



Management Letter

March 13, 2015

To the Honorable County Judge and
Members of the Commissioners' Court of
Polk County, Texas:

The American Institute of Certified Public Accountants Statement on Auditing Standards No. 115, *Communicating Internal Control Related Matters Identified in an Audit* (SAS 115), provides guidance to auditors on communicating internal control matters to management and the governing body, board of directors, or equivalent body.

It is important to note when reviewing findings reported within this letter that classification of the findings is based on the definitions required by SAS 115 as further discussed below. Please note that these classifications are based on the potential impact to the financial statements, not necessarily the likelihood of actual loss to Polk County, Texas (the "County"). Accordingly, the County's assessment of the "significance" or ranking of severity will likely be substantially different based on a number of factors including, but not limited to, its assessment of risk and the cost benefit of making the change.

Our report is as follows:

In planning and performing our audit of the financial statements of the the governmental activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the County as of and for the year ended September 30, 2014, in accordance with auditing standards generally accepted in the United States of America, we considered the County's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing an opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the County's internal control. Accordingly, we do not express an opinion on the effectiveness of the County's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies and other matters.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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Our findings and additional comments are as follows:

CURRENT YEAR MATTERS:

Significant Deficiencies:

2014-001. REDACTED REPORTING

Certain communications have been made to Commissioners' Court in executive session. The conditions giving rise to present the information in a nonpublic form still exists. As this letter is subject to open records request, matters presented to Commissioners' Court are excluded from this letter.

Criteria

(Redacted)

Condition

(Redacted)

Effect

(Redacted)

Cause

(Redacted)

Recommendation

(Redacted)

2014-002. DISTRICT CLERK BANK DEPOSITS

Criteria

Based on County policy, the District Clerk's office is responsible for accounting for, and making timely deposits of, money received from different sources.

Condition

Review of bank accounts received from the District Clerk's office shows large deposit amounts consisting of smaller collected amounts being deposited into the District Clerk's accounts twice during the year. One money order appears to have been held for three years. In addition, the District Clerk's registry of the court bank account has an outstanding deposit of \$7,000 dated March 5, 2007.

Effect

The District Clerk's office is responsible for money collected from different sources. If money is not deposited when collected, the risk is high for loss from theft or fire.

Cause

The District Clerk's office is holding checks and not depositing them in a timely manner. The District Clerk is the only individual who is responsible for making deposits for the trust accounts; however, this is not done on a daily basis.

Recommendation

The District Clerk's office should immediately implement a plan to make timely deposits of any checks received and record activity accurately. The District Clerk's office should assign the responsibility of taking trust deposits to the bank on a daily basis to more than one individual.

Management's Corrective Action Plan

The District Clerk's office agrees with this recommendation and is in the process of instituting procedures that will establish this process. The office plans to have the new process implemented by the end of the 2015 fiscal year.

2014-003. DISTRICT CLERK BANK RECONCILIATIONS

Criteria

Based on County policy, the District Clerk's office is responsible for balancing and reconciling bank statements and accurately accounting for District Clerk trust funds. A copy of the reconciliation report, applicable monthly bank statement, and other supporting documentation must be forwarded to the County Auditor by the 20th of the following month.

Condition

On August 5, 2014, certain reports, bank statements and reconciliations were requested from the District Clerk's office. Bank reconciliations were received February 25, 2015, after the conclusion of our on-site audit. The court records to verify the funds were not received as of the date of this letter.

Effect

The District Clerk's office is at high risk for loss from fire or theft of funds due to lack of accounting for cash and not reconciling bank statements.

Cause

The District Clerk's office does not reconcile bank statements in a timely manner.

Recommendation

The District Clerk's office should immediately implement a plan to reconcile cash monthly. The District Clerk's office should submit the reconciliation report, applicable monthly bank statement and other supporting documentation by the 20th of the following month.

Management's Corrective Action Plan

The District Clerk's office agrees with this recommendation and is in the process of instituting procedures that will establish this process. The office plans to have the new process implemented by the end of the 2015 fiscal year.

2014-004. DISTRICT CLERK TAX SALES FUNDS

Criteria

Based on Texas Government Code, the District Clerk's office is responsible for collecting money from tax sales, accounting for money collected and disbursement of funds to appropriate agencies or individuals.

Condition

The District Clerk's office has not disbursed funds related to tax sales for many years as presented in the court minutes and discussed in detail with the County Auditor's office.

Effect

The District Clerk's office is at high risk for misappropriation of funds due to lack of accounting for tax sales.

Cause

The District Clerk's office has not disbursed funds from tax sales as presented in Commissioners' Court minutes and discussed in detail with the County Auditor's office. Documentation was requested from the District Clerk's office on August 5, 2014 and has not been received as of the date of this letter.

Recommendation

The District Clerk's office should immediately implement a plan to disburse all funds with court orders to release funds to agencies or individuals.

Management's Corrective Action Plan

The District Clerk's office agrees with this recommendation and is in the process of instituting procedures that will establish this process. The office plans to have the new process implemented by the end of the 2015 fiscal year.

2014-005. DISTRICT CLERK COURT RECORDS

Criteria

Texas Government Code Title 2, Subtitle D, Chapter 51, Subchapter D, Sec. 51.303 states "the clerk of a district court has custody of and shall carefully maintain and arrange the records relating to or lawfully deposited in the clerk's office."

Condition

Court orders to verify all of the trust account receipts and disbursement were requested on August 5, 2014 from the District Clerk's office and were not provided as of the date of this letter. Without these documents, the balances of accounts were unable to be verified.

Effect

Funds collected by the District Clerk's office are possibly not accounted for correctly.

Cause

The District Clerk's office is at high risk for loss from fire or theft of funds due to not being carefully maintained.

Recommendation

The District Clerk's office should provide all documentation previously requested. The District Clerk's office should carefully maintain all records according to government statute.

Management's Corrective Action Plan

The District Clerk's office agrees with this recommendation and is in the process of instituting procedures that will establish this process. The office plans to have the new process implemented by the end of the 2015 fiscal year.

Other Matters:

2014-006. COLLATERAL PLEDGED SECURITIES

Background

The County is required to have bank accounts collateralized by securities with a collective market value that exceeds bank balances.

Finding

As of September 30, 2014, bank balances exceeded the market value of pledged securities and FDIC insurance for the County.

Recommendation

The County should acquire additional pledged securities in order to meet the collateral requirement.

2014-007. GASB STATEMENT NO. 68, ACCOUNTING AND FINANCIAL REPORTING FOR PENSIONS

Background

In 2015, all local governments will begin to report their pension liability on their financial statements resulting in some governments reporting deficit equity positions. As some governments' pension liability

becomes front page news, it is likely that pension liability will move to the arena of public discussions and, accordingly, elected and appointed officials need to be prepared to be familiar with key talking points, as noted in the recommendations below.

In June 2012, the Governmental Accounting Standards Board (GASB) issued Statement No. 68 (“GASB 68”), *Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27*, which replaces the requirements of GASB Statement No. 27, as well as the requirements of GASB Statement No. 50, as they relate to pensions that are provided through pension plans administered as trusts or equivalent arrangements. GASB 68 will be effective for fiscal years beginning after June 15, 2014. The requirements of GASB Statement Nos. 27 and 50 will remain applicable for pensions that are not covered by the scope of GASB 68.

GASB 68 establishes new standards of accounting and financial reporting for defined benefit and defined contribution pensions provided to the employees of state and local governmental employers. This statement establishes new standards for measuring and recognizing liabilities, deferred outflows of resources, deferred inflows of resources, and expense/expenditures, in addition to new disclosure and Required Supplementary Information reporting requirements. Implementation of GASB 68 will represent a significant change in the accounting and reporting of pension expense and the related liability. For fiscal year 2015, the County will be required to recognize its long-term obligation for pension benefits as a liability in its government-wide statements.

Key changes to financial reporting and disclosures required by GASB 68 are as follows:

- A net pension liability (unfunded accrued liability) will be recognized on the Statement of Net Position. Previously this was a note disclosure only.
- This liability amount being reported will likely be higher than the amount previously disclosed, as the following changes will impact the calculation:
 - Changes in the allowable amortization periods will result in larger expenses than previously reported.
 - Previous statements provided up to six allowable actuarial cost methods. GASB 68 will require the use of only the entry age normal cost method.
 - Previous standards allowed various asset smoothing methods to determine the values of plan assets. GASB 68 will require plan assets to be reported at fair market value.
 - New terminology (net pension liability and total pension liability) will be used.
 - Pension expenses will become more variable.
 - More extensive disclosures and Required Supplementary Information will be included.

Key changes to the County’s operations as a result of GASB 68 are as follows:

- Management will now be responsible for documenting and taking responsibility for controls related to employee data being transmitted to its pension plan administrator.
- The County’s independent auditor will now be required to review and test controls related to employee data being transmitted to the pension plan administrator.

Recommendation

Key talking points that management and elected officials should consider are:

1. The fundamentals of the government's finances have not changed.
2. This is an accounting rule change only.
3. Pension liability is a long-term liability paid off in the future.
4. The County is a member of Texas County and District Retirement System (TCDRS) and has made the necessary annual contributions as calculated by TCDRS' actuary.
5. Fund balance remains the best measure of the financial health of a government.

As a result of this new accounting statement, it is important that management has reviewed and documented its internal controls over pension benefits. Internal controls should include various activities over pension benefits, such as plan design and modifications, employee eligibility, employee and employer contributions, reporting, and application for plan benefits. In addition, it is the employer's responsibility for ensuring the reasonableness of its pension liability. Factors to be considered in determining reasonableness include reviewing evidence used in determining the total pension liability such as assumptions made and completeness of the census data provided to the actuary. Possible procedures to ensure accuracy of the census data could include tracing active employees from payroll records to census data and checking key information, tracing current year terminations per payroll records to census data to verify status and date of termination, and tracing key data from the census file back to originating employment records.

TCDRS will be providing the County with the information necessary to report its total pension liability and related disclosures. TCDRS is anticipating this information will be available to counties in May 2015 via the County Portal. If the County has not already signed up for access to TCDRS resources on the County Portal, it is highly recommended to do so. More information on this can be found at <https://www.tcdrs.org/Pages/Home.aspx>

Additional resources can be found on our website, www.texasauditors.com, as well as <http://www.gasb.org/jsp/GASB/Page/GASBSectionPage&cid=1176163527940> where GASB has provided an implementation toolkit for governments. Additionally, we will send out client alerts as additional information becomes available on this topic.

This communication is intended solely for the information and use of management, County Judge, Commissioners' Court and others within the County, and is not intended to be and should not be used by anyone other than these specified parties.

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September 30, 2014
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We would like to thank the members of Commissioners' Court, the County Judge, and the County's management for their cooperation during the course of our audit. Please feel free to contact us at your convenience to discuss this report or any other concerns that you may have.

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