



Finance and Audit Committee Meeting

First Quarter FY2017 – August 24, 2016

Audit Update

The Office of Internal Audit and Compliance (IAC) is an independent and objective assurance function designed to:

- **Assess and measure organizational risk through periodic enterprise risk assessments and**
- **Evaluate the effectiveness of internal controls, business processes, and enterprise risk management activities**
- **Assess compliance with applicable laws, regulations, ordinances, and Chicago Board of Education (Board or CPS) rules, policies, and procedures**
- Complete projects to assist management with improving organizational efficiency and effectiveness while minimizing organizational risk

IAC work is performed in accordance with applicable standards, such as American Institute of Certified Public Accountants, Institute of Internal Auditors, and the Government Accountability Office.

FY16 Accomplishments

- **Expanded the scope of district-managed school audits to increase the: number of in scope processes, testing sample sizes, in-scope time periods, and field time (one vs. two day audits) – all with the objective to more effectively monitor the internal control environment**
- Performed reviews of Internal Accounts and Supplemental Payment Systems and provided recommendations to strengthen internal controls, oversight, and transparency
- **Assisted management in designing the expansion of the School Support Center to help centralize financial and accounting functions performed at schools and improve business and cost effectiveness (implementation is ongoing)**
- Led efforts to monitor and reduce excessive food expenditures, travel, and non-required training, resulting in a nearly \$1 million reduction in year-over-year spend
- **Implemented purchase order and disbursement changes to increase transactional oversight and transparency, which combined with other organization actions, led to a reduction in expenditures**
- Consolidated audit and compliance functions to create a single, centralized team focused on strengthening, implementing and monitoring internal controls and compliance requirements

Overall Themes

Strengthening Internal Controls, Management Accountability, & Efficiency	Driving Internal Controls for Spend Management and Transparency	Monitoring Risk Through Improved Internal Audit and Compliance Program
<ul style="list-style-type: none"> Increased the number of audits across the District, including school-based audits Identified internal control gaps leading to process changes and the number of employees being held accountable for issues such as: <ul style="list-style-type: none"> ✓ Working less hours than reported ✓ Excessive or unsupported reimbursements ✓ Swiping in other employees ✓ Unauthorized access to data ✓ Inappropriate use of sick days Began improving audit processes and consolidating audit and compliance functions 	<ul style="list-style-type: none"> Recommended immediate implementation of spend controls & oversight that led to: <ul style="list-style-type: none"> ✓ A 65% decrease in food spend and 50% decrease in travel spend since September 2015 Recommended \$5,000 check limits for certain transactions to increase oversight and improve transparency Recommended additional approval of purchase requisitions for certain transactions over \$5,000 Recommended systems-based controls to help enforce annual vendor payment limits Recommended internal control changes to employee reimbursements to increase the ability to detect errors and issues 	<ul style="list-style-type: none"> Conducting comprehensive Enterprise Risk Assessment (ERA) to identify and prioritize external, strategic, financial, educational, and compliance risks: <ul style="list-style-type: none"> ✓ Current Update was needed due to significant changes at CPS ✓ Process includes interviews, surveys, and a facilitated session ✓ Output includes risk rankings based on impact and likelihood, risk profile, and risk definition for the top risks ERA results will help define the first truly risk-based Internal Audit plan for CPS in several years ERA results will also help define ongoing risk mitigation strategies for key areas such as: <ul style="list-style-type: none"> ✓ Information Technology Controls ✓ Financial Controls ✓ Facilities Management ✓ Safety and Security Separately, conducting a comprehensive Compliance Risk Assessment given the complexity of regulatory requirements

School Audit Highlights

FY16 School Audits Key Stats

- 27% of District schools audited in FY16

Fiscal Year	2014	2015	2016
Total School Audits	151	140	170

The most common audit findings observed during school audits are as follows:

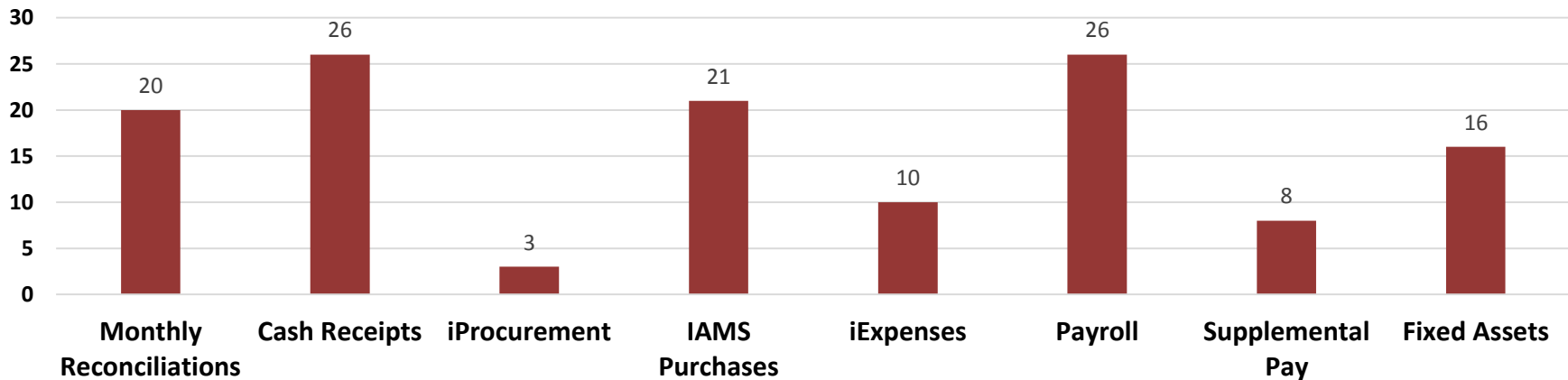
- Lack of required approval prior to purchase of goods and services
- Inadequate supporting documentation and/or approval for manual payroll edits
- Inadequate supporting documentation for cash receipts and cash disbursements (e.g., missing treasury and teacher receipts, missing requisitions, invoices, and/or evidence of receipt)
- Ineffective fixed assets tracking and accounting/management processes, often leading to accounting errors and reduced ability to locate certain assets

School Audit Highlights

The following root causes for the common findings above:

- **Infrequent Training** – Oracle training no longer required when access is provisioned. Internal Accounts training is suggested, but not required
- **Outdated Policies & Procedures** – Insiders’ Guide to Schools Accounts was last updated in 2008 and is not consistent with current practices.
- **Reduced Accountability & Capacity** – The monitoring of controls to ensure policy is being followed has been reduced, the capacity to manage the processes has been reduced, and maintaining the necessary level of financial and accounting expertise across 600+ schools has been challenging.

Frequency of High Risk Findings by Process Area



District-wide Audit Highlights

Below are highlights of key district-wide audits performed in FY16.

Internal Accounts Assessment

Objectives – To obtain a detailed understanding of Internal Account transactions (averaging \$200M annually), and identify process improvements to strengthen the overall internal control environment.

Results – Internal Accounts are outdated and overall internal controls are not sufficient to prevent transactions from violating Board policy. Internal Accounts as an enterprise system lacks functionality for effective oversight due to limited reporting (aggregate totals across CPS schools), and unnecessarily cumbersome school based chart of accounts.

Key Recommendations – Create a universal chart of accounts for all schools to use. Develop and distribute an updated Internal Accounts Manual incorporating all new directives and policy changes. Implement additional system-wide controls to prevent transactions that violate Board policy and enhance reporting capabilities to enable more robust transactional analysis – both for individual schools and all schools aggregated. Alternatively, create a broad-based school operations manual covering all financial, operational, and administrative processes to provide a single point of reference management and staff.

Supplemental Pay Systems Audit (SPS)

Objectives – To review the purpose of SPS or buckets (\$160M in original appropriations in FY16) and determine if effective controls are in place from opening a bucket through payment of hours worked. Buckets, which is mainly personnel costs, are used for temp employees, personnel (teachers, clerks, security) for after school programs, and coaches.

Results – System wide internal controls are limited, including lack of secondary review of pay rates leading to overpayments and unclear purpose of bucket and outcomes leading to unknown activities from year to year.

Key Recommendations – Reduce the number of programs under which buckets can be created. Require supporting documentation to be maintained at the schools including program purpose, pay rates, eligible employees, and evidence of participation and outcomes. Close and reestablish buckets for FY17 and increase FY17 oversight for creation and utilization all buckets.

Finance Update



CPS Demonstrated Willingness to Act to Address FY16 Challenges

- CPS made \$160 million of expenditure reductions in the beginning of FY16
- CPS made an additional \$225 million of mid-year expenditure reductions
- The majority of these cuts are structural in nature - \$173 million will carry over to FY17
- CPS ensured its continuous mission was fulfilled with limited classroom impact while difficult financial decisions were made

*All numbers in millions

Key FY16 Budget Balancing Measures	FY16 Impact*	FY17 Impact*
Central Office Cuts	\$33	\$45
Mid-Year Student-Based Budget Reductions	\$80	\$120
Furlough Days	\$30	--
Decrease in Pension Pick-up for Non-Union Employees & Healthcare Changes	\$4	\$7
Expense Control	\$66	\$1
Reimbursement of Capital Proceeds and GIC Termination	\$12	--
Total	\$225	\$173



\$300M in Management Cost Savings Initiatives for FY17

*All numbers in millions

Savings Initiative	Savings*
Sweep Vacancy Savings (2 % of Total Labor)	\$58
Reprogramming Grants to Classrooms	\$35
Centralized Purchasing Savings	\$35
Anticipated Labor Savings (1 % of Total Labor)	\$31
Phase-In of Shared Services	\$26
Charter School Share of Central Efficiencies	\$20
Reduction End Non-School Based Employees(since Jan.)	\$17
Savings from Teacher Retirements & Resignations	\$17
New TIF Revenue	\$15
Scheduling Efficiencies	\$15
Improved Medicaid Collections	\$12
Additional Central Office Streamlining	\$10
Additional Revenue (Sponsorships)	\$6
Central Summer Program Reductions	\$3
Total	\$300

Finance and Audit Committee Schedule

Tentative Meeting Date		Tentative Agenda Highlights
October 2016	FY17 Second Quarter Meeting	<ul style="list-style-type: none"> • Key audit activities update • Risk assessment results • Open audit findings update • Financial update
January 2017	FY17 Third Quarter Meeting	<ul style="list-style-type: none"> • Key audit activities update • Financial update • Additional items to be defined
April 2017	FY17 Fourth Quarter Meeting	<ul style="list-style-type: none"> • Key audit activities update • Financial update • Additional items to be defined

Appendix: COSO Lines of Defense

