



A REPORT
TO THE
ARIZONA LEGISLATURE

Financial Audit Division

Management Letter

Santa Cruz County
Year Ended June 30, 2002



Debra K. Davenport
Auditor General

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**STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL**

DEBRA K. DAVENPORT, CPA
AUDITOR GENERAL

WILLIAM THOMSON
DEPUTY AUDITOR GENERAL

March 20, 2003

Board of Supervisors
Santa Cruz County
2150 North Congress Drive
Nogales, AZ 85621

Members of the Board:

In planning and conducting our single audit of Santa Cruz County for the year ended June 30, 2002, we performed the following as required by *Government Auditing Standards* (GAS) and Office of Management and Budget (OMB) Circular A-133:

- Considered the County's internal controls over financial reporting,
- Tested its internal controls over major federal programs, and
- Tested its compliance with laws and regulations that could have a direct and material effect on its financial statements and major federal programs.

All audit findings that are required to be reported by GAS and OMB Circular A-133 have been included in the County's Single Audit Reporting Package for the year ended June 30, 2002. In addition, our audit disclosed internal control weaknesses and instances of noncompliance with laws and regulations that do not meet the reporting criteria. Management should correct these deficiencies to ensure it fulfills its responsibility to establish and maintain adequate internal controls and comply with laws and regulations. Our recommendations are described in the accompanying summary.

This letter is intended solely for the information of the Santa Cruz County Board of Supervisors and is not intended to be and should not be used by anyone other than the specified party. However, this letter is a matter of public record, and its distribution is not limited.

Should you have any questions concerning its contents, please let us know.

Sincerely,

Dennis L. Mattheisen, CPA
Financial Audit Director

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The County Treasurer's Office should improve internal controls and accurately account for its cash and investments

The Treasurer's primary responsibility is to manage public and trust monies of the County and other political subdivisions. The Treasurer currently has been entrusted with nearly \$23 million in public monies and, as a result, should maintain accurate accounting records of receipts, disbursements, and cash balances related to those monies, and safeguard assets from misappropriation.

However, the Treasurer's Office's accounting records were not always accurate. For example, the balances on the Treasurer's cash journal exceeded the Treasurer's Report balance by over \$67,000 because of more than 100 unrecorded reconciling items dating back to 1993. In addition, 239 checks totaling \$33,631 had been outstanding for more than 1 year and were listed as reconciling items on the Treasurer's servicing checking account reconciliation at June 30, 2002. These checks had not been investigated and reissued or restored to cash. Further, the Treasurer's cash journal balance exceeded the total of its check register and investment balances by \$646,316 because of unposted June 2002 activity to the cash journal.

Also, all three authorized check signers could prepare, approve, and sign checks. They also had access to the blank checks. Further, the Chief Deputy Treasurer, an authorized signer, prepared the checking account reconciliation, but no further review of the reconciliation was performed.

To help improve internal controls and ensure accurate account balances for the County and other political subdivisions, the Treasurer's Office should perform the following.

- Reconcile check register balances to all accounting records monthly and explain all reconciling items.
- Promptly investigate all reconciling items and propose appropriate journal entries to record the items or instruct the bank to correct its records.
- Record all transactions in the appropriate fiscal year.
- Establish the necessary guidelines to ensure the Office effectively separates employee responsibilities.

This recommendation was previously provided in our Management Letter to the County dated May 17, 2002.

The County should establish adequate policies and procedures for identifying and disclosing related party transactions

Financial accounting standards require that financial statements include disclosures of significant related party transactions. Arizona Revised Statutes (A.R.S.) §38-503 regarding conflicts of interest states that any public officer or public agency employee who has, or whose relative has, a substantial interest in any contract, sale, purchase, or service to that particular public agency shall make known that interest in that public agency's official records, and shall refrain from voting upon or otherwise participating in any manner as an officer or employee in such contract, sale, or purchase. The County's policy is consistent with this statute, however, County management failed to identify and disclose any such transactions. Also, the County School Superintendent's Office failed to comply with A.R.S. §38-503, as the Superintendent approved \$9,000 of expenditures for consulting services with a related party.

To help ensure that related party transactions are properly identified, accounted for, and disclosed, the County should establish policies and procedures to review the conflict-of-interest statements to ascertain and disclose significant related party transactions.

The County needs to document and test its disaster recovery plan and provide adequate security for its accounting system

The County uses a computerized accounting system to process its financial transactions and maintain its accounting system. Therefore, it is vital that the County have a contingency plan so it will be able to process its financial transactions should a major computer hardware or software failure occur. However, the County did not have a written disaster recovery plan for processing critical jobs. In addition, the County allowed all employees in the computer room where it stored its computer files and programs. Further, one employee performed both security and database administrative responsibilities.

To help ensure the integrity of financial data, the continuity of operations, and the preservation of accounting records, the County should establish, document, and test a disaster recovery plan. The plan should list the personnel assigned to disaster teams and each team member's emergency phone number; operating procedures; arrangements for a designated physical facility; a risk analysis identifying the critical applications, exposures, and an assessment of the impact on the entity; arrangements with vendors to support the needed hardware and software requirements; and any necessary documents and forms. Further, this plan should be stored off-site and updated and tested on a regular basis.

To adequately control and safeguard computer hardware, files, and programs, management should limit computer room access to operators. Access to the computer room can be limited and monitored by using of combination entry pads, card-key door locks, surveillance monitors, or intrusion detectors.

To provide adequate security over electronic data processing, the County should separate security and database administrative responsibilities. Also, management should perform a supervisory review and approval of new users' level of access and system security changes.

This recommendation was previously provided in our Management Letter to the County dated May 17, 2002.

The County should follow its written purchasing procedures

The County has a fiduciary responsibility to ensure that goods and services are obtained at the best possible price. As such, the County's purchasing guidelines require the purchasing agent to obtain verbal price quotations from three or more vendors for purchases costing between \$1,000 and \$3,000. For purchases costing between \$3,000 and \$10,000, the purchasing agent should obtain written price quotations from three or more vendors. Published advertisements and catalogs may constitute written price quotations. The purchasing agent should attach copies of verbal or written price quotations to the purchase requisition form submitted to the Finance department. However, purchasing agents did not always obtain or document verbal or written price quotations when required to do so.

To more efficiently manage budgetary resources, County management should provide training to all County departments concerning purchasing procedures and monitor the departments to ensure adherence with established procedures.

The County should accurately record and classify revenues

The Board of Supervisors depends on accurate accounting records and financial statements so it can fulfill its oversight responsibility. The County should also report accurate information to the public, lenders, and agencies from which it receives funding. To achieve this objective, management should ensure that transactions are recorded correctly, in the appropriate accounts, and in the proper fiscal year. However, the County did not accurately record and classify revenues when earned in its accounting records. As a result, revenue and receivable balances were understated on the general purpose financial statements. The County adjusted the financial statements for all significant errors noted by the auditors.

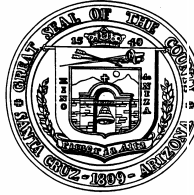
The County should ensure that the financial information it reports to its citizens, lenders, and the federal government is accurate and complete. Therefore, County management should establish procedures to ensure that all transactions are accurately accumulated and reported in schedules supporting the financial statements so they will be recognized in the appropriate accounting period.

BOARD OF SUPERVISORS SANTA CRUZ COUNTY

Manuel Ruiz
District 1

Robert Damon
District 2

John Maynard
District 3



2150 N. Congress Drive, Suite 119
Nogales, Arizona 85621

February 25, 2003

Ms. Debbie Davenport, Auditor General
State of Arizona, Office of the Auditor General
2910 North 44th Street, Suite 410
Phoenix, AZ 85018

Dear Ms. Davenport:

In response to the Management Letter for the County's audit for the fiscal year ended June 30, 2002, I substantially concur with the findings and will establish guidelines to improve all areas noted in the report.

The County Treasurer's Office should improve internal controls and accurately account for its cash and investments

Concur. The Treasurer's Office will make a greater effort to reconcile all items with the Treasurer's cash journal, check register, and Treasurer's report, as applicable. In addition, the outstanding checks and disbursements for income tax withholding will be investigated and a plan of action developed to clear the reconciling items and disbursements by December 31, 2003. Further, the Office will work closely with the Finance Department to establish controls over segregation of duties.

The County should establish adequate policies and procedures for identifying and disclosing related party transactions

Concur. County management will take greater care to help ensure that all related parties are disclosed and potential related party transactions do not occur.

The County needs to document and test its disaster recovery plan and provide adequate security for its accounting system

Concur. The accounting system disaster recovery plan has been implemented and tested by our consultants. The consultants are currently documenting the procedures and we hope to have those by June 30, 2003. Further, the County is working to establish the most effective controls over system security.

Do not concur. We do not feel that the computer room access should be further limited as the area is enclosed in glass and we can see if there is unauthorized access.

Ms. Debbie Davenport, Auditor General
February 25, 2003
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The County should follow its written purchasing procedures

Concur. County departments and the Finance department will take greater care in the future to ensure that the County's purchasing procedures are followed prior to the receipt of the goods and services.

The County should properly accrue and classify all revenues

Concur. The County will take greater care in the future to properly classify and accrue revenues and receivables.

Sincerely,

Jennifer K. St. John, CPA
Director of Administrative Services