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September 20, 2011

Honorable Mayor and Members of the
Board of Commissioners
City of Gallaway
P. O. Box 168
Gallaway, TN 38036

Gentlemen:

We have completed our investigative audit of selected records of the City of Gallaway. The audit focused on the period January 1, 2011, through June 30, 2011. The investigative audit concentrated on collections for the gas and water funds and a review of disbursements from those accounts and the general fund. However, when warranted, this scope was expanded.

We acknowledge the efforts of municipal officials to assist in our audit and correct the deficiencies as noted in this letter.

Our investigative audit revealed the following deficiencies:

1. We noted that the accounting system did not provide a reliable total of utility accounts receivable. Separate inquiries of the gas utility accounts receivable, made minutes apart, produced totals differing by more than $100,000. We have been informed by municipal officials that the accounts receivable balance must be manually produced. In addition, the natural gas utility does not appear to be self-supporting. We noted that the general fund paid certain expenses on behalf of the natural gas fund, including payroll expenses; however, the natural gas fund did not reimburse the general fund for these payments. We acknowledge the efforts of municipal officials to identify active utility accounts which have not been included in city account records.

   The *Internal Control and Compliance Manual for Tennessee Municipalities*, page 33, states that "Municipal officials should ensure that a management level employee periodically reviews … bank statements and the related reconciliations to determine that they are accurate and all activity is authorized and properly recorded."

2. Our examination revealed that adjustments were routinely recorded by municipal employees who were also responsible for making collections, recording collections, and preparing deposits. Since February 2011, adjustments have been reviewed by the city manager or the public works director. However, the list of adjustments reviewed was produced by the person making the adjustments and was not reconciled with the total amount of adjustments entered into the accounting system. Adjustments for the gas fund totaled $25,235[1] for the period of January 1, 2010, through December 31, 2010.

   The *Internal Control and Compliance Manual for Tennessee Municipalities*, page 57, states that

   > Municipal officials should ensure that charges disputed by customers are investigated and adjustments are approved, in accordance with the municipality's policy, by someone other than the bookkeeper handling receipt and payment records.
   >
   > NOTE: Adjustments should never be made by the employee who collects <u>or</u> posts the accounts paid. If the municipality utilizes a computer system, the employee who collects <u>or</u> posts should not have access to that portion of the computer system that allows adjustments.

   The *Internal Control and Compliance Manual for Tennessee Municipalities*, page 32, further states, "Municipal officials should separate duties of employees so that no one person has control over a complete transaction from beginning to end."

3. Our examination found that the city's computerized utility billing and utility collections system was separate from the general ledger accounting system. As a result, city employees were required to independently record the billing and collection information to the general ledger accounting system to ensure accurate accounting information. Our review revealed that office staff was not performing those procedures and, as a result, the general ledger accounts were not accurate. In addition, we noted that office staff did not regularly reconcile the utilities' accounts

[1] The entire accounts receivable for the gas fund were $36,873 as of June 30, 2010, according to the City of Gallaway's audited financial statements.

receivable[2]. During the course of our audit, we noted actions taken by municipal officials to address these issues.

The *Internal Control and Compliance Manual for Tennessee Municipalities*, pages 57-58, state that "Municipal officials should ensure that … the total amount of unpaid individual accounts on the utility billing sheet is reconciled to the applicable general ledger account total at the end of each month." The manual also describes additional procedures to be performed if the billing system is not integrated into the accounting system.

4. Finally, our review found that city employees had used a vehicle seized and forfeited to the city pursuant to Section 53-11-201, *Tennessee Code Annotated*, for activity related to the city's utility funds. State law prohibits the use of those forfeited vehicles for anything other than drug enforcement purposes.

The mayor and members of the board of commissioners should take immediate action to correct these deficiencies. If you have any questions or need additional information, please contact me.

Very truly yours,

Dennis F. Dycus, CPA, CFE, Director
Division of Municipal Audit

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[2] It should be noted that the city's information system did not produce sufficient reliable information to perform reconciliations in a timely manner