

Deloitte & Touche LLP  
2000 Manulife Place  
10180 - 101 Street  
Edmonton AB T5J 4E4  
Canada

Tel: 780-421-3611  
Fax: 780-421-3782  
www.deloitte.ca

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The City of Edmonton  
3<sup>rd</sup> Floor City Hall  
#1 Sir Winston Churchill Square  
Edmonton, AB T5J 2R7

Dear Audit Committee members:

We have completed our audit examination of the consolidated financial statements of The City of Edmonton (the "City") for the year ended December 31, 2006. Our examination was made in accordance with Canadian generally accepted auditing standards and, accordingly, included a review of a number of the systems of operating and financial controls and such tests and procedures, as we considered necessary in the circumstances. During the course of our audit, we identified matters that may be of interest to management. The objective of an audit is to obtain reasonable assurance whether the consolidated financial statements are free of material misstatement, and it is not designed to identify all matters that may be of interest to management in discharging its responsibilities. Accordingly, an audit would not usually identify all such matters.

## **A. CURRENT YEAR RECOMMENDATIONS**

### **A-1. Bank reconciliations**

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#### **Observation and implication**

During our control testing, we discovered that the bank reconciliations for the months of March and July were completed in October and November, respectively. We are aware that the City is having some difficulties with timeliness of bank reconciliations due to a higher than normal turnover rate and shortage of staff, given the current economic conditions in Alberta. The result is an increased likelihood of errors or inappropriate transactions going undetected for a longer than desired period of time.

#### **Recommendation**

The City should focus on the importance of timely reconciliations for the 2007 year and ensure that they are completed on a monthly basis. This emphasis is critical to the control environment and timely identification of errors and inappropriate and unauthorized transactions.

#### **Management's response**

Management agrees that bank reconciliations form a part of the control environment and should be completed on a timely basis. Bank reconciliations are performed by staff in Corporate Accounting and Reporting for both the Canadian and US Dollar bank accounts. For both bank accounts, staff endeavor to complete the bank reconciliations within 45 to 60 days following the month end. Returned items from the bank are received usually within 30 days, at which point the bank reconciliations are commenced. City

management is addressing the impact of staff turnover on the timeliness of bank reconciliations by cross-training additional resources.

It should also be noted that additional controls are in place prior to the overall bank reconciliation process. Treasury Management staff upload the electronic bank statement into the financial system daily after a match of the data with deposit and customer account information. Daily, files of cleared cheques cashed by vendors are executed and reconciliation of clearing accounts is performed. Reports, including exception reports, are generated and Corporate Accounting and Reporting staff review the reports for further action to resolve differences/outstanding items.

#### ***A-2. Payment without approval***

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##### **Observation and implication**

During our control testing we noted that all time entered into Peoplesoft using the webtime autopay system from individual departments is automatically paid regardless if manager's approval is present. This includes regular time, any overtime, sick days or vacation time entered by the employee. The manager approval is done electronically. If not completed for the period, an exception report is generated at the end of each pay period which indicates all unapproved time. All supervisors / managers with unapproved time are notified of these exceptions and it is their responsibility to review the information to determine whether the unapproved time is correct. The result of automatic payment without management's approval is the risk that employees are being paid for time not worked and therefore being overpaid.

##### **Recommendation**

The system should be enhanced to pay overtime only when approved. We suggest that the City could include a performance evaluation criteria related to timely approval of their respective employee's time. This will encourage management to approve the time at the end of each period. Any unapproved time appearing on the exception report, should have a maximum turnaround time to be approved after period end.

##### **Management's response**

With respect to PeopleSoft Web Time, the City reminds all Web Time Supervisors of their responsibility to review and approve their employees' time records via email on Web Time Approval Day. There are a small number of supervisors who do not approve time by the Approval cutoff. A query is run every pay to identify these supervisors and they are advised that they must complete a review of their employees' time records for the previous pay period. Supervisors also have the ability to run standard PeopleSoft reports that provide details on overtime and absences for their employees.

Alberta's Employment Standards Code requires employers to pay employees for all earnings not later than 10 days after the end of each pay period. The City's current process for Web Time Approval facilitates paying employees in compliance with the Code. Delaying payment of overtime unless approved by the supervisor would put the City in a position of non-compliance with the Code.

#### **A-3. Password access for TACs**

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##### **Observation and implication**

During the review of General Computer Controls, it was noted that a change applied to the application in 2005 inadvertently disabled the password expiration control for the TACs application. This was not discovered by the City until this period of review. The application is only able to provide a minimum 3 character password that is not required to change. Without periodic changes to the password it is more likely that the discovery of a password will remain for an extended period of time.

##### **Recommendation**

The City should include a password policy and standards as a part of an overall Access, Authorization, and Administration policy or a comprehensive security policy.

Section 5.2 of COBIT, the Control Objectives for IT framework suggests that *logical access to and use of IT computing resources should be restricted by the implementation of adequate identification, authentication and authorization mechanisms, linking users and resources with access rules. Procedures should also be in place to keep authentication and access mechanisms effective (e.g., regular password changes).*

The City should take steps to implement formal policies and controls to ensure that passwords are changed on a periodic basis (approximately 60 - 90 days). The City should also ensure that passwords are alpha-numeric, at least 7 characters and that they cannot be reused.

##### **Management's response**

The change to address the password control concerns in TACS was implemented in the release package of April 30. The release has introduced both a minimum length and password expiration period. Also refer to management comments provided to *Logical Access*, later in this document.

#### **A-4. Master file change reports**

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##### **Observation and implication**

During our control testing we noticed in two instances that the review of the Master File Change report generated by SAP could not be traced to source documentation. The written supporting documentation for these two changes could not be found as communication for the change was verbal. The consequence of a change being made through a phone call or verbal conversation is that there is no documentation or 'paper trail' detailing who initiates and approves the change. This could result in inappropriate and unauthorized changes occurring.

##### **Recommendation**

The City should ensure that there is some type of written back-up, i.e. emails, letters, etc., for all changes made to the Master File and/or all new vendors added to Master file.

### **Management's response**

Agreed. Management will take steps to ensure that all vendor changes are supported with appropriate written documentation.

### ***A-5. Concentration of knowledge with respect to the benefit plans and associated accounting responsibilities***

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#### **Observation and implication**

The Coordinator, Payroll and Benefit Accounting has the primary responsibility for all the accounting functions related to the benefit plans and it is our understanding that no other employees are cross trained to perform these duties.

If the Coordinator were to leave or terminate his employment with the City, there would be no other employees knowledgeable of how to perform the benefit plan related duties currently performed by the Coordinator, nor are the requirements of this position well documented. The cross training of employees can provide many benefits, which include:

- An increase in efficiency when other accounting personnel take time off;
- Reduction in duplication of effort;
- Expansion of employee's awareness of the entire accounting process; and
- Facilitation of the transition of new employees (easier to train replacements if others know how to do what the accountant that left did).

#### **Recommendation**

Consider cross-training at least one other individual in the benefit accounting area to ensure a reasonable level of knowledge transfer and continuity should an unexpected change occur in personnel. In addition, we recommend that the responsibilities, processes and procedures currently performed with respect of the benefit plans be fully documented.

#### **Management response**

Agreed. Management is committed to knowledge transfer and cross-training of staff. However, the strong economic environment and the increased number of retirements has added risk around coverage and job knowledge transfer in specialized or technical positions throughout the City, not unlike in most local organizations at this time. In 2006 both individuals that had previous experience with or had been cross-trained for aspects of this Coordinator position left the City organization.

The City of Edmonton has given a priority to workforce planning initiatives, led by the human resources branch. More specifically in this case, management is assessing alternatives to address the need for cross-training and adequate coverage. Process documentation will be assessed and strengthened as appropriate as resources allow.

**A-6. *Benefit and Pension Plan journal entries not documented and/or not reviewed prior to entry in system***

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**Observation and implication**

We noted that there is a lack of review of journal entries entered for both the benefit plans and the pension plans prior to the journal entries being entered into the system, or verification of journal entries after they have been entered. Based on our understanding, only working papers prepared at year end for purposes of the year end financial statements and audit are reviewed by someone senior to the preparer.

Journal entries should be reviewed and approved prior to posting. During the review process, management should inspect the supporting documentation to ensure that the entry being recorded is correct, valid and recorded in the proper accounting period. Even though management may have approved the journal entries, there is a risk that the entries could be incorrectly recorded due to data input errors.

**Recommendation**

We recommend that an appropriate level of management formally approve journal entries for both the benefit plans and the pension plans. We also recommend that supporting documentation be filed for all journal entries. Approval may be done manually or electronically. An appropriate level of management should review the entries to ensure that they are appropriate, accurately input and coded to appropriate accounts. We also recommend increasing the level of review of the accounting and financial reporting for both the benefit plans and the pension plans (i.e. monthly or quarterly review procedures).

**Management response**

This observation and the recommendation are a specific example of the more general comments made in the point below around *Journal entry findings*. Please see overall management's response to that recommendation. Management will see that changes incorporated from that review are also applied to the benefit and pension plan entry process.

**B. PRIOR YEAR RECOMMENDATIONS TO MANAGEMENT YET TO BE FULLY RESOLVED:**

***B-1. Write-off of uncollectible business taxes receivable***

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**Observation and implication**

During our review of internal controls and business processes, we noted that overdue business tax accounts were not written off in the year. It has been part of the City's year-end process to assess the collectibility of accounts receivable. Council approval is required to write-off uncollectible taxes related to business property accounts, leased properties and mobile homes. In prior years, Assessment and Taxation has prepared a summary report of proposed write-offs by category to present to Council. In the current year, due to staffing levels in Taxation and Assessments, this report was not prepared. As a result, uncollectible accounts were not written off, potentially overstating the business tax receivable and related allowance of the City. Management's estimate of the potential write-off was \$625,000 which was considered immaterial to the consolidated financial statements. This estimate was communicated to audit committee as part of our year-end report to audit committee.

**Recommendation**

We recommend that Assessment and Taxation ensure that all year-end processes are followed to ensure the consolidated financial statements include appropriate write-offs of uncollectible accounts.

**Management's response**

The 2005 year-end financial statements reflect an appropriate allowance for business taxes, based on a review of all outstanding balances (active and inactive accounts). It is normally our procedure to submit a write-off report to City Council for approval annually, reflecting all uncollectible accounts (inactive/bankruptcies) to December 31 of the previous year. Due to the vacancy of the Coordinator position from April 2004 to June 2005, this report was not submitted during 2005. However, all of the accounts that would have been included in the write-off report have been incorporated into the year-end reserve and will be included in our report going to City Council in the fall. The write-off report will be submitted on an annual basis in the future.

**2006 update**

The 2005 write-off had not been submitted to council during the year, but management plans to submit the 2005 and 2006 write-off reports to council for approval in 2007.

**2006 Management's response**

The 2005 write-off had not been submitted to council during the year, but management plans to submit the 2005 and 2006 write-off reports to council for approval in 2007. The 2006 year-end financial statements reflect an appropriate allowance for business taxes based upon a review of all outstanding accounts.

## ***B-2. Journal entry findings***

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### **Observation and implication**

During the year, Finance Branch management completed a self review of a selection of journal entries as part of the Office of the City Auditor's continuous auditing initiative. The journal entries tested were selected by the Office of the City Auditor. As part of the external audit, we reviewed management's findings and tested a sample of the journal entries selected. The following are the significant findings identified by the Finance Branch.

- There were a number of journal entries throughout the year where appropriate source documentation was not provided to Finance to support the journal entry selected.
- There were a number of journal entries identified through Finance's review that were either not approved by appropriate levels of department management or evidence of the approval was not provided.
- There was one instance noted of an SAP user posting and reversing journal entries to test the functionality of the system. This could result in fictional adjustments posted in the system if the test entries are incorrectly reversed.

### **Recommendation**

We recommend that Finance Branch management obtain further information regarding the potential control deficiencies identified through their review. Management should then develop a plan to address the control weaknesses identified. As part of the 2006 self review of journal entries, management should document the results of their follow-up as part of the self review documentation that is prepared.

### **Management's response**

Agreed. The initiation of the continuous monitoring of accounting entries served as a pilot in 2005, resulting in a number of observations and considerations for follow-up. In collaboration with the Office of the City Auditor, the process has been refined for continuation in 2006. Feedback is to be provided on the 2005 and future findings and an internal administrative procedure is being updated in 2006 to more formally set out expectations.

### **2006 Update**

There were no further instances observed of users using the live system to test functionality. There were additional instances of journal entries without source documentation provided and/or without evidence of appropriate approval. In addition, there was one instance noted of a journal entry reversing an earlier amortization which was found to be incorrect. The text field was inadequate to describe the journal entry and there was no preparer and approver data as well as no dates. This could result in fictional adjustments being posted in the system if there is no review of the journal entries at month end.

We recommend that Finance Branch management obtain further information regarding the potential control deficiencies identified through their review. The 2007 self-review should be timely i.e. completed on a monthly basis for prompt identification of inappropriate journal entries, in collaboration with the Office of the City Auditor. Management should also promptly develop and implement certain policies to address the control weaknesses identified through journal entry review.

### **2006 Management's response**

Management is currently also responding to a review done of the journal voucher process by the Office of the City Auditor. Similar observations were made. Finance management initiated a continuous monitoring self review process of journal voucher entries to get information on the state of the internal controls around the process and as background for considering any necessary changes. Refinements to the test were made in 2006 and a more formalized procedure was drafted. A revised journal voucher template was piloted during the 2006 year end by Corporate Accounting staff.

Upon review with various stakeholders, a number of areas where additional consideration needs to be given were identified and revisions are being considered. The procedure will then be updated and provided to the Finance Management Team and Finance Branch Manager for approval within 2007. In the interim, a summary of the errors identified in the testing will be shared with the respective areas in order that basic changes to process can be initiated.

### ***B-3. System documentation***

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#### **Observation and implication**

The existing system documentation for accounting and control procedures has not been maintained to reflect the large number of enhancements and changes that have occurred over the years. Up to date system documentation is crucial to ensure the employees are in compliance with established policies. A comprehensive accounting policies, procedures and control manual serves as a reference to accounting personnel to ensure that accounting policies and procedures are known and followed and controls are in place and operating effectively. Such a manual would also benefit the City during turnover or absence of key personnel.

#### **Recommendation**

All system documentation should be updated to the most recent policies in effect and changes should be updated in a timely manner. We recommend that the City prepare or enhance existing accounting policies and procedures for each of the following significant business cycles including expenditures, physical assets, payroll and personnel, taxation revenue, other revenues, treasury and budgeting. The system documentation should consider the following:

- Where appropriate, an organization chart including job descriptions and related qualifications.
- Major accounting conventions such as methods for calculating deferred revenue and expenses, depreciation, allowances and other significant estimates.
- Flowcharts of major processes.
- A closing schedule, including what duties are to be performed, by whom and when.
- Recurring journal entries and supporting schedules to be prepared by the accounting department.
- Recurring schedules and correspondence obtained from other departments and parties outside the City.
- A checklist to document the completion of the above procedures.
- Description of key controls in effect for each significant activity in the process.



### **Management's response**

Management acknowledges the value of developing and maintaining system documentation of significant business processes, for reference and training. A review of the existing documentation and a gap analysis will be completed in 2005, in consultation with the external auditors where appropriate. Needs will be prioritized and resources will be allocated, as available, to develop additional business process documentation and to consolidate and/or enhance existing documentation.

### **2006 Update**

The City has continued to make progress in improving the existing system documentation for accounting and control procedures. The City has a plan to address each of their significant business cycles over a number of years.

### ***B-4. Disaster Recovery Plan***

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#### **Observation and implication**

In previous years we have noted a lack of a fully tested Disaster Recovery Plan ("DRP"). The City has recognized the need for Business Continuity, and has hired a Continuity Manager. The City has made progress in developing the plan and has completed a business impact assessment, communication plan and data backup strategy. The city has also conducted tests of these components. While these are key components of a DRP, they still lack the detailed instructions for application/system recovery. This lack of detailed instructions places a strong reliance on the abilities of the individuals to rebuild a large complex environment without the benefits of detailed instructions. The development of the plan had included the need for an alternate processing facility that was not susceptible to a single event. Currently that facility does not exist in the City's IT infrastructure.

#### **Recommendation**

The City should take steps to complete the development of its DRP for all systems and applications deemed mission critical or necessary within the City's computing environment. The plan should accommodate the need for an alternate processing facility that currently exists or secure such a facility. The plan should also be tested on a regular basis to ensure its pertinence to the City's needs.

#### **Management's response**

The City understands and is committed to developing appropriate disaster recovery and Business Continuity processes. There is already a process in place to develop the recovery plans for each of the core applications. The new data protection strategy, currently in its testing and implementation phase, will be able to provide data recovery times within the recovery point objectives defined by the business impact assessment. The City continues to seek funding for an alternate site.

#### ***B-5. City Hall server room***

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##### **Observation and implication**

In previous years, we have noted the City of Edmonton relies on a processing facility located in City Hall with inadequate physical and environmental controls. The City continues to rely upon a facility with environmental concerns such as flooding, water pipes over servers, and poor air quality. The location also poses physical security concerns as it is a shared facility located in a publicly available area. The City has taken some steps to reduce the potential threats by improving the environmental monitoring, however the accommodation itself creates the potential concerns.

##### **Recommendation**

The City should consider relocating the City Hall server room to a more appropriate and secure location. The City should also ensure that server rooms have appropriate security controls in place to reduce potential malicious or unintended but predicable incidents. The IT department must be given authority over the granting and regulating of all persons who access any server room that contains IT Information Assets.

##### **Management's response**

The City agrees that the current City Hall server room does not meet the processing needs, and is attempting to re-secure funding for the alternative site.

#### ***B-6. Logical access***

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##### **Observation and implication**

As noted in prior reviews of the City's Computing environment, the approval process for granting access and maintaining pertinent access to the core applications is inconsistently applied. Each application applies its own access approval process that adequately assures appropriate access is granted, however no application examined conducts fully documented access reviews to ensure access remains appropriate. The City has made some progress in centralizing the administration of granting access, however it has not been completed for all applications and continues to be managed per application. Without a formally documented and complied with Access, Authorization and Administration policy or procedure, the City may be at risk of allowing persons with unauthorized or unintended access to City Information Assets.

##### **Recommendation**

The City should take steps to implement a City-wide Access, Authorization and Administration policy and procedures which include the applications. The policy and procedures could be built upon existing access request and authorization procedures and may include but are not limited to:

- Tracking all access requests in an auditable manner
- Formally identifying who is authorized to grant access.
- Identifying security issues or possibly conflicting access levels
- Formally reviewing all access within all systems or applications by business leaders or data owners on a scheduled basis.

- Formalizing a process to ensure that all access is removed when an employee changes positions within the City or terminates employment.

**Management's response**

The City continues to progress in the centralization of access authorization process to the Inside Information group. It agrees and recommends that departmental contacts conduct regular reviews. The User Access - File Permissions project was initiated in fall, 2006 and will address and improve all five concern areas identified in the Audit Recommendation that pertain to data file access. The core concept proposed by the project is delegated Branch-level accountability for defining and managing access "roles" for the staff within that Branch. Implementation of these new role-based approaches could be anticipated in the 2007/8 timeframe.

**C. THE FOLLOWING RECOMMENDATIONS FROM PRIOR YEARS HAVE BEEN FULLY ADDRESSED BY MANAGEMENT IN THE CURRENT YEAR:**

***C-1. Long-term debt records***

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**Observation and implication**

Our audit procedures include sending external confirmations to the City's long-term debt holders. We were unable to confirm the terms and outstanding balance of four of the City's Land Drainage debentures. The four debentures were initially issued in 1965 and 1966 and have a recorded outstanding balance of under \$100,000. This debt was originally issued under the Municipal Development Loans Act. The Municipal Development Loans Act expired in 1966 and administration of loans issued in the province of Alberta fell under the Central Mortgage and Housing Corporation on behalf of the Municipal Development Loan Board. As part of our audit work, we have reviewed the original amortization schedules and records held by the City. Based on the original records and loan numbers, we were unable to send a confirmation to the lenders with sufficient information for them to identify and confirm the loans. The City continues to make the scheduled debt payments to the Receiver General for Canada based on the original amortization schedule of the debt.

Although the City has all the original records related to the debt, the City does not have up to date information on the debt holder. As a result, management cannot make enquiries about payments, outstanding balances or terms. The current accounting records reflect the outstanding balance per the original payment schedule; however, it is possible that the balance is inaccurate as the City does not have the ability to verify the balance with the debt holder.

**Recommendation**

We recommend that the Finance Branch ensure up to date records are maintained of all debt facilities and holders that will facilitate knowledge transfer over long-term staffing changes. When debt holder information changes due to reorganization of the external agencies holding the debt, these records should be updated.

**Management's response**

Management has supporting documentation for the four debentures that includes the debt holder (Receiver General for Canada), Debenture numbers, reference numbers, amounts, rates and dates borrowed, bylaw authority numbers and repayment schedules. This information is summarized on the original accounting schedules that are in the City's possession. As the original terms and conditions of the debentures are unchanged, the balances reflected on the repayment schedules also remain unchanged. Unfortunately, the debt holder (Receiver General For Canada) was unable to satisfy audit confirmations. That is beyond the City's control and does not alter the terms and conditions of the debentures. As a result, repayments continue as scheduled and the debt holder continues to negotiate the payments.

**2006 Update**

We were able to obtain sufficient third party verification of long-term debt balances and were able to satisfy our audit requirements. Final payment was made on the debt in 2006. This recommendation has been fully resolved for 2007.

## ***C-2. Access to mill rates***

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### **Observation and implication**

During our review of internal controls, we noted that the same individual has the ability to enter and approve the mill rates entered into the Tax Assessment and Collection System ("TACS"). This lack of access controls results in employees having the ability to enter mill rates that could affect business and property tax revenue.

### **Recommendation**

We recommend that stronger access parameters be enabled and enforced in TACS that require a second individual to approve rate changes.

### **2004 Management's response**

Management is in agreement with the recommendation and has formalized a system change request for TACS, to be completed in mid 2005. The current business practice is to segregate the entry and approval functions for mill rates.

### **2005 Update**

During our review of internal controls, we observed that there have been no changes or improvements made to the TACS access parameters related to mill rates in the current year.

### **2005 Management's response**

A system change request was initiated in December 2004 (CSR 5038), however, due to IT resource issues and competing system priorities, this request has not been completed. The separation of entry and approval of annual tax rates is managed manually as part of the annual procedures and only supervisory accounting staff has access to update or approve tax and other rates. It should be noted that many staff are involved in the verification of levy calculations prior to printing the notices (both on individual accounts and in total) using the tax rates indicated in the approved Schedule A to the Tax Rate Bylaw.

### **2006 Update**

During our review, we observed that the system change request, CSR 5038, had been completed during the year. We are pleased to report that this recommendation has been fully addressed.

## ***C-3. Password access for Peoplesoft***

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### **Observation and implication**

During the review of General Computer Controls at the City, it was noted that passwords are not required to be changed in Peoplesoft or Posse.

## **Recommendation**

The City should include a password policy and standards as a part of an overall Access, Authorization and Administration policy or a comprehensive security policy.

Section 5.2 of COBIT, the Control Objectives for IT framework suggests that *logical access to and use of IT computing resources should be restricted by the implementation of adequate identification, authentication and authorization mechanisms, linking users and resources with access rules. Procedures should also be in place to keep authentication and access mechanisms effective (e.g., regular password changes).*

The City should take steps to implement formal policies and controls to ensure that passwords are changed on a periodic basis (approximately 60 - 90 days). The City should also ensure that passwords are alpha-numeric, at least 7 characters and that they cannot be reused.

## **Management's response**

The City's IT group will have to work with the business units to determine how to best implement a more secure password framework for these applications. The City is also moving towards the implementation of an identity management system which will provide a long-term strategy and controls over user access within the City's computing environment.

## **2006 Update**

We are pleased to note that the City has appropriately addressed the issues of Password controls for Peoplesoft.

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We wish to take this opportunity to thank you and your staff for their courtesies and cooperation throughout the audit process. If you have any questions or concerns regarding the above comments or any other matters, please do not hesitate to contact John Anderlic or Rachel Gosse at your convenience. This communication is prepared solely for the information of management and is not intended for any other purposes.

Yours truly,

*Deloitte & Touche LLP*  
Chartered Accountants