

MUNICIPALITY OF HOSMER
INTERNAL CONTROL REVIEW

October 2, 2024

MUNICIPALITY OF HOSMER
MUNICIPAL OFFICE
October 2, 2024

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RUSSELL A. OLSON
AUDITOR GENERAL

REPORT ON THE LIMITED STUDY OF INTERNAL CONTROL
PERFORMED IN ACCORDANCE WITH SOUTH DAKOTA CODIFIED LAW 4-11-4.1

Governing Board
Municipality of Hosmer
Hosmer, South Dakota

We have made a study of selected elements of internal control of the Municipality of Hosmer (Municipality) in effect on October 2, 2024. Our study was performed pursuant to South Dakota Codified Law (SDCL) 4-11-4.1 and was limited to selected accounting controls contained in the codified laws and other selected controls we felt were significant to the Municipality. Our study was not conducted in accordance with the standards established by the American Institute of Certified Public Accountants for the purpose of giving an opinion on internal control in effect at the Municipality.

The management of the Municipality is responsible for establishing and maintaining internal controls. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control policies and procedures. The objective of internal controls is to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of general purpose financial statements in accordance with generally accepted accounting principles.

Because of inherent limitations in internal controls, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the internal controls to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operations of policies and procedures may deteriorate.

Our study was more limited than would be necessary to express an opinion on internal control of the Municipality. Also, our study would not necessarily disclose all significant weaknesses in internal controls of the Municipality. Accordingly, we do not express an opinion on internal control of the Municipality in effect on October 2, 2024.

However, our study did disclose weaknesses in internal controls of the Municipality in effect on October 2, 2024, as discussed below:

a. The Municipality did not properly maintain the following necessary records:

1. Cash General Ledger
2. Cash Receipts Journal
3. Cash Disbursement Journal
4. Revenue Budget Record
5. Expenditure Budget Record

We recommend the Municipality properly establish and maintain the necessary accounting records.

- b. The 2023 annual financial report contained financial reporting errors resulting in inaccurate and incomplete information being presented to the users of the annual financial report. We recommend the Municipality accurately complete the annual financial report.
- c. The minutes gave a detailed statement of all governmental expenditures approved by name and amount; but did not show the purpose or service rendered as required by SDCL 9-18-1. We recommend the detailed statement of expenditures in the minutes include the name, purpose or service rendered and amount for each expenditure approved as required by SDCL 9-18-1.
- d. The Finance Officer did not perform formal proper monthly cash reconciliations for the accounts held by the Municipality. We recommend the Municipality prepare a formal proper monthly cash reconciliation.
- e. Several part-time employees were hired for the maintenance department and liquor store operations. The wage payments were recorded as an "other" expenditure and not as a "payroll" expenditure. This resulted in these wage payments not being subjected to payroll taxes and not being included in the quarterly filings of Form 941 or the annual filing of the W2 wage statements. We recommend all part time employees wages be recorded as salaries subject to payroll taxes.
- f. The liquor store maintains a petty cash checking account which does not have an established balance. This account should maintain a constant value in which the cash balance plus payments should always agree with an amount established by the governing board. In addition, the liquor store incorrectly deposited revenue in the petty cash checking account related to liquor sales, lottery commissions and amusement machine profits which should have been deposited with the Finance Office. We recommend that liquor store revenues be deposited with the Finance Office. We recommend that the Governing Board review whether the liquor store petty cash checking account is necessary and consider closing the account.
- g. The liquor store maintains a lottery change fund, consisting of a checking account and a petty cash bag, which are used to make payments for winning lottery tickets. The lottery change fund which includes the checking account, petty cash and paid lottery tickets should maintain a fixed amount equal to an amount established by the Governing Board.

The lottery change fund, checking account and petty cash, had a balance over \$55,000 on January 1, 2024, and grew to over \$65,000 in October 2024 because the liquor store incorrectly deposited several months of lottery commissions and amusement revenue into this account, which should have been remitted to the Finance Office.

Recently, the total lottery change fund established balance was set at \$15,000, including both the checking account and the petty cash. We recommend the balance of the lottery change fund which exceeds \$15,000 be remitted to the Finance Officer for the Liquor Fund. We recommend the lottery change fund only be used as a fixed change fund to account for the lottery pay outs and be monitored monthly by the Finance Officer as recommended in the Municipal Accounting Manual.

- h. We observed weaknesses in internal control over the operation of the Municipal liquor store operation.
1. A formal cash count sheet was not available to support the daily sales verification. We have provided a cash count form as an example for the Municipality.
 2. The daily sales recorded entered in the cash register were not recapped daily for each on-sale and off-sale category which is necessary to support the daily deposits. The deposits should agree with the total recorded sales of the cash register.
 3. The daily sales information from the cash register and recap were not provided to the Finance Officer for recording of revenue in the accounting records.
 4. The lottery and amusement machines settlements are performed twice a month by the machine's vendor. The vendor's settlement statements include an amount for reimbursement of lottery payouts and commission for the lottery machines and amusement machines. The settlement statements for the lottery payouts and commissions were not provided to the Finance Officer for recording revenue or monitored by the Finance Officer as recommended by the Municipal Accounting Manual. Not all lottery and amusement commission checks were given to the Finance Officer for deposit and recording in the Liquor Fund and were instead deposited in petty cash checking account and lottery change fund checking account in error.
 5. The purchases and sales of the liquor store inventory were not properly recorded and tracked by type (on-sale, off-sale) and category and a physical inventory was not taken during this review period. We were informed that a new point of sale software has been purchased to control inventory that will assist in monitoring inventory and sale usage. However, a physical inventory is still required to verify the accuracy of the inventory on hand. All of this information is necessary to properly compute the cost of sales and markup return for on-sale and off-sale operations.

We recommend the internal controls over the sales, purchases and inventory of the liquor store operation be strengthened and monitored by the Governing Board and the Finance Officer as recommended by the Municipal Accounting Manual.

This report is intended solely for the use of management and the governing board and should not be used for any other purpose. This restriction is not intended to limit the distribution of this report, which is a matter of public record.



Russell A. Olson
Auditor General

October 2, 2024