



MEMO

To: Lea Dunn, City Manager; Cheryl Delaney, Deputy City Manager
From: Eric Cannon, CPA, Chief Financial Officer
Re: Financial Update
Date: February 5, 2015

For your information and review, the following is a summary of the Town's progress in addressing the various initiatives provided within the COSO framework. In addition to the summary, a glossary of terms is provided for the reader's benefit as well as a high level summary of all the controls that are currently in place, the items that are to be implemented and the time line for implementing those items.

Payroll: Control Activities:

- **Segregation of duties**
- **IT general controls**
- **Financial Policies**

Over the past several months a considerable amount of work related to the Town's payroll process has been implemented. Specifically this includes transferring staff members to other departments in the organization and redefining employee responsibilities to ensure proper segregation of duties; limiting system access to the employee master file, migrating all treasury components to the secure "Cash Manager" system provided by Frost Bank and adding additional mitigating controls. Staff plans to have both Gradient Solutions and Weaver review the revised processes to ensure that it addresses the COSO framework.

In addition staff investigated the outsourcing of the payroll function. After visiting with several vendors, staff requested that ADP quote on two different options: Option 1 – provide for the outsourcing of the Town's check processing function and Option 2: fully integrate ADP payroll function.

Both options were developed to be in compliance with both municipal best practices and the COSO principals.

Option 1: Outsource check processing

The ten year cost for this option is \$129,000. This process would remove the printing responsibilities from the Town but would still require a staff member to coordinate the payroll function. Based on the cost and the fact that a dedicated staff member is required, staff does not recommend this option.

Option 2: Fully integrated ADP payroll function

The ten year cost to implement this option would be approximately \$1,500,000. This option would still require a dedicated payroll staff person. Based on cost, staff does not recommend this option.

Based on the costs associated with contracting with a third party vendor, the fact that a full time staff member is still required and the Town has implemented additional controls throughout the payroll process, staff recommends that the current payroll processes remain. Most importantly, efficiencies and additional controls will be realized with the implementation of the new ERP system.

Whistleblower Program: Control Environment

- **Transparency**

Recently the Town Finance staff completed a process in which they evaluated several companies that provide whistleblower programs. Based on the review, the decision was made to contract with Lighthouse Services. Lighthouse Services is an industry leader providing fraud and ethics hotline services. They service more than 1,000 organizations across the country as well as many Texas cities. The Town is in the process of implementing this program and anticipates it will be functional by the end of February. As part of this implementation, staff will include a comprehensive communication plan to inform employees and vendors about the program's purpose and how to access it.

The purpose of this program is to continue to define our control environment throughout the organization. Lighthouse Services is dedicated to providing its clients with confidential, anonymous reporting services. They help protect an organization's assets, board of directors, management, and employees. They are an independent third-party hotline provider, which ensures our employees will feel confident that their anonymity will be protected.

The sole focus of their business is compliance and ethics hotlines. Our comprehensive program with Lighthouse includes internal control and fraud reports, human resource complaints, and ethics and compliance violations.

Cash Receipting: Control Activities

- **Cash/Asset management & procedures**
- **Technology**

Dunbar cash vaults are set to be installed in the coming weeks. Site surveys have been completed at the identified locations; currently we are only waiting on the delivery of the equipment. This technology provides greater protection to our employees and enables the Town's Finance Department to reconcile the information more quickly.

Frost Digital Deposit machines have been installed at most Town locations. These machines allow for all checks to be processed and remitted to the bank electronically. By adding this technology we have removed inefficiencies that existed in our previous process. Most importantly, this technology has improved our collection cycle and increased our ability to collect funds.

The Town is also in the process of adding point of sale (POS) machines at various locations to provide the necessary treasury functions, but within the parameters established by the Finance Department. This technology is being added to ensure that Town staff is able to provide the necessary services while adhering to our control environment.

Inventory: Information and Communication, Monitoring

- **Financial Reporting**
- **Independent external audit**

We have awarded the bid to Records Consultants Inc. to complete the Town's inventory. Town staff is currently working to ensure that this process is successful and has as little impact on operations as possible.

Special Events: Information and Communication

- **Financial Reporting**
- **Technology**

Recently Council approved the hiring of a Senior Accountant. This position will be a key role in implementing some of the COSO initiatives as they relate to our Special Events.



Town of Addison

COSO Framework Model

February 2015 - Working Document

Committee of Sponsoring Organizations (COSO) Framework

Control Environment	Risk Assessment	Control Activities	Information and Communication	Monitoring
Sets the tone of an organization and serves as a foundation for all other components	Identifies and analyzes risks to achieving objectives. Determines how risk should be managed.	Encompass policies and practices along with process-level procedures that ensure management's directives are carried out.	Captures and exchanges relevant information to use as a basis for decision making. Also, effectively communicates roles and responsibilities for maintaining internal controls.	The ongoing assessment of internal control quality to assure controls are operating as intended.

Addison Strategy and Timeframe

Governance Oversight	Understanding Our Risk	Know What We Are Doing	Communicating to the Organization	How Are We Doing
In Place: Council's Vision GFOA Participation Job Descriptions & Market Analysis Mission Statement Organizational Chart Performance Evaluations Personnel policies & procedures Transparency	In Place: Annual business process review Attract and retain highly qualified financial personnel Management / Council Retreats Partnership with TML Risk Pool	In Place: Cash/asset management & procedures - Digital capture deposit Financial Policies IT general controls Manual and mitigating controls Opengov Procurement Manual Segregation of duties - Payroll Processing Technology	In Place: Financial Reporting Internal & external information Participative Budgeting Pre-audit meeting & external auditors Representation Letter from Management Review of internal controls & explanation to all departments Town-wide training and communication	In Place: Data analysis and sampling Independent external audit Monthly, quarterly, annual reviews

Planned Actions

Governance Oversight	Understanding Our Risk	Know What We Are Doing	Communicating to the Organization	How Are We Doing
Conduct Annual Financial Best Practices Workshops with Council and Management (Q2-2016) Develop Fraud Policy (2016) Ethics Training (Q3-2015) Municipal Court Financial Management Handbook for Texas Cities (2017) Whistle-blower Program (Q1-2015)	Business Process Review (Q1-2016) Evaluation of potential changes in risk associated with ERP (Q2-2015) Enterprise Risk Assessment (Q4-2015)	Capital asset reporting (2015) Cash Handling Training (Q2-2015) Cash management policy (Q1-2015) Purchasing/procurement enhancement (Q4- 2014) RFP for banking services (Q1-2015) RFP for investment services (Q4-2015)	Implementation of ERP (Q2-2015)	Internal Audit Procedures (Q1-2016)

* Dates listed throughout represent the inception or anticipated start of the project.

Glossary of Terms

A

Accrual Accounting – Recognition of the financial effects of transactions, events and circumstances in the period(s) when they occur regardless of when the cash is received or paid.

Appropriation – A legal authorization granted by a legislative body (City Council) to make expenditures and incur obligation for designated purposes.

Audit Standards – A set of systematic guidelines used by auditors when conducting audits on companies' finances, ensuring the accuracy, consistency and verifiability of auditors' actions and reports.

Accounting standards – Guidelines for financial accounting, such as how a city prepares and presents its income and expense, assets and liabilities. The Generally Accepted Accounting Principles is comprised of a large group of individual accounting standards.

B

Balance Sheet – The basic financial statement, which discloses the assets, liabilities and equities of an entity at a specific date in conformity with Generally Accepted Accounting Principles (GAAP).

Balanced Budget – Annual financial plan in which expenses do not exceed revenues.

Best Practices – A set of guidelines, ethics or ideas that represent the most efficient or prudent course of action.

Budget – A plan of financial operation embodying an estimate of proposed expenditures for any given period and the proposed means of financing them.

Business Process Review (BPR) – A process in which current business practices are evaluated for the purpose of identifying enhancements and opportunities for improvements; suggests how those processes should be modified to achieve maximum return and highest efficiency.

C

Capital Asset – A type of asset that is not easily sold in the regular course of a operations for cash and is generally owned for its role in contributing to the city's ability to serve customers; it is expected that the benefits gained from the asset will extend beyond a time span of one year. Typical capital assets include property and equipment.

Capital Outlays – Expenditures which result in the acquisition of or addition to fixed assets which are individually priced at more than \$5,000.

Contractual Services – The costs related to services performed for the Town by individuals, businesses, or utilities.

Control Activities – The policies, procedures, and practices that ensure management objectives are achieved and risk mitigation strategies are carried out.

D

Data Analysis – The process of systematically applying statistical and/or logical techniques to describe, illustrate, condense, recap, and evaluate data.

E

Encumbrances – Commitments related to unperformed contracts for goods and services used in budgeting. Encumbrances are not expenditures or liabilities, but represent the estimated amount of expenditures ultimately to result if unperformed contracts in process are completed.

Enterprise Resource Planning (ERP) – Business management software that is a suite of integrated applications that a government can use to collect, store, manage and interpret data.

Expenditures – Decreases in net financial resources. Expenditures include current operating expenses which require the current or future use of net current assets, debt service, and capital outlays.

F

Financial Policies – Policies related to the regulation, supervision, and oversight of the financial and payment systems.

Financial Reporting – The process of producing statements that disclose an organization's financial status to management and the governing body.

Fixed Assets – Assets of a long-term character, which are intended to continue to be held or used, such as land, buildings, improvements other than buildings, machinery and equipment.

Franchise – A special privilege granted by a government permitting the continuing use of public property, such as city streets, and usually involving the elements of monopoly and regulation.

Fund – A fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with all related liabilities and residual equities of balances, and charges therein, which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions or limitations.

Fund Balance – The difference between governmental fund assets and liabilities; also referred to as fund equity.

G

GAAP – Acronym for Generally Accepted Accounting Principles, which are a collection of rules and procedures that set the basis for the fair presentation of financial statements. The accounting and reporting policies of the Town conform to the GAAP applicable to state and local governments.

GASB – Acronym for Government Accounting Standards Board, an independent, non-profit agency responsible for the promulgation of accounting and financial reporting procedures for governmental entities.

Governmental Funds – Those funds through which most governmental functions typically are financed. The acquisition, use, and financial resources and the related current liabilities are accounted for through governmental funds (General, Special Revenue, Capital Projects, and Debt Service Funds).

GFOA – Acronym for Government Finance Officers Association. An association of public finance officials throughout the United States and Canada; includes federal, state/provincial, and local finance officials involved in planning, financing, and implementation of thousands of governmental operations in each of their jurisdictions; promotes the professional management of governmental financial resources by identifying, developing, and advancing fiscal strategies, policies, and practices for the public benefit.

I

Independent external audit – Periodic or ad hoc audit conducted by external, independent qualified accountant(s). Its objective is to determine, among other things, whether (1) the accounting records are accurate and complete, (2) prepared in accordance with the provisions of GAAP, and (3) the statements prepared from the accounts present fairly the organization's financial position, and the results of its financial operations.

Internal Controls – Processes for assuring achievement of an organization's objectives in operational effectiveness and efficiency, reliable financial reporting, and compliance with laws, regulations and policies.

M

Maintenance – The upkeep of physical properties in condition for use of occupancy. Examples are the inspection of equipment to detect defects and the making of repairs.

Market Analysis – A phase of marketing research conducted to determine the characteristics and extent of a market.

Mission Statement – A formal summary of the aims and values of a company, organization, or individual.

Modified Accrual Accounting – Accounting system in which revenues are recognized and recorded in the accounts when they are measurable, available and collectible in the fiscal year.

Modified Level of Service – A modified level of service represents an increase or decrease in a department's scope of service or funding levels. A modified level of service may be a request for additional funding submitted by a department during the budget process for new or expanding programs or services, or it may be the elimination of a position in a department. Modified levels of service are highlighted in the department narratives in alternate color text.

O

OpenGov – A web-based software that allows governments and citizens to access, explore, and share finance and budget information.

Operating Expenditure – Expenditure on an existing item of property or equipment that is not a capital expenditure.

P

Participative Budgeting – A budgeting process under which those people impacted by a budget are actively involved with the budget creation process.

Personnel Services – The costs associated with compensating employees for their labor.

P-Card – Acronym for procurement card, a Town-issued credit card which allows employees to make small purchases in a cost effective manner.

Purchase Order (PO) – A document which authorizes the delivery of specified merchandise or the rendering of certain services and the making of a charge for them.

R

Remote Capture Deposit – A system that allows a customer to scan checks remotely and transmit the check images to a bank for deposit, usually via an encrypted Internet connection.

Revenues – Increases in net financial resources. Revenues include the receipt of assets for goods sold or services provided in the current reporting period, intergovernmental grants, and interest income.

RFP – Acronym for request for proposal; a solicitation made often through a bidding process, by an agency or company interested in procurement of a commodity, service or valuable asset, to potential suppliers to submit business proposals.

S

Segregation of Duties – An internal control designed to prevent error and fraud by ensuring that at least two individuals are responsible for the separate parts of a task.

Special Revenue Fund – A fund used to account for the proceeds of specific revenue sources that are legally restricted or formally committed to expenditures for specified purposes.

T

Taxes – Compulsory charges levied by a government for the purpose of financing services performed for the common benefit. This term does not include specific charges made against particular persons or property for current or permanent benefits such as special assessment.

W

Working Capital – The amount of current assets which exceeds current liabilities.