

Corrective Action Plan for the Town of Paradise Valley

For the year ended June 30, 2019

FINDING 2019-01—CORRECTED MISSTATEMENTS FROM LAST FISCAL YEAR ENDED JUNE 30, 2018

CRITERIA

The financial statements for fiscal year ended June 30, 2019 includes correcting an error from last fiscal year ended June 30, 2018 that was found while preparing the statements for 2019.

BACKGROUND

GASB 68, *Accounting and Financial Reporting for Pensions*, establishes financial reporting requirements for most state and local governments that provide employees with pensions.

The Town's two pension programs are PSPRS (Public Safety Personnel Retirement System) for Police Officers regularly assigned to hazardous duty and ASRS (Arizona State Retirement System) for all other Town employees that meet eligibility requirements.

TIMING OF REPORTS

When the Town prepares its CAFR, the most recent financial reports for PSPRS & ASRS are one year in arrears. The Town will "defer certain inflows and outflows" to reconcile the timing difference of fiscal years. The PSPRS & ASRS pension financial reports for FY2017 are reported in the Town's FY2018 CAFR; pension reports for FY2018 are in the FY2019 CAFR.

PENSION REPORTING

The Town's "*Fund statements*" use the *modified* accrual basis of accounting and the *current financial resources measurement focus*. These statements have a direct link to the Annual Expenditure Limitation Report signed by the designated CFO.

These statements report all payments to PSPRS that are physically made in the fiscal year as a "Current expenditure" under "Public Safety". This includes both the minimum required contribution and payments toward the PSPRS Unfunded Liability. The expenditure is "subject to" the expenditure limitation and requires Council approved budget authority.

The Town's "*Government-wide statements*" use the *full* accrual basis of accounting and the *economic resources measurement focus*. These statements include balances from the "fund statements" plus items such as depreciation, compensated absences and pension liabilities.

These statements report only the required contributions as an "expense". Any additional amounts for the PSPRS Unfunded Liability are reported as "deferred outflow related to pension liability" for the Town to recognize in the same reporting year as PSPRS. Timing of reporting means PSPRS will report paying down the Unfunded Liability in the year the PSPRS received payment (FY2019), the Town reports the reduction of the Unfunded Liability in the next year (FY2020).

CONDITION

The Town's management is responsible for the preparation and presentation of the Town's financial statements. For a number of years, the Town had a separate engagement with its auditing firm to draft the Town's financial statements based on the Town's trial balance.

The Town provided the proper information for to report the PSPRS pension reporting, including amounts for the minimum contribution (expense) and paying down the Unfunded Liability (deferred outflow) to the contracted financial statement preparers.

The 2018 financial statements were drafted by the auditors. The Town reviewed the statements, had some changes, knew how the PSPRS contributions were to be reported and presumed it was being reported correctly, but did not catch the pension reporting misstatement. The pension reporting misstatement was missed when audited and then wasn't caught by the audit firm's concurring review team. In 2019, the pension misstatement from 2018 was discovered.

Closing June 30, 2018: The Town had new accounting staff on-board for a few months. With incomplete accounting records dating back to July 1, 2016 or older, their primary focus was on the "fund statements" and the impacts on the Annual Expenditure Limitation Report. This involved reconciling all account groups and realigning the reporting structure, internal controls and process to avoid other audit complications, including but not limited to: Account receivables, Employee benefits and insurance reporting, Capital assets, Interfund loans, Debt service disclosures, p-Card processing, Excise tax obligations spending and reporting, the budget document and presentation, donations and grant accounting.

Closing June 30, 2019: The Town had the same audit firm, but different lead and senior auditors engaged to prepare statements based on the Town's trial balance and conduct the financial audit. The PSPRS reporting error was discovered during the reconciliation process.

Impact of correcting the pension reporting misstatement: This pension reporting misstatement does not impact the Town's adherence to State Budget Law or the Annual Expenditure Limitation; it does not change the amount of the PSPRS Unfunded Liability, Annual Expenditure Limitation Carryforward or the General Fund balance.

AUDITOR'S FINDING

"In the prior year (Fiscal year ending June 30, 2018), the Town made pension contributions to the Public Safety Personnel Retirement System (PSPRS) in excess of the required contributions; however, the excess contribution was recognized as an expense in the governmental activities and should have been reported as a deferred outflow of resources."

AUDITOR RECOMMENDATION

The auditors "recommend the management reviews the summary of pension liability, deferred outflows of resources, deferred inflows of resources, and pension expense and reconcile the recorded pension activity to the reports provided by the public safety personnel retirement system (PSPRS) and to the contributions recorded as an expenditure at the fund level financial statements. Any variances should be investigated and resolved to prevent and detect a similar error in the future."

CORRECTIVE ACTION PLAN

Below is the Finance Division's corrective action plan, that was being implemented before this finding was discovered. Asterisks (*) denote an "auditor recommendation" from their 2019 report. All other steps were communicated and received auditor support. A check (✓) denotes the action has been completed.

Completion Date & Implemented Fiscal Year		Action
June 30, 2018 (FY2018)	✓	Create line items for the "Unfunded Liability" and "Prefunding" to separate from the "Minimum Contributions". This will help year end reporting and departments follow their budget status.
* October 2019 (FY2019)	✓	Correctly restate the FY2018 PSPRS Unfunded Liability ending balance for the FY2019 CAFR only; the General Ledger was correct.
September 2019 (FY2019)	✓	Run parallel financial statements to compare with auditor prepared statements.
* October 2019 (FY2019)	✓	Validate PSPRS source documents and obtain previous financial statement preparer's workpapers to reconcile the FY2019 CAFR to FY2018 PSPRS GASB 68 reports.
May 2020 (FY2020)		Update the Town's accounting structure to include recording all long-term assets and liabilities for the "statement of net position" and activities for the "statement of activities".
June 2020 (FY2020)		Facilitate third-party reviews of various finance related processes in the Town including systems, documentation, and internal controls.
September 2020 (FY2020)		Town take ownership of all financial reporting, including preparing the CAFR in-house. Be firmer when the Town believes is correct with understanding of GASB including reporting pensions as prescribed by GASB 68 during audits.
On-going (FY2021+)		Continue professional development for staff to stay current with GASB reporting requirements. Though the current staff has combined for preparing over 53 CAFRs for municipalities before coming to PV, it is important to stay current.

FOOTNOTE: FROM THE ARIZONA AUDITOR GENERAL'S WEBSITE

Regarding the filing requirements of the Annual Expenditure Limitation Report: "A.R.S. 41-1279.07(H) states that a chief financial officer who refuses to file the required reports with the Auditor General within the prescribed time period or who intentionally files erroneous reports is guilty of a class 1 misdemeanor. An erroneous report is one that contains a material misstatement. . . "

FINDING 2019-02—INFORMATION TECHNOLOGY USER ACCESS RIGHTS

BACKGROUND

When assessing internal control risks, it's not unusual for smaller finance operations to have a higher inherit risk than larger operations. In smaller operations there are a limited number of individuals to undertake many duties. Where in larger organizations there are more people to spread the same number of duties among. But that does not mean a smaller organization should ignore sound and vital internal controls.

CONDITION

In the 2018 financial audit, it was noted concern of management level employees having full user rights to the financial accounting software. But, believed the Town had other controls in place to mitigate that risk to a reasonable level. In the 2019 audit, the Town had the same audit firm, but different lead and senior auditors whom has a differing view. Current security configurations in the accounting software was set up based on the software company's recommendation for the systems the Town is running.

AUDITORS FINDING

"The auditor's noted that two management level employees had full user access rights to the financial accounting software. Maintaining segregation of duties and limiting user access rights will mitigate the threat of management override of controls over financial reporting."

AUDITORS RECOMMENDATION

"The Town should limit user access rights to those functions necessary to perform each employee's job function. Additionally, the Town should ensure user access rights are segregated so an individual does not have access to create, post, alter, and review transactions."

CORRECTIVE ACTION PLAN

Town management takes the integrity and protection of its data very seriously and is a top priority. The Finance Division will semi-annually review the access rights of all individuals whom use the financial accounting software to determine what is needed to do their assigned duties. A representative from the Town's financial accounting and billing software company will be back on-site to examine the Town's utilization of the programs and ensure the appropriate levels of security are in place.

Estimate completion: March 2020; report to Council April 2020.

The Finance Division will facilitate third-party review(s) of various finance related systems to assess processes and internal controls, provide documentation and recommendations. This service is in the Council approved FY2020 budget.

Estimated completion: August 2020; report to Council September 2020.