



Susan Montee, CPA
Missouri State Auditor

July 2007

City of Gerald, Missouri

Year Ended December 31, 2006



Office Of
Missouri State Auditor
Susan Montee, CPA

July 2007

The following findings were included in our audit report on the City of Gerald, Missouri.

Contrary to an Attorney General's opinion, the City Clerk of Gerald is responsible for all record-keeping duties of the city, including duties which would normally be performed by a City Treasurer and a City Collector. No personnel independent of the cash custody and the record-keeping functions provide adequate supervision or review of the work performed by the City Clerk. In addition, checks were sometimes signed in advance by the former Mayor.

The city does not have a formal bidding policy and did not solicit bids or retain bid documentation for some major purchases including the dam project at the city park (\$12,779) and cleaning services (\$2,550). In addition, there is no bid documentation for rock, excavating, and sewer supplies on a city sewer construction project completed in 2004.

The city does not periodically solicit proposals for audit or engineering services. Additionally, the former City Attorney/Prosecuting Attorney was paid \$11,680 in December 2006 although the attorney's written request did not provide a detailed accounting of dates and services provided to the city. Also, the city needs a written contract for providing certain services to the City of Rosebud.

The city paid \$2,160 in clothing allowances to city police officers in 2006; however, the officers were not required to submit invoices or itemized expense reports, nor were the allowances reported on their W-2 forms.

The city needs to adopt policies which address and prohibit nepotism. Because of the serious consequences which result by hiring a relative, the board should ensure its members abstain from any decision to hire a relative and that the action is fully documented in the board minutes.

The city's budgets do not include some information required by state law, budgets are not approved prior to the beginning of the fiscal year, and an annual maintenance plan for city streets is not prepared.

All reports are available on our website: www.auditor.mo.gov

YELLOW SHEET

CITY OF GERALD, MISSOURI

TABLE OF CONTENTS

	<u>Page</u>
STATE AUDITOR'S REPORT	1-3
MANAGEMENT ADVISORY REPORT - STATE AUDITOR'S FINDINGS	4-12
<u>Number</u>	<u>Description</u>
1.	Accounting Controls5
2.	Budgetary Practices6
3.	Expenditures and Related Matters8
4.	Written Contracts11
5.	Nepotism Policy.....11
HISTORY, ORGANIZATION, AND STATISTICAL INFORMATION	13-15

STATE AUDITOR'S REPORT



SUSAN MONTEE, CPA
Missouri State Auditor

To the Honorable Mayor
and
Members of the Board of Aldermen
City of Gerald, Missouri

The State Auditor was petitioned under Section 29.230, RSMo, to audit the City of Gerald, Missouri. The city engaged Ross, Spinner & Kummer, P.C., Certified Public Accountants (CPAs), to audit the city's financial statements for the year ended December 31, 2006. To minimize duplication of effort, we reviewed the report of the CPA firm. The scope of our audit of the city included, but was not necessarily limited to, the year ended December 31, 2006. The objectives of this audit were to:

1. Perform procedures to evaluate the petitioners' concerns.
2. Review internal controls over significant management and financial functions.
3. Review compliance with certain legal provisions.

To accomplish these objectives, we reviewed minutes of meetings, written policies, financial records, and other pertinent documents; interviewed various personnel of the city, as well as certain external parties; and tested selected transactions. Our methodology included, but was not necessarily limited to, the following:

1. We obtained an understanding of petitioner concerns and performed various procedures to determine their validity and significance.
2. We obtained an understanding of internal controls significant to the audit objectives and considered whether specific controls have been properly designed and placed in operation. However, providing an opinion on internal controls was not an objective of our audit and accordingly, we do not express such an opinion.
3. We obtained an understanding of legal provisions significant to the audit objectives, and we assessed the risk that illegal acts, including fraud, and violations of contract, grant agreement, or other legal provisions could occur.

Based on that risk assessment, we designed and performed procedures to provide reasonable assurance of detecting significant instances of noncompliance with the provisions. 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.

Our audit was conducted in accordance with applicable standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and included such procedures as we considered necessary in the circumstances. The work for this audit was substantially completed by March 2007.

The accompanying History, Organization, and Statistical Information is presented for informational purposes. This information was obtained from the city's management and was not subjected to the procedures applied in the audit of the city.

The accompanying Management Advisory Report presents our findings arising from our audit of the City of Gerald, Missouri.

A handwritten signature in black ink, appearing to read "Susan Montee".

Susan Montee, CPA
State Auditor

The following auditors participated in the preparation of this report:

Director of Audits: Thomas J. Kremer, CPA
Audit Manager: Mark Ruether, CPA
In-Charge Auditor: Terri Erwin

MANAGEMENT ADVISORY REPORT -
STATE AUDITOR'S FINDINGS

CITY OF GERALD, MISSOURI
MANAGEMENT ADVISORY REPORT -
STATE AUDITOR'S FINDINGS

1.	Accounting Controls
-----------	----------------------------

The city does not have proper segregation of accounting duties, checks are signed in advance, and some officials authorized to sign checks are not bonded.

- A. The City Clerk is responsible for all record keeping duties of the city, including duties which would normally be performed by a City Treasurer and a City Collector. These duties include receiving and depositing monies, preparing invoices for payment, signing checks, performing bank reconciliations, and preparing financial reports. No personnel independent of the cash custody and the record-keeping functions provide adequate supervision or review of the work performed by the City Clerk.

Attorney General's Opinion No. 24, 1955 to Dodds, concluded that in a fourth-class city the holding of the positions of City Clerk, City Treasurer, and City Collector, or any two of these three offices, by the same person at the same time would be incompatible. Holding two or three of these offices does not allow the separation of duties necessary for a proper evaluation and review of financial transactions. The current procedures jeopardize the system of independent checks and balances intended by state law.

To safeguard against possible loss or misuse of funds, internal controls should provide reasonable assurance that all transactions are accounted for properly and assets are adequately safeguarded. Internal controls would be improved by segregating duties to the extent possible. In addition, the board should require someone independent of the cash custody and record keeping functions to perform periodic reconciliations of receipts to deposits and checks issued to disbursement records, and review bank statements and bank reconciliations. Furthermore, this review of records should be documented.

- B. The city's checks require two signatures; however, checks were sometimes signed in advance by the former Mayor. City personnel indicated this was done when one or more of the check signers planned to be on vacation or out-of-town. The Mayor, the City Clerk, and one Alderman can sign checks issued on the city's bank accounts. In addition, the Mayor and the Alderman authorized to sign checks are not bonded.

Signing checks in advance does not allow for proper review of the documentation to support the disbursement and diminishes the control intended by dual signatures. To adequately safeguard assets, checks should not be signed until all pertinent information is completed and supporting documentation for the

disbursement is reviewed and approved by the Board of Aldermen. In addition, failure to bond all persons with access to assets exposes the city to risk of loss.

WE RECOMMEND the Board of Aldermen:

- A. Segregate accounting duties to the extent possible, and consider appointing separate individuals to perform the duties of a city clerk, city treasurer, and city collector. If proper segregation of duties cannot be achieved, at a minimum, there should be documented independent reviews of the cash custody and record keeping functions, including reconciliations of receipts to deposits and checks issued to disbursement records, and reviews of bank statements and bank reconciliations.
- B. Discontinue the practice of signing checks in advance and obtain bond coverage for all persons with access to city assets.

AUDITEE'S RESPONSE

- A. *A city treasurer was appointed effective May 2007. This should address the segregation of duties concern.*
- B. *There are now four officials who can sign checks, so signing checks in advance will no longer be done. We are in the process of obtaining bond coverage for all individuals who can sign checks.*

2. Budgetary Practices

The city's budgets do not include some information required by state law, budgets are not approved prior to the beginning of the fiscal year, and an annual maintenance plan for city streets is not prepared.

- A. The city's annual budgets include only budgeted receipts and disbursements for the current year. They do not include a budget message, a general budget summary, actual (or estimated) revenues and expenditures for the two preceding budget years, amounts required for interest charges on debt, or the beginning and the estimated ending available resources.

Section 67.010, RSMo, requires the preparation of an annual budget which shall present a complete financial plan for the ensuing budget year. A complete and well-planned budget, in addition to meeting statutory requirements, can serve as a useful management tool by establishing specific cost expectations for each area. A budget can also provide a means to effectively monitor actual costs by periodically comparing budgeted amounts to actual expenditures. A complete budget should include separate revenue and expenditure estimates, and include the beginning available resources and a reasonable estimate of the ending

available resources. The budget should also include a budget message, amount required for payment of interest charges on debt, and comparisons of actual revenues and expenditures for the two preceding years.

- B. The city does not normally approve the annual budget until the first board meeting in January; after the start of the fiscal year.

Section 67.030, RSMo, indicates the budgets shall be approved by the Board of Aldermen prior to the beginning of the fiscal year, and Section 67.070, RSMo, indicates that if a budget is not approved at the beginning of the fiscal year, the budget for the preceding year shall govern. To be of maximum benefit to the taxpayers and to properly monitor city activity, the city should adopt the budget prior to the beginning of the fiscal year.

- C. An annual maintenance plan for city streets has not been prepared. A formal maintenance plan should be prepared in conjunction with the annual fiscal budget and include a description of the streets to be worked on, the type of work to be performed, an estimate of the quantity and cost of materials needed, the dates such work could begin, the amount of labor required to perform the work, and other relevant information. The plan should be included in the budget message and be approved by the board. In addition, a public hearing should be held to obtain input from the city residents.

A formal maintenance plan would serve as a useful management tool and provide greater input into the overall budgeting process. Such a plan provides a means to more effectively monitor and evaluate the progress made in the repair and maintenance of streets throughout the year.

WE RECOMMEND the Board of Aldermen:

- A. Prepare budgets that contain all information required by state law.
- B. Adopt budgets prior to the beginning of the fiscal year.
- C. Prepare a formal maintenance plan for city streets at the beginning of the fiscal year and periodically update the plan throughout the year. In addition, the board should review the progress made in the repair and maintenance of streets to make appropriate decisions on future projects.

AUDITEE'S RESPONSE

A-C. *We agree and plan to implement these recommendations during the next budget cycle.*

3.**Expenditures and Related Matters**

The city does not have a formal bidding policy and does not solicit proposals for certain professional services. The city did not require a detailed accounting of the city attorney's services before paying his fee. The city's records of capital assets are not updated in a timely manner. Police officers receive a clothing allowance without being required to submit invoices, and the city pays employees a Christmas bonus.

- A. The city does not have a formal bidding policy. As a result, the decision of whether to solicit bids for a particular purchase is made on an item-by-item basis. The city did solicit bids and retain bid documentation for some major purchases; however, the following are examples of purchases made in 2006 for which bids were not solicited or bid documentation was not retained:

Purchases	Amount
Dam project at city park	\$ 12,779
Cleaning services	2,550
Tires	1,322

In addition, the city spent approximately \$104,000 on a sewer construction project which was performed by city employees and completed in 2004. There was no bid documentation for the following expenditures for that project:

Purchases	Amount
Rock	\$ 6,381
Excavating	5,355
Sewer supplies	4,913
Culverts	2,323
Oil	1,281

Formal bidding procedures for major purchases provide a framework for economical management of city resources and help ensure the city receives fair value by contracting with the lowest and best bidders. Competitive bidding helps ensure all parties are given an opportunity to participate in the city's business. Bids can be handled by telephone quotation, by written quotation, by sealed bid, or by advertised sealed bid. Various approaches are appropriate, based on dollar amount and type of purchase. Whichever approach is used, complete documentation should be maintained of all bids received and reasons noted why the bid was selected.

- B. In 2006, the city paid \$5,500 to a CPA firm for the annual audit of the city's financial statements. The city has used the same firm for several years and does not periodically solicit proposals for audit services. In addition, the city normally uses the same engineering firm without soliciting proposals for services, and the

city paid \$12,359 to this firm without soliciting other proposals for a sewer project which was completed in 2004.

While professional services are not subject to standard bidding procedures, it is good business practice to periodically solicit proposals for such services and select the best proposal based on cost, experience, the type of service to be provided, and any other relevant factors. Complete documentation should be maintained of all proposals received and reasons for selecting the winning proposal. In addition, Section 8.291, RSMo, requires political subdivisions to consider the qualifications of at least three firms when negotiating contracts for architectural, engineering, or land surveying services.

- C. The former City Attorney/Prosecuting Attorney made one request for the majority of his services provided in 2006, and in December 2006, the city paid \$11,680 (146 hours at \$80 per hour). While the request was made in writing, the letter did not provide a detailed accounting of the specific dates that his services were provided to the city.

To ensure the validity of payments made for legal services, the city should require invoices to be sufficiently detailed to include services rendered, including the number of hours worked by day, the work performed, and the hourly rate charged.

- D. The city maintains a listing of general capital assets; however, the listing is normally only updated annually prior to the city's financial statement audit, and some purchases and dispositions were not included on the list. For example, a copier for City Hall and a mower purchased for the City Park were both purchased during 2006 but were not added to the asset listing. In addition, the city does not perform annual physical inventories.

Records of capital assets should be maintained on a perpetual basis, accounting for property acquisitions and dispositions as they occur, and reconciling additions to purchases annually. Complete and accurate asset records are necessary to ensure better internal control over city property, and provide a basis for proper financial reporting and for determining proper insurance coverage required on city property. Annual physical inventories are necessary to ensure the asset records are accurate, identify any unrecorded additions and deletions, detect theft of assets, and identify obsolete assets.

- E. The city paid a total of \$2,160 in clothing allowances to city police officers in 2006. The officers were not required to submit invoices or itemized expense reports to support the allowance, nor were the allowances reported on their W-2 forms.

IRS Regulations 1.62-2(h) and 31.3401(a)-4(b) specifically require employee business expenses not accounted for to the employer to be considered gross income and payroll taxes to be withheld from the undocumented payments.

Procedures have not been established to ensure that IRS regulations are followed. As a result, the city may be subject to penalties and/or fines for failure to report all taxable benefits.

- F. All city employees received a \$100 bonus at Christmas during 2006, and the independent contractor who cleans City Hall received a \$50 bonus. The total bonuses paid in 2006 was \$1,050. This amount was not added to the employees W-2 forms or the contractor's 1099 form.

Bonuses given to employees appear to represent additional compensation for services previously rendered and, as such, are in violation of Article III, Section 39 of the Missouri Constitution and are contrary to Attorney General's Opinion No. 72, 1955 to Pray, which states, "...a government agency deriving its power and authority from the Constitution and laws of the state would be prohibited from granting extra compensation in the form of bonuses to public officers after the service has been rendered."

WE RECOMMEND the Board of Aldermen:

- A. Adopt formal bidding policies and procedures, and ensure bids are solicited for all major purchases and all related bid documentation is retained, including documentation of the board's decisions for selecting the winning bidder.
- B. Periodically solicit proposals for professional services and maintain all related documentation, including the reasons for the board's decisions.
- C. Ensure detailed invoices are received prior to the payment of legal services.
- D. Maintain perpetual records of all capital assets which are updated for purchases and dispositions as they occur, and perform annual physical inventories to ensure the asset records are complete and accurate.
- E. Require the police officers to submit itemized reports of uniform clothing purchases or report the uniform allowance payments as other income on the employees' W-2 forms. In addition, the prior years' W-2 forms should be amended for any reimbursements for which an adequate accounting cannot be provided.
- F. Discontinue the practice of paying bonuses to city employees.

AUDITEE'S RESPONSE

- A. *We agree and will work on adopting a bidding policy with the help of the city attorney as soon as possible.*

- B. *We agree and will solicit proposals for audit services for next year's audit. We have already solicited proposals from three engineering firms at the May 2007 board meeting.*
- C. *The current city attorney has submitted more detailed invoices on a monthly basis.*
- D. *We agree and will attempt to keep updated inventory records.*
- E. *This was implemented in March 2007.*
- F. *We will take this under advisement.*

4. Written Contracts

The city does not have a written agreement with the neighboring City of Rosebud for the use of the city's sewer maintenance equipment. Normally once or twice a year upon request of Rosebud city officials, the City of Gerald has allowed the City of Rosebud to use the equipment at no cost to Rosebud, and in some instances, Gerald city employees accompanied the equipment to Rosebud during normal working hours. The city has not estimated the related costs of this agreement.

The city should review this situation to ensure this arrangement is beneficial to the city. If the city desires to continue this arrangement, a written contract should be prepared and signed by the parties involved. The contract should specify the services to be rendered and the manner and amount of compensation, if any, to be paid. Written contracts are necessary to ensure all parties are aware of their duties and responsibilities and to prevent misunderstandings. Section 432.070 RSMo, requires contracts of political subdivisions be in writing.

WE RECOMMEND the Board of Aldermen review this matter to ensure there is a benefit to the city. If the city continues to allow the City of Rosebud to periodically use its sewer maintenance equipment, a written contract should be prepared which documents the services to be provided and any compensation to be paid, including the duties and responsibilities of both parties.

AUDITEE'S RESPONSE

We will determine whether to continue the current arrangement and enter into a written contract as necessary.

5. Nepotism Policy

The city has not adopted policies which address and prohibit nepotism. Two nephews of an Alderman were hired by the board to work on a city sewer project in December 2003. These individuals were considered city employees, and were placed on the city's payroll

as temporary employees for the duration of the project. Applicable board meeting minutes indicate the motion to hire these two individuals was seconded by the related Alderman, and the motion passed three-to-one on a voice vote.

Article VII, Section 6 of the Missouri Constitution provides that any public official who names or appoints to public office or employment any relative within the fourth degree shall forfeit his office. Because of the serious consequences which result by hiring a relative, the board should ensure its members abstain from any decision to hire a relative and ensure that action is fully documented in the board minutes. Discussions and decisions concerning situations where potential nepotism or conflicts of interest exist should be completely documented so that the public has assurance that no city official has benefited improperly. In addition, the board should consider establishing a policy which addresses these types of situations and provides a code of conduct for city officials.

WE RECOMMEND the Board of Alderman adopt policies to prohibit nepotism and ensure any future appointments comply with the restrictions of the Missouri Constitution. If a relative of a board member is considered for employment or appointment, that board member should abstain from voting on the issue and an adequate record of the abstention should be maintained.

AUDITEE'S RESPONSE

We agree that a policy is needed and will attempt to ensure applicable board members abstain from voting on such matters in the future.

HISTORY, ORGANIZATION, AND
STATISTICAL INFORMATION

CITY OF GERALD, MISSOURI
HISTORY, ORGANIZATION, AND
STATISTICAL INFORMATION

The city of Gerald is located in Franklin County. The city was incorporated in 1907 and is currently a fourth class city. The population of the city in 2000 was 1,171.

The city government consists of a mayor and a four-member board of aldermen. The members are elected for 2-year terms. The mayor is elected for a 2-year term, presides over the board of aldermen, and votes only in the case of a tie. The Mayor, Board of Alderman, and other officials during the year ended December 30, 2006, are identified below. The compensation of these officials is established by ordinance.

Mayor and Board of Alderman	Dates of Service During the Year Ended December 31, 2006	Compensation Paid for the Year Ended December 31, 2006
Diane Ballard, Mayor (1)	January 2006 to December 2006	\$ 1,100
Marie Wright, Alderman	January 2006 to April 2006	400
David Luechtefeld, Alderman	April 2006 to December 2006	400
Richard Pierce, Alderman	January 2006 to April 2006	400
Richard Johnson, Alderman	April 2006 to December 2006	400
Dan Maxwell, Alderman	January 2006 to December 2006	800
Larry Long, Alderman (2)	January 2006 to July 2006	600
Charlean Stockton, Alderman (2)	August 2006 to December 2006	200
Other Officials	Dates of Service During the Year Ended December 31, 2006	Compensation Paid for the Year Ended December 31, 2006
Beverly Maples, City Clerk (3)	January 2006 to December 2006	\$ 29,030
Carlos Terrill, Chief of Police (4)	January 2006 to December 2006	27,970
Keith Wehmeyer, Public Works Supervisor (5)	January 2006 to November 2006	28,136
Timothy Melenbrink, City Attorney/Prosecuting Attorney (6)	January 2006 to December 2006	15,940

- (1) Otis Schulte was elected Mayor in April 2007.
- (2) Larry Long resigned as Alderman in July 2006 and was replaced by Charlean Stockton in August 2006. Brad Landwehr was elected Alderman in April 2007.
- (3) Sarah Wheeler was appointed City Clerk in May 2007.
- (4) Clyde Zelch was appointed Chief of Police in April 2007.
- (5) Employment was terminated in November 2006, and the position remains vacant.
- (6) Payments are made by the city to Hansen, Stierberger, Downard, Melenbrink, & Schroeder, LLC, when legal services are rendered and billed to the city. Joseph Purschke was appointed City Attorney/Prosecuting Attorney in May 2007.

In addition to the officials identified above, the city employed nine full-time employees and one seasonal employee on December 31, 2006.

Assessed valuations and tax rates for 2006 were as follows:

ASSESSED VALUATIONS

Real estate	\$ 12,392,513
Personal property	<u>3,864,106</u>
Total	<u><u>\$ 16,256,619</u></u>

TAX RATES PER \$100 ASSESSED VALUATION

	<u>Rate</u>
General	\$.8000
Parks and recreation	.2200

TAX RATES PER \$1 OF RETAIL SALES

	<u>Rate</u>
General	\$.0100
Transportation	.0050