

Annual Report on Internal Financial Control

15th Edition

Calendar Year 2020

Department of Finance

March 1, 2021



Executive Summary

This Annual Report on Internal Control is issued pursuant to City of San Diego Municipal Code (SDMC) §22.0706, adopted by the City Council in October 2004 via Ordinance 19320 to achieve a high standard of quality in and efficacy of the City of San Diego's (City's) financial reporting and disclosure practices. SDMC §22.0706 requires that management:

1. Perform an annual evaluation of the City's internal financial controls;
2. Submit a written Annual Report to the Audit Committee and the City Council on management's annual evaluation of the City's internal financial controls;
3. Submit a Certification by City Management regarding the design, maintenance, and effectiveness of the City's internal financial controls.

The objective of a system of internal controls over financial reporting is to provide reasonable assurance that the financial information produced is reliable and that it reflects the City's transactions and events for the reporting period. It is not intended to eliminate all risk as factors such as collusion, human error, inconsistencies in judgement, impacts of external events outside management's control, and cost effectiveness can have an influence on an organization's control policies and procedures. Rather, the controls are intended to mitigate the risk of financial reporting errors to a level that is acceptable based on considerations of materiality. Materiality represents the magnitude of an omission or misstatement of an item in a financial report that in light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the inclusion or correction of the item.

Internal control is influenced by a board of directors, management, and other personnel. The City must consider the efficacy of the organization's governance structure and culture to produce accurate and reliable reporting. Management must continuously assess risk, as financial reporting standards or requirements change, and new software or technology is implemented. Risk can also increase as accounting and reporting processes change and as there is turnover in management and staff. As new risks are identified, management responds by implementing or enhancing controls to mitigate such risks.

Within the last 120 days, management evaluated the City's internal financial controls over financial reporting. Based on this evaluation, management concludes that the internal financial controls are effective and has certified the result (Attachment 1).

Starting with this edition of the report, the Department of Finance (DoF) is including an assessment template to illustrate the approach used for management's evaluation of internal financial controls. The template is intended to help the reader understand management's criteria in its evaluation and offer more visibility into the process. The template and its results are included as an attachment (Attachment 2) for reference and described in more detail later in the report.

This report summarizes management's approach to maintaining an internal control system that provides reasonable assurance that financial reporting objectives are met. Significant enhancements during calendar year 2020 and potential risks that were identified, either by management or through the audits performed by external auditors and the Office of the City Auditor (City Auditor), are included. For this reporting period, management did not identify any 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.

Financial Reporting Achievements and Internal Control Improvements

The list below identifies the most significant financial reporting achievements and internal control improvements implemented during the assessment period.

- Received an unmodified (clean) audit opinion on the City's fiscal year 2020 Comprehensive Annual Financial Report. No material adjustments, material weaknesses, or significant deficiencies in internal controls over financial reporting were identified through the Comprehensive Annual Financial Report independent audit.
- Received a Certificate of Achievement for Excellence in Financial Reporting from the Government Finance Officers Association (GFOA) for the fiscal year 2019 Comprehensive Annual Financial Report. In order to be awarded a Certificate of Achievement, the City must publish an easily readable and efficiently organized Comprehensive Annual Financial Report that satisfies both generally accepted accounting principles and applicable GFOA program requirements.
- Received a Distinguished Budget Presentation Award from GFOA for the fiscal year 2020 Adopted Budget. Recipients are awarded this honor for meeting guidelines set by the National Advisory Council on State and Local Budgeting (NACSLB) and GFOA's best practices on budgeting.
- Created the position of Chief Compliance Officer to assist the City in coordinating and enforcing compliance issues with various regulations, policies, and procedures. Created the Risk Oversight Committee (ROC) to aid the City in actively managing risk efforts.
- Implemented several system enhancements including improving the functionality of the City's budget monitoring module, adding an accounting review component to the City's infrastructure asset module, and added the ability to more efficiently record found or donated assets with verification.
- Upgraded several software applications to new versions or patched with service packs to add new features, fix known bugs, and improve data security. These include updates to Vendor Invoice Management (VIM) for automated invoice processing, SAP Budget and Planning for Public Sector (SBP) for budgeting, and SAP Governance Risk and Compliance (GRC) for risk identification and role assignment provisioning.

- Implemented a risk-based approach to review documentation for presence of controls. The DoF assesses the risks of material misstatement in a process narrative in order to prioritize more high-risk processes.
- Provided additional resources for employees eligible to work remotely such as hardware (laptops, monitors, and peripherals), remote access through Virtual Private Networking (VPN), and access to document sharing and collaboration software as well as video conferencing.
- Transitioned Finance Academy training to a virtual format allowing remote working employees to attend. These Academies are intended to train city employees responsible for financial data and inform employees of the proper procedures and expected standards.
- Performed a Business Impact Analysis/Risk Assessment (BIA/RA) of key business functions and identified applications supporting those functions. Created Disaster Recovery Plans (DRP) to minimize downtime and data loss.
- Implemented additional enhancements to internal controls to address the risk related to the restatement in the Fiscal Year 2019 Comprehensive Annual Financial Report, Statement of Net Position. These enhancements were implemented prior to the start of the Fiscal Year 2020 Comprehensive Annual Financial Report and included development of a formal materiality threshold policy, a risk based assessment over complex accounting transactions, the completion of a process narrative addressing bond refunding transactions, the creation of a special fund to account for Government-wide balances and activity, formalization of the analytical review process, and continuing education for staff including the conversion entry process.
- Created, or updated several Citywide financial reports including the Fund Certification Report, the Accounts Payable Dashboard, and the Human Resources Turnover Dashboard. In addition, approximately 40 additional financial reports were created for individual departments or programs.

Background

The City is accountable to San Diego residents and outside stakeholders for the management of the City's financial and economic resources. It meets this responsibility in large part by preparing financial reports made available to the public each fiscal year.

External Financial Reports

The Comprehensive Annual Financial Report is the most significant financial report produced by the City for external users. It is available on the City's website and can be accessed by residents, investors, rating agencies and other interested parties. The Comprehensive Annual Financial Report is a comprehensive financial document that includes the balances and activity of all funds and component units of the City and related disclosures. The report typically takes

five months to prepare and involves the collaboration of the DoF staff, as well as key outside department staff who provide necessary information for required disclosures. The Comprehensive Annual Financial Report is prepared in accordance with Generally Accepted Accounting Principles (GAAP), which are established by the Governmental Accounting Standards Board (GASB). The Comprehensive Annual Financial Report is audited annually by an external, independent auditing firm who expresses an opinion on whether or not the basic financial statements are fairly presented in all material respects in accordance with GAAP. The City received an unmodified (clean) audit opinion on the fiscal year 2020 Comprehensive Annual Financial Report.

The City also produces other financial reports for external use such as the Schedule of Expenditures of Federal Awards, which summarizes all expenditures of federal awards for the fiscal year and is subject to a single audit by an external independent auditor (Single Audit). The City received an unmodified (clean) audit opinion on the fiscal year 2019 Single Audit. The fiscal year 2020 Single Audit is expected to be completed by March 31, 2021. The City's external auditor also conducts an audit of the schedule of costs for the fiscal year related to the Metropolitan Wastewater System and the City's allocation of such costs to last audit period.

Internal Financial Reports

Reports for internal use are published and presented to the City's legislative body, the City Council, and available to the public. Not only are these reports mandated as part of City Charter or the SDMC, they promote transparency and oversight of management's financial spending and plans. The City's annual budget is in many respects the most important financial report because it informs readers of the Mayor's priorities in terms of financial characteristics and serves as a key tool for financial management and compliance. Proper planning through the budget also facilitates compliance with rules and regulations, and ensures restricted funding sources are spent appropriately.

The City also publishes a long-range forecasting report known as the Five-Year Financial Outlook to establish a framework for the development of the annual budget and anticipate potential funding needs over a medium to long-term horizon.

Lastly, the Chief Financial Officer publishes monthly expenditure and revenue reports known as Charter 39 Financial Performance Reports, and quarterly year-end projection reports known as Budget Monitoring Quarterly Reports. These reports assist management and City Council with managing budgets and explaining variances in spending or revenue collection.

Management's Approach Using an Internal Controls Framework

Internal control over financial reporting is defined as a process established by an entity's governing body, management and other personnel, which has been designed and implemented to provide reasonable assurance regarding the achievement of financial reporting objectives. The main internal control objective in preparing financial reports is that the information included in the report is reliable and that it reflects the City's transactions and events for the reporting period in accordance with GAAP or other reporting requirements.

The Committee of Sponsoring Organizations of the Treadway Commission's (COSO) Internal Controls Framework is an integrated framework commonly used by organizations. This Framework is a basis for the City's internal control program and provides guidance on internal controls over financial reporting. The framework put forth by COSO is comprised of five fundamental components which, when present and functioning together, work towards the goals of reducing risk to an acceptable level and achieving objectives for reliable financial reporting. These five fundamental components include:

1. Control Environment
2. Risk Assessment
3. Control Activities
4. Information and Communication
5. Monitoring Activities

The assessment of internal control over financial reporting focused on an evaluation of each of these five components.

For calendar year 2020, the DoF has incorporated a new management assessment template (Attachment 2) to help assess the effectiveness of the City's system of internal financial controls and ensure that it meets the following requirements:

- Each of the five components and relative principles are present and functioning.
 - A component of internal control supports an organization's efforts in achieving its financial reporting objectives. The component describes what is required for the organization to meet their objectives and are relevant to an entire entity or at any entity level, division, operating unit, or function of the organization.
 - A principle is a fundamental concept associated with one of the five components of internal control. There is a total of seventeen principles in the Framework.
- The five components are operating together in an integrated manner (Attachment 3).

The management assessment template contains the following four sections:

1. Overall Assessment—Summarizes management's determination of whether each of the components and relevant principles is present and functioning and components are operating together in an integrated manner.
2. Components—Summarizes management's determination of whether each component and relevant principles are present and functioning. A template for each of the five components is included.
3. Principles—Summarizes the controls to effect principles and management's determination of whether each relevant principle is present and functioning. A template for each of the seventeen principles is included. The Framework

also includes points of focus to describe important characteristics of each principle. However, the Framework does not require management to evaluate whether all points of focus are in place.

4. Deficiencies—A log of all identified internal control deficiencies that can be leveraged in the evaluation of components and principles and can enable the internal control deficiencies to be aggregated.

The template provides a logical structure for management to analyze and document the organization's assessment of effectiveness of internal controls and assist management in developing a process for identifying and evaluating internal control deficiencies. The template is not an integral part of the internal control framework but serves as an illustrative aide.

1. Control Environment

The Control Environment is the set of standards, processes, and structures that provide the basis for carrying out internal control across the organization. The Control Environment sets the tone of the organization and represents what is commonly referred to in the private sector as an entity's "corporate culture." It encompasses the City's integrity and ethical values; the City Council and Mayor's oversight, responsibilities, and delegation of authority; the process for attracting, developing and retaining employees; and the measures, incentives and rewards used to manage accountability and performance. The City has established policies and practices that provide for a strong control environment through the City Charter, San Diego Municipal Code, management policies and practices and a comprehensive financial training program.

City Charter

The City is organized as a strong-mayor form of government where the mayor acts as the executive branch of government carrying out the operating functions of the City, while the City Council acts as the legislative body. This model of government provides checks and balances through separation of powers and is codified in the San Diego City Charter. The mayor appoints the Chief Financial Officer of the City and the City Council confirms. City Charter Section 39 gives supervision and oversight responsibility over all financial accounts of the City to the Chief Financial Officer. It requires that all financial transactions of the City be performed based upon forms prescribed by the Chief Financial Officer.

Charter Section 39.1 establishes an independent audit committee to oversee the City's auditing function. The Audit Committee is composed of two members from the City Council facilitating independence from management and three members from the public who possess the appropriate technical expertise to carry out this responsibility.

Charter Sections 39.2 and 39.3 also establish independent positions to assist the City Council in maintaining checks and balances over the executive branch, including the Independent Budget Analyst and City Auditor. The Independent Budget Analyst provides budgetary and policy analysis for the City Council. The City Auditor is responsible for the internal audit

function of the City, with authority to investigate any material claim of financial fraud, waste, or impropriety within any City department. The City Auditor reports to the Audit Committee to prevent any conflicts of interest from reporting to the executive branch.

In May 2020, City Charter was amended to have the Council select the City Auditor from at least 3 candidates for a five-year term recommended by the Council's Audit Committee. Previously, the mayor appointed the City Auditor for a 10-year term and City Council confirmed.

The City, like most large governments and corporations, also retains an independent audit firm to independently audit its financial statements. The City's current external independent auditor, Macias Gini & O'Connell LLP, reviews the City's financial statements and accompanying notes and reports on any findings during their audit process. The contract for the City's external audit firm is administered by the City Auditor and is evaluated every five years.

San Diego Municipal Code (SDMC)

The SDMC incorporates all ordinances passed by the City Council and approved by the Mayor. On October 11, 2004, Ordinance No. 19320 incorporated Division 41: Securities Disclosure, which establishes the Disclosures Practices Working Group (DPWG), a group of senior City officials and disclosure counsel responsible for ensuring compliance by the City with federal and state securities laws, and for promoting the highest standards of accuracy in disclosures relating to securities issued by the City or by its related entities. As required by the SDMC, the DPWG has developed the Disclosure Controls and Procedures to effectuate its responsibilities under the SDMC.

The Disclosure Controls and Procedures establishes process requirements over the development of documents that have disclosure obligations under applicable federal and state securities laws, including bond documents and the City's Comprehensive Annual Financial Report. It establishes responsibilities for development and review of the financial documents and requires certification by those department heads that contribute information for development of such documents.

In addition, the SDMC establishes the Ethics Commission, which contributes towards a strong control environment for the City. As an independent department, the Ethics Commission monitors, administers and enforces the City's governmental ethics laws, conducts investigations, refers violations to appropriate enforcement agencies, reviews disclosure statements and advises and educates City officials, candidates, political committees, and lobbyists about governmental ethics laws. All City management is required to participate in training provided by the Ethics Commission once every two years.

Chief Compliance Officer and Risk Oversight Committee

The position of Chief Compliance Officer was created in early 2020 to assist the City in coordinating and enforcing compliance issues with various regulations, policies, and procedures. For example, the Chief Compliance Officer has played a key oversight role in reviewing department expenditures for eligibility of federal funding related to the recent COVID-19 pandemic. The U.S. Department of Treasury has provided Cities guidance agencies must follow and the Chief Compliance Officer has been working closely with departments to comply with federal requirements. Another key responsibility of the position is improving the coordination of Citywide responses to audit findings and recommendations especially when multiple departments are involved. The Chief Compliance Officer participates in Audit Committee meetings and serves as a representative for City management.

The City created a new Risk Oversight Committee (ROC) lead by the Chief Compliance Officer as the chair. The members of ROC consist of the Chief Operating Officer, Chief Financial Officer, all Deputy Chief Operating Officers, and the Chief Innovation Officer. The goal of ROC is to aid the City in actively managing risk efforts and considers financial controls in its discussions of enterprise risk.

Management Policies and Practices

The Chief Operating Officer issues Administrative Regulations (A.R.s) to establish policies, roles, and procedures of a continuing nature and to direct operations within the City. Additionally, departments involved in complicated, lengthy, or detailed operations are required to work with the Internal Controls Section in the DoF to develop and issue process documentation to detail the performance of these operations. Also, citywide policy memorandums are sent out as necessary to clarify or establish policies and procedures for the City's mayoral departments. The City's policies and procedures are communicated to employees via citywide email or by posting on the City's intranet and internet.

In 2017, A.R. 95.39-Management Responsibilities for Internal Financial Controls was established to provide a strong enhancement over the City's control environment. The A.R. establishes responsibility for developing citywide financial policies and procedures within the finance branch, including citywide dissemination of such policies and training as appropriate. It also emphasizes the role of the executive management team in creating an organizational culture that supports the internal control environment.

Financial Training

The City has implemented a comprehensive financial training program adopted on December 6, 2006 by Resolution R-302243. As part of citywide financial training, all levels of the organization are provided training to aid employees in submitting or reviewing financial data and reports. This includes city employees, city management, and elected officials. Under SDMC §22.4110, the City has established biennial mandatory Federal securities law training for members of management, relevant City staff, and elected officials to ensure material information in financial documents is disclosed in accordance with state and federal security

laws. In addition, elected officials are provided tailored trainings and presentations on financial topics such as budgeting principles and financial statement disclosure.

Continuing education for professional staff who have financial responsibilities is critical for delivering comprehensive and accurate financial information to the City's stakeholders. The City's Chief Financial Officer requires financial professionals to grow and maintain their professional competencies in all areas of accounting, reporting, compliance, internal controls, grant analysis, debt management, ethics, and other finance related fields. This is accomplished through training policies tailored to promote competencies in each department's respective area. For example, the Department of Finance's training policy requires that staff engaged in accounting, financial reporting, budget, and payroll functions participate in a minimum of 40 hours of formal subject matter training per year.

The DoF staff members are also encouraged to attain professional designations such as a Certified Public Accountant (CPA) to maintain professional expertise on the latest accounting standards and practices. As of the end of calendar year 2020, the DoF has 13 staff members with the designation and they are required to enroll in continuing education courses to maintain their active status. The DoF also registered 9 staff members for training on internal control practices under the COSO framework to bolster financial controls.

As a result of the COVID-19 pandemic, many in-person conferences, seminars, and classes were cancelled. However, many of these training opportunities were eventually replaced with an online training version in the form of webinars or virtual trainings. This allowed employees to maintain their training and sometimes at an even more cost-effective manner as webinars usually do not have the same overhead (parking, facilities, support staff) that an onsite training would charge.

Other Practices and Policies

Other practices and policies contributing to a strong control environment for the City include the adoption of an Employee Code of Conduct, the Fraud, Waste, and Abuse Hotline, Annual Report of the City of San Diego DPWG, and the Annual Report on Internal Financial Control.

2. Risk Assessment

A continuous and effective assessment of risk is a critical component of the internal control framework because it allows management to form a basis for determining how risk should be managed and mitigated. It allows management to identify the need for control and monitoring activities, improvements to the flow of information and communication or the need for changes to the control environment.

COSO defines *risk* as the possibility that an event will occur and adversely affect the achievement of objectives. As noted earlier, the main objective in preparing the Comprehensive Annual Financial Report is that the information included in the report is reliable and that it reflects the City's transactions and events for the reporting period in accordance with GAAP or

other reporting requirements. The policies and procedures established for financial reporting include controls that have resulted from management's risk assessment and its efforts to mitigate such risks.

Changes in Leadership

In November 2020, Todd Gloria was elected the new mayor of the City which resulted in changes to the administration. Some of these included a new Chief Operating Officer, new Chief Financial Officer, new Comptroller and Department of Finance Director, and reduction of the Assistant Chief Operating Officer position. The City Council also changed significantly when five of the nine councilmembers were replaced in the 2020 general election.

The search for a new City Auditor also concluded late 2020 after a ballot proposition passed to modify the selection process and have the mayor removed from choosing the City Auditor. The Independent Budget Analyst and a subcommittee consisting of Audit Committee members coordinated the hiring process. The Audit Committee recommended hiring the Interim Assistant City Auditor in the City's Auditor Office and City Council confirmed the appointment.

Changes to staffing are expected during an election year, but pose a risk from loss of operational knowledge and continuity. However, this is typically mitigated through existing policies, documentation, training, and supporting career staff that have institutional knowledge of operations and financial reporting requirements. In many of the positions with financial responsibilities, the risk is further mitigated by the fact that the individuals filling the high-level positions also possess a finance background with in-depth experience and have held various City management finance positions in the past.

Management's Risk Assessment on Comprehensive Annual Financial Report

At the beginning of each Comprehensive Annual Financial Report preparation cycle, management communicates areas of potential risk to the City's external auditor based on management's risk assessment and ongoing monitoring activities, including management's response to such risks through development and implementation of additional controls. For the fiscal year 2020 Comprehensive Annual Financial Report, no significant risks were identified to the City's external auditor.

Changes in Accounting Standards

To mitigate the risk associated with changes in accounting standards, the DoF staff that have primarily Comprehensive Annual Financial Report preparation responsibilities are provided training throughout the year, including an annual GFOA training introducing new accounting pronouncements, and disseminate this information through cross-training within the department. Staff actively reviews all new standards to determine the applicability and requirements to properly implement in the effective reporting period. Staff also works closely with the City's external auditors to ensure full compliance with reporting standards are met.

Each fiscal year, the DoF evaluates new accounting standards promulgated by GASB for potential financial impact. Research is assigned to the appropriate section in the department for in-depth analysis and implementation. In fiscal year 2020, the City successfully implemented GASB Standard No. 84 regarding Fiduciary Funds, GASB Standard No. 90 regarding Majority Equity Interests, and is currently researching the standards applicable for the fiscal year 2021 Comprehensive Annual Financial Report and beyond such as GASB Standard No. 87, Leases. This new standard for leases is expected to increase the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows or outflows of resources based on the payment provisions of the contract. Due to the scope of the standard and the volume of lease agreements the City is a party to, at least 800 leases, the expertise and resources needed to comply with the accounting and reporting requirements of the standard are substantial. To mitigate risks related to the implementation of this standard, the DoF has developed a comprehensive plan for the implementation of GASB Standard No. 87. This plan includes staff dedicated to a Citywide effort to identify, obtain, and review lease contracts and lease data from City departments. In addition, the DoF, in collaboration with DoIT and Real Estate Assets Department, is in the process of selecting a lease accounting software. GASB Standard No. 87 is required to be implemented into the Comprehensive Annual Financial Report by fiscal year 2022.

Changes in Technology

The City continues to modify and add modules to the core Enterprise Resource Planning (ERP) system in order to maximize the efficiency and span of control over business operations and reporting. Each of these changes introduces the risk of system generated errors, which are mitigated through configuration and development testing. Business process owning departments such as the DoF, the Department of Information Technology (DoIT), Purchasing and Contracting, Personnel, Human Resources, Risk Management, and the Office of the City Treasurer all work closely to ensure that any changes or improvements to the system are fully tested for operational needs and for the impact to financial reporting. At the completion of testing, signoffs are required by business process coordinators involved.

Several key enhancements were made to further tighten controls over financial systems data integrity including the following:

- An enhancement was made to the budget monitoring module that allowed users to post transactions that would close encumbrances when a department exceeded budget. Prior to this enhancement, the system would prevent these encumbrances from closing even though the encumbrance was not required anymore. The DOF had to perform more manual work to close the encumbrance. With the enhancement, manual override is no longer needed lessening the risk of manual intervention.
- An audit log was created to clearly show who processed various stages of the approval process from creation to posting of the funds block transactions. These transactions are used by the DoF to prevent departments from

overspending budgets or if current resources are insufficient to fund current expenditures. The audit log aides in monitoring segregation of duty violations to prevent one user from having unmitigated control to create and remove a funds block.

- An enhancement was made to the Enterprise Asset Management (EAM) module by adding an additional status to work order master data. The accounting review status now requires the DoF review and approval prior to releasing work orders that affect either a capital infrastructure asset or a Work Breakdown Structure (WBS). The DoF now reviews the appropriateness of the use of the accounting and settlement parameters.
- The City established a new SAP managed warehouse at Public Utilities Environmental Monitoring Technical Services (EMTS) Division to replace an outdated system that did not integrate with City financials. The new system provided better financial reporting of inventory, increased visibility into what is physically on the shelf, as well as the ability to perform physical inventory counts. This implementation brought EMTS in line with a majority of the other utility run warehouses that already adopted these practices.
- A new transactional code was implemented in SAP to enhance the recording of donated or found assets. The transaction code allows employees to upload transactions with multiple assets from a spreadsheet. The enhancement also allows for validity checks of the transactions prior to upload into SAP. Prior to this enhancement the process was very manually intensive and prone to errors.

Along with system enhancements it is important for the City to stay current with the versions of the software that are used on a day-to-day basis. These updates add new features, improve security, fix known issues, and help protect integrity and confidentiality of data.

During 2020, various modules of ERP were updated or upgraded to more current versions including the following: Vendor Invoice Management for automated invoice processing, Budgeting and Planning for development of the City's annual budget, and Governance Risk and Compliance for risk identification and role provisioning.

Advances in technology allow the City to improve current business processes, create efficiencies and reduce errors and/or risks. The Office of the City Treasurer is replacing Quadrant, their over-the-counter cashiering system, with iPayment, a centralized payment processing system. The design of iPayment has been completed and its online payment functionality was implemented in October 2020. Residents and businesses can now pay business tax, rental tax, and utility (water and wastewater) fees online through the portal. Once the module is stabilized, further testing will be performed prior to the implementation of iPayment's cashiering functionality. It is expected that iPayment will be fully implemented by the end of fiscal year 2021 after the completion of the necessary tests.

In 2019, the DoF performed a preliminary assessment of iPayment based on system specifications to gain an understanding of potential internal financial control weaknesses and did not identify any deficiencies that could impact the financial statements.

The Human Resources Department has automated more processes, including automating personnel hiring forms that would affect posting of personnel costs to the system. In 2020, the unclassified offer letter process has been automated to achieve more efficiency and create a system control in its review and approval process. The transition to automation increases transparency with an audit trail and reduces segregation of duties risk with security roles.

The DoF staff did not find any significant deficiencies over ERP system related internal financial controls that could impact the financial statements. However, due to the interrelationship between SAP modules and third-party systems, there is a potential risk that changes to a module could impact others. There is also a potential risk that system errors are not identified through testing. To address these risks, the production changes are reviewed by a change control board before deployment and by affected business process coordinators after deployment. Any newly identified system errors are communicated for correction. Management identifies the significant financial risks that require additional monitoring.

Risks associated with system changes and SAP enhancements are also mitigated with training, feedback and question & answer workshops provided to end users before and after implementation. Additionally, users can access training videos which are readily available online via SuccessFactors, the City's learning management module. These training videos in SuccessFactors are also used in conjunction with the GRC Access Request Provisioning tool to automatically verify users have completed the appropriate training prior to being provisioned the related roles. Process documentation is also developed or updated as needed.

Information Technology Disaster Plans

The City contracted with Atos IT Solutions and Services to perform a Business Impact Analysis/Risk Assessment (BIA/RA) and the creation of a Disaster Recovery Plan (DRP) in order to identify risks to the organization, the impact to business operations and impact of the threats as well as to offer recommendations for remediation to building organizational resilience with the capability of an effective response that safeguards the interests of the City's key stakeholders, reputation, brand, and value-creating activities.

The objectives of the BIA were to identify all business functions, including applications with a financial reporting relationship, assign each function a recovery time objective, identify applications supporting those functions, assign application criticality based on the functions, present findings and recommendations for areas of risk, and to identify upstream and downstream dependencies.

The DRPs provide guidance for re-establishing information technology services within the established recovery time and recovery point objectives to ensure minimal downtime and data

loss. The plans are designed to address how the City will prepare for and subsequently recover from any unplanned interruption to the production operating environment at each of the City's data centers. The DRPs have been completed and should be released by the end of fiscal year 2021.

In addition, the City is in the final stages of implementing the cloud-based data management tool, Rubrik, in order to move to a cloud-based storage solution as well as provide additional security from ransomware and malware. The City has also selected a new managed service provider which will add a more robust program including tabletop exercises, ongoing validation of recovery, as well as adding an additional recovery site that can leverage the cloud for the City's highest priority, tier 1, applications.

Risks Identified through Internal Audit Function

The City Auditor conducts an annual citywide risk assessment in order to plan for audits based on the level of risk to the City. This is accomplished by identifying a scope of auditable units, surveying management, and analyzing management's response to formulate risk scores. From this risk assessment, an audit work plan is created outlining planned performance audits for a fiscal year.

In each performance audit, a variety of actions are taken by the City Auditor such as gaining an understanding of the process by obtaining and reviewing relevant background document, identifying its major threats, and understanding the mitigating controls that are in place to mitigate the threats. At the conclusion of an audit, the City Auditor will report the audit results which include findings and recommendations as it relates to the audit, and address this information to department management. This allows the department to be aware of and to efficiently and effectively address concerns that have an impact on accounting and financial reporting, safeguarding of City assets, and issues affecting the internal control environment. The DoF management participates in City Auditor audit entrance and exit meetings with City departments.

The DoF also participates in the remediation of performance and hotline audits if the City Auditor directs departments to work with the DoF's Internal Controls Section to document processes or strengthen internal controls.

A series of performance audit reports related to the City's Human Capital Management were released in April 2020 and November 2020. The City Auditor performed an evaluation in how the City monitors and communicates core metrics of its workforce and in how they monitor and address employee performance issues. The City Auditor provided recommendations and identified improvements in internal controls in the areas of compensation, employee performance reviews, and the City's rewards and recognition program. These recommendations would help the City better attract, develop, and retain competent employees to ensure high-quality services are provided to the public.

To address the findings in the report, City management agreed to auditor recommendations including creation of a total compensation strategy, improving the special salary adjustment process, reviewing and monitoring the employee performance review process and the Rewards and Recognition Program, and providing training for City employees. Human Resources also agreed to work with the DoF and City management to evaluate cap levels for employee discretionary leave and to update A.R. 95.91–Employee Rewards and Recognition Program accordingly. The DoF reviewed these reports and identified these as internal control deficiencies to the Control Environment component in the COSO management assessment template. However, the DoF does not believe these are major deficiencies that would affect the City’s system of internal controls.

In a performance audit related to the Development Services Department (DSD), the City Auditor made recommendations to improve the administration and billing of deposit accounts for development projects. DSD agreed to establish more formal written policies and procedures and plans to work with the DoF, the DoIT, and the Office of the City Treasurer to implement direct invoicing of deposit accounts within SAP per the City Auditor’s recommendation.

COVID-19 Pandemic Risk

The outbreak of the Coronavirus disease 2019 (COVID-19) has caused an ongoing pandemic and changed the external environment in unprecedented ways. Beginning in March 2020, the State, County, and City issued executive orders to contain and limit the spread of the respiratory virus. The orders included closure of certain businesses and facilities, practicing social distancing, and limiting non-essential activity. In response, the City implemented a series of safety measures to protect its workforce and the public from exposure including a shift towards employees working from home. This affected a significant population of the workforce including those with financial reporting responsibilities.

Employees can face potential challenges especially when the shift to telework is sudden as was the case with the pandemic. Issues such as communication problems, inadequate technology or technology protocols, and lack of oversight can arise. In aggregate, these issues can lead to employees circumventing standard operating procedures and a breakdown in controls. To mitigate this risk exposure, the City implemented several controls as described in *Control Activities* later in the report.

During the pandemic, the City observed an increase in cyber fraud attempts. These include social engineering attacks or invoice fraud and other attacks that can cost substantial amounts of cash when the budget is already stressed. Cyber criminals are more likely to take advantage of an organization when their operations have been disrupted or the focus from leadership is on other pandemic response issues.

Other notable changes that required a risk assessment were impacts of new expenses and funding sources related to the pandemic. The City created the Small Business Relief Fund to assist businesses impacted by COVID-19 retain employees and sustain continuity of operations. Due to volume of applications, there would be a greater risk of fraud opportunities.

Management assessed and implemented controls to limit fraud risk while expediting payments.

The City also received \$248 million in federal direct payment from the Department of Treasury's Coronavirus Relief Fund (CRF), under the Coronavirus Aid, Relief, and Economic Security Act ("CARES Act") to use for COVID-19 related expenditures. The CRF is subject to the Single Audit Act 2 C.F.R. Part 200, Subpart F regarding audit requirements that apply to any non-federal entity. The DoF and Chief Compliance Officer have been tasked with working with departments to track, identify, review and approve eligible expenses to be reimbursed from the CRF. Appointing Authorities from each department have to certify that all expenses are allowable under the CARES Act and maintain all applicable documentation.

3. Control Activities

Control activities are the next step in response to risks identified through management's risk assessment. COSO defines *control activities* as the actions established through policies and procedures that help ensure that management's directives to mitigate risks are carried out. In the preparation of financial reports for external use, these are the policies and procedures, with embedded controls, that management develops and implements to mitigate risks of errors and omissions that could affect the reliability of the information presented in the reports. It also includes controls embedded within the City's ERP system.

Budgetary Control

The City adopts an annual budget authorizing the expenditure of funds based on current financial resources. Budgetary control and monitoring are fundamental elements of a government's system of internal controls.

In accordance with budgeting best practices, the City maintains a Budget Policy, CP 000-02, to guide the creation of the City's budget and outline standards for revenue generation and execution of operating and capital budget expenditures as recommended by GFOA (Government Finance Officers Association) and NACSLB (National Advisory Council on State and Local Budgeting).

Through the budget preparation process, management estimates annual revenues providing a basis for evaluating actual revenue as it is recorded during the fiscal year. Similarly, expenditures are monitored against those expenditure levels authorized in the budget. For the City, budgetary control is exercised at the department level for the General Fund and at the fund level for all other funds. In addition, the budget authorized for personnel expenditures (salaries and wages) for a fund or department may not be used for non-personnel expenditures. The City's financial system incorporates embedded controls in which non-personnel expenditures cannot be incurred if a budget appropriation is not available. The City also uses an encumbrance system of accounting as a mechanism to accomplish effective budgetary control. The budget and accounting structure that SAP maintains for expenditure control has the added benefit of ensuring that expenditures are properly categorized in the

Comprehensive Annual Financial Report by function. For example, expenditures charged against the Police department's budget will be reported as "Public Safety Expense" in the Comprehensive Annual Financial Report, with very low risk of misclassification.

Transaction Control Activities

The implementation of SAP provides the foundation for a well-designed internal control framework. SAP allows internal controls to be embedded in the system through restricted access, segregation of duties, and authorization workflows. These controls allow for review, validation, and approval of transactions, not only mitigating the risk of fraud but also preventing transaction errors or instances of non-compliance with laws and regulations.

The majority of user interactions within SAP occur in various departments as they perform their core responsibilities. Often transaction workflows are processed across multiple departments in order to properly segregate duties and mitigate the risk of fraud. For example, the DoF processes employee payroll, but only the Personnel department can change an employee's hourly compensation rate in SAP. Other transactions include vendor payments, generation of City invoices, cash deposits, payroll transactions, and journal entries, most of which segregate the creator of the transaction from the approver. These interactions make their way into the financial system either through direct input or through some type of interface application. The City's financial activity is consolidated with similar types of activities and is eventually presented in the Comprehensive Annual Financial Report and other financial reports.

Over the years, the City has implemented a variety of control activities over financial transactions. Where automated controls are not available, manual controls are used. These control activities ensure that the financial information is complete, accurate and valid. Below are some of the control activities embedded in the City's multiple accounting and financial reporting processes:

- Authorizations and approvals that affirm that a transaction is valid, such as the approval of a journal entry or an invoice payment;
- Verifications - comparing two or more items with each other, such as comparing goods received against a purchase order;
- Physical controls, such as comparing fixed asset inventories against control records;
- Reconciliations - comparing two data elements and taking action when differences are identified to bring the data into agreement, such as reconciling bank accounts to the general ledger;
- Supervisory controls that assess whether other transaction control activities are being performed completely, accurately and in accordance with policy; and

- Application Controls are those related to procedures to check the accuracy of the output data, including follow-up on exceptions. The functional analysts in the DoIT and the business process coordinators in City departments validate and approve any functional changes in the SAP system. Security related changes are also reviewed by the DoF's Internal Controls Section. The DoIT's Control Change Board reviews documentation, testing, and approvals before implementing the changes in production.

Internal Controls Section

The Internal Controls Section of the DoF provides dedicated staff focused on maintaining and enhancing the City's control environment. The Internal Controls Section is involved with the implementation or monitoring of new software and reviews the system implementation for process gaps, control weaknesses, segregation of duties, system access, data transfer to SAP, and the development of process narrative documentation. The Internal Controls Section also manages and oversees several post-monitoring reviews that are designed to enhance a process' internal financial control and ensures that reviews are performed in a timely manner as described in the *Monitoring Activities* section. Some of these monitoring programs are results of audit findings and recommendations management agreed to perform to prevent occurrences of fraud, misuse, or abuse.

Control Activities Deployed through Policies and Procedures

Management incorporates controls into financial reporting activities by establishing clear accounting policies and developing and implementing accounting procedures. Policies reflect management's statements of what should be done, guiding the actions of staff. Procedures consist of actions that implement a policy. Having policies, procedures and controls is key to preventing and detecting material errors and fraud. It is essential that policies are current, formally documented, and easily accessible to all employees. The following list highlights core policies that drive prudent fiscal planning and actions.

- The investment activities for the City Treasurer's Pooled Investment fund are governed by the City Treasurer's Investment Policy, which is based on California Government Code 53601 with additional constraints added by staff. The Investment Policy is reviewed by the Investments team, the City Treasurer, the City Treasurer's Investment Advisory Committee and then presented annually to the City Council for approval. The Investment Policy for calendar year 2021 was adopted by City Council in November 2020 and is posted on the City Treasurer's website.
- The City adopted a Debt Policy in November 2007, which was last amended by the City Council in May 2019. The Policy documents the procedures and goals for the use of various debt instruments to finance City needs and the sound management of existing debt obligations. A biennial review of the Debt Policy is performed, and changes are forwarded to City Council for consideration and approval. A new review of the policy should be performed in 2021.

- The City adopted a Reserve Policy, Council Policy 100-20, in October 2002, which was last amended by City Council on June 22, 2018. The Policy defines the City's reserves and sets policy targets for reserves across City operations, including General Fund, risk management and enterprise operations. These reserves help provide for strong fiscal management and mitigate financial risk.
- User fees are charged for services provided to residents and businesses in the City as a result of public need. Abiding by the standards and best practice guidelines established by GFOA and NACSLB, the City has formed a User Fees Policy, Council Policy 100-05, to identify factors to be considered in calculating the full cost of services in order to appropriately set fees.

These policies, in combination with the Budget Policy, Council Policy 000-02, lower the financial risk and help the City maintain compliance with laws and regulations which could materially affect reporting of liabilities.

In 2016, the Human Resources department initiated citywide efforts to update existing A.R.s and Department Instructions (D.I.)'s as an additional method to strengthen the control environment. This effort continued in 2019, with the responsibility transferred to the Deputy Chief Operating Officers for their respective departments for greater oversight. The A.R.s and D.I.s direct administrative policies and procedures of a continuing nature. It is important that policies as documented reflect the actual processes. The City's effort to update all A.R.s began with the revision of A.R. 1.00-Administrative Regulation and Department Instruction Preparation Procedures, which added the involvement of the Internal Controls Section to all future revisions of A.R.s or D.I.s.

Additionally, an internal review of the A.R. process, and the City's policy and documentation procedures overall, was conducted by the former Assistant Chief Operating Officer (ACOO), in order to identify issues and bring consistency to the City's governing documentation practices. The ACOO identified an inconsistent focus on policy or procedures, the use of unfriendly language and terminology, no clear delineation between the issuance of an A.R., process narrative, council policy, or other governing document, along with a cumbersome review process. To alleviate these concerns, several recommendations were made including distinguishing A.R.s between Administrative Policies and Administrative Procedures and converting existing A.R.s accordingly, streamlining the process to create, update, and review Administrative Policies and Procedures, and to establish roles, responsibilities, and definitions to better manage the issuance of governing documentation.

The City currently has over 100 documented A.R.s. Approximately 67 of these have been created or revised since the Citywide effort was initiated in 2016. During calendar year 2020 there were two (2) A.R.s that were revised, including A.R. 96.20-City Policy for People with Disabilities, and A.R. 90.66-Mobile Device Policy. The delay of additional documentation is a result of the ongoing pandemic.

The Internal Controls Section reviews and approves policies and procedures included in the A.R.s to ensure internal finance controls exist to mitigate risks and improve efficiency. Published A.R.s are utilized as a guide and standard in ensuring that City processes comply to the stated requirements. Though it is an ongoing effort, the Internal Controls Section ensures that if policies and procedures have been added or revised, control activities are also modified to enhance the current process and continued compliance.

The DoF continues to focus on formally documenting policies and procedures related to accounting and financial reporting. Most of these policies and procedures have been long-standing practice and are consistently applied each fiscal year. This allows the City to have a formal inventory of procedures and related controls that can be systematically monitored for effectiveness and continued relevance. The DoF has formally documented 716 processes and continuously assesses the need for further documentation. In calendar year 2020, the DoF documented 61 processes and will continue efforts in the current year.

COVID-19 Pandemic Response

The City created new policies and procedures for employees affected by COVID-19, instituted new workplace sanitation protocols, required departments implement additional safety measures to counteract spread, and offered new guidance for teleworking during the pandemic. To limit exposure and allow employees to continue to work, many employees including those with financial reporting responsibilities shifted to a telework schedule. While this limited the exposure to COVID-19 in the workplace, the risk exposure to employees not following standard operating procedures increased. Employees faced potential challenges communicating to other employees, lack of oversight, and breakdown of proper review and approval.

To mitigate the risks associated with having a large remote workforce, the City expanded telework resources by offering additional software to facilitate document-sharing and collaboration between employees and across departments such as Microsoft Teams and Zoom. Greater adoption of electronic signatures and electronic form routing were also observed as departments sought to maintain approvals while isolated at home or in the office. Timesheet submission and approval for classified employees from mobile devices was enabled ensuring employees are paid timely while working remotely. The City also procured additional remote access licenses to allow more employees to securely access shared drives, the City's ERP system, and other applications used by various City departments.

In early 2020, City management requested departments update department-specific contingency plans to maintain essential services in the event of limited staffing. These plans were known as Continuation of Operations Plans or COOPs which could be triggered in the event staff was unavailable due to COVID-19 or city facilities closed to the public.

As the pandemic progressed, departments submitted a significant number of system role assignment requests during the shift to telecommuting which equated to higher potential for unauthorized access. This was most likely due to the transition to telecommuting when some employees were resolving technical issues with system access at home and other employees

backfilled temporarily. The City maintained segregation of duties through established system controls that were in effect when City staff requested conflicting roles. This reiterates the importance of having a strong foundation of control activities.

Management also identified an increase in cyber fraud attempts. To counteract this increased risk, the DoF reviewed and enhanced the electronic fund transfer (EFT) enrollment process by adding a second verification process from a supervisor, removing the EFT form from the City's public facing website, and revising process documentation to reflect the changes to the process. The City also continues to annually provide mandatory training to all city employees on detection and prevention of cyber security threats such as phishing and social engineering scams.

Non-purchase order invoice activity increased by approximately 23% compared to the prior year due in large part to payments from the Small Business Relief Fund or SBRF Program for businesses impacted by COVID-19. The City worked expeditiously to create thousands of payee accounts and process payments to distribute \$17 million in SBRF funds while maintaining adequate controls to ensure payments were made to authorized businesses. Additional controls implemented were verification of valid business license and multiple approval layers for reviewing eligibility.

When City employees started working remotely, the City observed a rise in mobile device usage for City email and other common City processes. The Department of IT (DoIT) deployed a Mobile Data Management (MDM) system with Microsoft Endpoint Manager. The MDM system provides the services and tools to closely manage and monitor City mobile devices while further securing City data. The City provided licenses as well as registration and installment resources to all City employees with Apple and Android devices. The rollout of the MDM system coincides with the recent, January 2020, release of A.R. 90.66-Mobile Device Security, which establishes rules that govern the use of smartphones, tablets, and other mobile devices used for City of San Diego business. The A.R. also serves to protect the confidentiality and integrity of data and applications, the mobile devices and the data residing on them, as well as maintain continuity of the services that the City provides.

Towards the end of 2020, the City purchased and began distributing additional laptops and other workstation-related hardware with federal CARES Act funding to accommodate more employees and expand the workforce that could work from home.

4. Information and Communication

The Information and Communication component of the COSO framework supports the functioning of all components of internal control. COSO defines *communication* as the continual iterative process of providing, sharing and obtaining necessary information. In an organization as large as the City, it is critical that management establishes effective communication procedures to meet accounting and disclosure requirements under governmental accounting standards and under state and federal securities laws.

Formal Communication Processes

The City has formal communication processes to ensure relevant information is communicated effectively to those responsible for preparing the Comprehensive Annual Financial Report. The DPWG includes individuals in key City positions within the City and external counsel that can review disclosures, communicate known facts and other relevant information and ensure consistency throughout the City's financial disclosure documents. The DPWG has formal disclosure controls and procedures that define roles and responsibilities over the development and review of financial disclosures. These controls and procedures require that the City's Chief Financial Officer certify to the City Council that the City's financial statements included in the Comprehensive Annual Financial Report are fairly presented and that disclosures are true and complete. Similarly, department directors are required to also certify that contributions made by their staff are accurate and complete.

While the DPWG is responsible for ensuring that disclosures comply with federal and state securities laws, the DoF is responsible for ensuring financial statements and related disclosures are prepared in accordance with GAAP. The DoF relies on a formal distribution of work document that clearly communicates specific responsibilities for development of the Comprehensive Annual Financial Report, including who is responsible for preparing and reviewing the relevant sections of the report. During the preparation of the 2020 Comprehensive Annual Financial Report, the DPWG participated in the review of the report drafts. The DPWG reviewed and signed off on the disclosures included in the Comprehensive Annual Financial Report, including the Letter of Transmittal, Management's Discussion and Analysis, and Notes to the Basic Financial Statements.

The DPWG ensures the City's financial disclosures related to the public offering and sale of securities is accurate. The City prepares a Preliminary Official Statement (POS) that contains all material information provided to investors to help determine whether to purchase securities offered by the City. It is later referred to as an Official Statement once the security is sold. The DPWG reviews the statements before City Council approval of a public debt issuance and its related disclosure document. The City also conducts presentations with ratings agencies prior to marketing new securities. The DPWG is required to review all materials that the City presents to credit rating agencies and investors.

Pursuant to §22.4107 of the SDMC, DPWG is required to perform an annual evaluation of the City's disclosure controls and procedures. The results of DPWG's work and findings are to be presented to the City Council by January 31 of each year formally communicating any deficiencies.

During the audits of the Comprehensive Annual Financial Report and other financial reports, the external audit firm requests a broad range of supporting documents. The multiple items requested are managed through a master pending list. This allows for effective communication with the external auditor, as items are clearly assigned to relevant staff and tracked by management throughout the audit process.

The DoF uses a Financial Statement Checklist to assist in the preparation and review of the fund level financial statements. This helps to communicate expectations and ensures that statements are complete and accurate. The Supervisor can then review staff work against a standard set of expectations. In addition, the DoF relies on a comprehensive accounting and disclosure checklist developed by GFOA. Each question in the checklist is assigned to a staff member within the DoF based on area of responsibility. This allows for a clear and objective way to ensure compliance with existing governmental accounting standards.

Financial Reporting Tools

The DoF continues to work with the DoIT to develop and implement new financial reporting tools for citywide use through business intelligence reporting software that allows users to perform ad-hoc queries and efficiently access financial data stored in SAP. Information is useful when it is timely, accurate, and appropriate to the user. The following reporting tools were developed and published by the DoIT and finance branch departments in calendar year 2020:

- **Fund Certification Report:** A citywide report that was developed as an additional method to certify funds to help remain in compliance with Charter Section 39 that states “No contract, agreement, or other obligation for the expenditure of public funds shall be entered into by any officer of the City and no such contract shall be valid unless the Chief Financial Officer shall certify in writing that the money required for such contract, agreement, or obligation for such year is or will be in the treasury...” and Charter Section 80 which states “sufficient funds are or will be available in the City treasury to make such expenditures...”
- Developed in the later part of 2018, the AP Dashboard provides various information on Accounts Payable invoices, goods receipts and goods returns for a specific department. The dashboard provides a listing of outstanding invoices, goods receipts and goods return that require further processing by the department. It also provides historical statistics on invoice processing. During 2020, the AP Dashboard was modified to provide for improved monitoring and visibility to the vendor payment process and to the receipt of goods and services for department managers.
- The Human Resources (HR) Turnover Dashboard provides a real-time overview of turnover data in the organization along with trend tables, employee separations, and turnover percentages. Also developed in 2020, the HR Position Details Dashboard provides a real-time overview of position data. The dashboard has a combination of trend tables and counts of total position, vacant positions, filled positions, and vacancy data. It also displays a summary of positions, full-time equivalents, vacancies, and detailed data for individual positions.

In addition to the aforementioned reports, which were developed primarily for citywide use, multiple reporting tools were developed for specific departments or programs within the City

during 2020. These reporting tools are developed to meet the needs of the individual department or program rather than the City as a whole. Approximately 40 different reports were created during this time for various purposes including infrastructure asset management, supply chain management, human capital management, and finance.

Many SAP related initiatives were completed by the DoIT in calendar year 2020, including 44 SAP training videos, and approximately 8,251 SAP training instances including classroom and online courses.

Financial Training

The DoF coordinates two citywide financial training classes, a one-day class designed for newer city employees called Finance Orientation, and a multi-day class designed for seasoned employees called Finance Academy. Beginning 2020, the two classes transitioned to a virtual training allowing employees to continue attending while minimizing exposure to COVID-19 in the workplace. Subject matter experts representing various departments collaborated on these accelerated learning programs to strengthen core financial competencies of key individuals through a variety of lessons. Each topic focused on the latest government practices and processes in place to strengthen internal controls and improve financial reporting for the City. Additionally, the DoF provides other annual financial training, on topics such as disbursements and budgeting, to other City departments to keep staff current on the latest procedures.

5. Monitoring Activities

An effective internal control program requires continuous evaluation of each of the five COSO components to ensure that they are functioning effectively. This includes assessing whether risks are identified timely and control activities address identified risks. Management should evaluate whether controls are performed completely, accurately and in accordance with policy.

It also includes assessing whether information is communicated effectively to ensure disclosures are accurate and complete and that accounting policies and procedures are clearly understood by relevant staff.

Review of Independent Audits

As part of its monitoring activities, the DoF reviews the results of independent audits to identify potential areas of risk or areas for which controls need to be strengthened. External auditors are required by auditing standards to communicate to the appropriate governing body any material adjustments identified through the audit of the City's financial statements. For the audit of the fiscal year 2020 Comprehensive Annual Financial Report, there were no material adjustments identified by the external auditors. In addition, no material weaknesses or significant deficiencies in internal control over financial reporting were identified in the *Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government*

Auditing Standards, dated December 21, 2020 (see Attachment 4). The audit of the financial statements is not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. However, the audit process does require significant interaction between the audit team and management with a sustained communication effort throughout the process that allows for effective monitoring of controls over accounting and financial reporting.

The DoF also conducts an internal review of the preparation and completion of the Comprehensive Annual Financial Report to identify entries that occurred after the draft was submitted to the external auditor. This allows the DoF to identify potential areas of risk and implement controls to continuously improve the Comprehensive Annual Financial Report preparation process.

During the fiscal year 2019 Comprehensive Annual Financial Report preparation process, the DoF discovered that the amounts reported in specific classifications of *Net Position* in the *Statement of Net Position* for the fiscal year 2018 Comprehensive Annual Financial Report were not accurately categorized. Specifically, *Restricted Net Position in Governmental Activities* was understated by \$204 million and *Unrestricted Net Position in Governmental Activities* was overstated by the same amount. The *Total Net Position* was correct as reported. Once this deficiency was identified, the DoF took immediate steps to notify the City's external audit firm, outside disclosure counsel, and Audit Committee of the finding and corrective actions.

To address this risk, the DoF implemented the following enhancements to internal controls during 2020:

1. Develop a formal materiality threshold policy for financial statement transactions. Those transactions that meet specific materiality thresholds will require additional levels of review and approval from senior staff.
2. Perform risk-based assessment over complex accounting transactions. High risk transactions will require additional levels of review and approval from senior staff. This process is outlined in the materiality policy.
3. A new process narrative will be developed specifically addressing Bond Refunding transactions, including sample entries, additional levels of review and approval by the Financial Operations Manager and Assistant Director responsible for the Comprehensive Annual Financial Report. These fund level entries will be prepared when the issuance occurs, avoiding the lag time of many months until year-end when all conversion entries are performed.
4. Create a special fund to account for Government-wide Financial Statement balances and activity. Conversion entries will be recorded in SAP with formal approval in the system of record, including proper documentation supporting the transaction. Currently, conversion entries are prepared in an excel spreadsheet.

5. Reorganization of the Comprehensive Annual Financial Report Team. The report creation responsibilities will be concentrated within a core team.
6. Formalization of analytical review process. All variances over specific materiality thresholds will be formally documented with appropriate supporting documentation. Review and approval will be required by senior DoF staff. This process is outlined in the materiality policy.
7. Current training policy requires 40 hours of continuing education for accounting staff. Formal training specific to conversion entry process for relevant staff will be included in the annual training.

Each of these corrective actions was implemented before the start of the FY 2020 Comprehensive Annual Financial Report. The process narrative regarding the review of debt issuances and related journal entries, which include bond refunding transactions, was incorporated into the newly created materiality policy. These controls will continue to be in place for future fiscal years to ensure the City maintains adequate controls over financial reporting.

The DoF's Internal Controls Section reviews and monitors the results of audits performed by the City Auditor that directly or indirectly impact the financial reporting functionality and IT role access of the City. The Internal Controls Section monitors recommendations that impact internal controls and works closely with departments, as needed, to document or modify business processes, establish new controls, and strengthen existing controls. The audits are tracked to ensure that new or existing processes are documented and updated, respectively, and for timely remediation of internal control deficiencies.

Monitoring through GFOA Certificate Process

The City received the Certificate of Achievement for Excellence in Financial Reporting awarded by GFOA for the fiscal year 2019 Comprehensive Annual Financial Report. To receive this award, the City must comply with a comprehensive checklist that incorporates accounting and disclosure requirements in accordance with GAAP. Comments received from GFOA on the submittal of the Comprehensive Annual Financial Report also serve as a monitoring tool to ensure controls are effective. If GFOA identifies significant deficiencies in the report, they disqualify it from the Certificate of Achievement for Excellence in Financial Reporting award. The review of the fiscal year 2019 Comprehensive Annual Financial Report resulted in six comments and suggestions for improvements on presentation. The City responded to all comments and suggestions and two changes were incorporated in the fiscal year 2020 Comprehensive Annual Financial Report. The City anticipates receiving the award for the fiscal year 2020 Comprehensive Annual Financial Report.

In calendar year 2020, the City was awarded two certificates for its budget document: the Distinguished Budget Presentation Award (Budget Award) for exemplary budgeting practices by GFOA for the City's Fiscal Year 2021 Adopted Budget and the California Society of Municipal Finance Officer's Operating Budget Excellence Award. The Distinguished Budget Presentation

Award program was established in 1984 to assist state and local governments in preparing budget documents of the highest quality that reflect both the guidelines established by NACSLB and GFOA's best practices on budgeting, and to individually recognize governmental entities that succeed in achieving that goal. Reviews are conducted by selected members of GFOA professional staff and by outside reviewers with experience in public-sector budgeting, and feedback and comments received by the City are used to improve future year budgets.

Segregation of Duties Monitoring

The DoF continues to monitor for segregation of duties to ensure that no one individual has control over an entire process or multiple components of a process, which if abused, could cause harm to the City or result in misstatements in the financial statements. Due to the importance of maintaining controls around segregation of duties, continuous monitoring is performed. To assist users in selecting the proper roles and avoiding possible segregation of duty violations, the DoF and the DoIT have continued the annual review and update of a Role Definition Guide. The Role Definition Guide identifies and defines all available SAP roles and lists possible segregation of duty violations. The DoF works with the appropriate business process coordinators in departments to ensure the information is correct and updated.

The Internal Controls Section reviews and assesses existing and new risks that are introduced to the City's processes, along with the mitigating controls that are in place, and updates the information in GRC when deemed appropriate. This ensures the system controls are accurate, updated, and consistent with the City's actual process. In addition, the Section facilitates security role updates annually, and monitors activities performed at the transactional level either daily, monthly, or quarterly depending on the test. Automated testing is developed within GRC and the results are sent to the process owner for review and remediation where necessary.

The DoIT also continues to deploy the Business Role Management (BRM) concept to more business processes within the GRC Access Request Provisioning tool by transitioning most production systems' single roles to business roles in calendar year 2020. The BRM concept is a grouping of roles based on job tasks, which helps streamline and better manage changes to roles' access. The Internal Controls Section also provides independent monitoring of privileged user activities to assess whether these accounts are sufficiently controlled and comply with the DoIT's policies and procedures. The next expected enhancement is the expansion of the BRM concept for all production systems within the GRC Access Request Provisioning tool.

Assessment of Documented Processes and Controls

A key part of maintaining a strong internal control system is the periodic evaluation and monitoring of processes and their embedded controls. Process design assessments have been developed in the GRC module with the objective of testing the validity, accuracy, and performance of the process as documented. Control design assessments have also been developed to test the presence and performance of controls that have been identified in the process.

In calendar year 2020, the Internal Controls Section implemented a risk-based approach to assess the risks of material misstatement occurring in the financial statement within a documented process by measuring its inherent and control risk. Inherent risk refers to the susceptibility of an account balance or class of transactions to material misstatement, before consideration of any related controls. Control risk refers to the risk that the system of internal controls will fail to prevent or detect material misstatements on a timely basis by the controls described in the process documentation. The Internal Controls Section uses the designed risk-based approach to prioritize and select process documentations for the periodic assessments. For calendar year 2020, process design assessments and control design assessments were delivered within GRC to the respective process owners which include significant processes with financial reporting impacts.

The purpose of the assessments is to ensure documented processes are current and accurate and the predefined controls within a process are valid. The assessments identify processes that require changes to the documented process itself or to the related controls and the Internal Controls Section notifies process owners of the necessary revisions in a timely manner. As the nature of business processes may pertain to more than one department or personnel, it is critical that process documents are updated and re-uploaded to the City's intranet, CityNet, for all City employees to access.

Ongoing Monitoring

The DoF periodically evaluates the effectiveness of controls of transactional activities that are deemed significant by management. Monitoring of controls also includes considering whether the controls are operating as intended and that they are revised as appropriate for changes in the organization.

Several post-processing transactional monitoring activities have been established over the past few years. The following summarizes each monitoring activity:

Procurement Card Program (P-Card)

The Internal Controls Section developed a formal methodology for selecting departments, P-Card holders and transactions to review. At the beginning of each fiscal year, a review test cycle is created based on established criteria to ensure that all departments are reviewed at least once per fiscal year. The Internal Controls Section also primarily focuses on capturing the new P-Card holders who have not been tested, if applicable. On a monthly basis, the Internal Controls Section randomly selects transactions to review and schedules a manual test in GRC. Areas that are considered high-risk are reviewed more than once in a year. Under the supervision of the P-Card Administrator, the Assistant P-Card Administrator reviews these transactions for proper authorization, completeness, accuracy, validity, and compliance to ensure that the P-Card holders adhere to the City's policies and procedures. The Internal Controls Section monitors for timely completion of the review within the allotted time.

Findings are recorded in a summary log and provided to the P-Card Administrator monthly. Corrective actions are taken by the P-Card Administrator when findings are identified.

Aging Goods Receipts

The DoF developed and updated procedures for departments to review aging Goods Receipts (GR) without a corresponding invoice, or the GR and Invoice Receipts quantities do not match. If left unaddressed, this can result in expenses that are overstated leading to inaccurate financial reporting in the City's financial statements. Beginning in June 2020, the DoF started conducting monthly reviews of outstanding GRs and communications are sent to the departments to review and reverse any GRs that are no longer needed. A count of outstanding GRs are also sent to department managers on a monthly basis to provide better visibility and oversight.

Grant Accounts Receivable Invoices

The Internal Controls Section developed a monitoring test to review grant related accounts receivable (AR) invoices for segregation of duties violations. The DoF identified a segregation of duties issue that allows certain users to both create and post grant AR invoices. Due to most users being grant administrators across multiple departments, removing the roles will negatively impact these administrators and prevent them from continuing their job responsibilities. This detective test is performed on a monthly basis to determine if users who posted AR grant customer invoices and customer credit memos have committed a segregation of duties violation. The monitoring review provides reasonable assurance that invoices posted in SAP are in compliance with City's policies and procedures.

Journal Entries

The Internal Controls Section developed a monitoring test to review journal entries for segregation of duties violations. The DoF finance analysts are given access to submit and post journal entries to record financial transactions in the system. Finance analysts assist in reviewing and posting submitted journal entries made by departments citywide. Finance analysts may need to submit journal entries for a department, but reviewing and posting journal entries should be delegated to another department finance analyst. Submitting and posting by one City employee is a violation of segregation of duties and creates a potential for financial misstatements and/or fraud. The monitoring test is designed so that a supervising finance analyst reviews the finance analyst's journal entries to ensure that the City has proper internal controls over the submission and posting of journal entries. Another separate supervising monitoring test is designed to review the supervising finance analyst's journal entries to ensure proper internal controls over submission and posting of journal entries.

Travel and Tuition Reimbursements

The Internal Controls Section developed a monitoring test for travel and tuition reimbursements, and made minor enhancements in 2020 to ensure testing specifications continue to cover conditions set forth by the respective A.R.s. A random selection of travel and

tuition reimbursements are chosen to maintain impartiality. The sampling methodology also considers testing the majority of departments at least once within the calendar year. A tracking log is created each calendar year and accompanies the monitoring test to help the Internal Controls Section achieve this objective. Every two pay periods, the test is performed to review for accuracy, completeness, proper authorization, validity, and cutoff (reimbursements were made in the pay periods being reviewed). The monitoring review provides assurance that reimbursements comply and adhere to City's policies and procedures.

Jury Duty Leave

The Internal Controls Section developed a monitoring test with the objective of strengthening monitoring over paid time off for jury duty and ensuring compliance with the City's policies and procedures. In calendar year 2020, the Internal Controls and Payroll Sections reassessed the monitoring test's scheduling frequency and sampling methodology to ensure required court leave supporting documentation is submitted by City employees in a timely manner. Remediation plans were documented to assist in situations when a City employee did not comply with policies and procedures. The Internal Controls Section also contributed in updating requirements and procedures for paid leave for jury duty in the HR Quick Reference Guide, which was internally sent out to departments. The test is scheduled and performed every two pay periods and City employees are randomly selected. The DoF performs a review for accuracy, completeness, proper authorization, validity, and compliance with the Personnel Manual. The Internal Controls Section schedules a manual test in the SAP GRC module and monitors for timely completion of the review within the allotted time. Corrective actions by the Payroll Section of the DoF are taken when findings are identified.

Accounts Payable

The Internal Controls Section developed a daily monitoring review of invoices passing through the VIM system to ensure accuracy and compliance with the City's Accounts Payable procedures. The Internal Controls Section is responsible for obtaining a list of purchase order invoices that were posted daily in VIM and selecting invoices for review using a risk-based sampling methodology. The selections are forwarded to the Disbursement Section in the DoF to conduct the review prior to the daily payment run. In calendar year 2020, the Internal Controls Section reformatted the monitoring test to standardize reasons for failure and tracking remediation plans. Additionally, there was an increase in fraud attempts involving electronic banking changes as a result of the pandemic. As a result, the Internal Controls Section is in the process of creating a monitoring test to verify electronic banking changes requested by vendors are processed as intended.

Purchasing & Contracting (P&C)

The Internal Controls Section developed manual and semi-automated monitoring tests in GRC with the objective of improving monitoring, compliance, and contract surveillance of citywide contracts with the assistance of P&C. On a monthly and quarterly basis, the Internal Controls Section is responsible for scheduling monitoring for P&C to conduct the review, based on a

formal methodology and control focus. The purpose of these monitoring reviews is to (1) ensure threshold limits are not bypassed by the splitting of purchase orders; (2) check for expired insurance policies linked to current vendors; and (3) ensure that engaged vendors are licensed to perform business within the City. SAP is utilized to pull data, and if applicable, deficiencies are flagged for review. In calendar year 2020, the Internal Controls Section collaborated with P&C to modify these tests. The monitoring review test for purchase order splitting was redesigned with a new methodology and test questions. Full completion of the redesign and scheduling testing in GRC is expected by the end of March 2021. The monitoring review test to check for expired insurance policies was discontinued in 2020 and will be replaced with a new report created by P&C that will continue to monitor for expired insurance policies. The Internal Controls Section plans to conduct a periodic review of the new report to ensure proper internal controls are in place.

Conclusion

With the onset of the COVID-19 pandemic, the City has faced additional internal control challenges including transitioning to a remote environment, the increased likelihood and opportunity for fraud, and circumvention of controls resulting from the lack of direct supervision. In response, the City has reevaluated the control processes and assessed the risk that comes with the changing environment. To counter these challenges, the City provided additional resources and implemented additional systems to ensure continued effectiveness. In addition, the City's management has maintained strong and active communication with employees during the pandemic.

The City has established a high bar for the development of a comprehensive internal control program for a municipal government. Based on management's evaluation, the internal controls over financial reporting are effective. The City's internal controls over financial reporting are adequate with the system-embedded preventative and detective controls, combined with the numerous documented processes and controls currently in place, allow for the production of reliable financial information.

Establishing effective internal controls is a continuous process. The implementation of effective internal controls reduces the exposure to error, fraud, and theft. It is management's responsibility to design, implement, and maintain internal controls and consider the areas of risk. Implementation of effective policies and procedures can prevent, detect, and correct errors and fraud before they affect the financial statements. The DoF continues to develop written policies to document and confirm existing internal financial controls and continues to work with City departments in documenting processes and new system implementations. Management actively assesses risk as the organization changes and as new reporting requirements are issued. As with any effective system of internal controls over financial reporting, management responds to newly identified risks by implementing or enhancing controls to mitigate such risks, including those that have been identified in this report.

Sources

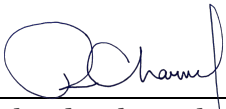
1. Gauthier, Stephen J. *Evaluating Internal Controls*. Chicago IL: Government Finance Officers Association of the United States and Canada, 2013. Print
2. Committee of Sponsoring Organizations of the Treadway Commission, *Internal Control – Integrated Framework, Framework and Appendices*, 2013
3. Committee of Sponsoring Organizations of the Treadway Commission, *Internal Control – Integrated Framework, Internal Control over External Financial Reporting: A compendium of Approaches and Examples*, 2013
4. Committee of Sponsoring Organizations of the Treadway Commission, *Participant Manual*, 2015

Attachments:

1. Certification by the Mayor and Chief Financial Officer
2. Management Evaluation Assessment Template
3. COSO Internal Control- Integrated Frameworks Principles
4. Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards



Matthew Vespi, Chief Financial Officer



Rolando Charvel, Director and City Comptroller, Department of Finance

CERTIFICATION BY MAYOR AND CHIEF FINANCIAL OFFICER

In accordance with the requirements of § 22.0706 of the San Diego Municipal Code, the Mayor's designee, the Chief Operating Officer and the Chief Financial Officer hereby certify that they:

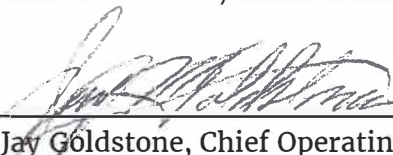
1. are responsible for establishing and maintaining the City's internal financial controls;
2. have identified the need to design such internal financial controls to ensure that material information relating to the City and its departments, offices, agencies, and affiliated "related entities" as defined in San Diego Municipal Code section 22.4102, 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 120 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 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: 
 Matthew Vespi, Chief Financial Officer

Date: 2/25/2021

Signed: 
 Rolando Charvel, Director and City Comptroller, Department of Finance

Date: 2/25/2021

Signed: 
 Jay Goldstone, Chief Operating Officer

Date: 2/25/2021

Introduction

The Committee of Sponsoring Organizations of the Treadway Commission (COSO) has issued the updated *Internal Control—Integrated Framework (Framework)* and a companion document: *Internal Control over Financial Reporting – Illustrative Tools for Assessing Effectiveness of a System of Internal Control (Illustrative Tools)*. It is expected that organizations will customize the templates presented in the *Illustrative Tools* to match the facts and circumstances in their particular organizations. To help organizations customize the templates for their assessment process and organization, this file is an extract of only the blank templates from the *Illustrative Tools*.

The form and use of the templates are explained in the Introduction to the *Illustrative Tools*; they should not be used without reading and understanding that chapter. Also, please refer to the *Framework* when using these templates, particularly, Chapter 2, Objectives, Components, and Principles, and Chapter 3, Effective Internal Control.

The templates are designed to present only a summary of assessment results. They are not an integral part of the *Framework*, and they may not address all matters that need to be considered when assessing a system of internal control. Further, they do not represent a preferred method of conducting and documenting an assessment. Their purpose is limited to illustrating one possible assessment process based on the requirements for effective internal control set forth in the *Framework*.

Four different templates are included:

- Overall Assessment—This template summarizes management's determination of whether each of the components and relevant principles is present and functioning and components are operating together in an integrated manner.
- Components—A component of internal control supports an organization's efforts in achieving its financial reporting objectives. The component describes what is required for the organization to meet their objectives and are relevant to an entire entity or at any entity level, division, operating unit, or function of the organization. All five components must be present and functioning together to have an effective system of internal control. This template summarizes management's determination of whether each component and relevant principles are present and functioning. A template for each of the five components is included.
- Principles—A principle is a fundamental concept associated with one of the five components of internal control. There is a total of seventeen principles in the Framework. The IC framework also includes points of focus to describe important characteristics of each principle. However, the framework does not require management to evaluate whether all points of focus are in place. This template summarizes the controls to effect principles and management's determination of whether each relevant principle is present and functioning. A template for each of the seventeen principles is included.
- Deficiencies—A log of all identified internal control deficiencies that can be leveraged in the evaluation of components and principles, and can enable the internal control deficiencies to be aggregated.

1. Overall Assessment of a System of Internal Control

Overall Assessment of a System of Internal Control				
Entity or part of organization structure subject to the assessment (entity, division, operating unit, function)		City of San Diego		
Objective(s) being considered for the scope of internal control being assessed		Considerations regarding management's acceptable level of risk		
Operations				
Reporting	The City's main objective of internal controls over financial reporting is to provide reasonable assurance that financial information produced for internal and external reports is reliable and transparent, reflects the City's transactions and events for the reporting period, and is in accordance with GAAP and other reporting requirements.	The acceptable level of risk is based on a general materiality threshold along with qualitative factors and professional judgement. Materiality also depends on the size and nature of the omission or misstatement judged in the surrounding circumstances.		
Compliance				
		Present? (Y/N)	Functioning? (Y/N)	Explanation/Conclusion
Control Environment		Y	Y	The City has established a set of standards, processes, structures, policies, and practices that encompass the City's integrity and ethical values and provide the basis for the City to carry out internal controls across the organization. All principles are present and functioning, despite two internal control deficiencies identified under this component.
Risk Assessment		Y	Y	The City conducts a continuous and effective assessment of risk that allows management to determine the need for controls and monitoring activities, improvements that can be made to information and communication, and to mitigate such risks that can affect the control environment.
Control Activities		Y	Y	The City has selected and developed budgetary controls, transaction controls, general controls over technology, and control activities deployed through policies and procedures to help mitigate the risk to the achievement of the City's financial reporting objectives.
Information and Communication		Y	Y	The City has established effective communication procedures through formal communication processes, financial reporting tools, and financial trainings in order to meet accounting and disclosure requirements and to share necessary financial information internally and externally.
Monitoring Activities		Y	Y	The City has established ongoing and separate monitoring activities and communicates internal control deficiencies identified during monitoring to ensure each of the five COSO components are present and functioning.
Are all components operating together in an integrated manner? Evaluate if a combination of internal control deficiencies, when aggregated across components, represent a major deficiency*		Yes - Although there are two internal control deficiencies, they do not represent major deficiencies.		
Is the overall system of internal control effective? <Y/N>*		Yes		
Basis for conclusion		The City has established a comprehensive internal controls program and believes the internal controls over financial reporting are effective. All 5 COSO components are present and functioning.		

* If it is determined that there is a major deficiency, management must conclude that the system of internal control is not effective.

2. Component Evaluation

Component Evaluation – Control Environment				
		Present? (Y/N)	Functioning? (Y/N)	Explanation/Conclusion
1. Demonstrates Commitment to Integrity and Ethical Values —The organization demonstrates a commitment to integrity and ethical values.		Y	Y	San Diego Municipal Code (SDMC) establishes the Ethics Commission; City also has fraud, waste, and abuse hotline, and employee code of conduct. The City's Strategic Plan has "Integrity" as one of the four main key values. Performance Evaluations of work standards are conducted for classified employees.
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
		Present? (Y/N)	Functioning? (Y/N)	Explanation/Conclusion
2. Exercises Oversight Responsibility —The board of directors demonstrates independence from management and exercises oversight of the development and performance of internal control.		Y	Y	Strong mayor-form of government with City Council as legislative body. City Charter establishes independent auditor reporting to an audit committee. Independent Budget Analyst advises City Council and Audit Committee.
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	

Component Evaluation – Control Environment				
		Present? (Y/N)	Functioning? (Y/N)	Explanation/Conclusion
3. Establishes Structure, Authority, and Responsibility —Management establishes, with board oversight, structures, reporting lines, and appropriate authorities and responsibilities in the pursuit of objectives.		Y	Y	Authority and relationships codified in City Charter, SDMC, and ARs: Charter Sections 39.1, 39.2, and 39.3; SDMC §22.4101; AR 95.39. Chief Compliance Officer chairs the Risk Oversight Committee.
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
		Present? (Y/N)	Functioning? (Y/N)	Explanation/Conclusion
4. Demonstrates Commitment to Competence —The organization demonstrates a commitment to attract, develop, and retain competent individuals in alignment with objectives.		Y	Y	Financial Training Program available, staff encouraged to attain professional designations (e.g. CPA), finance departments maintain training policies, Rewards and Recognition Program, Goal Setting, Performance Plans and Evaluations.
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Performance Audit of the City's Strategic Human Capital Management, Part I	Widespread uncompetitive compensation poses a growing shorthand long term risk to the City's ability to maintain and attract a high-quality workforce for providing public services, and has likely contributed to several negative effects on the City workforce and public services.	N	City agreed to auditor recommendations in their HCM audit report including creating a total compensation strategy; City uses special salary adjustments process to maintain competitive hiring; financial training program offered to entry level and experienced finance staff citywide; documentation to preserve institutional knowledge	
Performance Audit of the City's Strategic Human Capital Management, Part II	Employee performance can have an impact on an organization's environment and capability in providing high-quality public services. The City could improve its ability to effectively identify or address poor performance or misconduct issues and show employee appreciation and recognition to help engage employees and drive them to continue commendable performance. Otherwise, it could affect the City from providing high-quality public services for its customers and have an impact on other employee's performance and the control environment.	N	To mitigate some of these effects and help the City strengthen its capability to have an engaged workforce, management agreed to these key recommendations: report Employee Performance Review completion rates in the City's annual workforce report, review and monitor the Rewards and Recognition Program, strategically monitor aggregate discipline trends, and expand disciplinary processes and discipline-related training for supervising employees.	

Component Evaluation – Control Environment				
		Present? (Y/N)	Functioning? (Y/N)	Explanation/Conclusion
5. Enforces Accountability —The organization holds individuals accountable for their internal control responsibilities in the pursuit of objectives.		Y	Y	A.R. 95.39 outlines management responsibilities for internal financial controls. Rewards and Recognition Program Goal Setting, Performance Plans and Evaluations.
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Performance Audit of the City's Strategic Human Capital Management, Part II	Employee performance can have an impact on an organization's environment and capability in providing high-quality public services. The City could improve its ability to effectively identify or address poor performance or misconduct issues and show employee appreciation and recognition to help engage employees and drive them to continue commendable performance. Otherwise, it could affect the City from providing high-quality public services for its customers and have an impact on other employee's performance and the control environment.	N	To mitigate some of these effects and help the City strengthen its capability to have an engaged workforce, management agreed to these key recommendations: report Employee Performance Review completion rates in the City's annual workforce report, review and monitor the Rewards and Recognition Program, strategically monitor aggregate discipline trends, and expand disciplinary processes and discipline-related training for supervising employees.	
		Explanation/Conclusion		
Evaluate deficiencies across the component:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered across the component, represent a major deficiency**		There are two deficiencies stated under Principle 4 and one deficiency stated under Principle 5, but they do not represent major deficiencies.		
Evaluate the component using judgment and based on the principles and the deficiencies**		Yes/No		Explanation/Conclusion
Is the component present?		Y		
Is the component functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the component is not present and functioning and the system of internal control is not effective.

Component Evaluation — Risk Assessment				
		Present? (Y/N)	Functioning? (Y/N)	Explanation/Conclusion
6. Specifies Suitable Objectives —The organization specifies objectives with sufficient clarity to enable the identification and assessment of risks relating to objectives.		Y	Y	<p>Reporting Objectives: City ensures financial statements are in compliance with accounting standards. The Comprehensive Annual Financial Report is prepared in accordance with GAAP and the City's Materiality Policy.</p> <p>The City's internal reports informs of the Mayor's priorities in terms of financial characteristics and provides visibility on the City's progress in managing the City's finances.</p>
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
		Present? (Y/N)	Functioning? (Y/N)	Explanation/Conclusion
7. Identifies and Analyzes Risks —The organization identifies risks to the achievement of its objectives across the entity and analyzes risks as a basis for determining how the risks should be managed.		Y	Y	<p>At the beginning of each Comprehensive Annual Financial Report preparation cycle, management communicates areas of potential risk to City's external auditor based on management's risk assessment and ongoing monitoring activities.</p> <p>City Auditor completes a citywide risk assessment to help identify, measure, and prioritize the City's potential audits based on the level of risk to the City.</p> <p>Information Technology Disaster Plans identify risks and threats to the organization and the impact to the City's business operations.</p>
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	

Component Evaluation — Risk Assessment				
		Present? (Y/N)	Functioning? (Y/N)	Explanation/Conclusion
8. Assesses Fraud Risk —The organization considers the potential for fraud in assessing risks to the achievement of objectives.		Y	Y	<p>Management participates in audit entrance and exit meetings with City departments, so department can address concerns that have an impact on accounting and financial reporting, safeguarding of City assets, and issues affecting the internal control environment.</p> <p>Management participates in the remediation of City Auditor's fraud hotline audits and assess further opportunities for fraud risk.</p> <p>Risk Oversight Committee designed to identify and mitigate risks citywide.</p>
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
		Present? (Y/N)	Functioning? (Y/N)	Explanation/Conclusion
9. Identifies and Analyzes Significant Change —The organization identifies and assesses changes that could significantly impact the system of internal control.		Y	Y	<p>The DoF staff evaluates new accounting standards promulgated by Governmental Accounting Standards Board (GASB) and new changes in technology.</p> <p>In 2020, Management assessed changes in new City leadership and changes in the physical and economic environment due to the COVID-19 pandemic.</p>
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
		Explanation/Conclusion		
Evaluate deficiencies across the component:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered across the component, represent				
Evaluate the component using judgment and based on the principles and the deficiencies**		Yes/No		Explanation/Conclusion
Is the component present?		Y		
Is the component functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the component is not present and functioning and the system of internal control is not effective.

Component Evaluation — Control Activities				
		Present? (Y/N)	Functioning? (Y/N)	Explanation/Conclusion
10. Selects and Develops Control Activities —The organization selects and develops control activities that contribute to the mitigation of risks to the achievement of objectives to acceptable levels.		Y	Y	<p>Controls related to this include: segregation of duties, variety of transaction control activities (authorization & approvals, verifications, physical controls, reconciliations, supervisory controls).</p> <p>Management develops new control activities when risks are identified. In 2020, control activities were implemented for Electronic Funds Transfer and Invoice Processing.</p> <p>Process Narrative Annual Assessment conducted to test the validity, accuracy, presence, and performance of processes and controls defined in process narratives.</p>
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
11. Selects and Develops General Controls over Technology —The organization selects and develops general control activities over technology to support the achievement of objectives.		Y	Y	<p>IT General Controls: maintained through cyber security tools, patching and change management, user authentication, documentation, authorizing access to applications, managing access through roles and separation of duties, and physical security of IT infrastructure.</p> <p>Management reviews IT changes to the ERP system for adequate preventative or detective controls.</p> <p>In 2020, Management implemented additional IT control activities in response to the COVID-19 pandemic.</p>
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	

Component Evaluation — Control Activities				
		Present? (Y/N)	Functioning? (Y/N)	Explanation/Conclusion
12. Deploys through Policies and Procedures – The organization deploys control activities through policies that establish what is expected and procedures that put policies into action.		Y	Y	<p>Policies such as City's Investment Policy, Debt Policy, Reserve Policy and Budget Policy.</p> <p>Administrative regulations, department instructions, process narratives, and work instructions are updated and reviewed by responsible departments and stakeholders.</p> <p>At the beginning of the COVID-19 pandemic, Continuation of Operations Plans (COOPS), were updated to maintain essential services with limited staffing.</p>
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Explanation/Conclusion				
Evaluate deficiencies across the component:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered across the component, represent a major deficiency**				
Evaluate the component using judgment and based on the principles and the deficiencies**		Yes/No	Explanation/Conclusion	
Is the component present?		Y		
Is the component functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the component is not present and functioning and the system of internal control is not effective.

Component Evaluation — Information and Communication				
		Present? (Y/N)	Functioning? (Y/N)	Explanation/Conclusion
13 Uses Relevant Information – The organization obtains or generates and uses relevant, quality information to support the functioning of internal control.		Y	Y	<p>City uses financial reporting tools to perform ad-hoc queries or run reports to efficiently access financial data stored in SAP in a timely, accurate, and appropriate manner.</p> <p>Formal Communication Process in place ensures relevant information is communicated to those responsible for preparing the Comprehensive Annual Financial Report. The DPWG communicates known facts, and other relevant information to ensure consistency throughout the City's financial disclosure documents.</p>
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
		Present? (Y/N)	Functioning? (Y/N)	Explanation/Conclusion
14 Communicates Internally – The organization internally communicates information, including objectives and responsibilities for internal control, necessary to support the functioning of internal control.		Y	Y	<p>Finance Orientation & Finance Academy annual trainings to update on current processes; process documentation (AR's, PN's, and WI's); Internal Financial Statement Checklists; Fraud, Waste, and Abuse Hotline</p> <p>Formal distribution of work document to clearly communicate specific responsibilities for development of the Comprehensive Annual Financial Report.</p> <p>Financial reports to committees and city council, and internal meetings with Disclosures Practices Working Group (DPWG).</p>
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	

Component Evaluation — Information and Communication				
		Present? (Y/N)	Functioning? (Y/N)	Explanation/Conclusion
15 Communicates Externally – The organization communicates with external parties regarding matters affecting the functioning of internal control.		Y	Y	<p>Financial policies and ARs posted on city website; Annual report on financial internal controls; Preliminary Official Statements issued per bond issuance; bond rating agency interviews.</p> <p>At the beginning of each Comprehensive Annual Financial Report preparation cycle, management communicates areas of potential financial reporting risk to City's external auditor based on management's risk assessment and ongoing monitoring activities.</p> <p>Citywide risk assessment to help identify, measure, and prioritize the City's potential audits based on the level of risk to the City.</p> <p>The DPWG includes individuals in key city positions within the city and external counsel that can communicate known facts and relevant information.</p>
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Explanation/Conclusion				
Evaluate deficiencies across the component: Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered across the component, represent a major deficiency**				
Evaluate the component using judgment and based on the principles and the deficiencies**		Yes/No	Explanation/Conclusion	
Is the component present?		Y		
Is the component functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the component is not present and functioning and the system of internal control is not effective.

Component Evaluation — Monitoring Activities				
		Present? (Y/N)	Functioning? (Y/N)	Explanation/Conclusion
16 Conducts Ongoing and/or Separate Evaluations – The organization selects, develops, and performs ongoing and/or separate evaluations to ascertain whether the components of internal control are present and functioning.		Y	Y	Ongoing Monitoring for transactions related to: p-card, travel & tuition, jury duty, invoices, procurement, electronic banking changes, and aging good receipts. Annual review of process narratives and IT security roles. In 2020, the DoF developed a control risk-based approach to assess process documentation.
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
		Present? (Y/N)	Functioning? (Y/N)	Explanation/Conclusion
17 Evaluates and Communicates Deficiencies – The organization evaluates and communicates internal control deficiencies in a timely manner to those parties responsible for taking corrective action, including senior management and the board of directors, as appropriate.		Y	Y	City management reviews and monitors audits performed by City Auditor and works with departments to strengthen controls. The DoF reviews the independent audit conducted by external auditors to identify areas where internal controls can be strengthened. The DoF conducts an internal review of the preparation and completion of the Comprehensive Annual Financial Report to identify entries that occurred after the draft was submitted to external auditor. CFO committed to strengthening controls in Comprehensive Annual Financial Report reporting and completed 7 improvements on a timely basis.
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
		Explanation/Conclusion		
Evaluate deficiencies across the component:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered across the component, represent a major deficiency**				
Evaluate the component using judgment and based on the principles and the deficiencies**		Yes/No	Explanation/Conclusion	
Is the component present?		Y		
Is the component functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Section.

** If it is determined that there is a major deficiency, management must conclude that the component is not present and functioning and the system of internal control is not effective.

3. Principle Evaluation

Principle Evaluation – Control Environment				
Principle 1: Demonstrates Commitment to Integrity and Ethical Values				
–The organization demonstrates a commitment to integrity and ethical values.				
Points of Focus				
<ul style="list-style-type: none"> • Sets the Tone at the Top – The board of directors and management at all levels of the entity demonstrate through their directives, actions, and behavior the importance of integrity and ethical values to support the functioning of the system of internal control. • Establishes Standards of Conduct – The expectations of the board of directors and senior management concerning integrity and ethical values are defined in the entity's standards of conduct and understood at all levels of the organization and by outsourced service providers and business partners. • Evaluates Adherence to Standards of Conduct – Processes are in place to evaluate the performance of individuals and teams against the entity's expected standards of conduct. • Addresses Deviations in a Timely Manner – Deviations of the entity's expected standards of conduct are identified and remedied in a timely and consistent manner. • (Other entity specific points of focus, if any) 				
Summary of Controls to Effect Principle 1				
- Ethics Commission: Established through SDMC. Monitors, administers, and enforces the City's governmental ethics laws, conducts investigations, advises and educates City officials, candidates, political committees, and lobbyists about governmental ethics laws, etc.				
- Fraud, Waste, and Abuse Hotline: designed for reporting suspected cases of fraud, waste, or abuse. The City Auditor investigates all complaints in a timely manner.				
- Employee Code of Conduct: Emphasizes that each employee occupies a position of public trust which demands the highest moral and ethical standard of conduct.				
- City Strategic Plan: One of the four key values in the City's Strategic Plan is integrity.				
- Performance Evaluations: classified employees receive a performance plan and periodic performance evaluations of work standards and City uses progressive discipline philosophy to correct deviations.				
Deficiencies Applicable to Principle 1				
Identification No.	Internal control deficiency description	Evaluate internal control deficiency severity: (Consider whether controls to effect other principles within and across components compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Preliminary Severity – Is internal control deficiency a major deficiency? (Y/N)	Comments/ Compensating Controls	
Evaluate deficiencies within the principle:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered within the principle, represent a major deficiency.** <Update Summary of Deficiencies Template as required>		<Explanation>		
Evaluate the principle using judgment.**		Y/N	Explanation/Conclusion	
Is the principle present?		Y		
Is the principle functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the principle is not present and functioning and the system of internal control is not effective.

Principle 2: Exercises Oversight Responsibility

—The board of directors demonstrates independence from management and exercises oversight of the development and performance of internal control.

Points of Focus

- **Establishes Oversight Responsibilities**—The board of directors identifies and accepts its oversight responsibilities in relation to established requirements and expectations.
- **Applies Relevant Expertise**—The board of directors defines, maintains, and periodically evaluates the skills and expertise needed among its members to enable them to ask probing questions of senior management and take commensurate actions.
- **Operates Independently**—The board of directors has sufficient members who are independent from management and objective in evaluations and decision making.
- **Provides Oversight for the System of Internal Control**—The board of directors retains oversight responsibility for management's design, implementation, and conduct of internal control:
 - **Control Environment**—Establishing integrity and ethical values, oversight structures, authority and responsibility, expectations of competence, and accountability to the board.
 - **Risk Assessment**—Overseeing management's assessment of risks to the achievement of objectives, including the potential impact of significant changes, fraud, and management override of internal control.
 - **Control Activities**—Providing oversight to senior management in the development and performance of control activities.
 - **Information and Communication**—Analyzing and discussing information relating to the entity's achievement of objectives.
 - **Monitoring Activities**—Assessing and overseeing the nature and scope of monitoring activities and management's evaluation and remediation of deficiencies.
- (Other entity specific points of focus, if any)

Summary of Controls to Effect Principle 2

-City Charter Section 39: identifies the rights and authority of the Chief Financial Officer (CFO), City Council, and Audit Committee. City Council and Audit Committee provide oversight. Audit Committee's independence is maintained by filling positions from City Council and public members with sufficient financial reporting, accounting, and audit expertise.

-Independent Budget Analyst and City Auditor: release reports and advise City Council and Audit Committee members of relevant questions for management and courses of actions.

Deficiencies Applicable to Principle 2

Identification No.	Internal control deficiency description	Evaluate preliminary deficiency severity: (Consider whether other controls to effect this principle compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Preliminary Severity—Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Evaluate deficiencies within the principle:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered within the principle, represent a major deficiency** <Update Summary of Deficiencies Template as required>		<Explanation>		
Evaluate the principle using judgment.**		Y/N	Explanation/Conclusion	
Is the principle present?		Y		
Is the principle functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the principle is not present and functioning and the system of internal control is not effective.

Principle 3: Establishes Structure, Authority, and Responsibility

—Management establishes, with board oversight, structures, reporting lines, and appropriate authorities and responsibilities in the pursuit of objectives.

Points of Focus

- **Considers All Structures of the Entity**—Management and the board of directors consider the multiple structures used (including operating units, legal entities, geographic distribution, and outsourced service providers) to support the achievement of objectives.
- **Establishes Reporting Lines**—Management designs and evaluates lines of reporting for each entity structure to enable execution of authorities and responsibilities and flow of information to manage the activities of the entity.
- **Defines, Assigns, and Limits Authorities and Responsibilities** —Management and the board of directors delegate authority, define responsibilities, and use appropriate processes and technology to assign responsibility and segregate duties as necessary at the various levels of the organization:
 - **Board of Directors** — Retains authority over significant decisions and reviews management's assignments and limitations of authorities and responsibilities
 - **Senior Management**—Establishes directives, guidance, and control to enable management and other personnel to understand and carry out their internal control responsibilities
 - **Management**—Guides and facilitates the execution of senior management directives within the entity and its subunits
 - **Personnel**—Understands the entity's standard of conduct, assessed risks to objectives, and the related control activities at their respective levels of the entity, the expected information and communication flow, and monitoring activities relevant to their achievement of the objectives
 - **Outsourced Service Providers**—Adheres to management's definition of the scope of authority and responsibility for all non-employees engaged
- (Other entity specific points of focus, if any)

Summary of Controls to Effect Principle 3

- **Charter Section 39.1:** establishes an independent audit committee to oversee the City's auditing function and SDMC §26.1701 outlines duties including hiring an external auditor.
- **Charter Section 39.2 and 39.3:** establishes independent positions to assist City Council in check and balances over the executive branch.
- **SDMC §22.4101:** establishes Disclosures Practices Working Group (DPWG) responsible for ensuring compliance with federal and state securities laws.
- **AR 95.39:** establishes management responsibilities related to establishing, maintaining, monitoring and complying with a system of Internal Financial Controls.
- **Chief Compliance Officer:** coordinates response to compliance issues and chairs the Risk Oversight Committee to manage risk efforts in the City.

Deficiencies Applicable to Principle 3

Identification No.	Internal control deficiency description	Evaluate preliminary deficiency severity: (Consider whether other controls to effect this principle compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Preliminary Severity—Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Evaluate deficiencies within the principle:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered within the principle, represent a major deficiency** <Update Summary of Deficiencies Template as required> Evaluate the principle using judgment.**		<Explanation>		
		Y/N	Explanation/Conclusion	
Is the principle present?		Y		
Is the principle functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the principle is not present and functioning and the system of internal control is not effective.

Principle 4: Demonstrates Commitment to Competence

—The organization demonstrates a commitment to attract, develop, and retain competent individuals in alignment with objectives.

Points of Focus

- **Establishes Policies and Practices**—Policies and practices reflect expectations of competence necessary to support the achievement of objectives.
- **Evaluates Competence and Addresses Shortcomings**—The board of directors and management evaluate competence across the organization and in outsourced service providers in relation to established policies and practices, and act as necessary to address shortcomings.
- **Attracts, Develops, and Retains Individuals**—The organization provides the mentoring and training needed to attract, develop, and retain sufficient and competent personnel and outsourced service providers to support the achievement of objectives.
- **Plans and Prepares for Succession**—Senior management and the board of directors develop contingency plans for assignments of responsibility important for internal control.
- (Other entity specific points of focus, if any)

Summary of Controls to Effect Principle 4

- **Financial Training Program:** City employees, City management, and elected officials are provided training to aid employees in submitting or reviewing financial-data and reports. Elected officials are provided tailored trainings and presentations on financial topics such as budgeting principles and financial statement disclosure. SDMC §22.4110 established a biennial mandatory securities law training.

- **Training Policies:** centralized finance staff must meet minimum number of annual training hours and encouraged to pursue training and designations relevant to their job per their department's training policy.

- **Rewards and Recognition program and Tuition Reimbursement program:** Encourages retention amongst high-quality employees and pursuit of professional expertise.

- **Goal Setting, Performance Plans and Evaluations:** unclassified employees maintain goals and classified employees receive performance plan outlining objectives, responsibilities, and goals. Performance evaluations are conducted periodically by management to assess against work standards and deviations are corrected as necessary.

Deficiencies Applicable to Principle 4

Identification No.	Internal control deficiency description	Evaluate preliminary deficiency severity: (Consider whether other controls to effect this principle compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Preliminary Severity—Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Performance Audit of the City's Strategic Human Capital Management, Part I	Widespread uncompetitive compensation poses a growing shorthand long term risk to the City's ability to maintain and attract a high-quality workforce for providing public services, and has likely contributed to several negative effects on the City workforce and public services.	N	City agreed to auditor recommendations in their HCM report including creating a total compensation strategy; City uses special salary adjustments process to maintain competitive hiring; financial training program offered to entry level and experienced finance staff citywide; documentation created to preserve institutional knowledge	
Performance Audit of the City's Strategic Human Capital Management, Part II	Employee performance can have an impact on an organization's environment and capability in providing high-quality public services. The City could improve its ability to effectively identify or address poor performance or misconduct issues and show employee appreciation and recognition to help engage employees and drive them to continue commendable performance. Otherwise, it could affect the City from providing high-quality public services for its customers and have an impact on other employee's performance and the control environment.	N	To mitigate some of these effects and help the City strengthen its capability to have an engaged workforce, management agreed to these key recommendations: report Employee Performance Review completion rates in the City's annual workforce report, review and monitor the Rewards and Recognition Program, strategically monitor aggregate discipline trends, and expand disciplinary processes and discipline-related training for supervising employees.	
Evaluate deficiencies within the principle:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered within the principle, represent a major deficiency** <Update Summary of Deficiencies Template as required>		Deficiencies stated under Principle 4 do not represent major deficiencies.		
Evaluate the principle using judgment.**		Y/N	Explanation/Conclusion	
Is the principle present?		Y		
Is the principle functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the principle is not present and functioning and the system of internal control is not effective.

Principle 5: Enforces Accountability

—The organization holds individuals accountable for their internal control responsibilities in the pursuit of objectives.

Points of Focus

- **Enforces Accountability through Structures, Authorities, and Responsibilities**—Management and the board of directors establish the mechanisms to communicate and hold individuals accountable for performance of internal control responsibilities across the organization and implement corrective action as necessary.
- **Establishes Performance Measures, Incentives, and Rewards**—Management and the board of directors establish performance measures, incentives, and other rewards appropriate for responsibilities at all levels of the entity, reflecting appropriate dimensions of performance and expected standards of conduct, and considering the achievement of both short-term and longer-term objectives.
- **Evaluates Performance Measures, Incentives, and Rewards for Ongoing Relevance**—Management and the board of directors align incentives and rewards with the fulfillment of internal control responsibilities in the achievement of objectives.
- **Considers Excessive Pressures**—Management and the board of directors evaluate and adjust pressures associated with the achievement of objectives as they assign responsibilities, develop performance measures, and evaluate performance.
- **Evaluates Performance and Rewards or Disciplines Individuals**—Management and the board of directors evaluate performance of internal control responsibilities, including adherence to standards of conduct and expected levels of competence and provide rewards or exercise disciplinary action as appropriate.
- (Other entity specific points of focus, if any)

Summary of Controls to Effect Principle 5

-A.R. 95.39 - Management Responsibilities for Internal Financial Controls: established to provide a strong enhancement over the City's control environment. Holds management accountable for developing citywide financial policies and procedures within the Finance Branch, including citywide dissemination. Emphasizes the role of the Executive Management Team in creating an organizational culture that supports the internal control environment.

- Rewards and Recognition program and Tuition Reimbursement program: Encourages retention amongst high-quality employees and pursuit of professional expertise.

- Goal Setting, Performance Plans and Evaluations: unclassified employees maintain goals and classified employees receive performance plan outlining objectives, responsibilities, and goals. Performance evaluations are conducted periodically by management to assess against work standards and deviations are corrected as necessary.

Deficiencies Applicable to Principle 5

Identification No.	Internal control deficiency description	Evaluate preliminary deficiency severity: (Consider whether other controls to effect this principle compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Preliminary Severity—Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Performance Audit of the City's Strategic Human Capital Management, Part II	Employee performance can have an impact on an organization's environment and capability in providing high-quality public services. The City could improve its ability to effectively identify or address poor performance or misconduct issues and show employee appreciation and recognition to help engage employees and drive them to continue commendable performance. Otherwise, it could affect the City from providing high-quality public services for its customers and have an impact on other employee's performance and the control environment.	N	To mitigate some of these effects and help the City strengthen its capability to have an engaged workforce, management agreed to these key recommendations: report Employee Performance Review completion rates in the City's annual workforce report, review and monitor the Rewards and Recognition Program, strategically monitor aggregate discipline trends, and expand disciplinary processes and discipline-related training for supervising employees.	
Evaluate deficiencies within the principle:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered within the principle, represent a major deficiency** <Update Summary of Deficiencies Template as required>		Deficiency stated under Principle 5 does not represent a major deficiency.		
Evaluate the principle using judgment.**		Y/N	Explanation/Conclusion	
Is the principle present?		Y		
Is the principle functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the principle is not present and functioning and the system of internal control is not effective.

Principle Evaluation – Risk Assessment**Principle 6: Specifies Suitable Objectives**

—The organization specifies objectives with sufficient clarity to enable the identification and assessment of risks relating to objectives.

Points of Focus**Operations Objectives**

- **Reflects Management's Choices**—Operations objectives reflect management's choices about structure, industry considerations, and performance of the entity.
- **Considers Tolerances for Risk**—Management considers the acceptable levels of variation relative to the achievement of operations objectives.
- **Includes Operations and Financial Performance Goals**—The organization reflects the desired level of operations and financial performance for the entity within operations objectives.
- **Forms a Basis for Committing of Resources**—Management uses operations objectives as a basis for allocating resources needed to attain desired operations and financial performance.

External Financial Reporting Objectives

- **Complies with Applicable Accounting Standards**—Financial reporting objectives are consistent with accounting principles suitable and available for that entity. The accounting principles selected are appropriate in the circumstances.
- **Considers Materiality**—Management considers materiality in financial statement presentation.
- **Reflects Entity Activities**—External reporting reflects the underlying transactions and events to show qualitative characteristics and assertions.

External Non-Financial Reporting Objectives

- **Complies with Externally Established Standards and Frameworks**—Management establishes objectives consistent with laws and regulations, or standards and frameworks of recognized external organizations.
- **Considers the Required Level of Precision**—Management reflects the required level of precision and accuracy suitable for user needs and as based on criteria established by third parties in non-financial reporting.
- **Reflects Entity Activities**—External reporting reflects the underlying transactions and events within a range of acceptable limits.

Internal Reporting Objectives

- **Reflects Management's Choices**—Internal reporting provides management with accurate and complete information regarding management's choices and information needed in managing the entity.
- **Considers the Required Level of Precision**—Management reflects the required level of precision and accuracy suitable for user needs in non-financial reporting objectives and materiality within financial reporting objectives.
- **Reflects Entity Activities**—Internal reporting reflects the underlying transactions and events within a range of acceptable limits.

Compliance Objectives

- **Reflects External Laws and Regulations**—Laws and regulations establish minimum standards of conduct which the entity integrates into compliance objectives.
- **Considers Tolerances for Risk**—Management considers the acceptable levels of variation relative to the achievement of compliance objectives.
- (Other entity specific points of focus, if any)

Summary of Controls to Effect Principle 6

- **External Financial Reporting:** management creates the Comprehensive Annual Financial Report. The Comprehensive Annual Financial Report is the most significant external financial report and is prepared in accordance with GAAP. It includes the balances and activity of all funds and component units of the City and related disclosures. Materiality policy is followed and management risk assessment on the Comprehensive Annual Financial Report is conducted prior to the start of the report.

- **Internal Financial Reporting:** management creates the annual budget, and other informational reports for decision-making. The City's annual budget is the most important report because it informs readers of the Mayor's priorities in terms of financial characteristics and serves as a key tool for financial management and compliance. Department budget pages include goals and objectives. Five-Year Financial Outlook, monthly Charter 39 Financial Performance Reports, and budget monitoring quarterly reports provide the City visibility on progress in managing the City's finances.

Deficiencies Applicable to Principle 6

Identification No.	Internal control deficiency description	Evaluate preliminary deficiency severity: (Consider whether other controls to effect this principle compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Preliminary Severity—Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Evaluate deficiencies within the principle:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered within the principle, represent a major deficiency** <Update Summary of Deficiencies Template as required>		<Explanation>		
Evaluate the principle using judgment.**		Y/N	Explanation/Conclusion	
Is the principle present?		Y		
Is the principle functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the principle is not present and functioning and the system of internal control is not effective.

Principle 7: Identifies and Analyzes Risk

—The organization identifies risks to the achievement of its objectives across the entity and analyzes risks as a basis for determining how the risks should be managed.

Points of Focus

- **Includes Entity, Subsidiary, Division, Operating Unit, and Functional Levels**—The organization identifies and assesses risks at the entity, subsidiary, division, operating unit, and functional levels relevant to the achievement of objectives.
- **Analyzes Internal and External Factors**—Risk identification considers both internal and external factors and their impact on the achievement of objectives.
- **Involves Appropriate Levels of Management**—The organization puts into place effective risk assessment mechanisms that involve appropriate levels of management.
- **Estimates Significance of Risks Identified**—Identified risks are analyzed through a process that includes estimating the potential significance of the risk.
- **Determines How to Respond to Risks**—Risk assessment includes considering how the risk should be managed and whether to accept, avoid, reduce, or share the risk.
- (Other entity specific points of focus, if any)

Summary of Controls to Effect Principle 7

- **Comprehensive Annual Financial Report Risk Assessment:** Management performs an annual risk assessment at the beginning of each Comprehensive Annual Financial Report preparation cycle and communicates risks to the City's external auditor based on management's risk assessment and ongoing monitoring activities, including management's response to such risks through development and implementation of additional controls.

- **Information Technology Disaster Plans:** The City contracted with Atos IT Solutions and Services to perform Business Impact Analysis/Risk Assessment on IT applications housing the underlying transactions, including financial transactions, and created Disaster Recovery Plans to help identify risks and threats to the organization and the impact to the City's business operations.

- **Auditor's Citywide Risk Assessment:** City Auditor completes a citywide risk assessment to help identify, measure, and prioritize the City's potential audits based on the level of risk to the City.

Deficiencies Applicable to Principle 7

Identification No.	Internal control deficiency description	Evaluate preliminary deficiency severity: (Consider whether other controls to effect this principle compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Preliminary Severity—Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Evaluate deficiencies within the principle:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered within the principle, represent a major deficiency** <Update Summary of Deficiencies Template as required>		<Explanation>		
Evaluate the principle using judgment.**		Y/N	Explanation/Conclusion	
Is the principle present?		Y		
Is the principle functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the principle is not present and functioning and the system of internal control is not effective.

Principle 8: Assesses Fraud Risk

—The organization considers the potential for fraud in assessing risks to the achievement of objectives.

Points of Focus

- **Considers Various Types of Fraud**—The assessment of fraud considers fraudulent reporting, possible loss of assets, and corruption resulting from the various ways that fraud and misconduct can occur.
- **Assesses Incentive and Pressures**—The assessment of fraud risk considers incentives and pressures.
- **Assesses Opportunities**—The assessment of fraud risk considers opportunities for unauthorized acquisition, use, or disposal of assets, altering of the entity's reporting records, or committing other inappropriate acts.
- **Assesses Attitudes and Rationalizations**—The assessment of fraud risk considers how management and other personnel might engage in or justify inappropriate actions.
- (Other entity specific points of focus, if any)

Summary of Controls to Effect Principle 8:

- **Performance audit remediation:** Management participates in audit entrance and exit meetings with City departments, so departments can address concerns that have an impact on accounting and financial reporting, safeguarding of City assets, and issues affecting the internal control environment.

- **Fraud hotline remediation:** Management participates in the remediation of City Auditor's fraud hotline audits and assess further opportunities for fraud risk.

- **Risk Oversight Committee:** committee designed to identify and mitigate risks citywide.

Deficiencies Applicable to Principle 8

Identification No.	Internal control deficiency description	Evaluate preliminary deficiency severity: (Consider whether other controls to effect this principle compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Preliminary Severity—Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Evaluate deficiencies within the principle:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered within the principle, represent a major deficiency** <Update Summary of Deficiencies Template as required>		<Explanation>		
Evaluate the principle using judgment.**		Y/N	Explanation/Conclusion	
Is the principle present?		Y		
Is the principle functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the principle is not present and functioning and the system of internal control is not effective.

Principle 9: Identifies and Analyzes Significant Change

—The organization identifies and assesses changes that could significantly impact the system of internal control.

Points of Focus

- **Assesses Changes in the External Environment**—The risk identification process considers changes to the regulatory, economic, and physical environment in which the entity operates.
- **Assesses Changes in the Business Model**—The organization considers the potential impacts of new business lines, dramatically altered compositions of existing business lines, acquired or divested business operations on the system of internal control, rapid growth, changing reliance on foreign geographies, and new technologies.
- **Assesses Changes in Leadership**—The organization considers changes in management and respective attitudes and philosophies on the system of internal control.
- (Other entity specific points of focus, if any)

Summary of Controls to Effect Principle 9

- **Changes in Leadership:** A new mayor was elected which resulted changes in his administration, including a new Chief Operating Officer, Chief Financial Officer, and Comptroller and Department of Finance Director. Changes in staffing can pose a risk from loss of operational knowledge and continuity.

- **Changes in Accounting Standards:** The DoF participates in an annual GFOA training introducing new accounting pronouncements and actively review new standards. The DoF evaluates new accounting standards promulgated by GASB for potential financial impact. In fiscal year 2020, GASB 84 and GASB 90 were successfully implemented. Assessing impacts of GASB 87.

- **Changes in Technology:** The City ensures that any changes or improvements to the ERP system are fully tested for operational needs and for the impact to financial reporting. Advances in technology allow the City to improve current business processes, create efficiencies, and reduce and/or risks. Example: New centralized payment processing system iPayment, new automated processes for the routing personnel change forms and unclassified employee offer letters.

- **Changes in the External Environment:** Increased risk in the City's economic and physical environment due to the COVID-19 Pandemic.

Deficiencies Applicable to Principle 9

Identification No.	Internal control deficiency description	Evaluate preliminary deficiency severity: (Consider whether other controls to effect this principle compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Preliminary Severity—Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Evaluate deficiencies within the principle:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered within the principle, represent a major deficiency** <Update Summary of Deficiencies Template as required>		<Explanation>		
Evaluate the principle using judgment.**		Y/N	Explanation/Conclusion	
Is the principle present?		Y		
Is the principle functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the principle is not present and functioning and the system of internal control is not effective.

Principle Evaluation – Control Activities**Principle 10: Selects and Develops Control Activities**

—The organization selects and develops control activities that contribute to the mitigation of risks to the achievement of objectives to acceptable levels.

Points of Focus

- **Integrates with Risk Assessment**—Control activities help ensure that risk responses that address and mitigate risks are carried out.
- **Considers Entity-Specific Factors**—Management considers how the environment, complexity, nature, and scope of its operations, as well as the specific characteristics of its organization, affect the selection and development of control activities.
- **Determines Relevant Business Processes**—Management determines which relevant business processes require control activities.
- **Evaluates a Mix of Control Activity Types**—Control activities include a range and variety of controls and may include a balance of approaches to mitigate risks, considering both manual and automated controls, and preventive and detective controls.
- **Considers at What Level Activities Are Applied**—Management considers control activities at various levels in the entity.
- **Addresses Segregation of Duties**—Management segregates incompatible duties, and where such segregation is not practical management selects and develops alternative control activities.
- (Other entity specific points of focus, if any)

Summary of Controls to Effect Principle 10

- **Various Transaction Control Activities** embedded within multiple accounting and financial reporting processes including, authorization and approvals, verifications, physical controls, reconciliations, preventative system controls, and application controls.

- **Electronic Funds Transfer (EFT)**: Management determined the EFT enrollment process necessitated review due to the increase of cyber fraud attempts in 2020 and additional controls such as another layer of supervisory review was implemented.

- **Invoice Processing**: An increase in non-purchase order (NPO) invoices was observed from Small Business Relief Fund payments or SBRF Program and Parks and Recreation refunds for cancelled classes and events. Additional positions were dedicated to review and process the payments while maintaining a system of controls.

- **Segregation of Duties Monitoring**: The City ensures that no one individual has control over an entire process through SAP GRC module and Business Role Management (BRM). An increase in system role assignments was observed due to shift in telecommuting, but segregation of duties was still maintained through the system.

- **Process Narrative Annual Assessment**: Annual process design and control design assessments are conducted to test the validity, accuracy, presence, and performance of processes and controls that have been identified in the process.

Deficiencies Applicable to Principle 10

Identification No.	Internal control deficiency description	Evaluate preliminary deficiency severity: (Consider whether other controls to effect this principle compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Preliminary Severity—Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Evaluate deficiencies within the principle:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered within the principle, represent a major deficiency** <Update Summary of Deficiencies Template as required>		<Explanation>		
Evaluate the principle using judgment.**		Y/N	Explanation/Conclusion	
Is the principle present?		Y		
Is the principle functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the principle is not present and functioning and the system of internal control is not effective.

Principle 11: Selects and Develops General Controls over Technology

—The organization selects and develops general control activities over technology to support the achievement of objectives.

Points of Focus

- **Determines Dependency between the Use of Technology in Business Processes and Technology General Controls**—Management understands and determines the dependency and linkage between business processes, automated control activities, and technology general controls.
- **Establishes Relevant Technology Infrastructure Control Activities**—Management selects and develops control activities over the technology infrastructure, which are designed and implemented to help ensure the completeness, accuracy, and availability of technology processing.
- **Establishes Relevant Security Management Process Control Activities**—Management selects and develops control activities that are designed and implemented to restrict technology access rights to authorized users commensurate with their job responsibilities and to protect the entity's assets from external threats.
- **Establishes Relevant Technology Acquisition, Development, and Maintenance Process Control Activities**—Management selects and develops control activities over the acquisition, development, and maintenance of technology and its infrastructure to achieve management's objectives.
- (Other entity specific points of focus, if any)

Summary of Controls to Effect Principle 11

- **Pandemic Control Activities:** Management expanded the following teleworking technology and resources: offering additional software such as Microsoft Teams and Zoom, greater adoption of electronic signatures and electronic form routing for approvals, additional remote access licenses to allow employees to access shared drives, the City's ERP system, and other applications. Additional laptops and workstation related-hardware were provided to employees who did not have these resources at home. The DoIT also deployed the Mobile Data Management (MDM) system due to the increase of remote work and use of mobile devices for City email and other processes.

- **IT General Controls:** Between Department of IT, City's IT services contract vendors (Atos, Zensar, etc.), departments, and vendors, IT general controls are maintained through cyber security tools, patching and change management, user authentication, documentation, authorizing access to applications, managing access through roles and separation of duties, and physical security of IT infrastructure.

- **Role Definition Guide:** Management performs an annual review to identify new ERP roles and changes, and continuously assesses possible segregation of duties violations with each user role request.

- **Business Role Management:** grouping of roles based off tasks, which helps streamline and better manage changes to roles' access.

- **Internal Controls Review:** Management reviews IT changes to the ERP system for adequate preventative or detective controls.

Deficiencies Applicable to Principle 11

Identification No.	Internal control deficiency description	Evaluate preliminary deficiency severity: (Consider whether other controls to effect this principle compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Preliminary Severity—Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Evaluate deficiencies within the principle:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered within the principle, represent a major deficiency** <Update Summary of Deficiencies Template as required>		<Explanation>		
Evaluate the principle using judgment.**		Y/N	Explanation/Conclusion	
Is the principle present?		Y		
Is the principle functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the principle is not present and functioning and the system of internal control is not effective.

Principle 12: Deploys through Policies and Procedures

—The organization deploys control activities through policies that establish what is expected and procedures that put policies into action.

Points of Focus

- **Establishes Policies and Procedures to Support Deployment of Management's Directives**—Management establishes control activities that are built into business processes and employees' day-to-day activities through policies establishing what is expected and relevant procedures specifying actions.
- **Establishes Responsibility and Accountability for Executing Policies and Procedures**—Management establishes responsibility and accountability for control activities with management (or other designated personnel) of the business unit or function in which the relevant risks reside.
- **Performs in a Timely Manner**—Responsible personnel perform control activities in a timely manner as defined by the policies and procedures.
- **Takes Corrective Action**—Responsible personnel investigate and act on matters identified as a result of executing control activities.
- **Performs Using Competent Personnel**—Competent personnel with sufficient authority perform control activities with diligence and continuing focus.
- **Reassesses Policies and Procedures**—Management periodically reviews control activities to determine their continued relevance, and refreshes them when necessary.
- (Other entity specific points of focus, if any)

Summary of Controls to Effect Principle 12

- **Planning and Procedural Documentation:** At the beginning of the COVID-19 pandemic, department-specific contingency plans, called Continuation of Operations Plans (COOPS), were updated to maintain essential services with limited staffing. Protocols were developed in response to employees affected by COVID-19.

- **Process Documentation:** The DoF has formally documented 716 processes and continuously assesses the need for further documentation. In 2020, 61 process documents were documented.

- **Administrative Regulations:** The IC section reviews and approves policies and procedures included in the Administrative Regulations to ensure internal controls exist to mitigate risks and improve efficiency. Two AR's were new or revised in 2020. Ex: AR 96.20 City Policy for People With Disabilities, AR 90.66 Mobile Device Policy

- **Policies:** Reflect management's goals and guide decisions and actions of staff. Some financial policies include Investment Policy, Debt Policy, Reserve Policy, and Budget Policy.

Deficiencies Applicable to Principle 12

Identification No.	Internal control deficiency description	Evaluate preliminary deficiency severity: (Consider whether other controls to effect this principle compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Preliminary Severity—Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Evaluate deficiencies within the principle:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered within the principle, represent a major deficiency** <Update Summary of Deficiencies Template as required>		<Explanation>		
Evaluate the principle using judgment.**		Y/N	Explanation/Conclusion	
Is the principle present?		Y		
Is the principle functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the principle is not present and functioning and the system of internal control is not effective.

Principle Evaluation—Information and Communication**Principle 13: Uses Relevant Information**

—The organization obtains or generates and uses relevant, quality information to support the functioning of internal control.

Points of Focus

- **Identifies Information Requirements**—A process is in place to identify the information required and expected to support the functioning of the other components of internal control and the achievement of the entity's objectives.
- **Captures Internal and External Sources of Data**—Information systems capture internal and external sources of data.
- **Processes Relevant Data into Information**—Information systems process and transform relevant data into information.
- **Maintains Quality throughout Processing**—Information systems produce information that is timely, current, accurate, complete, accessible, protected, and verifiable and retained. Information is reviewed to assess its relevance in supporting the internal control components.
- **Considers Costs and Benefits**—The nature, quantity, and precision of information communicated are commensurate with and support the achievement of objectives.
- (Other entity specific points of focus, if any)

Summary of Controls to Effect Principle 13

- **Financial Reporting Tools:** business intelligence reporting software allows users to perform ad-hoc queries or run reports to efficiently access financial data stored in SAP in a timely, accurate, and appropriate manner. Examples: Fund Certification Report, AP Dashboard, Human Resources Turnover Dashboard

- In 2020, many SAP initiatives were completed by the DoIT: 44 SAP training videos, 1 Work Instruction, and 8,251 SAP training instances including virtual instructor led and online courses.

- **Formal Communication Process:** ensure relevant information is communicated to those responsible for preparing the Comprehensive Annual Financial Report. The Disclosures Practices Working Group reviews disclosures, communicates known facts, and other relevant information to ensure consistency throughout the City's financial disclosure documents. The DPWG has formal disclosure controls and procedures.

Deficiencies Applicable to Principle 13

Identification No.	Internal control deficiency description	Evaluate preliminary deficiency severity: (Consider whether other controls to effect this principle compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Preliminary Severity—Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Evaluate deficiencies within the principle:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered within the principle, represent a major deficiency** <Update Summary of Deficiencies Template as required>		<Explanation>		
Evaluate the principle using judgment.**		Y/N	Explanation/Conclusion	
Is the principle present?		Y		
Is the principle functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the principle is not present and functioning and the system of internal control is not effective.

Principle 14: Communicates Internally

—The organization internally communicates information, including objectives and responsibilities for internal control, necessary to support the functioning of internal control.

Points of Focus

- **Communicates Internal Control Information**—A process is in place to communicate required information to enable all personnel to understand and carry out their internal control responsibilities.
- **Communicates with the Board of Directors**—Communication exists between management and the board of directors so that both have information needed to fulfill their roles with respect to the entity's objectives.
- **Provides Separate Communication Lines**—Separate communication channels, such as whistle-blower hotlines, are in place and serve as fail-safe mechanisms to enable anonymous or confidential communication when normal channels are inoperative or ineffective.
- **Selects Relevant Method of Communication**—The method of communication considers the timing, audience, and nature of the information.
- (Other entity specific points of focus, if any)

Summary of Controls to Effect Principle 14

- **Financial Training:** Finance Orientation, Finance Academy, and annual trainings are held to update staff on the latest government practices, processes, and procedures. Training has continued while majority of DoF telecommutes through the use of virtual trainings offered from professional organizations like GFOA, CSMFO, IIA, and Skillpath.

- **Internal Financial Statement Checklists:** helps communicate expectations and ensures that statements are complete and accurate. Comprehensive accounting and disclosure checklists developed by GFOA are used to ensure compliance with governmental standards.

- **Formal distribution of work documents** are used to communicate specific responsibilities for development of the Comprehensive Annual Financial Report.

- **Fraud, Waste, and Abuse Hotline** serves as a safe mechanism to enable anonymous or confidential communication.

- **Internal Financial Reports:** City Auditor reports, Independent Budget Analyst reports, management policies and administrative regulations, annual budget, Five-Year Financial Outlook, monthly Charter 39 Financial Performance Reports, and budget monitoring quarterly reports provide management, City Council and Audit Committee information.

Identification No.	Internal control deficiency description	Evaluate preliminary deficiency severity: (Consider whether other controls to effect this principle compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Preliminary Severity—Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Evaluate deficiencies within the principle:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered within the principle, represent a major deficiency** <Update Summary of Deficiencies Template as required>		<Explanation>		
Evaluate the principle using judgment.**		Y/N	Explanation/Conclusion	
Is the principle present?		Y		
Is the principle functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the principle is not present and functioning and the system of internal control is not effective.

Principle 15: Communicates Externally

—The organization communicates with external parties regarding matters affecting the functioning of internal control.

Points of Focus

- **Communicates to External Parties**—Processes are in place to communicate relevant and timely information to external parties including shareholders, partners, owners, regulators, customers, and financial analysts and other external parties.
- **Enables Inbound Communications**—Open communication channels allow input from customers, consumers, suppliers, external auditors, regulators, financial analysts, and others, providing management and the board of directors with relevant information.
- **Communicates with the Board of Directors**—Relevant information resulting from assessments conducted by external parties is communicated to the board of directors.
- **Provides Separate Communication Lines**—Separate communication channels, such as whistle-blower hotlines, are in place and serve as fail-safe mechanisms to enable anonymous or confidential communication when normal channels are inoperative or ineffective.
- **Selects Relevant Method of Communication**—The method of communication considers the timing, audience, and nature of the communication and legal, regulatory, and fiduciary requirements and expectations.
- (Other entity specific points of focus, if any)

Summary of Controls to Effect Principle 15

- **Annual Report on Financial Internal Controls:** The Internal Controls Section releases an annual report to summarize management's approach in maintaining the City's internal controls system provides reasonable assurance that financial reporting objectives are met.

- **Policies and Procedures:** Financial policies and ARs posted on the City's website to communicate information to external parties.

- **City Auditor Risk Assessment and Audit Reports:** City Auditor completes a citywide risk assessment to help identify, measure, and prioritize the City's potential audits based on the level of risk to the City.

- **Comprehensive Annual Financial Report Risk Assessment:** At the beginning of each Comprehensive Annual Financial Report preparation cycle, management communicates areas of potential risk to City's external auditor based on management's risk assessment and ongoing monitoring activities.

- **External Reports:** such as the Comprehensive Annual Financial Report, financial policies, and administrative regulations are shared on the City's website to be accessed by residents, investors, rating agencies, and other interested parties.

- **The Disclosures Practices Working Group (DPWG):** includes individuals in key City positions within the City and external counsel that can review disclosures, communicate known facts, and relevant information and ensure consistency throughout the city's financial disclosure documents. The DPWG has formal disclosure controls and procedures.

- **Bond rating agency interviews and Offering Statements:** The City prepares a Preliminary Official Statement (POS) that contains all material information to help investors determine whether to purchase securities offered by the City. The DPWG reviews the statement before City Council approval of a public debt issuance and its related disclosure document. The City also conducts presentations with ratings agencies prior to marketing new securities. The DPWG is required to review all materials that the City presents to bond rating agencies and investors.

- **Fraud, Waste, and Abuse Hotline:** serves as a safe mechanism to enable anonymous or confidential communication.

- **Communication with external parties regarding assessments:** The City's external auditor, Macias, Gini & O'Connell LLP, reviews the City's financial statements and accompanying notes and reports on any findings during the audit process. City financial information is communicated to external auditor through a master pending list.

Deficiencies Applicable to Principle 15

Identification No.	Internal control deficiency description	Evaluate preliminary deficiency severity: (Consider whether other controls to effect this principle compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Preliminary Severity—Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Evaluate deficiencies within the principle:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered within the principle, represent a major deficiency** <Update Summary of Deficiencies Template as required>		<Explanation>		
Evaluate the principle using judgment.**		Y/N	Explanation/Conclusion	
Is the principle present?		Y		
Is the principle functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the principle is not present and functioning and the system of internal control is not effective.

Principle Evaluation—Monitoring Activities**Principle 16: Conducts Ongoing and/or Separate Evaluations**

—The organization selects, develops, and performs ongoing and/or separate evaluations to ascertain whether the components of internal control are present and functioning.

Points of Focus

- Considers a Mix of Ongoing and Separate Evaluations—Management includes a balance of ongoing and separate evaluations.
- Considers Rate of Change—Management considers the rate of change in business and business processes when selecting and developing ongoing and separate evaluations.
- Establishes Baseline Understanding—The design and current state of an internal control system are used to establish a baseline for ongoing and separate evaluations.
- Uses Knowledgeable Personnel—Evaluators performing ongoing and separate evaluations have sufficient knowledge to understand what is being evaluated.
- Integrates with Business Processes—Ongoing evaluations are built into the business processes and adjust to changing conditions.
- Adjusts Scope and Frequency—Management varies the scope and frequency of separate evaluations depending on risk.
- Objectively Evaluates—Separate evaluations are performed periodically to provide objective feedback.
- (Other entity specific points of focus, if any)

Summary of Controls to Effect Principle 16

- **Segregation of Duties Monitoring:** The City ensures that no one individual has control over an entire process through SAP GRC module and Business Role Management (BRM).

- **Assessment of Documented Processes and Controls:** Periodic evaluation for process design to test for validity, accuracy, and performance of the process as documented and control design assessments to test presence and performance of controls that have been identified within the process. In 2020, the DoF developed a control risk-based approach to assess process documentation. The designed control risk-based approach is used to prioritize and select process documentations for the periodic assessment.

- **Ongoing Monitoring:** Management conducts monitoring of the following transactions to ensure compliance with objectives: procurement card, travel and tuition, jury duty leave requests, invoices, journal entries, purchase order splitting, and vendor business licenses. A new monitoring test to verify electronic banking changes requested by vendors is being developed.

- **Aging Good Receipts (GR):** A new monthly review of outstanding GRs are conducted to ensure posted GRs are not duplicates or posted in error.

Deficiencies Applicable to Principle 16

Identification No.	Internal control deficiency description	Evaluate preliminary deficiency severity: (Consider whether other controls to effect this principle compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Preliminary Severity—Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Evaluate deficiencies within the principle:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered within the principle, represent a major deficiency** <Update Summary of Deficiencies Template as required> Evaluate the principle using judgment.**		<Explanation>		
		Y/N	Explanation/Conclusion	
Is the principle present?		Y		
Is the principle functioning?		Y		

* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the principle is not present and functioning and the system of internal control is not effective.

Principle 17: Evaluates and Communicates Deficiencies

—The organization evaluates and communicates internal control deficiencies in a timely manner to those parties responsible for taking corrective action, including senior management and the board of directors, as appropriate.

Points of Focus

- **Assesses Results**—Management and the board of directors, as appropriate, assess results of ongoing and separate evaluations.
- **Communicates Deficiencies**—Deficiencies are communicated to parties responsible for taking corrective action and to senior management and the board of directors, as appropriate.
- **Monitors Corrective Actions**—Management tracks whether deficiencies are remediated on a timely basis.
- (Other entity specific points of focus, if any)

Summary of Controls to Effect Principle 17

- **City Auditor Performance Audit Reports:** City management reviews and monitors audits performed by City Auditor and works with departments to strengthen controls.

- **Independent Audit Review:** Managements reviews the results of independent audit from MGO to identify potential areas of risks or areas for which controls need to be strengthened. Chief Compliance Officer and City Auditor monitors corrective actions have been completed through follow-up reports and status meetings. The DoF also works closely with departments to modify processes, establish new controls, or strengthen existing controls as it relates to financial reporting.

- **Comprehensive Annual Financial Report Review:** The DoF conducts an internal review of the preparation and completion of the Comprehensive Annual Financial Report to identify entries that occurred after the draft was submitted to external auditor.

- **Comprehensive Annual Financial Report Corrective Actions:** CFO committed to strengthening controls in Comprehensive Annual Financial Report reporting and completed 7 improvements on a timely basis.

Identification No.	Internal control deficiency description	Evaluate preliminary deficiency severity: (Consider whether other controls to effect this principle compensate for the internal control deficiency.)		List internal control deficiencies related to another principle that may impact this internal control deficiency
		Preliminary Severity—Is internal control deficiency a major deficiency? (Y/N)	Comments/Compensating Controls	
Evaluate deficiencies within the principle:* Evaluate if any internal control deficiencies or combination of internal control deficiencies, when considered within the principle, represent a major deficiency** <Update Summary of Deficiencies Template as required>		<Explanation>		
Evaluate the principle using judgment.**		Y/N	Explanation/Conclusion	
Is the principle present?		Y		
Is the principle functioning?		Y		

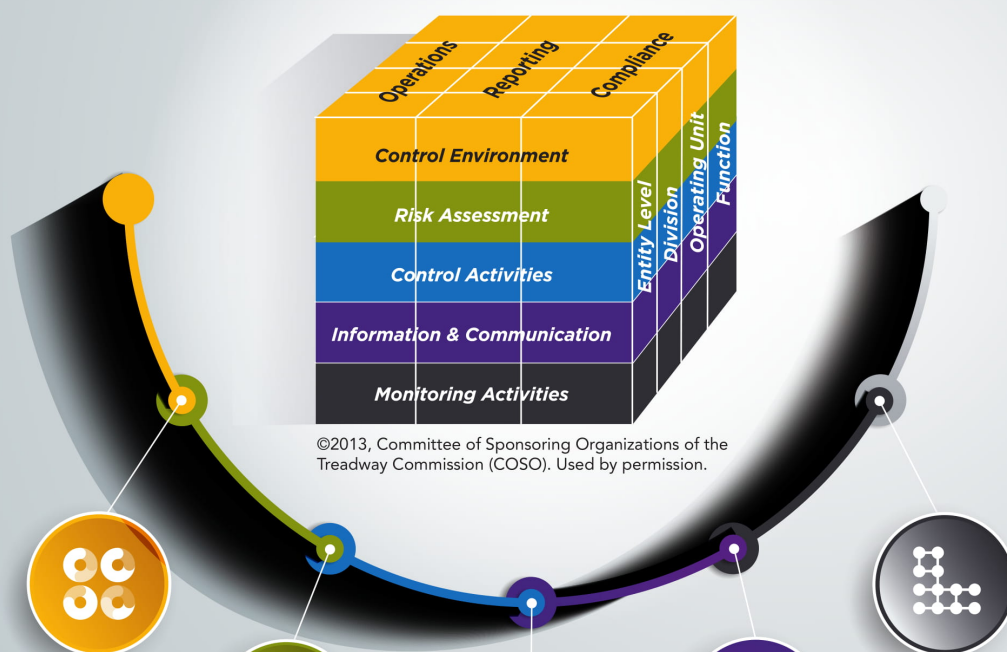
* Note: Record deficiencies in Summary of Deficiencies Template.

** If it is determined that there is a major deficiency, management must conclude that the principle is not present and functioning and the system of internal control is not effective.

4. Summary of Deficiencies

Summary of Deficiencies						
ID #	Source of the internal control deficiency		Internal Control Deficiency Description	Is internal control deficiency a major deficiency? (Y/N)	Owner	Remediation Plan and Date
	Component	Principle				
Performance Audit of the City's Strategic Human Capital Management	Control Environment	#4	Widespread uncompetitive compensation poses a growing shorthand long term risk to the City's ability to maintain and attract a high-quality workforce for providing public services, and has likely contributed to several negative effects on the City workforce and public services.	N	Several Departments	City agreed to auditor recommendations in their HCM report including creating a Total Compensation Strategy; City uses special salary adjustments process to maintain competitive hiring; financial training program offered to entry level and experienced finance staff citywide; increase in documentation to preserve institutional knowledge.
Performance Audit of the City's Strategic Human Capital Management II: Employee Performance Management	Control Environment	#4, 5	Employee performance can have an impact on an organization's environment and capability in providing high-quality public services. The City could improve its ability to effectively identify or address poor performance or misconduct issues and show employee appreciation and recognition to help engage employees and drive them to continue commendable performance. Otherwise, it could affect the City from providing high-quality public services for its customers and have an impact on other employee's performance and the city environment.	N	Human Resources & Personnel Departments	To mitigate some of these effects and help the City strengthen its capability to have an engaged workforce, management agreed to these key recommendations: report Employee Performance Review completion rates in the City's annual workforce report, review and monitor the Rewards and Recognition Program, strategically monitor aggregate discipline trends, and expand disciplinary processes and discipline-related training for supervising employees.

COSO Internal Control — Integrated Framework Principles



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Control Environment

- 1 The organization demonstrates a commitment to integrity and ethical values.
- 2 The board of directors demonstrates independence from management and exercises oversight of the development and performance of internal control.
- 3 Management establishes, with board oversight, structures, reporting lines, and appropriate authorities and responsibilities in the pursuit of objectives.
- 4 The organization demonstrates a commitment to attract, develop, and retain competent individuals in alignment with objectives.
- 5 The organization holds individuals accountable for their internal control responsibilities in the pursuit of objectives.

Risk Assessment

- 6 The organization specifies objectives with sufficient clarity to enable the identification and assessment of risks relating to objectives.
- 7 The organization identifies risks to the achievement of its objectives across the entity and analyzes risks as a basis for determining how the risks should be managed.
- 8 The organization considers the potential for fraud in assessing risks to the achievement of objectives.
- 9 The organization identifies and assesses changes that could significantly affect the system of internal control.

Control Activities

- 10 The organization selects and develops control activities that contribute to the mitigation of risks to the achievement of objectives to acceptable levels.
- 11 The organization selects and develops general control activities over technology to support the achievement of objectives.
- 12 The organization deploys control activities through policies that establish what is expected and procedures that put policies into action.

Information & Communication

- 13 The organization obtains or generates and uses relevant, quality information to support the functioning of internal control.
- 14 The organization internally communicates information, including objectives and responsibilities for internal control, necessary to support the functioning of internal control.
- 15 The organization communicates with external parties regarding matters affecting the functioning of internal control.

Monitoring Activities

- 16 The organization selects, develops, and performs ongoing and/or separate evaluations to ascertain whether the components of internal control are present and functioning.
- 17 The organization evaluates and communicates internal control deficiencies in a timely manner to those parties responsible for taking corrective action, including senior management and the board of directors, as appropriate.

For more information about COSO, visit coso.org.

**Independent Auditor's Report on Internal Control Over Financial Reporting and on
Compliance and Other Matters Based on an Audit of Financial Statements
Performed in Accordance With *Government Auditing Standards***

To the Honorable Mayor and Members of the City Council
City of San Diego, California

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of San Diego, California (the City), as of and for the fiscal year ended June 30, 2020, and the related notes to the financial statements, which collectively comprise the City's basic financial statements, and have issued our report thereon dated December 21, 2020. Our report includes a reference to other auditors who audited the financial statements of the San Diego Housing Commission, a discretely presented component unit, as described in our report on the City's basic financial statements. This report does not include the results of the other auditor's testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the City's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in dark ink that reads "Macias Gini & O'Connell LLP". The signature is written in a cursive, flowing style.

San Diego, California
December 21, 2020