



THE CITY OF SAN DIEGO
REPORT TO THE CITY COUNCIL

DATE ISSUED: January 25, 2011

REPORT NO: 11-019

ATTENTION: Honorable Members of the City Council and
Audit Committee Members

SUBJECT: Annual Report on Internal Controls

REQUESTED ACTIONS:

Approve this Report.

Background

In October 2004, City Council adopted Ordinance 19320 to achieve a “high standard of quality in and efficacy of the City’s financial and disclosure practices.” Municipal Code §22.0708 **Annual Report on Internal Controls**, implements this ordinance and requires that an annual report on the City’s internal controls be presented to the City Council. Accordingly, this report has been prepared for the calendar year 2010. While the Ordinance calls for an annual review and report, it is important to note that the City now has a dedicated unit, the Internal Controls Section (ICS), in the Office of the City Comptroller that is daily assessing and developing the City’s internal controls. The ICS prepares monthly reports for the Audit Committee on the status and progress made in the internal controls environment, a structural improvement that surpasses the Municipal Code requirement for annual assessment and reporting.

Discussion

It is management’s role and responsibility to establish an internal controls environment across all City operations and other areas that have a financial impact on the citywide financial reports. This includes City departments, offices, agencies, and affiliated “related entities” as defined in the San Diego Municipal Code Section 22.4102¹. While it is the responsibility of every City employee to ensure that work is conducted in accordance with established policies and procedures which support the City’s internal controls framework, the responsibility of internal controls design and monitoring currently resides with the Internal Controls Section (ICS), within the Office of the City Comptroller.

The ICS coordinates the development and documentation of the City’s financial policies and procedures. The section reviews new Process Narratives and works with department personnel to ensure adequate controls exist within each process that may have an impact on the financial

¹ Municipal Code §22.0708 states that the term “related entity” is defined in §22.1702 of the Municipal code, however, “related entity” is actually defined in §22.4102.”

statements. These Process Narratives form the basis for the ongoing monitoring and remediation of processes and control deficiencies. The ICS is currently developing the monitoring and remediation platform utilizing the tools contained within the SAP Governance, Risk and Compliance (GRC) module to strengthen the City's control environment. Once this monitoring and remediation process has been implemented, test results will indicate the level of compliance with the City's stated policies and procedures.

Currently, the ICS utilizes the GRC module to perform several key functions, including the management of segregation of duty conflicts that arise through role assignments in SAP and specific financial transaction testing. Where necessary, the ICS either develops mitigating controls that are applied to the user violation or recommends an alternative approach which will eliminate the segregation of duty violation entirely. The transaction testing process which is currently being performed supports the objective of ensuring that only transactions that have been reviewed and authorized are posted. These key functions are performed on a continuous, daily basis.

Management's internal control efforts include the citywide coordination of completing audit recommendations. The City is audited regularly both by external auditors and our internal auditors (Office of the City Auditor). Based on the findings of each audit, there is usually a list of recommendations proposed which are designed to improve operational effectiveness or correct an on-going error or non-compliance. The ICS manages a master audit recommendation database which keeps track of all open and completed audit recommendations. This database is shared with the Office of the City Auditor.

Reporting

The Office of the City Comptroller prepares a monthly Internal Controls Update report that is docketed for review at the Audit Committee on a bi-monthly basis. The most recent monthly Internal Controls Update report from December 2010 was presented at the January 10, 2011 Audit Committee (see Attachment 1).

There are no other required reports for external entities or regulating bodies concerning the City's internal controls environment. The Office of the City Comptroller meets annually with Macias Gini and O'Connell, our contracted independent financial auditors, to discuss the current sufficiency of our internal controls environment. After these discussions, the independent auditor then makes an assessment as to the level of audit risk assigned to the City engagement which determines the scope of audit field work. The Audit Committee in their due diligence review of the City's CAFR asks questions of the external auditor related to the City's internal control environment.

2010 Internal Controls Milestones

There were several noteworthy achievements this past calendar year that represent progress in developing the City's internal controls environment.

- The SEC Independent Monitor, Stan Keller, issued his final report on Kroll remediation efforts by the City of San Diego. The establishment of an internal controls framework (ICFOR) was a major remediation item. The SEC Monitor concluded that sufficient progress had been made by the City such that on-going monitoring of the internal control environment could be conducted through the governance of the Audit Committee.
- New operating agreements were signed and approved with CCDC and SEDC that require each corporation to document their policies and procedures and have those documents approved by their Board of Directors and well as by the City CFO and Agency Board. This was an internal control environment improvement for each corporation.
- A complete audit recommendation database was developed to keep track of all external and internal audit reports that have associated audit recommendations. The City identifies a “recommendation owner” within the appropriate department and a due date is identified as to management’s completion timetable for each audit recommendation. The City monitors progress against the established timelines and reports audit response completions to the Office of the City Auditor weekly. Cumulative completion statistics are also reported to the Audit Committee on a monthly basis.
- The note in the Redevelopment Agency audited financial statements *2003-1 Material Weakness in Internal Controls over Financial Reporting* was indicated as completed by our independent auditors Macias Gini and O’Connell. There were no new audit findings for the Redevelopment Agency which cited a material internal control weakness.
- Cumulatively, 132 Process Narratives and Workflow Diagrams have been developed and published. The total listing of identified Process Narratives has grown to 402 for citywide departments (270 remain to be written). Substantive progress has been made in the internal controls environment and management will begin testing internal controls in the first quarter of fiscal year 2012.

Conclusion:

Management is continuing to develop and strengthen its internal control environment and is making measured progress. Many material key controls have been designed and implemented. Internal controls are being embedded into the City’s financial processes. The City has at least two more years of structural development of our internal controls environment until reaching a steady operational state. Through the work described and the structural changes in developing and implementing internal controls, management will be prepared for an external risk audit after the close of fiscal year 2012.

There have not been any significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of management’s evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

RECOMMENDATIONS N/A

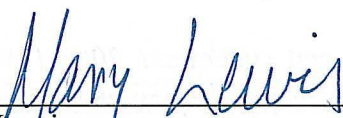
FISCAL CONSIDERATIONS: N/A

COMMUNITY PARTICIPATION AND PUBLIC OUTREACH EFFORTS: N/A

KEY STAKEHOLDERS AND PROJECTED IMPACTS: N/A

Attachments: 1. Internal Controls Progress Report – For the Month of December 2010
1. Certification by the Chief Operating Officer, Chief Financial Officer and City Comptroller

cc: Mayor Jerry Sanders
Jay M. Goldstone, Chief Operating Officer
Jan Goldsmith, City Attorney
Andrea Tevlin, Independent Budget Analyst



Mary Lewis
Chief Financial Officer



THE CITY OF SAN DIEGO
REPORT TO THE CITY COUNCIL

DATE ISSUED: January 10, 2011 REPORT NO: n/a
ATTENTION: Honorable Councilmember & Audit Committee Chair Kevin Faulconer
Honorable Members of the Audit Committee
SUBJECT: Internal Controls Progress Report – For the Month of December 2010

REQUESTED ACTION: This is an information only item, no action is required at this time.

STAFF RECOMMENDATION: n/a

SUMMARY: This is the Internal Controls Progress Report for the month ending December 31, 2010. In addition to the statistics presented in this report, we would like to provide an update on our accomplishments and activities.

We finished work on 11 process narratives and workflow diagrams in December for a total of 132 posted Process Narratives and 132 Workflow Diagrams. There are 56 additional written Process Narratives that have been submitted to Internal Controls as of December 31st that are in various stages of review. Our Master Schedule Summary indicates that there are now a total of 389 identified Process Narratives. There was an increase in past due process narratives in December to a total of 33. Generally speaking, employees have been responsive in meeting their self assigned due dates. We continue to publish our Master Schedule Summary each week and distribute it via email to the desktop of each assigned process owner.

We have continued to work on resolving segregation of duties user violations. We are pleased to report that we have been successful in mitigating all existing user violations for December. We will continue to be diligent in our on-going efforts to remediate user violations as they occur. Our goal is to keep this number to as close to zero as possible. During December, the Internal Controls Section partnered with OneSD Security to streamline the SAP access and role request processes. We are currently working to automate these processes utilizing the Access Control Module in SAP. This will increase efficiency and effectiveness while continuing to maintain the high level of security around access to the system and to functional roles. We expect to have a pilot system in place for testing and evaluation no later than March 31st, 2011 with full roll out across the organization expected no later than June 30th, 2011.

The Audit Master Database report is issued each Friday to audit response owners reminding them of their completion commitments. As of the end of December, there were 441 open audit recommendations in the database (both internal and external audits), with 255 recommendations showing as completed by City management. There are 47 individual audit reports that are marked as open. An audit will remain as open until all audit recommendations have been completed by City management and have been verified by the auditing agency (i.e. the Office of the City Auditor or an external auditing firm).

Included in our update report this month is a new table showing the number of open audit recommendations sorted by audit name and the responsible responding City Department. For each item listed, we have indicated the number of City completed audit recommendations and the number of audit recommendations where the department response is past due based on the response date provided by the respective department. This table will now be included monthly in our Internal Controls Update report.

During the month of December, the Internal Controls Section has allocated a resource on a part-time basis (approximately 4 hours per week), to assist the Customer Care Solutions (CCS) Team in the implementation of an internal control framework that integrates with the current structure being developed by the Office of the City Comptroller. Activities performed include review of the conversion risk assessments and related documented controls, familiarization with CCS activities, and the review of control frameworks.

The chart below details the activities and accomplishments of the Internal Controls section within the Office of the City Comptroller for the month of December 2010.

Category	Beginning Balance	Cumulative Completed	Estimated Items Remaining	Current Activity by Month			
	9/1/2009	12/31/2010		Sep-10	Oct-10	Nov-10	Dec-10

Operational

Process Narratives	0	132	257	12	15	14	11
Workflow Diagrams	0	132	257	12	15	14	11

Governance Risk and Compliance (GRC)

Mitigating Access Controls Developed	27	19	100	0	0	0	0
Entity Level Controls Developed	32	3	Ongoing	0	0	0	0
Process Controls Developed	181	6	300	0	0	0	0
Automated Control Monitoring Performed				120	124	120	132

Segregation of Duties

Users Analyzed				10,289	10,275	10,258	10,227
Users with no Violations				10,282	10,274	10,258	10,227
Users with Violations				7	1	0	0

Resources: Project Work Hours Available

Principal Accountant	0	532	1,151	116	107	102	44
Supervising Accountant	0	1,599	324	168	160	136	144
Staff Accountant	0	1,711	156	151	81	109	120
Staff Accountant	0	1,461	171	143	152	155	95
	0	5,304	1,802	578	500	502	403

Process Narrative Completion Report & Schedule as of 12/31/10

33 Items Past Due

	Code	Status
198	1	Pending Process Owner - Requested Open Item
3	2	Unassigned - Pending Assignment by Internal Controls
56	3	Pending Internal Controls - Received and Currently Reviewing
132	4	Completed Document - Posted to Internal Controls Website
389	Total	

Audit Summary Information	City Activity			
	Number of Audits	Number of Audit Recommendations	Monthly Completed	Cumulative Completed
Internal-OCA - Open	42	412	11	247
External - Open	5	29	1	8

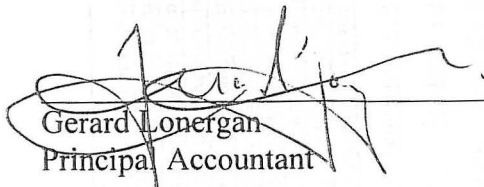
**Internal-OCA reports include all reports with recommendations, Audits, Hotline, Close-outs*


Audit Activity Since Prior Update Report - Added and Closed Audits

Status	Audit Type	Issue/Closed Date	Audit #	Audit Name	Number of Audit Recommendations
				No Activity Reported	0

Attachment: 1. Audit Recommendations Past Due Report 12/31/10

cc: Honorable Mayor Jerry Sanders
 Jay M. Goldstone, Chief Operating Officer
 Mary Lewis, Chief Financial Officer
 Andrea Tevlin, Independent Budget Analyst
 Eduardo Luna, City Auditor


 Gerard Lonergan
 Principal Accountant


 Ken Whitfield
 City Comptroller

Open Audit Recommendations by Audit and Responding Department

Audit #	Audit Report Title	Department	Issue Date	Audit Recommendations				
				Total # of Recommend	Completed by Management	% Reported Complete	Past Due	% Past Due
08-010	CENTRAL STORES INVENTORY AUDIT - PURCHASING & CONTRACTING DEPARTMENT	Purchasing & Contracting (HP)	12/10/2007	9	7	78%	0	0%
08-011	CITY OVERSIGHT OF THE SAN DIEGO PUBLIC LIBRARY FOUNDATION	San Diego Public Library	2/19/2008	20	20	100%	0	0%
08-019	CASH COUNT AND BANK RECONCILIATION AUDIT - KROLL REMEDIATION OF THE CITY'S BANK RECONCILIATION PROCESS	City Treasurer	4/28/2008	6	5	83%	0	0%
08-020	AUDIT OF PERMITS ISSUED FOR THE BLACKWATER FACILITY	Developmental Services	6/5/2008	8	7	88%	0	0%
09-001	AUDIT OF THE INTERNAL CONTROL REMEDIATION RELATED TO THE SAN DIEGO CITY EMPLOYEES RETIREMENT SYSTEM	Mayor's Office	8/29/2008	3	3	100%	0	0%
09-001	AUDIT OF THE INTERNAL CONTROL REMEDIATION RELATED TO THE SAN DIEGO CITY EMPLOYEES RETIREMENT SYSTEM	San Diego City Employees' Retirement System (SDCERS)	8/29/2008	3	2	67%	0	0%
09-004	AUDIT OF THE SAN DIEGO PUBLIC LIBRARY FEE COLLECTION PROCESS	San Diego Public Library	11/20/2008	9	9	100%	0	0%
09-005	AUDIT OF THE 2007 WILDFIRE DEBRIS REMOVAL PROJECT	Environmental Services Department	12/19/2008	14	7	50%	0	0%
09-006	HOTLINE INVESTIGATION OF THE JUNIOR LIFEGUARD PROGRAM'S DEPOSITS OF FUNDRAISER MONIES	Fire-Rescue	1/16/2009	1	1	100%	0	0%
09-008	HOTLINE INVESTIGATION OF THE DUPLICATION OF WATER METER BOX REPLACEMENT WORK	Metro Wastewater (MWWWD-JF)	2/23/2009	1	1	100%	0	0%
09-009	HOTLINE INVESTIGATION OF THE FOURTH DISTRICT SENIOR RESOURCE CENTER	Parks & Recreation	4/7/2009	1	0	0%	0	0%
09-013	THE CITY OF SAN DIEGO FACES UNIQUE OPERATIONAL AND ADMINISTRATIVE CHALLENGES IN MANAGING QUALCOMM STADIUM	Real Estate Assets Department	5/8/2009	9	0	0%	0	100%
09-014	AUDIT OF SAN DIEGO DATA PROCESSING CORPORATION'S COMPENSATION AND BUDGETING PRACTICES	San Diego Data Processing Corporation (SDDPC)	5/5/2009	6	5	83%	0	0%
09-016	AUDIT OF ACCOUNTS OF WENDI BRICK, FORMER CUSTOMER SERVICES DIRECTOR, ELMER HEAP, FORMER DEPUTY CHIEF OPERATING OFFICER, JILLANNE (JILL) OLEN, FORMER DEPUTY CHIEF OPERATING OFFICER, AND JOANNE SAWYERKNOLL, FORMER DEPUTY CHIEF OPERATING OFFICER	Personnel	6/16/2009	3	2	67%	0	0%
09-017	PARK & RECREATION POOL AUDIT	Parks & Recreation	5/20/2009	17	12	71%	0	0%
09-018	AUDIT OF THE SAP ERP IMPLEMENTATION - CURRENT TO INTEGRATION TESTING, CYCLE 1	ERP Development Team	6/11/2009	7	7	100%	0	0%
09-021	HOTLINE INVESTIGATION OF PROMOTE LA JOLLA, INC.	Economic Development Division	6/29/2009	4	3	75%	0	0%
09-023	AUDIT OF THE CENTRAL STORES INVENTORY	Purchasing & Contracting (HP)	2/27/2009	7	4	57%	0	0%
09-027	CAFR AUDIT - YELLOW BOOK	Comptroller's Office	12/21/2009	10	5	50%	2	20%
09-028	SINGLE AUDIT	Comptroller's Office	12/21/2009	14	0	0%	0	0%
09-029	RDA ANNUAL FINANCIAL REPORT	Comptroller's Office	12/23/2009	3	2	67%	0	0%
09-030	TRANSNET FUND	Comptroller's Office	2/1/2010	1	0	0%	0	0%
09-031	EXHIBIT E	Metro Wastewater (MWWWD-DM)	2/10/2010	1	1	100%	0	0%
09-0A-001	SOUTHEASTERN ECONOMIC DEVELOPMENT CORPORATION PERFORMANCE AUDIT OF OPERATIONS	Southeast Economic Development Corporation (SEDC)	9/10/2008	29	20	69%	0	0%
09-0A-001	SOUTHEASTERN ECONOMIC DEVELOPMENT CORPORATION PERFORMANCE AUDIT OF OPERATIONS	Mayor's Office/Auditor	9/10/2008	4	0	0%	4	100%
10-001	METROPOLITAN WASTEWATER DEPARTMENT CONTRACT COMPLIANCE AUDIT	Purchasing & Contracting (HP)	7/24/2009	1	0	0%	0	0%
10-001	METROPOLITAN WASTEWATER DEPARTMENT CONTRACT COMPLIANCE AUDIT	Metro Wastewater (MWWWD-DM)	7/24/2009	11	11	100%	0	0%
10-002	PERFORMANCE AUDIT OF THE SAN DIEGO HOUSING COMMISSION - PART I	San Diego Housing Commission (SDHC)	7/29/2009	19	11	58%	2	11%
10-003	PERFORMANCE AUDIT OF THE SAN DIEGO HOUSING COMMISSION - PART II	Mayor's Office	7/29/2009	1	0	0%	1	100%
10-003	PERFORMANCE AUDIT OF THE SAN DIEGO HOUSING COMMISSION - PART II	San Diego Housing Commission (SDHC)	7/29/2009	11	4	36%	4	36%
10-005	CENTRAL STORES AGREED-UPON PROCEDURES INVENTORY COUNT-FY2009	Purchasing & Contracting (HP)	9/8/2009	1	1	100%	0	0%
10-006	OFFICE OF THE CITY ATTORNEY PROPOSITION 64 FUNDS AUDIT	City Attorney	9/30/2009	7	7	100%	0	0%
10-007	PERFORMANCE AUDIT OF THE CITY'S STREET MAINTENANCE FUNCTIONS	Purchasing & Contracting (MS)	10/26/2009	4	3	75%	0	0%
10-008	HOTLINE INVESTIGATION OF A CITY COMPTROLLER EMPLOYEE	Risk Management	11/23/2009	2	1	50%	0	0%
10-009	SAN DIEGO DATA PROCESSING CORPORATION FOLLOW-UP AUDIT	San Diego Data Processing Corporation (SDDPC)	11/30/2009	14	13	93%	0	0%
10-009	SAN DIEGO DATA PROCESSING CORPORATION FOLLOW-UP AUDIT	Department of Information Technology	11/30/2009	2	0	0%	2	100%
10-010	PERFORMANCE AUDIT OF THE CITY TREASURER DELINQUENT ACCOUNTS PROGRAM	Developmental Services	12/2/2009	12	6	50%	0	0%


Open Audit Recommendations by Audit and Responding Department

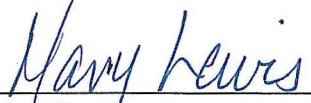
Audit #	Audit Report Title	Department	Issue Date	Audit Recommendations				
				Total # of Recommend	Completed by Management	% Reported Complete	Past Due	% Past Due
10-010	PERFORMANCE AUDIT OF THE CITY TREASURER DELINQUENT ACCOUNTS PROGRAM	ERP Development Team	12/2/2009	2	2	100%	0	0%
10-011	CITY CHARTER REQUIREMENTS FOR UNCLAIMED FUNDS	Comptroller's Office	12/30/2009	1	0	0%	0	0%
10-016	CITYWIDE REVENUE	City Treasurer	3/5/2010	9	7	78%	0	0%
10-016	CITYWIDE REVENUE	Comptroller's Office	3/5/2010	4	1	25%	0	0%
10-016	CITYWIDE REVENUE	Financial Management	3/5/2010	5	4	80%	0	0%
10-016	CITYWIDE REVENUE	General Services	3/5/2010	1	1	100%	0	0%
10-016	CITYWIDE REVENUE	Real Estate Assets Department	3/5/2010	4	2	50%	0	0%
10-017	PERFORMANCE AUDIT OF THE CITY TREASURER'S INVESTMENTS DIVISION	City Treasurer	3/25/2010	3	3	100%	0	0%
10-018	PERFORMANCE AUDIT OF THE PURCHASING AND CONTRACTING DEPARTMENT	Purchasing & Contracting (HP)	3/30/2010	6	0	0%	0	0%
10-019	PERFORMANCE AUDIT OF THE SUBCONTRACTOR OUTREACH PROGRAM	Administration Department	4/30/2010	13	6	46%	0	0%
10-020	PERFORMANCE AUDIT OF THE DEVELOPMENT SERVICES DEPARTMENT'S COLLECTION OF WATER AND SEWER FEES	Developmental Services	6/22/2010	7	3	43%	0	0%
10-OA-001	PERFORMANCE AUDIT OF THE CENTRE CITY DEVELOPMENT CORPORATION	Center City Development Corporation (CCDC)	7/10/2009	24	18	75%	0	0%
10-OA-002	AUDIT OF THE SAN DIEGO CONVENTION CENTER CORPORATION	San Diego Convention Center Corp (SDCC)	7/29/2009	11	11	100%	0	0%
10-OA-003	REVIEW OF THE HIRING PROCESS OF THE DIRECTOR OF PURCHASING AND CONTRACTING	Labor Relations	8/21/2009	5	5	100%	0	0%
11-001	PERFORMANCE AUDIT OF RISK MANAGEMENT'S PUBLIC LIABILITY AND LOSS RECOVERY DIVISION	Risk Management	8/31/2010	23	6	26%	0	0%
11-002	HOTLINE INVESTIGATION REPORT OF ABUSE FROM THE SALE OF SCRAP METAL	General Services	7/21/2010	1	1	100%	0	0%
11-006	PERFORMANCE AUDIT OF THE FIRE PREVENTION ACTIVITIES WITHIN THE CITY OF SAN DIEGO	Fire-Rescue	10/6/2010	23	2	9%	0	0%
11-007	PERFORMANCE AUDIT OF CITY TREASURER'S DELINQUENT ACCOUNTS PROGRAM	City Treasurer	10/25/2010	7	0	0%	0	0%
11-008	HOTLINE INVESTIGATION OF CONTRACT ADMINISTRATION WITH THE GREATER GOLDEN HILL COMMUNITY DEVELOPMENT CORPORATION	Planning	11/5/2010	3	1	33%	0	0%
11-009	PERFORMANCE AUDIT OF STREET MAINTENANCE	Public Works	11/29/2010	14	2	14%	0	0%

CERTIFICATION BY MAYOR AND CHIEF FINANCIAL OFFICER

In accordance with the requirements of §22.0708 of the San Diego City Ordinance 19320, the Mayor's designee, the Chief Operating Officer and the Chief Financial Officer hereby certify that they:

- (1) are responsible for establishing and maintaining the City's internal financial controls;
- (2) have identified the need to design such internal financial controls to ensure that material information relating to the City and its departments, offices, agencies, and affiliated "related entities" as defined in San Diego Municipal Code section 22.1702, is made known to the Mayor and/or the Chief Financial Officer by others within the City and its departments, offices, agencies, and affiliated "related entities," particularly during the period in which the Annual Report required by this section is being prepared;
- (3) have evaluated the effectiveness of the City's internal financial controls as of a date within 90 days prior to the Annual Report;
- (4) have presented in the Annual Report their conclusions about the effectiveness of their internal controls based on such evaluation as of that date;
- (5) have disclosed to the City's independent auditors and the Audit Committee all significant deficiencies in the design or operation of internal controls that could adversely affect the City's ability to record, process, summarize, and report financial data;
- (6) have identified for the City's independent auditors any material weaknesses in internal controls and any fraud, whether or not material, that involves management or other employees who have a significant role in the City's internal controls; and
- (7) have indicated in the Annual Report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of their evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Signed: 
Jay M. Goldstone
Chief Operating Officer

Signed: 
Mary Lewis
Chief Financial Officer

Date: 1-24-11

Date: 1-25-11

Signed: 
Kenton Whitfield
City Comptroller

Date: 1-25-11

