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REPORT NO. 05-680

December 21, 2005

Carolyn White, Board of Education President
Beaver County School District
291 North Main
P.O. Box 31
Beaver, Utah 84713

Dear Ms. White:

We have performed the procedures described below to certain aspects of the Beaver County School District's (the District) internal control for the period July 2002 through May 2005. The purpose of these procedures is to assist the District in evaluating its internal control. The procedures performed were as follows:

1. We reviewed internal control over cash receipting, cash disbursing, recording, and reconciliation duties, including adequacy of separation of duties, for internal control purposes for the District.
2. We reviewed the federal, state, and local grants received by the District. We also tested samples of grant expenditures to determine propriety and compliance with grant requirements.
3. We reviewed certain private donations received by the District. We also examined the District's tracking of these donations to ensure the funds are properly accounted for and expended in accordance with the donation requirements.
4. We tested a sample of the District's cash disbursements, including but not limited to credit card and travel payments, for propriety, reasonableness, and compliance with certain internal and State purchasing policies.
5. We reviewed the District's bookkeeping and tracking procedures for all District funds to ensure that the District is properly handling, recording, and accounting for its funds. In certain cases, we reviewed procedures for fiscal year 2006 due to the fact that the District has recently changed or improved certain bookkeeping and tracking procedures.

6. We reviewed the District's compliance with State laws and policies and procedures regarding remitting employee retirement funds, conflict of interest, surplus property, and equipment and supplies use. We performed testwork to ensure the District is in compliance with State law.
7. We performed other miscellaneous reviews and inquiries related to District procedures.

Our procedures were more limited than would be necessary to express an audit opinion on compliance or on the effectiveness of the District's internal control or any part thereof. Accordingly, we do not express such opinions. Alternatively, we have identified the procedures we performed and the findings resulting from those procedures. Had we performed additional procedures or had we made an audit of the effectiveness of the District's internal control, other matters might have come to our attention that would have been reported to you.

Our findings resulting from the above procedures are included in the attached findings and recommendations section of this report. We feel that Findings Number 1 through 10 are significant weaknesses to the District. If these weaknesses are left uncorrected, an unacceptable amount of errors or misappropriations could occur without detection.

This report is intended solely for the information and use of the District and is not intended to be and should not be used by anyone other than this specified party. However, the report is a matter of public record and its distribution is not limited.

By its nature, this report focuses on exceptions, weaknesses, and problems. This focus should not be understood to mean there are not also various strengths and accomplishments. We appreciate the courtesy and assistance extended to us by the personnel of the District during the course of the engagement, and we look forward to a continuing professional relationship. If you have any questions, please call Debbie Empey, Audit Director, at (801) 538-1342.

Sincerely,

Auston G. Johnson, CPA
Utah State Auditor

cc: Ray Terry, Superintendent

BEAVER COUNTY SCHOOL DISTRICT
FOR THE PERIOD JULY 2002 THROUGH MAY 2005

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BEAVER COUNTY SCHOOL DISTRICT

FINDINGS AND RECOMMENDATIONS FOR THE PERIOD JULY 2002 THROUGH MAY 2005

1. INADEQUATE SEPARATION OF DUTIES (Significant Weakness)

We noted separation of duties weaknesses at the Beaver County School District (the District) as follows:

- The Administrative Secretary has access to cash and checks received, has access to blank manual checks, can enter transactions into and make adjustments to the financial system, and prepares the bank reconciliation.
- The Accounts Payable Clerk has access to cash and checks received in the mail or brought into the office when the other clerk is not present, has the responsibility of preparing manual and system checks, and has access to the signature stamps and password for the signature function in the system. The clerk also mails the checks after they have been reviewed.
- The Business Administrator has access to cash and checks received, reconciles deposits to original receipt records, has access to blank checks, has access to the signature stamps and the password for the signature function on the system, makes entries in the accounting records, and is responsible for communicating financial information to various parties.
- All other employees in the District office have access to blank manual checks as well as cash and checks brought into the office when they are the only one in the office.

Inadequate separation of duties exists when the same individual has access to assets, access to accounting records and/or reconciling responsibilities. Failure to adequately separate duties can allow misappropriation of funds to occur without detection.

Recommendation:

We recommend that the District do the following to separate conflicting duties:

- **Restrict the Business Administrator from having access to cash and checks received.**
- **Restrict the Business Administrator and the Administrative Secretary from having the ability to initiate transactions in the accounts payable function of the accounting system.**
- **Restrict the Accounts Payable Clerk from having access to signature stamps or the password for the signature function in the payables system.**
- **Restrict the Accounts Payable Clerk from handling the payables checks after they have been reviewed. The checks should be mailed by someone who does not have access to the accounting records.**

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- **Have two people retrieve the mail from the post office box, open the mail, and prepare a mail log.**
- **Place a sign clearly visible to anyone paying in person that they should expect a receipt for payment in order to increase controls over cash and checks received over the counter.**
- **Safeguard manual checks by making them accessible to only authorized personnel (also see finding No. 9).**

District's Response:

All recommendations listed have been or are in the process of being implemented. Having two people retrieve the mail is impractical, but to help mitigate the compromise of one person picking up the mail, the BCSD office staff will randomly rotate the mail pick-up.

2. **WEAKNESSES RELATED TO EXPENDITURES** (Significant Weakness)

We reviewed various expenditures from July 2003 to June 2004. Most of the transactions were for travel related items, reimbursements, and credit card payments. We noted the following while reviewing these expenditures:

- a. Of the \$67,568.44 in expenditures reviewed, \$29,686 or 44% lacked adequate supporting documentation. Included in these totals were credit card payments of \$16,885 of which \$13,770 (82%) were unsupported by documentation. Although many of the expenditures generally appeared reasonable based on vendors and amounts, it is impossible to determine with certainty without supporting documentation. The District should ensure that adequate supporting documentation is retained with expenditures to indicate that the expenditure is appropriate, reasonable, and in compliance with purchasing policies. The lack of supporting documentation increases the risk that improper expenditures could occur without detection.
- b. The District policy allows travel advances with the approval of the School Board; however, there is no provision in the policy for any kind of reconciliation between the amount advanced and the amount actually spent on travel. Therefore, there appears to be a lack of accountability for the funds. We noted one travel advance payable to "cash" totaling \$1,450 that we were told was split up and given to four individuals to attend an out-of-state conference. Travel advances should be issued by check to each individual traveling. In addition to the advance, the cost of airfare for three of the participants' spouses was purchased using the District's credit card. Two of the participants reimbursed the District; however, they only reimbursed \$300 of the \$335 airfare, and one of the participants did not reimburse the District for the airfare. A lack of a reconciliation of travel expenses can cause fraud or errors to occur without detection.

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- c. There is no independent detailed review of high risk expenditures such as charges to the District's credit cards which totaled \$16,885 in fiscal year 2004, per diem travel reimbursements which totaled \$6,022 for the District administration, and the Business Administrator's use of the GASCARD. Expenditures such as these that are inherently at higher risk for fraud and waste should be reviewed and approved in detail by someone other than the person who incurred the expenditure. In addition, the Business Administrator reportedly reviews many of the District expenditures prior to payment; however, there is no evidence of this review in the form of initials or a signature. The Business Administrator should document his review and approval of all expenditures in some manner. The lack of independent reviews and approvals of expenditures could result in misappropriation or waste without detection.
- d. The District did not use the correct object codes listed by the Utah State Office of Education (USOE) chart of accounts on some expenditures we tested. The following incorrect account coding was noted:
- At least \$1,700 in food purchases (not related to school lunch) was recorded as supplies in fiscal year 2004. Since the USOE uses the costs of operating the District office in calculating the indirect cost rate to apply to federal grants for reimbursement, and since food costs are considered unallowable costs for federal grants, continual miscoding of these unallowable expenditures to the District office would eventually skew the indirect cost rate calculation, resulting in overcharges to federal grants.
 - A \$59 mileage reimbursement was incorrectly recorded as a travel expense related to the District office. Instead, it related to the food service function.
 - The District split one teacher's pay for one year over a two-year period. This is inappropriate because it misrepresents the timing of expenditures in the financial statements (see finding No. 7).
 - Several purchases of computer equipment totaling \$431 were recorded as travel expenditures.
 - A reimbursement claimed by a District employee included an expenditure that pertained to the prior fiscal year.
 - The District records expenditures of certain carryover funds as "contingency." The "contingency" code is a budgeting code only and should not be used for expenditures.
 - The District records vehicle labor expenditures under object code 440 which should only be used for vehicle rental expense.
 - The District charges all vehicle repair and maintenance costs to the Pupil Transportation Function. Repairs and maintenance on District vehicles should be charged to the appropriate function.
 - The District recorded a \$30 dry cleaning expenditure as supplies.

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Expenditures should always be charged to the appropriate year, fund, location, program, function, and object codes as listed in the USOE chart of accounts. Failure to record expenditures correctly could result in inaccurate information in the financial statements and other reports that are submitted to the USOE.

- e. The District incurred \$145 in late fees and \$92 in finance charges in fiscal year 2004 due to late payments on the District's two credit cards. Bills should be paid in a timely manner to avoid paying unnecessary late fees and interest.

Recommendation:

We recommend that the District:

- a. **Retain adequate supporting documentation with expenditures to indicate that the purchase was appropriate, reasonable, and in compliance with purchasing policies.**
- b. **Amend the travel policy to require that a reconciliation is performed between the amount of the travel advance and the amount spent, that travel advances be issued by check to each individual traveling, and that employees submit documentation for all travel expenses. Also, the District should seek reimbursement for the amounts not reimbursed to the District by employees' spouses.**
- c. **Review and approve all expenditures prior to payment. The approval should be performed by someone other than the person who incurred the expenditure and should be documented.**
- d. **Ensure that all expenditures are recorded properly using the appropriate fiscal year, fund, location, program, function, and object codes as listed in the USOE chart of accounts.**
- e. **Pay bills in a timely manner to avoid paying unnecessary late fees and interest.**

District's Response:

The BCSD travel policy has been amended to address the recommendations for the findings listed in section 2. All expenditures must have a three-tiered prior approval form signed before expending district funds. Proper documentation on all school expenditures, travel expenses or reimbursements must be attached to the three-tiered form prior to payment. Bills are paid on a weekly basis.

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3. INCOMPLETE CHECK REGISTER PROVIDED TO SCHOOL BOARD (Significant Weakness)

The District Administration has provided a report of expenditures to the School Board that is incomplete. The report that has been provided does not include checks that are voided or overruns from the previous check number. Therefore, the list excludes many check numbers every month. The School Board should be provided with a complete list of all checks (such as the "Check Register by Selected Date") issued from the system as well as manual checks (see finding No. 9.b.) and be able to determine the disposition of each check, whether it was issued, voided, or an overrun from a previous check. The School Board is responsible for approving all expenditures of the District; however, they cannot properly perform this function if they are unable to account for all checks issued from the District.

Recommendation:

We recommend that the District Administration provide the School Board with an expenditure report that includes all check numbers for the period under review.

District's Response:

A designated board member reviews all checks and expenditures on a monthly basis. The board of education receives a monthly update of all check numbers, amounts and explanations of expenditures.

4. INADEQUATE MONITORING OF GRANT FUNDS (Significant Weakness)

We reviewed 8 grants received by the District from federal, state, and private sources for the period, and found the following problems:

- a. The District does not maintain adequate records of grant funds received. District personnel were unable to provide a list of all grants received by the District or to provide a complete and reliable resource to compile this information.
- b. For six of the eight grants reviewed, the District did not have a grant document or award document, which outlines allowable activities or expenses for that grant. When questioned regarding the lack of these documents, the District told us that they are just the "fiscal agent." We are concerned that the District does not understand its responsibilities over grant funds. The District should assume full responsibility for the financial management of the grant funds and maintain sufficient documentation for the financial and compliance audit of the grant award. We were able to obtain sufficient information from other sources to perform our testwork; however, the District should

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maintain adequate documentation for its own monitoring purposes as well as for audit purposes.

- c. Some grant expenditures were not approved by both the program administrator over the grant and the Business Administrator. Grant expenditures should be approved by both individuals. Also, as a part of their approval responsibilities, the Business Administrator should be thoroughly familiar with OMB Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments*, to prevent unallowable costs from being charged to federal grants.
- d. Improper expenditures were charged to one grant reviewed. We reviewed one reading grant for \$3,500 received by an elementary school. During fiscal year 2004, \$338 was improperly charged to the grant. Although the expenditures charged were reading related, they were incurred by a school other than the school that received the grant. As a result, \$338 of \$3,500 or 9.7% of the grant was misspent.

These weaknesses can cause grant funds to be spent inappropriately.

Recommendation:

We recommend that the District maintain a list of all grants received, awards or grant documents, and detailed expenditure documentation. We also recommend that both the program administrator and the Business Administrator approve grant expenditures and ensure that all expenditures are allowable and charged to the proper grant account.

District's Response:

The recommendations listed have been or are in the process of being implemented. The business administrator, program administrator and the superintendent all will review and approve grant expenditures.

5. INADEQUATE BANK RECONCILIATIONS AND INACCURATE EXPENDITURE RECORDS (Significant Weakness)

The District's bank reconciliation procedures did not fully reconcile bank records to book records. As a result, we noted five instances in fiscal year 2004 where expenditures were not accurately reflected in the accounting records, including three checks that cleared the bank but the accounting system indicated the check was void (also see finding No. 7), and two checks that were void but the system did not show them as voided checks. The inadequate bank reconciliation procedures did not resolve the discrepancies. Based on our inquiry and observation, as of July 2004 the District has changed their bank reconciliation procedures to resolve the inadequacies; however, we did not perform audit tests to verify that the new

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procedures are adequate. The lack of an adequate bank reconciliation procedure, as well as inaccurate and unreliable expenditure records, increases the risk that misappropriation of funds or misstatement of financial records could occur without detection.

Recommendation:

The District should perform accurate, effective bank reconciliations and resolve discrepancies in the accounting records in a timely manner.

District's Response:

The recommendation has been noted and the change has occurred.

6. RELATED-PARTY TRANSACTIONS AND CONFLICT OF INTEREST ISSUES

(Significant Weakness)

The District has purchased goods and services from at least three District employees and at least two relatives of District employees without maintaining documentation justifying the related-party transactions. Currently, the District continues to purchase paging and radio communication services and vehicle repair services from related parties. According to *Utah Code*, Sections 67-16-7 and 67-16-8, which are incorporated into the District Policies and Procedures Ethics Policy Section I.D, an employee with a conflict of interest should disclose the conflict in a sworn statement to the School Board. We did not note any official disclosures in these instances. In the case of the vehicle repair services, the individual who has responsibility over the maintenance of District vehicles also works part-time at a service station where District vehicles are serviced. This represents a substantial conflict of interest. Although District administration is aware and approves of this situation, at a minimum, the School Board should review any arrangements having a potential conflict of interest and then give their approval in writing if the arrangement is deemed advantageous for the District. Furthermore, since transactions with related parties are generally considered to be higher risk, the District should be vigilant in ensuring that full value is received for funds spent and should retain documentation that indicates proper purchasing procedures were followed in selecting the related party as a vendor.

Recommendation:

We recommend that the District use caution when selecting related parties as vendors of goods and services to the District. When a related party is deemed to be the best provider, the District should disclose the conflict of interest to the School Board as required by District policies, retain documentation to justify the selection of the related party, and be vigilant in ensuring that the District receives full value for the funds spent. Furthermore, the District should review the current conflict of interest situations mentioned above.

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District's Response:

The district acknowledges the recommendations and has implemented changes to address the conflict of interest issue. All hires are done following the new hiring policy. Transportation maintenance is now on a bid basis. Any BCSD employee who may have conflict of interest must now disclose that information before the board will approve purchases of material or services.

7. **INAPPROPRIATE SALARY SPLIT** (Significant Weakness)

The District agreed to distribute and report one-year's salary for an employee over a two year period. The District indicated that the employee desired to have his income split over two years in order to avoid adverse financial consequences that would result by showing too much income in one year. We are uncertain as to the motives of the employee; however, based on information from the Social Security Administration, if the employee was receiving Social Security Benefits, the benefits would have been reduced by \$1 for every \$2 earned above limits set by the Social Security Administration. While it is unclear whether the administration understood the motives of the employee or the potential consequences of this action, allowing this situation without regard to the potential consequences indicates a weak control environment.

Recommendation:

We recommend that the District establish a strong control environment where all employees understand the importance of following established policies and procedures.

District's Response:

BCSD recognizes the significance of this issue and the appearance it may give towards income tax manipulation. The district has implemented procedures to prevent this issue from happening again.

8. **NEED FOR TRAINING RELATED TO THE FINANCIAL SYSTEM** (Significant Weakness)

The District seems to have an inordinate number of problems with "Fiscal," their financial system. Fiscal is a system that was developed and is supported by the Utah State Office of Education (USOE). The majority of the school districts in the State use Fiscal. However, based on our discussions with various individuals, compared to other districts, the Beaver District has many errors or problems which they attribute to the system, such as:

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- a. The system issues checks which clear the bank but are noted as “void” by the system. As a result, there were checks that cleared the bank that were not documented in the District’s financial records. Based on discussion with USOE personnel, this is due to user error and is not an inherent weakness in the system. (See related finding No. 5.)
- b. District personnel are unable to provide a trial balance, general ledger detail report, or other requested financial reports. As a result, it was difficult to obtain financial information necessary to conduct an audit. Based on discussion with USOE personnel, the system does have the capability of producing a general ledger report as well as many other ad hoc reports.
- c. The District has had at least two virus attacks on the system since fiscal year 2004, which resulted in some data loss. District personnel need to ensure they have an adequate virus protection program.

District personnel should obtain training so that they can utilize various financial reports necessary to accurately account for and report on the finances of the District and to protect the financial system from viruses. These problems result in a significant weakness in the District’s ability to monitor and properly account for its funds.

Recommendation:

We recommend that the District work closely with USOE in order to correct problems encountered with the system due to user error and to obtain additional training related to the system’s capabilities and reporting. We also recommend that the District consider the adequacy of its virus software.

District’s Response:

The recommendation has been noted and the change has occurred. BCSD is working closely with USOE to address this issue.

9. **OVERPAYMENTS TO VENDORS** (Significant Weakness)

We noted three instances in our review of expenditures where the District overpaid vendors. In one instance, the vendor was paid by both a high school and the District office for the same invoice. In this case, the vendor notified the District of the overpayment and returned the duplicate payment to the District. In the second instance, the District made a clerical error and overpaid a vendor. In this case, the overpayment was not returned until the overpayment was identified by the state auditors and the District notified the vendor of the overpayment. In the third instance, the District made a duplicate payment on the District’s credit cards. This resulted in a credit balance on the cards for two months. The District should have procedures in place to

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prevent and detect overpayments to vendors. Overpayments to vendors put District funds at risk and could result in a loss of funds.

Recommendation:

We recommend that the District implement procedures to prevent and detect overpayments to vendors.

District's Response:

With the implementation of paying the bills weekly, BCSD and the USOE feel this issue will be greatly mitigated.

10. **LACK OF CONTROLS OVER MANUALLY ISSUED CHECKS**

(Significant Weakness)

The District occasionally issues manual checks instead of checks generated on the financial system. We found several areas where controls need to be implemented and procedures need to be improved:

- a. The District has several different sets of manual checks with different numeric sequences and does not make any effort to use the checks sequentially. This destroys any potential for establishing accountability over these checks. The District should establish a check register or log to ensure that all checks are accounted for and consider destroying all but one set of the current manual checks.
- b. In the past, not all manual checks were recorded on the financial system in a timely manner, and at least one check was never recorded at all. Furthermore, it does not appear that all manual checks were reviewed by the School Board, as required. All disbursements should be recorded on the system in a timely manner and reviewed by the School Board.
- c. The District stores the blank manual checks in an unlocked area adjacent to the Business Administrator's office. Therefore, all employees have access to these checks and also have access to cash and checks received. Checks should be safeguarded in a secure area and only a limited number of employees should have access to those checks.

These weaknesses can cause a misappropriation of funds to occur without detection.

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Recommendation:

We recommend that the District:

- a. Establish accountability for manual checks by using a check register or log and consider destroying all but one set of manual checks.**
- b. Record all manually issued checks on the financial system in a timely manner and provide a complete list of disbursements to the School Board for their review.**
- c. Store checks in a secured area accessible to only authorized individuals.**

District's Response:

The recommendations have been noted and are being implemented or have all ready been implemented.

11. IMPROPER DISPOSITION OF VOIDED CHECKS

The District does not always properly deface voided checks and retain them in the file. We could not locate six checks that were reportedly void. In an additional instance, a voided check was retained and marked void; however, the signature block was still intact. Improper handling of voided checks makes it difficult to establish accountability over those checks and increases the risk that misappropriation could occur without detection.

Recommendation:

We recommend that the District properly deface voided checks and retain them in the file. If the check has been signed, the signature block should be removed.

District's Response:

The recommendation has been noted and is being implemented or all ready has been implemented.

12. CASH RECEIPTING WEAKNESSES

We reviewed all cash receipts received by the District for the period of July 2003 to April 2005 and noted the following problems:

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- a. Two receipt forms were improperly voided. The top copy of the receipt was missing, and the word “void” was written on the carbon copy. In addition, these voided receipts were then entered in the system for a different amount than the amount written on the receipt form. The District’s bank reconciliation procedures detected the error in this situation.
- b. Three receipt forms that were voided appeared to be for receipts received in the mail. However, there was no corrected receipt or explanation as to why the receipt was voided. Someone other than the person who opens the mail should review and initial voided receipt forms to indicate that the receipt is properly voided.
- c. The District re-numbers original receipt records when an error is made entering those receipts into the District’s computer system. The District records all receipts on manual receipt forms, which are then entered into the system. When an error is made which would cause the receipt forms to have a different number than the receipt entered in the system, the District alters the number on the manual receipt form to agree with what was entered in the system. The receipt number on original receipt records should never be altered.
- d. Funds received by the District from the County are received in 2 separate checks. The District records these checks on two separate manual receipt forms but combines these two checks into one receipt when entering them on the system. As a result, the District’s receipt register shows a skipped receipt number when compared to the manual receipt forms.

These weaknesses could cause misappropriation or fraud to occur without detection.

Recommendation:

We recommend that the District:

- a. **Properly void receipts by retaining both the top copy and the carbon copy of all voided receipts and marking the word “void” on the top copy so it also traces to the carbon copy.**
- b. **Have an independent person review and initial any voided manual receipt forms at the time of the void to indicate that the receipt is properly voided. This is especially significant for mailed-in receipts, where the payer is not expecting a copy of the receipt form.**
- c. **Enter manual receipts accurately into the system and refrain from altering the original receipt record when an error is made in the receipt numbering.**

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- d. **Combine the two checks received from the County onto one manual receipt so that the manual receipt record and the system receipt register agree.**

District's Response:

The district acknowledges the recommendations and has implemented changes to address the cash receipting weakness issue. The BCSD board member assigned to finances is responsible as the independent person to review and initial any voided manual receipt forms.

13. **LACK OF SURPLUS PROPERTY POLICY**

The District does not have a policy regarding the sale of surplus property and how the District will address the sale of surplus property to related parties. The District has recently implemented an on-line auction on their website to sell surplus property. Anyone, including District employees, can bid on the surplus property. The District should have a policy in place to ensure that surplus property is disposed of properly and in an independent and ethical manner. The District's policy should also include a procedure to ensure that any sale of surplus property to a related party is handled properly to avoid a conflict of interest or the appearance of a conflict of interest. The lack of policy regarding surplus property and the sale of surplus property to related parties could result in improper disposal of surplus property or a conflict of interest.

Recommendation:

We recommend that the District implement a policy regarding the sale of surplus property to ensure that any sale of surplus property to a related party is managed properly and in an independent and ethical manner in order to avoid a conflict of interest or the appearance of a conflict of interest.

District's Response:

A policy is now in place to address the sale of surplus property.