



A REPORT
TO THE
ARIZONA LEGISLATURE

Financial Audit Division

Management Letter

Pinal County

Year Ended June 30, 2005



Debra K. Davenport
Auditor General

The **Auditor General** is appointed by the Joint Legislative Audit Committee, a bipartisan committee composed of five senators and five representatives. Her mission is to provide independent and impartial information and specific recommendations to improve the operations of state and local government entities. To this end, she provides financial audits and accounting services to the State and political subdivisions, investigates possible misuse of public monies, and conducts performance audits of school districts, state agencies, and the programs they administer.



Copies of the Auditor General's reports are free.
You may request them by contacting us at:

Office of the Auditor General

2910 N. 44th Street, Suite 410 • Phoenix, AZ 85018 • (602) 553-0333

Additionally, many of our reports can be found in electronic format at:

www.azauditor.gov



DEBRA K. DAVENPORT, CPA
AUDITOR GENERAL

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

WILLIAM THOMSON
DEPUTY AUDITOR GENERAL

July 24, 2006

Board of Supervisors
Pinal County
P.O. Box 827
Florence, AZ 85232

Members of the Board:

In planning and conducting our single audit of Pinal County for the year ended June 30, 2005, 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.

There are no audit findings that are required to be reported by GAS and OMB Circular A-133. However, 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 that 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.

In addition, as required by Arizona Revised Statutes §41-1279.21(A)(1), we reviewed the County's financial records to evaluate whether the County used Highway User Revenue Fund monies and any other dedicated state transportation monies solely for authorized transportation purposes for the years ended June 30, 2004 and 2005. Our review identified instances of noncompliance, which are described in the accompanying summary as Recommendation 2.

This letter is intended solely for the information of the Pinal 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

TABLE OF CONTENTS



Recommendation 1: The County should establish policies and procedures over its credit card transactions	1
Recommendation 2: The County should spend highway user and vehicle license tax monies in accordance with state laws	2
Recommendation 3: The County needs to improve capital assets reporting	3
Recommendation 4: The Public Works Office should follow the County's purchasing policies and procedures	4
Recommendation 5: The County needs to implement previously reported recommendations	5
County Response	

The County should establish policies and procedures over its credit card transactions

Allowing employees to use county credit cards can result in inappropriate expenditures; therefore, it is important to establish effective policies and procedures governing their use. However, the County did not have policies and procedures over credit card transactions. The County maintained two credit card accounts, each with several authorized signers, that it used for travel-related expenditures and procurement expenditures. Approximately \$90,000 of travel-related expenditures and \$593,000 of procurement-related expenditures were charged to the County's credit card accounts for fiscal year 2005. The County allowed employees to fill out a certification statement for reimbursement when the employee did not provide a receipt verifying the charge and its purpose. A similar deficiency was reported in the prior 2 years' management letters.

Based on detailed testwork performed for fiscal year 2005 on 65 transactions, auditors identified the following:

- Ten transactions totaling \$830 were not supported by receipts. Further, only six transactions were supported by certification statements, and the remaining four transactions had no certification statements. As a result, auditors could not verify that the charges were for valid county purposes.
- Forty-six transactions with accompanying receipts totaling \$3,160 did not document the transaction's purpose. As a result, auditors could not determine if the charge was incurred for county business or if it resulted in a gift of public monies.
- The documentation for 22 meal charges for \$782 did not contain adequate information to determine if meal charges were within per diem rates.
- Seventeen meal charges for \$556 were for restaurants in the Town of Florence, the employee's place of business.

The County adopted credit card policies and procedures in August 2005. However, these new policies and procedures do not ensure that credit card charges are for a public purpose and not to promote a purely private or personal interest. The County should ensure that policies and procedures are adequate to control the use of credit cards and ensure that they are followed. Such policies and procedures should include the following:

- A stipulation that the county credit cards are not to be used for personal use or for expenses not allowed by county policy. Examples of such items include meals within a specified mile radius of an employee's designated place of employment, expenses exceeding the County's stated travel reimbursement policies, gifts, parties, and alcoholic beverages.
- A requirement that all credit card charges be supported by itemized receipts that include each charge's purpose and are submitted to the employee's supervisor.
- A requirement allowing certification statements only as a last resort submitted to the employee's supervisor who will review closely the charges for compliance with county policy.
- A requirement that a department supervisor review charges for propriety and compliance with the County's policies, sign the supporting receipt as evidence of approval, and submit all supporting documents to the finance department for payment.

The County should spend highway user and vehicle license tax monies in accordance with state laws

Each year, the State distributes Highway User Revenue Fund (HURF) monies and a portion of the vehicle license tax (VLT) monies to the County, and has mandated that the County use these monies solely for highway and street purposes, as specified in the Constitution of Arizona, Article IX, §14, and Arizona Revised Statutes (A.R.S.) §§28-5801(B)(1)(c) and (2)(c), and 28-5808(A)(2)(b) and (B)(2)(b). The County received more than \$30 million in HURF and VLT monies in fiscal years 2004 and 2005. The County's transportation department operated primarily from these monies.

Auditors reviewed county expenditures of HURF and restricted VLT monies, and noted expenditures that appeared to be unallowable based on the Arizona Constitution, A.R.S., and Attorney General Opinion No. I05-003. The following table summarizes those expenditures:

Unallowable Expenditures From HURF and Restricted VLT Monies Years Ended June 30, 2004 and 2005

Description	2004	2005
Liability insurance	\$358,504	\$344,710
Legal services	95,431	37,501
Settlements and judgments	<u>40,517</u>	<u>25,000</u>
	<u>\$494,452</u>	<u>\$407,211</u>

The County should develop written policies and procedures to ensure that HURF and restricted VLT monies are spent in accordance with the Arizona Constitution, state laws, and the Attorney General's Opinion, and ensure that its transportation department follows these policies and procedures. These policies should include a written description of the types of expenditures that are allowable and unallowable. In addition, management should review and approve expenditures to ensure that all expenditures charged to HURF and restricted VLT monies are only for allowable charges. Finally, the County should allocate local revenues for highway and street purposes to replenish the monies it spent inappropriately during fiscal years 2004 and 2005.

The County needs to improve capital assets reporting

Capital assets comprise more than 42 percent of the County's total assets. Therefore, it is essential that the County accurately reports these assets to its lenders, the public, and other interested parties. To accomplish this, it should maintain a reliable capital assets system and have procedures in place that accurately identify, accumulate, and reconcile capital assets and related depreciation costs. However, the County had not established an adequate system or internal control policies and procedures that would ensure that its capital assets were properly reported. For example, the County did not capitalize four assets totaling \$921,000 acquired through capital leases. Additionally, construction costs of \$3,870,000 for the Adult Juvenile Detention facility, road improvement costs, and related construction contracts payable were not recorded in the proper fiscal year. As a result of the problems with the capital assets system, the County restated July 1, 2004, infrastructure and construction in progress balances.

The following procedures can help the County accurately record its capital assets in its accounting records and report those assets in its financial statements:

- Establish, follow, and monitor internal control policies and procedures to ensure the capital assets system contains accurate and complete capital assets information that supports the amounts reported within the County's financial statements.
- Capitalize assets acquired through capital leases and recognize related depreciation expenses.
- Develop a capital assets system that accurately calculates depreciation expense and accumulated depreciation and provides a listing of current-year additions that can be reconciled to capital expenditures recorded in the financial accounting system annually.

The Public Works Office should follow the County's purchasing policies and procedures

The County's purchasing policies and procedures help to promote open and fair competition among vendors and help to ensure that the County receives the best possible value for the public monies it spends. However, the current county administration informed our Office of possible violations of A.R.S. and the County's policies and procedures relating to issuance of contracts to consulting firms for fiscal year 2004. As a result of investigating these contracts, auditors noted that the former county engineer failed to comply or document compliance with numerous state statutes and procurement policies and procedures for the following five contracts totaling approximately \$1,635,000.

- The County Engineer awarded three contracts without issuing invitations for bid requests for proposals as required by A.R.S. §§11-254.01 and 41-2533-34 and the County's own policies.
- The County Engineer awarded two contracts without following the direct selection process as outlined in A.R.S. §34-103. Direct selection is defined in A.R.S. §34-101 as "the selection of a technical registrant without the requirement of advertising or the use of a current register." Some examples of not following the process include the failure to document the discussions with at least three firms regarding the contracts, document the three firms deemed most qualified by a selection committee, and negotiate for a contract with the most qualified firm.
- The County Engineer extended a contract for one year without the Governing Board's approval, as required by county policy.
- An employee altered another employee's rating sheet for a contract award.

Because the County failed to follow state statutes and its own policy, these contracts may not have been awarded to the firm most advantageous to the County. In addition, two of these contracts were awarded to a firm owned by a former assistant Pinal County engineer at a higher cost.

To help ensure that county purchasing policies and procedures are followed, the County should provide ongoing training to all county employees with purchasing responsibilities. Also, the County should monitor departments to ensure adherence with established procedures. In addition, the Public Works Office should ensure that all employees adhere to the County's purchasing policies and procedures.

The County needs to implement previously reported recommendations

We have previously reported to the County specific recommendations to correct certain deficiencies noted during our previous years' audits to improve county operations. However, the County has not implemented all of our recommendations pertaining to budget preparation and monitoring; controls over its information system; information system disaster recovery; procurement, suspension, and debarment compliance requirements; and subrecipient monitoring compliance requirements. The County has not implemented the following recommendations reported in our Management Letter for the year ended June 30, 2004:

Budget preparation and monitoring process—The county budget is used to set public policy, to control taxing and spending, and to serve as a financial planning tool. Good stewardship over public monies and A.R.S. require that the County includes all accounts and funds that it administers in the County's adopted budget; that the County includes transfers in and out as part of the Board of Supervisors' approved budget; and that the County ensures that its actual expenditures, obligations, and liabilities do not exceed the amounts budgeted. However, the County did not follow these procedures. Therefore, it is important that the County ensure that its adopted budget is accurate, complete, properly monitored, and in accordance with statutes.

Controls over its information system—The County uses a computerized information system to process and record its financial transactions. Consequently, the County's computer information system is vital to its operations, and the County needs to ensure the integrity of the financial transactions processed on this system. However, the County's information system did not document the users who entered or approved financial transactions on the systems. To help ensure that records of financial transactions are complete, accurate, and valid, the County should establish a record within its computer system to identify users initiating and authorizing transactions, receiving goods or services, and approving payments to vendors.

Disaster recovery plan—The County has an information system that provides general ledger, accounts payable, payroll, personnel, and capital assets subsystems for the finance department, and general ledger and property tax management subsystems for the County Treasurer. These systems are critical to the County's operations. However, the County did not have a disaster recovery plan or a negotiated written backup agreement for its financial computer system. Such a plan will help ensure that electronic data files are not lost and transactions can be processed in the event of a disaster or other interruption. Therefore, it is important that the County prepare a disaster recovery plan and negotiate a written backup agreement as soon as possible to help maintain system integrity and security.

Procurement, suspension, and debarment—In accordance with each grantor agency's Code of Federal Regulations pertaining to administrative requirements, the County must verify that vendors and subrecipients are not suspended or debarred before entering into transactions with them to be paid with federal monies. This verification may be accomplished by checking the Excluded Parties List System maintained by the General Services Administration, obtaining a certification from the vendor or subrecipient, or adding a clause or condition to the contract with that entity. The County did not have policies and procedures in place to ensure that vendors and subrecipients are not suspended or debarred. However, for the major programs tested, auditors performed additional procedures and noted no instances of payments made to suspended or debarred individuals or organizations.

Subrecipient monitoring—In accordance with each grantor agency's Code of Federal Regulations pertaining to administrative requirements, the County must ensure that subrecipients spending \$500,000 or more in federal awards during the fiscal year meet the audit requirements of OMB Circular A-133. However, the County did not have policies and procedures to evaluate whether the subrecipients met the audit threshold requirements for an audit and, as a result, did not comply with this subrecipient monitoring requirement. Therefore, the Department could not ensure that its subrecipients are complying with all applicable program requirements. However, auditors performed additional procedures and noted no instances of material noncompliance.



Pinal County
Finance Department

31 N. Pinal Street • P.O. Box 1348 • Florence, Arizona 85232
(520) 866-6249 • Fax: (520) 866-6944

Victoria Prins
Director

July 7, 2006

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

Dear Ms. Davenport:

Pinal County Management has chosen to respond to the Management Letter for the fiscal year ended June 30, 2005. Our responses to the Management Letter are attached. The Management Letter resulted from a single audit conducted of Pinal County.

If you have any questions, please contact me at (520) 866-6209.

Sincerely,

Victoria Prins, CPA, MPA, CGFM
Chief Financial Officer

PINAL COUNTY
Response to Summary of Audit Findings
Year Ended June 30, 2005

The County should establish policies and procedures over its credit card transactions

Response: Concur. The County is working to implement updated policies and procedures to help strengthen controls over credit card transactions, based on the audit recommendations.

The County should spend highway user and vehicle license tax monies in accordance with state laws

Response: Concur. The County has corrected procedures to ensure that payments from the Highway User Revenue Fund are in compliance with state laws.

The County needs to improve capital assets reporting

Response: Concur. The County is working on improving the steps within the capital asset program to ensure proper accounting for additions, deletes and transfers. However, the County is limited by the program itself when it comes to the recording of depreciation. The County has also implemented new procedures to ensure that all products and services are accounted for in the proper year and capitalized accordingly.

The Public Works Office should follow the County's purchasing policies and procedures

Response: Concur. The County did recognize problems with the procurement of consultants and requested an audit by the State Auditor General in 2004. As a result of this audit, the Public Works Office has implemented procedures that fully comply with statutes. The Board of Supervisors approved the Pinal County Procurement Code on June 28, 2006.

The County needs to implement previously reported recommendations

Response:

Budget preparation and monitoring process: Concur. The County is working to implement policies and procedures to help strengthen controls over budget preparation and monitoring. The County currently monitors actual expense to adopted budget. The County's annually adopted Budget Resolution has guidelines for expenditure limits. Should a department(s) exceed these limits, the department(s) is placed on a budget hold status and all expenses must be approved by the Budget Office.

In order to account for unforeseen revenue/expenses, the Budget Office will make a recommendation to the County Manager for budget appropriation transfers throughout the year. These recommendations will be forwarded to the Board of Supervisors for their approval. These budget appropriation transfers will ensure that the department expenses do not exceed the adopted budget.

PINAL COUNTY
Response to Summary of Audit Findings
Year Ended June 30, 2005

Controls over its information system: Concur. Audit trails are in place based on user ID's and logins. However, due to the constraints of the current computer system, the audit trails requested were not easily obtainable or verified. The Management Information Systems Department is currently working with JD Edwards and the audit team to find reports that would satisfy this requirement.

Disaster recovery plan: Concur. The County is currently working on implementing a Disaster Recovery Plan that will facilitate new processes and procedures and an offsite location of hardware and backup tapes. This will facilitate a redundant environment in case a disaster strikes Building A allowing the ability to continue work on critical applications for the period of time required to bring in replacement hardware. This project has an expected completion date of March 2007.

The County has completed a Disaster Recovery Assessment for the AS400 and established a standard Disaster Recovery template to assist in developing disaster recovery plans throughout the County.

Procurement and suspension and debarment: Concur. The County is currently working on implementing procedures to ensure vendors or subrecipients are not suspended or debarred before entering into agreements.

Subrecipient monitoring: Concur. The County will work on implementing policies and procedures regarding monitoring of departments and subrecipients to ensure they are following federal guidelines.