Board of County Commissioners
Douglas County

We are pleased to present this report related to our audit of the regulatory basis financial statements of Douglas County, Kansas (County) for the year ended December 31, 2013. This report summarizes certain matters required by professional standards to be communicated to you in your oversight responsibility for the County's financial reporting process.

Required Communications

Generally accepted auditing standards (AU-C 260, *The Auditor's Communication with Those Charged with Governance*) require the auditor to promote effective two-way communication between the auditor and those charged with governance. Consistent with this requirement, the following summarizes our responsibilities regarding the financial statement audit as well as observations arising from our audit that are significant and relevant to your responsibility to oversee the financial reporting process.

Our Responsibilities with regard to the Financial Statement Audit

Our responsibility under auditing standards generally accepted in the United States of America, *Government Auditing Standards* issued by the Comptroller General of the United States; the provisions of the Single Audit Act; OMB Circular A-133; OMB's *Compliance Supplement;* and the *Kansas Municipal Audit and Accounting Guide* has been described to you in our arrangement letter dated December 9, 2013.

Overview of the Planned Scope and Timing of the Financial Statement Audit

We have issued a separate communication regarding the planned scope and timing of our audit and have discussed with you our identification of and planned audit response to significant risks of material misstatement.

Accounting Policies and Practices

Accounting Policies – Management has the ultimate responsibility for the appropriateness of the accounting policies used by the County. The County has elected to follow the regulatory basis of accounting as described in the Kansas Municipal Audit and Accounting Guide (KMAAG). This is in accordance with the County's Resolution No. 13-15, which waived compliance with generally accepted accounting principles, as allowed by K.S.A. 75-1120a(c). See Note I to the financial statements for a detailed description of the KMAAG regulatory basis of accounting, along with a description of all the County's significant accounting policies.

The County did not adopt any new significant new accounting policies nor have there been any changes in existing significant accounting policies during the current period.

Significant or Unusual Transactions – We did not identify any significant or unusual transactions or significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.

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Management's Judgments and Accounting Estimates – Following is summary information about the process used by management in formulating particularly sensitive accounting estimates and about our conclusions regarding the reasonableness of those estimates. The following describes the significant accounting estimates reported in the County's December 31, 2013 financial statements:

- Compensated absences: It is the County's policy to permit employees to accumulate certain amounts of vacation and sick leave. The County's policies are discussed in Note III.C.1. As a basis for our conclusions, we obtained a list of accumulated vacation and sick time through December 31, 2013 from the County's payroll system, and recalculated vacation and sick time per County policies for a sample of County employees. In addition, we reviewed total compensated absences by analytically comparing the current year results to prior year history.

- Incurred but not reported claims for workers' compensation and health insurance: The County is self-insured for these risks. Estimates related to health insurance claims are based on a past history of claims incurred, and estimates of the lag time between when a claim is filed and paid. As a basis for our conclusions, we reviewed the County's health insurance liability for claims incurred but not paid at December 31, 2013, in comparison to the historical lag time for claim payments, to ensure amounts projected to be paid after year-end were proper. The estimate for workers' compensation is based on information provided by the third-party administrator regarding outstanding open claims, and their estimates of reserves needed to cover those claims. We obtained these reports, and compared the estimated reserves to prior year data and the County's history of claims expenses.

- Accounting and Financial Reporting by Employers for Post-employment Benefits Other Than Pensions (OPEB): The County sponsors a single-employer defined benefit healthcare plan that provides healthcare benefits to retirees and their dependents, including medical, dental, and vision coverage. The County hires an external actuary to evaluate and estimate the expense/expenditures and related liabilities. See Note III.C.2. As a basis for our conclusions, we obtained the report issued by the actuary, and obtained an understanding of the methods and assumptions used by the actuary as well as evaluating the model used by the actuary for appropriateness and compliance with generally accepted accounting principles.

Audit Adjustments

There were 3 types of audit adjustments to the original trial balance presented to us to begin our audit: 1) to record adjustments to accounts payable to properly recognize current year accrued payroll, 2) to properly record operating and year-end transfers per County resolutions, and 3) to record accounts payable for health insurance claims.

During the course of our audit, we accumulated uncorrected misstatements that were determined by management to be immaterial, both individually and in the aggregate, to the opinion units of the financial statements. Therefore, the adjustments to correct these misstatements were not made to the financial statements. These uncorrected misstatements are summarized in the accompanying schedule.

Management Representations

In connection with our audit procedures, we have obtained a written management representation letter. This representation letter constitutes written acknowledgments by management that it has the primary responsibility for the fair presentation of the financial statements in conformity with generally accepted accounting principles. The representation letter also includes the more significant oral representations made by officers and employees during the course of the audit and includes specific representations, is intended to reduce the possibility of misunderstandings between us and the

County and reminds the signing officers to consider seriously whether all material liabilities, commitments and contingencies or other important financial information have been brought to our attention.

Other Disclosures

- We encountered no disagreements with management over the application of significant accounting principles, the basis for management's judgments on any significant matters, the scope of the audit or significant disclosures to be included in the financial statements.
- We are not aware of any consultations management had with other accountants about accounting or auditing matters.
- No significant issues arising from the audit were discussed or were the subject of correspondence with management.
- We did not encounter any difficulties in dealing with management relating to the performance of the audit.

Internal Controls

In planning and performing our audit of the regulatory basis financial statements of Douglas County as of and for the year ended December 31, 2013, in accordance with auditing standards generally accepted in the United States of America, we considered the County's internal control over financial reporting (internal control) as a basis for designing auditing procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the County's internal control. Accordingly, we do not express an opinion on the effectiveness of the County's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and therefore, significant deficiencies or material weaknesses may exist that were not identified. However, as disclosed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the financial statements will not be prevented, or detected and corrected on a timely basis.

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the following control deficiencies to be significant deficiencies:

<u>Segregation of Duties</u>:

- Payroll Processing: There is lack of adequate segregation of duties in the payroll function. The payroll clerk has access to add employees, modify master file information, process payroll and post to the general ledger. The clerk also has access to blank checks and the signature stamp software. Additionally, there is no reconciliation currently performed between the data in the payroll system and what is posted to the general ledger. Mitigating controls include the fact that department heads, the County Treasurer and Assistant County Administrator receive copies of payroll reports for review. Department heads also review timesheets. Additionally, new hires and terminations are approved by the department heads and County Administrator where applicable. We recommend that human resources set up and maintain employee master records and implement an authorization or approval process for changes made to the payroll system through review of the audit tables.

- Health Department: The Director and Director of Administrative Services have access to all functions in CYMA and the Accountant has access to most areas of CYMA. The Senior Office Assistant processed accounts payable and payroll, with complete access to master files, which would allow for changes in employee and vendor information. The Director of Administrative Services and the Senior Office Assistant can also post journal entries. These individuals also have access to enter cash receipts and adjust accounts receivable balances. Mitigating controls include the fact that all checks require dual signatures; the Senior Office Assistant did not have check signing authority, access to change funds, bank account information, the bank reconciliation module, or access to the blank check stock. Accounts receivable detail is also recorded on a separate system, and the Senior Office Assistant could not create after-the-fact journal entries in the general ledger module. For proper segregation of duties, certain functions should be restricted to avoid conflicts between incompatible functions.

- Journal Entries: Journal entries can be created and posted to the general ledger by the same person. There is no review or approval process of journal entries made, prior to the time they are released. There should be a separation of the creating function and the posting function within the system, or at a minimum, a procedure for conducting a secondary review of journal entries to ensure that undetected manipulation of data on the system does not occur.

- Tax System: During testing of access controls in the Manatron tax system, we noted that there is an “Administrator” function that allows users assigned to this role to have complete access to the system. In 2013, we noted that there are multiple individuals who have complete access to the system, but there are some mitigating controls that do exist: a) the appraised value of property is retained in a separate software package called Orion that only the Appraiser’s office has access to; therefore, these individuals could not change the value of a property, b) when corrections of errors are processed, it begins in the Appraiser’s office and goes through Board approval, and c) these individuals could move from a higher levying tax district to a lower levying tax district; however an outlier would be noticed when mapping out the tax districts.

<u>Financial Statement Preparation</u>:

- Encumbrances / Commitments: The County does not have a formal purchase order system to ensure that all purchase commitments are recorded at year-end. Without a systematic method of gathering this information, there is a risk that purchase commitments will go undetected. Under the statutory basis of accounting, expenditures include cash disbursements, as well as accounts payable and encumbered purchase commitments.

Potential effects of the above noted significant deficiencies include recording of fraudulent transactions resulting in potential misappropriation of assets that may not be detected in a timely manner.

Closing

This communication is intended solely for the information and use of the Board of County Commissioners, management, and others within the organization, and is not intended to be and should not be used by anyone other than these specified parties. It will be our pleasure to respond to any questions you have regarding this report. We appreciate the opportunity to continue to be of service to Douglas County.

Allen, Gibbs & Houlik, L.C.
CERTIFIED PUBLIC ACCOUNTANTS

July 10, 2014
Wichita, KS

Douglas County
Summary of Adjustments Passed
12/31/2013

Description	Debit (Credit) to				
	Assets	Liabilities	Beg. Equity	Revenues	Expenses
Effect of prior year's entries on current year:					
To record payables in non-budgeted funds	$ -	$ -	$ 88,000	$ -	$ (88,000)
To adjust for premiums and accrued interest not reversed correctly			139,140	(139,140)	-
To adjust Health Department cash to actual to correct a system generated error			27,820		(27,820)
Current year adjustments passed:					
To record payables in non-budgeted funds	-	(144,144)	-	-	144,144
	$ -	$ (144,144)	$ 254,960	$ (139,140)	$ 28,324

Current year effect	$ (110,816)
Cumulative effect	$ 144,144