

CITY OF NEWTON

FINANCIAL AUDIT ADVISORY COMMITTEE

ACCOUNTING and AUDIT SUB-COMMITTEE AGENDA

THURSDAY, FEBRUARY 28, 2013

Room 222
8 AM

Review of the following individual department responses to the Auditor's Management Letter with representatives of the Planning Department, Parks & Recreation Department, Information Technology, Treasury Department and Comptroller's Department.

- Newton Community Development Authority
- Parks and Recreation
- Disaster Recovery Plan
- Old Outstanding Checks
- Unclaimed Checks
- Service Organization Controls

Respectfully Submitted

Gail Deegan, Chairman

Comment

The Newton Community Development Authority (NCDA) was established to develop housing programs for low and moderate income families and elderly and handicapped persons. The NCDA is a legally separate entity that is governed by the City's Director of Planning and Development and is reported as a discretely presented component unit in the City's financial statements. Prior to fiscal year 2011, the NCDA's day-to-day financial activities were accounted for separately from the City's accounting information system.

During fiscal year 2011, the NCDA's financial activities were transitioned to the City's accounting information system. We identified the following deficiencies regarding the transition:

1. There is currently no process in place to authorize, record and reconcile loan activity between the Department of Planning and Development and the Comptroller's Office
2. Loans receivable were not reconciled to detailed amortization schedules (by loan recipient) during the year
3. Outstanding loans receivable balances are currently maintained in Excel

Recommendation

We recommend that the City and the NCDA implement appropriate controls surrounding the authorization, recording and reconciliation of NCDA loan activity.

We recommend the City implement controls to reconcile loans receivable to detailed amortization schedules.

We recommend the City utilize loan amortization software to maintain the NCDA loans.

Management's Response

The Comptroller is working with the City's new Community Development Director to improve on-going communications between Community Development program staff and the Comptroller's Office so that loan activity will be recorded on a timely basis and detailed loan receivable records, maintained by Community Development staff, are reconciled to the City's general ledger on a regular basis. Loan receivable activity is currently only reconciled mid-year and at the end of the each fiscal year. The City is considering contracting with an outside party to review existing recordkeeping procedures; to recommend improvements; and to train program staff.

2012

Parks and Recreation

Comment

We documented the system of internal control surrounding the Parks and Recreation Department's (Department) cash receipt activities and identified the following:

- Although daily bracelets are utilized at each swimming facility (Gath Pool and Crystal Lake), no log is maintained that identifies the starting and ending bracelet number sold for each day. In addition, no documentation exists that reconciles the number of daily bracelets sold to the actual cash receipts collected. The current process inhibits the ability to reconcile cash collections to the use of the facilities.
- The Schedule of Payments to City Treasurer (Schedule) submitted by the Department does not contain the signature of the preparer or reviewer of the document. As a result, key controls are not being documented, which is a weakness in internal control.
- There is no documentation (i.e., an initial or signature) supporting the review/reconciliation of the deposit made to the bank to the summary report of receipts entered into the Department's internal database (SportsMan).

Recommendation

We recommend the use of a manual log that identifies the starting and ending bracelet number sold each day. In addition, we recommend a daily formal reconciliation be prepared that reconciles the number of bracelets sold to cash collections.

We recommend the Schedule contain preparer and reviewer signatures.

We recommend the Department's bookkeeper formally document (i.e., a signature or initials) the reconciliation of deposits to receipts entered into SportsMan.

Management's Response

The Comptroller is in agreement with these recommendations and will work with the Parks Department to implement the improvements. Departmental cash receipt collections will be a primary area of focus for the City's Audit Committee during the next year.

Disaster Recovery Plan

Comment

The City has a documented disaster recovery plan that addresses its financial data and related software. However, the plan does not address the hardware required to access the data or the location(s) to operate the hardware. Therefore, in the event of a disaster, the City's financial data and software could be recovered, but the City may not have the ability to physically run the software and access the financial data to maintain financial operations.

Recommendation

We recommend management update the current disaster recovery plan by addressing the hardware requirements to access the financial data and the location(s) to operate the hardware.

Management's Response

The City has acquired a back-up server that will be located at a secure, primary remote site that is attached to the City's network. This server will be powered off and used only for quarterly testing and for actual emergencies. Documentation, tape drives, spare checks and cabling will be stored with the unit at the secure off-site location.

Disaster Recovery Plan

2012

Comment

In our prior year management letter, we identified that although the City had a documented disaster recovery plan that addressed its financial data and related software, it did not have a plan that addressed the hardware required to access the data or the location(s) to operate the hardware. As a result, in the event of a disaster, the City's financial data and software could be recovered, but the City may not have the ability to physically run the software and access the financial data to maintain financial operations.

During fiscal year 2012, the City addressed the hardware required to access the data and location to operate the general ledger software (Finance Plus). However, the hardware required to access the detailed accounts receivable data (MUNIS) has not been addressed by the City.

Recommendation

We recommend management update the current disaster recovery plan by addressing the hardware requirements to access the detailed accounts receivable data.

Management's Response

The City's Information Technology Department presented the Audit Committee with a detailed disaster recovery plan that addresses all issues that have been raised in the management letter earlier this fall.

2011

Old Outstanding Checks

Comment

The vendor and payroll outstanding checklists maintained by the Treasurer include many checks greater than three (3) months old totaling approximately \$259,000. Typically, checks greater than three (3) months old reflect checks that have been void, lost, misplaced or stolen.

Recommendation

We recommend that the Treasurer/Collector's office implement monthly procedures to investigate and resolve outstanding checks greater than three (3) months old. Implementation of this recommendation will strengthen internal controls over cash disbursements.

Management's Response

Treasury continues its efforts to address this issue. The process has been hampered largely due to procedural issues. It is the policy of the bank that provides the City's vendor and payroll processing to include stop payments on its outstanding list for a period of not less than six (6) months. After this time, the check is again presented to the City as a "positive pay" item. Treasury deems this system to be unacceptable, and has been working with the bank to develop new procedures involving alteration of their system as it applies to Newton. Successful efforts to date include the regular issuance of a "Stale Dated Check Report" by the bank. Additional internal actions taken by Treasury include working with the IT Department to match the check information to names and addresses in the City's records. Treasury will review the "Stale Dated Check Report" monthly to identify and to clear items as they appear. Also, outstanding checks will be posted on the City's website.

Old Outstanding Checks

2012

Comment

The vendor and payroll outstanding checklists maintained by the Treasurer include many checks greater than three (3) months old totaling approximately \$214,000. Typically, checks greater than three (3) months old reflect checks that have been void, lost, misplaced or stolen.

Recommendation

We recommend the Treasurer/Collector's office implement monthly procedures to investigate and resolve outstanding checks greater than three (3) months old. Implementation of this recommendation will strengthen internal controls over cash disbursements.

Management's Response

A system to address old checks was initiated in April 2012. Checks greater than 3 months old have been posted on the City's website since that time. A claim form has been made available as well. Claimed and reissued checks are deleted and new checks are added to the list on a monthly basis.

2011

Unclaimed Checks

Comment

At June 30, 2011, the City's general ledger reports a liability for unclaimed checks totaling approximately \$505,000. However, a current list of check numbers, check dates, payee names, address and related amounts that support the amount reported on the general ledger was not provided to us. This information (identified above) is critical when following up and resolving unclaimed check amounts.

Recommendation

We recommend that the Treasurer/Collector's office investigate and identify the check numbers, check dates, payee names and related amounts that reconcile to the balance reported on the general ledger.

We recommend that the Treasurer/Collector's office implement procedures to investigate and resolve the unclaimed check amounts.

Management's Response

Supporting information for unclaimed checks was available but not centralized at the time of the audit. A file containing supporting information is now available and will be maintained in the future. Additionally, unclaimed checks will be posted to the City's website together with the instructions and the form needed to claim the funds.

2012

Unclaimed Checks

Comment

At June 30, 2012, the City's general ledger reports a liability for unclaimed checks totaling approximately \$500,000. However, a current list of check numbers, check dates, payee names, address and related amounts that support the amount reported on the general ledger was not provided to us. This information is critical when following up and resolving unclaimed check amounts.

Recommendation

We recommend the Treasurer/Collector's office investigate and identify the check numbers, check dates, payee names and related amounts that reconcile to the balance reported on the general ledger.

We recommend the Treasurer/Collector's office implement procedures to investigate and resolve the unclaimed check amounts in accordance with Massachusetts Abandoned Property Laws.

Management's Response

Documents supporting the \$500,000 were sent to the Auditors on 11/26/12. It should be noted that this balance is approximately \$225,000 less than originally reported to the Comptroller, representing cleared items. The remaining items will be posted to the City's internet and handled much the same as old checks. Also, as part of Treasury's effort to finalize procedures. The City adopted MGL 200, Sec 9A, allowing the City to retain unclaimed proceeds, but requiring a process taking over one year.

Service Organization Controls

Comment

The City, like many local governments in Massachusetts, engages third-party service providers (service organizations) to process certain financial transactions (i.e., Deputy Tax Collector). In such instances, the related financial transactions are affected by the City's internal controls and the controls employed by the service organization. Therefore, as part of its monitoring efforts to ensure that internal controls over financial reporting are effective and functioning as intended, City management must evaluate whether service organization controls are suitably designed and effective.

Furthermore, service organizations often have information regarding employees and customers that must be protected (e.g., social security numbers). Such controls generally relate to the security, availability, processing integrity, confidentiality or privacy of information. Therefore, as part of its monitoring efforts to ensure the privacy and protection of its employees and customers' information, management must evaluate whether service organization controls are suitably designed and effective.

The most effective and efficient way for the City to accomplish its monitoring efforts is to obtain the appropriate *Service Organization Control (SOC)* reports from its third-party service providers.

There are two types of SOC reports that service auditors provide to service organizations for the benefit of their users, which are as follows:

- SOC 1 (previously SAS 70) reports - provide an opinion on controls at a service organization that are likely to be relevant to a user entity's internal control over financial reporting
- SOC 2 reports - provide an opinion on controls at a service organization that are related to the American Institute of Certified Public Accountants (AICPA) Trust Service Principles, which are (1) security; (2) availability; (3) processing integrity; (4) confidentiality; and (5) privacy.

Service organizations should be engaging a service auditor to provide the appropriate SOC report(s) and should make the resulting report available to their customers (e.g., the City).

Recommendation

We recommend the City identify each service organization utilized and request the applicable SOC report (annually).

Because all service organizations are an extension of the City's internal control, we recommend all service organization contracts include a requirement to obtain the appropriate SOC report (annually).

Management's Response

The Comptroller is in agreement with this recommendation and will work with the Treasurer and Planning and Community Development Department; and Retirement Board to implement the recommendation during the second half of fiscal year 2013.