



CITY OF WILMINGTON

Adjusting Journal Entries

Internal Audit Review

July 19, 2018

City Auditor's Office

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Highlights

Why We Did This Audit

The Internal Audit Department (IA) performed a scheduled Performance Audit of Adjusting Journal Entries. The audit was in accordance with the 2018 Internal Audit Plan.

Methodology

The objectives were met by reviewing prior year audits, testing of 16 non-internal service fund adjusting journal entries and their supporting documentation, reviewing the Accounting policy and procedure manual, reviewing government accounting best practices, and through discussions with Finance personnel.

Audit Review Committee:

Robert C. Johnson, Chair

Ciro Adams
Marchelle Basnight
Angelique Dennis
Bud Freel
Ronald Pinkett
Tanya Washington

Objective and Scope

As part of our audit plan, we conducted a Performance Audit of Adjusting Journal Entries for the period commencing July 1, 2016 and ending June 30, 2017. The objectives of the audit were to determine whether the operating procedures and internal controls provide adequate assurance that authorized transactions were processed completely and accurately; to determine whether entries were valid and appropriate; to determine that the business purpose underlying the transaction was valid; to determine that the entry was properly recorded in the general ledger; and to determine that the entry was properly recorded in the correct accounting period. IA believes that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

We conducted our audit in accordance with Generally Accepted Government Auditing Standards ("GAGAS"). These standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives.

Background

As of the date of the report, it is the City's practice to perform all necessary adjusting journal entries during the year-end financial close process. The financial close process includes a trial balance which is a snapshot of the City's income and expense statements as of September 30th. The trial balance is performed prior to the books being examined by the external auditors, and serves to detect any mathematical errors that have occurred in the City's double-entry accounting system. Once the trial balance is run and the total debits equal the total credits, the external auditors examine the City's financial statements. However, transactions classified improperly or those simply missing from the system {misstatements} could still be material accounting errors that would not be detected by the trial balance procedure. Any misstatements discovered by either the external auditors or the Department of Finance are counted as a finding as part of the annual audit of financial statements that is conducted by an external accounting firm. Findings related to journal entries were noted in the FY 2016 and FY 2017 single audits. A CAFR checklist is used to guide all accounting steps leading up to the closing of the City's financial books for each fiscal year. The trial balance is a critical step of the CAFR preparation process and marks the beginning of the City's external audit.

Key Statistics:

Deficiency	# of exceptions	% of population (16)
Untimely processing of standard journal entries	8	50%
Account did not undergo a documented dual review prior to the trial balance	6	38%
Lack of segregation of duty in journal entry and approval	5	31%
Policies are lacking with regard to the tested process	5	31%
Accounting Manager's journal entries were approved by a Senior Accountant instead of another member of financial management	4	25%
Insufficient supporting documentation of scanned journal entry	4	25%
Journal entry not scanned to TCM	1	6%

What we found

Key Findings

Following are key issues that resulted in a process/area to be risk rated a three or four. See **Attachment A** for the detail of these and all comments identified during the review.

Risk Ranking:

(See Attachment B for full rating definitions)

Process / Area	Process / Area Owner	1 Strong Controls	2 Controlled Effectively	3 Controlled - Improvement	4 Significant Improvement
Reconciliation	Roseanne Prado				✓
User Access	Roseanne Prado				✓
Policies and Procedures	Roseanne Prado Velda Jones Potter Patrick Carter			✓	
Record Retention	Roseanne Prado			✓	
Review & Approval Process	Roseanne Prado			✓	

Reconciliation

1. Controls need strengthening with regard to how the City prepares its Comprehensive Annual Financial Report (CAFR). The trial balance was run three times with noted errors, and 88% of the 16 adjusting journal entries tested occurred after the third run. 38% of the 16 journal entries tested were made on accounts that did not undergo a dual review prior to the trial balance being run. This indicates that management did not sufficiently validate the accuracy of the accounts prior to the close of the fiscal year and the beginning of the external audit.
2. Control weaknesses need improvement to ensure there is timely processing of standard journal entries. Fifty percent of journal entries tested were standard entries that occurred more than 30 days after the review completion date listed on the CAFR preparation checklist. The delay was caused by a lack of detailed, written close-out procedures for each account listed on the checklist.

User Access

3. User access controls need strengthening, due to an employee having the ability to enter, adjust, and post journal entries without the need for additional approvals.

Policies & Procedures

4. Controls for establishing necessary policies and procedures need strengthening. For 31.25% of journal entries tested, accounting steps were performed without reference to a documented accounting policy. Without a written policy to refer to, the City is at risk for inaccurate and inconsistent application of accounting procedures from year to year.
5. Based on a review of prior Adjusting Journal Entries audits, a lack of controls still exists surrounding detailed procedures for adjusting journal entries in the Accounting Manual. Procedures were not fully updated, as stated by management in their action plan. Journal entries appear to be “rubber stamped”, which is a prohibited practice in the manual.

Record Retention

6. Inconsistent controls exist with regards to scanning sufficient supporting documentation for non-standard journal entries. IAD was unable to determine the accuracy of twenty-five percent of the tested journal entries because they lacked sufficient, scanned supporting documentation.

Review & Approval Process

7. Controls need strengthening around the journal entry review and approval process. Twenty-five percent of journal entries tested were created by the Accounting Manager and approved by a Senior Accountant versus someone above the Manager approving the entries. For 31.25% of tested journal entries, segregation of duty did not occur.

Additional Observation

Management should consider offering regular Continuous Professional Education (CPE) opportunities to its accounting staff to ensure they remain abreast of changes in GAAP and government financial reporting rather than relying on the expertise of an external audit firm to ensure the accuracy of the City’s financial records.

Management Responses to Audit Recommendations

Summary of Management Responses

Recommendation #1: Accounting staff should fully validate and dual review each account prior to running the initial trial balance. Written procedures should be developed to ensure that each step of the validation process and the data to be reviewed for each account is captured.

Agree

Management response & action plan: Management responses were not received at the time of audit publication but will be provided by management at a later date.

Completion Date: TBD

Recommendation #2: Management should create detailed, written close-out procedures for each account and use them as a guide to create a monthly/quarterly processing schedule for standard journal entries. This will minimize the need for standard entries to be processed during the lengthy year-end closing process. The Department should also review AICPA closing cycle best practices for possible implementation by the City.

Agree

Management response & action plan: Management responses were not received at the time of audit publication but will be provided by management at a later date.

Completion Date: TBD

Recommendation #3: Management should review the employee's system permissions and only provide access to data as necessary for the employee to complete assigned work. Management should periodically review the system permissions of all employees, specifically when duties are shifted among staff.

Agree

Management response & action plan: Management responses were not received at the time of audit publication but will be provided by management at a later date.

Completion Date: TBD

Recommendation #4: Management should create policies for standard accounting procedures including, but not limited to the recording of deferred revenue extra duty pay, steps for the creation and accounting of capital leases, including required approvals and documentation, a written protocol for the review of net accounts, and the review process for automated accounting.

Agree

Finance Management response & action plan: Management responses were not received at the time of audit publication but will be provided by management at a later date.

Completion Date: TBD

Recommendation #5: The Department should follow Policies and Procedures Documentation best practices as discussed by GFOA. The manual should also provide step-by-step procedures for the journal entry process from the initial adjustment request to its entry to the general ledger.

Agree

Management response & action plan: Management responses were not received at the time of audit publication but will be provided by management at a later date.

Completion Date: TBD

Recommendation #6: The Accounting Procedure Manual should be updated to clearly define the criteria for "reasonable" supporting documentation, specifically for non-standard transactions. An established criterion should create a consistent standard and assist supervisors during the dual review process. Journal entries containing data from a third party should be supported by the documentation provided by the third party.

Agree

Management response & action plan: Management responses were not received at the time of audit publication but will be provided by management at a later date.

Completion Date: TBD

Recommendation #7: Journal entries made by management should be approved by another member of management or a Finance employee with higher authority. The Division should create a detailed policy regarding the approvals that properly indicate segregation of duty, whether it is the electronic workflow approval, the w signatures on the journal entry form, or both.

Agree

Management response & action plan: Management responses were not received at the time of audit publication but will be provided by management at a later date.

Completion Date: TBD

Audit Team

Yvette R. Johnson, Senior Auditor
Tamara Thompson, Audit Manager