



CITY AUDITOR'S OFFICE

Cash Handling — Fiscal Year 2011

June 2, 2011

AUDIT REPORT NO. 1114

CITY COUNCIL

Mayor W.J. "Jim" Lane

Lisa Borowsky

Suzanne Klapp

Vice Mayor Robert Littlefield

Ron McCullagh

Linda Milhaven

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June 2, 2011

Honorable Mayor and Members of the City Council:

Enclosed is the audit report, *Cash Handling - Fiscal Year 2011*. This audit consisted of conducting unannounced cash handling audits at eight of the City's more than 45 cash handling locations. The largest cash handling location, the Remittance Processing Program, was excluded from this audit as it was the subject of a separate audit (Audit Report No. 1110). In addition to reviewing cash handling of the day-to-day transactions, we also reviewed the five petty cash and seven change funds held at these eight locations.

Overall, City staff at the locations audited are appropriately accounting for and handling cash. However, improvements can be made at some of the audited locations to help prevent errors or irregularities, or make the detection of discrepancies easier. Additionally, cash handling locations that receive payments by mail should consider using the City's Remittance Processing program, and the cash handling administrative regulation can be clarified.

If you need additional information or have any questions, please contact me at (480) 312-7867.

Sincerely,

A handwritten signature in cursive script that reads "Sharron Walker".

Sharron Walker, CPA, CFE
City Auditor

Audit Team:

Kyla Anderson, Sr. Auditor
Lee Pettit, Sr. Auditor
Erika Keel, Auditor

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EXECUTIVE SUMMARY

This audit of *Cash Handling* was included on the Council-approved FY 2010/11 Audit Plan to conduct unannounced audits of selected cash handling locations. The term “cash handling” encompasses cash, check or electronic forms of tender.

City staff at various locations collects almost \$85 million during the course of a fiscal year. This amount excludes receipts handled by the City’s centralized Remittance Processing Program which processes the majority of customer mail-in and electronic payments. Remittance Processing was separately audited this year (Audit Report No. 1110).

Eight locations were selected from the more than 45 cash handling sites around the City. The locations receive payments for pool and recreation fees, library and court fines, merchandise sales, licenses, and other fees or services. Check payments are about 82% of the total received, with cash and electronic (credit/debit) payments comprising the rest. In addition, we reviewed the accountability and controls for five petty cash and seven change funds at these same locations.

Generally, City staff at these eight locations are appropriately accounting for and handling cash. Some of the locations can improve certain aspects of their cash handling practices to help prevent errors or irregularities, or make the detection of any discrepancies easier. In addition, efficiencies may be gained by increased use of the City’s centralized Remittance Processing to handle additional mail-in payments, and *Administrative Regulation 268—Cash Handling* can be clarified.

As each audit was completed, we provided specific recommendations to Division management for the location. The overall findings and recommendations for the eight locations are summarized in this report.

BACKGROUND

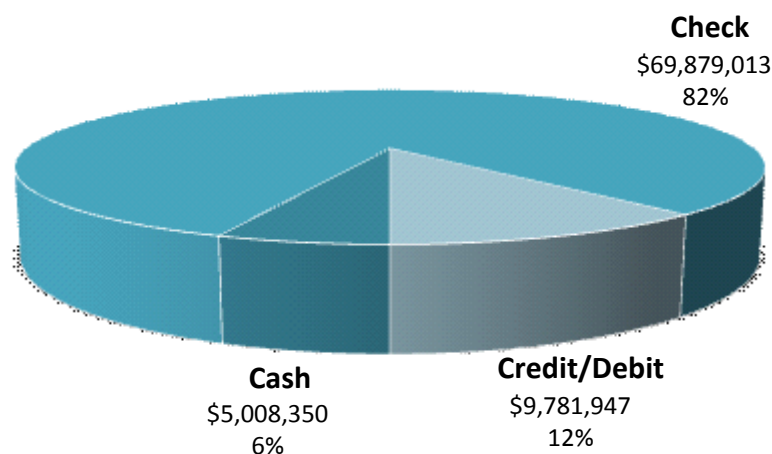
The term '*cash handling*' is used to encompass the controls and processes accounting for and safeguarding all negotiable instruments, whether in cash, check or electronic form of tender. In fiscal year 2009/10, staff throughout the City collected approximately \$84.7 million for various fines, fees, services, and products. This amount excludes payments received through the City's online or automated telephone systems or the Remittance Processing program. The Remittance Processing program, which processes about 78% of the City's mailed-in and electronic customer payments, was also recently audited (Audit Report No. 1110).

Asset misappropriation is the most common type of occupational fraud. Asset misappropriation includes theft of cash receipts, cash on hand, and inventory.

SOURCE: Association of Certified Fraud Examiners, *2010 Report to the Nation on Occupational Fraud and Abuse*.

As shown in Figure 1, the \$84.7 million consisted of about \$69.9 million in check form, \$9.8 million through electronic credit or debit transactions and another \$5.0 million in cash payments.

Figure 1. Receipts by Type*
FY 2009/10



* These amounts exclude transactions handled by Remittance Processing.

Source: Auditor analysis of FY 2009/10 summary iNovah and CLASS deposit reports.

The City's Customer Service offices, Court, and Development Services receive the greatest proportion, about 87%, of these monies.

OBJECTIVE, SCOPE AND METHODOLOGY

An audit of *Cash Handling*, including unannounced audits of various cash handling locations, was included in the FY 2010/11 Audit Plan approved by the City Council. The primary audit objective was to determine accountability for the City's cash handling, including compliance with related Administrative Regulations (AR) 268—*Cash Handling* and AR 270—*Petty Cash*.

For this fiscal year, we conducted unannounced cash counts at the following eight locations:

Location	Department	Division
<i>Arabian Library</i>	Library Systems	Community Service
<i>Civic Center Library</i>	Library Systems	Community Services
<i>Water Services Administration</i>	Water Services	Water Resources
<i>Scottsdale City Court</i>	City Court	City Court
<i>Club SAR</i>	Parks & Recreation	Community Services
<i>Scottsdale Sports Complex</i>	Parks & Recreation	Community Services
<i>Airport</i>	Aviation	Community & Economic Development
<i>WestWorld</i>	WestWorld	Community & Economic Development

Employees at more than 45 locations throughout the City handle cash and other negotiable instruments. Therefore, we selected locations based upon factors such as deposit volume and length of time since their last cash handling audit.

In addition to being accountable for payments received, cash-handling locations usually have a small change fund and some have petty cash funds for making small dollar purchases. During the unannounced cash counts, we also reviewed seven change funds and five petty cash funds.

As part of each unannounced audit, we:

- Counted all cash on hand (including cash, checks, and debit/credit payments) and reconciled to transaction records.
- Verified that change and petty cash funds balanced to the amounts approved by Finance & Accounting.
- Compared the location's written cash handling procedures to City AR requirements.
- Interviewed management and staff regarding procedures and reconciliations.
- Evaluated the design and effectiveness of cash handling controls.

Generally, City staff at the locations reviewed are appropriately accounting for and handling cash. Some of the locations can improve certain aspects of their cash handling practices to help prevent errors or irregularities, or make the detection of any discrepancies easier. In addition, efficiencies may be gained by increased use of the City's centralized Remittance Processing program to handle additional mail-in payments, and AR 268 can be clarified.

We conducted this audit in accordance with generally accepted government auditing standards as required by Article III, Scottsdale Revised Code, §2-117 et seq. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Audit work took place from August 2010 through May 2011, with Kyla Anderson, Lee Pettit, and Erika Keel conducting the work.

FINDINGS AND ANALYSIS

Some City cash handling locations can improve current practices to help prevent errors or irregularities or make their detection easier. Additional efficiencies may be gained by increasing use of Remittance Processing. Also, *Administrative Regulation (AR) 268—Cash Handling* requirements can be clarified. While this report summarizes the overall audit results, management was provided with more detailed information to facilitate addressing the controls in their specific areas.

1. Improving controls at some locations could help prevent errors or irregularities or make their detection easier.

- A. At two City locations, payment for donated and resale goods can be made through an 'honor box,' where patrons place cash or checks into an unattended locked box. As a result of this practice, sales records are not generated and customers are not given a receipt for their purchases. Because there are no sales records as there would be with a cash register or point of sale system, it is more difficult to ensure all money collected is subsequently deposited into the City's bank account. Additionally, inventory cannot be monitored for shrinkage. As a compensating control for the lack of sales records, the on-site staff reported that the honor boxes are always opened and counted in dual custody; however, there was no documentation to show this practice is being followed.
- B. At most cash handling locations, manual receipts are available that can be hand-written when the cash register or point of sale system is inoperable. In addition, some locations use manual receipts to facilitate customer service, such as beer permits at City parks and US Customs User Fee Billing forms at the Airport. Manual receipts are allowed to be used if they are prenumbered and regularly reviewed. An independent review can ensure all receipts have been recorded in the accounting system and deposited with the City's bank, and any missing or voided receipts are explained. However, at four locations the manual receipts were not being monitored for misuse, and one location used manual receipts that were not prenumbered.
- C. Perpetual inventory records or periodic inventory counts together with sales and ordering records can be used to detect inventory shrinkage. Four cash handling locations that sell or rent merchandise did not conduct or did not document conducting regular inventory counts.

Recommendation:

Division management should ensure that cash handling best practices and City administrative regulations are followed. Specifically, management should:

- A. Ensure that sales of City merchandise are recorded through a cash register or point of sale system to establish accountability. Honor boxes for sales of donated items should be opened and monies counted in dual custody. Responsibility for the dual custody count should be documented by having the two employees sign and date the

daily cash log.

- B. Ensure the numerical sequence of all manual receipts can be accounted for, and any missing and voided receipts can be explained.
- C. If the location sells or rents merchandise, ensure that staff periodically conducts an inventory count, and then reconciles sales and ordering records with merchandise on hand.

2. Based on usage, some cash fund amounts could be decreased.

Cash kept on hand for use as change or petty cash funds should be a minimal amount, designed to meet business needs, safeguard City funds and lessen the risk to cash-handling employees. Based on the reimbursement history for each of the five audited petty cash funds, the cash balances of four funds appeared to be higher than necessary. However, none of the five petty cash balances exceeded \$500.

Recommendation:

Management should review the historical use of petty cash funds and any known changes in the business environment and adjust the petty cash or change funds as appropriate.

3. At some locations, cash handling regulations were not being followed.

The following occurrences of non-compliance with *AR 268—Cash Handling*, were noted at various locations:

- Some individuals at two locations had both the combination and access to the key for dual custody safes. Instead, these duties should be separated to require two employees to be present to open the safe.
- The safe combination was not changed at one location when staff with the combination left the City's employ.
- At one location, the amounts charged for merchandise were not displayed properly for customers and staff.
- Nightly and/or end-of-shift balancing was not being done in dual custody at four locations, or evidence was not available to ensure this practice was followed.
- Staff at one location regularly took cash off-site to obtain from the City's bank smaller bill denominations for change.
- Three locations did not have a copy of the *Guide to US Paper Money*.

Recommendation:

Management at all cash handling locations should periodically review their staff's cash handling practices to ensure AR requirements are being followed.

4. Use of Remittance Processing and clarification of AR 268 could improve cash handling.

- A. Some locations throughout the City receive mail-in payments directly rather than having them processed through the centralized Remittance Processing area. To increase the segregation of duties between maintaining customer accounts and handling payments, to eliminate the onsite workload of processing mail-in payments, and to more efficiently use existing City resources, management should consider directing mail-in payments to Remittance Processing. Any associated paperwork, such as an account payment stub, could then be forwarded in electronic or paper form by Remittance Processing staff to the appropriate department as needed.
- B. Updates to AR 268—*Cash Handling* would clarify and/or improve controls:
- The AR states: “All cash overages/shortages must be closely monitored by departmental management and tied back into the employee’s performance evaluation.” In addition to balancing discrepancies, misappropriation of cash is commonly indicated through undocumented or unauthorized refunds and/or excessive voids. To improve the likelihood of detecting theft or loss, AR 268 should also require department management to track and monitor in the daily balancing documents the number and amount of refunds and/or voids processed by each cashier. Revising the over/short form to also require void and refund totals would allow Finance & Accounting to follow up with department management on unusual refund/void activity.
 - The AR requires documentation for phoned-in credit card transactions to include the name and contact phone number of the person requesting the charge. Consideration should be given to requiring the credit card security code and elements of the billing address when a credit card number is manually entered rather than the card being swiped. To accommodate this increased security, the credit card machines would need to be updated.
 - The AR states that access to a cash drawer must be restricted to one employee, or separate tills or moneybags must be used. This control would be strengthened by specifying that the tills or moneybags must be kept locked.
 - The AR states that petty cash funds should be counted on any day the funds are used; however there is no evidence that this is being done. Requiring petty cashiers to maintain a log that they would sign and date to evidence petty cash counts would help ensure the counts are performed.
 - The City accepts debit cards as a form of payment, processing them as credit transactions; however the AR only refers to credit card payments. For ease of understanding, AR statements regarding credit card transactions could be listed as “debit/credit card.”
 - The AR states the receipting department’s management is responsible for “Rotating cash handling employees on a regular basis and/or enforcing a vacation of at least 5 consecutive working days per year to ensure no irregularities are detected.” Removing “no” from this statement would clarify that the purpose of this policy is to “detect” irregularities.
 - The AR requires signs to be posted in public areas to restrict access to

appropriate city staff only. The AR could be clarified to state that the signs are to restrict public access to *cash handling* areas.

Recommendation:

Finance & Accounting should:

- A. In conjunction with department management, evaluate the feasibility of directing mail-in payments to Remittance Processing.
- B. Consider revising AR 268 to clarify or improve required controls.

MANAGEMENT RESPONSE

1. Community Services - Libraries

MANAGEMENT RESPONSE:

The following controls and consistency of practice have been implemented based upon audit recommendations:

- All libraries have implemented a new daily cash custody form for funds removed from the honor box, which is signed off in dual custody. Limited staff are assigned to remove funds from the honor box.
- The value of merchandise purchased for resale is minimal compared to the total amount of funds received through the honor box. Therefore, we will continue to accept payment for merchandise through the honor box.
- No staff member has access to both the key and combination for dual custody safes.
- Daily balancing documents will have two signatures indicating that cash handling activities were performed in dual custody. All cash overages/shortages are closely monitored at the management level and tied back to the employee's performance evaluation.

RESPONSIBLE PARTY: Rita Hamilton, Library Director

2. Community Services – Parks & Recreation

MANAGEMENT RESPONSE:

Management agrees with the audit findings relative to controlling inventory, safeguarding manual receipts, and decreasing the risk for loss of funds.

- An inventory control process has been established with a monthly check of inventory on hand and quarterly comparison to sales reports. Previously, we conducted a semiannual physical inventory count.
- Staff now has access to only one receipt book, with a second book locked in the safe for backup and the third book returned to Accounting. The manual receipts are accounted for daily. Also, staff has been trained in the proper cash handling procedure for when the CLASS system is unavailable.
- Price lists and *Guide to US Paper Money* are properly displayed at the cashier's desk. The price list is also posted near the customer entrance.
- Balancing is done at the end of each shift and reviewed, and documentation retained.
- The safe combination has been changed and will be changed whenever an employee leaves.

RESPONSIBLE PARTY: Jan Cameron, Parks & Recreation Director

3. City Court

MANAGEMENT RESPONSE:

City Court management requested a decrease of the petty cash fund and an increase in the change fund to ensure each fund is used for its stated purpose. Additionally, a new Court procedure was created to define each fund and its respective uses. The Court now uses the change service via the City's bank. Court procedures were also created to define which situations qualify as an emergency that justifies staff transporting cash to the bank to obtain change.

RESPONSIBLE PARTY: B. Monte Morgan, Presiding Judge

4. Finance & Accounting

MANAGEMENT RESPONSE:

The exceptions granted are related to staff reductions that made it very difficult to completely adhere to the administrative guideline. Senior management will be reminded that their involvement in monitoring this financial activity is an essential component of the exception that was allowed. Internal control can provide reasonable, not absolute, assurance that the objectives of our organization will be met. In addition, the concept of reasonable assurance implies a high degree of assurance, constrained by the costs and benefits of establishing incremental control procedures.

- AR 268 will be updated as follows:
 - o As other updates are needed, use of the term 'credit card' will be replaced with 'debit/credit card' where applicable.
 - o The word 'no' will be removed from §3 *Responsibilities* so that it is clear the purpose of the policy is to 'detect' irregularities.
 - o An administrative procedure will be implemented to ensure management reviews void and refund totals.
 - o The AR will be updated to recommend that tills and/or moneybags be kept locked, subject to available funding for needed replacements.
 - o The AR will be updated to add a requirement for a petty cash log to evidence that petty cash is counted on any day the fund is used.
 - o Information Systems will update the AR to maintain compliance with PCI/DSS standards. Modifications made will address the issues noted in the audit.
 - o The AR will be clarified by stating that the signs are to deter public access to cash handling areas.

RESPONSIBLE PARTY: Jeff Nichols, Accounting Director

5. Water Resources

MANAGEMENT RESPONSE:

Water Resources Management concurs with the recommendation to reduce the authorized petty cash fund to lessen the risk to the cash-handling employees.

RESPONSIBLE PARTY: Kathy Mutschler, Office Coordination Manager

6. Community & Economic Development - Aviation

MANAGEMENT RESPONSE:

- The US Customs User Fee Billings form was recently redesigned to clarify that it is not a receipt for payment. Aviation management will seek an exception from Finance & Accounting for the AR 268 requirement to use prenumbered manual receipts. Aviation management will periodically compare the US Customs list to recorded transactions to ensure completeness and will also review numerical sequences of manual receipts to ensure all numbered receipts are accounted for.
- Aviation staff will evaluate the recommendation to periodically reconcile inventory and payments received.
- Due to staff limitations, it is not always feasible for a second employee to review the cashiering documents the same day as processed. In those rare instances, the documentation is reviewed as soon as possible by an independent second party and signed off on.
- A guide to US paper money security features has been obtained.
- Although the Aviation petty cash fund is used on an infrequent basis, the need exists to keep the fund at the current level. The nature of an airport lends itself to the possibility there may be times when it is important to have sufficient petty cash on hand to deal with emergency situations.
- Management discussed the feasibility of mail-in payments being processed through the City's remittance processing area with Finance & Accounting, and Remittance Processing will begin processing mail-in payments in the near future.

RESPONSIBLE PARTY: Gary Mascaro, Aviation Director

7. Community & Economic Development - WestWorld

MANAGEMENT RESPONSE:

- We will institute a weekly review by a supervisor and a monthly review by a manager to ensure sequential use of manual receipts.
- WestWorld management will maintain the petty cash fund at the current level.
- WestWorld accounts receivable must be mailed to WestWorld for deposit and accuracy of deposit and account reconciliation. To segregate this duty makes the accounts more cumbersome and harder to reconcile.

RESPONSIBLE PARTY: Brian Dygert, WestWorld General Manager

City Auditor's Office

4021 N. 75th St., Suite 105
Scottsdale, Arizona 85251
(480) 312-7756

www.ScottsdaleAZ.gov/departments/City_Auditor

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