



A REPORT
TO THE
ARIZONA LEGISLATURE

Financial Audit Division

Report on Internal Control and Compliance

Navajo County

Year Ended June 30, 2011



Debra K. Davenport
Auditor General

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Navajo County
Report on Internal Control and Compliance
Year Ended June 30, 2011

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Comprehensive Annual Financial Report



DEBRA K. DAVENPORT, CPA
AUDITOR GENERAL

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

MELANIE M. CHESNEY
DEPUTY AUDITOR GENERAL

**Independent Auditors' Report on Internal Control over Financial Reporting
and on Compliance and Other Matters Based on an Audit of Basic Financial
Statements Performed in Accordance with *Government Auditing Standards***

Members of the Arizona State Legislature

The Board of Supervisors of
Navajo County, Arizona

We have audited the financial statements of the governmental activities, each major fund, and aggregate remaining fund information of Navajo County as of and for the year ended June 30, 2011, which collectively comprise the County's basic financial statements, and have issued our report thereon dated December 19, 2011. Our report was modified as to consistency because of the implementation of Government Accounting Standards Board Statement No. 54. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

The County's management is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the County's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the basic financial statements, but not for the purpose of expressing an opinion on the effectiveness of the County's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the County's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurances that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Recommendations, we identified certain deficiencies in internal control over financial reporting we consider to be material weaknesses and another deficiency that we consider to be significant deficiency.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the County's basic financial statements will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings and Recommendations as items 11-01, 11-02, and 11-04 to be material weaknesses.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiency described in the accompanying Schedule of Findings and Recommendations as item 11-03 to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the County's basic financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Navajo County's responses to the findings identified in our audit are presented on pages 7 through 9. We did not audit the County's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the members of the Arizona State Legislature, the Board of Supervisors, management, and others within the County, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record, and its distribution is not limited.

Jay Zsorey, CPA
Financial Audit Director

December 19, 2011

Navajo County
Schedule of Findings and Recommendations
Year Ended June 30, 2011

11-01

The County should strengthen access controls to its information systems

Criteria: The County should have effective system access controls to prevent and detect unauthorized use, damage, loss, or modification of programs and data, including sensitive and confidential information.

Condition and context: The County did not adequately limit logical access to its information systems during the year. The County's major systems include the County's general ledger system, the source of the County's financial statements, and other systems used by the County School Superintendent's and County Treasurer's Offices. Specifically, there were no formal policies and procedures for granting system access and for ensuring that the access granted was compatible with an employee's job responsibilities. In addition, the County did not have procedures in place for monitoring the activities of those users with elevated system access and securing user passwords. Further, the systems' automated features were not optimized to help prevent unauthorized access.

Effect: There is an increased risk that unauthorized access to the County's systems, including financial information and data that is confidential or sensitive in nature, may not be prevented or detected. This finding is a material weakness in internal control over financial reporting.

Cause: The County did not establish policies and procedures to secure its information systems, applications, and the data they contain against unauthorized access.

Recommendation: To help prevent and detect unauthorized access to its information systems, the County should establish policies and procedures that include the following:

- Periodically perform a comprehensive review of the access granted to users to ensure that system access, especially elevated access, is granted to only those individuals who need such access, and that the access granted is compatible with each employee's job responsibilities.
- Develop a standardized document for requesting and approving access granted. Requests for system access should be approved by the employee's supervisor.
- Monitor the access of those users with elevated access.
- Require user passwords to be changed on a regular basis and comprised of specified lengths and characters.
- Implement automated system features to help prevent unauthorized access.

This finding is similar to a prior-year finding.

11-02

The County should strengthen change management controls for its information systems

Criteria: The County should have effective policies and procedures to ensure that information systems function properly and that the integrity of the systems' data is protected against unauthorized changes. Additionally, a separation of responsibilities between the programmers who develop and test changes and the individuals who implement the changes should exist.

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Condition and context: The County did not ensure that changes to information systems, programs, and data were authorized, met user needs, and were subject to independent review and approval prior to being put into use. For example, auditors noted that only one employee was authorized to make changes to the County Treasurer's property tax system and, therefore, could approve, write, and implement changes without an independent review.

Effect: Inadequate change management controls could lead to unauthorized changes to information systems and programs and to the manipulation of data they contain. This finding is a material weakness in internal control over financial reporting.

Cause: The County does not have policies and procedures in place for making changes to its information systems and programs and the data they contain.

Recommendation: To help ensure that changes to information systems, applications, and the data they contain are authorized, the County should establish policies and procedures to:

- Require that all requests for changes be documented, authorized, tested, reviewed, and approved prior to being put into use.
- Separate the responsibilities for developing and implementing changes from the responsibilities of authorizing, testing, and approving the changes. Changes initiated by users should also be approved by users.
- Maintain documentation for testing changes and the results.

This finding is similar to a prior-year finding.

11-03

The County should have a complete and tested disaster recovery plan for its information systems

Criteria: To ensure the continuity of operations and that data is not lost in the event of a system or equipment failure or other interruption, the County should have a complete and tested disaster recovery plan for its significant information systems.

Condition and context: The County had a disaster recovery plan; however, auditors noted that the plan was not complete because it did not address critical items, such as a risk analysis identifying and prioritizing critical applications, off-site storage locations, or include a current emergency contact listing.

Effect: The County may not be able to process and record transactions in the event of a system or equipment failure or other interruption. This finding is a significant deficiency in internal control over financial reporting.

Cause: During the fiscal year, the County set up an off-site backup facility that may be used in the event of a disaster. However, the County has not completed updating its disaster recovery plan to address missing elements.

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Schedule of Findings and Recommendations
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Recommendation: The County should ensure that it has an updated and tested disaster recovery plan. In addition, the County should evaluate its disaster recovery plan annually and perform the following:

- Perform a risk analysis identifying and prioritizing critical applications.
- Communicate and distribute copies of the disaster recovery plan to all affected employees, ensuring a copy of the plan is kept off-site.
- Include a listing of the off-site storage locations.
- Maintain a current listing of employees assigned to disaster teams, including emergency telephone numbers.
- Establish procedures for processing critical transactions, including forms or other documents to use.
- Annually test the plan and maintain documentation of testing procedures and results, including resolutions to problems encountered or failed tests; and safeguarding and recovering data stored on backup files.

This finding is similar to a prior-year finding.

11-04

The County should establish written policies and procedures over its transaction processing and financial statement preparation

Criteria: The County should have written policies and procedures over processing transactions and preparing its financial statements. This guidance is necessary for controlling daily operations, establishing accountability, ensuring responsibilities for processing transactions are properly separated, and that transactions are approved and documented. Written policies and procedures provide the basic framework needed for establishing employee accountability and serve as a reference tool for employees seeking guidance on how to handle complex or infrequent transactions and situations. Also, this framework helps to ensure that the financial statements and note disclosures are compiled accurately and in accordance with generally accepted accounting principles (GAAP).

Condition and context: The County lacked up-to-date policies and procedures over processing financial transactions and financial statement preparation. Specifically, employees had no current guidance for processing and approving financial transactions for the following areas: payroll, travel, purchasing, receiving, accounts payable, operating transfers, journal entries, cash disbursements, cash receipts, and financial statement preparation. For example, auditors noted that there were several revenue transactions that were misclassified in the financial statements and the cash and investments ratings were not properly disclosed. Also, auditors noted that a proper separation of responsibilities did not exist for processing and recording county cash receipts and payroll transactions in the County School Superintendent's Office.

Effect: The lack of current policies and procedures and improper separation of responsibilities increases the risk of errors and irregularities, theft, fraud, and misuse of public monies. In addition, the County had multiple compilation errors in the financial statements and note disclosures. The County's financial statements and notes were corrected for all significant errors. This finding is a material weakness in internal control over financial reporting.

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Schedule of Findings and Recommendations
Year Ended June 30, 2011

Cause: The County had not fully allocated sufficient resources to establish formal policies and procedures. During fiscal year 2011, the County had begun to allocate resources to develop written policies and procedures and completed its travel policy.

Recommendation: The County should continue to develop written policies and control procedures that include the following:

- Separating responsibilities to help ensure that no one person controls both record-keeping and transaction processing activities.
- Documenting review and approval of all transactions processed and posted to the system to prevent duplicate or inappropriate transactions from occurring.
- Maintaining accounting records to help ensure that all transactions are valid and recorded accurately and in a timely manner, and to help ensure that no valid transactions have been omitted from the accounting records.
- Resolving errors to help ensure that errors detected at any stage of processing receive prompt corrective action and are reported to the appropriate level of management.
- Monitoring activities to help ensure that internal control procedures are placed into operation and operate effectively.
- Reviewing financial statements and note disclosures to ensure that information is properly prepared and presented in accordance with GAAP.

This finding is similar to a prior-year finding.

COUNTY RESPONSE

COUNTY RESPONSE



NAVAJO COUNTY

Finance Department

James Menlove • Finance Director

Mary Springer • Deputy Finance Director

"Proudly Serving, Continuously Improving"

February 10, 2012

Debbie Davenport
Auditor General
2910 North 44th Street, Suite 410
Phoenix, AZ 85018

Dear Ms. Davenport:

The accompanying Corrective Action Plan has been prepared as required by U.S. Office of Management and Budget Circular A-133. Specifically, we are providing you with the name of the contact person responsible for corrective action, the corrective action planned, and the anticipated completion date for each audit finding included in the current year's Schedule of Findings and Questioned Costs.

Sincerely,

W. James Menlove, CPA
Finance Director

Navajo County
Corrective Action Plan
Year Ended June 30, 2011

Financial Statement Findings

11-01

The County should strengthen access controls to its information systems

Contact person: James Menlove, Finance Director, 928-524-4343

Anticipated Completion Date: June 30, 2012

Corrective Action Plan: Concur. To help prevent and detect unauthorized access to our computer information systems, the County will establish policies and procedures that include the following:

- Periodically perform a comprehensive review of the access granted to users to ensure that system access, especially elevated access, is granted to only those individuals who need such access, and that the access granted is compatible with each employee's job responsibilities.
- Develop a standardized document for requesting and approving access granted. Requests for system access will be approved by the employee's supervisor.
- Monitor the access of those users with elevated access.
- Require user passwords to be changed on a regular basis and comprised of specified lengths and characters.
- Implement automated system features to help prevent unauthorized access.

11-02

The County should strengthen change management controls for its information systems

Contact person: James Menlove, Finance Director, 928-524-4343

Anticipated Completion Date: June 30, 2012

Corrective Action Plan: Concur. To help ensure that changes to systems, applications, and the data they contain are authorized, the County will establish policies and procedures to:

- Require that all requests for changes be documented, authorized, tested, reviewed, and approved prior to being put into use.
- Separate the responsibilities for developing and implementing changes from the responsibilities of authorizing, testing, and approving the changes. Changes initiated by users will also be approved by users.
- Maintain documentation for testing changes and the results.

11-03

The County should have a complete and tested disaster recovery plan for its information systems

Contact person: James Menlove, Finance Director, 928-524-4343

Anticipated Completion Date: June 30, 2012

Corrective Action Plan: Concur. The County will ensure that it has an updated and tested disaster recovery plan. In addition, the County will evaluate the disaster recovery plan annually and perform the following:

Navajo County
Corrective Action Plan
Year Ended June 30, 2011

- Perform a risk analysis identifying and prioritizing critical applications.
- Communicate and distribute copies of the disaster recovery plan to all affected employees, ensuring a copy of the plan is kept off-site.
- Include a listing of the off-site storage locations.
- Maintain a current listing of employees assigned to disaster teams, including emergency telephone numbers.
- Establish procedures for processing critical transactions, including forms or other documents to use.
- Annually test the plan and maintain documentation of testing procedures and results, including resolutions to problems encountered or failed tests; and safeguarding and recovering data stored on backup files.

11-04

The County should establish written policies and procedures over its transaction processing and financial statement preparation

Contact person: James Menlove, Finance Director, 928-524-4343

Anticipated Completion Date: December 31, 2011

Corrective Action Plan: Concur. The County will continue to develop written policies and control procedures that include the following:

- Separating responsibilities to ensure that no one person controls both record-keeping and transaction processing activities.
- Documenting review and approval of all transactions processed and posted to the system to prevent duplicate or inappropriate transactions from occurring.
- Maintaining accounting records to help ensure that all transactions are valid and recorded accurately and in a timely manner, and to help ensure that no valid transactions have been omitted from the accounting records.
- Resolving errors to help ensure that errors detected at any stage of processing receive prompt corrective action and are reported to the appropriate level of management.
- Monitoring activities to help ensure that internal control procedures are placed into operation and operate effectively.
- Reviewing financial statements and note disclosures to ensure that information is properly prepared and presented in accordance with GAAP.



Navajo County

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State of Arizona
Office of the Auditor General