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DEPARTMENT OF
FINANCE

CITY OF SACRAMENTO
CALIFORNIA

BETTY MASUOKA
DIRECTOR

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September 6, 1988
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DIVISIONS:
ACCOUNTING
BUDGET
REVENUE
RISK MANAGEMENT

Budget and Finance Committee
Sacramento, California

Honorable Members in Session:

SUBJECT: Touche Ross Letter of Recommendations

SUMMARY

The attached Touche Ross Letter of Recommendations was heard by the City Council on August 30, 1988, (item number 29) and referred to the Budget and Finance Committee for review.

No Committee action is required as the report is informational in nature. Touche Ross as well as applicable City staff will be in attendance to answer questions.

Respectfully submitted,

BETTY MASUOKA
Director of Finance

Attachment

APPROVED FOR COMMITTEE INFORMATION:

JACK R. CRIST
Deputy City Manager

September 13, 1988
All Districts

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CITY OF SACRAMENTO
LETTER OF RECOMMENDATIONS
JUNE 30, 1987

April 15, 1988

Honorable Mayor
and Council Members
City of Sacramento
Sacramento, California

We have examined the general purpose financial statements of City of Sacramento, California, for the year ended June 30, 1987, and have issued our report thereon dated April 15, 1988. As part of our examination, we made a study and evaluation of the system of internal accounting control of City of Sacramento, California, to the extent we considered necessary to evaluate the system as required by generally accepted auditing standards and the standards for financial and compliance audits contained in the U.S. General Accounting Office Standards for Audit of Governmental Organizations, Programs, Activities, and Functions. For the purpose of this report, we have classified the significant internal accounting controls in the following categories:

- . Utility billings and accounts receivable
- . Cash receipts
- . Purchasing and accounts payable
- . Cash disbursements
- . Payroll
- . Budgetary
- . Books and records
- . Fixed assets
- . Investments

Our study included all of the control categories listed above except that we did not evaluate the accounting controls over fixed assets because we examined the applicable account balances and reports at year-end. The purpose of our study and evaluation was to determine the nature, timing, and extent of the auditing procedures necessary for expressing an opinion on the entity's financial statements. Our study and evaluation was more limited than would be necessary to express an opinion on the system of internal accounting control taken as a whole or on any of the categories of controls identified above.

City of Sacramento
 April 15, 1988
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The management of City of Sacramento, California, is responsible for establishing and maintaining a system of internal accounting control. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control procedures. The objectives of a system are 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 financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any system of internal accounting control, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the degree of compliance with the procedures may deteriorate.

Our study and evaluation made for the limited purpose described in the first paragraph would not necessarily disclose all material weaknesses in the system. Accordingly, we do not express an opinion on the system of internal accounting control of the City of Sacramento taken as a whole or on any of categories of controls identified in the first paragraph. However, our study and evaluation disclosed no condition that we believed to be a material weakness, and pages 3 to 15 describe certain internal accounting control and operational efficiency weaknesses we believe should be strengthened.

* * * * *

This report is intended solely for the use of management and the Mayor and City Council of the City of Sacramento, and should not be used for any other purpose. This restriction is not intended to limit the distribution of this report which, upon acceptance, is a matter of public record.

Touche Ross & Co.

Certified Public Accountants

CITY OF SACRAMENTO

FINDINGS AND RECOMMENDATIONS

Cash Disbursements

During our review and testing of the internal controls over cash disbursements, we noted the following weaknesses:

Weakness #1: Supporting invoices for both automated and manually written checks were not cancelled.

Recommendation: We recommend all supporting invoices be cancelled in order to ensure that duplicate payments are not made.

Management Response: The Accounting Division will implement procedures to cancel all invoices paid through the accounts payable process.

Weakness #2: All journal voucher entries to adjust "reissue" checks were adjusted to the general fund cash account and not to the applicable fund's cash account.

Recommendation: To reduce the potential for misstatement of cash balances at year-end between funds (for checks restored to cash which have not been reissued), we recommend all journal entries for "reissue" checks be recorded to the applicable fund's cash account.

Management Response: This is only true initially. Later other payroll journal entries are prepared for "reissue" checks to record amounts to the cash accounts of the appropriate funds. It is a timing difference only. This timing difference is virtually unavoidable under the current payroll system.

CITY OF SACRAMENTO

FINDINGS AND RECOMMENDATIONS (Continued)

Cash Disbursements (continued)

Weakness #3: Access to the check signing room was not restricted.

Recommendation: We recommend that access to the check signing room be restricted.

Management Response: Due to physical space limitations, it is not feasible to locate the pre-loaded check printer in a secured area during the work day. However, other controls exist to help alleviate the need to isolate this printer.

CITY OF SACRAMENTO

FINDINGS AND RECOMMENDATIONS (Continued)

Payroll

During our review and testing of the internal controls over payroll, we noted the following weakness:

Weakness #1: The state tax withholding table in the automated payroll system was not updated for the current year.

Recommendation: We recommend periodic recalculation of payroll data on a test basis be performed by a responsible person to determine whether the computer application is properly calculating employee withholdings.

Management
Response: The Accounting Division tests payroll calculations manually whenever a mass payroll change occurs. Accounting makes every effort to follow this procedure, yet an oversight occurred when the state withholding tax calculations were not verified as correct.

CITY OF SACRAMENTO

FINDINGS AND RECOMMENDATIONS (Continued)

Pension

During our testing of the internal controls over retiree benefit payments, we noted the following weaknesses:

Weakness #1: In our random sample of benefit payments selected for testing, documentation of approval for several pension calculations was not performed by the responsible employee.

Recommendation: We recommend review and approval of all benefit payment calculations be performed and documented by a responsible employee.

Weakness #2: Our random sample of retiree benefits selected for testing disclosed that the approval to authorize pension benefit payments was not kept in the retiree's file.

Recommendation: We recommend the approval to authorize pension benefit payments be kept in the retiree's file.

Management
Response:

The Employee Services Division is aware of the weaknesses mentioned above and has corrected the problems. The benefit calculation documents are being properly initialed by the responsible employee after review and approval letters signed by the Retirement Systems Manager are being kept in the retiree's file.

CITY OF SACRAMENTOFINDINGS AND RECOMMENDATIONS (Continued)Cash ReceiptsBingo Operations

During the performance of agreed upon procedures with respect to selected bingo operations, we noted the following weaknesses:

Weakness #1: The City's policy to require monthly financial statements from bingo operations is limited to those operations with gross receipts in excess of \$5,000 a month.

Recommendation: To strengthen accountability of cash receipts by bingo licensees, we recommend that all bingo operators submit monthly statements.

Management
Response:

The observation that the City only requires monthly statements from operations with gross receipts in excess of \$5,000 a month was correct for the period under audit. The City now requires monthly statements from all bingo operations except for the social bingo game operations.

Weakness #2: Our report on agreed upon procedures for selected bingo operations disclosed that certain licensees were not adhering to the applicable sections of Chapter 18 of the Sacramento City Code.

Recommendation: We recommend that the City require annual written attestations from licensees reaffirming compliance with the Sacramento City Code. Also, we recommend the responsible City department work with the City's internal auditor to monitor bingo licensees' compliance with the City Code.

CITY OF SACRAMENTO

FINDINGS AND RECOMMENDATIONS (Continued)

Cash Receipts (continued)

Bingo Operations (continued)

Management

Response:

The observation that bingo operators are not

CITY OF SACRAMENTO

FINDINGS AND RECOMMENDATIONS (Continued)

Cash Receipts (continued)

General (continued)

Recommendation: We recommend that parties requesting services for special solid waste collections pay in advance or be charged during the normal billing process.

Management Response: The observation that no formalized procedure for the receipt of monies for special solid waste collections is correct.

CITY OF SACRAMENTO

FINDINGS AND RECOMMENDATIONS (Continued)

Books and Records

During the review and testing of internal controls over journal vouchers, we noted the following weaknesses:

Weakness #1: Based on a random sample of 25 journal vouchers, we noted two journal vouchers which were incorrectly keypunched into the City's financial accounting and reporting system (LGFS).

Recommendation: We recommend journal voucher entries posted to LGFS be compared on a test basis by an independent accountant to the original journal voucher form to ensure that entries were keypunched correctly.

Management Response:

The Accounting Division has centralized the data entry and the number assignment of journal voucher entries. Through centralization and the standardization of procedures and duty assignments, keypunch errors will be minimized.

Weakness #2: Supporting documentation for selected journal entries was not attached to the journal voucher form.

Recommendation: We recommend periodic inspections be performed by the City's internal auditor to determine whether the accounting department is properly attaching supporting documentation to the journal vouchers.

Management Response:

When recording unusual, complex, or unclear transactions that are otherwise not considered standard or self-explanatory, supporting documentation is required to be attached to journal vouchers.

CITY OF SACRAMENTO

FINDINGS AND RECOMMENDATIONS (Continued)

Budget

During our review of internal controls over the budget process, we noted the following weakness:

Weakness #1: Fund expenditures charged pursuant to the City's cost allocation plan could not be agreed or reconciled to the approved budget as the detailed schedule to reconcile the plan and budget was not retained.

Recommendation: We recommend procedures be implemented to reconcile the cost allocation plan to the approved budget to assure that allocated costs are properly being charged to the respective funds.

Management
Response:

The City has developed a schedule which extracts the central costs distributed to enterprise and internal service funds for use in creating the budget transfer schedule which "charges" the benefiting organizations and "credits" the central support organizations. The City budget input is the responsibility of a person other than the individual responsible for cost plan data extraction. Turn around documents are checked by several analysts in addition to the analyst responsible for the cost plan.

CITY OF SACRAMENTO

FINDINGS AND RECOMMENDATIONS (Continued)

Investments

During our testing of internal controls over investments, we noted the following weaknesses:

Weakness #1: City employees responsible for investing the City's cash occasionally exceeded the limits of authority prescribed by the City's investment policy.

Recommendation: We recommend the limits as defined by the investment policy be followed which includes having responsible persons approve the transactions as outlined in the investment policy.

Management Response:

The Treasurer concurs that treasury staff should not exceed the trading limits in the investment policy established several years ago by the City Treasurer.

Weakness #2: The Investment Committee which reviews and reports on the investment activities and strategies is not independent of the investment transactions.

Recommendation: We recommend an evaluation be performed to determine the feasibility of an independent review of investment activity.

Management Response:

The Treasurer concurs that the investment committee is comprised of treasury staff, some of whom execute day to day investment transactions. This practice is not uncommon in the investment industry and is identical to the independent investment managers retained by SCERS.

CITY OF SACRAMENTO

FINDINGS AND RECOMMENDATIONS (Continued)

Accounting

During the audit of the respective accounts, we noted the following weaknesses:

Cash

Weakness #1: Reconciliation and apportionment of the City's pooled cash accounts was not performed in a timely manner.

Recommendation: To strengthen control over cash management and to facilitate the timely closing of the City's funds at year-end, we recommend the reconciliation and apportionment of pooled cash accounts be performed in a timely manner.

Management

Response: For the past ten months, the Finance and Treasury Departments have brought the recording of reconciliation and apportionment activity up to date. Efforts to maintain a timely recording schedule will continue in order to meet closing schedules and to strengthen control over cash management.

Weakness #2: Several old reconciling items appeared on the treasurer's cash reconciliation.

Recommendation: We recommend old reconciling items on the cash reconciliations be identified and resolved as soon as possible to strengthen control over cash accountability.

Management

Response: The Accounting Division will identify and resolve old reconciling items.

Fixed Assets

Weakness #1: Selected old reconciling items appeared on the reconciliation (from the general ledger to the fixed asset records) of fixed assets.

CITY OF SACRAMENTO

FINDINGS AND RECOMMENDATIONS (Continued)

Accounting (continued)

Fixed Assets (continued)

Recommendation: To strengthen control over compliance with the City's capitalization policy and the safeguarding of assets, we recommend reconciling items between fixed asset records and capitalized expenditures accounting records be resolved between department personnel and the City's accountants on a timely basis.

Management Response: During the first half of the 1988-89, fiscal year, the fixed assets accounting subsystem will be updated. This effort will remove all reconciling items between the general ledger and the fixed assets records.

Weakness #2: Based on discussions with accounting personnel, we noted that a physical inventory of fixed assets had not been performed for several years.

Recommendation: We recommend a physical inventory of all assets be performed to verify the existence of assets listed on the City's fixed asset records.

Management Response: During the first quarter of the 1988-89 fiscal year, a physical inventory of all fixed assets will be performed in our effort to update the fixed assets accounting subsystem.

Weakness #3: Several completed construction projects were not transferred from construction-in-progress to the appropriate fixed asset accounts in a timely manner.

CITY OF SACRAMENTO

FINDINGS AND RECOMMENDATIONS (Continued)

Accounting (continued)

Fixed Assets (continued)

Recommendation: We recommend all open construction projects be reviewed as of year end to determine whether the projects should be closed out.

Management

Response: Departments responsible for reviewing construction projects will be reminded annually to request closure of completed projects. The Accounting Division is currently making every effort to relieve the backlog of completed projects to close.

Weakness #4: Additions of fixed assets were not updated in a timely manner on the detail fixed asset listing.

Recommendation: We recommend the responsible departments which requisition fixed assets notify the accounting department as soon as possible to record additions of fixed assets in a timely manner.

Management

Response: During the first half of the 1988-89 fiscal year, the fixed assets accounting subsystem will be updated. Thereafter, the Accounting Division will work closely with departments to maintain the fixed assets system. In the not-too-distant future, new computer software will be in place that will automate the interface between the general ledger and the fixed assets subsystem.

General

Weakness #1: Revenues earned by certain capital and operating grants were not collected in a timely manner.

CITY OF SACRAMENTO

FINDINGS AND RECOMMENDATIONS

Accounting (continued)

General (continued)

Recommendation: We recommend that the responsible City accountants prepare an aged trial balance for material receivables in order to identify amounts which are past due. In addition, a responsible person should pursue the collection of the receivables in a timely manner.

Management Response: Through contact with departments and the Revenue Division, the Accounting Division will make efforts to ensure more timely billing for grant funds.

Weakness #2: Detail schedules of account balances (i.e., accounts receivables and payables) could not be provided.

Recommendation: We recommend a study and evaluation be performed to determine the feasibility of generating detail schedules to facilitate reconciliations of general ledger balances.

Management Response: Upon request, the Accounting Division is now able to prepare detailed schedules of accounts receivable and accounts payable balances through FOCUS, a computer report writer.

CITY OF SACRAMENTOFINDINGS AND RECOMMENDATIONS (Continued)Accounting (continued)

General (continued)

Weakness #3: Pursuant to an inquiry from one of the City's federal grant funding sources, we noted that the inventory listing of federal, state and local grants prepared by the City's former internal auditor excluded approximately \$215,000 of federal pass-through grants. Failure to account for and report all federal, state and local grants increases the possibility of noncompliance with funding terms which could ultimately result in revocation of the funds awarded.

Recommendation: We recommend that the City Internal Auditor circularize a quarterly inventory listing of grants received by the City to all City department heads, who should confirm the completeness of the listing. The City should also establish formal reporting procedures for application and award of federal, state and local grants.

Management Response: The City Internal Auditor will begin maintaining a current inventory listing of grants at all times with details related to reporting, renewing, and closing requirements.