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NEWS RELEASE

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FOR RELEASE September 27, 2017

Auditor of State Mary Mosiman today released a report on a special investigation of the City of Armstrong, Iowa for the period July 1, 2015 through December 31, 2016. The special investigation was performed as a result of concerns regarding the lack of financial records available at the City and undeposited collections.

Mosiman reported the special investigation identified \$100,650.10 of undeposited utility collections and improper and unsupported disbursements. Mosiman also reported \$88,600.00 of this amount is composed of estimated utility collections which were unbilled or not properly deposited. The \$11,475.45 of improper disbursements identified includes \$936.00 of payroll costs, \$2,633.45 of unauthorized payments to City employees, and \$7,906.00 of late fees, penalties, and interest. The \$574.65 of unsupported disbursements included 2 payments which were not approved by the City Council and for which support was not available. As a result, it was not possible to determine the propriety of the payments.

Mosiman also reported it was not possible to determine if all collections were properly deposited or if additional amounts were improperly disbursed because sufficient records were not available.

Mosiman recommended City officials implement procedures to properly backup computer systems and properly secure City Hall, allowing after-hours access to only those staff needing such access. Mosiman also recommended City officials review control procedures to obtain the maximum internal control possible. In addition, utility records should be properly maintained and current and procedures should be established to reconcile utility billings, collections, and delinquent accounts each billing period. The City Council should exercise due care and require and review pertinent information and documentation prior to approving payments. Mosiman also recommended City officials review and implement internal control procedures to obtain the maximum control possible.

Copies of the report have been filed with the Emmet County Sheriff's Office, the Division of Criminal Investigation, the Emmet County Attorney's Office, and the Attorney General's Office. A copy of the report is available for review in the Office of Auditor of State and on the Auditor of State's web site at <https://auditor.iowa.gov/reports/1621-0303-B00F>.

**REPORT ON SPECIAL INVESTIGATION
OF THE
CITY OF ARMSTRONG
FOR THE PERIOD
JULY 1, 2015 THROUGH DECEMBER 31, 2016**

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Auditor of State's Report

To the Honorable Mayor and
Members of the City Council:

As a result of concerns regarding certain disbursements and at your request, we conducted a special investigation of the City of Armstrong. We have applied certain tests and procedures to selected financial transactions of the City for the period July 1, 2015 through December 31, 2016. Based on a review of relevant information and discussions with City officials and personnel, we performed the following procedures:

1. Evaluated the City's internal controls to determine if proper control procedures were in place and operating effectively.
2. Examined selected disbursements for proper approval, adequate supporting documentation, accurate accounting and compliance with the public purpose criteria established by Article III, Section 31 of the Constitution of the State of Iowa. We also determined if disbursements were recorded in a manner consistent with the recommended Uniform Chart of Accounts (COA).
3. Examined selected payroll and related transactions for propriety, proper authorization and accurate accounting.
4. Examined selected receipts for accurate accounting and consistency with the recommended COA.
5. Obtained and examined the City Clerk's financial reports and selected bank reconciliations to determine whether the bank balances properly reconciled to the general ledger account balances and monthly financial reports provided to the City Council. We also examined the City's fiscal year 2016 Annual Financial Report to determine whether it was completed and accurately reflects the City's financial information.
6. Examined the annual certified budget for proper authorization, certification and timely amendment to determine compliance with the requirements of the *Code of Iowa* and to determine whether the approved budget was exceeded.
7. Determined compliance with certain sections of the *Code of Iowa*. Specifically, we examined:
 - selected City Council meeting minutes for compliance with Chapters 21, 372.13(6) and 380,
 - surety bond coverage for compliance with Chapter 64,
 - investments to determine compliance with Chapter 12B,


- compliance with sections 12C.2, 12B.10B and 556.1(12) pertaining to required depository resolutions, investment policy and reporting of unclaimed property to the State of Iowa,
 - debt, including general obligation and revenue bonds/notes, and related transactions for proper authorization and compliance with Chapters 75, 384 and 403.9 and to determine whether the debt and related proceeds and repayments were properly accounted for,
 - reviewed and tested selected tax increment financing (TIF) transactions, including receipts, disbursements and transfers, for compliance and accurate accounting, including compliance with the TIF reporting requirements of Chapter 384.22, and
 - the City's TIF debt certification forms filed with the County Auditor, including requests for collection of reduced TIF amounts and to decertify certain TIF obligations, as applicable, for proper support and compliance with Chapter 403.19(6).
8. Examined City records to determine consistency with the City Finance Committee's recommended COA fund structure and to determine if required funds and fund balances are properly maintained and accurately accounted for.

These procedures identified \$100,650.10 of undeposited utility collections and improper and unsupported disbursements. Several internal control weaknesses were also identified. Because sufficient supporting documentation was not maintained, it was not possible to determine if all collections were properly deposited or if additional amounts were improperly disbursed. Our detailed findings and recommendations are presented in the Investigative Summary and **Exhibit A** of this report.

The procedures described above do not constitute an audit of financial statements conducted in accordance with U.S. generally accepted auditing standards. Had we performed additional procedures, or had we performed an audit of the City of Armstrong, additional matters might have come to our attention that would have been reported to you.

Copies of this report have been filed with the Emmet County Sheriff's Office, the Division of Criminal Investigation, the Emmet County Attorney's Office, and the Attorney General's Office.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of the City of Armstrong during the course of our investigation.


MARY MOSIMAN, CPA
Auditor of State

March 28, 2017

Report on Special Investigation of the
City of Armstrong
Investigative Summary

Background Information

The City of Armstrong (City) is located in Emmet County and has a population of approximately 900. The City employs a City Clerk who is responsible for the business operations of the City. The City also employs maintenance employees and a Police Chief.

Connie Thackery was the City Clerk/Treasurer until she retired in February 2016. Kate Staton became the City Clerk after Ms. Thackery's retirement. The City Clerk is responsible for the following functions:

- Receipts – collection, posting to the accounting records, and preparing and making bank deposits;
- Disbursements – making certain purchases, receiving certain goods and services, presenting proposed disbursements to the City Council for approval, maintaining supporting documentation, preparing, signing, and distributing checks, and posting to the accounting records;
- Payroll – calculating payroll amounts, preparing signing, and distributing checks, posting payments to the accounting records, and filing required payroll reports;
- Utility billings – preparing and mailing billings, receipting and depositing collections, posting collections to customer accounts and accounting records, and preparing and making bank deposits;
- Bank accounts – receiving and reconciling monthly bank statements to accounting records; and
- Reporting – preparing City Council meeting minutes and financial reports, including monthly City Clerk reports and the Annual Financial Reports.

The City's primary revenue sources include local option sales tax and road use tax from the State of Iowa and property tax collected by Emmet County and remitted to the City. Revenue is also received from customers for water, sewer, and garbage services. The City receives payments from the State and County electronically. Utility payments are collected through the mail, in person, or in the collection box at City Hall. City Clerks did not consistently prepare receipts for collections or record the collections on an initial receipts listing.

The City also collects revenue from operations at the City pool, including proceeds from the sale of seasonal passes, daily admissions, and concession sales.

We were engaged by the City to perform an audit of the City's financial statements for the year ended June 30, 2016. However, at the beginning of our fieldwork, we were informed the City's computerized accounting system had failed and financial records were not available. As a result, we informed City officials we were unable to perform an audit, but would attempt to compile the City's financial information. However, due to the state of the accounting records or lack thereof, we were also unable to compile the City's financial information for the year ended June 30, 2016. As a result, we performed a City examination pursuant to section 11.6 of the *Code of Iowa*. An examination is designed to focus on the financial processes of a city to help ensure accountability and compliance.

In November 2016, City officials voiced concerns regarding the lack of cash deposited for the pool and utility billings for several months. On November 29, 2016, the Emmet County Sheriff's Office (Sheriff's Office) removed various financial records from City Hall.

On December 8, 2016, we observed an envelope held at the Sherriff's Office containing a significant amount of cash which had not been counted or deposited. At that time, we were also informed City officials determined collections from the pool had been deposited to a City bank account, but because they were deposited to the incorrect account they were not initially identified. City officials also stated they believed the undeposited cash seized by the Sheriff's Office included collections from the City's pool.

As a result of the concerns identified and the confusion regarding the cash collections, we determined it was appropriate to perform a special investigation rather than an examination in accordance with section 11.6 of the *Code of Iowa*. To conduct the special investigation, we performed the procedures detailed in the Auditor of State's Report for the period July 1, 2015 through December 31, 2016.

Detailed Findings

The procedures performed identified \$100,650.10 of undeposited utility collections and improper and unsupported disbursements. Of the \$100,650.10 identified, \$88,600.00 is composed of estimated utility collections which were unbilled or not properly deposited. The \$12,050.10 of improper and unsupported disbursements identified includes \$936.00 of payroll costs, \$2,633.45 of unauthorized payments to City employees, and \$7,906.00 of late fees, penalties, and interest.

Because sufficient supporting documentation was not maintained, it was not possible to determine if all collections were properly deposited or if additional amounts were improperly disbursed. All findings are summarized in **Exhibit A** and a detailed explanation of each finding follows.

UNDEPOSITED COLLECTIONS

According to City officials, in May 2016, the City attempted to upgrade its operating system which supported the City's accounting software. The upgrade caused a computer failure which resulted in the City losing all financial information stored in its accounting system. The City did not have back-up procedures in place or a contract with the accounting software provider to back up its information. As a result, the City was unable to provide detailed financial information, including financial activity for each fund, general ledger balances, or utility system billing and other reports. While we were unable to verify the computer failure, we were unable to locate sufficient records in City Hall.

In addition, with the exception of a monthly utility billing report from February 2016, the City was unable to locate paper copies of general ledger and utility reports which may have been previously printed. As a result, a general ledger and utility records were not available for the period reviewed.

City records include a written assertion from Ms. Staton which states, in part, "Both maintenance men, the police officer, and mayor have access to city hall at any time of the day." The written assertion also stated, "I did not have the office locked appropriately," as a result, several individuals had access to all files and financial information. In the written assertion, Ms. Staton also stated others, such as the Mayor and a maintenance man sat at her desk when she was absent. She stated she was concerned money had been "misplaced" on 2 occasions while she was gone and personal checks of citizens were "misplaced" on 4 separate occasions. In addition, she stated several pieces of mail had been "lost."

Ms. Staton's written assertion also stated, "I was gone in late July [2016] shortly before our audit was to begin and when I returned my computer had completely crashed again (without having had an update or any reason to lose any information) [Mayor] Greg Buum had access to the computer at this time, and I never fully received an explanation as to why it might have gone down at this point." When we spoke with the Mayor, he stated he did not access the computer.

However, as Ms. Staton had documented in the written assertion, other City personnel also had access to the computer during this period. We were unable to verify the July computer failure described by Ms. Staton.

Based on Ms. Staton's statements, all employees have access to the City's computer, cash collections, and mail received at City Hall. City Hall is not adequately secured and collections are not properly accounted for and safeguarded until deposited. In addition, we determined the City's computer did not have proper password protection. As a result of these concerns and the concerns previously described regarding the undeposited collections, we performed certain procedures to determine if collections were properly deposited.

Utility Billings – Because the billing register for February 2, 2016 was the only utility report the City could locate, it was the only billing register available for testing. For 3 of the 17 customer billings tested from this billing register, the amounts recorded in the meter reading logs did not agree with the beginning of month balances in the billing register.

Based on our review of the meter reading logs, meters were read in February and March 2016. However, they were not read in April or May 2016. As previously stated, the City experienced a computer crash in May and all utility records were lost. During our fieldwork, City personnel were working to rebuild the utility billing system and determine if all usage had been properly billed. The utility billing system was not restored prior to the end of our fieldwork.

In addition to meters not being read in April and May 2016, City personnel we spoke with reported a number of meters had not been functioning properly for an extended period of time. City personnel were not able to provide a listing or any other records to document which meters were broken and/or unread. Because certain meters were broken or unread, the recorded meter readings were not reliable. City personnel stated utility billings were based on average usage amounts for the utility customers with broken or unread meters. However, the City did not retain documentation of how the bills were calculated or the amounts the City billed.

During our review of the February 2016 billing register, we determined the sewer tax was not properly charged for certain commercial customers. The tax not properly charged to the commercial customers is not included in **Exhibit A** due to the insignificant amount we could identify and the lack of records available for all activity.

Utility Collections – Because detailed utility records were not available, we were unable to determine if all utility collections received by the City were properly deposited in the City's bank accounts.

During our review of utility collections deposited to the City's bank accounts during June 2016 through September 2016, we determined the amounts deposited were not consistent each month and ranged from \$7,257 to \$13,422. We were unable to determine why the amounts deposited were not more consistent. However, the written assertion from Ms. Staton previously referred to stated, in part, "A cash deposit was made in June from payments made on May issued water bills. Because the system crashed the end of May no one received a water bill in June, therefore clearly no one paid a water bill either." However, based on bank statements, certain customers continued to pay for utilities even though billings were not distributed by the City.

Ms. Staton's written assertion goes on to state:

"In mid-July as I continued to work to rectify the issues with the computer I was able to send out bills for the time period or a portion of July through August (some of them hand written) then getting roughly half a set of water bills out, for which receipts and cash remain in the cash bag.

**a ding from my audit was that there is too much cash being held in city hall.

There are more cash receipts for the following months of September and October which were more on the right track but still aren't completely rectified and cash in the cash bag from this time period as well. In September I paid the community Center cleaning company in cash from the City Hall. There is an invoice relative to that."

Ms. Staton's notations did not specify the amounts billed or collected for the months during which she worked to recover the utility billing system.

Based on the number of approximate number of utility accounts and the approved minimum utility billing rates, we estimated the minimum amount the City should have billed each month from June through September of 2016. We then compared the estimated amount of billings to the total utility collections deposited to the City's bank account for each month. **Table 1** summarizes this comparison.

Table 1

Month	Estimated Utility Billings	Total Utility Bank Deposits	Difference
June 2016	\$ 33,800	9,685	24,115
July 2016	33,800	16,236	17,564
August 2016	33,800	7,257	26,543
September 2016	33,800	13,422	20,378
Total	\$ 135,200	46,600	88,600

As illustrated by the **Table**, the estimated amounts of minimum utility billings exceed the amounts deposited by \$88,600.00. However, because sufficient records are not available from the City's utility billing system, we are unable to determine what portion of the monthly estimated billings were not billed, not collected, and/or not deposited from June 2016 through September 2016. Because the City should have billed, collected, and deposited at least the \$135,200.00 estimated, the \$88,600.00 not properly deposited is included in **Exhibit A**.

In addition, during our review of deposits to the City's bank account for the period June 2016 through September 2016, we determined the deposits did not include any cash. However, for the months of January 2017 and February 2017 cash deposits averaged \$1,403 each month. City officials were not able to provide an explanation of why the deposits from June 2016 through September 2016 did not include any cash. However, as previously stated, Ms. Staton's written assertions found in the City's records includes a notation cash collected for utilities from June through September were in the cash bag. Because the City's records are not sufficient, we are unable to determine if cash collected for utilities were properly deposited.

Cash collections – On December 8, 2016, we observed an envelope at the Sheriff's Office containing a significant amount of undeposited cash. Based on inquiry of City officials, this cash was believed to be undeposited collections from the City's pool. However, supporting documentation was not available to verify this explanation.

In addition, on March 14, 2017 we observed 12 undeposited checks at City Hall totaling \$1,236 and dated between May 20, 2016 and November 16, 2016. Of the 12 checks, we determined 5 were for utility payments, 1 was issued to the pool, and 6 did not include a description or notation of what the payment was for.

We also determined 2 warrants from the State of Iowa to the Armstrong Public Library were not deposited in a timely manner. Specifically, we determined a \$1,170.55 warrant issued on September 2, 2015 was not redeemed until October 9, 2015 and a \$273.11 warrant issued on November 5, 2015 was not redeemed until November 30, 2015. In addition, an envelope containing \$43.00 in cash was in the cash box. The envelope was labeled as a memorial for an

individual who passed away 5 months prior to the cash count we performed. The cash should have been deposited until the memorial funds were properly disbursed.

With the exception of the 2 warrants issued to the Armstrong Public Library, all other warrants from the State of Iowa to the City were properly deposited. However, they were not properly recorded in the City's receipt records.

Because sufficient records were not prepared and/or maintained, we are unable to determine if any additional collections were received by the City but not properly deposited. As a result, we have not included an amount in **Exhibit A**.

IMPROPER AND UNSUPPORTED DISBURSEMENTS

We reviewed certain disbursements from the City's bank accounts for the period July 1, 2015 through December 31, 2016. We also attempted to review supporting documentation for the disbursements to determine if they were appropriate; however, supporting documentation was not maintained for some of the disbursements.

We reviewed available documentation. However, because supporting documentation was not available for all disbursements, we reviewed the payees and other notations on images of redeemed checks. We also reviewed minutes of City Council meetings and approved disbursement listings to determine if the payments were authorized. In addition, we discussed the disbursements with City officials to determine propriety.

Based on our review of any available supporting documentation, the vendor, the frequency, and the amount of payments, and discussions with City officials, we classified payments as improper, unsupported, or reasonable. Payments were classified as improper if they appeared personal in nature or were not reasonable for the City's operations. Payments were classified as unsupported if it was not possible to determine if the payment was related to the City's operations or was personal in nature. Disbursements were classified as reasonable if the vendor, frequency, and amount of payments to vendors appeared appropriate for the City's operations.

The improper disbursements identified are discussed in detail in the following paragraphs.

Payroll – The City Clerk is responsible for preparing payroll for all City employees. City employees are to be paid twice each month. Specifically, they are to be paid on the 15th and the last day of each month. Their gross payroll is based on an hourly pay rate and the number of hours for which they are paid should be supported by a time sheet which summarizes the amount of time worked during the pay period. During our review of the components of payroll costs, we identified several concerns which are summarized in the following paragraphs.

Payroll checks – During our review of payroll checks issued to City employees, we identified the following concerns:

- On May 9, 2016, Ms. Staton received a wage increase of \$0.75 per hour. On May 10, 2016, she received \$520.00 for 693.3 hours of back pay at \$0.75 per hour. Support for the 693.3 hours was not available. In addition, the back pay was not approved by the City Council. City officials we spoke with were not able to provide additional information. As a result, the \$520.00 is included in **Exhibit A** as an improper disbursement. The City's records are not sufficient to determine if the City incurred additional costs for the City's share of FICA and IPERS for the payment.
- For the period May 2016 through December 2016, 4 overtime payments were made to City maintenance employee, Tylor Evans; however, the records do not clearly identify the pay periods when the overtime was earned. In addition, of the 4 overtime payments identified, the overtime payment issued to Mr. Evans on

September 12, 2016 was not approved by the City Council. City officials we spoke with were not able to provide additional information. However, because the payments are reasonable, the amounts paid to Mr. Evans are not included in **Exhibit A**.

During our review of payroll disbursements, we also determined \$210.00 was withheld from Mr. Evans' payroll check dated August 11, 2016. While it is appropriate for the City to withhold garnishments for child support or other obligations, the amounts withheld are to be remitted to the party filing the garnishment. In this case, check number 21888 was issued to an individual in August for \$210.00.

Timesheets – During our review of time sheets maintained for City employees, we determined the following:

- For the period July 1, 2015 through December 15, 2016, timesheets were not available to support 12 of 32 pay periods tested for Ms. Staton.
- For the period May 25, 2016 through December 31, 2016, timesheets for Mr. Evans could not be located for 5 of 15 pay periods tested.
- There was no indication the timesheets we tested had been reviewed and approved by supervisory personnel.

Because timesheets were not available for certain pay periods, we are unable to determine if the amount paid to the employees was appropriate. As a result, we have not included any amounts in **Exhibit A**.

Timing of payments – The City's Employee Handbook states, "The standard pay period is on the 15th and the last day of the month." For 11 of the 33 pay periods between August 2015 through December 2016, payroll checks were written more than 1 day prior to the 15th or the last day of the month. The checks for these pay periods ranged from 2 to 6 days prior to the end of the pay period. While these payments were made prior to their authorized date, they were not for an improper amount. As a result, we have not included anything in **Exhibit A** for them.

Paid time off – The City's Employee Handbook states "Any Paid Time Off (PTO) not used by the anniversary date of the following year will not carry over. Remaining days left up to five (5) will be paid to the employee after the anniversary date."

The record of PTO provided by the City is not complete and is not reviewed and reconciled by an independent person.

Ms. Staton was paid \$936 on October 16, 2016 for 72 hours of PTO. In accordance with the City's policy, no more than 40 hours of unused PTO, or a total of \$520, should have been paid out. Because the PTO records were not complete, we were unable to determine the actual hours which should have been paid out. However, the City overpaid for unused PTO by a minimum of \$416. In addition, this payment was not approved by the City Council. As a result, the \$416 payment is included in **Exhibit A** as an improper disbursement.

Payments to Individuals – In addition to payroll, we tested certain other payments to City employees. During our review, we determined certain payments were not authorized by the City Council. We also determined the payments were not supported and/or not in compliance with the City's Employee Handbook. The payments identified are described in the following paragraphs.

- The City's Employee Handbook states, "Dental and Optical insurance are not provided, but \$400 per year will be paid toward dental and optical expenses for each employee." We determined \$400.00 checks were issued to both Ms. Staton and

Mr. Evans for vision and dental reimbursements on September 12, 2016 and October 11, 2016, respectively. However, there was no supporting documentation to substantiate the employees incurred vision and dental expenses. As a result, the employees were not authorized to receive the \$400 payments. In addition, the payments were not included in the employees' taxable wages. As a result, the payments are improper.

- The City does not have a policy regarding cell phone allowances. However, Ms. Staton received check number 21823 for \$300 on July 12, 2016 for a cell phone allowance during the period reviewed. As a result, the payment is improper. In addition, the payment was not included in her taxable wages.
- Ms. Staton issued herself check number 21892 in August 2015 for \$605.82. The check was cosigned by the Mayor but the payment was not approved by the City Council. We were unable to determine what the payment was for because supporting documentation was not available and City officials we spoke with were unable to provide an explanation for the unusually large payment. As a result, the payment is improper.
- Ms. Staton issued check numbers 21327 and 21347 for \$601.76 and \$325.87 to Mr. Evans on November 14, 2016 and December 14, 2016, respectively. We were unable to determine what the payments were for because supporting documentation was not available and City officials we spoke with were unable to provide an explanation for the unusually large payments. In addition, the payments were not approved by the City Council. As a result, they are improper.

The \$2,633.45 of improper payments to Ms. Staton and Mr. Evans are included in **Exhibit A** as improper disbursements.

Payments to Vendors – During our review of disbursements to vendors, we identified certain payments for which supporting documentation was not available. However, some of the payments were approved by the City Council and, based on the vendors and payment amounts, the disbursements appeared reasonable for City operations.

However, we identified 2 disbursements for which supporting documentation was not available and which were not approved by the City Council. Based on the vendors and the amounts of the payments, we are unable to determine of the payments were for City operations or personal in nature. The 2 disbursements identified are listed in **Table 2**.

Date Cleared	Check Number	Vendor	Amount
10/16/15	20826	Carlson Dental	\$ 400.00
04/14/16	21118	Postmaster	174.65
Total			\$ 574.65

As stated previously, The City's Employee Handbook states, "Dental and Optical insurance are not provided, but \$400 per year will be paid toward dental and optical expenses for each employee." As illustrated by **Table 2**, a \$400.00 check was issued to a dental office in October 2015. However, because supporting documentation was not available for the payment, we are unable to determine who received services or if they were eligible for the \$400.00 benefit from the City. As a result, the payment is classified as unsupported.

Because we were unable to determine the propriety of these payments, the \$574.65 total is included in **Exhibit A** as unsupported disbursements.

Late fees, penalties, and interest – During our review of disbursements, we identified late fees, penalties, and interest paid by the City, including penalties and interest paid to the IRS for the late submission of certain quarterly Internal Revenue Service (IRS) 941 reports. The amounts the City paid for late fees, penalties, and interest are summarized by vendor in **Table 3**. Late fees and interest were incurred on multiple occasions for certain vendors, including the City’s credit card, AgSource, and Ringtel.

Table 3

Description	Amount
IRS 941 reports for FY16	\$ 6,408.35
IRS 941 reports for FY17	982.94
Cardmember Service (credit card)	404.85
AgSource	31.72
IMWCA	30.30
Ringtel	20.00
Stanley Propane	20.64
One Source	7.20
Total	<u>\$ 7,906.00</u>

The \$7,906.00 of late fees, penalties, and interest paid by the City are included in **Exhibit A** as improper disbursements.

Recommended Control Procedures

As part of our investigation, we reviewed the procedures used by the City of Armstrong to perform bank reconciliations and process receipts, disbursements, and payroll. An important aspect of internal control is to establish procedures which provide accountability for assets susceptible to loss from error and irregularities. These procedures provide the actions of one individual will act as a check on those of another and provide a level of assurance errors or irregularities will be identified within a reasonable time during the course of normal operations. Based on our findings and observations detailed below, the following recommendations are made to strengthen the City's internal controls.

- (A) Accounting System and Records – Financial records, including the City's general ledger and utility reports were not available for review and procedures were not in place to ensure electronic records were periodically backed up to allow for continuation of operations in the event of a computer failure. In addition, financial records were not secured within City Hall.

Recommendation – City officials should develop written accounting procedures which include back up of the City's accounting system. Back up procedures should be completed at a minimum of once a week and the back-up tapes should be stored off site in a secure location.

City officials should also ensure City Hall is properly secured. Only approved staff who require access to the building outside normal business hours should have such access. The City should develop policies and procedures to ensure all financial records are secured and collections are properly accounted for and safeguarded prior to deposit. The City should also ensure computer access is limited to staff requiring access to perform their duties. In addition, computers should be password protected.

- (B) Segregation of Duties – An important aspect of internal control is the segregation of duties among employees to prevent an individual employee from handling duties which are incompatible. Generally, one individual has control over each of the following areas for the City:

- (1) Accounting system - performing all general accounting functions, including journal entries and having custody of assets.
- (2) Cash – preparing bank account reconciliations, initiating cash receipt and disbursement transactions, handling and recording cash and control of petty cash.
- (3) Investments – recordkeeping, investing, custody of investments and reconciling earnings.
- (4) Long-term debt – recording and reconciling.
- (5) Receipts – opening mail, collecting, depositing, recording and reconciling.
- (6) Utilities – billing, collecting, depositing, entering rates into the system and maintaining detailed accounts receivable records.
- (7) Disbursements – purchasing, invoice processing, check writing, mailing, reconciling, access to credit cards and recording.
- (8) Payroll – recordkeeping, preparing and distributing.
- (9) Financial reporting – preparing and reconciling.

- (10) Information system (computer usage) – performing all general accounting functions and controlling all data input and output.

Recommendation – We realize segregation of duties is difficult with a limited number of employees. However, the City should review its control procedures to obtain the maximum internal control possible under the circumstances utilizing currently available staff, including elected officials. Independent reviews of reconciliations should be documented by the signature or initials of the reviewer and the date of the review.

- (C) Reconciliation of Utility Billings, Collections and Delinquent Accounts – Utility billings, collections and delinquent accounts were not reconciled throughout the year and a delinquent account listing was not prepared monthly.

Recommendation – A listing of delinquent accounts should be prepared monthly. Procedures should be established to reconcile utility billings, collections and delinquent accounts for each billing period. The City Council or other independent person designated by the City Council should review the reconciliations and monitor delinquent accounts. The review should be documented by the signature or initials of the reviewer and the date of the review.

- (D) Bank Reconciliations – While it appeared some bank reconciliations were performed, they were not performed consistently throughout the year. For the bank reconciliations observed, the amounts were reconciled to a monthly City Clerk’s Report, however, it was not clear whether the bank and investment balances were reconciled to the City’s general ledger. In addition, a listing of outstanding checks was not maintained. Bank reconciliations observed were not independently reviewed.

Recommendation – The City should establish procedures to ensure bank and investment account balances are reconciled to the general ledger monthly and variances, if any, are reviewed and resolved timely. An independent person should review the reconciliations and document the review by signing or initialing and dating the monthly reconciliations.

- (E) Payroll – We determined payroll checks were issued between 2 and 6 days prior to the end of the pay period for 11 of the 33 pay periods between August 2015 and December 2016.

Recommendation – Someone independent of the payroll process, such as a City Council member, should review and countersign all payroll checks. This individual should ensure checks are not issued prior to the end of the pay period.

- (F) Monthly City Clerk’s Report – During our initial visit, the City was unable to provide copies of the monthly City Clerk’s Reports. However, copies of certain City Clerk Reports were provided subsequent to our initial visit. Due to the lack of a general ledger, we were unable to determine the accuracy of these reports.

The monthly City Clerk’s Reports reviewed included cash and investment balances by fund. However, the reports did not include of a comparison of year-to date disbursements to the certified budget by function.

Recommendation – The City should establish procedures to ensure City Clerk’s Reports are prepared monthly, and are retained. The monthly reports should be provided to the City Council for review and approval. To provide better control over budgeted disbursements and the opportunity for timely amendments to the certified budget, the monthly City Clerk’s Reports to the City Council should include comparisons of year-to-date disbursements to the certified budget by function.

(G) Computer System – To ensure the integrity of the City’s electronic data, the City does not have written policies for:

- (1) Requiring user IDs or passwords.
- (2) Requiring password privacy and confidentiality.
- (3) Requiring password changes every 60 - 90 days.
- (4) Maintaining password history to prevent employees from using the same password.
- (5) Ensuring only software licensed to the City is installed on its computers.
- (6) Personal use of City equipment and software.
- (7) Usage of the internet.
- (8) Back up procedures.
- (9) Disaster recovery plan.

Recommendation – The City should develop written policies addressing the above items to improve the City’s control over its computer system.

(H) Investments – An accounting record/register is not maintained for each investment.

Recommendation – An accounting record/register for each investment which includes the cost, description, date purchased, interest rate, maturity date and identifying number should be maintained.

(I) Prenumbered Receipts – Prenumbered receipts were not issued for all collections and an initial listing of collections was not prepared.

Recommendation – Prenumbered receipts should be issued for all collections and an initial listing of collections should be prepared. These collections should be compared to the bank deposit and the accounting records by an independent person and the evidence of review should be documented. In addition, the individual comparing the deposit to the accounting records should ensure deposits are made in a timely manner.

(J) Disbursements – During our testing, we determined certain disbursements were not properly supported and not all disbursements were properly authorized by the City Council.

Recommendation – All disbursements should be supported by invoices or other supporting documentation and should be approved by the City Council.

(K) Credit Cards – The City has credit cards and store charge accounts for use by various employees while on City business. The City has adopted a credit card policy which requires original itemized receipts to validate expenses on City issued credit cards and store charge accounts.

Itemized receipts were not consistently maintained or available to support all credit card and store charge card purchases. Also, 1 of 7 store charge card statement payments was not properly approved by the City Council.

Recommendation – Original receipts should be provided to the City Clerk and reconciled to the credit card or store charge card statements each month and charges should be reviewed and scrutinized for compliance with City policy prior to approval and payment. All payments on accounts should be approved by the City Council.

- (L) Vehicle Mileage Logs – The City utilizes credit cards and store charge cards to purchase fuel for City owned vehicles. Mileage logs are not completed and maintained to support fuel charges.

Recommendation – Mileage logs should be maintained and compared to credit card and store charge card receipts to verify the propriety of fuel purchases.

- (M) Revolving Loans – At June 30, 2016, the City had 9 outstanding economic development loans totaling \$96,865. Payments on one outstanding loan are current and partial payments have been made on another loan. The remaining seven loans are delinquent and payments do not appear to have been made on these loans for over two years.

Recommendation – The City should consider options for collecting the outstanding delinquent loans.

- (N) Chart of Accounts – The City has not fully implemented the recommended Uniform Chart of Accounts (COA) for Iowa City Governments approved by the City Finance Committee.

Recommendation – To provide better financial information and control, the recommended COA, or its equivalent, should be followed.

- (O) Loan Agreement – The City entered into a loan agreement totaling \$60,000 for painting the water tower. The City did not comply with the provisions of Chapter 384.24A of the *Code of Iowa* which requires certain authorization procedures be followed prior to entering into a loan agreement, including publication of intended action and time and place of a public meeting to approve the intended action.

In addition, the public hearing was held on September 14, 2015 while the loan is dated August 31, 2015 and the loan funds were received by the City on September 2, 2015.

Recommendation – The City should comply with Chapter 384.24A of the *Code of Iowa* prior to entering into future loan agreements.

- (P) City Council Meeting – The City Council went into closed session on May 9, 2016. The closed session was not in compliance with Chapter 21.5 of the *Code of Iowa*. The session was not closed by affirmative vote of at least two-third of the members and the specific exemption under Chapter 21.5 for closing the session was not identified or documented.

Recommendation – The City should comply with Chapter 21.5 of the *Code of Iowa*.

- (Q) Transfers – Supporting documentation was not maintained for interfund transfers and transfers were not approved by the City Council.

Recommendation – Supporting documentation should be maintained which substantiates interfund transfers. In addition, all interfund transfers should be approved by the City Council and the approval should be documented in the City Council meeting minutes or the budget, as applicable.

- (R) Local Option Sales Tax – The City imposed a local sales tax in the City with receipts to be allocated as follows: 60% for street repair, 10% for recreation, 10% for public safety, 8% for economic development, 5% for the library, 5% for the community center and 2% for senior citizens. Documentation has not been maintained to demonstrate the LOST receipts were spent in accordance with the provisions of the referendum authorizing the collection of the tax.

Recommendation – The City should maintain documentation to demonstrate local option sales tax collections are disbursed in compliance with the provisions of the LOST referendum.

- (S) Accounting Policies and Procedures Manual – The City does not have an accounting policies and procedures manual.

Recommendation – An accounting policies and procedures manual should be developed to provide the following benefits:

- (1) Aid in training additional or replacement personnel.
- (2) Help achieve uniformity in accounting and in application of policies and procedures.
- (3) Save supervisory time by recording decisions so they will not have to be made each time the same, or a similar, situation arises.

- (T) Tax Increment Financing (TIF) Indebtedness Certification – Chapter 403.19 of the *Code of Iowa* provides a municipality shall certify indebtedness to the County Auditor. Such certification makes it a duty of the County Auditor to provide for the division of property tax to repay the certified indebtedness and, as such, the County Auditor shall provide available TIF increment property tax in subsequent fiscal years without further certification until the amount of certified indebtedness is paid to the City. Indebtedness incurred is to be certified to the County Auditor and then the divided property tax is to be used to pay the principal of and interest on the certified indebtedness. In November 2015, the City certified a rebate agreement for \$118,933, which was previously certified. The Emmett County Auditor identified the debt as being previously certified and did not include as debt to be paid from available TIF funds.

Recommendation – The City should review its procedures to ensure TIF debt is certified only once, as required.

- (U) Annual Financial Report – Chapter 384.22 of the *Code of Iowa* requires a city to publish an Annual Financial Report (AFR) no later than December 1 of each year. The AFR shall contain a summary for the preceding fiscal year of all collections and receipts, all accounts due the city, and all expenditures, the current public debt of the city and the legal debt limit of the city for the current fiscal year. Due to lack of financial records, the City did not publish its fiscal year 2016 AFR by December 1, 2016.

Recommendation – The City should ensure records are maintained in a manner which allows for timely submission of the required AFR.

- (V) Financial Condition – At November 30, 2015, the most recent monthly City Clerk's Report available, the City had deficit balances of \$62,142 and \$55,012 in the General and Enterprise, Garbage Funds, respectively. Due to the lack of City records, we are unable to determine the accuracy of the amounts reported.

Recommendation – As previously stated, the City should ensure adequate financial records are maintained so the accuracy of reports may be readily verified by parties independent of their preparation. In addition, City officials should investigate alternatives to eliminate these deficits in order to return these funds to a sound financial condition.

- (W) Certified Budget – Chapter 384.20 of the *Code of Iowa* states, in part, "Public monies may not be expended or encumbered except under an annual or continuing appropriation." Due to lack of financial records, the City was unable to monitor its expenditures compared to the adopted budget.

Recommendation – The City should ensure records are maintained in a manner which allows for comparison of disbursements to the adopted budget.

Exhibit

Report on Special Investigation of the
City of Armstrong

Summary of Findings
For the period July 1, 2015 through June 30, 2016

Description	Table / Page Number	Improper	Unsupported	Amount
Undeposited collections:				
Estimated utility collections	Table 1	\$ 88,600.00	-	88,600.00
Improper and unsupported disbursements:				
Payroll check to Kate Staton	Page 9	520.00	-	520.00
Paid time off	Page 10	416.00	-	416.00
Payments to individuals	Pages 10 and 11	2,633.45	-	2,633.45
Payments to vendors	Table 2	-	574.65	574.65
Late fees, penalties, and interest	Table 3	7,906.00	-	7,906.00
Subtotal of improper and unsupported disbursements		11,475.45	574.65	12,050.10
Total		\$ 100,075.45	574.65	100,650.10

Report on Special Investigation of the
City of Armstrong

Staff

This special investigation was performed by:

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Jennifer Campbell, CPA, Manager
Michelle B. Meyer, CPA, Manager
Ryan J. Pithan, CPA, Senior Auditor II
Kelly L. Hilton, Senior Auditor
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