



City Wide Cash Handling Audit II

**Audit Report 13-03
December 2013**

December 27, 2013

Members of the City Council:

Cash handling operations are an important government fiscal operation. The Rapid City City Council approved this audit of City-wide cash handling practices as part of the COMPASS 2013-2014 Audit Plan.

Effective controls over cash handling require the development of written policies and procedures, consistently following those procedures and ensuring that City managers and staff understand the purpose of effective controls. In a decentralized operating environment like Rapid City, strong policies and procedures are especially important.

Based on recommendations from the City-Wide Cash Handling Audit released in February 2013, the Finance Office is developing guidelines for effective cash handling policies, procedures and practices for use by City departments. In addition, a number of departments have implemented or are in the process of implementing site-specific recommendations to improve cash handling policies, procedures and practices.

We have made nine recommendations to strengthen cash handling policies, procedures and practices at the cash handling sites included in this audit. We provided the Mayor and the department directors with a draft of this report on November 4, 2013. In addition, we met with department directors and managers to discuss site-specific findings and our recommendations for improving controls at those specific sites. Management's response is included in this report. We greatly appreciate the cooperation and assistance of City managers and employees with this audit.

We would be happy to discuss our audit conclusions, findings, and recommendations with any member of the City Council, City staff, or citizen.

This audit was conducted by Kelan Kelly and Sarah Kuntz.

Kelan Kelly
Chief Auditor

Table of Contents

Introduction	1
Scope and Methodology	2
Background	3
Conclusions	4
Criteria	6
Findings and Recommendations.....	7

Introduction

Cash handling is a very visible and important government fiscal function. Citizens expect government to provide high-quality services and, at the same time, be accountable for public funds. Cash handling audits determine whether cash resources are handled in a manner consistent with good business practices and whether assets are adequately safeguarded against misappropriation, misuse, loss and theft.

Cash handling audits assess the adequacy and effectiveness of internal controls throughout various cash handling sites in City departments. Cash handling audits consist of objective review and evaluation of the practices and procedures used by City employees related to the receiving, receipting, recording, depositing, transporting, reconciling and safeguarding of City resources.

For the purposes of this audit, the term “cash” refers to currency, coin, checks, money orders, debit and credit card payments.

Our review of City-wide cash handling operations focused primarily on the following four audit objectives:

1. Determine if internal controls over cash handling are appropriate;
2. Determine if cash is collected, receipted, recorded, deposited, transported, reconciled and secured in an adequate manner;
3. Ensure that change fund balances are accurate, fund limits are appropriate, and proper controls over account use are in place; and
4. Determine if City employees are adequately trained in cash handling responsibilities.

Scope and Methodology

This audit focused on written policies and procedures as well as observed activities and practices related to cash handling at selected sites across the City from August 2013 through October 2013. The audit work involved reviews of cash collections and records, and change funds at 10 sites throughout Rapid City that were not included in a previous audit. Sites included the outdoor aquatic and tennis facilities, water reclamation office, utility maintenance office, and the two library branches.

In conducting this audit, staff employed a number of audit methods and techniques. Staff reviewed relevant literature on cash handling from the AICPA, COSO, GAO and GFOA to develop criteria for effective cash handling controls. We also reviewed audit reports from other jurisdictions. We obtained a list of cash handling sites from the Finance Office as well as from individual departments. We requested and reviewed written policies and procedures from the departments responsible for cash handling at these specific sites. Staff analyzed revenue reports from the City's accounting system. We interviewed management and staff. We observed cash handling activities at specific sites throughout the City. Finally, we conducted unannounced cash counts for change funds.

Compliance with Government Auditing Standards

We conducted this audit in accordance with generally accepted government audit standards. These standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our audit findings and conclusions based on the audit objectives. We believe that the evidence obtained provides a reasonable basis for the conclusions and findings based on the audit objectives.

Background

Cash handling activities in the City of Rapid City are spread throughout the organization. The City accepts payments for items and services such as admission to aquatic, tennis and recreation programs, fines, septic hauler permits, and utility tap fees. Cash handling operations for this audit were reviewed at 10 sites that were not reviewed in the City-Wide Cash Handling audit released in February 2013. These sites deposit cash with the Finance Office.

In total, the City received more than \$195 million in cash in 2012 as reported by the Finance Office, and maintains approximately \$68,000 in change funds. For the sites included in this audit, receipts were less than \$1 million and sites held change funds that amounted to \$1,275.

Cash handling practices reflect both the need to maintain good customer service and the need to protect City assets. Effective practices protect assets from accidental loss and intentional misappropriation.

In general, sound cash handling principles require:

- An organizational structure and staffing resources sufficient to segregate incompatible responsibilities such as receiving revenue, recording transactions, depositing money, maintaining custody of assets and reconciling assets with transaction records;
- A physical environment conducive to safeguarding money;
- Employees qualified in cash handling practices; and
- Management oversight at an appropriate level for the specific cash handling environment.

Conclusions

We found a number of areas where cash handling practices could be improved by implementing best business practices at the sites reviewed for this audit. Controls over cash handling could be improved by strengthening existing policies and procedures; developing policies and procedures where they are lacking; employing safeguards; improving management oversight of cash handling activities; and providing training for employees responsible for cash.

Objective One: Determine if controls over cash handling are appropriate.

Controls can be improved by establishing written policies and procedures consistent with generally accepted criteria for cash handling internal control.

The Finance Office is charged with custody of City funds in accordance with South Dakota law. At the time of our audit, the Finance Office was in the process of developing cash handling guidelines to provide a framework for policies and procedures for City departments.

During our review of cash handling policies and procedures collected from City departments we noted that some departments have developed policies and procedures. The Aquatics program in the Parks and Recreation Department had used recommendations in the City-Wide Cash Handling audit (released February 2013) and developed detailed policies and procedures for aquatics staff with cash handling responsibilities. One department had not developed written policies and procedures. The remaining policies we reviewed were incomplete and need improved to provide effective control over cash handling activities. We also noted a lack of consistency and documented revision dates in the policies and procedures developed by City departments.

Objective Two: Determine if cash is collected, receipted, recorded, deposited, transported, reconciled and physically secured in an adequate manner.

Through audit testing, discussions with staff and observations, we determined that the lack of management oversight in cash handling functions is the most common risk in the sites included in this audit. There is a lack of segregation of duties of cash handling functions, and a lack of proper cash safeguards at some locations. In some locations no process is in place for reviewing missing, voided, or canceled receipts.

Objective Three: Ensure that change fund balances are accurate, fund limits are appropriate, and proper controls over account use are in place.

The Finance Office maintains a list of outstanding change funds, but the list is not complete as it does not list change funds by location and function. Change funds records should identify fund locations and the party and/or position responsible for the fund.

During our audit work we tested change funds for accuracy. Our counts showed few and insignificant differences between the amounts in the accounts at the time of our count and the amount departments reported should be in them. We commend City employees for maintaining accurate change fund accounts.

Objective Four: Determine if City employees are adequately trained in cash handling responsibilities.

Our audit work indicated that aquatics staff in the Recreation Division received cash handling training which provided them with sufficient knowledge to properly perform cash handling duties. However, at the other sites we reviewed, we noted a lack of training for City employees whose positions require cash handling responsibilities.

Criteria

Criteria represent standards against which performance is measured. Depending on the audit topic, criteria may include laws, regulations, contracts, grant agreements, expected performance measures, benchmarks and defined business practices. Criteria identify the required or desired state or expectation with respect to program or operation. Rapid City does not have a formal, written citywide cash handling policy for the receipt of cash or for change funds. Therefore, our criteria consisted of guidelines issued by the Committee on Sponsoring Organizations of the Treadway Commission (COSO), recommendations from the American Institute of Certified Public Accountants (AICPA), guidance issued by the United States General Accountability Office (GAO) and industry best practices for governmental cash handling activities. We were also guided in our work by South Dakota law which charges the Finance Office with the responsibility to collect all City funds (SDCL 9-22-1) and to control City finances and property (SDCL 9-12-2).

Based on this guidance, best practices for receipt of cash and change funds include:

- Written policies and procedures;
- Payments are controlled by an electronic receipting system or pre-numbered receipts;
- Voids are adequately documented;
- Checks are restrictively endorsed upon receipt;
- Segregation of duties for receipts, deposits and reconciliations;
- The fund is accurately reconciled to the financial system;
- Cash is properly safeguarded;
- The fund is balanced to the authorized amount; and
- The amount of the fund is appropriate for operational needs.

Findings and Recommendations

Controls over cash handling and change funds should be improved at the sites we reviewed. While we found no instances of loss, misuse or misappropriation of City assets, when controls are lacking, the risk increases for errors or misappropriations to escalate to significant amounts and loss of funds to Rapid City. We have made a number of recommendations to ensure City resources are properly safeguarded and best practices for cash handling are followed by City employees. We discussed site-specific findings and recommendations with department directors, managers and staff.

Policies and Procedures

One of the ten cash handling sites we evaluated had not established written policies and procedures for cash handling functions. The policies and procedures established by City departments and used at four sites we reviewed are incomplete and should be strengthened to address risks to City assets associated with cash handling. At two sites written policies and procedures for change funds have not been established.

We also noted in our audit work that City management is in the process of establishing cash handling guidelines to provide City departments, divisions, and programs with a framework for developing effective cash handling policies and procedures.

Lack of effective, written policies and procedures for cash handling activities can result in the potential for loss, misuse and misappropriation of City assets and for accounting and recording errors to go undetected.

Recommendation 1: We recommend the City Finance Office develop cash handling guidelines to assist City departments in developing effective written cash handling policies and procedures.

Management's Response – Finance Office The finance office has begun to develop cash handling guidelines to assist City departments in developing effective written cash handling policies and procedures that address collection, receipts, deposits, recording transactions, cash reconciliation, deposit reconciliation and safeguards. Once a draft has been reviewed, the guidelines will be forwarded to all City departments for their implementation. Finalization of this project should occur within the next 30-60 days.

Recommendation 2:	<p>We recommend that City departments use these guidelines in drafting policies and procedures and make modifications as necessary to address site-specific situations. All policies and procedures should address the following:</p> <ul style="list-style-type: none"> • Collection • Receipts • Deposits • Recording Transactions • Cash Reconciliation • Deposit Reconciliation • Safeguards
Management's Response - Library	I have reviewed these findings, and our library business office drafted revisions to existing library procedures that addressed these concerns.
Management's Response – Water Reclamation	Our solution to the issues associated with our septage hauler permit program is to have Finance take care of the cash handling component. We will be putting together permit packages to send out to the Septage haulers in May of 2014 for renewals. All cash and checks will be handled by Finance.
Management's Response – Utility Maintenance	We agree with this recommendation, and Utility Maintenance will come up with a policy/procedure for taking checks at Utility Maintenance.
Management's Response – Parks and Recreation	The Parks and Recreation Department does employ formal departmental Cash Handling Procedures at all facilities including outdoor pools and tennis courts. Staff will review the established procedures to ensure site-specific coverage of all areas of cash handling, including collection, receipts, deposits, recording transactions, cash reconciliation, deposit reconciliation and safeguards.

Fund Documentation

South Dakota law assigns responsibility for assets (cash and property) to the Finance Office. We identified issues regarding documentation and maintenance of change funds during our audit work. First, the Finance Office does not have a complete and accurate list (record) of outstanding change funds used by departments. We identified five funds for which the Finance Office records did not match the amounts used by departments or lacked a proper description of the fund. Second, for those funds authorized by City Council Resolution we found the resolution did not always:

- Have an assigned resolution number prior to 2008;
- Identify which division or program within a department the fund was established for; and
- Identify if the fund was new or an existing fund in which the amount was increased or decreased.

A lack of financial records documenting the creation of change funds and subsequent increases or decreases in amounts and/or changes to fund use impairs the Finance Office's ability to carry out its statutory responsibilities to control municipal finances by conducting complete and accurate audits of the assets in change funds.

Recommendation 3: We recommend the City Finance Office create and maintain a complete and accurate list of all change funds that are properly supported by City Council Resolutions. We also recommend that all future resolutions are written to ensure:

- The custodial division or program is identified;
- The authorization specifies a new fund or an increase or decrease to an existing fund;
- Proper identification as a change fund; and
- The fund function is explained.

Management's Response – Finance Office The Finance Office will prepare a resolution to re-establish all of the necessary petty cash and change funds. This resolution will include the following for each fund: custodial division or program identification; whether the fund is new, increasing or decreasing; proper identification as a petty cash or change fund; and fund function. This project should take one month for completion and implementation.

Receipts

City departments use either booklets of pre-numbered receipts issued by the Finance Office, or electronic accounting systems that generate numbered receipts. Our review identified five City sites that do not have a process to review for missing, voided or canceled receipts.

A review process for missing, voided or canceled receipts is an important safeguard to reduce the possibility of loss or misuse of City assets.

Recommendation 4: We recommend the City Finance Office develop a process for City department employees to use to review for missing, voided, or canceled receipts when pre-numbered or system generated receipts are used.

Management's Response – Finance Office We will include this in the written policies and procedures noted in the first finding. Finalization of this project should occur in the next 30-60 days.

Segregation of Duties

We identified improper segregation of duties at two sites due to a lack of staff resources and no mitigating control. This included improper division of duties over the following cash handling activities:

- Collection and reconciling of cash;
- Collection and depositing of cash;
- Reconciliation of deposits;
- Opening mail and creating a remittance list; and
- Reconciling the deposits to the remittance list.

Improper segregation of duties over cash handling activities creates the potential for loss and misuse of City assets as well as significantly increased risks for fraud and/or errors to go undetected.

Recommendation 5: We recommend department managers properly segregate cash handling duties where resources are available. We also recommend they implement mitigating controls where resources are limited. Duties to segregate include, but are not limited to:

- Collection and reconciliation of cash;
- Collection and depositing of cash;
- Reconciliation of deposits to financial system records;
- Opening mail and creating a remittance list; and
- Reconciling the deposits to the remittance list.

Management's Response – Water Reclamation Our solution to the issues associated with our septage hauler permit program is to have Finance take care of the cash handling component. We will be putting together permit packages to send out to the Septage haulers in May of 2014 for renewals. All cash and checks will be handled by Finance.

Management's
Response – Utility
Maintenance

We agree with this recommendation and will have the Water Superintendent as the Primary Reconciler and the Administrative Secretary as the Secondary Reconciler.

Safeguards

In our review of City cash handling sites we observed instances of inadequate safeguards over cash assets. At seven sites, checks are not immediately restrictively endorsed and one location does not lock the cash register till during business hours.

Utility Maintenance staff collect tap fees through the mail and from walk-in contractors at the office. Checks received through the mail are received at CSAC, because the City currently makes efforts for all mail to be received at CSAC. Once received tap fee payments are opened and placed in a mailbox to be picked up and taken to the Utility Maintenance office for processing. After processing, checks are returned to CSAC for deposit. The result of this process is that checks are handled by more individuals than necessary before being deposited. In addition to placing assets at higher risk, the process of receiving mail at one location and transporting it to a second location for processing creates the potential for unnecessary trips to CSAC for the sole purpose of obtaining mail.

Where physical security measures are inadequate, cash is at a higher risk of loss, theft or misuse. Accepting checks without immediate endorsement, storing cash without adequate safeguards and transporting cash unnecessarily increases the potential for loss and misuse of City assets.

Recommendation 6: We recommend that management properly safeguard cash and that all staff receiving checks restrictively endorse them immediately where practicable.

Management's
Response - Library

I have reviewed these findings, and our library business office drafted revisions to existing library procedures that addressed these concerns.

Management's
Response - Parks and
Recreation

Checks received at the outdoor pools are endorsed immediately and placed in a locked safe until daily deposit. Beginning this coming year, checks received at the tennis facility will also be endorsed immediately and placed in lock safe until daily deposit. Cash is kept in a locked cash register drawer or safe and balanced daily.

Recommendation 7: We recommend that all payments for tap fees be received and processed at the Utility Maintenance Facility.

Management's
Response – Utility
Maintenance

We agree with minimizing the number of times a check is handled. The majority of tap fees collected are collected in person at the Utility Maintenance office, so most checks will only be transported once to CSAC for deposit. We propose that checks for Utility Maintenance that are received at CSAC are held in the Finance office with a notice given to Utility Maintenance that the funds have been received. The Utility Maintenance staff will return a deposit slip and receipt to the Finance office so that the check can be deposited to the appropriate fund. This new process has been discussed and agreed upon with the staff in the Finance office.

Management Oversight

Under the guidelines for effective cash handling controls issued by COSO, internal control systems need to be monitored. Monitoring by management ensures that internal controls continue to operate effectively. This process involves assessment by appropriate personnel of the design and operation of controls on a timely basis, and taking necessary actions to correct weaknesses. Circumstances may change causing internal controls to be less capable of identifying risks. It is management's responsibility to review and determine whether existing internal controls continue to be effective.

At the sites reviewed for this audit, management oversight of cash handling activity can be strengthened. At nine sites cash and deposit reconciliations are not reviewed. At seven sites management does not review change funds for accuracy.

A lack of adequate management oversight of cash handling activity can result in the potential for errors or fraud to go undetected.

Recommendation 8: We recommend department management develop and implement monitoring procedures over cash handling to ensure that records are complete and accurate; and that change funds are accurate, reasonable, and sufficient.

Management's
Response - Library

I have reviewed these findings, and our library business office drafted revisions to existing library procedures that addressed these concerns.

Management's
Response – Parks and
Recreation

Management has taken a proactive role in providing training to all cashiers and cash handlers to strengthen controls and reduce risks. The written departmental cash handling procedures carefully outline proper cash and check handling methods. Management will continue to monitor cash handling functions at all facilities and increase oversight where necessary.

Management's
Response – Water
Reclamation

Our solution to the issues associated with our septage hauler permit program is to have Finance take care of the cash handling component. We will be putting together permit packages to send out to the Septage haulers in May of 2014 for renewals. All cash and checks will be handled by Finance.

Training

The GAO has issued criteria for employee training with regard to internal control standards. Accordingly, all personnel need to possess and maintain a level of competence that allows them to accomplish their assigned duties, as well as understand the importance of developing and implementing good internal controls. Management is responsible for identifying the appropriate level of knowledge and skills needed for various jobs and providing the necessary training.

During our review of cash handling activities, we noted a consistent lack of training for City employees with cash handling responsibilities. A lack of training prevents employees from using sound business practices when handling cash and increases the risk of loss or misuse of City assets.

Recommendation 9: We recommend the City Finance Office develop and provide training on proper internal controls for all City employees with cash handling responsibilities.

Management's
Response – Finance
Office

The Finance Office will develop and provide training on proper internal controls for all City employees with cash handling responsibilities as part of the written policies and procedures noted in the first finding. Finalization of this project should occur within the next 30-60 days.