



FINAL REPORT

City of Stockton
CITYWIDE INTERNAL CONTROLS REVIEW

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Table of Contents

I. Executive Summary	1
A. Scope and Methodology	1
II. Background, Scope, and Methodology	3
A. Background	3
B. Scope and Methodology	3
III. Internal Controls Review	5



I. EXECUTIVE SUMMARY

A. SCOPE AND METHODOLOGY

The City of Stockton (the City) engaged its internal auditor, Moss Adams LLP (Moss Adams, we, our), to perform an evaluation of the City's internal controls framework. The internal controls review took place between April 2023 and February 2024. There were multiple delays that occurred which caused the project duration to be longer than our initial expectation. The internal controls review focused on assessing select key controls in areas deemed important to protecting the City's assets and resources and to processing and reporting timely financial information.

The review of internal controls was completed in accordance with Standards for Consulting Services established by the American Institute of Certified Public Accountants (AICPA). As such, this work was not an audit of internal controls that resulted in a formal opinion or other form of assurance.

We reviewed the City's internal controls for design but did not test those controls for operating effectiveness. Specific areas where controls were reviewed included:

- Accounts Receivable
- Cash Management
- Financial Reporting, Close, and Reconciliations
- Fixed Assets and Asset Management
- Inventory
- IT General Controls
- Overall Control Environment
- Purchasing and Accounts Payable
- Revenue and Billing

During the planning of this engagement, the City was in the process of implementing the new payroll enterprise resource system and internal controls around this area would be changing. As such, we did not review payroll internal controls, which should be reviewed at another time.

The City appeared to have internal controls developed for many functions and was in the process of implementing internal controls for other functions. Some examples of commendable activities include:

- Monitoring and reconciliation controls related to:
 - Accounts Receivable
 - Cash Management
 - Financial Reporting, Close, and Reconciliations
 - Fixed Assets and Asset Management
 - Inventory
 - Purchasing and Accounts Payable
 - Revenue and Billing
- Monthly and quarterly review of budgets by department supervisors



- Monitoring IT service requests to mitigate the risk of requests being inactive
- Reviewing purchase card users and user activity

Similar to most cities, there is an opportunity to strengthen policies, procedures, systems, and training. Gaps in internal controls of varying degrees were discovered in several of the functions reviewed, especially in the case of decentralized operations.

The primary conclusion from this review is that the City has an opportunity to improve internal controls and strengthen processes and procedures. Suggested priorities to address over the next six to 12 months include, but are not limited to:

- Accounts Receivable
 - Documenting reviews and approvals for reconciliations and aging reports
 - Updating policies and procedures
- Financial Reporting, Close and Reconciliations
 - Timelier reviews for month-end, quarter-end, and year-end closing journal entries
 - Updating policies and procedures
- Fixed Assets and Asset Management
 - Updating policies and procedures
- Purchasing and Accounts Payable
 - Updating policies and procedures
- Revenue and Billing
 - Reviewing and approving invoices before sending to customers



II. BACKGROUND, SCOPE, AND METHODOLOGY

A. BACKGROUND

The City engaged its internal auditor, Moss Adams, to perform an evaluation of the City's internal controls framework and to identify opportunities for improvement that exist across City functions. The last internal controls review for the City was performed during fiscal year 2017-2018, which included reviewing controls in the following areas:

- Payroll and Timekeeping
- Cash Handling
- Procurement and Accounts Payable
- Monthly Close and Reconciliation

In the 2017-2018 internal controls review, we identified significant gaps in internal controls for all four of the areas assessed including a lack of defined policies and procedures, lack of thorough reviews, and lack of documented approvals. Since the time of that review, the City's management has been committed to making improvements and instilling a strong internal controls environment including a focus on updating/expanding policies and procedures, implementing monitoring and reconciliation controls in key financial areas, and ensuring proper segregation of duties.

B. SCOPE AND METHODOLOGY

The scope of our review included a high-level evaluation of the City's key internal controls to determine the general adequacy of enterprise internal controls and identify areas warranting more in-depth review in the future.

The scope of the internal controls review included the following functional areas:

- Accounts Receivable
- Cash Management
- Financial Reporting, Close, and Reconciliations
- Fixed Assets and Asset Management
- Inventory
- IT General Controls
- Overall Control Environment
- Purchasing and Accounts Payable
- Revenue and Billing

For each functional area assessed, we conducted a review of key controls which included:

- Identifying control objectives in specific areas and controls that would satisfy each control objective
- Reviewing policies and procedures (P&Ps)
- Examining relevant documentation in support of select key controls



- Performing control walkthroughs to observe the design of key controls and understand workflow processes
- Obtaining an understanding of the characteristics of each relevant control activity (who performs it, how often it is designed to operate, whether it is designed to mitigate the risk of fraud, whether it is a manual or programmed/automated control, and whether it is a preventive, detective, or corrective control)
- Assessing whether the controls in place would prevent or detect errors
- Providing recommendations on key controls that need to be implemented or changed

The work performed included interviews with personnel involved in managing functions, processing and approving key accounting transactions, and handling physical assets in the following departments:

- Finance
- Information Technology

In support of the internal controls review, the matrix provided in Section III provides results for each key functional area reviewed and presents the:

- Control objective
- Control issue
- Corresponding recommendation
- Likelihood of occurrence
- Impact of occurrence

Likelihood of occurrence is defined as the probability of a negative event occurring. Impact of occurrence is defined as the level of significance if a negative event occurs. Risk levels of low, moderate, or high were used to rate the likelihood and impact of occurrence for each finding.

Beyond those controls that have been noted within this report as an issue, additional controls were reviewed without exception. It should be noted that many controls were reviewed multiple times in relevant, separate department reviews, but not all controls or departments were reviewed. Departments were selected to provide a broad understanding of the City's control environment. Key controls with exception conditions are reported in Section III of this report.



III. INTERNAL CONTROLS REVIEW

Control Objective		Control Issue	Recommendation	Likelihood of Occurrence	Impact of Occurrence
A. Accounts Receivable					
1	The Revenue Supervisor reviews and approves the A/R aging schedule.	The annual aging schedule for the period of July 1, 2022, through June 30, 2023, was not formally reviewed and approved, which could lead to not identifying vendors with overdue invoices that need to be sent through the collections process.	<p>A/R management should establish a process to formally review and approve A/R aging schedules. A formal approval might be made via the City's A/R system, email, or physical sign-off.</p> <p>The review should be detailed to identify specific vendors that are late on payment, to allow the City to easily identify which invoices need to be sent to collections.</p> <p>Additionally, the City should consider including a "comments" column in the aging schedule to include any relevant comments about past due balances (over 120 days) and any actions that are being taken to address these outstanding balances.</p>	High	Low
2	The City-wide P&Ps for billing and collection of A/R are well-documented and current.	The current A/R P&Ps are not comprehensive or complete, as they do not address all key functional areas of the A/R process. Specifically, the City's A/R P&Ps do not address key areas recommended by best practices including A/R tracking and reporting, systems access controls, allowance for doubtful accounts and bad debt management, or collection efforts including handling of past	<p>While the City does not appear to have control issues for the A/R process aside from the items above, it should formally document these processes via a City-wide P&P, which should be developed to include items such as:</p> <ul style="list-style-type: none"> • A/R management, including A/R tracking and reporting, aging analysis, and reporting on delinquent accounts • Systems access controls related to A/R management systems, to ensure proper segregation of duties 	Moderate	Moderate



	Control Objective	Control Issue	Recommendation	Likelihood of Occurrence	Impact of Occurrence
		due/delinquent accounts and write-offs.	<ul style="list-style-type: none"> ● Allowance for doubtful accounts establishment, recording of bad debt expenses, and criteria for estimate development ● Handling refunds and account credits, including required documentation and approvals ● Guidance to departments for developing their specific billing P&Ps, to ensure consistency and enhance revenue capture ● The criteria used to determine when a past due/delinquent account will be sent to a collection agency, and how revenue-collecting service providers will be engaged and monitored ● When account write-offs can occur, what approvals are required, and how write-offs/account adjustments must be documented and controlled <p>Departments that are responsible for collecting funds on the City's behalf should have department-specific procedures documented to ensure that billing and collection activities are performed consistently and in a controlled manner.</p>		
B. Cash Management					
1	Petty cash use aligns with applicable City and department-specific policies and procedures.	The Police Department's petty cash use appears to be for expenses that would typically be reimbursed to employees via payroll instead of reimbursed via cash.	We recommend the City review the Police Department's petty cash use to determine if the petty cash fund is being used as intended. Specifically, the City should consider reimbursing employees for expenses via payroll to limit the use of petty cash. Considering the inherently	High	Low



	Control Objective	Control Issue	Recommendation	Likelihood of Occurrence	Impact of Occurrence
			risky nature of cash, the petty cash fund should only be used when necessary and should only be used for small transactions (typically less than \$30 per the Petty Cash Fund Procedures).		
C. Financial Reporting, Close, and Reconciliations					
1	Month-end, quarter-end, and year-end closing journal entries are reviewed and approved by the Accounting Manager or Accounting Supervisor.	<p>Closing entries are entered and approved in Tyler Munis; however, the entry was not performed timely. Specifically, following closing entries were not entered timely:</p> <ul style="list-style-type: none"> Journal Reference 47 for monthly closure of Bankcard fees for February 2023 had an entry date of May 10, 2023. Journal Reference 6 for monthly closure of sales tax on credit card purchases for February 2023 had an entry date of June 27, 2023. 	<p>The City should review the process for entering closing entries to ensure entries are able to be reviewed and approved timely within the close of the reporting period. Timely entries and approvals are essential to promote the overall accuracy of financial reporting and to ensure management is aware of the City's financial position.</p> <p>For month-end and quarterly close entries, entries and approvals should occur within approximately two weeks from the end of the period depending on when supporting documentation is available, such as the monthly bank statement.</p> <p>For year-end close entries, approvals should occur approximately three weeks from the end of the period.</p>	Moderate	Moderate
2	Month-end, quarter-end, and year-end journal entry logs are complete, with details supporting the closing entries.	Month-end, quarter-end, and year-end journal entry logs are completed; however, the level of detail, justifying the purpose of each closing entry, is not consistent. The inconsistent detail might cause confusion on the purpose of journal entries that do not include the level of detail that other journal entries do.	Journal entry reviewers should perform thorough reviews of journal entry forms and supporting documentation to ensure the level of detail is sufficient to justify the purpose of the closing entry. The reviews should ensure the legends, notes, and descriptions are consistently completed.	Low	Low



	Control Objective	Control Issue	Recommendation	Likelihood of Occurrence	Impact of Occurrence
3	The City-wide P&Ps for financial reporting, close, and reconciliation are well-documented and current.	The current financial reporting, close, and reconciliation P&Ps are not comprehensive or complete, as they do not address all key functional areas of the financial reporting, close, and reconciliation process. Specifically, the City's financial reporting, close, and reconciliation P&Ps do not address key areas recommended by best practices including chart of accounts setup, timelines and responsibilities for month-end and year-end close, financial monitoring and reviews, and reconciliation processes.	<p>While the City does not appear to have control issues for the financial reporting, close, and reconciliation process aside from the items above, it should formally document these processes via a City-wide P&P, which should be developed to include items such as:</p> <ul style="list-style-type: none"> ● Chart of accounts setup and General Ledger maintenance ● Fund accounting and reporting ● Cost allocation, classification, and tracking ● Month-end and year-end detailed closing procedures, including timelines, responsibilities, and details ● Financial monitoring and reviews ● Reconciliations, including details on specific accounts, variance analysis, segregation of duties, responsibilities, reviews, and approvals ● Financial reporting, including frequency, trend analysis, City Council reporting, and management oversight ● Audit coordination and oversight, and monitoring of findings 	Moderate	Moderate
D. Fixed Assets and Inventory					
1	The Accounting Manager or Accounting Supervisor reviews and approves the fixed asset reconciliation at year-end.	The City provided the capital asset roll forward, which confirmed the balance of asset categories; however, it is not a complete listing and inventory of all capitalized assets across the City, which is what this control pertains to. An asset count at	The City should update the fixed asset reconciliation process to include a detailed listing of all capitalized assets inventoried, to help ensure asset accuracy, asset condition, and interdepartmental transparency. Some	Moderate	Low



	Control Objective	Control Issue	Recommendation	Likelihood of Occurrence	Impact of Occurrence
		<p>year-end serves to confirm the assets that the City has on-hand as well as the status and condition of each asset.</p> <p>Additionally, the fixed asset reconciliation for the year ending June 30, 2022 was not reviewed and approved timely, as it was not approved until January 23, 2023.</p>	<p>details to include in the listing are as follows:</p> <ul style="list-style-type: none"> ● Asset ID ● Purchase date ● Asset value ● Depreciation ● Status/condition <p>We recommend the City review the fixed asset reconciliation process to ensure timely review and approval at year-end.</p>		
2	<p>The Accounting Supervisor reviews and approves capital asset disposals before sending to City Council for final approval.</p>	<p>The City provided City Council's approval to dispose of assets in March 2023, but we did not observe Accounting Supervisor review and approval prior to sending to City Council. Having the Accounting Supervisor review and approve the proposed disposals helps to verify that the proper assets are listed and are truthfully ready to be disposed.</p>	<p>The City should confirm each asset disposal is reviewed and approved, prior to submission to City Council. Specifically, the Accounting Supervisor should ensure the following for each asset scheduled to be disposed of:</p> <ul style="list-style-type: none"> ● Status in Tyler Munis ● Accurate depreciation ● Updated inventory ● Custody <p>While the City Council's approval is sufficient for the disposal, it does not ensure that the proper assets have been listed for disposal.</p>	Low	Moderate
3	<p>The City-wide P&Ps for fixed assets and asset management are well-documented and current.</p>	<p>The City's Administrative Directive for Asset Accountability – Capital Assets has not been updated since 2007, which poses a risk that current policies and/or procedures do not match the outdated Administrative Directive. In addition, the Administrative Directive does not</p>	<p>The City should review the Administrative Directive for Asset Accountability – Capital Assets and make updates, as needed, to reflect current policies and procedures. Having an updated Administrative Directive will help to ensure that employees across departments understand the basics of</p>	High	Moderate



	Control Objective	Control Issue	Recommendation	Likelihood of Occurrence	Impact of Occurrence
		address key areas of the capital asset function.	capital asset management. While the City does not appear to have control issues for the fixed asset and inventory process aside from the items above, it should formally document these processes via a City-wide P&P, which should be developed to include items such as: <ul style="list-style-type: none"> ● Accounting and reporting fixed assets (including vehicles, equipment, property, and other fixed assets) ● Cost criterion ● Capitalization thresholds ● Depreciation ● Methods of disposition ● Transfers ● Idle and surplus assets ● Accountability for assets ● Repairs and maintenance ● Physical inventory procedures ● Fixed asset listing 		
E. IT General Controls					
1	The City-wide P&Ps for IT asset disposals are well-documented and current.	The City does not currently have a policy in place relating to disposing of IT assets, although they are working to create a policy for this area.	A defined policy will help formalize and standardize these processes to allow for safe and secure disposal of IT assets. While the City does not appear to have control issues for the IT disposal process, it should formally document these processes via a City-wide P&P, which should be developed to include items such as: <ul style="list-style-type: none"> ● Roles and responsibilities ● Disposal methods 	High	Low



Control Objective		Control Issue	Recommendation	Likelihood of Occurrence	Impact of Occurrence
			<ul style="list-style-type: none"> Security measures Compliance with applicable regulations Documentation and reporting 		
2	A formal Disaster Recovery Plan (DRP) is documented, implemented, and tested.	There is a written policy for a DRP, but it has not been updated in approximately five years and the DRP is not formally tested.	The City's documented DRP should be formally tested and updated, if needed. Testing should be documented and the results should be addressed. The DRP should be evaluated, updated, and tested regularly to ensure that it addresses the City's current environment and systems and the City is prepared in the event of a major disaster.	Moderate	High
F. Purchasing and Accounts Payable					
1	The Procurement Department compiles purchasing data into a spreadsheet and reviews the data for purchasing trends.	The City has demonstrated that it can query the purchasing trends report; however, the review of that report is not formally documented.	The City should update the process for reviewing and approving the purchasing trends report to support budgeting, forecasting, and decision-making, and evaluate for any unusual trends that warrant a deeper review. Reviews that occur should be formally documented.	Low	Low
2	The City-wide P&Ps for procurement are well-documented and current.	<p>The due diligence thresholds defined in the Informal Procurement Policy and General Procurement Policy differ from what was told to us during interviews, which might indicate a lack of understanding of the policy or that the policies are not current. During interviews performed, we were informed of the following due diligence thresholds:</p> <ul style="list-style-type: none"> Purchases \$10,000 and below require one quote 	The City should review its Informal Procurement Policy and General Procurement Policy and make updates to due diligence thresholds as needed to match current practices. If the policies are correct, the City should consider conducting a training for procurement staff to ensure they understand and adhere to the policies.	Moderate	Moderate



	Control Objective	Control Issue	Recommendation	Likelihood of Occurrence	Impact of Occurrence
		<ul style="list-style-type: none"> ● Purchases over \$10,000 up to \$100,000 require a minimum of three quotes ● Purchases over \$100,000 require formal solicitation and City Council approval <p>The Informal Procurement Policy and General Procurement Policy state:</p> <ul style="list-style-type: none"> ● Purchases up to \$4,999 require one quote ● Purchases between \$5,000 and \$75,000 require a minimum of three quotes ● Purchases \$75,000 and above require formal solicitation and City Council approval 			

