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From:         Robert B. Wasserbach  
Subject:      Review of Monthly Bank Reconciliations  
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## **BACKGROUND**

In November 2010, we were asked by a County Council Member to evaluate the internal controls over the monthly bank reconciliations of the Register of Wills' (ROW) checking account, as an aid to the newly elected Register of Wills. We reviewed the bank reconciliations for the period July through November 2010. We believe the internal controls over the bank reconciliations are adequate; however, because our testing was limited to a short timeframe, we are not expressing a formal audit opinion on the internal controls. Our testing did reveal certain areas where the bank reconciliation could be improved and the internal controls strengthened.

While reviewing the bank reconciliations, we also analyzed the internal controls over cash receipts and cash disbursements.

## **COMMENTS AND RECOMMENDATIONS**

### **Electronic Bank Reconciliation**

The ROW office does both electronic and hand-prepared bank reconciliations. This comment deals with the electronic bank reconciliation (reconciliation). Each month, a reconciliation is generated in the ROW System. The preparer of the reconciliation puts in the system the ending balance from the bank statement and the "as of date", and the system generates the reconciliation.

There is an issue with the automatically calculated escrow amounts (at least with the newspapers). We observed that the amounts due to the different newspapers are automatically calculated by the system, based on the information from the different estates. These calculated amounts are used by the system to determine the checks due to the three different newspapers utilized.

This automatic calculation causes problems when the amount billed by the newspaper does not equal the amount calculated by the system. As a result, the Account Clerk III will enter a “dummy” check number (usually the check number followed by an A) with the incorrect amount calculated by the system. The Account Clerk III then adds a “dummy” deposit to equal the incorrect amount calculated by the system, thus zeroing out the incorrect amount and having the correct amount stay in the reconciliation. The ROW office informed us that the system does not allow them to validate the amounts before they are calculated. As a result, the reconciliation has to be manipulated and, although the dollar amounts are not high, this opportunity to manipulate the reconciliation by entering “dummy” checks and deposits could lead to irregularities.

Please note that we observed this situation with newspaper payments, but it could also apply to other vendor payments.

We recommend that the ROW office discuss with Information Systems the best means to utilize the system so that “dummy” check numbers and deposits do not have to be created.

### Segregation of Incompatible Duties

With the election of a new Register of Wills and the filling of job vacancies within the ROW office, we believe there is an opportunity to strengthen internal controls. Below are the suggested internal controls for Cash Receipts, Cash Disbursements and the Bank Reconciliation.

An “incompatible” duty is one that would put a single individual in the position of being both able to commit an irregularity<sup>1</sup> and then to conceal it. Accordingly, such incompatible duties should be segregated. In practice, three types of functions are commonly considered to be incompatible: authorization, recordkeeping, and custody of assets. Thus, regarding the ROW office, the following duties surrounding cash<sup>2</sup> should theoretically be segregated. As the cost of internal controls should not exceed the benefit to be derived, it may not be practical in some instances to segregate incompatible duties

#### **Cash Receipts**

The following duties should ideally be segregated: (1) the receipt of cash, (2) the recording of cash receipts in the ROW’s accounting records, (3) the preparation and making of the daily deposit, and (4) the performance of the bank reconciliation.

Please note that, although we are concerned with both checks and currency/coins, there is more susceptibility of an irregularity occurring with currency/coins. Our review of a ROW System report indicated that approximately \$128,000 in currency/coins was received for Calendar Year 2010.

Currently, all three persons in the Accounting area have the ability to initiate a charge (a charge must be created before cash is accepted), receive cash, and record the cash receipt in the ROW System. Also, one of these persons prepares the daily bank deposit and prepares the manual monthly bank reconciliation. (The Chief Deputy generates the automated monthly bank reconciliation.)

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<sup>1</sup> Please note that we do not have any reason to believe that there have been any irregularities in this office.

<sup>2</sup> Please note that we use the term “cash” to denote checks, currency, and coins.

Since the Office does not appear to have the manpower to segregate all of these functions, we have the following recommendations:

- It is our understanding that the majority of the checks received are a result of the client meeting with one of the deputies (e.g., to open the estate, receive the Inventory, close the estate), and that the deputy creates the charge and walks the client to the Accounting area to make the payment. The check is restrictively endorsed by the Accounting area. To alleviate the possibility of irregularities with checks received, we recommend that management consider having the deputies restrictively endorse the checks rather than Accounting.
- We recommend that management consider having someone independent of the Accounting area prepare the daily bank deposit.
- We recommend that someone independent of the Accounting area prepare the manual monthly bank reconciliation.

## **Cash Disbursements**

The following duties should ideally be segregated: (1) the preparation of the check and associated documentation, (2) the reviewing, signing, and mailing of the check, and (3) the performance of the bank reconciliation. Also, the person(s) having control over access to the blank check stock should be independent of the Accounting function.

The way the cash disbursement process currently works is as follows:

- The Account Clerk III in the Accounting area prepares the checks. Other people in Accounting as well as the Register of Wills, the Chief Deputy, and the Operations Manager also have the ability to generate vendor checks; however, only the Account Clerk III, the Register of Wills, and the Chief Deputy have the ability to issue refund checks (checks issued from individual estates where there has been an overpayment of fees). We believe the bigger risk lies with refund checks.
- The Chief Deputy or Operations Manager reviews and signs the checks. If the check is for a client refund, there is a special form which the Chief Deputy is required to sign prior to the issuance of the check.
- **Who actually mails/delivers the checks?**
- The Chief Deputy generates the automated bank reconciliation (but does not prepare the manual one).
- **Who controls the blank check stock?**

We recommend that management consider segregating the duties of signing checks and performing/reviewing the monthly bank reconciliations.

## **Bank Reconciliation**

The person performing the reconciliation and the person reviewing the reconciliation should be independent of the cash receipts and cash disbursement functions. We have already addressed our recommendations concerning the bank reconciliations.

## Voided Transactions

An analysis of the Voided Transaction Report for Fiscal Year 2011 (approximately through the end of March) revealed that there have been 676 voided transactions since July 1, 2010. This equates to about 4 voided transactions per working day, ranging from a transaction for \$17,339.93 to a transaction for (\$15,260.10). Most of these transactions did not include a description as to why the transaction was being voided. Also, although many of these transactions were voided within the same day, some of the voided transactions were

for transactions that took place in prior fiscal years. One such example is for a transaction that took place in Fiscal Year 2006. The absolute value of all these voided transactions is \$182,398.

From reviewing the system access levels, it appears that all people who can post charges and/or post client payments are also able to void that same transaction. Although we do not suspect that someone would void a cash payment and then misappropriate the cash, we suggest that there be some safeguards placed within the system, similar to what takes place with a cash register. One such safeguard would be limiting the amount that an individual can void. If the amount to be voided is above this management-determined threshold, then a supervisor would have to void the transaction instead. If, for example, this management-determined amount was \$25, then there would have been approximately 180 transactions thus far in Fiscal Year 2011 that would have had to be authorized by a supervisor.

Management could also consider restricting the ability to do a void if a management-determined number of days have passed since the original transaction.

We have spoken to Information Systems who told us that the system could be modified to put restrictions on voids.

We recommend the following:

- Management periodically review, and evaluate the reasons for, voided transactions.
- Management instruct staff to document in the system the reason for the voided transaction (for a proper audit trail).
- As discussed above, management consider putting restrictions on one's ability to void a transaction, and having a supervisor review the transaction if the transaction meets the restriction criteria.

#### Automated System

In the brief time we spent in the ROW office, we observed that there are some functions performed manually which Information Systems informed us could be done by the automated system (e.g., manual ledger sheets, manual bank reconciliation, checks prepared on typewriters, calculation of funds due to County). We do not know all the particulars behind why these functions are done manually; however, ROW management did inform us that there are several areas where the system does not work as anticipated and that they need to work out these issues with IS. Management informed us that they have not been able to do so the last few years due to staff vacancies.

We encourage management to meet with IS to discuss ways the system can be utilized for items which are currently handled manually.