

RECORDER OF DEEDS

LUZERNE COUNTY

AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2002 TO JANUARY 31, 2005

CONTENTS

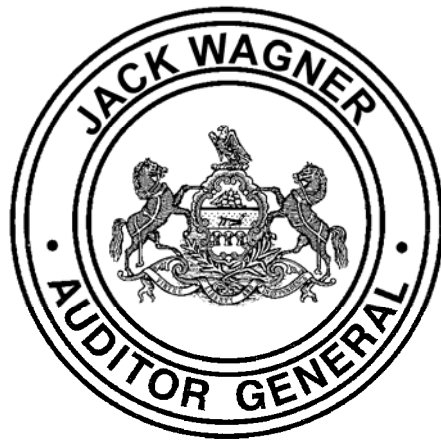
	<u>Page</u>
Background Information.....	1
Independent Auditor's Report.....	3
Financial Statements:	
Statements Of Receipts And Disbursements – Cash Basis:	
Realty Transfer Taxes	5
Writ Taxes And Judicial Computer System/Access To Justice Fees.....	6
Notes To The Financial Statements.....	7
Supplemental Information:	
Schedule 1 – Reconciliation Of Settled Reports – Realty Transfer Taxes.....	9
Exhibit 1 – Schedule Of Reporting Errors And Audit Adjustments – Realty Transfer Taxes.....	11
Report On Compliance And On Internal Control Over Financial Reporting.....	13
Findings And Recommendations:	
Finding No. 1 - Lack Of Internal Controls Over Bank Deposits Resulting In Missing Funds Of At Least \$147,310	15
Finding No. 2 - Inadequate Internal Controls Over The Bank Reconciliations	19
Finding No. 3 - Inefficient Use Of Bank Accounts.....	22
Finding No. 4 - Inadequate Segregation Of Duties	24
Finding No. 5 - Unmonitored System Access.....	27
Report Distribution	31

RECORDER OF DEEDS
LUZERNE COUNTY
BACKGROUND INFORMATION
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

On January 26, 2005 the Luzerne County Recorder of Deeds contacted the Luzerne County District Attorney's office regarding a possible theft of funds. At that time, an employee in the office was suspended pending the outcome of the District Attorney's investigation. According to the officeholder, during the fall of 2004, a bookkeeper in the Recorder of Deeds' Office started noticing a negative cash flow on virtually a daily basis. The Recorder of Deeds began comparing a report which indicates the amount of cash and checks that each register drawer collected and compared that report to the bank deposits. The computer reports indicated that there was more cash collected, according to cash register records, than was reaching the bookkeepers' desk. The officeholder also noticed that a pattern had emerged, whereby several deposits were being held back and deposited several weeks later.

The Department of the Auditor General, Bureau of County Audits, had already planned on auditing the Luzerne County Recorder of Deeds for the period January 1, 2002 to December 31, 2004. Because of newspaper articles relating to the above allegations, it was decided that the updated audit period would be January 1, 2002 to January 31, 2005 and our audit testing would be expanded as deemed necessary by the auditors as a result of the above noted conditions.

The Department of the Auditor General, Bureau of County Audits, audits only the Commonwealth portion of costs collected at the Recorder of Deeds' office. As part of our audit, we determine that if monies are due the Commonwealth, they are remitted to the Commonwealth.



Independent Auditor's Report

The Honorable Gregory C. Fajt
Secretary
Department of Revenue
Harrisburg, PA 17128

We have audited the accompanying statements of receipts and disbursements – cash basis of the Recorder of Deeds, Luzerne County, Pennsylvania (County Officer), for the period January 1, 2002 to January 31, 2005, pursuant to the requirements of Sections 401(b), 401(d), and 902 of *The Fiscal Code*. These financial statements are the responsibility of the county office's management. Our responsibility is to express an opinion on these statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. 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. We believe that our audit provides a reasonable basis for our opinion.

As described more fully in Note 1, the accompanying financial statements were prepared using accounting practices prescribed by the Pennsylvania Department of Revenue, which practices differ from accounting principles generally accepted in the United States of America. The effects on the financial statements of the variances between these regulatory accounting practices and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material. The financial statements present only the Commonwealth portion of cash receipts and disbursements and are not intended to present fairly the financial position and results of operations of the County Officer, in conformity with accounting principles generally accepted in the United States.

Independent Auditor's Report (Continued)

In our opinion, because of the effects of the matter discussed in the preceding paragraph, the financial statements referred to above do not present fairly, in conformity with accounting principles generally accepted in the United States of America, the financial position of the County Officer, as of January 31, 2005, the changes in its financial position, or where applicable, its cash flows for the period then ended.

In our opinion, the financial statements referred to above present fairly, in all material respects, the operations of the County Officer as it pertains to receipts made on behalf of the Department of Revenue, for the period January 1, 2002 to January 31, 2005, on the basis of accounting described in Note 1.

Our audit was made for the purpose of forming an opinion on the financial statements of the County Officer taken as a whole. The accompanying Schedule 1 for the period January 1, 2002 to January 31, 2005, is supplemental information required by the Department of Revenue and is not a required part of the financial statements. The information in that schedule has been subjected to the procedures applied in the audit of the financial statements, and in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 6, 2005, on our consideration of the County Officer's internal control over financial reporting and on our tests of its compliance with certain provisions of laws and regulations. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

This report is intended solely for the information and use of the Pennsylvania Department of Revenue and the County Officer and is not intended to be and should not be used by anyone other than these specified parties.

December 6, 2005

JACK WAGNER
Auditor General

RECORDER OF DEEDS
LUZERNE COUNTY
REALTY TRANSFER TAXES
STATEMENT OF RECEIPTS AND DISBURSEMENTS – CASH BASIS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

Receipts:

Realty Transfer Taxes (Note 2)	\$ 19,454,997
Disbursements to Department of Revenue (Note 4)	<u>(19,500,901)</u>
Balance due Department of Revenue (County) per settled reports (Note 5)	(45,904)
Audit adjustments (Exhibit 1)	<u>45,791</u>
Adjusted balance due Department of Revenue (County) for the period January 1, 2002 to January 31, 2005	<u><u>\$ (113)</u></u>

Notes to the financial statements are an integral part of this report.

RECORDER OF DEEDS
 LUZERNE COUNTY
 WRIT TAXES AND JUDICIAL COMPUTER SYSTEM/ACCESS TO JUSTICE FEES
 STATEMENT OF RECEIPTS AND DISBURSEMENTS – CASH BASIS
 FOR THE PERIOD
 JANUARY 1, 2002 TO JANUARY 31, 2005

Receipts:

Writ Taxes	\$	113,665
Judicial Computer System/Access To Justice Fees		1,321,390
Earned Interest On Commonwealth Funds		<u>207</u>
Total Receipts (Note 2)		1,435,262
Commissions (Note 3)		<u>(3,410)</u>
Net Receipts		1,431,852
Disbursements to Department of Revenue (Note 4)		<u>(1,431,852)</u>
Balance due Department of Revenue (County) per settled report (Note 5)		-
Audit adjustments		<u>-</u>
Adjusted balance due Department of Revenue (County) for the period January 1, 2002 to January 31, 2005	\$	<u>-</u>

Notes to the financial statements are an integral part of this report.

RECORDER OF DEEDS
LUZERNE COUNTY
NOTES TO THE FINANCIAL STATEMENTS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

1. Summary Of Significant Accounting Policies

Basis Of Presentation

The financial statements were prepared in accordance with the requirements of the Pennsylvania Department of Revenue. These financial statements are not intended to present either financial results of operations or financial position in conformity with generally accepted accounting principles.

Basis Of Accounting

The financial statements were prepared on the cash basis of accounting. Under this method, revenues were recognized when received and expenditures were recognized when paid.

Audit Requirement

The financial presentation has been prepared in accordance with Title 72 P. S. Section 401 (b) of *The Fiscal Code*, which requires the Department of the Auditor General to determine whether all money collected on behalf of the Commonwealth has been remitted properly and to provide the Department of Revenue with a report to enable them to settle an account covering any delinquency. A statement of assets and liabilities was not a required part of the financial presentation because of the limited reporting scope by the Recorder of Deeds. Therefore, a statement of assets and liabilities was not audited and is not a part of this report.

2. Receipts

Receipts consist of monies collected on behalf of the Department of Revenue. These include monies collected for the following taxes and fees:

- The Pennsylvania Realty Transfer Tax is a documentary stamp tax of 1 percent on the value of the interest in real property transferred by deed.
- Writ Taxes represent a \$.50 tax imposed on various types of documents and a \$10 tax on notary public commissions processed through the office.
- Judicial Computer System/Access To Justice Fees represent a \$10 fee, for filings after November 1, 2002, imposed for each filing of a deed, mortgage, or property transfer.

RECORDER OF DEEDS
LUZERNE COUNTY
NOTES TO THE FINANCIAL STATEMENTS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

3. Commissions

Acting in the capacity of an agent for the Commonwealth, the Recorder of Deeds is authorized to collect a commission on the Commonwealth's portion of taxes as follows:

<u>Tax</u>	<u>Commission</u>
Realty Transfer	1%
Writ	3%

Commissions of \$194,550 for Realty Transfer Taxes were paid to the County by the Department of Revenue which are not reflected in the statements of receipts and disbursements – cash basis.

4. Disbursements To Department Of Revenue

Realty Transfer Taxes

The Recorder of Deeds participates in the Department of Revenue's cash management system for Realty Transfer Taxes. Under this system, the "Agent" deposits Realty Transfer Tax collections to a local account approved and established in the name of the Department of Revenue, thereby eliminating the need for the agent to issue a check to disburse these taxes.

Writ Taxes And Judicial Computer System/Access To Justice Fees

All disbursements of Writ Taxes and Judicial Computer System/Access To Justice Fees are made by check to the Department of Revenue on a monthly basis.

5. Balance Due Department Of Revenue (County) For The Period
January 1, 2002 To January 31, 2005

This balance reflects a summary of monthly transmittal reports as settled by the Department of Revenue. The balance does not reflect adjustments disclosed by our audit. Refer to Exhibit 1.

6. County Officer Serving During Audit Period

Mary K. Dysleski served as Recorder of Deeds during the period January 1, 2002 to January 31, 2005.

SCHEDULE 1
 RECORDER OF DEEDS
 LUZERNE COUNTY
 REALTY TRANSFER TAXES
 FOR THE PERIOD
 JANUARY 1, 2002 TO JANUARY 31, 2005

Schedule 1 - Reconciliation Of Settled Reports – Realty Transfer Taxes

Date of Summary of Collections Report	Balance Due - Settled Reports Dept. of Revenue (County)	Adjustments	Adjusted Balance Due Dept. of Revenue (County)
2002			
January	\$ (71,809)	\$ -	\$ (71,809)
February	-	-	-
March	10	-	10
April	-	-	-
May	-	-	-
June	(10)	-	(10)
July	-	-	-
August	-	-	-
September	-	-	-
October	-	-	-
November	-	-	-
December	-	-	-
2003			
January	-	-	-
February	-	-	-
March	-	-	-
April	26,018	-	26,018
May	1	-	1
June	-	-	-
July	-	-	-
August	-	-	-
September	-	-	-
October	-	-	-
November	(176)	-	(176)
December	(91)	-	(91)

SCHEDULE 1
 RECORDER OF DEEDS
 LUZERNE COUNTY
 REALTY TRANSFER TAXES
 FOR THE PERIOD
 JANUARY 1, 2002 TO JANUARY 31, 2005

Schedule 1 - Reconciliation Of Settled Reports – Realty Transfer Taxes (Continued)

Date Of Summary Of Collections Report	Balance Due - Settled Reports Dept. of Revenue (County)	Adjustments	Adjusted Balance Due Dept. of Revenue (County)
2004			
January	\$ (200)	\$ -	\$ (200)
February	376	-	376
March	-	-	-
April	-	-	-
May	-	-	-
June	-	-	-
July	-	-	-
August	-	-	-
September	49	-	49
October	(2,502)	-	(2,502)
November	2,430	-	2,430
December	-	-	-
2005			
January	5,990	(5,990)	A -
Balance due Department of Revenue (County) per settled reports			(45,904)
Audit adjustments (Exhibit 1)			45,791
Adjusted balance due Department of Revenue (County) for the period January 1, 2002 to January 31, 2005			\$ <u>(113)</u>

A = Amount represents a prior audit credit for the period January 1, 1998 to December 31, 2001.

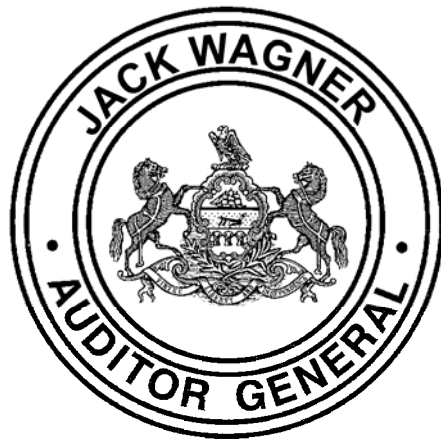
EXHIBIT 1
 RECORDER OF DEEDS
 LUZERNE COUNTY
 REALTY TRANSFER TAXES
 FOR THE PERIOD
 JANUARY 1, 2002 TO JANUARY 31, 2005

Exhibit 1 - Schedule Of Reporting Errors And Audit Adjustments – Realty Transfer Taxes

<u>Month</u>	<u>Year</u>	<u>Total Due Per Settled Report</u>	<u>Total Deposits Per Settled Report</u>	<u>Balance Due Per Settled Report</u>	<u>Audit Adjustment</u>	<u>Explanation</u>
January	2002	318,697	\$ 390,506	\$ (71,809)	\$ 71,809	1
April	2003	357,050	331,032	26,018	<u>(26,018)</u>	2
				Total	<u><u>\$ 45,791</u></u>	

1 = Amount represents a prior audit payment for the months of September 2001 through December 2001.

2 = Amount represents a deposit of \$26,018 which was not credited by the Department of Revenue on the April or May 2003 monthly transmittal.



Report On Compliance and On
Internal Control Over Financial Reporting

The Honorable Gregory C. Fajt
Secretary
Department of Revenue
Harrisburg, PA 17128

We have audited the statements of receipts and disbursements – cash basis of the Recorder of Deeds, Luzerne County, Pennsylvania (County Officer), for the period January 1, 2002 to January 31, 2005, and have issued our report thereon dated December 6, 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.

Compliance

As part of obtaining reasonable assurance about whether the County Officer’s financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement 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 no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the County Officer’s internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance 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,

Report On Compliance And On
Internal Control Over Financial Reporting (Continued)

could adversely affect the County Officer's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. These reportable conditions noted were as follows:

- Lack Of Internal Controls Over Bank Deposits Resulting In Missing Funds Of At Least \$147,310.
- Inadequate Internal Controls Over The Bank Reconciliations.
- Inefficient Use Of Bank Accounts.
- Inadequate Segregation Of Duties.
- Unmonitored System Access.

A material weakness is a 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 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, we consider all the reportable conditions described above to be material weaknesses.

We are concerned in light of the County Officer's failure to correct previously reported audit findings. The County Officer should strive to implement the recommendations and corrective actions noted in this audit report.

This report is intended solely for the information and use of the Pennsylvania Department of Revenue and the County Officer and is not intended to be and should not be used by anyone other than these specified parties.

December 6, 2005

JACK WAGNER
Auditor General

RECORDER OF DEEDS
LUZERNE COUNTY
FINDINGS AND RECOMMENDATIONS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

Finding No. 1 - Lack Of Internal Controls Over Bank Deposits Resulting In Missing Funds Of
At Least \$147,310

The Recorder of Deeds' Office deposited collections into three bank accounts during the audit period:

- Fee book account (Writ Taxes, Judicial Computer Project/Access to Justice Fees, and County Fees)
- Realty transfer tax account (cash management account).
- Municipal tax account (county monies).

The two accounts that involve Commonwealth funds are the fee book account and the realty transfer tax account. At the end of each day, the Recorder of Deeds' Office summarized the receipts per the daily cash receipts journals, per account, and then recorded the amount collected on the deposit slip for each account. The deposit slips were brought to the bank with the collections. However, the aggregate collections of cash and checks taken to the bank were not separated by account or deposit slip. The deposit slips taken to the bank were not always for the receipts collected on the same day and deposits were held for long periods of time as explained in more detail below. The bank credited each account in the amount per the Recorder of Deeds' Office deposit slips.

Our audit revealed significant weaknesses in the internal controls over the bank deposits. The receipts we tested included collections for both the Commonwealth and the County. Therefore, a receipt could be deposited into more than one bank account. Of the 40 receipts tested in which monies were due both the Commonwealth and the County, we noted the following:

- There were 24 receipts in which the Commonwealth's portion of the receipts was not deposited on the same day as collected. The time lapse from the date of receipt to the subsequent date of deposit ranged from two to seven days.
- There were 25 receipts, not associated with Commonwealth monies, which were not deposited on the same day as collected. These monies were deposited into the municipal tax account. The time lapse from the date of receipt to the subsequent date of deposit ranged from 2 to 26 days.

RECORDER OF DEEDS
LUZERNE COUNTY
FINDINGS AND RECOMMENDATIONS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

Finding No. 1 - Lack Of Internal Controls Over Bank Deposits Resulting In Missing Funds Of
At Least \$147,310 (Continued)

- The total days' collections in all 40 receipts did not equal the total amount deposited.
 - Receipts in 34 instances tested totaled \$5,571 greater than the associated deposit. The deposits ranged from \$1 to \$2,375 less than the amounts received.
 - Receipts in 6 instances tested totaled \$622 less than the associated deposit. The deposits ranged from \$6 to \$327 more than the amounts received.

From the 40 receipts tested above, we selected 23 days, plus an additional 8 days, for a total of 31 days, to determine if the mix of cash and checks on the daily cash receipts journals agreed with the mix of cash and checks per the corresponding daily bank deposit slips and noted the following deficiencies:

- On all 31 days, the mix of cash and checks on the daily cash receipts journals did not agree with the mix of cash and checks per the corresponding daily bank deposit slips.
- On 27 days, the total amount of cash deposited was less than the total cash received per the daily cash receipts journals. The difference ranged from \$39 to \$578.

We further tested all 20 business days in January 2005 to determine if total receipts per the daily cash receipts journals agreed with the corresponding daily bank deposits. As of January 31, 2005, there was at least \$147,310 in missing funds which consisted of the following:

- The deposit for collections received on January 25, 2005 for the fee book account was \$10,594 less than the amount received.
- There were four days in which there were no corresponding deposits for collections totaling \$136,716 in the municipal tax account. This included collections of \$35,026 on January 6, 2005; \$46,079 on January 7, 2005; \$21,567 on January 10, 2005; and \$34,044 on January 25, 2005.

However, based on the above testing, it appears monies due the Commonwealth were remitted to the Commonwealth.

RECORDER OF DEEDS
LUZERNE COUNTY
FINDINGS AND RECOMMENDATIONS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

Finding No. 1 - Lack Of Internal Controls Over Bank Deposits Resulting In Missing Funds Of
At Least \$147,310 (Continued)

Good internal accounting controls ensure that all cash, checks and money orders collected for a day equal the cash, checks and money orders deposited. Good internal accounting controls also ensure that all monies collected are deposited in the bank at the end of every day. Without these controls, the potential for money being unaccounted for and/or misappropriated increases significantly.

Recommendations

We recommend that the office improve internal controls over receipts by ensuring that the cash, checks and money orders receipted for the day equal the cash, checks and money orders being deposited for the day. Any discrepancies should be immediately investigated and resolved. We further recommend that the office deposit all receipts at the end of each day as required by good internal accounting controls. Additionally, we recommend that appropriate Luzerne County officials investigate the reasons for the missing funds and take the appropriate actions.

Auditee Response

The Recorder of Deeds responded as follows:

One of the reasons monies receipted on a particular day were not deposited on that day was due in large part to the receipt of funds in the Hazleton satellite office of the Recorder of Deeds. Prior to February 1, 2005, the daily receipts for the Hazleton office were hand delivered to the Wilkes-Barre office. Upon receipt of delivery, these funds were deposited. Based upon this system, the deposits for the Hazleton office receipts were 24 hours behind the actual day of receipt. If the weather was inclement, the delivery could be delayed beyond the 24-hour period. Since February 1, 2005, a new procedure has been instituted. The Hazleton employee takes the daily receipts and makes a night deposit. While night deposits seem to be an obvious solution to the lag time between receipts and deposit of receipts, there is only one employee in the Hazleton satellite office. Because of the night deposits, the Hazleton office now closes early so that the night deposits can be made.

RECORDER OF DEEDS
LUZERNE COUNTY
FINDINGS AND RECOMMENDATIONS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

Finding No. 1 - Lack Of Internal Controls Over Bank Deposits Resulting In Missing Funds Of
At Least \$147,310 (Continued)

Auditee Response (Continued)

We have also utilized the Landex accounting system that now generates a daily report of cash receipts and a separate report for check numbers and check amounts. The Wilkes-Barre office and the Hazleton satellite office have separate daily reports of cash receipts and check receipts. The daily deposits for Wilkes-Barre are done separately. These daily reports are checked against the actual cash deposits and check deposits to insure that they match what the Landex report indicates. Within 24 hours of each deposit, the Recorder or Deputy Recorder verifies the deposit slips for the previous day's deposits against the Landex report. The Recorder or the Deputy Recorder immediately investigates any discrepancies.

The Recorder is without actual knowledge to explain why checks received in the Wilkes-Barre office prior to February 1, 2005 were not being deposited the same day or within 24 hours of receipt by the Office. When the Recorder learned of the almost daily cash shortage in the cash register drawers (which matter led to further investigation of a substantial amount of cash missing in the office and which matter will be further addressed hereinafter), the Recorder and Deputy Recorder investigated further the ledgers maintained by office employees to see if they could explain the cash shortage. Through this investigation, the Recorder first learned that numerous checks were held back from the deposits and held in an employee's drawer. Because cash had been missing, the Recorder did not mention the same to the employee at that time but waited to see if those checks were deposited. They were in fact deposited within a short period of time. Within a few days of discovering this practice, it became clear that large amounts of cash were now being taken from the office. The Recorder turned the matter over to the District Attorney's Office. The employee's practice of holding checks back was pointed out to the Detectives assigned to the case because this practice seemed unusual. Because of the ensuing investigation into the missing funds, the Recorder was asked by the District Attorney's Office not to make inquiries into these practices but to allow the detectives to investigate the same. The Recorder takes no position on or if any other employees of its office are involved in any illegal activities under investigation by the District Attorney's office.

Auditor's Conclusion

Although the Recorder of Deeds stated that monies not deposited within 24 hours of receipt was due in large part to the existence of a satellite office in Hazelton and/or inclement weather, our testing revealed that the time lapse from the date of receipt to the subsequent date of deposit ranged from 2 to 26 days.

RECORDER OF DEEDS
LUZERNE COUNTY
FINDINGS AND RECOMMENDATIONS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

Finding No. 2 - Inadequate Internal Controls Over The Bank Reconciliations

Our testing of the accounting records of the Recorder of Deeds' Office revealed the following deficiencies:

- The office maintained an inaccurate list of outstanding checks in the fee book and municipal tax accounts. The list of outstanding checks for the current month also included checks issued in a subsequent month. Therefore, the bank reconciliations were not prepared correctly.
- There was inadequate accountability over undisbursed funds in the fee book and municipal tax accounts. Liabilities at the end of each month were not compared to cash-on-hand.
- There was a cash shortage at the end of the audit period of \$10,546 (which includes the missing \$10,594 from the January 25, 2005 deposit) in the fee book account. This account is for collections of both Commonwealth and county monies. During the month of January 2005, an employee in the Luzerne County Recorder of Deeds' Office was suspended for allegedly misappropriating funds. At that point, the officeholder compared the general ledger receipt report to cash-on-hand and realized there was a cash shortage. Furthermore, because there was inadequate record keeping for the municipal tax account, we were unable to reconcile the ending cash balance to undisbursed receipts as of the end of the audit period. However, as noted in Finding No. 1, there were four days in which there were no corresponding deposits for collections totaling \$136,716 in the municipal tax account.

These conditions occurred because the Recorder of Deeds' Office failed to establish and implement an adequate system of internal controls over the bank accounts.

Based on the above testing, it appears monies due the Commonwealth were remitted to the Commonwealth.

RECORDER OF DEEDS
LUZERNE COUNTY
FINDINGS AND RECOMMENDATIONS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

Finding No. 2 - Inadequate Internal Controls Over The Bank Reconciliations (Continued)

A good system of internal control ensures that:

- The outstanding check list is properly prepared each month. The outstanding check list should not include checks issued in a subsequent month.
- Bank reconciliations are prepared as of the last day of the month as soon as the bank statement is received.
- The ending adjusted bank balance is reconciled with liabilities on a monthly basis and any discrepancies are immediately investigated and resolved.

Without a good system of internal controls over the bank account, the potential is increased that funds could be lost, stolen, or misappropriated.

The condition of the ending cash balance not reconciling to the liabilities in the fee book account was cited in two prior audit reports; the most recent report period ending December 31, 2001.

Recommendations

We recommend that the Recorder of Deeds' Office prepare bank reconciliations correctly upon receiving its bank statements. We again recommend that the office reconcile the ending cash balance monthly to liabilities and immediately investigate and resolve any differences. We further recommend that appropriate Luzerne County officials investigate the reasons for the cash shortage and take the appropriate actions.

Auditee Response

The Recorder of Deeds responded as follows:

The Recorder of Deed's Office attempted to begin using the computer program "Quicken" in September of 2004 in order to balance the bank statements and detect any discrepancies in the financial records. The individual assigned to utilize the program repeatedly failed to institute the same indicating difficulty in working the program. Despite training in the program and unlimited access to assistance with the program, the individual was unable or unwilling to learn the program. In January 2005, the duty was reassigned to another individual in the office who is familiar with the program. This program has been used effectively since this change in assignment was made.

RECORDER OF DEEDS
LUZERNE COUNTY
FINDINGS AND RECOMMENDATIONS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

Finding No. 2 - Inadequate Internal Controls Over The Bank Reconciliations (Continued)

Auditee Response (Continued)

Immediately following the discovery of cash shortages, the Recorder turned over the investigation to the Luzerne County District Attorney's Office (hereinafter referred to as the D.A.'s Office). Two detectives were assigned to the case. The Recorder has fully cooperated with the investigation. The Recorder was advised that a suspect who is no longer employed by the office, confessed to taking the cash from the office. The Recorder was advised that the Detectives believed this individual may not have been acting alone but it is possible there were others involved. The Recorder was requested by the D.A.'s Office not to investigate or take any action in this matter as it relates to office personnel but to allow the detectives to proceed with their investigation, as they deemed necessary. The Recorder has made what are believed to be necessary and prudent changes in the operation of the office to protect against further theft without compromising the integrity of the ongoing investigation. The Recorder has also learned that the D.A.'s Office requested a forensic audit in February of 2005 with the hopes the same would help indict the individual or individuals involved in the crime. As of the date of this response, the Recorder is without actual knowledge as to whether or not the County Commissioners have approved expenditure of the funds necessary to pay for the audit. Consequently, it continues to be a strong possibility that persons responsible for the theft are still employed in the office. The matter is still pending in the District Attorney's Office.

RECORDER OF DEEDS
LUZERNE COUNTY
FINDINGS AND RECOMMENDATIONS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

Finding No. 3 - Inefficient Use Of Bank Accounts

During our testing of cash receipts, we observed inefficiency in the system used to deposit receipts. The Recorder of Deeds' Office maintained the following accounts into which collections were deposited:

- Fee book account (Writ Taxes, Judicial Computer Project/Access to Justice Fees, and County Fees).
- Realty transfer tax account (cash management account).
- Municipal tax account (county monies).

At the end of each day, the Recorder of Deeds' Office summarized the receipts per the daily cash receipts journals, per account, and then recorded the amount collected on the deposit slip for each account. The deposit slips were brought to the bank with the collections. However, the aggregate collections of cash and checks taken to the bank were not separated by account or deposit slip. The deposit slips taken to the bank were not always for the receipts collected on the same day. The bank credited each account in the amount per the Recorder of Deeds' Office deposit slips.

Good internal accounting controls ensure the efficient use of bank accounts. The Recorder of Deeds' Office should establish a general account into which each day's total receipts can be deposited and then transfer by check, the exact amount due the various other accounts to the respective accounts. The failure to implement these procedures increases the possibility that funds could be lost, stolen, or misappropriated.

This condition was cited in our three prior audit reports; the most recent ending December 31, 2001.

Recommendation

We again recommend that the Recorder of Deeds' Office establish a general account into which each day's total receipts can be deposited and then transfer by check, the exact amount due the various other accounts to the respective accounts. By establishing a general account to replace the current system, internal controls over cash receipts will be significantly improved.

RECORDER OF DEEDS
LUZERNE COUNTY
FINDINGS AND RECOMMENDATIONS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

Finding No. 3 - Inefficient Use Of Bank Accounts (Continued)

Auditee Response

The Recorder of Deeds responded as follows:

The Recorder incorrectly believed the office had instituted and was following the recommendations of the Auditor General and of prior audit reports. The Recorder processes over 60,000 transactions each year. Most transactions require the monies paid be apportioned between three separate accounts. It was possible, but highly cost prohibitive, to require the presenting party to submit three separate checks for each transaction. Rather than having three checks submitted in those transactions, the Recorder accepted one check. When the deposit was made each day, three deposit slips were used with the segregated amounts being indicated on one of the three deposit slips, which corresponded to one of the segregated accounts. In late July of this year, the Recorder was more fully instructed by the Auditor General of the procedure to be followed. Commencing January 1, 2006, the Recorder expects to have a new procedure in place whereby one deposit will be made into the Fee Book Account. The appropriate amounts will then be transferred from the Fee Book Account into the PA Realty Account and the Municipal Account either by web banking or by separate check.

Auditor's Conclusion

The prior audit recommendation was the same as the current audit recommendation, which is to establish a general account into which each day's total receipts can be deposited and then transfer by check, the exact amount due the various other accounts to the respective accounts. In fact, in the auditee response section in the prior audit, the Recorder of Deeds stated that the office now makes one general deposit of all funds and then transfers the appropriate money into each account. However, this procedure was not implemented as of the completion date of our audit, December 6, 2005.

RECORDER OF DEEDS
LUZERNE COUNTY
FINDINGS AND RECOMMENDATIONS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

Finding No. 4 - Inadequate Segregation Of Duties

Our audit revealed that one employee in the Recorder of Deeds' Office was responsible for performing the following functions:

- Preparing deposit slips.
- Summarizing accounting records.
- Determining how much money is deposited into each bank account.
- Reconciling the bank account.
- Posting disbursements to the disbursements journal.
- Preparing and signing checks.

A good system of internal controls requires adequate segregation of duties. One employee should not have custody of cash and at the same time maintain the accounting records for the cash. These duties should be segregated and rotated daily. As an alternative control, someone independent from maintaining the accounting records and handling cash should review the employee's work daily. The reviewer should sign and date the records and documents reviewed.

Without adequate segregation of duties, the possibility of errors or irregularities occurring increases significantly.

Recommendation

We recommend that the Recorder of Deeds' Office provide for greater segregation of duties within the office. This can be done by cross-training personnel and rotating job functions that include the handling of cash and maintaining the accounting records for the cash. As an alternative and/or additional control, someone independent from the handling of cash and the accounting records should review the employee's work at the end of each day. The reviewer should sign and date the records and documents reviewed.

RECORDER OF DEEDS
LUZERNE COUNTY
FINDINGS AND RECOMMENDATIONS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

Finding No. 4 - Inadequate Segregation Of Duties (Continued)

Auditee Response

The Recorder of Deeds responded as follows:

The Recorder of Deeds hired a bookkeeper in August of 2002 to act as a check and balance on the one employee responsible for the office accounting. It was because of this addition to the staff that the cash shortage was detected by the Recorder and brought to the attention of the District Attorney. Each year, the office is audited by three different sources; i.e. the state, the county and private auditors, none of whom detected any cash shortages. The shortages would not have been found except for the additional checks and balances put into place by the Recorder. In fact, in reviewing the Findings and Recommendations with an Audit Supervisor with the Auditor General's Office, he clearly stated that it was or should have been obvious to a trained accountant there was serious indications theft was an ongoing problem in the office. He advised that in the (40) days sampling, the actual cash receipts never matched the cash deposits on any given day. He stated this is always indicative of a greater accounting problem. To the knowledge of the Recorder, this is the first time; the auditors actually reviewed a random sampling of cash receipts and cash deposits. It is the belief of the Recorder that this sampling was done only because the Recorder advised the auditors of the theft in the office. The Recorder is not a trained accountant and relied heavily upon an office employee with an accounting background and the work of the auditors over the years to call to her attention any problems which dealt with the abuse of office finances and/or mismanagement. It is of great concern to the Recorder that since she has been in office, none of the auditors have ever reviewed a random sampling of the cash receipts ledgers and cash deposits ledgers to compare the cash receipts with actual cash deposits, or if they did review the same, why this matter was never addressed in prior audit reports. The Recorder is without explanation to explain why the employee designated to perform the accounting functions did not call this matter to her attention or advise her of what these discrepancies potentially indicated. However, in order to maintain the integrity of the on-going investigation by the District Attorney, a detailed explanation was not requested of the employee in question.

RECORDER OF DEEDS
LUZERNE COUNTY
FINDINGS AND RECOMMENDATIONS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

Finding No. 4 - Inadequate Segregation Of Duties (Continued)

Auditee Response (Continued)

In January of 2005, the bookkeeper's duties were expanded and refined. There is a double check on the daily deposits. The Deputy Recorder reviews the deposits daily and reconciles the bank accounts. Only the Recorder and the Deputy Recorder are authorized to sign checks. Cash in each register is counted at the end of the workday by the recording clerk for that clerk's register and initialed by that clerk. Thereafter, the cash is recounted by the Administrative Assistant and then counted again by the bookkeeper who verifies the same with the computer generated cash report for the day.

Not all accounting privileges are available to those who are responsible for the deposits. The Recorder of Deeds' Office has also made numerous changes in the way we do business. The office no longer allows customers to maintain monies on account. Another significant change in the office is that cash refunds are given only in the case of a cash transaction. Checks accepted by the Recorder must be in the exact amount for the transaction completed. Any check amount in excess of the actual transaction cost is forfeited to the County unless the customer wishes to submit a new check.

Auditor's Conclusion

In regards to the Recorder of Deeds' allegation that a cash shortage was not cited in our prior audit reports, our prior audit report for the period January 1, 1995 to December 31, 1997 noted that there was a cash shortage in the checking account and our prior audit report for the period January 1, 1998 to December 31, 2001 noted that there was a cash overage in the checking account. The finding in both audit reports was titled "Inadequate Internal Control Over The Checking Account." We believe that if the Recorder of Deeds would have taken the appropriate action to investigate the reason for these discrepancies noted in our prior audit reports, the conditions cited in this audit report could have been prevented or detected on a timely basis.

Furthermore, as part of our audit, we always test to determine if there are adequate internal controls over Commonwealth collections and deposits. Our audit is concentrated towards monies due the Commonwealth and to determine if the Commonwealth received its due portion in a timely manner.

In addition, good business practice dictates that it is management's responsibility to establish and implement an adequate system of internal controls over receipts.

RECORDER OF DEEDS
LUZERNE COUNTY
FINDINGS AND RECOMMENDATIONS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

Finding No. 5 - Unmonitored System Access

Luzerne County uses software purchased from and supported by an outside service organization (vendor) to account for transactions in the Recorder of Deeds' Office (County). The vendor has remote access to the County's computer system and data.

During discussions with County personnel, we learned that the vendor has the ability to make changes to the County's data in a manner that would not be recorded through the normal accounting processes and, therefore, would not generate a normal audit trail.

We also noted the following weaknesses:

- The software maintenance agreement between the County and the vendor has not been updated since 2003. Furthermore, this agreement limits the vendor's liability concerning loss of data or system functionality that may be caused by the vendor's actions. The maintenance agreement states, in part, . . . "under no circumstances does [the vendor] warrant or accept responsibility for any incidental, indirect, special or consequential damages resulting from the services provided herein, or in connection with, or arising out of, the existence, furnishing, failure to furnish or use of the Software, even if [the vendor] knew or should have known of the possibility of such damage."
- The vendor has unmonitored access to the County's data. The County was not monitoring the vendor's system accesses. The County office only received monitoring reports when they requested them from the vendor.
- County office users were not required to periodically change their passwords.

Effective security policy and practice requires the County's approval and monitoring of any computer data changes made by the vendor, particularly because of the vendor's access to critical applications. Furthermore, to ensure confidentiality, passwords should be changed periodically and not exchanged between employees.

According to the Computer Emergency Response Team (CERT) of Carnegie Mellon University, inadequate contractor security policies and practices can result in undetected intrusions or security violations, lack of data integrity, and loss of privacy.

RECORDER OF DEEDS
LUZERNE COUNTY
FINDINGS AND RECOMMENDATIONS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

Finding No. 5 – Unmonitored System Access (Continued)

Further, CERT documents also caution that a system might experience loss of confidentiality and integrity due to the contractor using an unsecure method of remote access. This may result in intruders gaining unauthorized access to, modifying, or destroying the County's information systems and assets; deliberately introducing security vulnerabilities or viruses; and launching attacks on other systems from the County's network and perhaps making the County liable for damages.

This condition was cited in our prior audit report ending December 31, 2001.

Recommendations

We again recommend the following:

- The County's Department of Information Services, in cooperation with the County, should establish procedures to periodically generate monitoring reports that include the date, time, reason for change(s), change(s) made, and who made the change(s). The Recorder of Deeds should routinely review these reports to determine that access was appropriate and that data was not improperly altered.
- The County's Data Processing Department should continue to take prudent steps to properly secure their production servers from unauthorized access using the remote access software installed on their system. We recommend consideration of security practices published by respected authorities in the field, such as the CERT Security Module entitled:

Outsourcing Managed Security Services

<http://www.cert.org/security-improvement/modules/m03.html>).

- The County should negotiate an updated contract and software maintenance agreement with the vendor. During this process the County's legal counsel should consider how to protect the County's interests in the event that errors or fraud occur as a result of vendor employees accessing the County's data. Further, in accordance with the CERT document cited above, the following computer security issues should be considered for inclusion in the contract:
 - Assurances that vulnerabilities to known forms of attack have been addressed in the contractor software (i.e., all security patches have been updated and applied), assertions that contractor software is installed and configured to operate securely, and warranties that no malicious code (i.e., Trojan Horses) or viruses exist in contractor software.

RECORDER OF DEEDS
LUZERNE COUNTY
FINDINGS AND RECOMMENDATIONS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

Finding No. 5 – Unmonitored System Access (Continued)

Recommendations (Continued)

- The remote access method, the user authentication process, and a requirement that the contractor communicate securely with the County's site when operating remotely.
 - The ability to restrict systems administrator-level access to authorized users, as well as the ability to log appropriate activities for purposes of detecting intrusions and attempted intrusions.
 - A recently completed security evaluation of the contractor encompassing the technology being selected.
 - A non-disclosure agreement if the contractor may encounter proprietary information on the County's systems.
- The County should always maintain an updated contract so as to provide appropriate legal recourse in the event of disputes with the vendor.
 - County office users should be required to periodically change their passwords.

Auditee Response

The Recorder of Deeds responded as follows:

It is necessary to the maintenance of our computer system for the software vendor to have remote access to the Recorder's computer system and data. The software company provides support during the operating hours of the Recorder's Office. Should any problems arise during business hours, the software vendor can identify the problem and frequently, provide immediate correction through remote access. This quick response is necessary for the continued and efficient operation of the Recorder's Office and is expected by those customers who rely on access to our records in their daily work.

The Recorder or the Deputy Recorder must submit a written request for changes that are to be made by the vendor. Effective January 2006, the Recorder's Office will request that the vendor submit a monthly report of any unsolicited remote access by the vendor's office. The software company does inform us any time they intend to make an update or change to the program.

RECORDER OF DEEDS
LUZERNE COUNTY
FINDINGS AND RECOMMENDATIONS
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

Finding No. 5 – Unmonitored System Access (Continued)

Auditee Response (Continued)

As of May 1, 2003, the Recorder of Deeds' computer software requires employees to change their password every three months. Should the employee fail to do so, he/she is denied access. Employees received an Office Memo from the Recorder directing them not to share their password with others. It is impossible to insure that this does not happen. Each employee is responsible for his or her own terminal and aware that any transactions that occur under their password are their responsibility. The software allows the employee to change their password anytime during the three month time period if they believe it has been compromised.

The Recorder will confer with the solicitor on recommendations for updated contracts with the vendor. By the auditor's own omission, the disclaimer language in the current contract appears routinely in computer vendor contracts. Reasonable efforts will be made to negotiate the recommended changes in the vendor contracts.

Auditor's Conclusion

Although we acknowledge that the vendor needs remote access to the Recorder's computer system and data, proper monitoring of access and/or changes to the system needs to be performed by the Recorder of Deeds' Office.

RECORDER OF DEEDS
LUZERNE COUNTY
REPORT DISTRIBUTION
FOR THE PERIOD
JANUARY 1, 2002 TO JANUARY 31, 2005

This report was initially distributed to:

The Honorable Gregory C. Fajt
Secretary
Department of Revenue

Recorder of Deeds
Luzerne County
Luzerne County Courthouse
Wilkes Barre, PA 18711

The Honorable Mary K. Dysleski	Recorder of Deeds
The Honorable Gregory A Skrepenak	Chairman of the Board
The Honorable Stephen L. Flood	Controller

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