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NEWS RELEASE

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FOR RELEASE _____ February 12, 2010 _____

Auditor of State David A. Vaudt today released a report on the City of Hills Fire Department, also known as Hills Fire Fighters (Department), for the period July 1, 2006 through September 30, 2009. The procedures were performed at the request of the Mayor and City Clerk as a result of concerns regarding the accounting for and reporting of Department financial information.

The City of Hills maintains a Fire Fighters account for the Department, from which it pays the Fire Chief's salary, insurance, fire truck lease and building expenses. The Department also maintains 3 checking accounts separate from the City account, as well as 2 certificates of deposit. The separate accounts are used for expenses not paid from the City's account. Vaudt reported the payments from these accounts are not approved by the City Council and the disbursements are not properly supported. The separate accounts were maintained by the Treasurer of the Department, who is a member of the Fire Department.

Vaudt reported the Department is a function of the City and all activity should be accounted for by the City. Disbursements from the separate fire accounts were to support the operations of the Fire Department and, as such, were obligations of the City which should have been subject to review and approval of the Council. In accordance with section 384.20 of the *Code of Iowa*, City funds should not be separately maintained and should be subject to Council review and the City's budget process. As a result, all collections should have been deposited to the City's General Fund.

Vaudt reported the review identified \$30,790.66 of unsupported disbursements, including \$25,222.12 from the Department's separately maintained accounts and \$5,568.54 from the Fire Fighters account administered by the City.

The unsupported disbursements include cash withdrawals/debit memos, payments to grocery and retail vendors and catering. Proper documentation for Department disbursements was not maintained by Department officials or by the City.

In addition, Vaudt reported the procedures identified \$13,728.64 of disbursements which may not meet the test of public purpose as defined by an Attorney General's opinion dated April 25, 1979. Of these disbursements, \$7,565.52 was for food and grocery purchases, \$3,663.07 was for pop, water and Gatorade, \$1,199.94 was for floral purchases and \$1,300.11 was for alcohol. Some of these purchases were for fundraisers and meals and parties for the volunteer firefighters.

The report also includes recommendations to strengthen the Department's internal controls, such as improvements to segregation of duties, controls over financial accounting records and maintaining adequate supporting documentation.

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 <http://auditor.iowa.gov/specials/index.html>.

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**REPORT ON SPECIAL INVESTIGATION
OF THE
CITY OF HILLS FIRE DEPARTMENT

FOR THE PERIOD
JANUARY 1, 2006 THROUGH SEPTEMBER 30, 2009**

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Auditor of State's Report

To the Honorable Mayor, Members
of the City Council and the Fire Chief:

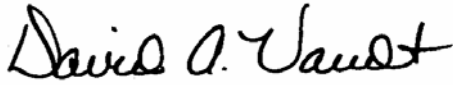
At the request of City officials, we conducted certain tests and procedures to selected financial transactions of the Hills Fire Department, also known as the Hills Fire Fighters, (Department) for the period July 1, 2006 through September 30, 2009, or as otherwise noted. Based on discussions with the Mayor, City Clerk, Department Treasurer and a review of relevant information, we performed the following procedures:

- (1) Evaluated the organization of the Department to determine whether it is a function of the City or a separate entity.
- (2) Evaluated internal controls for both the Department and the City to determine whether adequate policies and procedures were in place and operating effectively.
- (3) Examined all disbursements and available supporting documentation from the Department's separate bank accounts to determine if disbursements were for appropriate purposes and supported by adequate documentation.
- (4) Examined all disbursements and available supporting documentation from the Fire Fighters account maintained by the City to determine if disbursements were for appropriate purposes and were supported by adequate documentation for the period January 1, 2008 to September 30, 2009.
- (5) Evaluated the 28E agreement between the City of Hills, the Department and Townships to determine if payments received from the Townships were properly deposited in the City's Fire Fighters account.
- (6) Examined available receipts for collections received by the Department from donations and various fund-raising activities to determine if the collections were properly deposited into the Department's accounts.
- (7) Examined all payroll disbursements by the City to the former Fire Chief to determine if the appropriate number of payroll disbursements had been made, if the amounts paid were appropriate and to identify any improper or unsupported disbursements.


These procedures identified several internal control weakness. Our detailed findings and recommendations are presented in the Detailed Findings and Recommendations section of this report.

The procedures we performed 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 financial statements of the Department and the City of Hills, other matters might have come to our attention that would have been reported to you.

We would like to acknowledge the assistance and many courtesies extended to us by officials and staff of the Hills Fire Department and the City of Hills during the course of our review.



DAVID A. VAUDT, CPA
Auditor of State



WARREN G. JENKINS, CPA
Chief Deputy Auditor of State

January 7, 2010

City of Hills Fire Department

Detailed Findings and Recommendations

The City of Hills is located in Johnson County. The City maintains a Fire Fighters account for the Department from which it pays the Fire Chief's salary, insurance, fire truck lease and building expenses. The Department also maintains 3 separate checking accounts and has 2 certificates of deposit which are not maintained by the City. The separate accounts are maintained by the Treasurer of the Department and are used for expenses not paid from the City's Fire Fighters account. The Treasurer is a volunteer member of the Fire Department.

We reviewed the procedures used by the City and the Department to process receipts and disbursements. An important aspect of internal control is to establish procedures that 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 noted within a reasonable time during the course of normal operations. Based on our findings and operations detailed below, the following recommendations are made to strengthen the Department's and City's controls.

- (A) 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. The Treasurer for the Department had control over each of the following areas for the Department:
- 1) Receipts – collecting, depositing and posting,
 - 2) Disbursements – check preparation, signing and mailing/distribution,
 - 3) Investments – investing, recording and custody,
 - 4) Financial Reporting – receipt of the bank statements and preparation of the Department's monthly statements.

Because the City Clerk administers the Fire Fighters account, we reviewed the City's controls over this account. Based on our review, and as identified in the City's fiscal year 2006 financial audit, the City Clerk had control over each of the following areas:

- 1) Receipts – collecting, depositing and general accounting,
- 2) Disbursements – check preparation, signing, mailing/distribution, posting and general accounting,
- 3) Payroll – preparing, signing and mailing/distribution,
- 4) Investments – investing, recording and custody,
- 5) Financial Reporting – receipt of the bank statements, preparation of the bank reconciliations and preparation of the City's financial statements,
- 6) Accounting System – performing all general accounting functions and having custody of assets.

Recommendation – We realize segregation of duties is difficult with a limited number of staff. However, the Department and the City should review their control procedures to obtain the maximum internal control possible under the circumstances utilizing currently available personnel and elected officials.

- (B) Separately Maintained Accounts – As reported in the City’s fiscal year 2006 financial audit, the Department maintains 3 separate bank accounts: a checking account, a raffle account and an equipment and maintenance account. In addition, the Department had 2 certificates of deposit from donations received prior to fiscal year 2006. The City also maintains a separate Fire Fighters account for the Department. City officials requested we review the Department’s activity to determine if the City was responsible for the Department or if the Department is a separate entity.

The 28E agreement between the City of Hills, the Department and various townships served by the Department requires the “City of Hills to furnish fire protection and first responder protection by the Hills’ Fire Fighters Volunteer Fire Department and shall provide the necessary equipment and housing to furnish said fire protection and first responder protection.” As stated previously, the City pays the Fire Chief, insurance, fire truck lease and building expenses. The Hills Fire Fighter By-Laws set forth the structure and membership requirements for the Department. The by-laws provide for the appointment of officers by the Fire Chief who is elected by the members. We reviewed the Secretary of State’s web site and found no record of the Department being registered as a separate legal entity. Therefore, we determined the Department is part of the City.

As a result, the Department’s separate accounts would be considered public funds. Based on our review of the sources of the deposits made to the account, the funds in the Department’s separate accounts are public funds collected for a City purpose. The account is not held or currently administered by a City official. In addition, transactions and the resulting balances have not been reported to the Council and disbursements from the account are not reviewed or approved by Council.

Recommendation – Section 384.20 of the *Code of Iowa* states, in part, “A city shall keep accounts which show an accurate and detailed statement of all public funds collected, received, or expended for any city purpose.” All financial transactions of these accounts should be included in the City Clerk’s monthly financial reports.

Because public funds are held in the Department’s separately maintained accounts which are currently maintained by someone outside of City government, City officials should work with legal counsel to take the steps necessary to move the Department’s separately maintained accounts and certificates of deposit to the control of the City Clerk and/or another City official and to remove the names of non-city employees from the authorized check signers. The Department’s activity should be subject to City Council review and the City’s budget process.

In addition, internal control would be strengthened and operating efficiency could be increased by integrating the receipts and disbursements of these accounts with the City’s accounting records in the City Clerk’s office.

- (C) Public Purpose – Section 384.3 of the *Code of Iowa* states, in part, “All moneys received for city government purposes from taxes and other sources must be credited to the general fund of the city.” As previously stated, we determined the Department is a part of the City and, therefore, all monies received by the Department are subject to section 384.3 of the *Code of Iowa*.

During the course of our review, we identified \$13,728.64 of disbursements which may not meet the test of public purpose as defined in an Attorney General’s opinion dated April 25, 1979 since the public benefits to be derived have not been clearly documented. These disbursements include:

- \$7,565.52 of food and grocery purchases,

- \$1,300.11 of alcohol purchases,
- \$3,663.07 of pop, water and Gatorade purchases and
- \$1,199.94 of floral purchases.

Some of these purchases were for fundraisers and dinners or parties for the volunteer firefighters. According to the Attorney General's opinion, it is possible for these disbursements to meet the test of serving a public purpose under certain circumstances, although such items will certainly be subject to a deserved close scrutiny. The line to be drawn between a proper and an improper purpose is very thin. However, generally alcohol should not be purchased with City funds, unless the Council can document a public purpose served by the purchase of alcohol.

The disbursements identified were not approved by the City Council and the public purpose of the disbursements was not documented.

Recommendation – City officials should determine and document the public purpose served by these expenditures before authorizing any further payments from City accounts or the separate accounts. If these practices continue, City officials should establish written policies and procedures for documenting the public purpose served.

It is not unusual for local fire departments to establish legally separate auxiliary organizations which raise funds used to support the department. Proceeds raised by legally separate auxiliary organizations are typically from fundraisers and similar events. As a result, the proceeds are not considered public funds and may be maintained separate from the City's accounts. These funds may be used for purchases the City Council does not deem an appropriate use of City funds or for items which may not meet the test of public purpose.

- (D) Supporting Documentation – We identified \$30,790.66 of disbursements for which adequate supporting documentation was not maintained. Of this amount, \$25,222.12 was from the Department's separately maintained accounts and \$5,568.54 was from the Fire Fighters account administered by the City.

The \$25,222.12 of unsupported disbursements from the Department's separate accounts were made between July 1, 2006 and September 30, 2009. Based on the name of the vendor and/or notation in the memo portion of the checks, the unsupported disbursements were categorized as:

- \$7,570.15 to a caterer and grocery vendors,
- \$4,240.00 to non-profit organizations and memorials as donations, sponsorships or fund-raising activities,
- \$3,640.96 for equipment purchases, repairs and rentals,
- \$2,517.95 of cash withdrawals and debit memos,
- \$1,890.14 to retail vendors and a restaurant,
- \$1,549.17 for disbursements which appear to be related to training, certification or subscriptions to professional publications,
- \$1,445.24 for clothing and embroidery services,
- \$1,095.89 of reimbursements to volunteer fire fighters or family members,
- \$866.62 of miscellaneous disbursements and

- \$406.00 to other fire or rescue organizations.

The \$5,568.54 of unsupported disbursements from the City's Fire Fighters account were for made between January 1, 2008 and September 30, 2009. Based on the name of the vendor and/or notation in the memo portion of the checks, the unsupported disbursements were categorized as:

- \$2,568.61 for equipment purchases and repairs,
- \$1,458.34 for fuel purchases,
- \$570.00 for disbursements which appear to be related to training or professional publications,
- \$408.79 for utilities,
- \$387.80 to a caterer and convenience store and
- \$175.00 of reimbursements to volunteer fire fighters.

During our review, we also identified sales tax totaling \$676.29 which was paid on purchases made by the Department. The City is not required to pay sales tax.

Recommendation – The Department and the Council should implement policies requiring adequate supporting documentation be provided in order to determine the goods and services purchased and the related quantity. Disbursements should not be approved unless adequate supporting documentation is available. Disbursements should be approved by the Council prior to payment. In addition, all deposits should be properly supported.

The Department should implement procedures to ensure sales tax is not paid.

- (E) Undeposited Receipts – Deposits made to the Department's accounts should be supported by initial listings or prenumbered receipts.

We examined available supporting documentation for collections from donations and various fund-raising events and attempted to trace to deposits into the Department's bank accounts. Because of the lack of supporting documentation, we were unable to determine if \$1,323.38 in collections from donations and various fund-raisers were properly deposited. We did identify deposits which exceeded the amounts shown on available documentation.

Recommendation – The Department and the Council should implement policies requiring adequate supporting documentation, including prenumbered receipts, be maintained to reconcile the amounts collected to deposits to the bank account.

- (F) Financial Accounting Records – Very limited financial records were maintained by the Department for the period of our review. The following conditions were identified:

- 1) No ledger was maintained.
- 2) Receipts and disbursements were not posted.
- 3) Pre-numbered receipts were not issued for collections from donations and fund-raising activities.
- 4) Disbursements were not approved or documented in the minutes of City Council meetings.

- 5) Monthly bank account reconciliations were not completed and bank statements were delivered to and reviewed by an individual responsible for disbursing the Department's funds.
- 6) Financial reports detailing bank balances submitted at the monthly Department meetings were not supported by account records.

Recommendation – The Department should work with the City to determine the amount and extent of records which should be maintained on behalf of the City. Pre-numbered receipts should be used for collections. Since the Department is not a legally separate auxiliary organization, disbursements should be approved by the Council prior to payment and documented in the minutes. All checks should be prepared and signed by the City Clerk and reviewed and countersigned by the Mayor or a Council Member. The review should include comparing invoices and supporting documentation to the check. In addition, monthly bank to book reconciliations should be prepared by an independent person. Financial reports submitted at the monthly Department meeting should be supported by account records.

- (G) Social and Charitable Gambling License – As part of its fund-raising efforts, the Department conducts an annual raffle each fall. A total of \$6,000.00 in cash prizes is awarded at the annual raffle and the first place prize is \$3,000.00. The Department is not licensed with the Iowa Department of Inspections and Appeals. Chapter 99B.7 of the *Code of Iowa* requires organizations to obtain a social and charitable gambling license to conduct fund-raising activities or social gambling. The Department was not licensed for the 2006, 2007, 2008 or 2009 raffles.

Recommendation – The Department should ensure it obtains a qualified organization license from the Iowa Department of Inspections and Appeals prior to conducting any fund-raising activities or social gambling.

- (H) 1099 Forms – As previously stated, the Department conducts an annual raffle each fall and cash prizes are awarded. The Department is not filing a 1099 form with the Internal Revenue Service for those recipients receiving raffle winnings in excess of \$600.00.

Recommendation – The Department should ensure all recipients receiving raffle winnings in excess of \$600.00 receive a 1099 form as required by the Internal Revenue Service. Recipients should receive 1099 forms even if the raffle winnings are donated back to the Department.

- (I) Timely Deposits – As previously stated, the City and the Department have a 28E agreement with various townships to provide fire protection and first responder protection in exchange for bi-annual payments. Each township is responsible for making bi-annual payments on the first day of December and June of each fiscal year. The City is responsible for collecting payments from townships and depositing collections. During our review, we identified receipts received from the townships/districts which were not deposited timely.

Recommendation – The City should ensure all receipts are deposited timely.

We also reviewed the findings identified in the City's fiscal year 2006 financial audit report to determine if findings and recommendations were resolved. The following findings and recommendations were not resolved at the time of this report and the recommendations are repeated below.

- (J) Official Depositories – A resolution naming official depositories required by section 12B.10B of the *Code of Iowa* has not been adopted by the Council for the City.

Recommendation – The Council should adopt a resolution naming official depositories which complies with the provisions of section 12B.10B of the *Code of Iowa*.

- (K) Electronic Check Retention – Section 554D.114 of the *Code of Iowa* allows the City to retain cancelled checks in an electronic format and requires retention in this manner to include an image of both the front and back of each cancelled check. The City retains cancelled checks through electronic image, but does not obtain an image of the back of each cancelled check as required.

Recommendation – The City should obtain and retain an image of both the front and back of each cancelled check as required. If the Department creates a legally separate auxiliary organization, we also would recommend the Department obtain and retain an image of both the front and back of each cancelled check.

- (L) Signature Stamp – The City utilizes dual signatures; however, the City Clerk has access to the Mayor’s signature stamp.

Recommendation – The Mayor’s signature stamp should be under the control of an independent person if not under the control of the Mayor.

Report on Special Investigation of the
City of Hills Fire Department

Staff

This special investigation was performed by:

Annette K. Campbell, CPA, Director
James S. Cunningham, CPA, Senior Auditor II
James R. Wittenwyler, Staff Auditor
Lara K. Van Wyk, Assistant Auditor



Tamera S. Kusian, CPA
Deputy Auditor of State