



Request for Audit Committee Action from the Department of Finance

Date: 11/10/2010

- **To:** The Honorable Diane Hofstede, Chair

Subject: Present scope and plan for the Internal Control Documentation project

Recommendation: Receive & File scope and plan for the Internal Control Documentation project

Previous Directives: None

Department Information

Prepared by: Jacob Cherucheril, Manager, Financial Accounting & Reporting

Approved by: Patrick Born, Chief Finance Officer

Presenters in Committee:

Charles Elliott, Controller

Overview

A Finding from the Minnesota State Audit Report on the City's financial statements regarding Monitoring Internal Controls says, *"In our previous reports, we commented on the responsibility of City management for monitoring its internal controls and performing a risk assessment of existing controls over significant functions of its accounting system used to produce financial information. Significant functions and internal controls include and cover such areas as cash, capital assets, major funding sources, expenditure/expense processing and payroll. We also commented on the need for the City to formalize its assessments of risks in its review of internal controls; to document the significant internal controls; to perform monitoring activity of the internal controls on a regular basis, no less than annually; and to document the monitoring activity."*

The decision was made to create a group reporting to Jacob Cherucheril, Manager of Financial Accounting and Reporting, to begin a remediation plan for this finding. Two consultants were contracted to address the finding, determine an efficient course of action, and create a monitoring plan outline.

Work Plan

The consultants' goal is to produce Process Narratives, Risk Assessment Analyses and Control Activity and Reporting Summaries (evaluations of design and effectiveness of the identified key internal controls) in the following significant functions affecting the City's financial statements:

1. Cash/Treasury
2. Capital Assets by Major Fund Type
3. Expenditures
4. Payroll Processing and Expense Reimbursements
5. Journal Entries and Month-End Close
6. Revenues and Major Funding Sources

At this time, Revenues and Major Funding Sources are to be part of "Phase II." Journal Entries and Month-End Close was not a significant function in the original scope, but was added due to its affect on the City's Financial Statements.

Process Narratives

For each of the significant functions, the consultants made a preliminary list of primary processes (based on current State auditor narratives) and then interviewed the process participants and/or managers to create a process narrative. By discussing the process and reviewing procedures, internal controls were identified and highlighted.

At this time, narratives have been completed for Treasury, Capital Assets, Payroll and Journal Entries. The narrative for Expenditures is in process.

Risk Assessment

With an understanding of each process documented in process narratives, the Consultants coordinated a risk assessment meeting with process owners, and as often as possible, Jacob Cherucheril and Chuck Elliott. As preparation for these meetings, for each specific process the Consultants identified goals & objectives (what needs to be done), and related risks (what can go wrong) based on industry standards. For each risk, the Consultants identified City internal controls to manage the risk. During the risk assessment meeting, the goals & objectives and related risks were reviewed for completeness. For each risk, a risk ranking of high, medium, or low was determined.

The risk assessment for Treasury is in process. Risk assessments for payroll, capital assets and journal entries are scheduled before the Thanksgiving holiday.

Control Activity Summary and Reporting Summary

For risks ranked as medium or high, an evaluation of the design and function of the control will be performed. Processes with low risk will be evaluated during a subsequent phase.

A demonstration of the actual control will be observed and documented including examples, copies, screen prints, etc. Based on the findings of the demonstrations and documentations, a recommendation will be given as to the strength and effectiveness of the control as well as a proposed monitoring plan. The monitoring plan will be the basis for clearing the audit function. As managers take ownership of the narratives, risk assessments and evaluations, they will be able to document updates and current monitoring findings. This documentation would then be the foundation for the auditors to test.

Control activity and reporting summaries will be started once risk assessment analyses are completed.

Monitoring Internal Controls Remediation Plan: High Level

Activity	Contact	Auditor	1-Oct	8-Oct	15-Oct	22-Oct	29-Oct	5-Nov	12-Nov	19-Nov	26-Nov	3-Dec	10-Dec	17-Dec	24-Dec
Review existing internal control structure (ICS), Policies and Procedures		AWS	X	X		X									
Review standards to document risk assessment, control activities, and monitoring		AWS	X	X	X										
Draft templates for documenting each significant function		KLS / AWS			X	X									
Obtain Agreement on Remediation Plan		KLS / AWS			X										
Cash	Larry Parker														
Process Narrative		KLS					X	X							
Risk Assessment Summary		KLS							X						
Walkthrough of Key Controls		KLS										X			
Reporting Summary		KLS											X		
Payroll	Lisa Brown														
Process Narrative		AWS				X		X		X					
Risk Assessment Summary		AWS								X	X				
Walkthrough of Key Controls		AWS										X			
Reporting Summary		AWS												X	
Capital assets	Mary Dunning														
Process Narrative		AWS				X	X								
Risk Assessment Summary		AWS							X		X				
Walkthrough of Key Controls		AWS													
Reporting Summary		AWS										X		X	
Expenditures	? Jacob C./ Mary D.														
Process Narrative		KLS						X	X	X					
Risk Assessment Summary		KLS									X	X			
Walkthrough of Key Controls		KLS											X		
Reporting Summary		KLS												X	
Journal Entries	Jacob C/ Mary D.														
Process Narrative		AWS						X							
Risk Assessment Summary		AWS								X					
Walkthrough of Key Controls		AWS										X			
Reporting Summary		AWS											X		
Plan for ongoing monitoring and resolve open matters		KLS / AWS												X	X