

The Corporation of the City of Windsor

Recommend Annual Budgets

Final Internal Audit Report

8 July 2015

Distribution List

For action

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Summary of Internal Audit Results

The engagement has been performed in accordance with the scope of work per Appendix A.

Report Classification

In general, management controls in the Recommend Annual Budget process are sufficiently reliable for the purpose envisaged. The process is guided by the Budget Timelines Council Report which is approved by Council, as well as the Budget Guidelines Document, which is prepared by the Chief Administrative Officer. The process is centralized through the Financial Planning group, which has an employee in each City department as a liaison between the two. The prior year Council-approved budget is carried forward, with any modifications requiring the drafting of a budget issue, which is reviewed by the Corporate Leadership Team (“CLT”) and approved by City Council.

Control Environment

The activities of this process occur on an annual basis, and they are guided by two documents:

- The Budget Timelines Council Report: this document is prepared by the Financial Planning group, as well as Asset Planning, which provides key milestones and deadlines for significant events of the process, up to and including City Council deliberations. By receiving Council approval, it is an authoritative document by which all departments must comply in order to have their budget issues considered. We considered this document and tested the key events noted therein.
- The Budget Guidelines Document: this document is prepared by the Chief Administrative Officer, and communicated to all City departments. This document provides provisions and stipulations by which departments may prepare their budget issues, as well as providing them updates to forecasted overhead amounts. The provisions set out in this document were considered during testing.

The CLT and City Council are responsible for determining the final budget as all budget issues are reviewed by the CLT and the final budget approved by City Council.

Risk Assessment

The key risks of the process were analyzed by the Financial Planning group, including Budget Modelling, overhead allocation, timelines, and budget issue review. No major changes were made in the year from prior budget years.

When reviewing budget issues, the CLT considers the risk impact of acceptance or rejection of the issue.

Control Activities

The process is centralized, and relies on the Questica Team Budget software package. Through this program, the prior year budget is carried forward, all budget issues are entered and approved/rejected, the new recommended budget is approved, and validation checks into the budget are carried out.

Segregation of duties were noted in that access to the software program are restricted with several users able to edit the budget, but only one has the ability to publish the changes.

The effectiveness of IT general controls, application controls and reporting integrity controls was beyond the scope of this review but have a direct relation to the effectiveness of the controls and information we tested.

Information & Communication

The process begins with the approval of the Proposed Budget Timelines Council Report with key provisions distributed to City departments in the Budget Guidelines Document. These provide key deadlines and qualitative information to consider when preparing budget issues.

All departments are given the opportunity to meet with the CLT to present their budget issues and discuss whether they will be included.

Monitoring

The Financial Planning group oversee the process and provide an employee to each department to allow for communication between the two groups. Using Questica, they are able to oversee that budget issues are entered properly and in a timely fashion.

Before tabling a recommended budget for Council approval, the CLT reviews all budget issues submitted to Financial Planning to provide management's perspective of the changes being proposed by departments.

Based on the controls identified and tested as part of the Internal Audit of the City's Recommend Annual Budgets process and controls we have determined that there is reasonable evidence to indicate that:

	No or limited scope improvement	No Major Concerns Noted	Cause for Concern	Cause for Considerable Concern
Controls over the process are designed in such a manner that there is:				
Sample tests indicated that process controls were operating such that there is:				

Please refer to Appendix B for a description of each classification category.

Management has provided comprehensive action plans, which we believe will address the deficiencies noted.

Summary of Positive Themes

During the review of the processes and controls, the following areas were noted as positive themes:

Communication of Key Dates and Provisions: The City provides documentation to all City departments concerning the key deadlines of the budgeting process through the Proposed Budget Timelines Council Report, as well as key updates and provisions in the Budget Guidelines Document. This provides all City departments an equal opportunity to provide their budget issues in a timely manner to allow the City to finalize and approve the recommended budget in time to effectively carry out its service delivery commitments.

Centralization: The City's budgeting process is centralized, with all budget issues entered into Questica by Financial Planning Administrators, who are employees of Financial Planning that are located in each City department. The issues are then reviewed by the CLT before being published by the Manager, Operating Budget Development. While some other staff have read-only access to the system, the ability to edit the recommended budget is restricted to allow for a centralized process.

Review of Budget Issues: All budget issues go through three levels of review: the department's CLT member, the CLT as a whole, and City Council. Budget issues are documented and made public in either the Accepted or Not Accepted document. Thus, any changes to the prior year budget cannot be made without approval from all three levels. The recommended budget is reviewed by the CLT to determine whether their decisions were carried forward into the revised document.

Employee List Reconciled with Human Resources: On an annual basis, human resources provides its staff listings to Financial Planning who perform a reconciliation to determine any discrepancies between the two lists, providing a means to further validate the completeness of the budget's staffing establishment and its Full-Time Equivalent (FTE) statistics.

Data Validation: Questica provides several validation mechanisms to allow Financial Planning to review the budget for mathematical accuracy and a means to check the reasonability of the budgeted amounts at various levels, including department, office and corporation. Furthermore, these validation checks can be run to consider a retrospective view of the information that was entered at any point in the budget process.

Public Viewing: Following review and tabling of the recommended budget by the CLT, all budget documents and issue documents are made available to the public on the City's website, as well as physical copies at City Hall and Windsor Public Library branches. These are made available for a period of two weeks which allows any resident or business in the City an opportunity to register as a delegate and speak at the budget deliberations meeting of City Council.

Summary of Findings: Recommend Annual Budgets

Finding #	Topic	Rating ¹			Management Action
		High	Moderate	Low	
Data Collection & Budget Creation					
1	Insurance Overhead Allocation			X	Update cost drivers for departmental allocation – Manager of Budget Control & Financial Administration – 2015 Q4
2	Utilities Rate Determination		X		Development of documentation to support allocation – Manager of Corporate Energy Initiatives – 2015 Q4
Total		0	1	1	

Summary of Significant Findings

We noted no significant findings as part of our review.

Management Comments

There is no prescribed process for determining hydro rates. While the industry provides a recommended rate for water, no such recommendation exists for hydro and natural gas. The process enlisted to determine a rate is a survey of various industry reports and projections from various sources, which speak to rate projections in Ontario. The result is a range of reasonable rates generated from these various professional industry reports and projections. The range of possible rates is then considered along with local experiences as well as other world and local events which for any given year may influence which rate is recommended. The recommended rate is then presented at the CLT level for further consideration of the range of rates and other influencing factors currently known or reasonably known to be expected in the next year which could influence the rate to be selected. However management does not dispute that documentation of the data sources and logic used to select a rate would be beneficial.

Name: Onorio Colucci
Title: CFO and City Treasurer (Project Sponsor)
Date: 14/07/2015

Detailed Observations

Findings & Action Plans

Finding	Rating ¹	Recommendation & Action Plan
1. Insurance Overhead Allocation		
<p>Observation Insurance budgets are approved corporately by the Office of the City Solicitor and subsequently allocated to the specific departments to reflect the full cost of the programs and services. It was noted that during the calculation of the overhead allocation of insurance premium expenses, three factors are considered: average number of claims (25%), average dollar value of claims (50%), and net budget amount (25%). The total allocated premiums for the year was \$3,672,934.</p> <p>However, it was noted that the first two factors consider claims history pertaining to 2006-2010, while the net budget amount consideration pertains to the 2011 budget.</p>	<p>Overall Low</p>	<p>Recommendation While the method of determining its allocations is reasonable, management should reconsider its inputs by utilizing the most recently available information at the time of budget preparation for overhead expenses requiring allocation.</p>
<p>Implication By relying on information from many years prior, it may result in less accurate reporting of the costs to deliver the City's programs and services.</p>	<p>Impact Low</p>	<p>Management Action Plan An annual process will be developed that will update the cost drivers of the allocation model with the most recent data to ensure the budget and cost allocations to departments are as accurate as possible.</p> <p>Responsibility Manager of Operating Budget Control and Financial Administration</p> <p>Due Date 2015 Q4</p>
<p>Root Cause More recent claim statistics and a more recent budget have not been used in determining appropriate allocation of insurance expenses.</p>	<p>Likelihood Likely</p>	

¹ See Appendix B for Basis of Finding Rating and Report Classification

Finding	Rating ²	Recommendation & Action Plan
2. Utilities Rate Determination		
<p>Observation When determining inflation rates for hydro and gas expenses to be allocated, management relies on industry trends, publications, and other forms of media to arrive at its conclusions. While professional judgment is required in arriving at a final estimate, it is not formally documented, and thus no audit trail exists to support the inflation amounts selected.</p>	<p>Overall Moderate</p>	<p>Recommendation Management should document the current process whereby inflationary estimates from industry trends are used in budget forecasts. Annual documentation should be prepared for final recommended percentages, illustrating what industry trends, publications, and other materials were considered in arriving at final estimates, as well as what professional judgments were required. The estimates should continue to be reviewed by an appropriate level of management before being submitted as a budget issue.</p>
<p>Implication By not providing support for inflationary amounts, management may be unable to support its conclusions if scrutinized. Furthermore, should the estimate be performed by another employee in a subsequent period, there would be no documented method to carry this out. This would result in potentially inconsistent analyses and/or improperly budgeted amounts.</p>	<p>Impact Medium</p>	<p>Management Action Plan There will be formal documentation outlining what information is reviewed to provide a recommended amount. Further the rationalization used for the recommended amounts, which are based on professional judgement, will be documented going forward.</p>
<p>Root Cause A standard guideline has not been developed regarding the documented support of inflation estimates.</p>	<p>Likelihood Likely</p>	<p>Responsibility Manager of Corporate Energy Initiatives</p> <p>Due Date 2015 Q4</p>

² See Appendix B for Basis of Finding Rating and Report Classification

Considerations for Improvement

1 – Multi-Year Budgeting

Observation: While the City of Windsor’s Capital Budget features a five-year plan, the Operating Budget is only for one year.

It was noted that the City’s budgeting process occurs annually, whereby only the next twelve months are included in the operating budget. While this gives direction to City departments in terms of its spending and an expectation of service delivery for rate payers, this provides only twelve months of guidance.

While Management currently includes a three-year forecast/projection in its budget documents to provide a potential outlook as to expected tax levies, this assumes the status quo in terms of departmental funding and expenditures. Management and Council should consider the overall cost-benefit and implications of implementing a multi-year budgeting model. A formal policy would include roles and responsibilities, timelines, and guidelines for establishing the multi-year budget, a protocol for reviewing and approving adjustments to the budget, reporting and accountability for favourable and unfavourable variances, contingencies, and the presentation of the multi-year budget.

The City of Calgary and York Region have long since utilized a multi-year budgeting process, which has recently been adopted by the City of London beginning in 2016. Multi-year budgeting provides many advantages to rate payers, City Council, City Administration, and City Departments. These benefits include, but are not restricted to:

- Identification of long-term operational goals, with the ability to implement a long-term plan to reach these;
- Provides a clear direction in regards to expected spending forecasts for City Departments and service delivery for rate payers;
- Allows for consideration of expected tax rate adjustments for future years to allow rate payers to be aware of possible changes sooner;
- Increased transparency into the City’s long-term plan;
- Enables City Departments to determine when and how many staff can be hired over a pre-determined number of years; and
- Complements the Corporate Strategic Action Plan.

Appendix A: Background & Scope

Linkage to the internal audit plan

As part of the Council approved 2014/15 Internal Audit Plan, Internal Audit reviewed processes surrounding the annual operating and capital budgets at The Corporation of the City of Windsor (the “City”) and the associated processes and controls to determine whether City policies are implemented.

As part of the internal audit plan development, this business process area has processes and controls associated with mitigating and managing the following corporate risks: Funding, Public Relations and expectations, Economic factors, Governance, Planning and resource allocation, Public policy, Reputation, Conflicting priorities/demands, Transparency, Service delivery, Information for decision making, Capital structure, Treasury/liquidity, Major initiatives, Sourcing/cessation, Time/cost.

Scope

Overview of the business/process reviewed

Budgeting is vital to the economic well-being of the City, providing guidance for how the City will operate for the coming year, as well as providing necessary limits to promote its financial stability as well as holding departments accountable for their operations. Given this importance, we evaluated whether the processes in place surrounding the annual operating and capital budgets are appropriate in assisting the City with meeting its goals and objectives.

As part of internal audit of the business processes and controls in effect, internal audit considered the following four (4) review areas:

1. Budget Modelling
2. Data Collection and Budget Creation
3. Budget Consolidation and Review
4. Approving annual budgets

The objectives and risks associated with this scope area are expanded upon in the Risks and Objectives section below.

The process for developing a budget model serves as critical inputs into the budget creation and review processes.

We considered the systems (i.e. Team Budget) and processes the Council has put in place to manage effectively its financial risks and opportunities, and to secure a stable financial position. We considered how Administration incorporates the inputs from Council and confirms that the budget models are applied. We evaluated whether the timelines and procedures for budget preparations are presented to Council for approval and whether these procedures and timelines were followed.

We understand that the City uses several systems and end user computing applications throughout the budgeting process and we evaluated the processes management has in place to validate the integrity of these systems/applications and application controls, where applicable.

Our scope covered the most recent processes and controls established for preparing and recommending annual operating budgets, the period of July 2014 to February 2015.

Although these processes may be present at the departmental level, our internal audit focused on the review of these processes at the City enterprise level and more specifically the roles of the corporate leadership team and senior management teams. Therefore, specific departmental control processes and activities were beyond the scope of this internal audit and we focused on enterprise/corporate wide processes and controls.

Approach

Given the operating and capital budgets are prepared once per year and the timing of this review, we had an opportunity to evaluate whether policies and procedures were followed in the preparation of the 2015 budgets. We collaborated with management to understand what key activities are performed and how management considers

relevant inputs into the preparation of the consolidated budgets. We met with management to understand all of these inputs and the handoffs of information throughout the process and identify opportunities for improvement to the overall process, where appropriate.

We obtained an understanding of processes and controls in place through facilitation of control assessment discussions with management, from which we drafted a listing of management processes and controls. Internal Audit then selected the key enterprise level controls to focus on when evaluating how well the highlighted risks are managed.

Our approach to this project was with the objective of assessing the design of processes and controls to determine that control objectives are met efficiently and effectively. Our review considered this process in two phases:

- 1) Assess the design of processes and controls relating to Data Collection and Budget Creation while determining that the inputs (i.e. Budgeting Model and Procedures) are followed
- 2) Assess the design of budget review and approval processes and controls

Where possible, an evaluation of control operating effectiveness was combined with the tests of design effectiveness. The design assessment phase conducted by Internal Audit helped to determine the following:

- If the controls are effectively designed to address the associated risks; and
- If there is reasonable evidence to indicate that the control has been implemented as designed.

In order to ensure that a control is designed effectively, Internal Audit relied upon discussions with management and examination of document and records. Internal Audit selected a sample of service areas across various City Departments and relevant Agencies Boards and Commissions to ensure that the budget processes and controls are being applied consistently.

Specific Scope Considerations:

As part of the Council Approved 2014/15 Internal Audit Plan, Internal Audit is also conducting a review of the City's Infrastructure management processes. The processes for managing infrastructure are closely related to the processes for updating the 5-year Capital Budget. It is our understanding that there are slight differences in the processes for preparing the annual Operating Budget compared to the Capital Budget and the focus of this project was on the processes and controls relating to the Operating Budget. **While we originally planned to consider a design assessment of the Budget Modelling review area for the Capital Budget, this is being considered in a concurrent review, Manage Infrastructure.**

Specific Scope Limitation

While our engagement may involve the analysis of financial information and accounting records, it does not constitute an audit or an audit related service in accordance with Canadian generally accepted accounting standards, and accordingly no such assurance will be provided in our report.

Consistent with commonly accepted practices, our work will be dependent on the following management activities which were excluded from the scope of this review:

1. The effective design, implementation and operation of the Information and Technology (IT) environment and IT general controls.
2. The effective design, implementation and operation of business system and application controls related to the capture, processing, storage, reporting/presentation and exporting of information and data.
3. Controls over the completeness, accuracy, reliability and validity of the evidence, information and data provided by management during the course of this review.

The following processes were not included in the scope of this review:

1. Performance Monitoring (i.e. Budget to Actual variance analysis)
2. Budget Amendments (i.e. changes to Council approved budget)
3. Debt Management System (i.e. level of debt, limits etc.)

Appendix B: Basis of Finding Rating and Report Classification

Findings Rating Matrix

Audit Findings Rating		Impact		
		Low	Medium	High
Likelihood	Highly Likely	Moderate	Significant	Significant
	Likely	Low	Moderate	Significant
	Unlikely	Low	Low	Moderate

Likelihood Consideration

Rating	Description
Highly Likely	<ul style="list-style-type: none"> History of regular occurrence of the event. The event is expected to occur in most circumstances.
Likely	<ul style="list-style-type: none"> History of occasional occurrence of the event. The event could occur at some time.
Unlikely	<ul style="list-style-type: none"> History of no or seldom occurrence of the event. The event may occur only in exceptional circumstances.

Impact Consideration

Rating	Basis	Description
HIGH	Dollar Value ³	Financial impact likely to exceed \$250,000 in terms of direct loss or opportunity cost.
	Judgemental Assessment	<p>Internal Control Significant control weaknesses, which would lead to financial or fraud loss.</p> <p>An issue that requires a significant amount of senior management/Board effort to manage such as:</p> <ul style="list-style-type: none"> • Failure to meet key strategic objectives/major impact on strategy and objectives. • Loss of ability to sustain ongoing operations: <ul style="list-style-type: none"> - Loss of key competitive advantage / opportunity - Loss of supply of key process inputs • A major reputational sensitivity e.g., Market share, earnings per share, credibility with stakeholders and brand name/reputation building. <p>Legal / Regulatory Large scale action, major breach of legislation with very significant financial or reputational consequences.</p>
MEDIUM	Dollar Value	Financial impact likely to be between \$75,000 to \$250,000 in terms of direct loss or opportunity cost.
	Judgemental Assessment	<p>Internal Control Control weaknesses, which could result in potential loss resulting from inefficiencies, wastage, and cumbersome workflow procedures.</p> <p>An issue that requires some amount of senior management/Board effort to manage such as:</p> <ul style="list-style-type: none"> • No material or moderate impact on strategy and objectives. • Disruption to normal operation with a limited effect on achievement of corporate strategy and objectives • Moderate reputational sensitivity. <p>Legal / Regulatory Regulatory breach with material financial consequences including fines.</p>
LOW	Dollar Value	Financial impact likely to be less than \$75,000 in terms of direct loss or opportunity cost.
	Judgemental Assessment	<p>Internal Control Control weaknesses, which could result in potential insignificant loss resulting from workflow and operational inefficiencies.</p> <p>An issue that requires no or minimal amount of senior management/Board effort to manage such as:</p> <ul style="list-style-type: none"> • Minimal impact on strategy • Disruption to normal operations with no effect on achievement of corporate strategy and objectives • Minimal reputational sensitivity. <p>Legal / Regulatory Regulatory breach with minimal consequences.</p>

³ Dollar value amounts are agreed with the client prior to execution of fieldwork.

Audit Report Classification

Report Classification	The internal audit identified one or more of the following:
Cause for considerable concern	<ul style="list-style-type: none"> • Significant control design improvements identified to ensure that risk of material loss is minimized and functional objectives are met. • An unacceptable number of controls (including a selection of both significant and minor) identified as not operating for which sufficient mitigating back-up controls could not be identified. • Material losses have occurred as a result of control environment deficiencies. • Instances of fraud or significant contravention of corporate policy detected. • No action taken on previous significant audit findings to resolve the item on a timely basis.
Cause for concern	<ul style="list-style-type: none"> • Control design improvements identified to ensure that risk of material loss is minimized and functional objectives are met. • A number of significant controls identified as not operating for which sufficient mitigating back-up controls could not be identified. • Losses have occurred as a result of control environment deficiencies. • Little action taken on previous significant audit findings to resolve the item on a timely basis.
No major concerns noted	<ul style="list-style-type: none"> • Control design improvements identified, however, the risk of loss is immaterial. • Isolated or “one-off” significant controls identified as not operating for which sufficient mitigating back-up controls could not be identified. • Numerous instances of minor controls not operating for which sufficient mitigating back-up controls could not be identified. • Some previous significant audit action items have not been resolved on a timely basis.
No or limited scope for improvement	<ul style="list-style-type: none"> • No control design improvements identified. • Only minor instances of controls identified as not operating which have mitigating back-up controls, or the risk of loss is immaterial. • All previous significant audit action items have been closed.