

**LOWER MACUNGIE TOWNSHIP
INTERNAL CONTROL STRUCTURE EVALUATION**

March 25, 2009

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Mr Bruce Fosselman
Township Manager
Lower Macungie Township
3400 Brookside Road
Macungie, PA 18062

Dear Mr. Fosselman:

Pursuant to your request, and in accordance with our engagement arrangements, we have completed our engagement to assist with Lower Macungie Township's ("Lower Macungie" or the "Township") financial and internal control policies and procedures. The overall objective of this project was to review and evaluate the township's internal control structure with particular emphasis on strengthening internal controls and increasing segregation of duties.

The accompanying report describes the project objectives, the project scope and approach and our observations and recommendations. We appreciate this opportunity to be of service to you. If you have any questions regarding our report or require any additional information pertaining to the evaluation, please do not hesitate to contact us.

Sincerely yours,

REINSEL KUNTZ LESHER LLP

Gretchen G. Naso, MBA, AVA

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EXECUTIVE SUMMARY

Project Objective

In May of 2008, the Board of Commissioners of Lower Macungie Township engaged Reinsel Kuntz Leshar LLP to conduct an internal control structure review and evaluation. The overall objective of this project was to review and evaluate the Township's internal control structure with particular emphasis on strengthening internal controls and increasing segregation of duties.

Scope and Approach

Our major project worksteps included the following:

1. We completed "walk-through" of the Township's major financial functions; to include revenue (earned income taxes and real estate transfer taxes, sewer and water receipts, licenses and permits, grants and interest), purchases and accounts payable (computer-generated and manual), treasury (cash and short-term investments), capital assets, payroll and financial reporting.
2. We reviewed internally developed written procedures for each of the Township's major financial functions listed above.
3. We obtained detailed job task information from key departmental employees to evaluate lines of authority, reporting relationships, department staffing, workflow and staffing needs. We observed daily departmental activities and workflow and conducted personal interviews with key managers and support staff.
4. We documented and assessed existing internal control policies and procedures for each of the financial functions listed above.
5. We developed written recommendations for improvements to existing internal control policies and procedures for each financial function based on our understanding of existing deficiencies and our knowledge of industry best practices.

Recommendations & Observations

Our report provides general organizational recommendations, specific recommendations and suggested best practices to improve the Township's internal controls and achieve greater segregation of duties for each of the Township's major financial functions.

INTERNAL CONTROLS-AN OVERVIEW

Overview

An effective system of internal controls is a coordinated set of policies and procedures established by management to achieve objectives and meet responsibilities. An effective internal control framework should accomplish the following:

1. **Provide a favorable control environment.** A favorable control environment is one on which (a) management is knowledgeable about internal controls, (b) management is committed to establishing and maintaining controls, and (c) management communicates its support for internal controls to staff at all levels.
2. **Continually assess risk.** A variety of risks may hamper or prevent management from fulfilling its responsibilities and achieving its goals. Some of these risks can arise from internal factors, while others can originate from outside the organization. When management is able to anticipate such risks, it is better prepared to manage them. Accordingly, an effective system of internal controls must provide for the ongoing identification and assessment of potential risks.
3. **Establish and maintain effective policies and procedures.** Specific policies and procedures should be developed as tools for achieving internal control. In some cases, policies and procedures may be adequate to prevent undesired actions and events. In other instances, the goal of policies and procedures is to alert management of undesired actions and events in time to take corrective action.
4. **Effectively communicates information.** The reliability, selection, timeliness and accessibility of information are crucial factors to an organization's decision-makers. An effective system of internal controls will ensure that reliable information is provided to the appropriate individuals on a timely basis.
5. **Monitors the effectiveness of control policies and procedures and the resolution of potential problems.** Once appropriate controls are in place, management must ensure that the controls continue to function properly on an ongoing basis. Management must also monitor the effectiveness of its own response to potential problems identified by those controls.

The characteristics of effective internal control system include the following:

1. Staff members are adequately trained and supervised.
2. Provides reasonable assurance that transactions are executed as authorized; this requires independent evidence that transactions are executed as authorized, and that authorizations are issued by persons acting within the scope of their authority.
3. Ensures that transactions are recorded at the amounts and in the accounting periods in which they were executed and classified in the appropriate accounts.
4. Access to assets is limited to authorized personnel.
5. Recorded balances of assets are confirmed by someone other than the person responsible for recording and reporting of the balances.

Internal controls are essentially management techniques and are an inextricable part of how management operates. Accordingly, management is primarily responsible for the effectiveness of internal controls. Management's performance is subject to oversight by an entity's governing board. Therefore, while management is primarily responsible for internal controls, the governing board is ultimately responsible for ensuring that management fulfills this duty.

Segregation of Duties

The concept of segregation of duties is a basic, key element of an organization's overall internal control system. At the most basic level, segregation of duties prohibits a single individual from having control over two or more phases of a transaction or operation. Segregation of duties help to prevent a deliberate fraud because it would require collusion of two or more persons and it increases the likelihood that innocent errors will be found. If a single person can carry out and conceal errors and/or irregularities in the course of performing their day-to-day activities they have generally been assigned or allowed access to incompatible duties or responsibilities. The four general categories of duties or responsibilities that should be segregated are as follows:

- Authorization;
- Custody;
- Record keeping; and
- Reconciliation.

In an ideal system, different employees would perform each of these four major functions. In other words, no one person should have control of two or more of these responsibilities. The more negotiable the asset, the greater the need for proper segregation of duties - especially when dealing with cash, negotiable checks and inventories.

In those instances where duties cannot be fully segregated, mitigating or compensating controls should be established. Mitigating or compensating controls are additional procedures designed to reduce the risk of errors or irregularities. For instance, if the record keeper also performs a reconciliation process a detailed review of the reconciliation could be performed and documented by a supervisor to provide additional control over the assignment of incompatible functions.

Policies and Procedures

Every entity should document its accounting policies and procedures in the form of an accounting policies and procedures manual. Management should emphasize their importance and authority to all staff members and formally evaluate/update the policies and procedures annually. Changes in policies and procedures that occur between these periodic reviews should be updated in the documentation promptly as they occur. A specific employee should be assigned the duty of overseeing this process. Management is responsible for ensuring that this duty is performed consistently.

Accounting policies and procedures should be readily available to all employees who need it. It should delineate the authority and responsibility of all employees, especially the authority to authorize transactions and the responsibility for the safekeeping of assets and records. Likewise, the Accounting policies and procedures should indicate which employees are to perform which procedures. Procedures should be described as they are actually intended to be performed rather than in some idealized form. Also, accounting policies and procedures should explain the design and purpose of control-related procedures to increase employee understanding of and support for controls.

ORGANIZATIONAL STRUCTURE

General

Lower Macungie's Township Manager, Bruce Fosselman, leads the Township's management team. He has direct responsibility for the overall administration and operation of the Township. The Director of Finance and the Director of Public Works report directly to Mr. Fosselman.

The Organizational Chart provided to Reinsel Kuntz Leshar LLP was outdated and incorrect. Moreover, based on this chart and our review procedures, it appears as though some staff members are assigned job titles that are not reflective of their actual responsibilities and position in the Township. For instance, four staff members whose job responsibilities are related to accounting and finance are listed on the Organizational Chart as Receptionist/General Office. The staff member who sits at the receptionist area and who answers incoming phone calls is listed on the Organizational Chart as the Sewer/Solid Waste Billing Clerk.

Additionally, there is a lack of adequate segregation of duties in some functions at Lower Macungie Township. This has been identified as a critical issue for the Township and its management team. And, as discussed above, segregation of duties goes hand-in-hand with an effective system of internal controls. Therefore, to improve internal controls and achieve greater segregation of duties, we recommend that the Board of Commissioners consider a number of changes in the Township's organizational chart. Our specific recommendations follow.

Finance

Based on her position description, the Director of Finance, Cassandra Williams, has overall responsibility for directing all aspects of the Township's fiscal management program, including maintaining all accounting and internal control systems, budgets and strategic planning processes and policies and procedures. She is also responsible for effective delegation, supervision, monitoring and oversight and review. She oversees and directs the "Financial Staff" that is comprised of the following individuals:

- Office Administrator – L. Baatz
- EIT Officer – K. O'Brien
- Administrative Assistant – P. Galiardo
- Administrative Assistant – K. Paey
- Administrative Assistant – M. McKitritch
- Receptionist – K. Molnar
- Administrative Assistant – D. Fowler
- Accounts Payable – S. Panarelli
- Contracts – L. Lichtenwaner
- Recreational Programs – D. Foulke, C. Hausmann
- Sewer/Solid Waste Billing Clerk – G. Pearl

We recommend that the Board of Commissioners consider reorganizing this "Financial Staff" and creating an Accounting/Finance Group led by the Director of Finance. Job responsibilities should be reassigned to achieve segregation of duties.

Specifically, “best practices” dictate the following segregation of duties:

1. Responsibility for opening mail and listing remittances should be segregated from those for recording receipts and posting to the general ledger.
2. Responsibility for preparing deposits should be segregated from those for opening mail.
3. Responsibility for cash receipts functions should be adequately segregated from those for cash disbursements.
4. Responsibility for entries in the cash receipt and disbursement records should be adequately segregated from those for general ledger entries.
5. Responsibility for preparing and approving bank account reconciliations should be adequately segregated from those for other cash receipt or disbursement functions.
6. Responsibility for preparation of invoices should be segregated from those for recording cash receipts.
7. Responsibilities for disbursement preparation, approval, recording and purchasing functions should be separated.
8. Responsibilities for processing bills should be adequately segregated from those for customer account maintenance and adjustments.

The following table presents a recommended reassignment of job responsibilities that would increase segregation of duties and improve internal controls:

<p>Director of Finance Budget Preparation Forecasting Investment Management Financial Reporting Issues</p>		
<p>“Accounting Supervisor” Bank Reconciliation General Ledger Reconciliation Monthly Close Financial Statement Preparation</p>		
<p>“Accounting Assistant #1” Accounts Payable Payroll Other Functions <i>(as determined by the Director of Finance)</i></p>	<p>“Accounting Assistant #2” Cash Receipts Utility Billings¹ Other Functions <i>(as determined by the Director of Finance)</i></p>	<p>“Accounting Assistant #3” Capital Assets Accounts Receivable Other Functions <i>(as determined by the Director of Finance)</i></p>

¹**Note:** Cash receipts functions should generally be segregated from billing functions. However, as long as utility receipts are handled via a lockbox, adequate segregation of duties is achieved.

Staff members should be assigned job titles and provided with written position descriptions that are reflective of their revised responsibilities and functions within the group.

We also recommend that the Board of Commissioners consider creating a new position to function between the Director of Finance and the accounting staff. This "Accounting Supervisor" would be responsible for the daily operations of the Accounting/Finance Group in support of the Director of Finance. Specific responsibilities could include developing and maintaining complex accounting records and account analyses, summarizing transactions, compiling reports, performing closings, preparing reconciliations and other schedules, reviewing work prepared by the Finance/Accounting staff and resolving accounting discrepancies.

The above changes would not only improve internal controls and provide opportunities to increase segregation of duties, but would also allow the Director of Finance the opportunity to evolve in her position as the Director of Finance.

REVENUE

Earned Income Tax Revenue

In July 2008 Pennsylvania Governor, Edward G. Rendell, signed legislation that mandates a major consolidation of earned income tax collection in Pennsylvania and creates county-specific "tax collection committees". Pennsylvania's number of Earned Income Tax (EIT) collectors will be reduced from 560 to 69. The legislation, which will be phased in starting in 2010, will reduce the loss of tax revenue for municipalities and school districts through standardized collection practices, coordination, reporting and accountability among and between jurisdictions and collectors.

Currently, the Township's Tax Collector, EIT Officer and two Administrative Assistants currently handle most of the bookkeeping and accounting work associated with the tax collection function. We recommend that the Board of Commissioners consider outsourcing these functions to an independent third party who would assume responsibility for all aspects of the tax assessment; collection and reporting cycles during the two-year period before the above legislation become effective. Given the complexity of tax collection, we believe that the use of an independent third party would be a cost effective option for the Township and would ease the transition to a county-wide system.

We noted several instances of internal control weaknesses in the Township's current policies and procedures related to tax assessment, collection and reporting. Specifically, we noted a lack of segregation of duties and inadequate reconciliation and review procedures. Such internal control weaknesses could result in the following:

- Cash receipts recorded, but not deposited;
- Cash receipts amount recorded incorrectly;
- Incomplete tax rolls;
- Appropriate penalties not assessed;
- Appropriate collection techniques not followed for delinquencies;
- Cash receipts not recorded or deposited;
- Cash receipts deposited, but not recorded;
- Cash receipts credited to wrong account;
- Cash receipts credited to wrong period;
- Taxes recognized as revenue in financial statements before date due;
- Taxes recognized as revenue in governmental funds before they are available to finance liabilities of the current period (not to exceed 60 days);

In the event that the Board of Commissioners elect to maintain the tax function "in-house", we recommend that the following "best practices" be incorporated into the Township's policies and procedures:

1. **Authorization and Approval.** Changes to tax rolls, tax calculations and exemptions should be approved.
2. **Security of Assets and Records.** A lockbox should be used for all tax payments. Appropriate collection techniques should be followed for delinquent accounts.

3. **Segregation of Incompatible Duties.** Segregation of 1) the handling and listing of cash receipts, 2) the posting to the general ledger, 3) the maintenance of the cash receipts book, and 4) the making of deposits. Additionally, incoming cash items should be listed and subsequently reconciled to deposits by an individual independent of recording the cash receipts. Overdue accounts receivable balances should be investigated and collected. An individual independent of the billings and taxes receivable functions should be responsible for investigating complaints from taxpayers. Finally, an individual independent of the billings and taxes receivable functions should be responsible for performing monthly reviews of the bank reconciliations.
4. **Periodic Reconciliations.** Bank reconciliations should be prepared on a monthly basis by an individual independent of the billings and taxes receivable function. The reconciliation process should include a comparison of the control account in general ledger with balances in subsidiary ledger.

Charges for Services

We noted several instances of internal control weaknesses in the Township's current policies and procedures related to the billing and collection of revenue. We noted a lack of segregation of duties and inadequate reconciliation and review procedures. Such internal control weaknesses could result in the following:

- Billings to wrong party or for incorrect account;
- Billings recorded incorrectly;
- Services or facilities provided to poor credit risk;
- Cash receipts recorded, but not deposited;
- Cash receipts amounts recorded incorrectly;
- Services or facilities provided, but not billed;
- Cash receipts not recorded or deposited;
- Cash receipts deposited, but not recorded;
- Billings for services or facilities not provided;
- Cash receipts credited to wrong fund or account;
- Cash receipts credited to wrong period; and
- Receivable not presented net of allowance for doubtful accounts.

We recommend that the following "best practices" be incorporated into the Township's policies and procedures to ensure that the authorization to provide services or facilities is reflected in the accounting records, all receipts are recorded accurately and deposited and allocated to the correct account in the correct period, and properly allocated to the correct account in the correct period, and properly applied.

1. **Prior Authorization and Approval.** All documents and lease agreements should be approved before execution.
2. **Properly Designed Records.** Documents, lease agreements, etc., should be required before providing services or facilities.
3. **Security of Assets.** Credit references should be checked before providing services or leasing facilities. Security deposits should be required for new utility customers. Cutoff procedures should be in place for delinquent utility customers. For payments made in person, pre-numbered receipts should be used to record payment.

4. **Segregation of Incompatible Duties.** Billings should be recorded by someone independent of invoice preparation. The duties of (1) handling and listing cash receipts, (2) posting to receivables subsidiary ledger and the general ledger, (3) maintaining the cash receipts book, and (4) making deposits should be segregated. Additionally, incoming cash items should be listed for subsequent reconciliations to deposits by someone independent of recording cash receipts. Bank reconciliations should be independently reviewed and approved. An independent investigation and follow-up of overdue receivable balances should be performed. And, an individual independent of the billings and receivables functions should investigate and document all complaints.
5. **Periodic Reconciliations.** Bank reconciliations should be prepared on a monthly basis and independently reviewed and reconciled. Additionally, a monthly reconciliation of the control account in the general ledger with the related account balances in the subsidiary ledger should be performed. A monthly reconciliation of the subsidiary ledger with the related account balances maintained by Lehigh County Authority should be performed.
6. **Periodic Verification.** Billing rates and leasing terms should be verified for accuracy and billings should be based on appropriate use/service documentation.
7. **Analytical Review.** The reasonableness of billings should be assessed by investigating variances from estimated amounts and the amount billed to customers should be compared to the amount of services provided.

We also have the following recommendations to improve the overall efficiency of procedures related to Charges for Services.

1. **Deposits for Community Center.** Township residents who wish to lease the Community Center are required to submit a \$ 100 or \$ 200 security deposit. The Township currently records the security deposit and deposits these checks. Refunds of security deposits are processed through the Township's accounts payable system which entails setting up each resident as a "vendor" and obtaining approval for not only the vendor but also the disbursement from the requisite management/Board of Commissioners. The accounts payable system carries each of these residents in its master vendor file until they are purged. We recommend that the Township consider an alternate procedure to streamline this process and eliminate the need for security deposit refunds to be processed through the accounts payable system.

Intergovernmental Revenues

Effective internal controls for intergovernmental revenues help to ensure that (1) the authorization for grants/entitlements billings result in the preparation of accounting records that recognize only allowable amounts, (2) all receipts are recorded accurately and deposited and (3) all receipts are allocated to the correct account, in the correct period and properly applied. Internal control weaknesses could result in the following:

- Unallowable amounts incurred;
- Amounts billed at incorrect amounts;
- Billings recorded incorrectly;
- Billings prepared incorrectly;
- Cash receipts recorded, but not deposited;
- Cash receipts amount recorded incorrectly;

- Amounts incurred, but not billed;
- Cash receipts not recorded or deposited;
- Cash receipts deposited, but not recorded;
- Cash receipts credited to wrong fund or account;
- Cash receipts credited to wrong period;
- Receivables reported in governmental funds for entitlements that are not yet available; and
- Revenue recognized for expenditure-driven grants before all grant requirements have been met.

We recommend that the following “best practices” be incorporated into the Township’s policies and procedures:

1. **Prior Authorization and Approval.** Letters of credit or payment vouchers should be approved.
2. **Security of Assets and Records.** Lockboxes should be used for proceeds when deemed cost effective. Electronic funds transfers should be used when possible,
3. **Segregation of Incompatible Duties.** Billings should be compared to award or entitlement by individual independent of billings. Billings should be recorded by individual independent of preparation. Duties for (1) handling and listing cash receipts, (2) posting to the receivables subsidiary ledger and the general ledger, (3) maintaining the cash receipts book and (4) making deposits should be segregated. Incoming cash items should be listed for subsequent reconciliations to deposits by an individual independent of recording cash receipts. Bank reconciliations should be independently reviewed. Overdue receivable balances should be independently investigated and followed-up by an individual independent of billings and receivables. An individual independent of the billings and receivable functions should investigate disallowed amounts.
4. **Periodic Reconciliations.** Bank reconciliations should be prepared at regular intervals by an individual independent of billings and receivables. Reconciliations should be reviewed and approved.
5. **Periodic Verifications.** Amounts should be billed only after comparison with grant/entitlement award. The validity of amounts billed should be verified prior to billing. Letters of credit or payment vouchers should be reviewed for accuracy. Open grants should reviewed periodically to ensure timeliness of billings

PURCHASES AND ACCOUNTS PAYABLE

The Board of Commissioners recently implemented additional review and approval procedures for the Township's accounts payable and disbursement function. The Township requires that all invoices be supported by a purchase order or check request and be approved by the Township Manager and Department Head. Effective in early 2008, on a test basis, several Commissioners reviews checks, and supporting information before the Board meets in its regular bi-weekly meeting. Once approved, the A/P Clerk processes the checks for approval by the Board of Commissioners. Upon approval, the A/P clerk generates the approved checks and forwards them to the President of the Board of Commissioners for approval. Due to limitations in the Township's accounts payable system, no additional invoices can be processed until the Board approves the current "run" of checks. This is resulting in a 5-day suspension of accounts payable activity twice per month and has caused a number of past-due bills and late fees.

We understand that the Township is currently working on a formal Purchasing Policy and revised procedures that will include the use of the purchase order system in its accounting application. Once these procedures have been fully implemented, we recommend that the Board of Commissioners consider its additional bi-weekly review and approval procedures so that the Township can move to a true on-line accounts payable system and avoid late fees and past-due bills.

The objectives of a sound Purchasing/Accounts Payable policy are (1) to ensure that the authorization to purchase supplies and services is reflected in the accounting records, including compliance with requirements for formal or informal bids, purchase order approval based on available budget, recording and elimination of encumbrances, establishment of purchase prices, terms and commitments, requisitioning of supplies and services, recording of purchases in the correct time period and amount with sufficient documentation and proper expenditure of financial assistance; and (2) to ensure that all expenditures made are reflected in the accounting records, including payment amount and allocation, in the correct time period, to the appropriate fund or account with sufficient information to identify the payee.

Internal control weaknesses could result in the following:

- Purchase recorded, but goods or services not received;
- Double payments;
- Encumbrance and/or purchase recorded incorrectly;
- Payment amount recorded incorrectly;
- Payment made, but not recorded;
- Purchases made, but not recorded;
- Unauthorized purchases;
- Ineligible expenditure of grant funds;
- Budget over-expended;
- Encumbrance and/or purchase misclassified;
- Payment recorded in wrong fund or account;
- Payment recorded in wrong period;
- Encumbrances reported as expenditures in the GAAP financial statements; and
- Failure to reserve fund balance in governmental funds for non-lapsing encumbrances (reservation of fund balance for lapsing encumbrances is optional).

The following best practices can mitigate these weaknesses:

1. **Prior Authorization and Approval.** Requisitions should be approved by appropriate department head for all purchases. Purchase orders should be approved by the Department Head.
2. **Properly Designed Records.** Pre-numbered requisition forms should be used and accounted for all purchases. Pre-numbered purchase orders should be used and accounted for. Encumbrances should be recorded and canceled when expenditures are recorded. Pre-numbered checks or warrants should be used. Vouchers should be canceled when paid (with all supporting documentation stamped or perforated to prevent reuse). Proper cutoff procedures should be in place to ensure that purchases are reported in the appropriate period.
3. **Security of Assets and Records.** Access to blank requisition forms, purchase orders and receiving reports should be strictly controlled.
4. **Segregation of Incompatible Duties.** Independent reviews of expense analysis, account designation on invoices and the serial continuity of checks should be periodically performed and documented. Independent reconciliation and review of vendor/supplier statements should be periodically performed and documented. Receipt of ordered goods should be confirmed by a receiving report issued by a separate department before payment is authorized. The receipt of services should be confirmed in writing by an individual other than the one who requisitioned the services before payment is authorized.
5. **Periodic Reconciliations.** Bank reconciliations should be performed regularly by an individual who is independent of the payables function. Encumbrance records should be agreed to open purchase orders. Invoice, receiving report, purchase order and requisition quantities should be compared. Used and unused requisition forms and purchase orders should be regularly reconciled to ensure that all such forms are properly accounted for. Numerical sequence of unused checks or warrants should be accounted for. Payment should not be authorized until management has examined and matched the requisition form, the purchase order, the receiving report and the invoice.
6. **Periodic Verifications.** Purchase orders should be compared to budget ordinance prior to recording encumbrance. Grant/entitlement expenditures should be compared to grant/entitlement award conditions or restrictions. Proper classification by fund and account should be verified before purchases are recorded in the accounting records.

Developers' Escrow

We noted a number of internal control weaknesses related to the Township's internal procedures related to the Developers' Escrow account. For example, formal procedures do not exist to monitor and follow-up on the total remaining in each developer's escrow versus the total amount of expenses paid on the developers' behalf. In many cases, developers owe the Township for expenses paid on their behalf in excess of the escrow. However, formal billing/collection procedures do not exist. Moreover, formal bank statements are not reviewed and reconciliations are not completed. All data related to Developers' Escrow is maintained in QuickBooks, separate from the Township's accounting application. We recommend that the Township consider integrating this function into the Foundations system.

We also recommend that the Township implement procedures for the developer's escrow that include the above best practices. Payment of invoices on the behalf of developers who do not have an adequate escrow balance should be prohibited. Amounts owed to the Township should be followed-up and collected. Bank reconciliations should be performed by an individual who is independent of the developers' escrow function.

TREASURY

Cash

The Township currently has approximately 30 bank accounts. We recommend that the Board of Commissioners consider consolidating these various accounts and eliminating those that are not necessary.

Recommendations for best practices to include in a formal *Cash Disbursements* Policy include the following:

1. **Authorization and Approval.** Blank checks should be maintained in a secure place with access only granted to authorized personnel. Authorized limits for check signatories (including dual signatures) should be defined and adhered to. Voided checks should be defaced and maintained. Physical control and mailing of checks should be performed by individual without access to accounts payable module of accounting system. Supporting information should be prepared and reviewed for each cash disbursement. Dual signatures should be required on wire transfers. Pre-authorized wires should be used for recurring wire transfers. Check/debit cards should be authorized by supervisory position. Bank statements should be reviewed for any unauthorized use of access cards. ACH transmissions should be reviewed for unusual activity. Bank and deposit limits should be subject to periodic review and reauthorization. Automatic transfers from lockbox accounts should be established for cash management purposes. A formal credit card policy that established restrictions on the use of the Township's credit cards should be developed and implemented.
2. **Initiation and Recording.** Processes should be in place to regularly reconcile bank statement activity to cash disbursements/receipts journal and general ledger. Bank statements should be opened by someone independent of the reconciliation process. Bank reconciliations should be reviewed and approved by a supervisor. Cash balances per bank and general ledger should be periodically monitored as part of cash management process.
3. **Security of Assets and Records.** Bank accounts should be reconciled and reviewed periodically by independent or supervisory personnel. Analysis of key ratios and results should be compared to budget. Deposits should be insured or otherwise collateralized in accordance with the Township's investment policy, ordinances, statutes or other requirements.
4. **Segregation of Incompatible Duties.** The preparation of cash disbursements should be performed by an individual who is independent of the approval of cash disbursements. The approval of cash disbursements should be segregated from the maintenance of the system. Bank reconciliations should be prepared by an individual who is independent of the cash disbursement function. Physical access to cash disbursements should be segregated from the accounts payable function.

Recommendations for best practices to include in a formal *Cash Receipts* Policy include the following:

1. **Initiation and Recording.** Processes should be in place to regularly reconcile bank statement activity to cash receipts postings. Lockbox should be used when cost effective to capture cash collections before they can be misappropriated. Checks should be restrictively endorsed by an individual who does not have access to receivable system. Cash receipts should be recorded using a cash register. Cash registers should be counted and balanced daily. Customers should be provided with the register receipt and the total **daily** receipts per the register should be balanced to cash deposited in the bank.

2. **Security of Assets and Records.** Cash receipts system and general ledger should be integrated. Bank accounts should be reconciled and reviewed periodically by independent or supervisory personnel. Mail should be opened by two individuals. Upon mail opening, an itemized listing (in duplicate) of daily receipts should be prepared and signed off by both individuals opening the mail. The total daily receipts per the listing should be balanced to the daily deposit.
3. **Properly Designed Records.** Pre-numbered cash receipt slips should be used and accounted for at all transactions points when the Township obtains a direct receipt from a resident (with the exception of the swimming pool).
4. **Periodic Reconciliations.** Bank accounts should be reconciled and reviewed periodically by independent or supervisory personnel. Procedures should be in place for follow-up and collection of checks returned for “insufficient funds”.
5. **Segregation of Incompatible Duties.** Responsibilities for collection and deposit preparation functions should be segregated from those for recording cash receipts and general ledger entries. Cash receipts functions should be adequately segregated from those for cash disbursements and accounts receivable. Responsibility for entries in the cash receipt (and disbursement) records should be adequately segregated from those for general ledger entries. Preparing and approving bank account reconciliations should be adequately segregated from those for other cash receipt (or disbursement functions). Checks returned for “insufficient funds” should be delivered to someone independent of those processing and recording cash receipts or reconciling cash/bank statements.

Investments

The Board of Commissioners is authorized by statute to invest funds as defined in the Township Code. We recommend that the Township develop and implement a formal Investment Policy that is compliant with the 1st Class Code. Such a policy will help to ensure that purchases of investments are properly authorized and accurately recorded, investments are properly safeguarded and sales of investments are properly authorized and accurately recorded.

Internal control weaknesses could result in the following:

- Investments recorded, but not acquired;
- Investment disposals recorded, but investments not sold;
- Sold investments recorded at wrong amount;
- Investment acquired but not recorded;
- Investments sold, but not recorded;
- Investments unauthorized;
- Unauthorized sales;
- Inadequate insurance or collateralization of deposits;
- Government’s claim to investments evidenced by securities not properly secured;
- Investments or earnings misclassified between funds or accounts;
- Investment income not properly allocated among funds;
- Investment policy not disclosed;
- Violations of investment policy not disclosed;
- Deposits not reported at both bank and book value;
- Bank value of deposits not classified by degree of custodial credit risk;

- Investments not reported at both book value and market value;
- Investments evidenced by securities not reported by degree of custodial credit risk;
- Disclosure not made of fact that significantly larger amounts of deposits or investments were in highest category of custodial credit risk at some time during the year than at year end;
- Disclosure not made of type of investments held during the year, but not at year-end;
- Reverse repurchase agreements not reported as an asset and liability;
- Securities lending agreements with cash collateral (or collateral securities that can be pledged or sold without a default) not reported as an asset and liability; and
- Reported value of investments not reduced for decreases in value that are “other than temporary”.

An effective Investment Policy should include the following “best practices:

1. **Prior Authorization and Approval.** All investment transactions should be formally approved after verifying conformity with written Investment Policy. All investment transactions should be certified as conforming to written investment policy. Investment policies should include list of approved brokers and investment types.
2. **Properly Designed Records.** Appropriate evidence should be obtained for all purchases prior to recording. Remittance advice should be received from trustee prior to recording investments sold.
3. **Security of Assets and Records.** Adequate physical safeguards and custodial procedures over investments should be in place such as requiring dual signature or authorizations to obtain release of securities from safekeeping or to obtain access to the governmental unit’s safe deposit box (or where securities are kept). Persons with access to securities should be formally authorized. Individuals with access to securities should be bonded. Wire transfers should be restricted to only designated accounts and only by authorized individuals. Investment receipts should be regularly reconciled to dividend due dates and dividend rates. Bank statements, broker statements and cash management reports should be reconciled and reviewed by appropriate supervisory personnel. Controls should be established to provide for periodic review of compliance with authorized depositories and trustees, insurance and collateralization requirements, and maintenance of bonding.
4. **Segregation of Incompatible Duties.** Investment purchases and sales should be posted to investment ledger by individual independent of other investment functions. Monthly reconciliations should be performed.
5. **Periodic Reconciliations.** Subsidiary investment ledgers should be maintained. Investment purchases and sales should be agreed to investment ledger. Bank statements and broker statements should be reconciled to investment ledger and the general ledger. Remittance advices for investments sold should be agreed to amounts recorded.
6. **Periodic Verifications.** Investments should be reviewed to determine if their classification is consistent with stated accounting policy and GAAP. Bank statements and broker statements should be reconciled and reviewed by appropriate supervisory personnel. Investment certificates should be periodically inspected. Sold investments should be reviewed prior to recording. Proper bidding procedures should be followed when acquiring investments.

CAPITAL ASSETS

The Township lacks a formal, documented Capital Asset Policy. While it adheres to the bidding and authorization requirements dictated by the Commonwealth of Pennsylvania, we recommend that the Township develop and implement a formal policy that addresses asset acquisition, asset disposal, depreciation and asset impairment. Such a policy will strengthen internal controls and help to ensure that the cost of equipment and inventory is properly reflected in the accounting records and allocated to the correct time period.

Ineffective internal controls could result in the following:

- Requisition of equipment and/or supplies recorded, but equipment and/or supplies not issued
- Equipment disposals not properly recorded
- Equipment or supplies lost (e.g., casualty loss, theft)
- Equipment or inventory obtained and/or used but not charged to fund or departments
- Material balances of inventory related to governmental funds and expendable trust funds using the "purchases method" not reported on the balance sheet
- Equipment reported in propriety funds not depreciated

Best practices that should be included in a Capital Asset Policy include:

1. **Authorization and Approval.** A capital expenditure budget should be maintained and reviewed periodically by management. Purchase orders should be completed and approved for capital asset purchases. Receiving documents should be matched to purchase orders and differences should be investigated. A listing of current capital asset additions should be maintained, reviewed and reconciled. Capital asset additions should be compared to approved purchase orders. Approval of capital asset purchases should be separate from accounts payable personnel. Annual impairment testing should be reviewed and approved by management. An up-to-date inventory of infrastructure assets should be maintained.
2. **Initiation and Recording.** Capital asset acquisition costs should be reviewed by someone independent of the acquisition. Journal entry to record capital asset acquisition should be reviewed by management. Listing of capital asset acquisitions should be compared to the account activity for the period. Formal capitalization policies should exist and should be communicated to accounts payable and purchasing personnel. Depreciation calculation methods should be periodically reviewed by management.
3. **Security of Assets and Records.** Appropriate controls over the movement of equipment and supplies should be in place. Capital asset list should be cross-referenced against insurance policies.
4. **Periodic Verifications.** Capital asset ledger reports are reconciled to the general ledger. Total capital asset additions/deletions should be reconciled to the general ledger activity in the capital asset accounts. Additions should be compared to the capital improvement plan and minutes. Activity in the capital asset general ledger accounts should be reviewed periodically by someone independent of capital asset purchasing duties. Capital asset additions should be reviewed by someone independent of data entry to verify proper useful life and depreciation method.
5. **Analytical Review.** Periodic investigations of variances between budget and actual usage should be performed.

Capital Asset Module-Fundations

During our review we noted that the Township maintains its capital asset listing and depreciation calculation in an Excel spreadsheet. The use of a separate system creates an internal control weakness. We recommend that the Township consider using all of the capabilities of the fixed asset module integrated with the Fundations accounting system.

PAYROLL

The Township uses a third party service provider that handles the majority of the functions related to payroll. However, there are no formal, documented policies in place. To improve internal controls, we recommend that the Township develop and implement formal payroll policies and procedures to ensure that employees are hired, terminated, and compensated in accordance with the Township's personnel policies, payroll transactions are initiated in accordance with the Township's personnel policies and procedures, all payroll transactions are properly recorded in and processed by the payroll system and payroll reports are accurate and payroll transactions are properly classified.

Ineffective internal controls could result in the following:

- Errors in payroll calculation and summary;
- Employee overpaid/payroll inflated;
- Employee paid for work not done;
- Employee underpaid/payroll understated;
- Wages/salaries charged to wrong fund or account; and
- Liability for compensated absences is incorrect.

Best practices to include in the payroll policies and procedures include:

1. **Authorization and Approval.** All new employees should be required to complete and sign an employment application form. A complete personnel file should be maintained for each employee. All personnel file changes should be authorized by department heads. Terminated employees should be communicated to the payroll supervisor to ensure the employee is removed from the payroll system. Personnel file change reports should be generated for all employee master file changes and should be reviewed by appropriate supervisory personnel.
2. **Initiation and Recording.** Employees should complete and sign their time sheets. These time sheets should be reviewed by supervisory personnel. Other payroll transactions such as bonuses, advances, loans, or commissions should be approved by appropriate person prior to entry into the system. Payroll register details are reviewed by a responsible official to ensure employees are not paid after departure. Written preapproval of overtime should be required. Manual input controls should exist to ensure that entry of payroll information is complete and accurate. Examples include recalculation of time sheets, batch control totals, comparison of number of time sheets to number of hourly employees and number of payroll entries, and review of input reports for reasonableness prior to processing. Edit reports and on-line edit routines should identify invalid employee numbers and reviews should be performed on the reasonableness of hours input.
3. **Reporting.** A payment register should be maintained of all employees detailing salary or wages and other employee benefits. This payment register should be reviewed for reasonableness and unusual items. A payroll journal should be prepared and approved prior to entry into the general ledger. Employee earnings and payroll control accounts should be periodically reconciled to the general ledger. Payroll expenses should be compared to budget monthly and significant differences should be identified and explained.

4. **Segregation of Incompatible Duties.** Payroll should be prepared by a person independent of time card approval, check signing and distribution. The distribution of payroll checks function should be segregated from other payroll functions. The payroll bank account should be regularly reconciled by individual independent of the payroll function after all disbursements have been issued.
5. **Security of Assets and Records.** Access to personnel files should be restricted to authorized staff and employee privacy should be protected.

Compensated Absences – Vacation and Sick Time

The Township has an extremely complicated and unusual method for calculating an employee's vacation and sick time. The policy requires employees' time to be recorded in a separate Access database in order to compute earned vacation and sick time. This is time-consuming and a duplication of efforts. We recommend that the Commissioners review the Township's policy for compensated absences and to the extent possible, consider implementing revisions to create a more straight-forward approach to vacation and sick time.

BUDGETING

The Township lacks a formal, documented budgeting process. The Board of Commissioners adopts the annual budget by ordinance. Traditionally, the Township Manager, the Director of Finance and the Department Heads collaborate on the annual budget. We understand that the Board of Commissioners and the Township Manager are considering the implementation of full encumbrance accounting, which would begin with the budgeting process. Regardless of the decision related to full encumbrance accounting, we recommend that the Township formally document its budgeting process and policies. An effective budgeting process should assist management to (1) establish broad goals to guide decisions, (2) develop strategies and financial policies, (3) design a budget supportive of strategies and goals and (4) focus on the necessity of continually evaluating an entity's success at achieving the goals that it has set for itself (i.e., performance).

Potential weaknesses in a budgeting process include the following:

- Budget based on erroneous assumptions or erroneously recorded;
- Budget not prepared based on all sources of revenues or appropriations;
- Budget changes not recorded;
- Unauthorized budget changes made;
- Budget items misclassified;
- Budget to actual comparisons in financial statements not based on final amended budget;
- Budget and actual data not presented on the budgetary basis of accounting;
- Non-GAAP budget presentation not reconciled to GAAP operating statement;
- Failure to state whether encumbrances lapse at the end of the fiscal year;
- Failure to disclose in notes that the original budget was amended; and
- Failure to reserve fund balance in governmental funds for non-lapsing encumbrances (reserves for lapsing encumbrances are permitted, but not required).

We recommend that the Township Manager and Director of Finance develop written policies and procedures related to the budgeting process. Issues that should be addressed to mitigate the above weaknesses include the following best practices:

1. **Authorization and Approval.** The budget should be prepared based on ordinance and in accordance with state laws (as appropriate). All changes to the budget should be approved prior to recording.
2. **Segregation of Incompatible Duties.** The budget should be approved by someone independent of approval and preparation. All budget components should be reviewed in detail by someone independent of preparation.
3. **Periodic Verification.** The budget should be compared to grant/entitlement awards and other support. The recorded budget should be reviewed and compared to the authorized budget. Proper verification should be performed to ensure that budget changes have been correctly recorded. Budget monitoring procedures should be in place when amendments are necessary so expenditures don't exceed approved appropriations.
4. **Timely Preparation of Financial Reports in Conformity with GAAP.** Monthly financial statements should be prepared to facilitate comparison of actual results to budgeted amounts.

FINANCIAL REPORTING

We recommend that the Township undertake a process, at least quarterly and preferably monthly, to ensure the ongoing completeness and accuracy of the financial records. This process should include monthly or quarterly closings, appropriate reconciliations to identify needed adjustments, preparation of quarterly (or monthly) financial statements and financial analyses of interim financial statements to identify irregular or incomplete data that needs to be corrected. Such a year-long process can provide regular financial information to management and the Board of Commissioners and to avoid material auditor-identified adjustments. Ideally, the close should occur within a week to ten days following the end of the period. To avoid delays, all items related to budgetary expenditures (e.g., purchase orders) should be recorded by the end of the period.

Best practices that can mitigate internal control weaknesses in a financial reporting process include the following:

1. **Authorization and Approval.** Authorization levels should be established for standard and nonstandard journal entries and adjustments of general ledger accounts. Management should establish policy statements and procedure manuals that specify how, when and by whom posting, adjustments to accounts and transfers are to be made.
2. **Properly Designed Records.** Management should require that all nonstandard journal entries be supported by adequate documentation and approved by appropriate supervisory personnel. A chart of accounts should be used as applicable for each fund. Presentations and disclosures required by GAAP should be appropriately determined and made in a timely manner. Accounting pronouncements newly applicable to the Township should be identified, evaluated and implemented in a timely manner. Regular financial statements should be prepared and reviewed.
3. **Security of Assets and Records.** Access to subsidiary ledgers, journals and the general ledger should be restricted to appropriate individuals.
4. **Segregation of Incompatible Duties.** A regular independent review of journal entries and supporting documentation should be performed.
5. **Periodic Reconciliations.** Regular reconciliations of control accounts to the related subsidiary records should be performed.
6. **Analytical Review.** Regular extraction of fund trial balances and prompt investigation of any unusual items.

CAPITAL ASSETS

ASSET ACQUISITION

I. Process

The Township adheres to the bidding requirements dictated by the Commonwealth of Pennsylvania. The Board of Commissioners approves the purchase of capital assets based on the results of the bidding process. However, the Township does not have a formal Purchasing & Procurement Policy.

Upon approval of the purchase of a capital asset, a purchase order is completed. When the A/P Clerk receives the invoice and the purchase order for the asset she reviews the information for accuracy and enters the invoice into the Foundation's A/P system. The system allows the user to "flag" the purchase as a fixed asset.

The Township is not using all of the capabilities of the Foundation's Fixed Asset module. Therefore, the purchase information (a copy of the invoice) is forwarded to the Director of Finance who enters the asset information into Excel spreadsheets. The Excel spreadsheets are used to calculate depreciation expense and accumulated depreciation. The Director of Finance adheres to "best practices" to estimate asset useful lives as follows:

- Land Improvements - 20 years;
- Building and Building Improvements - 20-40 years;
- Machinery and Equipment - 5-20 years;
- Vehicles - 5-20 years; and
- Sewer Collection System - 20-50 years.

The general ledger is updated through manual journal entries as follows:

- As expenses are incurred for capital projects in the Proprietary/Sewer System, the Township records an expense and at the end of the year performs a manual entry to record the capital asset. The depreciation expense for the Sewer system is recorded through a journal entry based on an Excel-based spreadsheet.
- All fixed assets in the governmental system are recorded as capital outlays. The depreciation expense for the government fund is posted in conjunction with year-end closing procedures and is provided by the Township's external auditor.

The Township does not have a formal policy or procedure to track its capital assets such as fixed asset tags. The Township does not take an inventory of its existing fixed assets on a regular basis. However, the Public Works Director maintains an asset inventory and has assigned unit numbers (generated by Foundations upon the generation of a purchase order) on each large piece of equipment and vehicles. For other assets, the Director of Finance manually assigns a sequential number which is noted in the Foundation's description field.

Although asset disposals are rare, The Township does not have a formal process for capital asset disposals or for impairment testing of existing capital assets.

II. Evaluation of Control Design and Test of Controls

A. Authorization. Capital asset acquisitions and disposals are approved.

Controls. The Township adheres to a formal bidding process. A one-year capital expenditure budget is maintained. The capital expenditure budget is reviewed periodically by management. Purchase orders are completed and approved for capital asset purchases. A listing of current capital asset additions is maintained. Capital asset additions are compared to approved purchase orders. Approval of capital asset purchases is separate from accounts payable personnel.

- RKL discussed these procedures with the A/P Clerk, the Director of Finance and the Interim Township Manager. They confirmed that the above controls are in place.
- RKL reviewed several purchase orders to verify that proper approval was obtained to support the payment of invoices.
- RKL reviewed Board Minutes noting approval of Bids above the \$ 10,000 threshold.

Recommendations:

- A formal Purchasing and Procurement Policy should be developed to document the Township's bidding requirements and authorization requirements.
- The Township should develop formal policies for impairment testing and asset disposal.

B. Initiation and Recording. Capital asset costs are accurately recorded. Capital asset disposals are approved.

Controls. Capital asset acquisition costs are reviewed by someone independent of the acquisition. Capital asset disposals are approved.

- RKL discussed these procedures with the Finance Director who confirmed that she reviews capital asset costs upon data entry to the Excel spreadsheet.

Recommendations:

- The journal entry to record capital asset acquisition should be reviewed by management.
- A listing of capital asset acquisitions should be compared to the account activity for the period, on a monthly basis.
- Formal capitalization policies should be developed and communicated to accounts payable personnel.

C. Processing. All capital asset records are properly updated.

Controls. Capital asset list is cross-referenced against list provided by insurance carrier.

- RKL discussed this procedure with the Finance Director who confirmed that she reviews the capital asset list provided by the Insurance Carrier on a periodic basis.

Recommendations:

- Activity in expense accounts related to capital assets, (i.e., capital outlay, repairs, rent, supplies, maintenance, etc.) should be reviewed by management.

- Capital asset acquisition reports should be reviewed by someone independent of the purchasing function.
- A capital asset inventory should be taken and items not included on the capital asset listing should be investigated.
- Capital asset records should be reconciled to the general ledger on a periodic basis (monthly).

D. Reporting. Capital asset acquisitions and disposals are properly recorded in the fixed asset general ledger accounts.

Controls. The accounting system allows the expenditure to be flagged as a capital outlay. The Excel-based spreadsheet is reconciled to the general ledger as part of the year-end procedures.

Recommendations:

- Total capital asset additions and disposals should be reconciled to the general ledger activity in the capital asset accounts on a monthly basis.
- Additions and disposals should be compared to the capital improvement plan and minutes, as appropriate.
- Activity in the capital asset general ledger accounts should be reviewed periodically by someone independent of capital asset purchasing duties.
- The Township should fully implement the fixed asset module of Fundations.

DEPRECIATION

A. Authorization. Depreciation methods and estimated lives are approved.

Controls. The Township adheres to financial reporting standards for depreciation methods and useful lives.

- RKL confirmed the above procedures with the Finance Director.

Recommendations:

- Capital asset ledger entries should be approved by management.
- Capital asset ledger reports should be periodically reviewed by management.
- Depreciation calculation should be periodically reviewed by management.

B. Initiation and Recording. Capital asset depreciation is accurately recorded.

Controls. The Finance Director uses an Excel-based spreadsheet to calculate capital asset depreciation.

- RKL reviewed the Excel-based spreadsheet and recalculated estimated useful lives, depreciation methods used and depreciation expense on a test basis.
- RKL confirmed the above procedures with the Finance Director.

Recommendations:

- Capital asset ledger reports should be reconciled to the depreciation expense accounts on a monthly basis.
- Capital asset acquisition costs should be reviewed by someone independent of the acquisition.
- Capital asset system additions should be reviewed by someone independent of data entry to verify proper useful life and depreciation method.
- Capital asset disposals should be compared to the listing of fixed assets included in the capital asset ledger.

C. Processing. All depreciation transactions are accurately processed.

Controls. The Township uses an Excel-based spreadsheet to calculate and track depreciation transactions.

- RKL reviewed the Excel-based spreadsheet and recalculated estimated useful lives, depreciation methods used and depreciation expense on a test basis.
- RKL confirmed the above procedures with the Finance Director.

Recommendations:

- The Township should implement and fully use all the features available with the fixed asset module within Foundations.
- The capital asset system should be reconciled to the depreciation expense accounts on a monthly basis.

D. Reporting. Depreciation expense is properly recorded in the accumulated depreciation and depreciation expense general ledger accounts.

Controls. The Township uses an Excel-based spreadsheet to calculate and track depreciation transactions.

- RKL reviewed the Excel-based spreadsheet and recalculated estimated useful lives, depreciation methods used and depreciation expense on a test basis.
- RKL confirmed the above procedures with the Finance Director.

Recommendations:

- The Township should implement and fully use all the features available with the fixed asset module within Foundations.
- The capital asset system should be reconciled to the depreciation expense accounts on a monthly basis.

Purchases and Accounts Payable

Purchases

I. Process

According to the Code Township's policy, purchases in excess of \$ 10,000 require formal bids; purchases greater than \$ 4,000-\$ 10,000 require a telephone quote from at least three vendors. All purchases up to \$ 4,000 must be approved by the Director of Finance. Purchases in excess of \$ 4,000 must be approved by the Township Manager.

The Township utilizes a purchase order system that is integrated with Foundations accounting software. All employees can be involved as a requester (to order below the bidding guidelines and those established by the Township - \$ 4,000 for bid and above; \$ 500 or less for day-to-day purchases). If a Township employee wants to place an order they are required to complete a purchase order. Purchase orders are approved by the Department Head. All purchase orders are input into the purchase order module by Kim Molnar, and Donna Fowler, Receptionist/General Office and then approved by the Director of Finance. A green copy of the purchase order is sent to the A/P Clerk, and a pink copy is returned to the originating department to use as a confirmation receipt. When goods are received, the requestor signs off on the pick copy of the purchase order to confirm receipt and forwards this copy to the A/P Clerk.

The A/P Clerk matches the green copy of the purchase order to the invoice when it is received by the Township. If the A/P Clerk does not have a corresponding approved purchase order for an invoice, she contacts the appropriate individual for resolution. As a matter of policy, invoices are not paid without an approved purchase order or check request.

The general ledger account number to charge is written on the Purchase order. The Director of Finance verifies the general ledger code on all purchase orders before approval. When the invoice is received and entered, the A/P Clerk verifies the general ledger account for appropriateness. In addition, if the item purchased is "capital" in nature, the A/P Clerk makes a copy of the invoice for inclusion in her fixed asset file for financial reporting purposes.

II. Evaluation of Control Design and Test of Controls

A. Access. Access is restricted to authorized employees.

Control. Access to Foundations and A/P system is restricted via passwords.

- Unique user IDs are used and passwords can be unique if the user so chooses. When a new system is installed or when requested, all user passwords are reset to a generic password. Upon the next login, users may change their password but are not required to do so. Therefore, several users may have the same generic password. Only the Director of Finance and the Project Coordinator have the administrative password, which is not changed. After 3 invalid logon attempts, user accounts are disabled. Employees are assigned security levels that restrict their access to the system. The Township does not allow remote access to systems other than e-mail retrieval.

Recommendations:

- Develop procedures to ensure that employees use unique passwords and that these passwords are changed every 90 days.
- Eliminate the “Administrative User”. The Director of Finance should be given appropriate administrative rights to Foundations within her user profile. If deemed necessary, the Township could appoint another employee as a backup to the Director of Finance in her absence. Administrative actions performed by this employee should be subsequently reviewed and approved by the Director of Finance.

B. Authorization. All purchases are properly authorized.

- Controls. Departments requesting assets, goods or services submit approved, serially numbered purchase orders to the A/P Clerk. The appropriation or budgetary account to be charged is noted on purchase requisition forms before they are approved. An individual independent of requester reviews the request for propriety. The Township only makes purchases from an approved vendor/supplier listing. Access to the approved supplier/vendor listing is restricted to authorized personnel. When above a certain threshold, bidding procedures are used.
- The Director of Finance and the A/P Clerk indicated that they were aware of the Township's policy on purchase authorizations.
- RKL reviewed Board Minutes noting approval of Bids above the \$10,000 threshold.
- RKL reviewed several purchase orders noting proper approval and documentation of account to be charged.

Recommendations:

- The Township should periodically review prices from various competitors.
- The Township should implement formal procedures to determine if sufficient unobligated funds exist in the appropriation or budget account before a purchase commitment is made.

C. Initiation and Recording. Terms of requested purchases are accurate.

Controls. Terms of requested purchases are checked by two individuals.

- The Director of Finance indicated that she checks the accuracy of purchase orders.
- The A/P Clerk confirmed that she checks the accuracy of the invoice and matches it with the receiving report. However, she does not spot check to see if extensions on invoices are accurately computed by the provider of the service/purchase. Additionally, this information is reviewed by the Commissioners during their bi-monthly review of invoices.
- RKL checked the mathematical calculation on the invoice selected for walkthrough compared to amount paid. No exception noted.

Recommendations:

- The A/P Clerk should recalculate invoices to verify that extensions are accurately computed by the provider of the service/purchase

- Purchase order specifications should be defined and monitored on a regular basis.

D. Processing. All approved purchase orders are processed.

Controls. Pre-numbered purchase orders are used and forwarded to the appropriate departments.

- RKL discussed this process with the A/P Clerk. She confirmed that pre-numbered purchase orders are used.
- For item selected above, RKL noted that a purchase order was attached to the invoice.

Recommendations:

- Numerical sequence of purchase orders should be periodically reconciled.

E. Reporting. All approved purchases will be accurately recorded in subsidiary and general ledgers.

Controls. Subsidiary ledgers are reconciled to general ledger at end of year. Pre-numbered purchase orders are used. These forms identify general ledger account codes.

- RKL discussed these control processes with the Director of Finance and the A/P Clerk.
- December 31, 2007 audit procedures included verification that the subsidiary ledger was reconciled to the general ledger.

Recommendations:

- The subsidiary ledger should be formally reconciled to the general ledger on a monthly basis by an employee who is independent of the purchasing/payables function. This reconciliation should be approved by Supervisory personnel.

Accounts Payable

I. Process

The receptionist opens all incoming mail. Invoices are segregated and forwarded to the appropriate department (Public Works, Community Center, Office Administration). A designated employee in each department matches the invoices to the appropriate check request form or purchase order. Invoices are then forwarded to the Township Manager (or in his absence, the Director of Finance) for approval. All invoices must be approved by either the Township Manager or the Director of Finance. The approved invoices are forward to the A/P Clerk who reviews the information on the check request form or the purchase order for completeness and accuracy. Documentation that is incomplete or inaccurate is returned to the appropriate employee for verification and/or correction.

The Township has a 10% plus or minus rule. For example, if a purchase order is written for \$ 100 but the invoice is within 10%, the A/P Clerk can proceed to pay without further investigation-anything outside of that scope gets turned back to the originator to provide explanation or to request accurate price information from the vendor. In all cases, the Director of Finance must provide supervisory approval for the Foundations system to accept an invoice with terms and price that does not match the purchase order.

The A/P Clerk enters the invoice into the Foundation's Accounts Payable system including the vendor (selected via a pull-down menu or entered by keystrokes), invoice number, invoice date, amount, terms and description. A vendor must exist in the system for an invoice to be processed. After the invoices are entered, the A/P Clerk generates a "Bills by Vendor Report" and reviews the accuracy of the data entry. She corrects any errors noted and generates a revised report, if necessary. The Township has historically not taken advantage of favorable payment terms afforded by its vendors. As the invoice is entered, a credit is recorded to accounts payable and a debit is recorded to the indicated expense account.

Invoices that cause an account to be over-budget cannot be entered into the Foundation's system. When the A/P Clerk receives an "over-budget" warning, the system will only allow the invoice to be deleted. When an invoice is deleted, system controls exist to prevent to re-use of the invoice number. Foundations will not allow an invoice number to be used more than once. If an invoice number is entered more than once, Foundations prevents the user from proceeding with the transaction and returns an error message indicating the number has already been used. All over-budget exceptions are forwarded to the Director of Finance.

The A/P Clerk performs a "cut-off" and posts the invoices to the General Ledger on the Friday prior to the Board of Commissioners bi-monthly Thursday meeting. She produces a "Bills by Vendor Report". On a test basis, several of the Township's Commissioners perform a review of these invoices. They select a sample of the invoices from the Bills by Vendor Report, request back-up documentation from the Director of Finance and perform a detailed review of the information provided. If necessary, they request additional information to substantiate the payment.

An "Accounts Payable Report for Payment of Bills" is prepared that includes invoice totals for each fund is presented to the Board of Commissioners for final approval at their bi-monthly Thursday meetings. Upon this approval, the A/P Clerk cuts checks on Friday and obtains the signature of the President of the Board of Commissioners and the Treasurer. When the checks are cut, a credit is recorded to cash and a debit is recorded to accounts payable. The Township does not issue manual checks. When the checks are signed, the A/P Clerk mails the check and files copies of the check and invoice in a filing cabinet in her office, alphabetical by vendor.

Accounts payable records are reconciled to the General Ledger at the end of the calendar year. The A/P Clerk prepares a journal entry to reverse out the prior year accounts payable balance and record the current year's accounts payable.

As part of the year-end procedures, the detailed general ledger is reviewed by the Director of Finance for unusual or mis-posted items.

II. Evaluation of Control Design and Test of Controls

A. Authorization. Invoices received are properly authorized.

Controls. Invoices must be matched to an authorized purchase order, contract or check request before an invoice can be paid. Invoices received are properly authorized before processing. Any invoices not authorized are investigated, by direct contact with the appropriate individual. Accounting department maintains approved purchase order, check requisition and invoice from vendor.

- RKL discussed this procedure with A/P Clerk. She confirmed that this is the process the Township utilizes.

- RKL reviewed several invoices and supporting documentation to verify that documentation existed to support the payment of invoices.

B. Initiation and Recording. Invoices and expenses are recorded at proper amounts and in the proper accounts and in the correct period. Proper cut-off is achieved.

Controls. Invoice, purchase order, and data entered into system are reviewed by person independent of A/P process. Check amounts are compared to the approved amounts by the Commissioner signing checks. Accounting Department records goods received into accounts payable.

- RKL discussed this process with the Director of Finance and the A/P Clerk. As part of the sampling process by the Commissioners, the invoice amount is compared to purchase order/check request/contract. When checks are signed, the Board President and the Treasurer (or one of alternate signatories) should compare the check amounts to the approved amounts for accuracy.
- RKL discussed cut-off procedures with the A/P Clerk and the Director of Finance. The Township performs a cut-off only at year-end.

Recommendations:

- Exception reports should be generated to identify input errors, check numerical sequence of purchase orders and invoices, and identify unusual transactions. These reports should be reviewed by Supervisory personnel.
- The subsidiary ledger should be formally reconciled to the general ledger on a monthly basis. This reconciliation should be approved by Supervisory personnel.

C. Processing. Accounts payable subsidiary records accurately reflect all transactions.

Controls. Unmatched invoices are investigated. Access to the vendor master file is limited to authorized employees. Procedures are in place to provide for accurate account distribution of invoice processing entries.

- RKL discussed these procedures with the A/P Clerk. Unmatched invoices are investigated and resolved with the appropriate individuals. Purchase orders or check requisitions must include the account number to be charged. The A/P Clerk and the Director of Finance have access to the vendor master file.

D. Reporting. Accounts payable records and expenditure accounts are updated accurately.

Controls. Supervisory personnel regularly review general ledger account codes on purchase orders and invoices.

Recommendations:

- Expenses should be regularly compared to budgets and variances should be investigated.
- Supervisory personnel should regularly review general ledger activity.

E. Segregation of Duties

Recommendations:

- The cash disbursement function should be segregated from the bank reconciliation function.
- Bank statements should be opened by an individual who is independent of the bank reconciliation function.

Developers' Escrow**I. Process**

Developers and/or property owners are required to make a deposit when submitting an application and plans for building projects. The escrow account deposits are required to reimburse the Township for expenses including engineering, planning, legal and other expenses connected with the review of submitted materials and plans.

A developer/property owner is required to complete a Subdivision/Land Development/Conditional Use Application. The Zoning Officer collects a \$ 50 application fee, signs off on the application and forwards it to Keystone Consulting Engineers, Inc. ("Keystone"). Keystone assigns the project a unique number and assesses an escrow deposit requirement that is dependent upon the project type. The application is forwarded back to the Zoning Officer who collects the escrow deposit from the developer/property owner. The application and check are forwarded to the Finance Director or the Receptionist/General Office Clerk (K. Molnar).

The Receptionist/General Office Clerk enters the developer/property owner information into QuickBooks. Checks are batched and held in a file folder in the Director of Finance's office. On a weekly basis, the Receptionist/General Office Clerk prepares a deposit slip and the checks are deposited to a Developers' Escrow bank account at Lafayette Bank. The Director of Finance prepares and makes the appropriate journal entry.

The Receptionist/General Office Clerk opens all mail and segregates invoices related to the developers' escrow accounts. She enters the invoices into QuickBooks and prepares payment checks approximately twice a month. To prepare payment checks, the Receptionist/General Office Clerk generates an Unpaid Bills Detail which lists all unpaid invoices by vendor name and a Check Request which lists the payee, description and amount. The Check request must be approved by the Director of Finance and the Township Manager (if over \$ 4,000). Upon approval, the Receptionist/General Office Clerk prepares the checks through QuickBooks. The checks must be signed by the Township's Treasurer and an additional Commissioner.

The Receptionist/General Office Clerk prepares the bank account reconciliation on a monthly basis. The bank reconciliation is reviewed by the Director of Finance.

The Township only remits statements to those developers/property owners who owe the Township money. The Township does not send past due notices. The Township continues to pay invoices as they are received regardless of the developers/property owners' escrow balance. At January 31, 2009, developers escrow accounts receivable greater than 90 days outstanding approximated \$ 127,000. The Permits Coordinator receives a copy of the A/R Aging Detail Report generated from QuickBooks and will not issue a Certificate of Occupancy until monies owed to the Township are paid.

When a building project is completed, Keystone sends the Township a written notification indicating that the project should be closed and the escrow account should be brought to a \$ 0 balance. The Director of Finance contacts the vendors to request all outstanding invoices for the project. After 30

days, the Director of Finance generates a refund check for monies remaining. No additional approval of a refund check is required.

II. Evaluation of Control Design

A. Authorization. Appropriate rates and charges are established.

Controls. Not applicable. Keystone Consulting Engineers assesses the initial escrow deposit amount.

Recommendations:

- According to the Subdivision/Land Development/Conditional Use Application, once an escrow account has decreased below 50% of its original balance, the developer/property owner must make a deposit to return to the account to its original balance. The Township should implement procedures to ensure adherence to this policy.
- The Township should implement procedures to ensure that invoices are not paid on behalf of developers/owners who do not have an adequate escrow balance.

B. Initiation and Recording. Cash receipts are properly recorded. Disbursements are properly recorded.

Controls. The Director of Finance and/or the Township Manager approves all disbursements from escrow accounts. Bank statements are reconciled on a monthly basis. The Township reconciles cash receipts and cash disbursements to bank statement activity on a monthly basis.

RKL reviewed completed bank reconciliations, noting completeness and accuracy. We performed walkthroughs of receipt and disbursement transactions.

Recommendations:

- Due to lack of integration, the Township should consider using Foundations for all developers' escrow activity as a replacement for QuickBooks.
- Monies received from developers/property owners should be deposited at the bank the day received by the Township.
- Monies received from developers/property owners should be acknowledged with a system generated receipt.
- The Township should consider preparing and distributing monthly statements for each escrow account.

C. Processing. All items are reconciled and recorded.

Controls. Bank statements are reconciled on a monthly basis.

RKL reviewed completed bank reconciliations, noting completeness and accuracy.

Recommendations:

- Due to lack of integration, the Township should consider using Foundations for all developers' escrow activity as a replacement for QuickBooks.

D. Reporting. Transactions are accurately summarized and posted to the general ledger.

Controls. The Director of Finance prepares and makes a monthly manual journal entry to record developers' escrow account activity. The Director of Finance reviews QuickBooks activity.

Recommendations:

- Due to lack of integration, the Township should consider using Foundations for all developers' escrow activity as a replacement for QuickBooks.
- The Township should consider preparing and distributing monthly statements for each escrow account.

E. Segregation of Duties.

Recommendations:

- Escrow account cash receipts should be handled by an individual who is independent of the cash disbursement function.
- Bank reconciliations should be prepared by an individual who is independent of the cash receipt and cash disbursement functions.
- Responsibility for following up with past due accounts should be assigned to someone independent of the cash receipts and cash disbursement function.

REVENUE

I. General

In the statement of activities, revenues that are derived directly from each activity or from parties outside the Township's taxpayers are **program revenues**. Amounts reported as program revenues include (1) charges to customers or applicants for goods or services or privileges provided, (2) operating grants and contributions and (3) capital grants and contributions including special assessments.

The **proprietary funds'** operating revenues generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The Township has two proprietary funds i) Solid Waste Fund and ii) Sewer Fund. The principal operating revenues of these funds are usage charges. The Township also recognizes the portion of tapping fees intended to recover the cost of connecting new customers to the system as operating revenues. The principal non-operating revenue of the Township's proprietary fund is interest income.

The most significant revenues recognized in the **governmental funds** are earned income taxes (EIT), real estate transfer taxes and monies derived from licenses and permits. This revenue is captured in the General Fund.

Solid Waste & Sewer Revenue

I. Process-

The Township collects solid waste and sewer fees from approximately 12,000 customers. The recognition of solid waste and sewer revenue begins with the Township's billing cycle which includes two groups; Cycle A and Cycle B. The Township bills each cycle quarterly. Sewer fees are calculated in three ways as follows: (i) based on water consumption, (ii) flat fee or (iii) based on meter readings performed by the Lower Macungie Township Department of Public Works. Trash service is billed at a flat rate of \$ 62.50 per quarter. If a resident is provided both solid waste and sewer services, their invoices will include fees for both.

The Lehigh County Authority ("LCA") provides the Township with a Customer Water Usage Report that details customer water consumption. The Utility Billing Clerk, enters this usage information from the LCA reports into the Foundations system. The system calculates the invoice amount based on the usage and a rate that was predetermined when the customer was set-up. The system does not allow the billing clerk to alter the information in the system once the invoices are posted. Therefore, the Utility Billing Clerk reviews the invoices on-line for errors and runs a Billing Register Report prior to posting the invoices. The Utility Billing Clerk documents necessary changes on a "Change From" form which is approved by the Director of Finance. After the review, the invoices are posted. When the invoices are generated and posted, Foundations automatically posts a journal entry to record the receivable and the revenue.

Customers are billed in January for October through December of the prior year. Customers are billed in March for the previous December through February. The Utility Billing Clerk prepares and posts a journal entry in January and in March to properly record revenue in the proper period. The Director of Finance approves the journal entry.

Utility receipts are received through the mail, in person or from the lockbox established at Commerce Bank. The Township uses Remote Deposit Capture ("RDC") through Commerce Bank for payments received through the mail or in person at the Township. The Utility Billing Clerk, records all payments

received in the Foundations system. For cash accepted at the Township's offices, the Accounts Receivable Clerk prepares a manual 2-part receipt. One copy is given to the resident and the other copy is maintained. All cash is maintained in a locked box in the Administrative Assistant's office. The A/P Clerk collects the cash, reconciles it to the total and takes it to the bank on a weekly basis.

The Administrative Assistant opens and sorts the utility mail. If a payment stub is not included with the resident's payment, she makes a copy of the check. The Administrative Assistant runs a tape of (a) all checks received and (b) all payment stubs. If the totals agree, she scans the checks through the RDC scanner. The RDC system provides a batch total. The Administrative Assistant reconciles the RDC batch total to her manual calculation of the total payments and resolves any discrepancies. The funds are automatically deposited into the Township's Utility account. The Administrative Assistant maintains the original checks until she has verified that the deposit was properly recorded by Commerce Bank. At this point, the Administrative Assistant shreds the original check. Commerce Bank maintains electronic copies of the checks for 365 days. Commerce Bank also sends the Township a monthly CD with copies of all processed checks. The Director of Finance maintains the CD's in a locked cabinet in her office. The Administrative Assistant forwards the RDC report and copies of the checks and payment stubs to the Utility Billing Clerk who records the receipt into Foundations.

For lockbox receipts, Commerce Bank delivers a large envelope to the Township which includes a "Deposit Detail Report Wholesale Lockbox Department" which lists the business date, lock box reference number, item count and total deposit amount. Each of the deposits is accompanied by a copy of the resident's check and a copy of the original invoice. The Utility Billing Clerk posts the payments into the Foundations system and documents the Foundations control number and the total amount of the trash fees and the sewer fees. She also documents the posting date on the face of the "Deposit Detail Report". The Sewer/Solid Waste Billing Clerk runs a report "Posted Journals" that shows the date, invoice number, account, account name and the debit and or credit. Foundations posts an automatic journal entry to record the cash received and reduce the appropriate receivable. The Utility Billing Clerk gives the Deposit Detail Report to the Director of Finance, who transfers the appropriate amount from the Utility Billing Cash account into the Solid Waste or Sewer Cash account.

II. Evaluation of Control Design

A. Authorization. All users are properly identified. The billed rates are approved.

Controls. Approved rates are entered into the system. The Township receives notification from the Lehigh County Authority of properties to be billed. Only the Board of Commissioners may authorize a rate change through an ordinance or resolution.

RKL discussed the above with the Sewer/Solid Waste Billing Clerk, the Receptionist and the Director of Finance. RKL reviewed LCA usage reports that detail resident water usage by address.

Recommendations:

- Edit reports detailing changes to approved rates should be generated and reviewed by Supervisory personnel.

B. Initiation and Recording. All users are entered into the system. Billed rates are entered into the system.

Controls. Approved rates are entered into the system. The Township receives notification from the Lehigh County Authority of properties to be billed.

RKL discussed the above procedures with the Sewer/Solid Waste Billing Clerk. We randomly selected a service address, reviewed a copy of the quarterly bill. We traced amounts to inclusion in the appropriate general ledger account.

Recommendations:

- Edit reports detailing changes to approved rates should be generated and reviewed by Supervisory personnel.
- Unusual usage readings should be documented and investigated on a timely basis.
- Billing disputes and adjustments are addressed by an individual independent of maintenance of the receivable ledger.

C. Processing. Utility billings are reconciled and recorded.

Controls. Bank statements are reconciled on a monthly basis.

RKL discussed the processing procedures with the Utility Billing Clerk. The Township does not formally reconcile utility accounts on a regular basis.

Recommendations:

- The Township should reconcile utility revenue accounts on a monthly basis.
- Management should review utility revenue accounts in comparison to budget amounts on a monthly basis.
- Management should review and approve bank statement reconciliations on a monthly basis.

D. Reporting. Transactions are accurately summarized and posted to the general ledger

Controls. Fundations automatically creates journal entries for utility billings.

RKL discussed the processing procedures with the Utility Billing Clerk. The Township does not formally reconcile utility accounts on a regular basis.

Recommendations:

- Management should review transaction activity in revenue and receivable accounts periodically.
- Subsidiary ledgers should be reconciled to the general ledger monthly.

Earned Income and Real Estate Transfer Taxes.

I. Process

The Earned Income Tax Office (and Lehigh County) remit payments (checks) to the Township for earned income taxes (EIT) and real estate transfer taxes. The Township receives the checks through the mail or in person at the Township office. EIT receipts come from (a) taxpayers, (b) employers in Lower Macungie Township and (c) employers outside of Lower Macungie Township with employees who reside in the Township. Real estate transfer taxes are generated by Lehigh County based on a percentage of the selling price of real estate. The Director of Finance receives the checks from Lehigh County and enters the information on an Excel spreadsheet. She forwards all checks to the Administrative Assistant who records it on an Excel spreadsheet and prepares a deposit slip. She forwards the checks and deposit to the A/P Clerk who takes the deposit to the bank.

Receipts. The Administrative Assistant opens and sorts all the EIT and real estate transfer tax mail. She stamps the documentation with the date received and restrictively endorses the checks with a stamp that is maintained in her desk. The Administrative Assistant also receives payments in person in the form of check or cash. She records the payment in a receipt book and includes the name, amount paid, social security number and form of payment. The Administrative Assistant also prepares a two-part receipt. One copy is given to the resident and one copy is maintained. The Administrative Assistant also records all receipts (mail and in person) on an Excel-based spreadsheet.

The Administrative Assistant prepares a deposit slip. She forwards a copy of the Excel spreadsheet and the deposit slip to the A/P Clerk who verifies the accuracy of the deposit and takes it to the bank. The Administrative Assistant forwards a copy of the Excel spreadsheet and all related paperwork to the Tax Collector, Kathy O'Brien. The Tax Collector enters the payment information into a stand-alone Tax Collection application and generates a daily summary report. The Tax Collector reconciles the total received per the stand-alone system to the total per the Excel spreadsheet and daily deposit.

At the end of each month, the Director of Finance posts a journal entry in Foundations to record all of the EIT and real estate transfer tax receipts. The journal entry is approved by the Township Manager prior to posting and is as follows:

	Debit	Credit
Cash-Fiscal Agent	\$ XX.XX	
Restricted Earned Income Receipts		\$ XX.XX

Distributions. Employers in the Township withhold 1% of an employee's quarterly earnings. These amounts are forwarded to the Tax Collector's Office with documentation supporting the payment including names of employees and addresses. The Tax Collector, or Paulette Galiardo, Administrative Assistant enters the information from the employer's reports into a stand-alone tax collection system. This system calculates what is owed to other tax collectors and generates distribution checks based upon these calculations. The Tax Collector or the Administrative Assistant mails the checks.

II. Evaluation of Control Design

A. Authorization. Taxpayers and other applicable users are properly identified. Appropriate rates and charges are established.

Controls. Not applicable. The Township receives checks for EIT and real estate transfer taxes.

B. Initiation and Recording. Fee used is accurate. Cash receipts are accurately recorded.

Controls. The Township does not process billing statements for EIT and real estate transfer taxes and therefore, does not initiate these transactions. Revenue is recognized at the end of the month through a journal entry.

Recommendations:

- The Township should eliminate the use of manual receipts and fully implement Foundation's cash receipts system for earned income and real estate transfer taxes.
- Management should review revenue accounts in comparison to budget amounts on a monthly basis.
- Management should review and approve bank statement reconciliations on a monthly basis.

C. Processing. All revenue items are reconciled and recorded.

Controls. Bank statements are reconciled on a monthly basis.

RKL discussed the processing procedures with the Administrative Assistant. The Township does not formally reconcile EIT and real estate transfer revenue accounts on a regular basis. RKL vouched significant revenue amounts and traced the EIT and real estate transfer tax revenue through the Foundations system.

Recommendations:

- The Township should reconcile revenue accounts on a monthly basis.
- Management should review revenue accounts in comparison to budget amounts on a monthly basis.
- Management should review and approve bank statement reconciliations on a monthly basis.

D. Reporting. Transactions are accurately summarized and posted to the general ledger.

Controls. Journal entries are approved prior to posting.

RKL discussed the above procedures with the Director of Finance and reviewed journal entry documentation.

Recommendations:

- Transaction activity in revenue accounts should be reviewed monthly
- Subsidiary ledgers should be reconciled to the general ledger monthly.
- Internal financial statements should be compared to budgets and/or historical results on a monthly basis.
- Unusual items investigated by appropriate level of management.

Sewer Allocation Fees

I. Process

Before a builder or an individual begins construction of new property in the Township, they must complete an "Application for Wastewater Treatment Allocation" and remit payments to Lehigh County Authority and Lower Macungie Township. The fees are based upon the property type. The Application for Wastewater Treatment Allocation is manually completed by the requestor and physically brought into the Township's Permit Department. The Permits Coordinator or the Permits Clerk calculates the fees owed to the LCA and to the Township based on information that is pre-printed on the application form. The requestor remits two separate checks. The Permits Coordinator or the Permits Clerk processes the check payable to the Township through the point-of-sale terminal, enters the transaction in the cash register receipt system and generates a receipt for the fee paid to the Township. The Permits Coordinator or the Permits Clerk makes a copy of both checks. The Permits Coordinator or the Permits Clerk stamps the back of the Township's check with a restrictive endorsement and places the check in the cash drawer. The "customer" is provided with a receipt of the transaction.

The application is forward to the Projects & Contracts Manager for approval. Once approved, the Permits Coordinator or the Permits Clerk forwards the application, check payable to LCA and the check copies to the Receptionist/General Office Clerk (K. Molnar). The Receptionist/General Office Clerk reviews the application for accuracy and completeness and logs the application information into an excel-based spreadsheet. Information maintained on the spreadsheet includes the customer name, property address, development name, allocated EDU's and gallons, allocation date, property type and allocation number (a sequential number manually assigned by the Receptionist/General Office Clerk).

The applications and the checks payable to LCA are maintained in a file in the Director of Finance's office until they are physically delivered to the LCA on the 15th and 30th of each month by the Receptionist/General Office Clerk. The Receptionist/General Office Clerk does not obtain a receipt for or a verification of the checks delivered to the LCA. The LCA subsequently faxes approved applications back to the Receptionist/General Office Clerk who distributes copies of the approved applications to the property owner and the Permits Coordinator. A third copy of the application is filed.

II. Evaluation of Control Design

A. Authorization. Developers and other applicable builders are identified. Appropriate rates and charges are established.

Controls. Not applicable. The LCA establishes sewer allocation rates. The Township does not bill users for the tapping fees. The transaction is initiated by the builder or the property owner prior to the start of construction on the property.

B. Initiation and Recording. Fees applied are accurate. Cash receipts are properly recorded.

Controls. The Township uses pre-printed application forms that require the calculation of fees owed based upon the property type and expected usage. The completed application forms and fees calculated are reviewed for completeness and accuracy and approved by the Projects & Contracts Manager. RKL reviewed several completed application forms and recalculated the imposed fees noting the accuracy of the calculated fees and the proper approval. We also reviewed the supporting documentation including check copies and receipt copy. The Township

processes its portion of the fees through the cash drawer. The customer is provided with a receipt of the transaction. The cash drawer is balanced out weekly by the A/P Clerk.

Recommendations:

- The Township should revise the current allocation application to include a pre-printed sequential number. Usage of the application forms should be reconciled on a monthly basis. The Township should follow up on missing applications.
- Monies received should be deposited at the bank on the day received.
- The Township should balance the cash drawer on a daily basis.

C. Processing. All revenue items are reconciled and recorded.

Controls. Bank statements are reconciled on a monthly basis.

RKL discussed the processing procedures with the Receptionist/General Office Clerk. The Township does not maintain a subsidiary ledger to account for sewer allocation fees collected or to reconcile the sewer allocation revenue account. RKL reviewed the Excel-based spreadsheet maintained by the Receptionist/General Office Clerk.

Recommendations:

- The Township should maintain a subsidiary ledger of fees collected and reconcile revenue accounts on a monthly basis.
- Management should review revenue accounts in comparison to budget amounts on a monthly basis.
- Management should review and approve bank statement reconciliations on a monthly basis.
- The Township should requiring applicants to process the LCA portion of sewer allocation fees directly with the LCA.

D. Reporting. Transactions are accurately summarized and posted to the general ledger.

Controls. Cash receipt system is integrated with the general ledger. Foundations automatically posts receipts to the general ledger.

Recommendations:

- A subsidiary ledger should be maintained and reconciled to the general ledger monthly.
- Transaction activity in revenue accounts should be reviewed monthly.
- Internal financial statements should be compared to budgets and/or historical results on a monthly basis.
- Unusual items should be investigated by appropriate level of management.

E. Other.

Recommendations:

- The Township should implement procedures to ensure that checks payable to the LCA for sewer allocation fees are processed the day received by the Township.

Licenses and Permits

I. Process

The Township imposes fees for issuing licenses and permits. Such fees are initiated from the Permit Department. All transactions are recorded through a point-of-sale terminal and entered via the cash register receipt system by the Permits Coordinator or the Permits Clerk. The major sources of these revenues, associated general ledger account and current fee are set forth in the table below:

Electrical Licenses	01.321.200	\$ 60.00
Plumbing Licenses	01.321.300	60.00
Peddler Licenses	01.321.400	25.00
Junk Yard Licenses	01.321.500	70.00
Building Permits	01.360.100	30.00
Commercial Plan Review	01.360.410	250.00
Sale of Subdivision & Land Development	01.361.530	50.00
Sprinkler System Inspection	01.362.020	50.00
Fire Code Plan Review	01.362.021	250.00
Building Permits-Residential	01.362.100	30.00
Building Permits-Commercial	01.362.150	250.00
Electrical Permits	01.362.200	30.00
Plumbing Permits	01.362.300	30.00
Sewage Permits	01.362.400	30.00
Mechanical Permits	01.362.350	30.00
Zoning Permits	01.362.500	30.00
On-lot Grading Permits	01.362.600	130.00

When an individual requests a permit they are provided with a four-part permit. Upon completion, the Permit Department forwards it to the Zoning Office for approval. Once the individual's permit is approved, they are charged the appropriate fee and a permit number is assigned. When the Township collects payment, either the Permits Coordinator or the Permits Clerk process it through the cash drawer. The Permits Coordinator or the Permits Clerk must enter the appropriate information including check number and check amount before the cash drawer will open. The Permits Coordinator or the Permits Clerk stamp the back of the check with a restrictive endorsement and places the check in the drawer. The customer is provided with a receipt of the transaction.

The cash register is balanced out weekly and the A/P Clerk reconciles the cash in the drawer and posts the transactions to Foundations.

II. Evaluation of Control Design

A. Authorization. Appropriate rates and charges are established.

Controls. Approved fees are entered into the system. Fees are verified to ordinance.

RKL discussed the above procedures with Permits Coordinator. We reviewed the input screen and noted the name, fee and amount fields.

Recommendations:

- Periodic reviews of master fee file information for license and permit fees and general ledger account numbers should be performed by authorized management.
- The Township should use permit forms with pre-printed sequential numbers and periodically reconcile usage.

B. Initiation and Recording. Fee used is accurate.

Controls. Approved fees are entered into the system. Fees are verified to ordinance.

RKL discussed the above procedures with the Permits Coordinator. We reviewed the input screen and noted the name, fee and amount fields.

Recommendations:

- Periodic reviews of master fee file information for license and permit fees and general ledger account numbers should be performed by authorized management.
- The Township should use permit forms with pre-printed sequential numbers and periodically reconcile usage.
- The Township should balance the cash drawer on a daily basis.

C. Processing. All revenue items are reconciled and recorded.

Controls. Bank statements are reconciled on a monthly basis.

RKL discussed the processing procedures with the Permits Coordinator. RKL vouched significant revenue amounts and license and permit revenue through the Foundations system.

Recommendations:

- The Township should reconcile revenue accounts on a monthly basis.
- Management should review revenue accounts in comparison to budget amounts on a monthly basis.
- Management should review and approve bank statement reconciliations on a monthly basis.

D. Reporting. Transactions are accurately summarized and posted to the general ledger. Foundations automatically posts receipts to the general ledger.

Controls. Journal entries are approved prior to posting. Cash receipt system is integrated with the general ledger.

Recommendations:

- Transaction activity in revenue accounts should be reviewed monthly
- Subsidiary ledgers should be reconciled to the general ledger monthly.
- Internal financial statements should be compared to budgets and/or historical results on a monthly basis.
- Unusual items investigated by appropriate level of management.

TREASURY**Cash****I. Process**

The Township utilizes over 30 different bank accounts. The principal banking relationships are with Lafayette Bank, Commerce Bank and Pennsylvania Local Government Investment Trust ("PLGIT").

All checks require two signatures. Darryl Yothers, Treasurer, must sign all checks. One of three Board members (E. Keller Kline, Julianna Timmcke or William Spaide) must also sign with the Treasurer. Wire transfers may be initiated by the Director of Finance. PLGIT wire transfers must be approved by the Treasurer. The Director of Finance faxes a memo to the Treasurer for approval. Once this approval is obtained, the Director of Finance faxes the approved memo to Commerce Bank to initiate the transfer. Wire transfers from Commerce Bank must be approved by the Township Manager, Bruce Fosselman. The Director of Finance initiates the transfer on-line. The Township Manager must go on-line to approve the transfer. Wire transfers and disbursements are automatically posted to the Foundations system when entered.

The A/P Clerk prepares reconciliations of each bank account monthly typically within 7 to 10 days of the first of the month. She uses the bank reconciliation module provided with the Foundations system which identifies unreconciled differences. The A/P Clerk identifies the problem as either external, internal or software and takes appropriate action to resolve. The Director of Finance reviews and approves all bank reconciliations.

II. Evaluation of Control Design

A. Authorization. Cash disbursements made are properly authorized and related to legitimate purchases or expenses. All other forms of cash disbursements such as wire transfers, ACH, and check/debit cards are restricted to appropriate personnel.

Controls. Checks and supporting information are reviewed prior to signing process. Blank checks maintained in a secure place with access only granted to authorized personnel. Authorized limits for check signatories (including dual signatures) are defined and adhered to. Voided checks are defaced and maintained. Dual signatures required on wire transfers.

RKL discussed the above procedures with the Director of Finance and the A/P Clerk.

Recommendations:

- Physical control and mailing of checks and signatures obtained should be performed by individual without access to A/P module.
- Sequential order of checks (including voids) should be periodically accounted for by Supervisory personnel.
- The Board of Commissioners should periodically review and reauthorize bank and deposit limits.

B. Initiation and Recording. Cash disbursements are accurately recorded.

Controls. Information for checks is automatically obtained from the A/P system. The Township has processes in place to regularly reconcile bank statement activity to the general ledger. Bank reconciliations are reviewed and approved by the Director of Finance. Fundations will not allow an invoice number to be used more than once. If an invoice number is entered more than once, Fundations prevents the user from proceeding with the transaction and returns an error message indicating the number has already been used. The system will not allow a user to enter an invoice number twice. Invoices are stamped ""PAID"" once they have been paid.

RKL discussed the above procedures with the Director of Finance and the A/P Clerk. RKL performed walkthroughs of several A/P disbursements. We reviewed bank reconciliations and traced noted balances to the general ledger. We performed walkthroughs of several wire transfers noting proper approval and traced amounts to the general ledger.

Recommendations:

- Bank statements should be opened by someone independent of the reconciliation process.
- An analysis of key ratios and results should be compared to budget on a monthly basis.

C. Processing. Accounts payable records updated for all transactions.

Controls. Bank accounts are reconciled and reviewed periodically by independent or supervisory personnel

RKL discussed the above procedures with the Director of Finance and the A/P Clerk. RKL performed walkthroughs of several A/P disbursements, tracing disbursements to appropriate general ledger accounts. We reviewed bank reconciliations and traced noted balances to the general ledger.

Recommendations:

- Accounts payable listing and activity should be periodically reviewed by appropriate supervisory personnel.
- An analysis of key ratios and results should be compared to budget on a monthly basis.

D. Reporting. All cash transactions are properly recorded in the appropriate general ledger accounts.

Controls. Cash disbursement function within A/P is integrated with the general ledger so all postings are performed automatically. Bank accounts are reconciled and reviewed periodically by independent or supervisory personnel

RKL discussed the above procedures with the Director of Finance and the A/P Clerk. RKL performed walkthroughs of several A/P disbursements, tracing disbursements to appropriate general ledger accounts. We reviewed bank reconciliations and traced noted balances to the general ledger.

Recommendations:

- An analysis of key ratios and results should be compared to budget on a monthly basis.

E. Segregation of Duties

Recommendations:

- Bank statements are opened by an employee who is also responsible for preparing bank reconciliations. These duties should be segregated.
- Bank reconciliations are performed by the same employee who is responsible for balancing cash drawers, taking deposits to the bank and for the accounts payable function. Bank reconciliations should be prepared by an individual independent of these responsibilities.

Investments**I. Process**

The Board of Commissioners is authorized by statutes to invest the Township's funds as defined by the Township Code. The Board has authorized a number of banking institutions and has delegated the investment function to the Director of Finance. The Director of Finance records investment activity through manual journal entries. The A/P Clerk maintains manual subsidiary ledgers for all of the Township's investments. The investment function is not fully integrated with the Foundations system. The Director of Finance performs a monthly reconciliation between investment account statements received from third parties, the manual subsidiary ledgers and the general ledger.

II. Evaluation of Control Design

A. Authorization. Short-term investment transactions are properly approved and authorized.

Controls. Investment policies exist and are adhered to. Investment policies include list of approved brokers and investment types.

RKL discussed the above procedures with the Township Manager and the Director of Finance. We reviewed the Township's Investment Policy.

B. Initiation and Recording. Investment transactions are properly recorded in the accounting system.

Controls. Bank statements are reconciled and reviewed by appropriate supervisory personnel

RKL discussed the above procedures with the Director of Finance and the A/P Clerk. We reviewed bank reconciliations and traced noted balances to the general ledger.

Recommendations:

- The Director of Finance should review and evaluate the Township's compliance with authorized depositories and trustees, insurance and collateralization requirements, and maintenance of bonding.

C. Processing. Investment transactions are processed properly.

Controls. Balances per G/L are reconciled to bank statements and/or broker statements.

RKL discussed the above procedures with the Director of Finance and the A/P Clerk. We reviewed bank reconciliations and traced noted balances to the general ledger.

Recommendations:

- Accounts payable listing and activity should be periodically reviewed by appropriate supervisory personnel.
- An analysis of key ratios and results should be compared to budget on a monthly basis.

D. Reporting. Investments are properly classified in the general ledger and financial statements.

Controls. Separate general ledger accounts have been set up for short term investment accounts. Bank statements and broker statements are reconciled and reviewed by appropriate supervisory personnel. RKL discussed the above procedures with the Director of Finance. We reviewed the general ledger noting accounts for short-term investments.

Debt

I. Process

The Township's debt consists solely of bonds issued in 2001. The bank account for this bond issue is with M & T Bank. The Director of Finance is responsible for posting two manual journal entries to record interest. The A/P Clerk reconciles the bank accounts monthly. The Director of Finance reviews and approves the reconciliation.

II. Evaluation of Control Design

A. Authorization. All new debt agreements and debt extinguishments are authorized in accordance with the entity's policies and procedures.

Controls. All new debt agreements must be authorized by the Board of Commissioners.

B. Initiation and Recording. New debt, debt extinguishments and debt payment transactions are initiated in accordance with the entity's policies and procedures. Debt transaction information is properly recorded in the accounting system by fund.

Controls. The Director of Finance reviews debt statements from the bank on a monthly basis.

RKL discussed the above procedures with the Director of Finance and the A/P Clerk. We reviewed bank reconciliations and traced noted balances to the general ledger. Recording of initial debt is subject to review by appropriate supervisory personnel.

Recommendations:

- Amortization schedules should be reconciled to general ledger on semi-annual basis.

C. Processing. All proceeds from and payments made on debt obligations are properly entered in the accounting system on both fund level and government-wide level.

Controls. All proceeds from and payments made on debt obligations are properly entered in the accounting system on both fund level and government-wide level.

RKL discussed the above procedures with the Director of Finance. We reviewed general ledger activity.

D. Reporting. All approved debt obligations and interest expense are properly recorded in the appropriate general ledger accounts.

Controls. A standard journal entry is used to record interest expense.

RKL discussed the above procedures with the Director of Finance. We reviewed the general ledger noting accounts for debt.

Recommendations:

- The Director of Finance should review general ledger accounts on a monthly basis for reasonableness.
- The Director of Finance should compare interest expense to budget on a monthly basis. Variances should be investigated and explained.

PAYROLL

I. Process

The Board of Commissioners authorizes employment and termination decisions based on recommendations from Department Heads. Upon Board approval, background checks are conducted and potential employees are sent an offer letter. Public Works employees are required to pass a drug test and a physical examination. The Township does not have formal termination procedures for non-union employees. However, in all cases the Township consults the Board and the Township's attorney before taking termination action. The Township's contract with the Union addresses termination of union employees. Salary increases are recommended by Managers and are approved by the Board of Commissioners.

The Township is on a two-week pay cycle. All employees are required to complete a bi-weekly time sheet and submit their completed and approved timesheet to the A/P Clerk on the Monday following the end of the pay period. A Supervisor or Department Heads must approve all time sheets. The A/P Clerk organizes the time sheets alphabetically by last name and inputs the information in an Access database, that tracks employees' overtime, vacation, sick time and call-back time. She also inputs each employee's hours into AD Computer system. The A/P Clerk verifies that the information entered agrees with data entered in the Access program. She then transmits this information to AD Computer. On the Wednesday of the pay-week, an AD Computer messenger delivers payroll reports and payroll checks to the Township in a sealed envelope. The A/P Clerk opens the envelope, examines the contents, places the checks in envelopes for distribution and prepares a journal entry based on information in the "Labor Distribution Report". The Director of Finance, Public Works Director and the Community Center Director distribute the payroll checks to employees in their departments. The A/P Clerk forwards the reports, checks and journal entry to the Director of Finance. The Director of Finance reviews the payroll reports and the journal entry. She transfers the appropriate amount from the general bank account to the payroll bank account via telephone. Any discrepancies are brought to the attention of the Director of Finance who resolves the identified issue.

The A/P Clerk inputs salary changes and other account maintenance into the AD Computer application. Salary changes are based on authorization as noted in the minutes of Board of Commissioner's meetings and change of address/account maintenance forms is completed by employees.

The A/P Clerk reconciles the payroll checking account on a monthly basis. Because AD Computer prepares the payroll checks, each check is not recorded into the accounting system. The A/P Clerk enters any outstanding checks as a monthly reconciling item. These entries are supported with documentation showing the composition of the outstanding checks.

Payroll records are maintained in a filing cabinet in a locked office. The Township Manager, the Director of Finance and the A/P Clerk have access to those records.

II. Evaluation of Control Design

A. Authorization. Employees are hired, terminated and compensated in accordance with the Township's personnel policies and procedures.

Controls. All new employees are required to complete and sign an employment application form. A complete personnel file is maintained for each employee in a locked filing cabinet in the Director of Finance's office.

RKL discussed the above procedures with the Director of Finance and the A/P Clerk. We reviewed payroll files. We reviewed Board of Commissioners' meeting minutes noting instances of salary change approvals.

Recommendations:

- All personnel file changes should be authorized by a supervisor.
- Terminated employees should be formally communicated to the A/P Clerk to ensure the employee is removed from the payroll system.
- The Township should request employee file change reports from AD Computer. An appropriate supervisor should formally review and approve these reports.

B. Initiation and Recording. Payroll transactions are initiated in accordance with the entity's personnel policies and procedures. All payroll transactions are properly recorded in the payroll system.

Controls. Employees complete and sign their time sheets. These time cards are reviewed and approved by supervisory personnel. Payroll register details are reviewed by the Director of Finance to ensure employees are not paid after departure. Manual input controls exist to ensure that entry of payroll information is complete and accurate.

RKL discussed the above procedures with the Director of Finance and the A/P Clerk. We reviewed employee time sheets noting supervisory approval. We reviewed the reconciliation performed by the A/P Clerk between the Access database system and the AD Computer system.

Recommendations:

- All personnel file changes should be authorized by a supervisor.

C. Processing. Payroll transactions are accurately processed by the payroll system.

Controls. The payroll software used is a standard package from a reputable software house.

RKL discussed the above procedures with the Director of Finance and the A/P Clerk. We reviewed payroll reports generated by AD Computer.

D. Reporting. Payroll reports are accurate and payroll transactions are properly classified.

Controls. A payment register is maintained of all employees detailing salary or wages and other employee benefits. This payment register is reviewed by the Director of Finance for reasonableness and unusual items.

RKL discussed the above procedures with the Director of Finance. We reviewed the general ledger noting accounts for debt.

Recommendations:

- Payroll expenses should be compared to budget monthly and significant differences identified and explained.

- Employee earnings and payroll control accounts should be reconciled to the general ledger on a monthly basis.
- Payroll change reports should be generated for all employee file changes and reviewed by appropriate supervisory personnel.

E. Safeguarding of Assets. Access to personnel files and records is restricted to authorized personnel and access to ACH and check processing is restricted.

Controls. Access to personnel files is restricted and employees' privacy is protected. Payroll is prepared by an external 3rd party processor that is independent of time card approval, check signing and distribution. The distribution of payroll checks function is segregated from other payroll functions.

RKL discussed the above procedures with the A/P Clerk and the Director of Finance.

Recommendations:

- The payroll bank account should be reconciled by an employee who is not involved in the payroll process.
- The Township should consider mandatory ACH processing of all payroll transactions.

F. Segregation of Duties.

Recommendations:

- Payroll checks and reports should be delivered to and opened by the Director of Finance.

FINANCIAL REPORTING

Financial Reporting Close Process

General journal entries can be posted by the A/P Clerk, the Administrative Assistant, and the Director of Finance. During 2008, the Director of Finance implemented a general journal entry form. This form requires the preparer to describe the journal entry, sign-off as preparer and obtain the signature of a reviewer. All supporting documentation is attached to the journal entry form and all forms are filed in date order in a binder that is maintained in the Administrative Assistant's office. The Township Manager reviews and approves entries prepared by the Director of Finance.

The Director of Finance is a CPA who gained experience in both public and private practice. One member of the Board of Commissioners is a CPA. On an ongoing basis, the Director of Finance assesses the competencies of accounting staff and training received over the year, and summarizes findings to the Board of Commissioners.

Recommendation:

- The Township should implement a monthly general ledger closing process including reconciliations, monthly financial statements and financial analyses of interim financial statements.