



INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL
REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN
AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE
WITH *GOVERNMENT AUDITING STANDARDS*

Town of Forest Heights
Forest Heights, Maryland

We have audited the financial statements of the governmental activities and the major fund of the Town of Forest Heights, Maryland, as of and for the year ended June 30, 2004, which collectively comprise the Town of Forest Heights, Maryland's basic financial statements and have issued our report thereon dated August 15, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Town of Forest Heights, Maryland's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Town of Forest Heights, Maryland's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying Description of Findings as items 2004-1 through 2004-10.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider items 2004-1 through 2004-10 to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Town of Forest Heights, Maryland's financial statements are free of 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 statements 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 instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* which are described in the accompanying Description of Findings as item 2004-11.

This report is intended solely for the information and use of the audit committee, management, and Town Council, and is not intended to be and should not be used by anyone other than these specified parties.

Bridgett, Mock & Associates, P. A.

Waldorf, Maryland
August 15, 2005

**TOWN OF FOREST HEIGHTS MARYLAND
DESCRIPTION OF FINDINGS
For The Year Ended June 30, 2004**

2004-1 AUDIT PLANNING AND ASSISTANCE

At the time of the audit, the Town of Forest Heights's accounting records, supporting schedules, documents, and other files were not in order and were in a general state of disarray. This extreme level of disorganization has the potential to cause serious errors in the financial records and financial statements. There is also a substantial risk that irregularities such as fraud and defalcation could occur and, because there is no reliable system of detection, continue undetected. This severe situation should be corrected as soon as possible with the establishment of an accounting system that contains adequate controls and related checks and balances. The future of the Town of Forest Heights is dependent on its ability to establish and maintain a sound accounting system that produces timely and accurate financial information. We have made the Town of Forest Heights aware of this, and we suggest that efforts be made during the current year to improve accounting processes and the condition of the records and files. Orderly accounting records and supporting document files should be maintained on a consistent basis so that this information is readily available to the Town of Forest Heights. Financial statements should be well supported by the corresponding backup information included in these records.

2004-2 ESTABLISH AND IMPLEMENT ACCOUNTING POLICIES AND PROCEDURES

As a result of our audit, we found an overall lack of review and reconciliation in many areas of the accounting and finance functions. We noted numerous instances where input was duplicated and journal entries and transfers between accounts were incorrect. We feel that the contributing factors to the deficiencies mentioned above include:

- Consistent turnover in accounting department and administration.
- Lack of well-defined accounting policies and procedures.
- Lack of training in the accounting department.

It is imperative that the Town of Forest Heights establish review and reconciliation policies and procedures at all levels of management. We feel that many of the problems identified by the audit process could have been avoided or brought to the attention of management much earlier if the records were reviewed and reconciled on a timely basis by appropriate personnel.

2004 -3 ACCURATE POSTINGS

There has been continuous turnover at the Town Administrator position and the Treasurer position, leading to conflicting procedures and a growing backlog of current transaction processing and lost and misplaced documentation. This disorganization in the accounting function will continue to weaken internal controls and the ability to produce accurate financial statements. During our audit procedures, we noted numerous posting errors, which required that corrections be made. This particular type of error is such that some errors may never be discovered. All adjusting entries should be documented and supported by a description indicating the need for such adjustments.

We strongly recommend the Town hire competent accounting staff. The Town of Forest Heights should give the accounting department issues the highest priority in the upcoming months.

2004-4 CASH MANAGEMENT

During our fieldwork, we noted the Town of Forest Heights went through extended periods without a definitive and reasonable estimate of its current cash flow position. Continued problems in receiving timely and current financial information can significantly impact management's abilities, such as providing relevant oversight and budgetary control. This has seriously impacted the Town of Forest Heights' ability to effectively and efficiently monitor its operations and manage its cash flow. We strongly suggest that the Town of Forest Heights' accounting staff post transactions on a timely basis.

During the audit, we also noted that bank statements for the Town of Forest Heights' various accounts were not reconciled to the general ledger. We recommend that all of the bank accounts be reconciled monthly to the general ledger and that all reconciling items be promptly investigated and adjusted with adequate explanations. We suggest the Town of Forest Heights' manager regularly review the bank reconciliation. If these tasks can become routine and accurate, cash management procedures can then be enacted, which could result in much improved interest earnings.

We also recommend that the inactive bank accounts be reviewed to determine the necessity for these accounts. We noted several accounts with no activity other than service charges.

2004-5 CASH RECEIPTS: SEGREGATION OF DUTIES

We noted that there was a lack of segregation of duties within the cash receipts area. The objective of internal control over cash receipts is to obtain control over amounts received at the time of receipt. Currently, the Town has one employee handling the cash receipts functions. We feel that separating these closely related functions in the cash receipts system of the Town of Forest Heights will result in much greater internal control in this particular area. To achieve this control, certain duties involving receipts should be handled by more than one member of the Town of Forest Heights' personnel. The following are examples of procedures that could be enacted to improve efficient internal control:

- One employee, preferably the receptionist, should open the mail, make a control list of all receipts, and restrictively endorse all items received as “for deposit only.” This would prevent any unauthorized endorsement should the checks be misplaced or lost before being deposited.
- The receipts should then go to another employee for further processing and deposit to the bank on a timely basis.
- Then, someone who does not otherwise handle receipts should compare the deposit slips to the list of receipts to ensure that all funds reflected on the receipts were deposited.

We were unable to trace at least one deposit confirmed by the state for police protection to the bank statements.

2004-6 PERSONAL PROPERTY TAXES

During our audit, we noted that the business personal property taxes had been billed randomly. This is a significant source of revenue for the Town. We recommend management review the personal property billing process and implement procedures to insure all Town businesses personal property tax assessments are billed and collected in a timely manner.

2004-7 SUPPORT FOR CASH DISBURSEMENTS NEEDED

In numerous instances, we noted that check copies were the sole documentation retained in support of disbursements. To provide adequate disbursement documentation, a copy of the invoice, or a check request form containing a description of the purpose when there is no invoice, should be retained for each disbursement. We suggest that this practice be initiated as soon as possible. Also, approval should be clearly noted on the invoice by the responsible party.

2004-8 CASH DISBURSEMENTS: SEQUENTIAL, NUMERICAL CHECK CONTROL

While conducting cash disbursements testing, we noted that many checks were written out of sequence. Cash disbursements control procedures should be designed to be practicable and to provide reasonable assurance that no unauthorized payments are made, all liabilities are timely paid, and payments are accurately recorded. These controls include accounting for the sequential order of checks as they are released for use, prior to preparation. We recommend that strict numerical control be kept over all checks issued and that checks be issued in sequence.

2004-9 PAYROLL

Payroll costs are the single highest expense category for the Town. A strong system of internal controls should be implemented to avert and detect errors and misappropriations. The following functions should be performed:

- Comparison of actual expenses to budgeted information and review of unexpected variances.

- Close supervision and review of reports prepared by the outside payroll service.
- Separation of payroll functions of employment, timekeeping, payroll preparation and record keeping.
- The Town improperly recorded the payroll expense during the year. The employee-net payroll was charged to the expense accounts and all the payroll taxes were grouped together. The payroll posting should be a consistent recurring adjustment each pay period.

2004-10 PENSION PLAN

The contributions to the pension plan on behalf of the Town employees should be made in a timely manner. We noted that two years of contributions were made in fiscal year 2004. We also encourage the Town to determine if all the necessary filing requirements for the pension plan are current and the plan documents meet the Internal Revenue Service regulations.

2004-11 OVER-EXPENDITURE

The Town's actual expenditures exceeded the budgeted amount by \$87,564. This is in violation of the Town's charter. The Administrative department, Public Works, and the Police department overspend their budgets. We recommend the actual revenues and expenses as compared to the budget be reviewed periodically and budget amendments made when necessary.