red flags that warranted, but failed to receive, closer scrutiny.

Red Flag No. 1: Failure to segregate duties

The segregation of duties is a critical aspect of any organization's internal control program. In Dixon, Crundwell controlled too much of the financial reporting process. She was able to receive, sign, and deposit checks with little oversight from any other city official. Under the Dixon commissioned government, the mayor and four part-time officers oversee their own divisions, which enabled Crundwell to oversee the majority of city financial functions. Crundwell balanced the checkbook, made deposits, and obtained all financial statements sent to the city of Dixon mailbox, over which she had full control. While the city of Dixon was suffering through yearly budget deficits and spending cuts (see “The Dixon Fraud Timeline”), Crundwell had the opportunity to embezzle amounts as large as \$5.8 million in 2008.

Dixon's failure to segregate duties allowed Crundwell to set up and operate a fairly simple fraud scheme. In December 1990, Crundwell opened the aforementioned RSCDA bank account in the name of the city of Dixon, with the city of Dixon as the primary account holder and “RSCDA c/o Rita Crundwell” stated as the second account holder. Between December 1990 and April 2012, Crundwell transferred funds from Dixon's money market account to various other city bank accounts and transferred city funds into her RSCDA account. The Illinois Fund, a money market mutual fund available to Illinois municipalities, contained revenues from taxes, fees, and federal grants that were deposited by each city. Crundwell would regularly wire money from the Illinois Fund into several city accounts and then transfer money from the accounts into the Capital Development account.

With the increase in Capital Development funds, Crundwell would write checks made out to “Treasurer” and deposit the funds into the RSCDA account. Crundwell created 159 fictitious invoices purported to be from the state of Illinois to show the city's auditors that the funds she was fraudulently depositing into the RSCDA account were being used for legitimate purposes. She repeatedly transferred city funds into the RSCDA account and used the money to pay for her personal and private business expenses, including horse farming operations, personal credit card payments, real estate, and vehicles.

Red Flag No. 2: Lavish lifestyle

Exactly what prompted Crundwell to start stealing from Dixon has not been revealed, but she spent much of her ill-gotten gains in building a quarter horse breeding operation that produced 52 world champions as recognized by the American Quarter Horse Association (AQHA). The AQHA named Crundwell its breeder of the year eight consecutive years before her arrest in 2012.

Crundwell poured millions of dollars in stolen funds into RC Quarter Horses LLC, building a large ranch in Dixon, traveling to competitions, and buying horse trailers with price tags in the six figures and motor homes with price tags north of \$1 million. She was willing on several occasions to spend well into the six figures to buy individual horses. The total she spent on her operation is not known, but when federal authorities seized Crundwell's assets after her arrest, she owned 400 horses.

After the asset seizure, the U.S. Marshals Service was in charge of maintaining the care of her quarter horses. Jason Wojdylo, chief inspector of the Asset Forfeiture Division of the U.S. Marshals Service, said that the government spent approximately \$200,000 per month caring for the horses before they were sold at auction.

Crundwell's spending was not limited to her quarter horse operation. She lived an extravagant lifestyle for someone who received an \$80,000 annual salary. In addition to the horse farm, she owned several family residences, including one in Florida, approximately 80 acres of land, and numerous impressive personal vehicles. In addition, she shelled out tens of thousands of dollars for jewelry purchases.

Some Dixon residents raised questions about Crundwell's lavish living, but they were answered by a number of rumors that explained her income, including one that Crundwell had an investor in her horse business and another that her family was in the satellite business and her family owned all of the cellphone towers in Illinois.

Crundwell pleaded guilty to the fraud and on Feb. 14 was sentenced to 19 ½ years in prison. The 60-year-old must serve at least 16 ½ years, or 85%, of her sentence, which was slightly less than the maximum 20 years sought by prosecutors. Crundwell, who also was ordered to repay the nearly \$54 million she stole, is appealing the sentence. The town is unlikely to see more than a fifth or so of that money returned, according to prosecutors on the case.

The Dixon fraud timeline

A timeline of major events in the Rita Crundwell fraud scheme.

- 1983: The city of Dixon, Ill., names Rita Crundwell comptroller and treasurer.
- 1990: Crundwell opens a secret bank account in the name of the city of Dixon.
- 1991: Crundwell steals \$181,000 from the city of Dixon. She spends \$18,728 in July to buy a 28-foot Suncruiser Pontoon boat with a deluxe buggy top, wet bar, propane grill, and playpen cover. She also spends more than \$3,000 on diamond stud earrings and other jewelry.
- 1992: Crundwell steals \$121,367.

- 1993: Crundwell steals \$225,287. The city of Dixon reports a deficit of nearly \$415,000 and makes budget cuts totaling \$195,000.
- 1994: Crundwell steals \$117,281. Dixon cuts more than \$150,000 from budget.
- 1995: Crundwell steals \$103,664. Dixon reports a deficit of \$322,214 and slashes the budget by more than \$185,000.
- 1996: Data not available.
- 1997: Crundwell steals \$328,622 and uses stolen funds to pay for a custom saddle, enclosed golf cart, and a horse named Two Thumbs Up. The city reports deficits as high as \$232,600 and makes more than \$100,000 in budget cuts.
- 1998: Crundwell steals \$767,487 and uses stolen funds to buy a motor home for \$100,000, a deck boat for \$50,000, and a 1998 Chevy pickup truck for \$28,000.
- 1999: Crundwell steals nearly \$1.1 million and buys a horse named Can't Fool Patty for \$125,000.
- 2000: Crundwell steals \$1.9 million and spends \$450,000 to remodel and expand her home in Dixon. The city reports a deficit of \$370,674 before making tens of thousands in budget cuts.
- 2001: Crundwell steals \$2.6 million and buys three horses for a combined \$525,000. The city reports a deficit of \$730,576 before another round of budget cuts.
- 2002: Crundwell steals a shade under \$3 million and uses stolen funds to buy a motor home for \$400,000, purchase a horse for \$200,000, and buy her boyfriend a 1967 Chevy Corvette for \$56,000. The city of Dixon institutes a hiring freeze due to budget deficits.
- 2003: Crundwell steals slightly more than \$3 million. The city reports a deficit of nearly \$1.3 million blamed in large part on state funding cuts.
- 2004: Crundwell steals almost \$3.5 million and buys a new motor home costing \$1.7 million. Dixon reports a deficit of \$1.6 million before additional budget cuts are made.
- 2005: Crundwell steals \$4.6 million and builds a horse ranch facility in Dixon, writing checks to construction companies totaling about \$650,000. She also trades in the motor home she bought 11 months earlier and pays a \$235,000 balance to buy a new motor home for \$1.82 million.
- 2006: Crundwell steals \$4.4 million. The city reports a deficit of \$1.7 million and announces a budget freeze plus \$700,000 in cuts from the capital equipment budget.
- 2007: Crundwell steals \$4.75 million. She trades in the motor home she bought in 2005 and pays a balance of \$545,000 to buy a new motor home costing \$1.96 million. The city reports a deficit of more than \$1.1 million.
- 2008: Crundwell steals \$5.8 million. She spends \$425,000 and trades in the motor home she bought the previous year to purchase a new motor home costing \$2.1 million.
- 2009: Crundwell steals \$5.6 million. She spends \$335,000 to buy a pair of horses and \$260,000 to buy a new horse trailer. She also wires \$105,097 for the purchase of a home in Englewood, Fla.
- 2011: A Dixon city clerk opens the mail while Crundwell is on vacation, discovers the RSCDA account and immediately alerts the mayor, who then contacts the FBI.
- 2012: Crundwell is arrested and pleads guilty to fraud charges.
- 2013: A judge sentences Crundwell to 19 years, 7 months in prison