

## **PART II, FINDINGS RELATING TO THE FINANCIAL STATEMENTS**

Findings and recommendations as a result of our examination are presented below. We reviewed these findings and recommendations with management to provide an opportunity for their response. The county mayor's written response is paraphrased in this report. Other officials offered oral responses to certain findings and recommendations; however, these oral responses have not been included in this report.

### **SMITH COUNTY AND SMITH COUNTY SCHOOL DEPARTMENT**

**FINDING 04.01**      **GOVERNMENT-WIDE FINANCIAL STATEMENTS WERE NOT PRESENTED IN ACCORDANCE WITH GENERALLY ACCEPTED ACCOUNTING PRINCIPLES**  
(Material Noncompliance Under Government Auditing Standards)

Smith County and the Smith County School Department did not identify and determine the historical value of their capital assets and the related depreciation amounts of these assets. Therefore, Smith County and the Smith County School Department were unable to provide the information necessary to prepare government-wide financial statements for all of their activities, as required by Governmental Accounting Standards Board (GASB) Statement No. 34, Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments. GASB is the standard-setting body for accounting principles that state and local governments are required to follow. As a result of this omission, Smith County and the Smith County School Department's financial statements are not presented in accordance with generally accepted accounting principles; thus, we have issued an adverse opinion on their financial statements.

The Office of the Comptroller of the Treasury, State of Tennessee, requires counties that do not implement GASB Statement 34 to issue a financial report in compliance with Financial Reporting Standards for County Governments, Component Units of County Governments, and Special School Districts That Do Not Implement Governmental Accounting Standards Board Statement 34, established by the Comptroller of the Treasury. Smith County and the Smith County School Department's financial statements are presented in compliance with these requirements.

### **RECOMMENDATION**

Smith County and the Smith County School Department should present government-wide financial statements in conformity with generally accepted accounting principles, and should compile and maintain records that properly account for their capital assets. These records should document the historical cost of the county's capital assets and the related depreciation amounts of these assets. This information is necessary to present the county's and the School Department's financial statements in accordance with generally accepted accounting principles.

**OFFICE OF COUNTY MAYOR**

**FINDING 04.02      **THE OFFICE DID NOT MAINTAIN THE SOLID WASTE DISPOSAL FUND ON THE ACCRUAL BASIS OF ACCOUNTING****

(Material Noncompliance Under Governmental Auditing Standards)

The Solid Waste Disposal Fund was presented on the accounting records of the County Mayor's Office as an enterprise fund; however, our audit noted the following deficiencies in the maintenance of the fund:

- A. County officials did not determine and record landfill closure and postclosure care costs of \$202,621 on the accounting records of the Solid Waste Disposal Fund for the year. We determined this amount from information obtained from records on file from the county's landfill engineer and prior audit working papers. State and federal laws and regulations require the county to place a final cover on its landfill site when it stops accepting waste and to perform certain maintenance and monitoring functions at the site for 30 years after closure. Although these closure and postclosure care costs will be paid near or after the date that the landfill stops accepting waste, generally accepted accounting principles require county officials to accrue and report a portion of these closure and postclosure care costs as a liability and as an operating expense in each year of operation based on the estimated landfill capacity used.
  
- B. County officials did not adjust the balances of long-term liabilities presented on the balance sheet at June 30, 2004, to reflect principal payments made during the year. Principal amounts paid on a capital outlay note (\$78,352) and a capital lease (\$67,270) during the year were shown as expenses of the fund on the county's financial statements.

We presented adjustments to county officials for them to approve and post to the general ledger for proper financial statement presentation.

**RECOMMENDATION**

County officials should maintain the Solid Waste Disposal Fund on the accrual basis of accounting, as required by generally accepted accounting principles. All assets, liabilities, and fund equity accounts associated with the operation of this fund should be included on the balance sheet.

**FINDING 04.03      THE OFFICE HAD DEFICIENCIES IN ITS PURCHASING PROCEDURES**

(A. and B. Internal Control – Reportable Conditions Under Government Auditing Standards; C. Material Noncompliance Under Government Auditing Standards)

Our examination of the purchasing procedures of the county mayor revealed the following deficiencies:

- A. Purchase orders were not issued for some applicable purchases, and in several instances, purchase orders were issued after the purchases were made. Purchase orders are necessary to control who has authority to make purchases and to document purchasing commitments. The practice of issuing purchase orders after the purchase defeats the purpose of their issue and makes the purchase orders approvals for payment, rather than authorizations to purchase.
- B. In several instances, invoices were paid without documentation that goods had been received or services had been rendered. This practice weakens controls over the purchasing process. We extended our audit procedures and determined that these purchased goods and services were received.
- C. Competitive bids were not solicited for the purchase of liability insurance (\$89,444), vehicle and equipment insurance (\$28,599), a cleaning contract for county buildings (\$21,000), hauling crushed stone to the county landfill (\$22,966), and environmental testing (\$8,982). Section 5-14-204, Tennessee Code Annotated, requires all purchases exceeding \$5,000 to be based on competitive bids solicited through public advertisement.

**RECOMMENDATION**

To strengthen internal controls over the purchasing process and to document purchasing commitments, the office should issue purchase orders for all applicable purchases before purchases are made and should obtain proper documentation before making disbursements. Furthermore, competitive bids should be solicited for all purchases exceeding \$5,000, as required by state statute.

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**FINDING 04.04      THE COURTHOUSE AND JAIL MAINTENANCE FUND HAD A FUND DEFICIT**

(Noncompliance Under Government Auditing Standards)

The Courthouse and Jail Maintenance Fund had a fund deficit of \$14,682 at June 30, 2004. This fund deficit resulted from the expenditure of funds reserved for the construction and renovation of the courthouse and jail.

RECOMMENDATION

County officials should eliminate the fund deficit in the Courthouse and Jail Maintenance Fund and take appropriate steps to prevent such a deficit from recurring.

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FINDING 04.05      **APPROPRIATIONS EXCEEDED ESTIMATED AVAILABLE FUNDS IN THE GENERAL FUND**  
(Material Noncompliance Under Government Auditing Standards)

Appropriations approved by the County Commission exceeded estimated available funds in the General Fund, resulting in a budgeted fund deficit of \$186,157 at June 30, 2004.

RECOMMENDATION

Appropriations that exceed estimated available funds should not be submitted to the County Commission, and the County Commission should not approve such appropriations.

MANAGEMENT'S RESPONSE – COUNTY MAYOR

This happened because Smith County amended the budget out of the fund balance instead of amending revenue line items to offset additional appropriations. The actual fund balance of the General Fund increased during the fiscal year.

REBUTTAL

The budget amendments presented to and approved by the County Commission resulted in a budgeted fund deficit. If additional revenues are received to offset increased expenditures, the budget amendments should reflect both the additional revenues as well as the additional expenditures.

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FINDING 04.06      **DEFICIENCIES WERE NOTED IN AMBULANCE SERVICE OPERATIONS**  
(A. Internal Control – Reportable Condition Under Government Auditing Standards; B., C., and D. Noncompliance Under Government Auditing Standards)

Our examination of Ambulance Service operations noted the following deficiencies:

- A. Duties were not segregated adequately. The Ambulance Service's office manager collected funds, issued receipts, deposited funds with the county trustee, maintained the computerized billing and accounts receivable system, computed employees' payroll checks, and distributed the payroll checks.

Sound internal controls require segregation of incompatible duties involving the receipt and disbursement of funds.

- B. The Ambulance Service did not follow County Commission policies concerning the collection of patient accounts. Ambulance Service personnel's collection efforts were limited to sending statements to patients. Also, the computerized billing system's capability to age accounts receivable as a means of enhancing collection efforts for delinquent accounts was not used.
- C. The computerized billing system provided a total of patients' accounts receivable. However, this accounts receivable amount and the related allowance for uncollectible accounts and other deferred revenues were not determined by Ambulance Service personnel and were not recorded in the accounts of the Ambulance Service Fund, as required by generally accepted accounting principles. We determined the current patient accounts receivable from available records and gave adjustments to county officials for them to approve and post to the general ledger for proper financial statement presentation.
- D. County Commission policies for the write-off of uncollectible accounts were not followed. Ambulance Service personnel informed us that uncollectible accounts were substantial but had not been written off in recent years.

#### RECOMMENDATION

Employees' duties should be segregated in the Ambulance Service for effective internal control over the receipt and disbursement of funds. Also, the collection policies established by the County Commission should be followed, and accounts receivable and related accounts should be periodically determined and recorded in the financial statements of the Ambulance Service Fund. Furthermore, write-off policies established by the County Commission should be followed.

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FINDING 04.07      **THE OFFICE HAD DEFICIENCIES IN PERSONNEL RECORDS**  
(Internal Control – Reportable Condition Under Government Auditing Standards)

We noted the following deficiencies in the maintenance of personnel records of the County Mayor's Office:

- A. Employees' leave records consisted only of vacation, sick, and compensatory leave used during the month. Records did not document employees' vacation, sick, and compensatory leave earned during the month and their beginning and ending leave balances. Therefore, we could not determine if employees were entitled to the amount of vacation, sick, and compensatory leave taken.

- B. Time and attendance records were not maintained for employees of the Offices of Youth Services, Assessor of Property, Election Registrar, and Veterans' Administration. In addition, some employees in the Sheriff's Office did not properly document hours worked on their time sheets, and most employees did not sign their time sheets. Without properly prepared and approved time and attendance records, we could not determine if these employees were paid the correct amounts.
- C. Supervisors at the Sheriff's Office did not sign and approve time sheets for their employees.
- D. There were no written authorizations on file for the salaries of the youth service officer and employees of the Sheriff's Office.

**RECOMMENDATION**

The County Mayor's Office should do the following:

- A. The office should maintain leave records that document employees' vacation, sick, and compensatory leave earned, used, and beginning and ending balances.
- B. All county offices should be required to maintain records documenting employees' time and attendance. All employees should properly maintain and sign their time records.
- C. All time and attendance records should be approved and signed by the appropriate official, department head, or supervisor to verify and document hours worked by county employees.
- D. The office should establish written authorizations for each employee's salary.

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**FINDING 04.08      WRITTEN GUIDELINES GOVERNING THE USE OF CELLULAR TELEPHONES HAD NOT BEEN ADOPTED  
(Internal Control – Reportable Condition Under Government Auditing Standards)**

The county provided several county officials and employees with cellular telephones. However, the County Commission had not adopted written guidelines governing the use of these cellular telephones.

**RECOMMENDATION**

The County Commission should adopt written guidelines governing the use of cellular telephones. These guidelines should identify those who are entitled to have a county-assigned cellular telephone and the purposes for which telephones can be used.

**FINDING 04.09      INVENTORY RECORDS WERE NOT MAINTAINED ADEQUATELY**  
(Internal Control – Reportable Condition Under Government Auditing Standards)

County officials maintained inventory records of assets owned by Smith County; however, some assets were not labeled as county property. Furthermore, the office did not have provisions to ensure that new items were added to the respective inventories and that the accuracy of the inventories was verified. Generally accepted accounting principles require accountability for all county-owned assets, such as equipment, furniture, and vehicles.

**RECOMMENDATION**

Smith County should label all assets as county property and ensure that all items are added to the inventory list. Furthermore, personnel independent of maintaining the inventory should periodically verify the inventory records.

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**OFFICE OF HIGHWAY SUPERINTENDENT**

**FINDING 04.10      RECEIVABLES AND PAYABLES WERE NOT DETERMINED AND POSTED TO THE ACCOUNTING RECORDS**  
(Material Noncompliance Under Government Auditing Standards)

Receivables and payables were not determined and recorded on the accounting records, as required by generally accepted accounting principles. We performed additional audit procedures to determine receivables and payables at June 30, 2004. Adjustments to receivables and payables totaling \$165,271 and \$140,913, respectively, have been presented to county officials and county officials posted these adjustments to the records. Therefore, receivables and payables are properly presented in this report.

**RECOMMENDATION**

Receivables and payables should be determined and reflected on the accounting records in accordance with generally accepted accounting principles.

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**FINDING 04.11      THE OFFICE HAD BIDDING DEFICIENCIES**  
(Material Noncompliance Under Government Auditing Standards)

The Uniform Road Law, Section 54-7-113, Tennessee Code Annotated, requires purchases exceeding \$5,000 to be made after public advertisement and solicitation of competitive bids. Our examination noted the following bidding deficiencies:

- A. Competitive bids were not solicited for the purchase of vehicle and equipment insurance (\$27,302).
- B. Competitive bids were solicited for the purchase of cold-mix asphalt, as required by state statute, and the department determined and documented the low bidder. The Highway Department purchased cold-mix asphalt on five occasions during the year, but only one of these purchases (\$6,680) was made from the vendor who was awarded the bid. The other four purchases (\$30,723) were made from a vendor who had not submitted a bid.

**RECOMMENDATION**

Competitive bids should be solicited for all purchases exceeding \$5,000, as required by state statute, and the department should not make purchases from vendors who are not awarded bids.

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**FINDING 04.12**      **THE OFFICE HAD DEFICIENCIES IN PURCHASING PROCEDURES**  
(Internal Control – Reportable Condition Under Government Auditing Standards)

Our examination of the office’s purchasing procedures noted the following deficiencies:

- A. Purchase orders were not issued for some applicable purchases. Also, some purchase orders were issued without a date, making it impossible to determine if the purchase order was issued prior to the purchase. Properly issued purchase orders are necessary to control who has authority to make purchases and to document purchasing commitments.
- B. In some instances, invoices were paid without documentation that goods and services were received. This practice weakens controls over the purchasing process. We extended our audit procedures and determined that these purchased goods and services were received.

**RECOMMENDATION**

To strengthen internal controls over the purchasing process and to document purchasing commitments, the office should issue purchase orders containing all pertinent information for all applicable purchases and should obtain proper documentation before making disbursements.

**FINDING 04.13      SOME ASSETS WERE NOT LABELED AS HIGHWAY DEPARTMENT PROPERTY**  
(Noncompliance Under Government Auditing Standards)

The highway superintendent maintained inventory records of assets owned by Smith County; however, some assets were not labeled as county property. The County Uniform Road Law, Section 54-7-112, Tennessee Code Annotated, requires that “all machinery, equipment, and tools shall be plainly marked as property of the ... department and each item shall be numbered ...”

**RECOMMENDATION**

All county-owned assets should be plainly labeled as property of the Highway Department, as required by state statute.

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**OFFICE OF DIRECTOR OF SCHOOLS**

**FINDING 04.14      THE OFFICE PURCHASED INSURANCE COVERAGE AND BUS CAMERA EQUIPMENT WITHOUT SOLICITING COMPETITIVE BIDS**  
(Material Noncompliance Under Government Auditing Standards)

Competitive bids were not solicited for the purchase of liability insurance (\$20,113), building and contents insurance (\$49,142), vehicle and equipment insurance (\$30,246), and a bus camera system (\$9,600). Section 49-2-203, Tennessee Code Annotated, requires purchases exceeding \$5,000 to be made after public advertisement and solicitation of competitive bids.

**RECOMMENDATION**

Competitive bids should be solicited for all purchases exceeding \$5,000, as required state statute.

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**FINDING 04.15      INVENTORY RECORDS WERE NOT MAINTAINED ADEQUATELY**  
(Internal Control – Reportable Condition Under Government Auditing Standards)

School officials maintained inventory records of assets owned by the School Department, but all assets were not identified on the inventory records by serial number or detailed description that would allow for proper identification of the assets. Furthermore, the department did not have provisions to ensure that new items were added to respective inventories and that the accuracy of the inventories was verified. Generally accepted

accounting principles require accountability for all department-owned assets, such as equipment, furniture, and vehicles.

RECOMMENDATION

The School Department should adequately maintain inventory records of all assets, as required by generally accepted accounting principles. Furthermore, personnel independent of maintaining the inventory should periodically verify the inventory records.

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OFFICE OF CIRCUIT AND GENERAL SESSIONS COURTS CLERK

FINDING 04.16      **THE CIRCUIT AND GENERAL SESSIONS COURTS CLERK DID NOT REQUIRE A DEPOSITORY TO COLLATERALIZE FUNDS THAT EXCEEDED FDIC COVERAGE**  
(Material Noncompliance Under Government Auditing Standards)

The circuit and general sessions courts clerk did not require a depository holding county funds to pledge securities to protect funds that exceeded Federal Deposit Insurance Corporation (FDIC) coverage. At June 30, 2004, funds on deposit exceeded FDIC coverage by \$98,228. Section 5-8-201, Tennessee Code Annotated, provides for county officials to require any bank that is a depository of county funds to deposit in an escrow account in a second bank collateral security equal to 105 percent of the funds that exceed FDIC coverage.

RECOMMENDATION

County officials should require all depositories to pledge securities to protect county funds exceeding FDIC coverage, as required by state statute.

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OFFICE OF SHERIFF

FINDING 04.17      **THE OFFICE DID NOT DOCUMENT CONFIDENTIAL DRUG FUND EXPENDITURES IN COMPLIANCE WITH STATE GUIDELINES**  
(Noncompliance Under Government Auditing Standards)

Several forms and reports required by the Office of the Comptroller of the Treasury to account for drug control funds were not completed. These forms and reports are necessary to document the administration of confidential drug funds and to account for cash transactions related to undercover investigative operations.

RECOMMENDATION

The sheriff should ensure that the office completes all forms and reports required by the Office of the Comptroller of the Treasury.

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## **OTHER FINDINGS AND RECOMMENDATIONS**

**FINDING 04.18**      **A SYSTEM OF CENTRAL ACCOUNTING, BUDGETING, AND PURCHASING HAD NOT BEEN ADOPTED**  
(Internal Control – Reportable Condition Under Government Auditing Standards)

County officials had not adopted a central system of accounting, budgeting, and purchasing. Establishing a central system would significantly improve internal controls over the accounting, budgeting, and purchasing processes.

### **RECOMMENDATION**

Smith County officials should consider adopting either the County Financial Management System of 1981 or a private act, which would provide for a central system of accounting, budgeting, and purchasing covering all county departments.

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**FINDING 04.19**      **DUTIES WERE NOT SEGREGATED ADEQUATELY IN THE OFFICES OF COUNTY MAYOR, HIGHWAY SUPERINTENDENT, DIRECTOR OF SCHOOLS, TRUSTEE, COUNTY CLERK, CIRCUIT AND GENERAL SESSIONS COURTS CLERK, CLERK AND MASTER, REGISTER, AND SHERIFF**  
(Internal Control – Reportable Condition Under Government Auditing Standards)

Duties were not segregated adequately among the officials and employees of the Offices of County Mayor, Highway Superintendent, Director of Schools, Trustee, County Clerk, Circuit and General Sessions Courts Clerk, Clerk and Master, Register, and Sheriff. Officials and employees responsible for maintaining accounting records were also involved in receipting, depositing, and/or disbursing funds. We realize that due to limited resources and personnel, management may not be able to properly segregate duties among employees. However, our professional standards require that we bring this matter to the reader's attention in this report.