


MEMORANDUM

Stafford County Administrator's Office

TO: Board of Supervisors

FROM: Anthony J. Romanello
Deputy County Administrator 

SUBJECT: Presentation on 2006 Annual Audit

DATE: February 1, 2007

Attached are preliminary draft copies of letters from Phibbs, Burkholder, Geisert, and Huffman (PBGH), LLP regarding the 2006 Annual Audit.

Staff will provide the Board with its comments no later than close of business on Friday, February 2, 2007 via email.

SC:AR:myb

Attachments (2)

To the Honorable Members of the Board of Supervisors
County of Stafford, Virginia
Stafford, Virginia

This letter is intended to inform the Board of Supervisors (Board) of the County of Stafford, Virginia (County) about significant matters related to the conduct of the annual audit so it can appropriately discharge its oversight responsibility, and that we comply with our professional responsibilities to the Board of Supervisors.

In addition to our report on your basic financial statements, we have provided, under separate cover, a letter dated November 9, 2006 concerning the reportable condition and compliance issues we noted during our audit of the County's financial statements for the year ended June 30, 2006.

The following summarizes various matters which must be communicated to you under auditing standards generally accepted in the United States of America.

*The Auditors' Responsibility Under Auditing Standards
Generally Accepted in the United States of America*

Our audit of the financial statements of the County of Stafford, Virginia, for the year ended June 30, 2006 was conducted in accordance with auditing standards generally accepted in the United States of America; *Government Auditing Standards*, issued by the Comptroller General of the United States; the provisions of the Single Audit Act, OMB Circular A-133 and OMB's Compliance Supplement; and *Specifications for Audits of Counties, Cities and Towns*, issued by the Auditor of Public Accounts of the Commonwealth of Virginia. Those standards, circulars, supplement and specifications require we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error, fraudulent financial reporting or misappropriation of assets. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. Accordingly, the audit was designed to obtain reasonable, rather than absolute, assurance about the financial statements. We believe our audit accomplished that objective.

In accordance with *Government Auditing Standards*, we have also performed tests of controls over internal control over financial reporting and tests of compliance with certain provisions of laws, regulations, contracts, and grant agreements that contribute to the evidence supporting our opinion on the financial statements. However, they do not provide a basis for opining on the County's internal control over financial reporting or on compliance and other matters.

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Management Judgments and Accounting Estimates

Accounting estimates are an integral part of the preparation of financial statements and are based upon management's current judgment. The process used by management encompasses their knowledge and experience about past and current events and certain assumptions about future events. Management has informed us that they used all the relevant facts available to them at the time to make the best judgments about accounting estimates, and we considered this information in the scope of our audit. Estimates significant to the financial statements include such items as: reserves for uncollectible accounts, lives for depreciable assets, fair value of donated capital assets, retirement benefits and liability, and health insurance claims that have been incurred but not reported. The Board may wish to monitor throughout the year the process used to compute and record these accounting estimates.

Adjustments

There were 111 adjustments to the original trial balance presented to us to begin our audit. Some of the adjustments during the audit resulted in a significant change in equity (fund balance or retained earnings) to several funds. There were also other entries that had no effect on equity of the fund but were significant in nature.

Fund	Increase (Decrease) in Equity
General:	
Increase in receivables and revenue	\$ 155,000
Decrease in payables and expenditures	162,000
Increase in deferred revenue and reduction of revenue	(1,774,000)
Record additional personal property tax receivable and deferred revenue of \$916,000	-
Water and Sewer:	
Increase in receivables	371,000
Increase in capital assets	262,000
Reduction of construction in process and account payable of \$410,000	-
School Capital Projects:	
Increase in retainage payable	991,000

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Construction in progress for governmental activities on the Statement of Net Assets was increased approximately \$2.5 million for unrecorded projects.

Uncorrected Misstatements

There were no material uncorrected misstatements that came to our attention during the audit.

Accounting Policies and Alternative Treatments

Management and the Board of Supervisors have the ultimate responsibility for the appropriateness of the accounting policies used by the County. During the year, the County adopted Governmental Accounting Standards Board Statement No. 44, *Economic Condition on Reporting: the Statistical Section, an amendment of NCGA Statement No. 1*, which changed the required presentation in the statistical section of the financial statements. Following are descriptions of significant accounting policies that have been issued but have not been implemented as of June 30, 2006 and that management has not yet determined the effect on the County's financial statements:

- GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, establishes standards for the measurement, recognition, and display of OPEB expense/expenditures and related liabilities (assets), note disclosures, and required supplemental information. Statement No. 45 will be effective for periods beginning after December 15, 2006.
- GASB Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*, establishes criteria that governments will use to ascertain whether the proceeds received collateralized by future collections of receivables or revenues should be reported as revenues or as a liability. This Statement also includes a provision that stipulates that governments should not revalue assets that are transferred between financial reporting entity components. Statement No. 48 will be effective for periods beginning after December 15, 2006.

We did not identify any significant or unusual transactions or significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.

Other Information in Documents Containing Audited Financial Statements

We are not aware of any other documents that contain the audited basic financial statements. If such documents were to be published, we would have a responsibility to determine that such financial information was not materially inconsistent with the audited statements of the County.

Major Issues Discussed With Management Prior to Retention

No major issues were discussed with management prior to our retention to perform the aforementioned audit.

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Disagreement With Management and Consultation with Other Accountants

Following is a description of the disagreement with management on financial accounting and reporting matters which would be significant to the County's financial statements or our report on those financial statements.

The trial balance which we were provided to begin the audit reflected \$1.8 million in revenue, which increased fund balance by \$1.8 million. Management did not want to adjust revenue to recognize the revenue over the 70-year lease term.

We were informed by management that they obtained opinions from at least two other independent accountants on the application of accounting principles generally accepted in the United States of America concerning the accounting for the receipt of funds for a 70-year operating lease where all of the lease proceeds were collected by the County at the beginning of the lease and was recognized as revenue instead of deferring the revenue over the life of the lease. Ultimately, management agreed to properly recognize the revenue over the least term.

Difficulties Encountered in Performing the Audit

Following is a description of serious difficulties we encountered in dealing with management during the course of our audit of the financial statements for the year ended June 30, 2006:

- Convincing management to adjust \$1.8 million of lease proceeds from revenue to a deferred revenue amount.
- Delays in receiving a trial balance for us to begin our audit.
- Lack of cooperation in scheduling meetings to perform inquiries, observations, and other audit procedures.
- Obtaining financial statements prepared by the County staff that agreed to the audited trial balance.
- Delays in receiving an accurate Schedule of Federal Awards for us to audit.
- Dealing with different levels of management who were reticent to make proposed audit adjustments.

We will be pleased to respond to any questions you have about the foregoing information. We appreciate the opportunity to be of service to the County of Stafford, Virginia.

This report is intended solely for the information and use of the Board of Supervisors and management and is not intended to be and should not be used by anyone other than these specified parties.

Harrisonburg, Virginia
February 6, 2007

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The Honorable Members of the Board of Supervisors
County of Stafford, Virginia
Stafford, Virginia

In planning and performing our audit of the financial statements of the County of Stafford, Virginia (County) for the year ended June 30, 2006, we noted a certain matter involving internal control and its operation that we consider to be a reportable condition under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control that, in our judgment, could adversely affect the County's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

Cash Reconciliations

Cash reconciliations were not being performed timely throughout the year. It is important to have an accurate bank reconciliation performed timely after each month-end. Cash reconciliations are an integral part of the internal control environment and are done to ensure that accurate financial information is available on a timely basis. Performing these reconciliations timely helps with cash management issues, assists in discovering possible errors made by the bank or County, and decreases the risk of funds being misappropriated for an extended period of time.

Following are compliance findings we identified during our audit.

Business Continuity Plan for Social Services

The Virginia Department of Social Services has stipulated that all local agencies should have a documented Business Continuity Plan. The Business Continuity Plan should address different types of disaster scenarios, prioritize recovery tasks, and assign responsibilities. The County's Social Services Department had not completed its Business Continuity Plan at fiscal year end. We recommend this Plan be completed and tested as soon as possible.

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Statements of Economic Interest

The State and Local Government Conflict of Interests Act is designed to assure that the judgment of public employees is not compromised or affected by inappropriate conflicts. The Act prohibits local government officers or employees from participating in certain transactions. The County requires certain personnel to file this information as well, even if they are not required by state law to do so. Statements of economic interests are required to be filed with the Clerk of the governing body by January 15 of each year. We concluded that 27 of the economic interest statements were not filed timely.

Federally Funded Capital Asset Compliance

The County School Board does not have a written policy for tracking federally funded capital assets. Under federal funding guidelines, when capital assets with an original purchase value of over \$5,000 are acquired with federal funds and subsequently sold, any proceeds are required to be remitted to the funding agency unless the agency specifically allows the proceeds to be kept by the County. We suggest management develop a written policy to track federally funded capital assets in order to avoid possible problems with any of their funding agencies.

In addition, we have the following comments and suggestions for your consideration:

Property Tax Reconciliations

The County maintains the necessary information to reconcile property taxes, including assessments, supplementals, abatements, collections, tax relief, etc. However, the information is not summarized and reconciled timely to the general ledger. We recommend the County prepare a detailed reconciliation of property taxes at least twice throughout the year as a means of providing additional control over errors or misstatements of the receivable and revenue balances. Since this is the single largest revenue source of the County, and not having this revenue source reconciled could have a significant impact on the undesignated fund balance, it is important that property tax revenue be reconciled in a timely manner.

Capital Assets

We identified numerous journal entries that needed to be made for capital assets and depreciation to the County's general ledger. Reconciliations are done to ensure that accurate financial information is available on a timely basis, and to identify possible errors or misclassifications that may occur. We believe that performing capital asset reconciliations more than once a year would assist with the year-end closing process and to assist with improving the process of preparing for the year-end audit.

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Administration of Child Care Assistance

The Child Care Cluster was a major program tested in accordance with the *U.S. Office of Management and Budget Circular A-133 Compliance Supplement*. We found that one individual administers the program without any oversight from anyone else within the department. This individual reviews applications, determines eligibility, and prepares and approves purchase orders. During our interviews with respect to this program and other interviews in the Social Services Department, we found that many times only one person knows the program they are handling. If that individual were to leave the County or be off work for a long period of time, others in the Department would have a difficult time filling in for the individual. We recommend mandatory cross training within the Department and segregating duties with respect to preparing and approving purchase orders.

Accounts Payable

We identified several significant adjustments to accounts payable for the County during our audit. We recommend management review the accounts payable listing at year-end and test significant items for accuracy and completeness. Due to our audit, several items were removed from the accounts payable listing because the County did not have possession of the items until July 2006. Each person responsible for determining if a purchased item should be included in accounts payable at year-end needs to be trained to gain an understanding of what items should and should not be included in accounts payable at year-end.

Accounting Policies and Procedures Manual

Since departure of certain accounting department supervisory employees is unpredictable and can occur at any time, we recommend that the Finance Department finalize its accounting procedures manual. The manual should include a chart of accounts, adequate explanations of account content, month-end and year-end closing procedures, appropriate descriptions of all accounting procedures and routines, and all matters that bear directly or indirectly on the functioning of the system of internal accounting control. Once the manual is complete, subsequent revisions should be subject to formal approval procedures. It will take much less time if the current experienced employees finalize the manual than if subsequent employees have to reconstruct procedures each time there is turnover in personnel.

Recording of Retainage Payable

The previous fiscal year's retainage payable was not adjusted prior to our audit at the School Board. Also, the *Code of Virginia* states that retainage withheld on construction contracts cannot exceed 5% of the amount earned by the contractor. We learned from interviews that no one tracked the liability throughout the year; therefore, the prior year's balance was not changed and the current year's liability was not recorded. We discussed this with the School's Finance Department and they are aware that this item needs to be monitored and adjusted prospectively. We suggested assigning the responsibility to someone to monitor this large liability and to ensure that no more than 5% retainage be withheld at any given time.

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GASB Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions

The objective of the Statement is to improve the representations and usefulness of information included in the financial reports regarding other postemployment benefits (OPEB). OPEB refers to post employment benefits other than pension benefits and includes 1) postemployment healthcare benefits and 2) other types of postemployment benefits if provided separately from a pension plan.

This Statement will help governments measure the cost of OPEB during the periods when employees render their services or to provide relevant information about OPEB obligations and the extent to which progress is being made in funding those obligations. This liability for future expenses to the County will need to be assessed and is required to be recorded as a liability in the Statement of Net Assets. The County has until the 2007-2008 fiscal year to implement this standard and calculate its liability.

* * * * *

If you have any questions concerning any of these items, or if we can be of further assistance, please contact us. We thank you for the opportunity to conduct your audit for the year ended June 30, 2006 and express our appreciation to everyone for their cooperation during this engagement.

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Harrisonburg, Virginia
November 9, 2006