

City of Cupertino, California Interim Audit Results

July 11, 2017

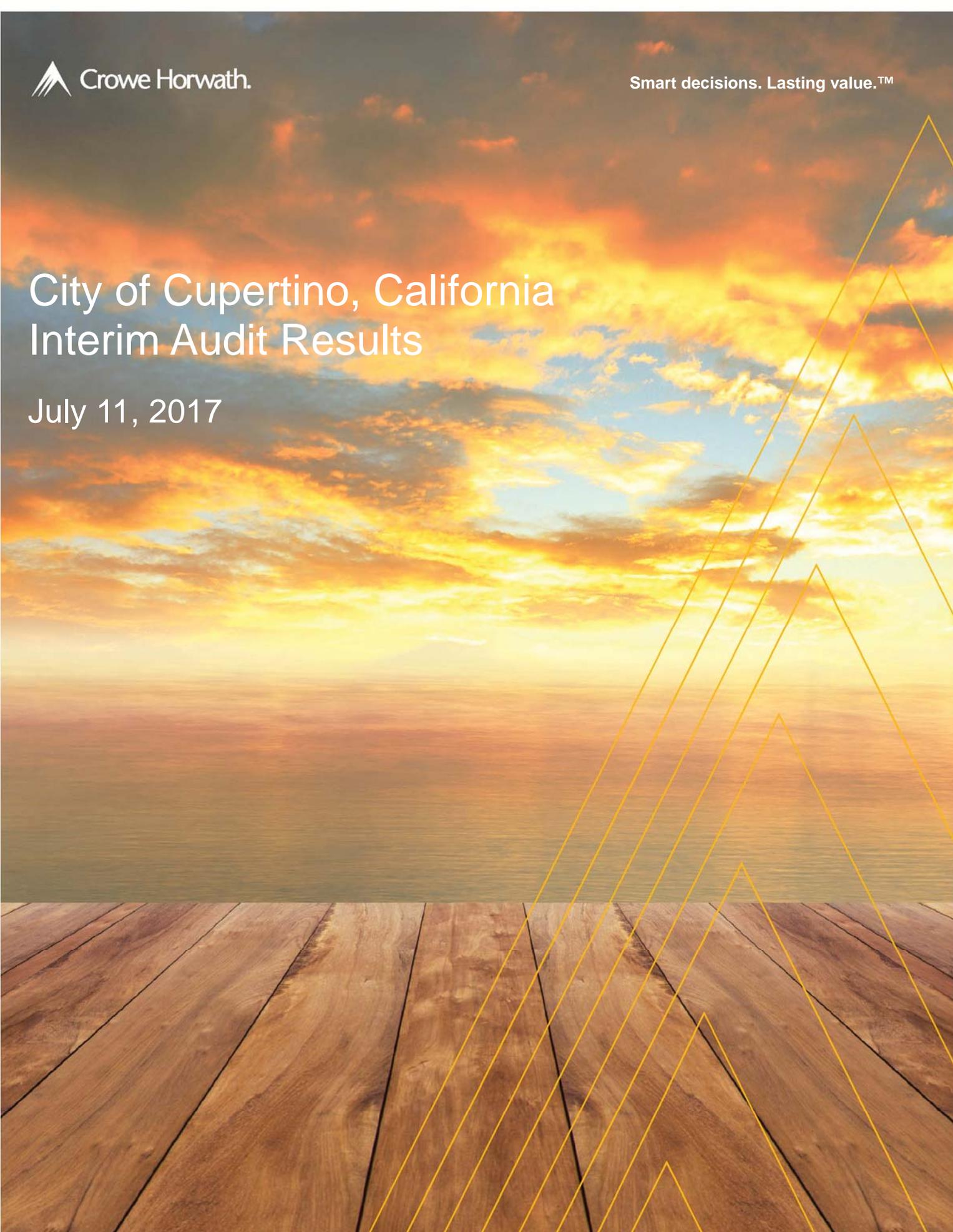


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Interim Audit Results

2017-001 – Information System Controls

Criteria:

Internal controls over information systems are a key component of an organization's control environment. Entities should have internal controls including policies and procedures regarding user access, change management, and back-up and recovery. Where adequate segregation of duties cannot be employed via system access restrictions, detective and monitoring review controls should be established that adequately mitigate such risks. Such controls enable entities to increase efficiency by reducing manual processes and improving the accuracy and quality of the data used across those information systems. Such controls are also important to prevent erroneous and fraudulent transactions or entry to systems.

Condition: We evaluated system access to the City's Active Directory as well as the financial reporting system, New World Systems (NWS). The Active Directory authenticates and authorizes all users and computers in a Windows domain type network—assigning and enforcing security policies for all computers and installing or updating software. For example, when a user logs into a computer that is part of a Windows domain, Active Directory checks the submitted password and determines whether the user is an authorized user.

During our assessment of the City's information system controls, we noted the following:

Financial Reporting System/Active Directory

- The City's Finance Manager and Accountant II maintain super user access to the financial reporting system, in addition to operational roles in the normal course of business. Super user access includes the ability to add/modify/delete user accounts as well as assign security privileges to user accounts.
- The City's information and technology (IT) and finance departments do not have a process to evaluate the propriety of changes to user access within the financial reporting system. For example, the City's IT and finance departments are not able to provide evidence that access was removed from NWS in a timely manner. We selected a sample of 5 out of 44 terminated employees during the period reviewed. While we can confirm that user access has been removed from NWS as of the date of fieldwork, neither the IT department or the finance departments maintained records indicating the date that user access was removed.

Policies and Procedures

- The City's information technology policies and procedures have not been recently updated to reflect the practices that are currently in use. It is unknown when the City last reviewed the IT policies and procedures. For example, areas such as the disaster recovery plan and internet access and use monitoring policy, are no longer applicable to the City due to changes in hardware, software and/or management structure, yet are still presented therein.

Cause:

Financial Reporting System/Active Directory

- Super user access was granted to the 2 individuals, as management had not yet identified a position within the City, but outside the finance department, which could permanently fulfill this role. As of June 15, 2017, super user access was removed from the users identified during testing.
- User access requests for the financial reporting system are informal, typically verbal or through email. The City does not have a mechanism for tracking when user access is changed. Within the financial reporting system, the City has not yet identified the key reports which should be utilized to evaluate changes made to user access.

Policies and Procedures

- With regard to the City's IT policies and procedures, there have been systematic changes to the City's disaster recovery plan, and other IT areas which have not yet been carried forward into the City's written policies.

Effect:**Financial Reporting System/Active Directory**

Improper user access could result in fraudulent and/or unauthorized transactions being recorded in the City's financial reporting system, where management would not be able to detect such activity.

Policies and Procedures

Outdated policies and procedures may not provide the City a mechanism to restore critical information systems should there be a disaster recovery event. Further, in the event that key IT employees separate from the City, outdated policies and procedures may deter the City's ability to smoothly transition responsibilities to successors.

Recommendation:**Financial Reporting System/Active Directory**

- The City should establish written policies and procedures which provide for the appropriate levels of user access based on the relative roles and responsibilities within the financial reporting system. A best practice is to provide the lowest level of access based on operational need. Further, we recommend the City perform a systematic review and maintain documentation of user's access rights within the financial reporting system, to ensure that a) there are not users with super user access who also have the ability to perform operational functions within the financial reporting system and b) users access roles are only for those functions which are necessary to perform in the normal course of business.

Policies and Procedures

- We recommend that the City update its policies and procedures to reflect current conditions and establish a process to ensure periodic review occurs. IT policies should be reviewed and approved by management or those charged with governance on a periodic basis.

Management's Response and Planned Corrective Action:

The City agrees with Auditor's recommendation and have already started drafting a policy on user security that will include all components outlined the "Financial Reporting/Active Directory" sections of this assessment.

2017-002 – Timely Processing of Bank Reconciliations

Criteria A bank reconciliation is used to compare the records of the City to those of the bank, to see if there are any differences between those two sets of records for cash transactions. Performing timely bank reconciliations is critical to the accurate financial reporting of the City. In addition, the bank reconciliation cannot be considered complete until it has been reviewed and approved, and where applicable, changes to the City's financial records have been processed.

Condition Prior to beginning the interim audit procedures for the fiscal year ended June 30, 2017, we noted that the predecessor auditor reported (among other conditions) material unreconciled variances between the financial records of the bank and the financial records of the City. During our interim procedures, we noted that the City has been continuously evaluating the accuracy of the underlying financial activity included in the bank reconciliation information in order to have confidence in the data interfacing with the financial reporting system. The City has engaged another CPA firm to assist with this process and ensure that the bank reconciliation process is completed for the entire fiscal year and prior years. To date, this process has not been completed, with the City targeting completion by the end of August 2017. The period covered by the bank reconciliation project is December 2014, to-date.

Cause The City implemented its new financial reporting system in the previous fiscal period. As a result, the bank reconciliation process was not completed timely and fell behind schedule in prior years.

Effect Transactions which have not been reviewed could be recorded incorrectly, and not corrected in a timely manner.

Recommendation We recommend the City continue its process of reviewing its bank reconciliations and clearing exceptions by posting correcting entries to the general ledger, when necessary. This will result in more accurate financial reporting,

Management's Response and Planned Corrective Action:

The City agrees with Auditor's recommendation and will continue reviewing its bank reconciliation process. The City has retained Vavrinek, Trine, Day & Co., LLP (VTD), a CPA firm to assist on resolving this finding. Staff will continue to update the City Council and Audit Committee on the status of bank reconciliation on a biweekly basis until it is resolved. City staff will continue working toward a sustainable ongoing solution to ensure proper financial accounting and reporting with a current completion date of August 31, 2017.

Status of Prior Year Audit Findings

2016-01 – Bank Reconciliation

Finding Summary: Bank reconciliations for the fiscal year ended June 30, 2016 were not performed timely, did not include evidence of proper review or approval and included unreconciled amounts.

Status of Corrective Action: This finding has been repeated and included as finding 2017-002.

2016-02 – Super User Rights

Finding Summary: The Finance Manager has super user access in the City's New World System.

Status of Corrective Action: This finding has been repeated and included as part of finding 2017-001.

2016-03 – Cash Receipts Process

Finding Summary: Inadequate segregation of duties among the cash receipt process was noted (i.e. the Account Clerk was responsible for opening daily mail, performing daily reconciliations, and performing daily/weekly deposits to the bank), as well as periodic cash reconciliations (monthly/quarterly) to the general ledger were not being performed.

Status of Corrective Action: The lack of segregation of duties has been corrected. The periodic cash receipts reconciliation finding has been repeated and included as part of finding 2017-001.

2016-004 – Recording of Capital Related Expenditures

Finding Summary: Capital outlay expenditures were not properly reconciled and accounted for in the Governmental Activities opinion unit.

Status of Corrective Action: This has been corrected, as management has performed a review of the activity covered by the prior audit report and reflected the corrections in the financial system accordingly. Crowe will evaluate the internal controls over capital related expenditures during final fieldwork.

2015-001 – Financial System Conversion, Year End Closing and Staff Resources

Finding Summary: The beginning balances for certain General Fund retainer deposits were not reconciled prior to deployment of the new accounting system. In addition, insufficient staffing in the finance department in conjunction with increased activity in public works, building permits and construction activities resulted in difficulties in the year-end financial reporting process. Monthly bank reconciliations were not completed timely.

Status of Corrective Action: This is partially implemented. The City has hired additional finance staff and is working to complete the bank reconciliations. The bank reconciliation issue has been identified in finding 2017-002. However, the Finance Manager position has recently been vacated, during a critical year-end closing and financial reporting time frame. Crowe will evaluate the internal controls over these areas during final fieldwork.