



A REPORT  
TO THE  
ARIZONA LEGISLATURE

Financial Audit Division

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Report on Internal Control and Compliance

# Navajo County

Year Ended June 30, 2013

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**Debra K. Davenport**  
Auditor General

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Navajo County  
Report on Internal Control and Compliance  
Year Ended June 30, 2013

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DEBRA K. DAVENPORT, CPA  
AUDITOR GENERAL

STATE OF ARIZONA  
OFFICE OF THE  
AUDITOR GENERAL

MELANIE M. CHESNEY  
DEPUTY AUDITOR GENERAL

**Independent Auditors' Report on Internal Control over Financial Reporting  
and on Compliance and Other Matters Based on an Audit of Basic Financial  
Statements Performed in Accordance with *Government Auditing Standards***

Members of the Arizona State Legislature

The Board of Supervisors of  
Navajo County, Arizona

We have audited, in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the governmental activities, each major fund, and aggregate remaining fund information of Navajo County as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the County's basic financial statements, and have issued our report thereon dated December 17, 2013.

**Internal Control over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the County's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the basic financial statements, but not for the purpose of expressing an opinion on the effectiveness of the County's internal control. Accordingly, we do not express an opinion on the effectiveness of the County's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the County's basic financial statements will not be prevented, or detected and corrected, on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies, and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify certain deficiencies in internal control described in the accompanying Schedule of Findings and Recommendations as items 2013-01, 2013-02, 2013-03, and 2013-04 that we consider to be significant deficiencies.

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the County's basic financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

## **Navajo County Response to Findings**

Navajo County's responses to the findings identified in our audit are presented on pages 7 through 9. The County's responses were not subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we express no opinion on them.

## **Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the County's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the County's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Jay Zsorey, CPA  
Financial Audit Director

December 17, 2013

Navajo County  
Schedule of Findings and Recommendations  
Year Ended June 30, 2013

Financial Statement Findings

**2013-01**

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**The County should improve its controls over infrastructure asset reporting**

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Criteria: The County should have effective policies and procedures to ensure that infrastructure assets are properly recorded and reported in accordance with generally accepted accounting principles (GAAP).

Condition and context: The County routinely performed road-resurfacing projects as part of normal road maintenance. However, auditors found that prior and current-year costs associated with road maintenance projects were capitalized incorrectly since the road's service utility, capacity, or useful life was not extended. Specifically, auditors noted approximately \$6.5 million of resurfacing costs capitalized in prior years and \$898,863 of resurfacing costs capitalized in the current year.

Effect: Because of the incorrectly capitalized maintenance costs in the current and prior years, the County overstated its year-end capital asset balances. However, after auditors found the errors, the County restated its beginning net position by approximately \$6.5 million to correct its capital asset balances for prior years and reduced its current-year capital asset additions by \$898,863.

Cause: The County lacked sufficient internal control policies and procedures over its infrastructure asset management, which led to the improper capitalization of maintenance costs.

Recommendation: To strengthen controls over infrastructure asset reporting, the County should:

- Develop and implement written policies and procedures describing the capitalization policy for infrastructure assets in accordance with GAAP.
- Ensure that policies and procedures are effectively communicated to county departments.

**2013-02**

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**The County should continue to strengthen controls over granting access to and monitoring of its information systems**

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Criteria: The County's information systems include its general ledger system, the source of the financial statements, and other systems used by the County Treasurer's and the County School Superintendent's Offices. Therefore, the County should have effective system access controls defined by detailed policies and procedures to prevent and detect unauthorized use, damage, loss, or modification of systems and data, including confidential and sensitive information.

Condition and context: The County did not adequately control logical access to its information systems during the year. Specifically, the County did not use or maintain access request forms to grant users access

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Year Ended June 30, 2013

and could not show that user rights were removed in a timely manner for terminated employees. In addition, the County did not have procedures in place for monitoring system activities, including those of users with elevated system access.

Effect: There is an increased risk of theft, manipulation, or misuse of financial and confidential or sensitive information by unauthorized users or users whose access was not adequately controlled, restricted, monitored, or terminated.

Cause: The County did not follow its policies and procedures for granting user access rights. In addition, the County has not developed detailed policies and procedures for actively monitoring system activity and removing user access rights for terminated employees.

Recommendation: To help prevent and detect unauthorized access to its systems and data, including confidential and sensitive information, the County should:

- Ensure that employees follow county policies and procedures for granting user access rights and maintaining applicable documentation.
- Develop and implement detailed policies and procedures for terminating user access rights in a timely manner and maintaining the necessary documentation.
- Develop and implement detailed policies and procedures for monitoring system activities, including those of users with elevated system access.

This finding is similar to a prior-year finding.

**2013-03**

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**The County should continue to develop a complete and tested disaster recovery plan for its information systems**

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Criteria: To help ensure that the County can continue to process transactions and that data is not lost in the event of a system or equipment failure or other interruption, the County should have a complete and tested disaster recovery plan for its information systems.

Condition and context: The County's disaster recovery plan has not been updated to include current information, such as emergency contacts, hardware configurations, and the priority of the systems, information, and functions to be restored. Also, while the County has performed limited tests of recovering backup data, it has not fully tested the plan to validate or reassess the plan's feasibility.

Effect: The County may not be able to process and record transactions in the event of a system or equipment failure or interruption.

Cause: The County has taken steps to develop a disaster recovery plan, including designating an offsite backup facility that may be used in the event of a disaster and updating its information technology policies. However, the County has not developed detailed disaster recovery procedures or tested the reliability of the disaster recovery plan.

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Recommendation: The County should ensure that it has a complete and tested disaster recovery plan by implementing the following procedures:

- Perform a risk analysis identifying and prioritizing critical applications to be restored.
- Update the plan to include a current listing of employees assigned to disaster teams, including emergency telephone numbers; hardware configurations; lists of backup data and storage locations; and any arrangements for a designated offsite facility.
- Communicate and distribute copies of the disaster recovery plan to all affected employees, ensuring a copy of the plan is kept offsite and that protocols for the notifications to key personnel are included.
- Establish detailed procedures for processing critical transactions and safeguarding and recovering data stored on backup files.
- Test the plan annually and maintain documentation of testing procedures and results, including resolutions to problems encountered or failed tests.

This finding is similar to a prior-year finding.

#### **2013-04**

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#### **The County should strengthen controls over cash at the County Superintendent's Office.**

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Criteria: In addition to handling public monies related to the educational programs it provides for the County, the County School Superintendent's Office processes school district warrants and assists schools within the County with other administrative functions, such as receiving and disbursing grant monies. Therefore, it is imperative that the County School Superintendent have effective policies and procedures over cash to help ensure that monies are safeguarded and to help mitigate the risk of theft and misappropriation.

Condition and context: The County School Superintendent's Office did not have adequate internal control policies and procedures to properly safeguard cash and process cash disbursements. Specifically, auditors noted that responsibilities were not adequately separated as follows:

- Several employees in the office shared the same password and had access to the Superintendent's electronic signature, while also having access to blank warrants.
- Monthly bank reconciliations of cash with expenditure and revenue activity were performed by the same employees who had access to the electronic signature and blank warrants. These reconciliations were also not formally reviewed by a supervisor for accuracy.
- Some employees who prepared monthly bank reconciliations were sometimes responsible for depositing cash.
- Some employees had authority to both initiate and authorize cash disbursements, and therefore, had the ability to process payments without a supervisor's review and approval.

Effect: The County's financial statements and supporting schedules could omit important and required information or contain other misstatements. In addition, the County has an increased risk of errors due to fraud, such as theft and misappropriation, without adequate internal control policies and procedures over cash.

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Schedule of Findings and Recommendations  
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Cause: Although the County had formal policies and procedures for its departments to follow that promote the proper separation of responsibilities, the County School Superintendent's Office did not follow these policies and procedures.

Recommendation: To help prevent and detect theft and misappropriation and to help establish an adequate internal control environment over cash and cash disbursements at the County School Superintendent's Office, the County should:

- Follow the County's existing policies and procedures, or develop additional written policies and procedures at the County School Superintendent's Office, to promote the proper separation of responsibilities and strong internal controls over cash and cash disbursements.
- Restrict access to the Superintendent's electronic signature and blank warrants to only a limited number of employees, ensuring that no one employee has access to both.
- Ensure that monthly bank reconciliations are written, contain evidence of a supervisor's approval, and are prepared by an employee who does not also have the ability to process cash disbursements and make bank deposits or withdrawals.
- Separate employees' responsibilities and system access so that no one employee has the ability to initiate, process, and approve cash disbursements without a review by another employee.





# NAVAJO COUNTY

## FINANCE DEPARTMENT

James Menlove • Finance Director

Mary Springer • Deputy Finance Director

*"Proudly Serving, Continuously Improving"*

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February 12, 2014

Debbie Davenport  
Auditor General  
2910 North 44th Street, Suite 410  
Phoenix, AZ 85018

Dear Ms. Davenport:

The accompanying Corrective Action Plan has been prepared as required by the standards applicable to financial audits contained in *Government Auditing Standards*. Specifically, we are providing you with the corrective action planned for the financial reporting findings, the names of the contact persons responsible for corrective action, and the anticipated completion date for each audit finding included in the current year's Schedule of Findings and Recommendations.

Sincerely,

W. James Menlove, CPA  
Finance Director

Navajo County  
Corrective Action Plan  
Year Ended June 30, 2013

**2013-01**

**The County should improve its controls over infrastructure asset reporting**

Contact person: James Menlove, Finance Director, 928-524-4343

Anticipated Completion Date: December 31, 2013

Corrective Action Plan: Concur. In prior years, the County considered road overlay and slurry seal projects to extend the useful life of a roadway. Consequently, the County capitalized these projects and expensed these costs over the useful life of the project. The infrastructure assets and depreciation expense were presented as such in the County's audited financial statement from fiscal years 2007 through 2012. After a reexamination of this accounting application during the fiscal year 2013 audit it was determined that these projects did not substantially extend the original useful life of the roadways and therefore, should be expensed in the year the project was completed. This change in accounting application has been incorporated into the County's procedures and the County's capital asset listing has been amended.

**2013-02**

**The County should continue to strengthen controls over granting access and monitoring of its information systems**

Contact person: James Menlove, Finance Director, 928-524-4343

Anticipated Completion Date: June 30, 2014

Corrective Action Plan: Concur. The County has worked extensively with its software vendors to strengthen access controls and monitoring capabilities within the software systems. In addition, to enhance system access controls the County has implemented a two-factor identification protocol which eliminates the risk of external system access. To further enhance prevention and detection of unauthorized access to our systems and data the County will:

- Ensure that employees follow county policies and procedures for granting and terminating user access rights and maintaining applicable documentation.
- Continue to work with software vendors to enhance system monitoring capabilities.

**2013-03**

**The County should continue to develop a complete and tested disaster recovery plan for its information systems**

Contact person: James Menlove, Finance Director, 928-524-4343

Anticipated Completion Date: June 30, 2014

Corrective Action Plan: Concur. An update of the County's information systems disaster recovery plan was completed December 31, 2013. The County's complete Continuation of Government (COG) and Continuity of Operations plans are under revision and will be completed by June 30, 2014. To address this audit finding the County has performed the following:

- Completed a risk analysis identifying and prioritizing critical applications.
- Prepared a current listing of employees assigned to disaster teams, including emergency telephone numbers. In addition, the emergency management team meets at least monthly or more often as necessary such as for preparation for the summer's wildland fire season.

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- Established procedures for processing critical transactions, including forms or other documents to use, and safeguarding and recovering data stored on backup files.
- Frequent testing of the County's disaster recovery plans.

The County has requested that IT staff from the Arizona Office of the Auditor General be present during testing procedures to ensure the County's plans and processes are adequate.

**2013-04**

**The County should strengthen controls over cash at the County Superintendent's Office**

Contact person: Tami Phillips, Chief Deputy Superintendent, 928-524-4202

Anticipated Completion Date: June 30, 2014

Corrective Action Plan: Concur. To help prevent and detect theft and misappropriation and to help establish an adequate internal control environment over cash and cash disbursements at the County Superintendent of Schools' Office (Superintendent) the following will be implemented.

- Follow the County's existing policies and procedures, or develop additional written policies and procedures for the Superintendent's Office, to promote the proper separation of responsibilities and strong internal controls over cash and cash disbursements.
- Restrict access to the Superintendent's electronic signature and blank warrants to only a limited number of employees, ensuring that no one employee has access to both.
- Ensure that monthly bank reconciliations are written, contain evidence of a supervisor's approval, and are prepared by an employee who does not also have the ability to process cash disbursements and make bank deposits or withdrawals.
- Separate employees' responsibilities and system access so that no one employee has the ability to initiate, process and approve cash disbursements without a review by another employee.



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**Navajo County**

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Year Ended June 30, 2013

State of Arizona  
Office of the Auditor General