
MAY 22, 2017

4:15 – 5:30 pm

MODERATOR/SPEAKER
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SPEAKERS
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#GFOA2017
Part I: Accounting Operations & Controls
DISCLAIMER and Notes

• All views expressed herein are solely those of the speaker, and do not necessarily reflect those of GFOA, The City of New York, The Comptroller of the City of New York, or any other person, institution or organization with which the speaker may be associated.

• Not all of GFOA’s Best Practices on Accounting, Auditing and Financial Reporting are specifically addressed, due to time limitations.

• GFOA also has Advisories on its websites along with Best Practices, but only the Best Practices are included in this presentation.
GFOA ACCOUNTING, AUDITING AND
FINANCIAL REPORTING BEST
PRACTICES

• 35 in total (at last count)

• GFOA uses four overlapping categories:
  • Accounting (14)
  • Auditing (10)
  • Financial Reporting (12)
  • Internal Control (6)

• For this session, using three mutually exclusive categories:
  • Accounting Operations & Controls (18)
  • Grants (4)
  • Reporting (13)
Internal Control
Internal Control From the Ground Up

1. Establishing a Comprehensive Framework for Internal Control
2. Framework for Internal Control – The Control Environment
3. Framework for Entity-wide Grants Internal Control*
4. Getting Management Involved in Internal Control
5. Documenting Accounting Policies and Procedures
6. Encouraging and Facilitating the Reporting of Fraud and Questionable Accounting and Auditing Practices
7. Establishing an Internal Audit Function
8. Practical Steps to Avoid, Limit, or Eliminate Internal Control Deficiencies
Internal Control

• A **process** designed to provide reasonable assurance regarding the achievement of an organization’s objectives.

• Necessary to provide governments a reasonable basis for asserting (and believing!) they are **meeting their Operational, Reporting, and Compliance objectives**

• Operational Objectives:
  • Effectiveness
  • Efficiency
  • Safeguarding of Assets

• GFOA Recommends that state and local governments adopt …
COSO

• Committee of Sponsoring Organizations (COSO) Internal Control – Integrated Framework originally issued in 1992 and expanded in 2013

• Framework composed of five (5) essential Components, seventeen (17) Principles and many Points of Focus

• Essential Components:
  1. Control Environment
  2. Risk Assessment
  3. Control Activities
  4. Information and Communications
  5. Monitoring Activities
Great Visual !!!  [Courtesy of COSO]

Three kinds of Objectives

Organizational Structure

Five Components
First and Foremost: Control Environment

- A set of standards, processes and structures that provide the basis for carrying out internal control
- The governing body (elected and appointed officials), upper level management, and all levels of staff should **demonstrate a commitment** to achieving operational, reporting and compliance objectives
- The Governing body should **assume responsibility** for overseeing internal control
- Management should
- Ensure staff accountability by:
  - Formalizing organizational charts
  - Requiring (and maintaining!) written procedures for important processes, incorporating control activities, process flowcharts, workflow approvals
Control Environment (cont.) – Management Responsibilities

• Develop Organization Structures for Accountability
  • Formalizing organizational charts
  • Requiring (and maintaining!) **written procedures** for important processes, incorporating control activities, process flowcharts, workflow approvals

• Commit to Attracting and Retaining (**and developing**) Competent Employees

• Holding Individuals Accountable
  • Job descriptions including control processes
  • Timely, fact-based performance appraisals
  • **Disciplinary action where appropriate** – Zero-tolerance (theft, abuse)
  • Internal Audit
  • Whistleblower hotlines & protections (staff should be able to report on superiors)
Documentation of Policies & Procedures

- **Every government** should document its accounting policies and procedures in writing
  - Explain design and purpose of control procedures
  - Describe what is actually intended to be done, not unattainable ideals
- Make sure documents are readily available to employees
- Clearly delineate the authority and responsibility of all employees, including:
  - Which employees are responsible for which functions
  - Authority to authorize transactions
  - Responsibility for safekeeping of assets and records
NYC Example – Comptroller’s Directives

• High level accounting and control policy mandates & suggestions to City agencies and component units maintained and available on-line
• Agencies can/should cross reference Directives with their own policies and procedures to help ensure alignment and completeness
• Directive #1 specifically addresses detailed control procedures
Identifying & Addressing Control Deficiencies

• Establishing and using an Internal Audit function
• Encouraging “Whistle Blowers” to report fraud and questionable practices
• Taking measures to avoid, limit or eliminate control deficiencies
Internal Audit Function

- **Every government** should **consider the feasibility** of having an Internal Audit (IA) function.
- If dedicated staff IA is not practical, consider using other internal staff or outsourcing.
- **IA assists management** in monitoring the proper design and function of control procedures.
- Establish function formally (in Charter or enabling legislation).
- **Hire qualified staff** (relevant degree and/or certification).
- Perform Audits under **GAGAS**.
- Annual IA plans and all reports should be available to **audit committee** or equivalent.
Encourage Compliance & Facilitate Enforcement

- Have a formal, **widely publicized** ethics policy
- Establish practical mechanism(s) to permit reporting of concerns about fraud, abuse, or questionable accounting practices (e.g., hotlines) that are:
  - **Confidential**, and
  - **Anonymous**
- Train staff who deal with public to recognize and direct potential whistle blowers
- Internal auditors (or equivalent) who receive reports **must have**: appropriate procedures, training and resources to: record, track, investigate, and report to appropriate internal and/or external officials
- Disposition of all cases should be reported to Audit committee
Preventing, Limiting or Eliminating Auditor-Identified Control Deficiencies

- Auditors are required (by professional standards) to report **Material Weaknesses (MW)** and/or **Significant Deficiencies (SD)** in internal control over financial reporting identified in a financial statement audit.
- Government may hire 3rd party to prepare financial statements, but **if auditors prepare** financial statements because **client is unable**, that is evidence of **either a MW or SD**.
- Documenting the existence of a sound financial reporting system and minimizing likelihood of material adjustments may reduce the risk of reported MW or SDs.
- **Auditors** get final say.
Asset Accounting and Control

1. Establishing Capitalization Thresholds for Capital Assets
2. Maintaining Control over Items That Are Not Capitalized
3. Determining Estimated Useful Lives of Capital Assets
4. Periodic Inventory of Tangible Capital Assets
Capitalization & Control

• Establish minimum thresholds for capitalization based on **length of life** and **cost**. **Not less than 2 years and $5,000.00**
• Apply thresholds to individual items, not groups of similar items (generally)
• Maintain control over key “controlled capital type” items even when not capitalized
  • Where required for compliance, such federal grant funded items costing >$5,000
  • When public safety and potential liability exist, such as for police weapons
  • When there is high risk of theft due to ease of transporting and selling items, such as portable technology and sound equipment
• **Physical inventory counts** should be completed at least every five years, even if reliable perpetual inventory system is in use.
Asset Lifetimes

• Useful lives matter!  
  \[ \text{(much less than human lives)} \]

• Life spans assigned to capital assets greatly affect depreciation expense reported in each period and may skew cost analysis.*

• Best source of information on useful lives is generally past experience. Comparability is affected by differences in Quality, Intended Use, and Environment

• Establish useful lives by category of assets

• Periodically compare estimated to actual lives and update as needed.
Fund Accounting &
Fund Balance
Fund Accounting and Fund Balance

1. Using Fund Accounting Effectively
2. Appropriate Level of Unrestricted Fund Balance in General Fund
3. Determining the Appropriate Levels of Working Capital in Enterprise Funds
Funds: Why and How Many?

- Fund accounting assists government and F/S users in determining compliance with laws, rules and regulations, as well as contract terms.
- For **accounting**: as many funds as **needed for management** and compliance
- For **financial reporting**: group funds logically to meet (less detailed) information **needs of users**
- Generally, use **as few funds as practical**
General Fund Balances

- Distinguish between **Budgetary** (fund) Balance and **accounting** Fund Balance
- Maintain adequate level of fund balance ("reserves") to mitigate risks based a government’s own circumstances, such as volatility and predictability of revenues and expenditures but **no less than two months’ revenue or expenditures**
- Policies should define **circumstances warranting use** of FB reserve and establish a time period for **replenishment within three years**
Enterprise Fund Working Capital

• Maintain adequate level of working capital to mitigate risks
• Establish a target working capital based on many factors specific to the enterprise
• General target level is **90 days**, and should **not be below 45 days**, worth of operating expenses
Cost Accounting and Management
Cost Accounting and Management

1. Measuring the Full Cost of Government Service
2. Taking Advantage of Indirect Cost Allocations
3. Applying Full-Cost Accounting to Municipal Solid Waste Management Activities*
4. Planning for Recovery from a Technology Disaster
Measuring Full Cost of Services

- **Governments should calculate the full costs of different services** they provide; which is useful for benchmarking, fee setting, contracting in/out decisions, etc.

- Full cost includes **Direct and Indirect Costs** and is a **full accrual** concept - include costs paid or to be paid in other periods (comp absences, pension, OPEB, asset use*)

- Depending on purpose, may need to identify **fixed, variable** and **avoidable costs**

- Direct Costs maybe:
  - Exclusive to a service/program (salaries and benefits for dedicated staff, materials, etc.)
  - Costs *allocated using a (disclosed!) systematic and rational basis* (shared administrative costs, facilities, technology).
Indirect Cost Allocations

• Indirect cost allocations should be performed as need, or at least every 3 years, for full cost of service calculations, grant program cost reimbursement, etc.

• May be performed in house or contracted out, based on considerations including expertise and acceptability *

• If outsourced,
  • Management and staff should be involved and knowledgeable of methodology used
  • The government should have ownership of final work product
Last but NOT least... Disaster Recovery

- Should formally establish and disseminate **written policies and procedures** for minimizing disruption following a disaster
  - Assign disaster recovery coordinators for each department, forming a recovery team
  - Creation and **securing (offsite!)** of **back-up data**
- Unavailability of technology is not the only consideration:
  - Worksite unavailable
  - Workforce unavailable
  - Technology unavailable
  - External service providers unavailable
Next Up

Irfan Bora and GFOA Best Practices in Financial Reporting and Grants Management
and MUCH BETTER LOOKING SLIDES!!!!

Irfan Bora, CPA, CMA, CGFM
Director, Rutgers Master’s in Governmental Accounting Program
Basis of Accounting Versus the Budgetary Basis

• Important to understand differences in basis of accounting and how budgetary basis can vary from Governmental GAAP
• Addresses the recognition of transactions (revenues and expenditures)
• Budget document needs to describe these differences
  – **Revenues**: under GAAP, recognized when measurable and available
    • Budgetary basis: could be recognized on a cash basis
  – **Encumbrances**: most commonly treated as expenditures under budgetary basis- never shown as expenditures under GAAP
  – **Leases**: recognition of NPV
  – Classification of “other financing sources” and “other financing uses” under GAAP
Basis of Accounting Versus the Budgetary Basis

• Differences arising due to financial reporting period and budgetary period--Grants/Projects
• Differences due to fund structure and the inclusion of component units
• Treatment of proprietary funds can vary dramatically under the two bases of accounting
Conforming to Governmental Accounting, Auditing and Financial Reporting Standards

• Comprehensive Annual Financial Report is expected to follow principles of:
  – Generally Accepted Accounting Principles (GAAP)
  – Generally Accepted Auditing Standards (GAAS)
  – Generally Accepted Governmental Auditing Standards (GAGAS)
Conforming to Governmental Accounting, Auditing and Financial Reporting Standards

- Adopt and implement accounting system which conforms to governmental GAAP
- Issue GAAP financial statements on a timely basis
  - For small governments (when GAAP statements not feasible) issue statements on a modified accrual basis
- Have financial statements independently audited in accordance with GAAS and/or GAGAS
Audit Procurement

• Determining Audit Scope
  – Extending coverage to individual funds and component units
• Auditor should be required to follow GAGAS standards
  – GAAS standards are not sufficient
• Multiyear agreements encouraged (at least 5 years)
  – More cost competitive with more efficient allocation of resources
  – Auditor rotation encouraged but sometimes not feasible
• Use competitive procurement process
  – In many cases an RFP process is utilized
  – Price should not be the sole factor
• Nonaudit services could impair independence
  – Carefully analyze its impact on the audit engagement
Audit Committees

• Understand strategic role of Audit Committees in public sector
• The three players:
  – Internal management
  – Independent auditors
  – Governing body
• Governing body establishes audit committee
  – Oversees the appointment, compensation, retention, and oversight of auditors
  – Governing charter guides structure and membership
  – Members should possess basic understanding of Governmental GAAP, Financial Policies and Internal Controls—indeed of management
  – Generally 3 members with at least one expert member (internal/external)
  – Committee members should have access to internal auditor’s work
  – Prepares annual report to full governing body outlining its work
Improving the Timeliness of Financial Report

• Background
  – GASB Concept Statement #1--Objectives of Financial Reporting identifies timeliness as an important characteristic
  – Balance timeliness with the need for reliability and cost/benefit

• Recommendations:
  – Timely recording of transactions throughout the year
    • Use reconciliations and financial analysis to identify problem areas
    • Accounting policies and procedures should provide guidance on recording transactions
  – Closing process and financial statement preparation
    • Define annual closing process (normally 7-10 days)
    • Incorporating component units in a timely manner
    • Dealing with unforeseen circumstances, lawsuits, legal/contractual violations
Improving the Timeliness of Financial Report

• Recommendations (cont.):
  – Implementation of new GASB standards
    • Preparing plan for implementation based on effective dates for new standards
  – Financial Reports Distribution
    • GFOA encourages electronic distribution
    • Website, PDF, XBRL (future)
Presenting Official Financial Documents on your Government's Website

• Why publish CAFR on government’s web site?
  – Factors such as costs, accessibility, interaction with constituents, and broadened potential scope

• Issues to Consider
  – Technological infrastructure
    • Software compatibility and features
    • Security and placement
    • Direct links
Presenting Official Financial Documents on your Government's Website

• Issues to Consider (cont.)
  – Formatting
    • Consistency with printed version, though do use additional capabilities
    • Legibility and pagination
    • Consider file size
  – Electronic financial reporting language
    • Use of XBRL to standardize government electronic financial reporting
  – Distribution
    • Inform users of availability
  – Information disclaimer and historical information
Effective Grant Administration

• Developing a Grant Policy
  – Outline key steps in grant management including steps before application and acceptance

• Administering to meet grants requirement
  – Is process in place to meet grant terms and conditions?
  – Are specific personnel identified with responsibilities for project plan?
Effective Grant Administration

• Financial Management
  – Proper cost allocation with consistency
  – Indirect cost allocation
  – Integration of grants into annual budget process
  – Reconciliation of internal records with grant reports
  – Adequate cash management procedures for disbursements and drawdowns
  – Treating allowable/unallowable and direct/indirect costs
Effective Grant Administration

• Maintaining Internal Controls
  – Documentation of grant procedures
  – Compliance issues
  – Determining program level risk (high/medium/low)

• Subrecipient Monitoring
  – Requirements on progress reports
  – Administrative and financial monitoring
  – Single Audit review and follow up

• Audit Requirements
  – An understanding of audit requirements (applicability of GAGAS, GAAS, OMB guidance)
  – Grant close-out requirements
  – Grant information in GAAP basis financial statement
Effective Grant Administration

• Communication
  – With grant sponsors, oversight and cognizant agencies, external auditors

• Specialized Reporting
  – Maintaining a comprehensive list of reporting requirements with timelines
  – Preparation and certification of specialized reports
  – Aggregating information for the Schedule of Expenditures of Federal Awards
Implementing OMB Uniform Guidance

• Uniform Administrative Requirements, Cost Principles and Audit Requirements for Federal Awards
• Objectives:
  – Streamlines federal grant-making and monitoring process
  – Eases administrative burden for grant applicants and recipients
  – Reduces risk of waste, fraud, and abuse
Implementing OMB Uniform Guidance

• GFOA Recommendations:
  – Disseminate Uniform Guidance requirements to entire organization
  – Determine monitoring level for subrecipients who do not meet the spending threshold of $750,000
  – Ensure subaward agreements cover federal award requirements on financial and performance reports
  – Are subrecipients able to comply with performance measurement requirements?
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