



Office of the City Auditor

CONSENT CALENDAR
October 9, 2007

To: Honorable Mayor and
Members of the City Council

From: Ann-Marie Hogan, City Auditor

Subject: Invisible Problems: Weak Internal Controls Require Disclosure by City
Manager and Possible Future Council Action on Budget and Workplans

RECOMMENDATION

Request the City Manager to require departments to begin to identify and quantify the risks of any significant internal control weaknesses that have not been addressed because of insufficient resources or staff capabilities. A written report from each department on their three major risk areas should be included in the annual budget submission and updated at quarterly meetings with the City Manager. If possible, preliminary information should be drafted by key departments and reviewed by the Budget Office before the mid-year budget review in February.

CURRENT SITUATION AND ITS EFFECTS

Over four years of budget cuts, the City Auditor's Office has noted weaknesses in departmental internal controls that, as City Auditor, I am referring to Council. To determine the extent of the potential seriousness of these conditions, my office is requesting the City Manager take action to identify and analyze problems in each department.

Current audit reports disclose a lack of internal controls such as supervisory review and monitoring, eliminating or minimizing incompatible duties (segregation of duties), up-to-date written procedures, and physical safeguarding of assets. Internal controls should provide reasonable assurance that:

- program objectives of Council and the City Manager are met efficiently and effectively
- information is accurate and reliable; and
- City assets and people are safeguarded.

Based on our audit work and observations, it appears that many weaknesses found may be related to budget cuts, including position freezes, vacancies, and reductions. Staff has been under pressure to maintain service levels with fewer resources.

FISCAL IMPACT OF RECOMMENDATION

Improving the City's ability to identify control risks and estimate the cost of addressing them will take staff time and, according to the City Manager, should be addressed

incrementally. He believes that staff in the departments may need assistance and training in internal controls and in how to perform a cost-benefit analysis.

Accordingly, improvements may not be immediate. This is consistent with findings and recommendations in our November 1999 [Departmental Budget Monitoring Audit](#) which called for more training and clearer guidelines for needed skills for departmental budget monitors. The City Auditor's Office and Finance provide some training in internal controls. However, there may be costs associated with providing additional training.

The City's tuition reimbursement program covers courses in financial and managerial (budgetary) accounting. Tuition and textbooks are paid for by the City, and employees attend and study on their own time. These courses should offer a good understanding of internal controls and enable proficiency in cost and benefit analysis.

BACKGROUND

Control risks related to budget reductions were discussed in reports available on our web site:

- [Internal Controls Risks Associated With Budget Cuts and Freezes](#) (12/09/03)
- [Delayed Implementation of Audit Recommendations](#) (5/16/06)
- [Outstanding Audit Recommendations](#) (6/26/07)

In response to our report on internal control risks in 2003, members of the Council audit advisory committee requested additional reports if the auditors noticed further erosion of internal controls.

As noted in the City Manager's budget message:

"The proposed budget is balanced with few cost increases to Berkeley taxpayers and minimal reduction of frontline services. However, the organization is still adjusting to the major reductions that were made over the last four years, including recurring General Fund expenditure cuts of almost \$20 million and the 6.8 percent reduction in the City's workforce (120 FTE's)."

It appears that internal controls have been hard hit by the City's difficult adjustment. Weak controls are "invisible problems" and they tend not to be addressed until they become visible.

That being the case, the City needs to address some "deferred maintenance" in oversight and accountability.

RATIONALE FOR RECOMMENDATION

The extent to which the City is at risk because of "invisible problems" related to internal controls can best be addressed by requiring departments to articulate and analyze control weaknesses in regular reports to management.

CONTACT PERSON

Ann-Marie Hogan, City Auditor, 981-6750