

**CFO? - Handcuffed
Reconciliation? - None
Controls? - Weak**

Problem...?

One Local Government's Cautionary Tale of the Importance of Internal Controls

DISCLAIMER

Views and Comments Expressed are Ours and Ours Alone and May Not Necessarily Represent those of our Employers.

AGENDA

- Background
- Communication & Control Breakdowns
- Lessons Learned
- Q&A

One Local Government's
Cautionary Tale of the
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Background

One Local Government's Cautionary Tale of the Importance of Internal Controls

- Growing Suburban, Bedroom Community
- Population: < 30,000 residents
- Increased need for access to Interstate Highway
- Collaborated with two neighboring towns to finance and develop a new interchange.
 - *Tax Increment Financing*
 - *School Compensation Agreements*
- Great Recession
 - *State Funding Impact to General Fund*
 - *Layoffs in all Departments*

Background

YEAR 1 (20x3)

- \$18M+ annual operating budget → Cash Basis
- Paper-Based except Payroll & Debt Service
- Payroll – In-House, 75+ employees
- January - Finance Department staffing:
 - Director (Experience 30+ Years)
 - Payroll Assistant (Experience 13+ Years)
 - Payables Assistance (Experience 10+ Years)
 - Fiscal Officer (Experience 8 Months)
- April - Finance Department staffing:
 - ~~Director~~ (retired March)
 - Payroll Assistant
 - ~~Payables Assistance~~ (position eliminated Feb)
 - Fiscal Officer (part-time, elected position)

Background

YEAR 1

July – New Finance Director identified

2nd Half – IPA completes a biennial review of previous two year end financial statements

December – Request for External Assistance in Preparing Financial Statements

YEAR 2

- Financial Statements – Year 1 prepared

YEAR 3

- Financial Statements – Year 2
- July – Auditor of State team begins biennial audit of previous two year end financial statements

Background

YEAR 3

- July 1 – August 31
 - Auditor of State begins Biennial Audit of FY 1 - FY 2
 - Unable to Reconcile Cash – 30 days to correct
 - Audit Team exits
 - Finance Director arrested at Office
 - Interim Finance Director identified and hired
- September 1 – December 31
 - Meeting with Auditor of State Team Leaders
 - Coordinated but Separate Efforts Begin with monthly updates with state team.
 - Identification of Reconciling Items Begins

YEAR 4

- January - May
 - Auditor of State team returns for fieldwork
 - Mandatory Online Financial Statement Filing Begins
 - Identification of incorrect, missing, duplicate, netted and compilation entries continues.
 - Reconciliation Difference Persist with no discernable pattern or explanation
- May/June
 - Reconciliation Variance Identified
- June – December
 - Cash Reconciliation Stabilizes with Consistent Difference for Six Months
 - Auditor of State concludes testing and publishes Audited Financial Statements with **Unqualified Opinion**

Communication & Control Breakdowns

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- Segregation of Duties
- Monthly Reconciliations
- Uncontrolled Spending
- Self-Inflicted Litigation

Key Audit Findings

Communication & Control
Breakdowns

Segregation of Duties

- Accounting Clerk
 - Accounts Payable
 - Accounts Receivable
 - Posts transactions to the system
 - Maintains blank check stock
 - Controls the check signing software
 - Distributes payable checks
 - Processes and distributes Payroll.
- Director
 - Interest Income Recognition
 - Apportionment Receipts & Expenses

Key Audit Findings

Communication & Control
Breakdowns

Monthly Reconciliations

- Cash/Investment to System
 - Never Balanced
 - Force Balanced at Last IPA Review
- Reconciling Differences system
 - Seemingly Random – No Pattern
 - Limited Research for Cause
- Lack of Clarity
- Limited Distribution
- Limited Oversight

Key Audit Findings

Communication & Control
Breakdowns

Uncontrolled Spending

- Credit Card Usage
 - Minimal Guidance
 - Inconsistent Documentation
 - Inappropriate Vendors & Purchases
- Procurement Process (\$500K+ annually)
 - Lack of Formal Process
 - Inconsistent Bidding Parameters
 - Incomplete Document of Bidding Efforts
- Contract Review/Implementation
 - Right to Audit
 - Advance Payments

Key Audit Findings

Communication & Control
Breakdowns

Self-Inflicted Litigation

- Inconsistent HR Practices
 - Inadequate Employee Manual
 - Insufficient Standards
 - High-Profile Missteps
- Wrongful Terminations
 - Settlements in Excess of \$225K
 - Additional Cases Pending

Key Audit Findings

Communication & Control
Breakdowns

Lessons Learned

One Local Government's Cautionary Tale of the Importance of Internal Controls

- Defined Roles
- Clear Communication
- Open Door Culture
- Governance

Lessons Learned

Defined Roles

- Reviewed and Revised Job Descriptions
- Reclassified Specific Positions
- Established Due Process Standards

Lessons Learned

Clear Communication

- Finance Department
 - Ledger Entries
 - Receipts Combined - **NO**
 - Expenses Netted from Receipts - **NEVER**
 - Director Posts Entries - **NOPE**
 - Clear/Repeatable Footprints
 - Semi-Annual Apportionment
 - Revenue/Receipts Recognition
 - Reconciling Differences
- External Audiences
 - Standard Chart of Accounts
 - Allocated Expenses Documentation
 - Monthly Reconciliation Report

Lessons Learned

Open Door Culture

- Finance Department
 - Understanding of Processes
 - Semi-Annual Apportionment
 - Revenue/Receipts Recognition
 - Reconciling Differences
- External Audiences
 - Periodic Feedback Sessions
 - Standard Chart of Accounts
 - Allocated Expenses Documentation
 - Monthly Reconciliation Report

Lessons Learned

Governance Lessons

- Employee Manual - Major Revisions
- Chief Compliance and Ethics Officer reporting directly to the Board
- Oversight Efforts – Finance Department
 - Established Investment Oversight Committee
 - Monthly Reconciliation Review by Compliance
 - Department Head review/approval of invoices
- Improved Contract Review Process
 - Right to Audit
 - Record Retention

Lessons Learned

Questions

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