

# **Kennewick Irrigation District**

**Independent Accountants' Report  
On Applying Agreed-Upon Procedures**

**For the Years Ended December 31, 2006  
through December 31, 2009**



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# Kennewick Irrigation District

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## Contents

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	<i>Page</i>
<i>INDEPENDENT ACCOUNTANTS' REPORT</i>	2
<i>Agreed-Upon Procedures Performed:</i>	
<i>Review state Auditors' office audit reports and findings</i>	3-4
<i>Review fund reconciliations</i>	4-5
<i>Review the LID loan activity</i>	5
<i>Review the refunds to customers</i>	5-6
<i>Review existing documentation of internal controls over financial reporting</i>	6-10
<i>Review land sales and contracts and analyze the sources and uses of funds within the realty fund</i>	10
<i>Review the reserve fund and analyze the sources and uses of funds</i>	10-11
<i>Other items</i>	11-12
<i>Attachment: TROI IT Solutions report</i>	

Bellevue

Boise

Grandview

Moses Lake

Omak

Othello

Quincy

INDEPENDENT ACCOUNTANTS' REPORT  
ON APPLYING AGREED-UPON PROCEDURES

Board of Directors and Management  
Kennewick Irrigation District  
Kennewick, Washington

We have performed the procedures outlined in the following report, which were agreed to by the Board of Directors and management of Kennewick Irrigation District (KID), solely to assist you in evaluating KID's compliance with the identified objectives for the years ended December 31, 2006 through 2009. Kennewick Irrigation District's management is responsible for the sufficiency of the procedures performed. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of those parties specified in this report. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

These agreed-upon procedures do not constitute an audit of financial statements or any part thereof, the objective of which is the expression of opinion on the financial statements or a part thereof. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

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

*LeMaster & Daniels PLLC*

Tri-Cities, Washington  
April 14, 2010

# Kennewick Irrigation District

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## Agreed-upon Procedures Performed

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At the request of the Board of Directors and management of Kennewick Irrigation District (the District, KID), we performed the following agreed-upon procedures:

1. **Review the State Auditor's Office (SAO) audit reports and findings contained in those reports for the years 2006 through 2008, and analyze KID's compliance with the recommendations cited in those reports.**

We reviewed the State Auditor's Office Financial Statement and Accountability Audit Reports for the years ended December 31, 2006 through 2008. We noted the SAO identified two findings for fiscal year 2006; the SAO subsequently cleared both findings during the fiscal 2007 audit and noted no additional issues. There were no findings noted in the audited financial statements and accompanying reports for the year ended December 31, 2008.

### *General findings:*

- a. Based on the results of Procedure 5, the District has made substantial progress, but has not fully addressed the finding indicated in the SAO's Accountability Audit Report for fiscal year 2006 regarding adequate documentation of public works projects. This includes adequate evidence of project approval, change orders, and other items. Strong document retention policies are critical to developing adequate audit trails.
- b. Based on our review of Board minutes for the fiscal years 2006 through 2009, the District has adequately addressed the finding indicated in the SAO's Accountability Audit Report for fiscal year 2006 regarding the Open Public Meetings Act for Special Meetings.
- c. In addition, we noted that developing the necessary financial records for the annual audit is currently the only financial statement reporting responsibility performed by the Accounting Division. The Board of Directors and management are not being provided with routine financial reports. This has prevented the District from being informed of all financial matters on a current basis, decreased the ability to react to financial issues timely, and increased the likelihood that errors in the financial records may go undetected for a significant period of time.
- d. Based on our interviews with the Board of Directors, we noted that the members of the Board have not been adequately briefed on the annual financial statement and accountability reports issued by the State Auditor's Office.

### *Recommendations:*

- a. The District should continue to emphasize the use and completion of the Contract Checklist in each public works project file to assist in ensuring that all necessary documentation is present in file.

# Kennewick Irrigation District

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## Agreed-upon Procedures Performed (continued)

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- b. None.
  - c. Routine and detailed financial reports should be prepared and reviewed with the Board on a monthly basis so that the Board of Directors and management can effectively operate the District. This will require the Accounting Division to reconcile and close the books once a month so that monthly financial reports can be developed and distributed. A typical closing schedule includes: (1) the tasks necessary for the monthly statement preparation, (2) the responsible party to perform the task, (3) the due date for completion of the task, and (4) the financial statement publication and review dates with the Board of Directors and management.
  - d. The Board should request an in-depth presentation of the reports by the State Auditor's Office. The Board should also receive training on financial statement reporting to aid in their understanding of the annual reports and allow for improved monitoring of internal financial reports throughout the year.
2. **Review fund reconciliations for the calendar years 2006 through 2009, including cash deposits, transfers, and disbursements, using sampling techniques, with a focus on the transactions during the calendar year 2009.**

We performed walkthroughs of a selection of reconciliations for the fiscal years 2006 through 2009 with Accounting Division staff and interviewed members of management and the Board of Directors.

*General findings:*

- a. Based on our walkthroughs, the bank reconciliation process was four months behind schedule. It was noted that the reconciliations were partially completed, but have remained open due to difficulties in reconciling online customer payments. The performance of timely and accurate bank reconciliations is necessary to provide evidence and comfort to the Board of Directors and management that the District's liquid assets are in good order. Failure to perform these functions increases the chance that potential errors or abuse may go undetected.
- b. Based on review of monthly cash investment reports for the years 2006 through 2009, we noted that the District's investments continued to decrease as its certificates of deposit's (CD's) were redeemed monthly by the Accounting Division to cover operating expenses. We were unable to identify documentation supporting the appropriate authorization of the transfer of investment funds to the operating cash account. Additionally, we were unable to identify evidence that the Board of Directors received and reviewed the monthly investment reports.

# Kennewick Irrigation District

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## Agreed-upon Procedures Performed (continued)

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*Recommendations:*

- a. We recommend that all of the bank accounts be reconciled monthly to the general ledger and that all irregular reconciling items be promptly investigated and adjusted with adequate explanations. Most of the issues encountered within the area of cash can be avoided if a proper system of checks and balances is incorporated into the District's procedures. The District should reevaluate its procedures and make changes as necessary to improve the timeliness of the reconciliation process.
  - b. The District should establish a clear line of authorization necessary to perform transfers, withdrawals, or other actions related to the investments and the general cash accounts. The Board should also review and approve the monthly investment reports prepared by the Accounting Division.
- 3. Review the LID loan activity during the calendar years 2006 through 2009, including assessments collected to service the debt and the debt service payments made.**

We performed interviews with the Board of Directors and management and reviewed selected Board minutes and other documentation.

*General findings:*

- a. Based on our testing and interviews, we did not identify any irregularities or significant accounting errors related to the customer refunds of LID loan balances. However, we did note that there is conflicting information regarding whether the refunds were ultimately necessary or if the LID loan balances should have been maintained and the collection of payments continued.

*Recommendations:*

- a. Supporting documentation of research and conclusions for significant accounting decisions should be maintained and organized. This would help accommodate future inquiries from the Board, management, or the general public.
- 4. Review the refunds to customers during the calendar years 2006 through 2009, using sampling techniques.**

We performed testing on selections of General Ledger activity and manual Journal Entries for the years 2006 through 2009. Based on interviews with the Board of Directors and management, we expanded our selection scope to also include payroll, cash receipts, and accounts payable.

# Kennewick Irrigation District

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## Agreed-upon Procedures Performed (continued)

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### *General findings:*

- a. Many of the District's customers are sent a standard bill even though their assessments are collected by their mortgage escrow accounts. This has resulted in customer confusion and has necessitated the periodic review and refund of avoidable credit balances.
- b. Nonrecurring journal entries are kept in binders with supporting documentation and evidence of preparer and reviewer sign-offs. However, it was noted in some instances that the review had not occurred for a month or more following the initial creation and posting of the entry.
- c. Recurring batch entries and related supporting documentation are kept accessible in the Accounting Division. However, it was noted that evidence of sign-offs was generally limited to the Springbrook user names on the attached reports.

### *Recommendations:*

- a. None. The District already has changes in process to address the issue.
  - b. Increase efforts to perform reviews timely. This is a best-practice for all areas within the Accounting Division.
  - c. Require a cover sheet be attached to all journal entries and require sign-offs by the authorized preparers and reviewers. The District Manager or Treasurer should periodically review the files to check for adequate documentation of review.
- 5. Review existing documentation of internal controls over financial reporting for the calendar years 2006 through 2009. This will include the following:**
- a. **Identify the key financial operating controls.**
  - b. **Identify the key information technology controls and analyze the accounting software utilized in the financial reporting process.**
  - c. **Interviews with staff and management to document financial departmental policies, procedures, and internal controls.**
  - d. **Interviews with Board members to document Board policies and procedures.**
  - e. **Analyze control deficiencies identified during the process.**

# Kennewick Irrigation District

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## Agreed-upon Procedures Performed (continued)

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- f. **Recommend changes in procedures to remediate key control deficiencies, based on industry best practices, and/or identify mitigating controls.**
- g. **Perform a walk-through of processes to verify the practices of KID as compared to the documented controls.**

We performed walkthroughs and interviews with Accounting Division staff and other critical personnel. We adapted our scope and procedures as necessary, based on the information gathered during the interview and walkthrough processes. In addition, an Information Technology Specialist reviewed the District's controls surrounding its information technology processes. The Specialist's findings are documented in the attached TROI IT Solutions report.

*General findings:*

- a. The lack of adequate segregation of duties was noted to be a systemic problem throughout the District. The most critical issues identified are as follows:
  - i. The recording of cash receipts and the posting of payments to customer accounts are both performed by the Accounting Technician.
  - ii. The processing of invoices, posting to accounts payable, and the printing of accounts payable disbursement checks are all performed by the Accounting Technician.
  - iii. The Human Resources module within Springbrook has not been implemented. Functions normally segregated by this module are being performed with the payroll module, which is fully accessible by the Accounting Clerk and the Human Resources Manager. The Accounting Clerk has full access to payroll functions per above and also prints manual payroll checks and prepares the ACH direct deposit files.
  - iv. The Accounting Manager has the administrative user account for the District's online banking. The administrator user account can add new users, assign rights to existing users, change settings, and perform other critical functions. Additionally, the Accounting Manager can perform direct transfers between bank accounts and can redeem certificates of deposit without the need for a second or third level of review and electronic authorization.
- b. The District's current policy manual is primarily limited to operational issues such as vacation, sick leave, holidays, safety, reimbursements, etc. Although some staff have developed their own documentation, the Accounting Division does not have a formal, approved set of policies and procedures related to the financial reporting functions of the District.

# **Kennewick Irrigation District**

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## **Agreed-upon Procedures Performed (continued)**

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- c. The Treasurer lacks the necessary accounting background to fully perform the basic functions required of an accounting department manager and to utilize the Springbrook software. As such, the District has not been provided with accurate, complete, and timely financial reports, nor has the District benefited from its substantial investment in new accounting software.
- d. The District does not have a consistent system of performing periodic inventory counts. This is a substantial weakness in the system of controls and has the potential for allowing abuse, including fraud and other defalcation, to exist and not be detected.
- e. Purchase orders are, at times, approved after the purchase has already occurred. Field staff are allowed to call the District office to obtain a purchase order number from an Administrative Assistant while in the process of making a purchase. This circumvention of the purchase order process may allow expenditures that are not legitimate or appropriate, or are fraudulent, to be incurred by the District.
- f. The District has nine credit cards issued to management and other personnel. Testing indicated that receipts are not always retained by personnel and management review and authorization is not performed timely on a consistent basis. Additionally, there are instances where a company card is used without the individual to whom the card is issued being present. When support was requested for one credit card transaction, the Accounting Technician reported that the supporting packet for the entire month's credit card activity was unaccounted for.
- g. The purchasing function for the District's operations has traditionally been performed at many levels of management. This practice causes a loss of control and efficiency.
- h. Our scope was expanded to include the review of personnel files for integrity and proper documentation of pay increases and performance reviews. We noted a lack of documentation supporting pay increases and performance reviews in multiple personnel files. Specifically, there was no written authorization from the Board of Directors regarding the District Manager's pay increase in January 2009.

### *Recommendations:*

- a. The District should evaluate the roles and responsibilities of the Accounting Division staff and other personnel involved in the financial reporting processes. The implementation of the Human Resources module and leveraging other functions within Springbrook to control user access privileges will improve segregation significantly.

# **Kennewick Irrigation District**

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## **Agreed-upon Procedures Performed (continued)**

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- i. To improve controls over receipts, we suggest that an employee independent of the receivable function prepare a list of daily cash receipts. Another employee should then be responsible for retaining the actual checks and for making the bank deposit. Also, the Credit Manager's access to cash receipts should be terminated. Only customer remittance invoices should be forwarded to the receivable department and, where none exist, a copy of the check or an internally prepared remittance form should be used.
  - ii. It is desirable to segregate the duties of processing invoices and accounts payable from the printing and mailing of expense disbursement checks.
  - iii. This combination of duties is completely incompatible and significantly increases the chance of an error or irregularity going undetected. We recommend, at a minimum, the standard Human Resource functions be separated from the other payroll processes.
  - iv. We strongly recommend that the District receive a complete and clear understanding from the banking institution of the abilities granted as a function of online access. Transfer authorization should only be made accessible to a limited number of people, and transfers should be restricted to only the District's accounts within the bank. Policies and procedures should be developed that incorporate effective controls and safeguards over cash activities for any online access situation.
- b. A detailed accounting manual should be developed that includes policies on general internal controls, general ledger and journal entries, cash, fixed assets and supplies, purchasing, employee reimbursements, cash, revenue, investments, long and short-term liabilities, payroll, and human resources. A written policy gives personnel clear and consistent guidance to perform their functions and, if necessary, perform as a backup during a vacation or emergency.
  - c. The District should require the Treasurer to attend trainings or classes to obtain the basic skills necessary to perform his functions.
  - d. Physical counts of inventory should be performed at least quarterly. The results should be reviewed and reconciled to the perpetual system by the Accounting Manager. The perpetual inventory listing should be reconciled to the general ledger, with any large discrepancies investigated and explained. Any adjustments, along with the cost of goods sold entries, should be made and a procedure should be implemented to allow for these adjustments to occur on a monthly basis.
  - e. The pre-authorization of purchase orders is a critical internal control to ensure that expenditures are valid and appropriate. The District should conduct employee trainings to educate staff about

# **Kennewick Irrigation District**

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## **Agreed-upon Procedures Performed (continued)**

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the required procedures. This should be followed by strict enforcement by the Board of Directors and management.

- f. The District should discontinue the use of company credit cards and implement a reimbursable expense policy. This type of policy shifts the burden of proof to the employee as they are at personal financial risk to front the expense, which creates personal incentive for employees to substantiate their expenditures as valid and appropriate. Timeliness of submittal of documentation is also improved due to employee's desire to be reimbursed as soon as possible.
- g. We suggest that the District centralize the purchasing function and assign responsibility for major categories of goods purchased to specific individuals within the Purchasing Department. This would allow for more frequent individual contact with suppliers. Additionally, by consolidating all District purchases of large quantities, better volume discounts may be possible.
- h. A checklist, or other means of documentation, should be included in personnel files to ensure they contain adequate documentation of changes to pay rates, hours, benefits, or other items and also include the required annual performance evaluations.

**6. Review land sales and contracts during the calendar years 2006 through 2009 and analyze the sources and uses of funds within the realty fund.**

We reviewed land sales contracts for 2006 through 2009 and interviewed Realty Division personnel to determine the sources and uses of funds within the realty fund.

*General findings:*

- a. During our analysis of the Realty Division land transactions based on contracts and other documentation within the specified period, we noted that the sources of funds are from land sales. The proceeds are used for Realty Division operating expenses and deposits into the reserve fund.

*Recommendations:*

- a. See Procedure 7 below.

**7. Review the reserve fund for the calendar years 2006 through 2009 and analyze the sources and uses of funds. This will include the following:**

- a. **Analyze policies and procedures surrounding reserve fund disbursements.**
- b. **Reconcile the reserve fund balance for the calendar years 2006 through 2009, identifying sources and uses of funds.**

# Kennewick Irrigation District

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## Agreed-upon Procedures Performed (continued)

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- c. **Identify any specific instances of disbursements made from the reserve fund that were inconsistent with identified policies and procedures, based on our analysis and reconciliations.**

We discussed the history and other aspects of the reserve fund with members of the Realty Division and interviewed staff members, management, and the Board of Directors. We also reviewed investment activity for the years 2006 through 2009, focusing on disbursements from the reserve funds.

*General findings:*

- a. Based on review of monthly cash investment reports for the years 2006 through 2009, we noted that the District's investments continued to decrease as its CD's were redeemed monthly by the Accounting Division to cover operating expenses. We were unable to identify documentation supporting the appropriate authorization of the transfer of investment funds to the operating cash account. Additionally, we were unable to identify evidence that the Board of Directors received and reviewed the monthly investment reports.
- b. We were unable to perform a reconciliation of the reserve fund or perform a detailed analysis of disbursements due to a lack of sufficient documentation. Per our review procedures, it appears that a significant portion of the reserve was used for general operations.

*Recommendations:*

- a. The District should establish a clear line of authorization necessary to perform transfers, withdrawals, or other actions related to the investments. The Board should also review and approve the monthly investment reports prepared by the Accounting Manager.
- b. The District should maintain documentation related to transactions within all funds, to provide an adequate audit trail and to monitor activity within each fund.

### 8. Other items.

We performed a review of the Board of Directors meeting minutes for the years 2006 through 2009.

*General findings:*

- a. The Board voted to eliminate Policy 67 at its February 7, 2006 meeting. One of the criteria for amending the policy, per the original Policy 67 approved by the Board on December 9, 1997:

*Two (2) votes by the Board of Directors to amend the endowment must be held. Said votes to amend the endowment must have unanimous approval by the Board of Directors. These votes shall be memorialized by appropriate resolutions and shall be taken at two regularly scheduled Board meetings, no less than 30 days apart and no more than 60 days apart.*

# **Kennewick Irrigation District**

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## **Agreed-upon Procedures Performed (continued)**

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Per the February 7, 2006 minutes, the motion to eliminate Policy 67 was carried despite the opposition of one Board member. In addition, there is no indication from the Board minutes that the second, required, vote took place during the time period specified above.

*Recommendations:*

- a. The Board needs to research and follow procedures set for itself by its predecessors.

We believe that the implementation of these recommendations will provide Kennewick Irrigation District with a stronger system of internal control while also making its operations more efficient. We will be happy to discuss the details of these recommendations with you and we would like to assist the District in implementing these recommendations with a detailed action plan to be created in cooperation with the District Manager and his staff.



# **Kennewick Irrigation IT Audit Review**

March 9, 2010

Below is the summary for the IT Audit performed on March 9, 2010. This IT Audit was performed on-site with Clark Haueter, District Treasurer; Brad Crawford, IT Specialist; Deannette Warn, Accounting Technician and Chuck Freeman, District Manager.

## System Development

- Kennewick Irrigation District, KID, does not develop or modify application systems. Changes to their core accounting system, SpringBrook, are made by the vendor. Implementation instructions are supplied to the client when updates to the SpringBrook application are required. The SpringBrook vendor does not have access into the client's network.

## Change Management

- Significant software vendor upgrades or changes related to critical information technology infrastructure are tested and approved prior to being released into production. The level of testing depends on the complexity and risk of the change to critical financial systems. This process is not formally documented.

## Security and Access - Logical

- Application access is segregated by department and appropriate access is granted by logical groups.
- There is one system administrator for the network and one system administrator for SpringBrook.
- The Default Domain Security Setting requires passwords to be changed every 90 days. Passwords are required to be 6 characters long and require both characters and numbers to be part of the password. The "Passwords must meet complexity requirements"

setting is enabled. Password procedures are followed but not formally documented.

- Application-level segregation of duties is enforced by assigning user access rights to predefined roles, but the users assigned to these roles are not periodically reviewed by management.
- The current remote access configuration allows all authenticated users, via Terminal Server, to have complete access into their network, but this process is not monitored by management.
- Antivirus software definition files are current and appropriately updated to workstations.
- Unsuccessful login attempts are captured, but not reviewed by IT or management.
- In general, departments and users are segregated by job functions with no access to one another. Only members of specific departments are granted system access based on their job functions within the organization.

## Security and Access – Physical

- The KID computer room containing telephony, network equipment and servers is secure and the environment is properly controlled.
- Access codes are required to enter the computer room and these codes are restricted to appropriate management and IT staff.
- The computer room does not have an adequate fire suppression system.
- A Linux firewall is in place to protect KID from unauthorized internal and external network access.

## Computer Operations - Data Backup

- Backup procedures are in place, but they are not documented or approved by management.
- Full backups are performed weekly, monthly, and quarterly.
- Backup tapes are secured offsite.
- Random files are periodically restored from the backup tapes to verify the reliability of the media.

## Computer Operations - Third Party Vendor Management

- Third-party contracts are reviewed and approved by management prior to being signed.
- An individual is assigned to manage the third-party relationship. This management function includes approval of major changes to the hardware and software installed by the third party.

## Application Controls

- Data input and output are reviewed for general acceptability and completeness, including any control totals.
- User accounts are unique and appropriate application controls are in place.

## End User Computing

- No End User Computing application is used by the client.

## Electronic Commerce

- System initiated Public Network transactions, which release entity assets or commit entity resources, are reviewed by an appropriate supervisor before releasing of assets or commitment of resources.
- Activity is monitored and reviewed by appropriate supervisory personnel. All users such as customers/vendors are identified and authenticated before further transaction processing takes place.
- All users are restricted from accessing private or proprietary data.
- Software is used to ensure data is completely and accurately transmitted or received. Data is reconciled and balanced in a timely manner and the reconciliation is reviewed by appropriate supervisory personnel.

## **Suggested IT Best Practice recommendations for follow up:**

1. The client should formally document their Change Management policy and procedures. It should document responsibilities of management, users and the board of directors.
2. The client's Security Policy should contain a Password and Authentication Policy. This policy should included responsibilities for management, staff, and the board of directors.
3. Management should periodically review user access rights to verify that they are appropriate for the staff's job duties.
4. The client should consider using a VPN connection to manage remote access. The Security Policy should include an Access Control Policy which would include management approval and monitoring.
5. Unsuccessful login attempts should be monitored by the IT staff. The IT Security Policy should contain an Incident Response Plan that documents the responsibility of management and staff.
6. A fire extinguisher should be added to the computer room.
7. The client's Security Policy should include a Disaster Recover Policy that addresses management and staff responsibilities.
8. Best practices recommends that the organization's data should be backed up daily, not weekly.

TROI found no significant deficiency or material weakness items; the design and/or effectiveness of operation of the IT general controls do not adversely impact the reliability of application controls including manual controls that rely on information produced by the accounting system.