1. Segregation of Duties

Auditors’ Finding and Recommendation

One of the basic elements of internal accounting control involves segregation of duties in such a manner in which the work of one employee is checked by others, and the responsibilities for custody of assets is not placed it the same employees that maintains the accounting records. Due to the District’s limited number of personnel, the segregation of duties is not always possible. However, consideration should be given to implementing new checks and balances that would partially offset the internal control weaknesses discussed below.

- We noted that some employees that handle cash receipts and post payments to customer accounts also have the authority to write-off account balances and edit customer accounts. This allows for the employee to retain customer cash while writing off the amounts to be received from the customer. To strengthen internal control, the employees’ who have access to cash receipts should not have the ability to authorize write-offs of customer accounts or edit customer accounts.

- We noted that cash receipts for miscellaneous receivables are handled by the same individual who deposits cash. We recommend that another employee make a control list of all receipts for miscellaneous receivables, and restrictively endorse all items received as “for deposit only”. This would prevent any unauthorized endorsement should the checks be misplaced or lost before being deposited. The receipts should then go to another employee for further processing and deposit to the bank on a timely basis.

Management’ Response

The Director of Finance is currently working with the Customer Service Manager and Finance staff to review the segregation of duties related to the cash receipts process in both customer service and Finance.

Updated Response

- The Customer Service Manager is the designated “Super-user” of the enQuesta system. She has full system access and is able to handle cash receipts, post payments, write-off account balances and edit customer accounts. Unless the Customer Service area is short

Management Letter Comments
June 30, 2011 Audit
1. Segregation of Duties (Cont.)

staffed the Customer Service Manager does not handle cash receipts or post payments to customer accounts. The Customer Service Manager does approve write-offs that are done by the customer service staff. To strengthen the checks and balances in this area, a monthly write-off report that is produced from the enQuesta system is included in the month-end package that goes to the Finance department. The Director of Finance reviews and approves the monthly write-off report.

- In reviewing the cash receipting process for the miscellaneous receivables, Finance has changed the process to enhance the checks and balances and strengthen internal control. The process change has the payroll accountant opening the mail and endorsing the checks. She then gives the checks to the Finance/Budget Analyst for coding and making the deposit to Union Bank via the remote software.

2. Journal Entries

Auditors’ Finding and Recommendation

We noted instances in which journal entries are prepared and approved by the same individual. We also noted instances in which documentation to support the journal entries was not attached. To minimize incorrect journal entries being posted to the accounting system, all journal entries should be approved by a person independent of the preparation of the journal entries and that supporting documentation be attached to the journal entries for the review process.

Management’s Response

The Director of Finance has reviewed the journal entry process with the Finance staff and these recommendations have been implemented.

Updated Response

Since the original response in the management comments the journal entry process has been automated. Journal entries are input into an excel journal format and uploaded into the G/L. The back-up is scanned and attached to the journal entry and forwarded to the Director of Finance for review and approval.
3. Inventory

Auditor’s Finding and Recommendation

During our review of controls over inventory, we noted the following:

- The District’s warehouse is managed by one employee. The employee is responsible for receiving inventory from vendors and issuing inventory to employees. However, we noted that the employee has other duties and is not present in the warehouse at all times. Several maintenance employees have access to inventory at all times. While the District requires employees to fill out an inventory control form when they take an inventory item, there is no one to monitor that this is followed. This can result in unauthorized usage of inventory. We recommend that the District consider assigning a storekeeper to the warehouse at all times to control issuance of inventory.

- Based on our observation of inventory locations, although items are kept in a neat order, we noted that not all inventory items are properly labeled. This could lead to employees not familiar with inventory to report the wrong inventory item on the inventory control form. We recommend that the District ensure that all inventory items are labeled properly for easy identification by all employees taking inventory out.

- During our observation of inventory, we noted several items that the staff indicated that the District no longer uses. These items are currently still included in the inventory. We recommend that the District identify obsolete items included in the inventory listing and remove them from the list. We also recommend that the obsolete items are physically separated from other inventory items to avoid having them counted during physical inventory.

- We noted that the District currently performs an inventory count once a year. Per our review of the physical count report, we noted several physical counts had material variances from the perpetual inventory listing. Also, we noted an item in the inventory that contained a costing error. An overall accurate inventory balance is composed of two major components. The first component is proper quantities of goods in inventory and the second is accurate inventory costing. We strongly recommend that the District periodically review the perpetual inventory listing and compare inventory costs to the invoice amounts to ensure accuracy of the unit costs. This practice should help to ensure
3. Inventory (cont.)

that inventories are accurately valued for financial statement purposes. In addition, the perpetual inventory listing should be periodically reconciled to the general ledger.

Management’s Response

District staff will meet to address the concerns noted above by the auditors regarding the District’s inventory. The Director of Finance and Finance staff is currently revising the monthly inventory reconciliation process to incorporate a periodic review of the perpetual inventory listing and reconciliation to the general ledger.

Updated Response

- At this time, it is not feasible to assign a storekeeper to the warehouse at all times to control the issuance of inventory. The area where the inventory is stored is kept locked and is accessible to staff who have keys to the facility. The Director of Operations has been working with his staff to refine the process of filling out the inventory control sheets when inventory is used. Prior to the implementation of the CMMS system, the inventory was tracked through an ACCESS database and inventory control forms were filled out by hand. The inventory is now being managed through the CMMS program by staff who notes on the CMMS work order any items removed from inventory. This automatically updates the amount of items removed from inventory when the work order is closed. Through the inventory control module, the inventory control person is able to count and make adjustments to the inventory as well as adding or deleting items monthly. When a work order is issued, any items removed from inventory required to complete the job are listed on the work order and then updated through the CMMS program by the inventory control person.

- All inventory items have been properly labeled.

- The Director of Operations and the Operations Superintendent have both looked at the inventory and determined that we do not have any obsolete inventory at this time. If we should have items that are considered obsolete down the road, we are working to be able to designate them as such in the CMMS system and run a separate report for the obsolete inventory. Storage of obsolete inventory will be considered in the future.
3. **Inventory (cont.)**
   
   - The Finance Department has been working closely with those personnel in Operations who are responsible for inventory control and the CMMS system. Weekly usage reports are provided to Finance to facilitate the booking of inventory that is used during the month. Work is continuing on getting monthly transaction reports from CMMS showing new inventory added with the associated costs. This report will assist Finance in reviewing the activity against the invoices and purchase orders to ensure accuracy. Once this process is complete, Finance will be able to reconcile the perpetual inventory list to the general ledger monthly. It is anticipated that this will be done by the end of this fiscal year.

4. **Bank Reconciliation**

   **Auditor’s Finding and Recommendation**

   During our review of bank reconciliations, we noted the monthly bank reconciliation is a two-step process. First, finance staff prepares a reconciliation of the receipts and disbursements per the general ledger to the bank statement and forwards to the Director of Finance for review. Second, the Director of Finance reviews the bank statements and general ledger for any other reconciling items. These other reconciling items were not included and documented in the monthly bank reconciliation document prepared by staff. We recommend that the entire bank reconciliation process be formalized into one monthly bank reconciliation document.

   **Management’s Response**

   The recommendation was implemented effective July 2011.

   **No further action required.**
5. Compliance with Investment Policy

Auditors’ Finding and Recommendation

The District’s investment policy sets guidelines on how much can be invested in certain types of investments. These guidelines are more restrictive than the limits set forth by the California Government Code. During our review of the investment policy, we noted that for the month of June, the percentage of the District’s investment in LAIF and Federal Home Loan Bank Securities exceeded the limits set forth in the District’s investment policy. Although, the District remained in compliance with California Government Code, this resulted in the District not meeting the guidelines outlined in the District’s policy. We recommend that the District establish procedures that would ensure adherence to the guidelines spelled out in the District’s investment policy.

Management’s Response

The District’s investment policy reflects both the limits set forth by the California Government Code as well as internal District guidelines. The limitations of the Government Code are the maximum allocations allowed while the District’s more restrictive limitations act as guidelines for management to achieve proper diversification. Per the District’s investment policy, management is required to report to the Board of Directors in the quarterly investment policy any investment types/groups which exceed the guidelines set forth in this policy. The LAIF and FHLB overages were reported to the Board in the Portfolio Compliance Report as part of the Annual Investment Report as of June 30, 2011.

No further action required.