

Office of Administrative Services

Inspection Report
Treasury Cash Count
November 5, 2012



**Office of the Public Auditor
State of Yap**



OFFICE OF THE STATE PUBLIC AUDITOR

YAP STATE GOVERNMENT

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EXECUTIVE SUMMARY

This report presents the results of our unannounced cash count conducted on November 5, 2012 and inspection of the controls and procedures for cashing activities of the Treasury function in the Office of Administrative Services (OAS).

The purpose of our inspection was to verify the accuracy of Treasury's change and petty cash funds and the amount of undeposited receipts, evaluate the controls over the safekeeping of these funds, and review the monitoring of cashing activities and the cash fund policies and procedures.

Our cash count disclosed immaterial variances in the amount of coin and currency on hand compared to the recorded amounts, and these have been discussed with management. Our inspection disclosed a deficiency in connection with the review and monitoring of cashing activity which we consider to be a material weakness in internal control. There is no monitoring of the activity of payments made to Treasury from departments and agencies that collect revenue and, therefore, no assurance this is being done in accordance with public law. We noted unexplained lapses in turning in funds to Treasury by at least one department, with no evidence of follow up by Treasury or OAS.

We identified certain other deficiencies in internal control that we consider significant. These include deficiencies over the custody and control of cash funds, safeguarding of cash, cash counts, and the policies and procedures for Treasury.

A draft copy of this report was circulated to the Director of OAS, who has declined to provide an official response.



Patrick J. Zacchini, CPA

Acting Public Auditor

November 5, 2012



Pacific Association of Supreme Audit Institutions (PASAI)



Association of Pacific Island Public Auditors (APIPA)

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INTRODUCTION

Background

The Treasury function is part of the Division of Finance and Treasury of the Office of Administrative Services (OAS). OAS is composed of the divisions of Finance and Treasury, Personnel, Property Management, and Revenue and Taxation. Under Yap State Code (YSC) Title 13 §1231 “public money raised or received by the State of Yap,” from whatever source, must be deposited in the Treasury. Additionally, Financial Management Act (FMA) Section 104 provides that “all funds received by any Yap State Government Agency” be turned over to the State Treasurer “each and every business day.” The funds turned in to Treasury must be deposited promptly into an approved depository account. Under §1231, the Director of Administrative Services is responsible for ensuring that public money is timely turned in to Treasury, and for follow up with agencies which are delinquent.

The principal function of Treasury is to receive payments on collections of revenue. Payments are received both from individuals and organizations directly or from departments and agencies which maintain their own cash receipt functions. Various departments and agencies make collections for fees and services, which include payment for such items as permits, licenses and registrations, equipment rental, fines, court costs, transportation, airport departure fees, and so forth. These collections are in turn deposited with Treasury.

A change drawer fund of \$100, used to make change readily available for those submitting payments, is maintained by Treasury. Treasury is responsible for reconciling their funds and preparing cash reports. Treasury also maintains the government-wide petty cash fund in the amount of \$300. Departments and agencies may receive imprest funds up to \$25 each. These funds are replenished as needed by departments and agencies through the submission of vouchers and other documentation supporting their expenditures.

Objectives

The purpose of our inspection was to conduct an unannounced count of the cash funds maintained by Treasury and perform the following:

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- Verify the accuracy of Treasury's change and petty cash funds, and the amount of undeposited receipts.
- Evaluate the controls over the safekeeping of these funds.
- Review Treasury's cashiering and cash fund policies and procedures.

Scope

Our inspection included the cashiering activities and the custody and control of cash funds maintained by the Treasury function of the OAS.

Methodology

In conducting our cash count and inspection, we determined through physical inspection the amount of all currency and coin on hand and reconciled these amounts to supporting documentation. We also reviewed procedures over the custody and control of cash funds, overnight safekeeping of cash, observation of cashiering activities, and the tallying of undeposited receipts and preparation for the deposit of those receipts. Our cash count was conducted in accordance with the Quality Standards for Inspections and Evaluations issued by the Council of Inspectors General on Integrity and Efficiency (CIGIE) and pursuant to the authority vested in the Public Auditor as codified under Title 13, Chapter 7, and § 703 of the Yap State Code, which states in part:

"The Public Auditor shall inspect and audit all accounts, books, and other financial records of the State Government, to include but not limited to, every branch, department, office, political subdivision, board, commission and agency, and other public legal entities or non-profit organizations receiving public funds from the State Government, and to prepare written reports of such inspections and audits for presentation to the Governor and the Legislature;"

Additionally, we evaluated the Treasury policies and procedures for the purpose of identifying any internal control deficiencies or weaknesses. A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal

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course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a 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 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.

Our consideration of internal control over Treasury cash funds and cashiering was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over cash that might be deficiencies, significant deficiencies or material weaknesses.

Prior Audit Coverage

To the best of our knowledge there has not been a recent cash count of Treasury performed by this office.

Conclusion

Our cash count disclosed variances in the amount of coin and currency on hand compared to the recorded amounts. The variances, which were discussed with management, were immaterial in amount. However, we did identify as a deficiency in internal control over cash the failure to properly review and monitor cashiering activity which we consider to be a material weakness, as defined above. This material deficiency, along with certain other deficiencies we identified in internal control over the custody and control of cash funds, safeguarding of cash, cash counts, and the policies and procedures for Treasury, is described in the accompanying pages.

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FINDINGS AND RECOMMENDATIONS

Review and Monitoring of Cashiering Activity

There is no monitoring of the payment activity in to Treasury of departments and agencies who make collections of revenue. These departments and agencies maintain their own cash receipt functions, some of which only periodically or infrequently transfer those funds to Treasury.

For example, we noted no deposits with Treasury by the State Court in fiscal years 2008, 2010, and 2011, only one transfer in 2009, and three in 2007. Presently, payments from the State Court are turned in to Treasury every week, but there is nothing reflected in 2012 prior to July 30. The failure to properly monitor the activity of these payments could result in fraud that may go undetected or not be timely detected.

Financial Management Act (FMA) Section 104 provides that “all funds received by any Yap State Government Agency” be turned over to the State Treasurer “each and every business day.” Yap State Code (YSC) Title 13, §1231 stipulates that the Director of Administrative Services is responsible for ensuring that “internal revenue” is timely turned in to Treasury, and should “provide checks on agencies which may be delinquent in transmittal.”

Recommendation

To reduce the likelihood of misappropriation of assets, ensure that payment activity in Treasury by departments and agencies is periodically reviewed and:

- Any significant lapses in time should be followed up and explanations obtained for inconsistencies in activity.
- The performance of this monitoring procedure should be subject to supervisory review.
- Both the monitoring procedure and its supervisory review should be properly documented.

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Additionally, to ensure compliance with public law, reemphasize to all departments and agencies engaged in collections of fines, fees, and other State revenues that they are required to daily submit their collections to Treasury.

Combination Safe

During our inspection of the security of cash and undeposited receipts, we noted that combinations to the safe, which is used to secure the change and petty cash funds, are not periodically changed. To the best of our knowledge, the combination of the safe has never been changed; notwithstanding there have been changes in OAS personnel who had access to this information.

Additionally, one or more backup keys are maintained by the same persons who have access to the combination. Backup keys are intended to provide emergency access in case the combination is lost.

Recommendation

To reduce the risk of loss arising from tampering, the combination to the safe should be periodically changed, especially when there are changes in personnel. Additionally, the backup key(s) should be secured in an offsite location, such as a safe deposit box, and by persons who do not regularly have access to the safe. It would also be a good idea to have the safe serviced at least once a year to ensure it is operating correctly.

Custody and Control of Cash

The custody and control over change and petty cash funds could be improved. At the end of each day, Treasury counts the cash on hand and proves out the cash receipts for the day to the system. Treasury also counts the cash at the beginning of each day. However, this is not documented.

Presently, there is only one individual in Treasury. This person accepts cash and checks for receipt, records the cash receipt in the system, processes void transactions, has custody of cash

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receipts and change funds, and prepares the deposit. We understand several individuals have been cross-trained to serve as backups in the event of illness or other conditions that would necessitate a replacement. However, at any one time, only person is working in Treasury.

We also noted the following:

- Although a second person verifies the deposit of funds by comparison with the total of undeposited receipts (printed copies of the receipt given to each person who presents cash to Treasury) before submission to the bank, this verification is performed based on a manually prepared summary prepared by the Treasury give official, and not a system generated report of cash receipts. The total of undeposited receipts consists of the currency, coin, and checks on hand and the printed cash receipt vouchers, a copy of which is given to those who turn in funds to Treasury to evidence their remittance.
- Checks received by Treasury are not immediately restrictively endorsed. This type of endorsement of checks is a control technique to restrict further action in regard to a financial instrument so that it is no longer a negotiable instrument that can be passed along to a third party.
- There is a general lack of adequate supervision of Treasury operations. We noted two checks from 2005 secured in the safe along with the cash from the change and petty cash funds. The checks are drawn on the Bank of Hawaii and payable to Yap State Government, though the amounts are not material. However, their presence in the safe raises some serious questions about the level of supervisory review. Notwithstanding the checks are stale dated and it is very unlikely a reputable financial institution would honor their payment, such items are particularly susceptible to fraud.

Recommendation

To reduce the risk of error and ensure adequate custody and control over cash and the recording of receipts, ensure the following:

- All cash counts and proofs are documented.
- Checks are immediately restrictively endorsed to reduce the likelihood of misappropriation.

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- Voided cash receipts are approved by a supervisor. Consider establishing an additional layer of security in the system that would require a supervisory override in order to void cash transaction.
- The verification of the deposit amount is based on a system generated report.
- Adequate supervisory review over the daily proof and verification of receipts for deposit.

Policies and Procedures

Presently, formal written policies and procedures have not been established for Treasury. Committing policies and procedures to writing assists in communicating objectives, goals, and management philosophies, and provides a framework for decision-making. It also provides employees with guidelines in the exercise of their functions and ensures standardization and consistency of application.

Recommendation

Develop a manual of operations for Treasury. This should address key issues confronting the section and include, among other things, guidelines for the handling of exceptions, areas of responsibility, supervision, document flow and control, etc. Many companies have also found it useful to develop written desk procedures, which detail specific actions and define precise activities within the Treasury area.

Cash Counts

Observation

Surprise cash counts of Treasury are not performed by OAS.

Recommendation

Surprise inspections and counts are critical to effective internal control of cash. It reduces the

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risk of both innocent errors and deliberate inappropriate actions. Failure to periodically verify the amounts of cash on hand could result in misappropriation of assets or errors that go undetected or are not timely detected. Moreover, lacking the self-checking nature of surprise cash counts, the likelihood of errors and misstatements are increased.

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The Director of OAS has declined to provide an official response.